

(2004) 09 KAR CK 0045
In the Karnataka High Court
Case No : Writ Appeal No. 2922 of 2002

State of Karnataka and Others	Vs	APPELLANT
Thirumala Distilleries		RESPONDENT

Date of Decision : 23-09-2004

Acts Referred:

Evidence Act, 1872 — Section 114
Karnataka Excise (Distillery and Warehouse) Rules, 1967 — Rule 25, 26
Karnataka Excise Act, 1965 — Section 16, 22, 23, 36, 45

Citation : (2004) 6 KarLJ 194

Hon'ble Judges : H. Billappa, J;B. Padmaraj, J

Bench : Division Bench

Advocate : V.Y. Kumar, for the Appellant; Puttige R. Ramesh, Imran Pasha and R. Lokesh, for the Respondent

Final Decision : Dismissed

Judgement

B. Padmaraj, J.—Heard the arguments of the learned Government Advocate for the appellants and the learned Counsels for the respondent, at a considerable length and carefully perused the relevant case papers, including the impugned judgment and order of the learned Single Judge, in the light of the relevant provisions of the Karnataka Excise Act, 1965 and the Rules framed thereunder and also the precedents.

2. This is a writ appeal filed by the appellant-State and its authorities against an order of the learned Single Judge of this Court in Thirumala Distilleries, Tumkur Vs. State of Karnataka and Others, , whereby the writ petition filed by the respondent-distillery has been allowed and the orders made by the appellants 2 and 3 at Annexures-J and G to the writ petition, have been set aside or quashed and an amount of Rs. 11,00,000/- deposited, if any by the respondent-distillery with the appellant 3 in compliance with the interim order dated 7-6-2000 has been ordered to be refunded to the respondent distillery within a specified date, failing which the said amount becomes payable to the respondent-distillery with

simple interest at 12% per annum thereon calculated from the date of its deposit till the full payment thereof to the respondent and that he shall be entitled to refund of the same with interest accordingly. Aggrieved by such order of the learned Single Judge of this Court, the appellants herein are in appeal before us.

3. The respondent herein is a distillery, manufacturing India made liquor under a licence granted by the appellants under the provisions of Karnataka Excise (Distillery and Warehouse) Rules, 1967. The respondent-distillery as per the terms and conditions of the licence issued to it, is bound by the conditions of the licence as well as the provisions of the Karnataka Excise ? Act and the Rules framed thereunder particularly the Karnataka Excise (Distilleries and Warehouse) Rules. The respondent for the purpose of manufacture, purchases rectified spirit from the primary distilleries and transports it to the distilleries under the permit issued by the competent authority and utilizes the rectified spirit so purchased for the purpose of manufacture of India made liquor, on which the respondent is liable to pay the excise duty. The provisions of the rules and the conditions of the licence regulate the storage, manufacture, transport, use and sale of rectified spirit brought to the distillery for the purpose of manufacture of the India made liquor. It is stated that the distillery officer attached to the respondent distillery detected a shortage of 11,624 litres of rectified spirit in the storage tank No. 1 of the respondent and on satisfying himself that there was shortage of the above mentioned quantity of rectified spirit, registered a case in No. 1/94-95 and intimated the factum of registering the FIR to the authorities concerned. After investigation, it was found that the respondent herein could not account for the shortage of 11,624 litres of rectified spirit. During the pendency of the investigation of the above offence committed by the respondent herein, the respondent filed a representation/application before the second appellant u/s 45 of the Karnataka Excise Act, 1965, seeking for compounding of the offence by admitting the shortage and agreed to compound the offence and offered to pay the compounding fee and the value and such other duty on 11,624 litres of rectified spirit. On receipt of the said application of the respondent herein, the 3rd appellant passed the impugned order dated 3-6-1995 compounding the offence by levying the composition fee and directed the respondent to pay the composition fee along with the excise duty, sales tax, surcharge etc., on the India made liquor that would have been manufactured by the respondent from out of the 11,624 litres of the rectified spirit which was found deficit and not accounted for by the respondent. After the receipt of such order, the respondent herein had paid only the composition fee of Rs. 5,000/- and did not pay the excise duty and the other fees levied by the 3rd appellant and challenged the impugned order of the 3rd appellant before the second appellant u/s 61(2) of the Karnataka Excise Act. The 2nd appellant after hearing the matter confirmed the order passed by the 3rd appellant and dismissed the A KLJ PUBLICATION appeal of the respondent by its impugned order dated 19-8-1999. Aggrieved by the orders passed by the 2nd and 3rd appellants, the respondent herein filed the writ petition contending inter alia that the appellate authorities have no authority to

