(2006) 09 PAT CK 0048

In the Patna High Court

Case No : CWJC No. 13927 of 2005

McDowell and Co. Limited — APPELLANT

Vs

The State of Bihar and Others — RESPONDENT

Date of Decision : 21-09-2006

Acts Referred:

Constitution of India, 1950 — Article 265

Citation : (2006) 4 PLJR 269

Hon'ble Judges : J.N. Bhatt, C.J;Shiva Kirti Singh, J

Bench : Division Bench

Advocate : Sidharth Shankar Ray, R.B. Mahto, G.P. Vimal and Satyabir Bharti, for the Appellant; P.K. Shahi and Pumendu Singh for the State, for the Respondent

Final Decision : Allowed

Judgement

1. The Board of Revenue, Bihar in exercise of powers conferred by Section 90 of the Bihar Excise Act, 1951 (hereinafter to be referred to as ''the Act'') framed Rule 15B by way of amendment in the Bihar Excise Rules (hereinafter to be referred to as ''the Rules''). The purpose of which is to make a distiller responsible of maintaining minimum fermentation and distillation efficiencies and such minimum recovery of alcohol from molasses as prescribed in Rule 15B. Inter alia, this rule also provides in sub-rule (3) that "In case the recovery of alcohol is below the prescribed minimum, the officer incharge shall call for explanation of the distiller and forward the same along with his comments to the Excise Commissioner. The Excise Commissioner shall, if necessary, make enquiries in the matter and pass necessary order imposing penalty". It is the aforesaid power of the Excise Commissioner to impose penalty in the given situation which is under serious challenge in this writ petition filed by a Company which holds licences in Forms 19, 19B, 19C, 20 and 28A prescribed under the Act. The Company manufactures Extra Neutral Alcohol (ENA) as well as rectified spirit both being non-potable alcohol, unfit for human consumption. The

Company uses ENA in the manufacture of India Made Foreign Liquor (IMFL) and also exports ENA and rectified spirit to other distilleries and other industrial units. For admitted failure on the part of Company to maintain minimum recovery of alcohol during the period January 2000 to November 2001, the Company was given a notice for submitting explanation as to why penalty be not imposed for recovery of alcohol below the prescribed minimum. The petitioner submitted its explanation which was not accepted and a penalty of Rs. 1,19,07,614.08 paise was imposed by the Excise Commissioner, Bihar through an order dated 26.9.2002. On challenge by the petitioner through a writ petition bearing CWJC No. 13813 of 2002, the said order of the Excise Commissioner was found to be too cryptic and was, accordingly, set aside and the matter was remitted back to the Excise Commissioner, Bihar, Patna for passing a speaking order after affording an opportunity of hearing to the petitioner. Pursuant to said judgment and order dated 24.11.2003 petitioner was given opportunity of hearing and by impugned order dated 11.3.2005 contained in Annexure-15 the Commissioner of Excise, Bihar, Patna by a reasoned order rejected the explanation of the petitioner and decided to impose penalty under Rule 15B of the Rules on the basis of a principle adopted by the Excise Commissioner that penalty must be such as to compensate the State of Bihar for the loss of excise duty and loss of sales tax on the quantity of rectified spirit/ENA which could not be produced due to failure of the petitioner to achieve the minimum recovery of alcohol prescribed by Rule 15B. After calculating the penalty on the basis of order of the Excise Commissioner, the Excise Department has served the petitioner with a demand notice dated 4.10.2005 contained in Annexure-16 series whereby for the entire period between January 2000 to November 2002 a sum of Rs. 1,45,41,694.13 paise as penalty on account of notional loss of excise duty and Rs. 72,27,525.86 paise on account of notional loss of sales tax was imposed on the petitioner. The order of the Excise Commissioner contained in Annexure-15 and the demand notice contained in Annexure-16 series have also been challenged through this writ petition.

2. The main issues raised on behalf of the petitioner are following:

(i) The first ground for challenging the vires of Rule 15B is whether the State of Bihar can impose such penalty which amounts to excise duty on notional loss or production of rectified spirit i.e. alcohol not fit for human consumption, in view of Article 265 read with Entry 8 and Entry 51 of List II of the Seventh Schedule of the Constitution of India.

