
(2002) 08 AHC CK 0038

In the Allahabad High Court

Case No : Central Excise Reference No. 11 of 2001

Flex Engineering Ltd.

APPELLANT

Vs

Commissioner of Central Excise

RESPONDENT

Date of Decision : 26-08-2002

Acts Referred:

Central Excise Rules, 1944 — Rule 57A

Citation : (2002) 84 ECC 516 : (2003) 161 ELT 4

Hon'ble Judges : S.K. Sen, C.J;Ashok Bhushan, J

Bench : Division Bench

Advocate : A.P. Mathur, for the Appellant; S.P. Kesharwani, Standing Counsel, for the Resondent, for the Respondent

Judgement

S.K. Sen, C.J.—Brief facts of the case, inter alia, are that the applicant M/s. Flex Engineering Limited manufactures packaging machines of various types of classifiable under Chapter 84 of the Central Excise Tariff. It is the case of the applicant that it was availing the benefit of Modvat credit oh laminated plastic films and poly papers. Show cause notices were issued to the applicant with regard to denying the benefit on the above inputs on the ground that they are used for the purpose of testing of their final product "packaging machines" and is not an input as defined under Rule 52A of the Central Excise Rules. The adjudicating authority denied the benefit or Modvat credit. The applicant preferred an appeal, which too was rejected. The applicant filed appeals before the Customs, Excise and Gold (Control) Appellate Tribunal. Following the earlier order in the case of the same applicant the Tribunal, on 17th April, 1998 1998 (102) ELT 387 , upheld the order passed by the Commissioner (Appeals). In the meantime, in regard to the earlier order Court, on 1st July, 1997, had directed the Tribunal to refer questions of law to this Court for opinion. Accordingly, the following questions of law have been referred to this Court for opinion:

1. "Whether, in the circumstances of the present case, facts of which are not in dispute, duties paid on material, namely, plastic films/poly paper used for testing

machines for forming commercial/technical opinion as to their marketability/excisability would be eligible to be taken as credits under Rule 57A read with relevant notification?"

2. "Whether such use of material in testing in view of the purposes mentioned above, could be said to be "use in the manufacture of or use in relation to the manufacture of the final products viz., Machines as assembled?"

2. Heard Shri A.P. Mathur, learned Counsel for the applicant and Shri S.P. Kesharwani, learned Standing Counsel for the respondent. Both the parties have also submitted their written note of submissions. We have carefully gone through the entire documents, placed before us, including the written note of submissions.

3. It has been contended by Mr. Mathur, learned Counsel for the applicant that there are no testing machines and the laminated plastic films and poly papers are not used in any testing machines. On the other hand, laminated plastic films and poly papers are used by the applicant in the process of manufacture of filling and sealing machines, which is also evident from Order No. Ref/42/96-NB passed by the Tribunal on the reference application filed by the applicant 1996 (86) ELT 660 .

4. The learned Counsel has drawn our attention to the relevant portion of the reference application, which is quoted herein below:

"This is a reference application u/s 35G(1) of the Central Excises and Salt Act, 1944 arising from the order of this Tribunal dated 24th November, 1995. The question arose in this case whether flexible plastic films/poly paper can be regarded as an input for the manufacture of filling and sealing machines (F.S. Machines) and also whether the cost of flexible plastic films/poly paper was eligible for Modvat Credit as an input."

5. He has further referred to final order dated 24th November, 1995 passed by the Tribunal on the appeal of the applicant, which is as follows :

"Heard the submissions. On careful consideration of the submissions made before us we find that the question in short compass is whether Modvat Credit under Rule 57A of the Central Excise Rules, 1944 was admissible on flexible plastic films used in testing the performance of the form fill and sealing machines."

6. Contention of the learned Counsel for the applicant is that there are no test machines and the flexible plastic films or poly papers are used directly for testing the form fill and sealing machines in the process of manufacturing the same by the applicant. Accordingly, he has submitted that the applicant is fully eligible to avail Modvat credit on flexible plastic films/poly papers used as inputs in testing the form fill and sealing machines in the process of the manufacturing the same in terms of Rule 57A of the Central Excise Rules, 1944.