levy excise duty on the rectified spirit and that further the levy of excise duty on the India made liquor is on the basis of a presumption and that no tax or duty could be levied on the basis of presumptions. The appellants resisted the writ petition and filed their detailed statement of objections contending that the appellants are well-within their powers to levy excise duty on the India made liquor as the respondent is duty-bound to account for the shortage of the rectified spirit brought to the distillery for the purpose of manufacturing of India made liquor and that thereby he has contravened the provisions of the distillery rules as well as the Karnataka Excise Act. The appellants further contended that when once the respondent invited the order of compounding, he cannot retract from the compounding order and comply with only a portion of the order and challenge the other portion of the order wherein he is legally liable to pay the excise duty, which was calculated on the basis of the shortage of the rectified spirit. The learned Single Judge heard the parties apart from receiving the written arguments and the replies filed by the parties, and by his impugned order dated 15-3-2002 allowed the writ petition, holding that the appellants have no authority to levy the excise duty on the rectified spirit and further directed the appellants to refund Rs. 11,00,000/- that was deposited by the respondent with the 3rd appellant in compliance with the interim order dated 7-6-2000 on or before the date 30-4-2002, failing which the said amount becomes payable to the respondent with simple interest at 12% per annum thereon calculated from the date of its deposit till the full payment thereof to the respondent. Calling in question the legality of the order passed by the learned Single Judge, the instant writ appeal has been filed by the appellants.

4. Learned Government Advocate for the appellants, while assailing the impugned judgment and order of the learned Single Judge, has contended as under:

The learned Single Judge has misconstrued the provisions of law thereby holding that the appellants are insisting on payment of excise duty on rectified spirit. On the contrary what has been demanded by the excise authorities is the excise duty on India made liquor that would have been manufactured by the respondent-distillery from 11,624 bulk litres of rectified spirit. The provisions of the relevant rules particularly Rule 25 and Rule 26 of the Karnataka Excise (Distillery and Warehouse) Rules, 1967 casts the entire burden upon the respondent to account for any shortage or deficiency in stock or to report the breaches in law committed by their servants. Further when a certain quantity of spirit is received into the distillery, Rule 16 postulates that such spirit received by the distillery shall be accompanied by the permit issued by the Deputy Commissioner and all those spirits shall be gauged and proved on their arrival in the presence of the distiller by the distillery officer and the distiller is again cast with the responsibility for the quantity A KLJ PUBLICATION and strength of the spirits received and stored in the warehouse in the joint lock and key of the distiller and the distillery officer. Under the circumstances, therefore, an inevitable presumption has to be drawn from the above that all those spirits