(ii) The vires of Rule 15B, particularly that part which vests the Excise Commissioner with the power to impose penalty has also been challenged on the ground that such power amounts to power of imposing excise duty by way of penalty through a subordinate legislation i.e. Rules framed by an Executive Authority, the Board of Revenue although no such power is vested in the Board of Revenue u/s 90 of the Act. Another related issue is whether Rule 15B is ultra vires the Act, particularly Section 27 thereof. Some other issues raised on behalf of the petitioner are to the effect that (iii) Rule 15B prescribes unrealistic and unattainable minimum efficiency and recovery levels without taking into consideration several ground realities and difficulties of distillers, particularly of the petitioner; (iv) loss of sales tax cannot be taken into account for the purpose of imposing penalty by the Excise Commissioner under the provisions of the Act and the Rules; (v) Rule 15B should not be applied to the petitioner because it is manufacturing ENA which is in technical parlance, a silent spirit of higher purity than rectified spirit "and for producing ENA a more complicated technical process is required which is bound to lead to lesser recovery of alcohol and (vi) that impugned order passed by the Excise Commissioner is illegal on account of improper consideration of various objections raised by the petitioner in its reply to the show cause notice contained in Annexure-12.

3. There is not much dispute over the relevant facts so far as they are essential for deciding the relevant issues. Hence, it is not deemed necessary to refer to the averments in the writ petition or their reply in the counter affidavit and supplementary counter affidavit of the State. On facts, the only specific reference made by learned Senior Counsel for the petitioner, Mr. Sidharth Shankar Ray was to paragraph 16 in the writ petition wherein the petitioner has enumerated various facts by way of reasons as to why the distillation efficiency of 97 per cent cannot be achieved. It was shown from paragraph 28 of the counter affidavit that the State and its authorities explicitly chose not to make comments on those averments in the writ petition. However, by a supplementary counter affidavit filed a day before the close of arguments, the State denied the contention of the petitioner mainly on the ground that under the same condition of electricity and with the same quality of molasses some other distilleries at Sitamarhi and West Champaran in Bihar were able to achieve recovery of rectified spirit from molasses almost to the required quantity as per Rule 15B of the Rules.

4. Mr. Sidharth Shankar Ray, learned Senior Advocate for the petitioner submitted that Section 27 and other relevant provisions of the Act make it clear that power to impose duty under the Act has been vested in the State Government which may prescribe rates in respect of various excisable articles either imported, exported, transported or manufactured. On facts, he demonstrated that notional excise duty by way of penalty was sought to be imposed by the Excise Commissioner when admittedly no such article was ever manufactured in the distillery of the petitioner. The ways of levying such duty as prescribed in Section 28(e) of the Act was also relied upon to submit that on spirit or beer manufactured in any distillery or brewery, duty may be imposed in permissible ways mentioned in that section. The main emphasis in the aforesaid submissions is upon the word "manufacture'' which is of relevance in this case. According to both the parties, penalty is being imposed to recover deemed toss of excise duty and some other losses such as sales tax due to lesser recovery of non-potable alcohol.

5. By referring to Section 90 of the Act, Mr. Ray further submitted that the power

of Board to make Rules is exhaustive. The 14 sub-sections of Section 90 cover different fields but none of them vests the Board of Revenue with the power to impose penalty by way of excise duty etc. on excisable goods admittedly not manufactured at all.

6. On the first and foremost issue of power of the State of Bihar under the constitutional scheme, it was submitted that Article 265 of the Constitution provides that no tax shall be levied or collected except by authority of law and the excise duty being a tax it cannot be levied even by way of penalty unless it falls within the legislative competence of State Legislature. Mr. Ray referred to List II i.e. the State List in Seventh Schedule, particularly Entry 8 and Entry 51 to show that the subject of production, manufacture, possession, transport, produce and sale of intoxicating liquor falls under the legislative competence of the State as per Entry 8, but this does not authorise the State Legislature to impose tax or cess on intoxicating liquor whereas Entry 51 specifically permits the State to levy duties of excise on the alcoholic liquors for human consumption manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India. By reference to Entry 84 of the List I i.e. the Union List, Mr. Ray pointed out that duties of excise on tobacco and other goods manufactured or produced in India could be levied by the Centre except on some goods enumerated as exceptions which include alcoholic liquors for human consumption hence, it was submitted that so far as alcoholic liquor for human consumption is concerned, the States had the legislative competence to authorise duties of excise but on other kinds of alcohol such as rectified spirit unfit for human consumption the legislative competence under the constitutional scheme vests only in the Centre.