7. Rule 57A, at the relevant time, provided as under:

"Rule 57A. Applicability. -- (1) The provisions of this section shall apply to such finished excisable goods (hereinafter referred to as the "final products") as the Central Government may, by notification in the Official Gazette, specify in this behalf, for the purpose of allowing credit of any duty of excise or the additional duty u/s 3 of the Customs Tariff Act, 1975 (51 of 1975), as may be specified in the said notification (hereinafter referred to as the "specified duty") paid on the goods used in or in relation to the manufacture of the said final products (hereinafter referred to as the "inputs") and for utilizing the credit so allowed towards payment of duty of excise leviable on the final products, whether under the Act or under any other Act, as may be specified in the said notification, subject to the provisions of this section and the conditions and restrictions that may be specified in the Notification :

Provided that the Central Government may specify the goods or classes of goods in respect of which the credit of specified duty may be restricted.

Explanation. -- For the purpose of this rule, "inputs" includes -

(a) inputs which were manufactured and used within the factory or production in or in relation to the manufacture of final products, and

(b) paints and packaging materials,

but does not include -

(i) machines, machinery, plant, equipment, apparatus, tools or appliances used for producing or processing any goods or for bringing about any change in any substance in or in relation to the manufacture of the final produces;

(ii) packaging materials in respect of which any exemption to the extent of the duty of excisable payment on the value of the packaging materials is being availed of for packaging any final products;

(iii) packaging materials the cost of which is not included or had not been included during the preceding financial year in the assessable value of the final products u/s 4 of the Act;

(iv) cylinders for packing gases;

(v) plywood for tea chests."

8. Mr. Mathur, learned Counsel has further submitted that the provisions of the said rule shall apply to such finished excisable goods (hereinafter referred to as the final products) as the Central Government may, by notification in the Official Gazette, specify in this behalf, for the purpose of allowing credit or any duty of excise or the additional duty u/s 3 of the Customs Tariff Act, 1975 (51 of 1975), as may be specified in the said notification (hereinafter referred to as the specified duty), paid on the goods used in or in relation to the manufacture of the said final products--whether directly or indirectly and whether contained in the final product or not-(hereinafter referred to as the inputs) and for utilizing

the credit so allowed towards payment of duty of excise leviable on the final products, whether under the Act or under any other Act, as may be specified in the said notification, subject to the provisions of this section and the conditions and restrictions that may be specified in the notification.

9. It has been further submitted by the learned Counsel for the applicant that undoubtedly Laminated Plastic Films/Poly Paper and packaging machines are specified input and final products under Rule 57A and hence Modvat credit should be available to the applicant. He has also referred to Section 2(f) of the Central Excise Act/1944 and has submitted that "manufacture" includes any process-

(i) incidental or ancillary to the completion of a manufacture product; and

(ii) which is specified in relation to any goods in this section or Chapter Notes of the Schedule to the Central Excise Tariff Act, 1985.

10. It is the contention of the learned Counsel for the applicant that the applicant is engaged in the manufacture of Automatic Form Fill and Sealing Machines, which are used by the purchasers for packing and sealing their products in plastic pouches. Before the machine is ready to be marketed and can be said to be finally manufactured, the applicant has to use Laminated Plastic Films/Poly Paper for the purpose of testing, tuning and adjusting various parts of the machine so as to ensure that they are fit and ready for packing and sealing the required size of pouches. It is the case of the applicant that the purchasers place their orders to the applicant mentioning the specifications of the pouches, which they require for packing and sealing their products. Unless and until tuning and adjustment is done by the applicant with the help of Laminated Plastic Films/Poly Paper, the machine cannot be tuned and adjusted in accordance with the purchase order and the same will not be purchased by the purchaser. In other words, without tuning and adjustment to make the machine in conformity with the specifications of the purchaser, it cannot be said that the machine has been manufactured. Manufacturing is not complete unless the tuning and adjustment has been done as per specifications given by the purchaser.