which are received by the distiller and stored in the warehouse are meant for manufacture of India made liquor and the distiller cannot use this stock for any other purpose. That in the instant case, it is an admitted fact that out of the total stock of rectified spirit received by the respondent, which was kept in the warehouse, the distillery officer found a shortage of 11,624 litres of rectified spirit, for which the respondent was unable to account for. In fact the respondent admitted to the shortage so detected. Under these circumstances, the excise authorities were duty-bound to levy excise duty on the quantity of the India made, liquor that would have been manufactured out of this 11,624 litres of rectified spirit. The learned Single Judge has failed to take note of the Full Bench judgment of this Court in *S.V. Bagi Vs. State of Karnataka*, wherein the Full Bench has categorically held that once the offence is compounded, the offender cannot retract from his voluntary action of getting the offence compounded. The learned Single Judge without assigning any reasons has observed that the said decision is not applicable to the facts of this case. When once the offence is compounded by the authorities, it is not open to the offender to retract from his voluntary action more so when the offender had come up with an application seeking to compound the offence thereby admitting the guilt and in lieu of prosecution for cancellation of its licence submitted himself to the jurisdiction of the authority and compounded the offence. That in the instant case, when the shortage of 11,624 litres of rectified spirit was brought to the notice of the respondent, the respondent being assured of the possibility of being found guilty of the offence and upon satisfying itself that it was in its best interest and to avoid the disgrace and ignominy of the prosecution, voluntarily filed an application for compounding the offence, accepted the compounding order and paid the compounding fee, but however refused to pay the excise duty which is a consequential order. Having invited a decision and paid the compounding fine by virtue of which the process of compounding was complete, the respondent cannot now resile from the consequential order passed by the excise authorities, which action would have been taken even otherwise if the respondent had to manufacture India made liquor out of the quantity of the rectified spirit which was found to be short. That the impugned compounding order passed by the excise authorities is a composite order wherein a sum of Rs. 5,000/- has been levied as a composition fine and the consequential excise duty has been demanded and as such it has to be accepted as a whole. That the learned Single Judge has totally misunderstood the provisions of the rules and has misapplied his mind to the facts of this case and instead applied principles for levying sales tax on taxable commodities wherein a presumption could not be drawn for levying sales tax. The levy of excise duty stands on a different footing from that of the provisions of the Karnataka Sales Tax Act, 1957 or the commodities exigible to the sales tax. The respondent-manufacturer owes a duty under Rule 25 of the Karnataka Excise (Distillery and Warehouse) Rules to give satisfactory account for all the spirits, which are not forth coming in excess of 1% wastage allowed and to pay excise duty on such liquor or spirits, which are not accounted for or found in excess of 1% wastage allowed. Furthermore, u/s 45 of the

Karnataka Excise Act whenever a case has been compounded and any material is seized as being liable for confiscation, such materials can be returned to the party on payment of the value thereof as estimated by the authority, compounding the case. In the present case, both the issues are involved. Under Rule 25 of the Karnataka Excise (Distillery and Warehouse) Rules, there is a responsibility on the distiller to account for the shortages in excess of 1% and also to pay excise duty, in case, he could not explain satisfactorily for such excess losses or shortages. Secondly, u/s 45 of the Karnataka Excise Act, the distiller has requested to compound the case and also came forward to pay the composition amount. In addition to the fine levied in lieu of the cancellation or suspension of licence, wherever any property is involved, the value also has to be paid. The value includes the basic price of liquor, excise duty and sales tax thereon. Accordingly, since the petitioner had engaged in the manufacture of liquor on the excess shortages, the value of liquor, excise duty and sales tax has been levied on the value of the liquor. Further, Section 23 of the Karnataka Excise Act deals with the manner of levying excise duty and excise duty can be levied on the goods manufactured or goods issued or on the alcoholic contents in the liquor or on the value of the liquor or on the raw materials used for the manufacture of liquor. Rule 2 of the Karnataka Excise (Excise Duties and Fees) Rules, 1968 makes it clear that an excise duty shall be levied on the excisable articles specified in column (2) of the Schedule A at the rates prescribed therein, when such excisable articles are issued from any distillery and accordingly, the excise duty on the liquor that could have been manufactured has been calculated and imposed on the respondent. In the case of *United Breweries Limited and Anr. v. State of Karnataka and Anr.*, W.P. No. 1024 of 1987, DD: 4-2-1992, this Court has held that in the absence of actual manufacture, the provisions to levy excise duty on the norms fixed by the Government on the raw materials utilised, cannot be levied as earlier to this case, there were no rules to levy excise duty on the materials used. But, however, this defect has been cured by introducing the Karnataka Excise (Regulation of Yield, Production and Wastage of Spirit, Beer, Wine or Liquors) Rules, 1998. Rule 8 of the said Rules specifically deals with levying of penalty for excess wastage or loss incurred during the process or production of spirit notwithstanding anything contrary contained in any other rules and to impose penalty at the rates equivalent to the rates of excise duty leviable on liquors under the Karnataka Excise (Excise Duties and Fees) Rules, 1968 and such reported excise wastage. That in the instant case, the respondent admits shortage of 11,620 litres of rectified spirit and in the absence of any explanation on the part of the respondent with regard to such shortage, the one and the only inference that can be drawn is that the said quantity of rectified spirit which was found deficit in the distillery has been converted into the IML and sold the same as Seconds and thus there is a clear evasion of excise duty. Thus the imposition of excise duty is on the liquor that was manufactured by the respondent by utilising the rectified spirit that was found short at the distillery and the authorities have not imposed any excise duty on the rectified spirit as such.