7. On a bare perusal of the case laws cited on behalf of the petitioner which will be noticed hereinafter, the aforesaid proposition advanced by Mr. Ray appears as welt established and the learned Advocate General, appearing for the State of Bihar has accepted that the State Legislature can levy excise duties only on alcoholic liquors for human consumption. However, according to the learned Advocate General, the State Legislature has necessary competence to control the production, manufacture, possession, transport, produce and sale of intoxicating liquor under Entry 8 of the State List and in exercise of such power of control, if there is less production of non-potable alcohol by a distiller leading to loss of raw material and consequent loss in production of alcoholic liquors for human consumption within the State, it can impose penalty to prevent such loss or to make good the loss. According to him, the authority to impose penalty is different than power to levy duties of Excise on non-potable alcoholic liquor and such authority flows from the power to control production etc. as noticed earlier.

8. On behalf of the petitioner reliance has been placed upon judgment of a Division Bench of this Court in the case of The New Swadeshi Sugar Mills Ltd. vs. The State of Bihar, reported in 1983 PLJR 105. In that case the petitioner had challenged demand of a huge amount by the Excise Department on ground of

loss of revenue because rectified spirit, unfit for human consumption as alcoholic liquor was lost in transit through a truck under a transport pass issued by excise official. The demand was quashed while holding that rectified spirit is not fit for human consumption and therefore, no duty can be levied by the State Government in view of relevant constitutional provision i.e. Entry No. 51 of List II in Schedule VII of the Constitution. It was pointed out that it is well settled that if an article becomes dutiable at later stage by becoming fit for human consumption, excise duty cannot be levied at the prior stage where it is not fit for human consumption. This judgment was affirmed by the Supreme Court and the appeal of the State of Bihar was dismissed by judgment reported in (2003)11 SCC 478. The Supreme Court upheld the aforesaid proposition relying upon its judgment in the case of Synthetics and Chemicals Ltd. and Others Vs. State of U.P. and Others, .

9. Reliance was also placed on behalf of the petitioner on another Division Bench judgment of this Court in the case of Industrial Corporation Pvt. Ltd. and etc. Vs. State of Bihar and Others, . From paragraphs 20 and 21 of the said judgment it was shown that in similar situation, since there had been a shortfall in production of rectified spirit from moiasses the State had imposed penalty. This Court found that if molasses are diverted or misutilised, the contravention is under the Molasses Act or the rules framed there under but neither that Act nor the Excise Act contains any provision envisaging levy of any penalty and since "penal duty is also a part of excise duty, when State has no jurisdiction to impose excise duty. It certainly cannot levy any penal duty". Further, in paragraph 21 this Court held that requiring production of a particular quantity of country spirit from molasses supplied envisages fixed parameters and conditions and if such parameters are not met the production may be uneconomical but that itself cannot lead to a conclusion that there has been wastage or diversion of molasses inviting penalty under the Molasses Act. It was further noticed that spirit manufactured from molasses (since it is unfit for human consumption) cannot be subject to excise duty by the State under the Excise Act and it is too much to assume that because of shortfail of production of spirit there would be consequent shortfall of manufacture of potable liquor causing loss of revenue to the State. Reference was also made to Section 17 of the Act which contemplates payment of duty on removal from distillery, brewery, warehouse or other place of storage. There can be no removal of potable alcoholic liquor (intoxicant) unless the process for its manufacture is complete. On such consideration the Division Bench held that the excise authorities of the State of Bihar had no jurisdiction to levy the penalty or penal duty under the Act. This judgment was also affirmed by the Supreme Court in material aspect as the appeal of the State of Bihar was dismissed by judgment reported in State of Bihar and Others Vs. Industrial Corporation Pvt. Ltd. and Others, wherein after noticing the judgment of the Supreme Court in the case of Synthetics and Chemicals Ltd. and Others Vs. State of U.P. and Others, , it was held in paragraph 24 that only spirit meant for human consumption can be subjected to excise duty as held in The New Swadeshi Sugar