11. It has further been submitted by the learned Counsel that under the Central Excise Act, it is nowhere defined that at what stage various products, covered by the Central Excise Tariff Act, 1985, will be termed as completely manufactured. In the applicant's case the machines are completely manufactured only after the same are tested. The machines are tailor made and each machine is to import a distinct and different result. If the results are not as per the requirement of the customer, the machine loses its marketability because it is of no use to any other customer. The Laminated Plastic Films are used to find out as to whether the result desired to be obtained is available from the machine so made. Unless this is done the process of manufacture is not complete. The machines manufactured by the applicant is entered in the R. G. I. Register (a Register prescribed for entering fully manufactured goods) only after the same are tested by the applicant as the process of such testing is an essential ingredient of manufacture.

In the instant case, admittedly, the goods are manufactured on the specific order and design of the customer with specified test mandatory before delivery of goods. Under the circumstances, the manufacture can be deemed to be complete after the qualitative and other specification tests are undergone. The tests conducted by the applicant are the parts of the process of manufacture and without the same the manufacture is not complete.

12. In support of his contention learned Counsel has relied upon the following decisions:

1. 1991 (32) ECR 504 .
2. 2000 (124) E.L.T. 267(SC)() (Tribunal), Prayas Castings Ltd. v. Collector of Central Excise, Baroda.
3. Collector of Central Excise, Calcutta-II Vs. Eastend Paper Industries Ltd.,
4. 1996 (88) E.L.T. 273 (Tri), Machine Fabrik Polygraph (I) Ltd. v. Collector of Central Excise, Pune.
5. 1996 (63) ECR 1 90 .
6. 2000 (120) ELT 105

13. It is also the contention of the learned Counsel that the expression "in or in relation to the manufacture" used in Rule 57A is a term of extremely wide import and it does not admit of any exclusion on the basis of the stage of production or whether the inputs have been used interior or posterior to manufacture. If the use of inputs has nexus to the manufacture, that would suffice. However, in the instant case, the applicant has used the inputs, in question, in the course of manufacture itself for the purposes of tuning, adjusting and finishing the machine so as to make it in conformity with the specifications mentioned in the purchase orders. The inputs i.e. Laminated Plastic Films/Poly papers are used by the applicant in or in relation to the manufacture of the machines. According to the learned Counsel there is no scope for doubt when the raw materials/inputs are actually used in the main stream of manufacture of final products, that is, actually used in the physical or chemical processes of manufacture. It is certainly an input used in the manufacture of final products. Doubt may arise only in regard to use of some articles not in the main stream of the manufacturing process but in another scheme of manufacturing something, which is to be used for rendering final product marketable or used otherwise in assisting the process of manufacture. Such doubt is set at rest by use of the words "used in relation to the manufacture". The use of Laminated Plastic Films/Poly Paper is for rendering the final product marketable and without the use of the same machines cannot be called as fully manufactured.

14. Learned Counsel has further submitted that in the instant case the goods manufactured by the petitioners are, admittedly, tailor-made according to specific order and design of the customer with specified test mandatory before

delivery of goods. Demonstration of goods is always conducted on the goods, which have been cleared from the factory. In the instant case, the goods are not cleared from the factory and the tests are conducted in the process of manufacture of the said goods by the applicant in the factory itself. No adverse inference can be drawn against the applicant even if the tests are conducted in the presence of the representative of the customers. Accordingly, learned Counsel claims that benefit of Modvat credit should have been allowed to the applicant in the instant case and there is no scope for denial of the same.

15. It has been submitted on behalf of the respondent that finding of the Tribunal is that fill and seal machine is used for testing the performance. That being so, it is not a process of manufacture and, therefore, flexible plastic films used for testing the performance of the machine cannot be termed as inputs for the purpose of allowing Modvat credit of duty paid on flexible plastic films. It has also been mentioned on behalf of the respondent that the applicant has annexed purchase order, which appears at pages 100 and 101 of the paper book and under the column Inspection/trial the contractual obligation is written, which is reproduced below :

"Inspection/Trial will be carried out at your works in the presence of our Engineer before despatch of equipment for the performance of the machine."