5. In support of his submissions, the learned Government Advocate for the appellants has relied upon the following decisions:

1. Mohan Meakin Breweries Ltd. Vs. Excise and Taxation Commr., Chandigarh and Others, ;

2. S.V, Bagi's case.

6. Per contra, the learned Counsel for the respondent-distillery in support of the impugned judgment and order of the learned Single Judge, has contended as under:

The specific case of the respondent was that the rectified spirit amounting to 11,624 bulk litres has been lost as waste while the distillery was under repair and hence the authorities ought to have collected payment for the same under Rule 25 of the Rules read with Schedule C of the Amendment Rules. If the authorities had collected on the said basis, the amount would have come to Rs. 5,912/-. Hence, the authorities have failed to exercise the power conferred on them. The first demand of Rs. 27,52,000/- and the modified demand at Rs. 21,18,989/- is based on notional levy of excise duty on the rectified spirit. It is stated that such a levy could not have been levied. The respondent does not dispute the fact that he had agreed to compound the offence. However, the accord of consent for compounding does not amount to accord for imposing penalty and it is all the more so in the light of Rule 21 of the Rules read with Schedule C of the Amendment Rules. The authorities erred in not noticing the same. The demand of penalty of Rs. 21,18,989/- for the wastage of 11,624 bulk litres of rectified spirit cannot be supported in law. The appellants admit that in the case of United Breweries Limited, this Court has held that in the absence of actual manufacture or the provisions to levy excise duty on the norms fixed by the Government on the raw materials utilised, excise duty cannot be levied and the appellants further admit that earlier to this case, there were no rules to levy excise duty on the materials used and that the said defect is stated to have been cured by introducing the Karnataka Excise (Regulation of Yield, Production and Wastage of Spirit, Beer, Wine or Liquors) Rules, 1998. Therefore, even as admitted by the appellants themselves, the defect has been cured in the year 1998 and till 1998, it was not cured and the case at hand is the one pertaining to the year 1995. Therefore, in the face of such admission made by the appellants themselves, there was no provision to levy excise duty on the raw materials utilised in the manufacture of the IML and hence the authorities were not justified in levying excise duty on the basis of the rectified spirit that was found deficit at the distillery. In the instant case, it is not in dispute that the respondent herein is running a distillery and he gets the rectified spirit for the purpose of manufacture of the IML and the rectified spirit so procured would be stored at the distillery and under Rule 14 of the relevant rules, the Commissioner of excise has power to appoint an officer in respect of each of the distilleries and accordingly, the 4th appellant was appointed under Rule 14 of the Rules in the distillery of the respondent herein to be in-charge to supervise the activities of