Mills Ltd. vs. The State of Bihar and hence in paragraph 25 of the judgment, the Apex Court held that no penal duty could have been imposed on rectified spirit. In this judgment reliance was also placed upon judgment of the Supreme Court in the case of State of U.P. and Others Vs. Modi Distillery and Others, . On behalf of the petitioner reliance has been placed on that judgment also. In paragraph 9 of the said judgment reliance was placed upon a Constitution Bench judgment of seven Judges in the case of Synthetics and Chemicals Ltd. vs. State of U.P. to hold that "intoxicating liquor" meant only that liquor which was consumable by human beings as it was. In paragraph 10 of the judgment levy of excise duty by State in cases of wastage of liquor after distillation, but before dilution and in case of pipeline loss of liquor during the process of manufacture, before dilution, was found to be without legal authority on the ground that the State in those situations was seeking to levy excise duty not upon alcoholic liquor for human consumption but upon the raw material or input still in process of being rendered fit for consumption by human beings.

10. Reliance was also placed on behalf of the petitioner on judgment of the Supreme Court in the case of Mohan Meakin Ltd. Vs. Excise and Taxation Commissioner, H.P. and Others, . In that case the issue was that beer, an alcoholic liquor fit for human consumption becomes liable to excise duty not. while it is in the process of manufacture and but only when it becomes finished product, the Court held that it can be subjected to excise duty only when it becomes finished product and is sought to be removed from the place of storage. On behalf of the petitioner reliance was also placed upon a judgment by three Judges of the Supreme Court in the case of Deccan Sugar & Akbari Co. Ltd. vs. Commissioner of Excise, (2004)1 SCC 243. That judgment is a brief one in which reliance has been placed upon judgments of the Supreme Court in Synthetics and Chemicals Ltd. vs. State of U.P. (supra) and in the case of State of UP vs. Modi Distillery (supra) to hold that certain wastage of ethyl alcohol which is not potable liquor fit for human consumption cannot be taxed by the State Legislature by levy of excise duty.

11. On the other hand, learned Advocate General, on behalf of the State has placed reliance upon judgments of the Supreme Court in the case of Bihar Distillery and Another Vs. Union of India (UOI) and Others, and in the case of State of U.P. and Others Vs. Vam Organic Chemicals Ltd. and Others, both by Bench of two Judges, to submit that the State Government has significant powers in respect of rectified spirit, although it is not alcoholic liquor fit for human consumption, to ensure that it is not diverted or misused for potable purposes and that duties of excise on rectified spirit cleared/removed for the purposes of obtaining or manufacturing potable liquors can be levied by the State Government concerned.

12. On careful consideration of the case laws, noticed above, and the relevant constitutional provisions, it is clear that Bench of three Judges of the Supreme Court in the case of State of U.P. vs. Modi Distillery (supra) have relied upon

judgment of Constitution Bench in the case of Synthetics and Chemicals Ltd. (supra) and decided in favour of the contention raised on behalf of the petitioner that State can levy excise duty only upon alcoholic liquor fit for human consumption when its manufacture is complete and not upon the raw material or input still in process of being rendered fit for consumption by human beings. State cannot impose duty of excise or sales tax on industrial alcohol i.e. alcohol unfit for human consumption. Again the judgment in the case of Deccan Sugar and Akbari Co. Ltd. vs. Commissioner of Excise (supra) by three Judges of the Supreme Court clearly supports the stand of the petitioner that State Legislature cannot impose any excise duty on rectified spirit because it does not fall under the category of potable liquor fit for human consumption.