16. In fact, it is the contention of the learned Counsel for the applicant that the purchase order and the condition as aforementioned have been relied upon by him and he urged that the plastic films/poly papers used for testing the performance amounts to process of manufacture and, therefore, in an input. Learned Counsel for the respondent has, however, submitted before us that a bare perusal of the conditions clearly shows that the aforesaid argument is misconceived.

17. Learned Counsel for the respondent has relied upon Section 2(f) of the Central Excise Act, 1944, which defines the term "manufacture" and submitted that the word "manufacture" shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also a person, who engages in the production or manufacture, on his own account. Learned Counsel for the respondent has also referred to Rule has submitted that the term "input" includes (a) inputs, which were manufactured and used within the factory of production in or in relation to manufacture of final products, and (b) paints and packaging materials. It is, therefore, implied from the aforesaid provision that only those goods, which are used within the factory in or in relation to the manufacture of final products, can be regarded as "input". Thus, the most important term requiring interpretation is the interpretation of the term "in or in relation to the manufacture". It has been contended by the learned Counsel for the respondents that it is clear from the definition of the term "manufacture", as provided in Section 2(f) of the Act that "manufacture is a process to the completion of a manufactured product and in the instant case the same is complete in all respect and the machines so

manufactured were final product and the plastic films/poly papers used for testing machine is after complete manufacturing of machine and unless the machine has been completely manufactured, no testing is possible. It is apparent that in fact the plastic films/poly papers used for testing the performance of machine is merely for the satisfaction as to its performance and there is no scope for considering the same to have been used in or in the materials used for the manufacture.

18. We have considered the submissions made by learned Counsel for the parties and the decisions cited by them. The use of laminated plastic films and poly paper for filling and sealing machine, used for testing the performance of machine for inspection/trial in the presence of Engineer before despatch of the equipments, cannot be termed as "inputs" for the purpose of allowing Modvat credit of duty paid on flexible plastic films. Section 2(f) of the Central Excise Act, 1944 defines the term "Manufacture" and from this definition, it clearly implies that use of plastic film/Poly paper for the purpose of inspection/trial or demonstration is not part of the manufacturing process. Learned Counsel for the applicant, however, has relied upon the decision of the Supreme Court in the case of Collector of Central Excise, Calcutta-II Vs. Eastend Paper Industries Ltd., wherein it was held that since wrapping paper is marketed in packed or wrapped condition, the wrapping paper used in wrapping of paper is to be treated as raw material or component part for other variety of paper which is wrapped. Accordingly, it was held that wrapping paper, so consumed or utilized, would be entitled to exemption under Notification No. 18-A/83-C.E. In that view of the situation, wrapping paper should be treated as raw material. Manufacture in the sense it is used in the Excise law, was not complete until and unless wrapping was done. It is settled law that excise is a duty on manufacture. Manufacture is the process or activity, which brings into existence new, identifiable and distinct goods. Goods have been understood to be articles known as identifiable articles known in the market as goods and marketed or marketable in the market as such. This view finds support from the decisions of the Supreme Court in Bhore Industries Ltd., Bombay Vs. Collector of Central Excise, Bombay, South Bihar Sugar Mills Ltd., etc. Vs. Union of India (UOI) and Others, Union of India (UOI) Vs. Delhi Cloth and General Mills, ; Union Carbide India Limited Vs. Union of India (UOI) and Others, and Civil Appeal No. 2215 (NA) of 1988; Collector of Central Excise, Baroda Vs. M/s. Ambalal Sarabhi Enterprises (P) Ltd., judgment delivered on 10th August, 1989. In the case of Empire Industries Limited and Others Vs. Union of India and Others, , reported in paragraph 4 of the judgment, the Supreme Court has explained the concept of "Process" in Excise Law, In view of the principle laid down therein and other relevant decisions, processes incidental or ancillary to wrapping are to be included in the process of manufacture, manufacture in the sense of bringing the goods into existence as these known in the market as not complete until these are wrapped in wrapping paper. The Supreme Court in the case of J.K. Cotton Spinning and Weaving Mills Co. Ltd. Vs. Sales Tax Officer, Kanpur and Another, while construing the