the distillery. Rule 20 of the Rules provides that such officer shall exercise direct supervision of the distillery. For the working of the distillery, the respondent gets the spirit from the Government and the same is stored as provided under Rule 16 of the Rules under the joint lock and key of the distillery with the officer appointed by the department. During the excise year 1994-95, it was felt desirable to carry out certain works in the distillery and as such, permission was sought for from the 4th appellant and the same was granted and thereafter repair works were undertaken. During the aforesaid period, there was leakage and evaporation of rectified spirit which had not been noticed by the Manager of the distillery and the same was reported by the 4th appellant and on the basis of such report, the 3rd appellant registered a case in No. 1 of 1994-95 on 30-7-1994 and made a report to the 2nd appellant herein. The said shortage of rectified spirit found at the distillery was admitted by the respondent herein and he sought for compounding and also admitted to pay levy under the 1993 notification. The offence was accordingly compounded u/s 45 of the Act. The respondent herein does not dispute the legal principle that one cannot retreat or resile from the offence compounded. Applying the same principle with regard to the appellants also, when they have compounded the offence, they cannot now reopen the same and cannot retreat. When the appellants made the demand for excise duty in respect of the deficit rectified spirit, the respondent felt that the department is re-opening the issue and hence came to the Court seeking appropriate relief. In respect of loss of rectified spirit, two courses were open to the department, one was to launch the criminal proceedings against the respondent u/s 36 of the Act and then impose the excise duty if they are entitled under law. As regards the criminal proceedings, it came to an end with the compounding of the offence u/s 45 of the Karnataka Excise Act, 1965. The only other debatable point is whether the excise duty is or is not payable by the respondent? As per the provisions contained under the Karnataka Excise Act, the excise duty could be levied u/s 22 of the Act on any excisable article manufactured or produced in the State under any licence or permit granted under the Karnataka Excise Act. Even if one were to manufacture liquor without a licence, no excise duty can be levied as the condition precedent is that it must be under a licence or permit. Therefore, if the respondent herein has manufactured illicit liquor without licence, excise duty cannot be levied and he can only be prosecuted in accordance with the provisions of the Karnataka Excise Act. For the breach of the conditions of the licence committed by the respondent, he could have been prosecuted u/s 36 of the Act, but no excise duty is leviable u/s 22 of the Act which is a charging section. There is no provision either under the Karnataka Excise Act or under any of the rules framed by the State to impose excise duty on the rectified spirit as the excise duty could be levied only on the excisable article manufactured or produced. That apart, it is highly difficult to believe that the respondent herein could have manufactured the IML by utilising the deficit stock without the same being noticed by the excise authorities who were deputed at the distillery to supervise the activities of the distillery and it cannot be expected that the said excise authorities could have remained silent if

the respondent had clandestinely manufactured the IML by making use of such a huge quantity of the rectified spirit which was found deficit at the distillery. It is humanly impossible for the respondent to have clandestinely manufactured the IML keeping the authorities in dark. The respondent does not allege anything against the 4th appellant. The fact that there is no connivance of the 4th appellant in the alleged fraudulent act is admitted by the appellants and that being so, the respondent could not have committed such fraudulent act without the same being noticed by the 4th appellant. Therefore, the alleged fraudulent act attributed to the respondent is only a myth. In the instant case, there is no seizure of any property and hence the question of paying the value thereof by the respondent will not arise. The notional theory sought to be pressed into service by the appellants is clearly impermissible in law. Further, this is not a case where there has been no explanation on the part of the respondent and on the other hand the respondent has clearly stated that when he was on pilgrimage tour, such a mistake has occurred in his absence and the same could be attributable to his manager. That apart, the respondent herein having gone on pilgrimage tour, he cannot explain as to how the deficit has occurred and it is for the 4th appellant to explain the same. But, however the respondent herein having admitted such deficit quantity of rectified spirit at the distillery, had compounded the offence with the department and paid the composition fee that was imposed u/s 45 of the Act. The offence having been compounded by the respondent, the appellants could not have imposed the excise duty on the deficit rectified spirit that was found at the distillery and hence there was a cause for the respondent to come to the Court seeking redress. Even otherwise, such a levy of excise duty by the excise authorities is clearly impermissible in law. Rule 25 of the Karnataka Excise (Distillery and Warehouse) Rules, 1967 has absolutely no application to this case. But, notwithstanding this, the respondent herein made an offer to make payment of the excise duty under the provisions contained in Karnataka Excise (Excise Duties and Privilege Fees) (Amendment) Rules, 1993 as per Schedule C. It is this offer, the respondent herein made in view of the word "value" referred to in Section 45 of the Karnataka Excise Act, 1965. The specific case of the respondent however is that there is no provision to collect excise duty and the said position of law is well-settled. When the appellants make reference to Rule 8 of 1998 Rules, they are virtually accepting the case of the respondent herein, as these rules were framed for the first time in the year 1998 and earlier to that there were no such rules to impose excise duty on the raw materials. As per 1998 Rules, lesser production of final product is covered by Rule 7 and loss of ingredient is covered by Rule 8 and accordingly under Rule 7 the authority can impose fine and likewise under Rule 8 it can impose penalty. But, no such rules were in existence as on the date when the offence was reported in the year 1995. The respondent reported loss of certain quantity of raw-material which he had taken for production of the IML and the same would have secured an income of Rs. 21.00 lakhs to the State exchequer in the form of the excise duty and since the final product is not there, the excise duty was sought to be levied by the appellants which is clearly impermissible in