13. So far as judgments cited by the learned Advocate General are concerned, they deal only with situations requiring administrative control over manufacture of rectified spirit for purpose of further use and in that context the power of the State Government was recognised that it can frame schemes to ensure that such rectified spirit is removed or used only for lawful purposes and not for manufacture of illegal potable liquor in the State. The issue in those cases were different and did not relate to the controversy at hand as to whether the State Government can impose excise duty upon alcoholic liquor unfit for human consumption directly or even by way of penalty under the Excise Act. So far as this issue is concerned, the stand of the petitioner is fully supported by judgments of the Apex Court cited on behalf of the petitioner on the basis whereof it can safely be held that State cannot levy excise duty on rectified spirit or other kind of alcohol unfit for human consumption and it cannot do so even by resorting to levy penalty on the ground of alleged loss or inefficiency in the system of a distiller engaged in manufacture of industrial alcohol, rectified spirit or any alcoholic liquor unfit for human consumption.

14. On behalf of the State no good reasons could be advanced as to why this Court should not follow the earlier views expressed by Division Benches of this Court in the case of The New Swadeshi Sugar Mills Ltd. and M/s Industrial Corporation Private Ltd. which have been affirmed by the Supreme Court as noticed earlier, upholding principles of law which clearly favour the stand of the petitioner as noticed in this judgment.

15. Since the demand of penalty by way of duty of excise on deemed loss of rectified spirit due to inefficient manufacturing process of the petitioner is beyond the legislative competence of the State Legislature and in fact not contemplated by the provisions of the Act nor the State is competent to impose Sales Tax on industrial alcohol and that too, by way of penalty, hence, the impugned order of the Excise Commissioner and the impugned demand have to be quashed. They are quashed accordingly.

16. Before parting with the judgment, it appears necessary to address the anxiety of the State Government that it must have some means to ensure that alcoholic liquor unfit for human consumption such as rectified spirit is not

diverted or misused for potable purposes specially by manufacturers like the petitioner which also manufacture potable liquors using the rectified spirit as a raw material. In response to such an anxiety reflected in the submissions advanced on behalf of the State of Bihar, it is deemed necessary to point out that the State Government has necessary power, short of levying excise duty, to exercise administrative control over manufacture of rectified spirit. This is recognised not only in paragraph 43 of the Supreme Court judgment in the case of State of U.P. vs. Vam Organic Chemicals Limited, relied upon by the learned Advocate General but also in paragraphs 63 and 86 of judgments of the Constitution Bench of the Supreme Court in the case of Synthetics and Chemicals Limited vs. State of U.P. which have been quoted in paragraphs 27 and 28 of the aforesaid judgment in the case of State of U.P. vs. Vam Organic Chemicals Limited. As per the Constitution Bench judgment- "The State have the power to regulate the use of alcohol and that power must include power to make provisions to prevent and/or check industrial alcohol being used as intoxicating or drinkable alcohol". In that judgment it was also concluded that "it may lay down regulations to ensure that non-potable alcohol is not diverted and misused as a substitute for potable alcohol". Although the State Government cannot impose duty of excise on industrial and/or non-potable alcohol, it can charge fees based on quid pro quo. It is for the State Government to create required infrastructure for exercise of aforesaid administrative control over manufacture of industrial alcohol and it may also levy reasonable fee to realize the cost of such machinery in case such machinery is created and if it succeeds in collecting evidence regarding surreptitious conversion of industrial alcohol into potable alcohol then the matter would definitely stand on a different footing. In that event on account of evidence regarding surreptitious manufacture of potable alcohol the State may proceed to realise loss of excise duty. It is entirely for the State Government to keep in mind the aforesaid legal position for framing appropriate scheme, if so advised. Nothing more needs to be stated in respect of aforesaid anxiety of the State Government. In view of success of the petitioner on the first issue itself, it is not necessary or desirable to go into merits of other issues raised on behalf of the petitioner and hence, the other issues are not taken up for decision. The writ petition is allowed and the impugned order contained in Annexure 15 as well as the impugned demand contained in Annexure 16 series are hereby quashed. In the facts of the case, there shall be no order as to costs.