expression "in the manufacture or processing of goods for sale" in the context of Sales Tax Law, though the concept is different under the Excise Law, has held that manufacture of goods should normally encompass the entire process carried on by the dealer of converting raw materials into finished goods. Where any particular process, the Supreme Court further emphasized, is so integrally connected with the ultimate production of goods that, but for that process, manufacture or processing of goods would be commercially inexpedient, articles required in that process, would fall within the expression "in the manufacture of goods". The Supreme Court further illustrating the position, observed that "for instance in the case of a cotton textile manufacturing concern, raw cotton undergoes various process before cloth is finally turned out. Cotton is cleaned, carded, spun into yarn, then cloth is woven, put on rolls, dyed, calendered and pressed. All these processes would be regarded as integrated processes and included "in the manufacture" of cloth. It would be difficult to regard goods used only in the process of weaving cloth and not goods used in the anterior processes as goods used in the manufacture of cloth. To read the expression "in the manufacture" of cloth in that restricted sense would raise many anomalies. Raw Cotton and machinery for weaving cotton and even vehicles for transporting raw and finished goods would qualify under Rule 13, but not spinning machinery, without which the business cannot be carried on". The judgment and decision in the case of Collector of Central Excise v. Jay Engineering Works Ltd., reported in 1989 (43) E.L.T. 169 (S.C) may also be taken note of. In the aforesaid case before the Supreme Court, the respondent was a manufacturer of electric fans and brought into its factory nameplates under Tariff Item 68 of the erstwhile Central Excise Tariff. The nameplates were affixed to the fans before marketing them. The respondent claimed the benefit of proforma credit in terms of Notification No. 20-I/79, dated 4th June, 1979, which was for the purpose of relief on the duty of excise paid on goods falling under Tariff Item 68, when these goods were used in the manufacture of other excisable goods. The said notification stated that in supersession of the Notification No. 178/77 of the Central Excise dated 18th June, 1977, all excisable goods on which duty of excise was leviable and in the manufacture of which any goods falling under Item No. 68 have been used, were exempted from so much of the duty of excise leviable thereon as was equivalent to the duty of excise already paid on the inputs. In that case, the question before the Tribunal was whether the nameplates could be considered as component part of the electric fan, so as to be eligible for proforma credit under the exemption notification. It was found by the Tribunal that no electric fan could be removed from the factory for being marketed without the nameplate. The Tribunal also noted in that case that even though it could be said that electric fans could function without the nameplates, for actual marketing of the fans, the affixation of the nameplate was considered an essential requirement. To be able to be marketed or to be marketable, it appears to us, that it was an essential requirement to be goods, to be wrapped in paper. Anything required to make the goods marketable, must form part of the manufacture and any raw material or any materials used for the same would be

component part for the end product. In the instant case, however, laminated plastic/poly paper did not form part of the manufacturing process nor became part of the package machine of various types sold in market. They were only used for the purpose of testing which could not form part of the manufacture. The applicability of Modvat is covered by Rule 57A of the Central Excise Rules, according to which, credit of duty paid on goods used in or in relation to the manufacture of the final product, namely, the inputs, can be allowed for utilizing towards payment of duty on the final product. In this case before us, the admitted position is that the extrusion machines manufactured by the applicant, after being fully manufactured, are tested by feeding them with plastic granules to see whether the machines so manufactured produce lay flat tubing without any defects. Therefore, the plastic granules are used after the final product, namely, the extrusion machine, manufactured by the applicant is fully finished. It is only to detect defects, if any, in the finished product.

19. In this view of the matter, and having regard to the scope of Rule 57A of the Act, we are unable to accept the contention of the applicant that materials used for testing the fully finished machines would also be the materials used in or in relation to the manufacture of the final product, namely, the extrusion machine. In the instant case, we find that Form Fill and Seal Machine is used for testing its performance. Testing performance is not a process of manufacture and, therefore, flexible plastic films used for testing the performance of the machine cannot be termed as "inputs" for the purpose of allowing Modvat credit of duty paid on flexible plastic films.

20. In the above facts and circumstances of the case, we are unable to accept the contention of the applicant. Accordingly, both the questions are answered in the negative, i.e. against the applicant and in favour of the respondents.

21. The reference stands disposed of accordingly.