law. In the instant case, the demand has been made on a notional basis and it is now a well-settled position of law that no demand of excise duty could be made on notional basis. Assuming that the alleged rectified spirit has been used in the manufacture of the IML, then also the respondent herein is not liable to pay the excise duty as it has taken place without his knowledge. The taxing statute cannot be interpreted on the basis of certain presumptions and assumptions. Therefore, when the excise duty was sought to be imposed by the appellants on the basis of certain assumptions and presumption, the learned Single Judge of this Court was right in holding that the excise authorities are not empowered under law to demand such levy and hence the demand and levy made by the excise authorities has been rightly quashed by the learned Single Judge. Hence the impugned order made by the learned Single Judge warrants no interference in the appeal.

7. In support of his submissions, the learned Counsel for the respondent has relied upon the following decisions:

1. K.H.K. Rehaman and Ors. v. State of Mysore and Ors., ILR 1973 Mys. 124;
2. K.H. Abdul Salam v. State of Karnataka 1980(1) Kar. L.J. 104;
3. Unreported judgment of the learned Single Judge of this Court in the case of Mis. Gemini Distilleries (Private) Limited v. State of Karnataka and Ors., W.P. No. 8781 of 1983 connected with W.P. No. 8788 of 1983, DD: 4-12-1987;
4. Unreported judgment of the learned Single Judge of this Court in the case of Mis. United Breweries Limited;
5. Synthetics and Chemicals Limited v. State of Uttar Pradesh and Ors., ;
6. State of U.P. and Others Vs. Modi Distillery and Others, ;
7. Deccan Sugar and Abkari Co. Ltd. Vs. Commissioner of Excise, A.P., ;
8. Govindanaik G. Kalaghatigi Vs. West Patent Press Co. Ltd. and Another, ;
9. State of Mysore v. Hosbu Rush Gowda, 1973(1) Mys. L.J. 92;
10. M. Narasimhaiah Vs. Deputy Commissioner for Transport, Bangalore Division, Infantry Road, Bangalore and Another, ;
11. Bimal Chandra Banerjee Vs. State of Madhya Pradesh etc., ;
12. Vam Organic Chemicals Limited and Anr. v. State of Uttar Pradesh and Ors., 1997(43) Kar. L.J. 243 : (1997)2 SCC 716 : 1997(1) Supreme 550 : 1997 Scale 361;
13. State of Karnataka and Ors. v. J.P. Distilleries and Ors., W.A. Nos. 3501 to 3540 of 1997, DD: 16-3-2001.

8. While placing reliance upon these decisions, the learned Counsel for the respondent has vehemently contended before us that the demand made on

notional basis by the excise authorities was clearly impermissible in law and that further when the matter had been compounded by the respondent with the department, the same stands closed and the appellant State is estopped from re-opening the said issue again by seeking to impose the excise duty on the rectified spirit that was found deficit at the distillery. Besides this, the impugned order made by the excise authorities imposing excise duty on the deficit rectified spirit was hit by Section 22 of the Karnataka Excise Act for the reason that the excise authorities cannot levy excise duty on the rectified spirit and there cannot be any imposition of excise duty on notional basis in view of the decision rendered by this Court in United Breweries case. The excise duty sought to be imposed by the excise department on the notional theory was clearly unsustainable in view of the decision rendered by this Court in United Breweries case, which was holding the field as on date and the legal defect pointed out in United Breweries case, came to be cured only by 1998 Rules which have no retrospective effect.

9. By way of reply, the learned Government Advocate for the appellants has further contended that the appellants do not dispute the propositions of law laid down by any of the decisions relied upon by the learned Counsel for the respondents, but they have no application to the facts and circumstances of the case at hand. That in the instant case, the respondent does not dispute and on the other hand the respondent specifically admits that there was a shortage of rectified spirit at the distillery owned by it and having admitted such deficit, he had made an offer to compound the offence committed by him and accordingly the offence was compounded by an order made u/s 45 of the Karnataka Excise Act. When once the process of compounding is completed, the respondent cannot decline to pay the amount demanded under the order of compounding of the offence. Further, from the admitted and proved facts, coupled with the conduct of the respondent, a reasonable inference is that the respondent had utilised the said quantity of rectified spirit that was found deficit in the distillery for manufacturing the IML and hence liable for excise duty. That in the instant case, the State Government has not demanded excise duty on the rectified spirit that was found deficit at the distillery, but had demanded the excise duty on the IML which was manufactured clandestinely by the respondent by utilising the quantity of the rectified spirit that was found deficit at the distillery. That apart, in the process of compounding, the excise authorities having suggested certain other amounts to be payable by the respondent and the same having been accepted by the respondent, the order of compounding was binding upon the respondent and it was not open to him to challenge it. The calculation of the excise duty was made on the basis of Section 23(b) of the Karnataka Excise Act read with Rule 25 of the Karnataka Excise (Distillery and Warehouse) Rules, 1967 and the said calculation was made on the basis that the respondent had clandestinely manufactured the IML by utilising the deficit rectified spirit that was found at the distillery which has not been properly accounted for by the respondent. Under the circumstances, therefore, it is not a case of notional loss but a case of actual

admitted loss of the rectified spirit which has been utilised in the manufacture of IML by the respondent. Hence, the order passed by the learned Single Judge warrants interference in the appeal.

10. Having heard the submissions on both sides and having carefully perused the relevant provisions of the Act and Rules in the light of the decisions relied upon by the learned Counsel on either side, the question for consideration is whether the impugned order made by the learned Single Judge in the writ petition, warrants any interference in the appeal?

11. Now it is well-settled that a decision is an authority for which it is decided and not what can logically be deduced therefrom. It is also well-settled that a little difference in facts or additional facts may make a lot of difference in the precedential value of a decision. Each case depends on its own facts and a close similarity between one case and another is not enough because even a single significant detail may alter the entire aspect. In deciding such cases, one should avoid the temptation to decide cases by matching the colour of one case against the colour of another. To decide therefore, on which side of the line a case falls, the broad resemblance of another case is not at all decisive. In this connection, a reference may be made to the decisions of the Hon''ble Supreme Court in the case of *Ashwani Kumar Singh Vs. U.P. Public Service Commission and Others*, , in the case of *Haryana Financial Corporation and Another Vs. Jagdamba Oil Mills and Another*, , in the case of *Megh Singh Vs. State of Punjab*, and in the case of *Padmasundara Rao and Others Vs. State of Tamil Nadu and Others*, .

12. Bearing in mind, the above principles, we shall now proceed to consider the case on merits with reference to the facts and peculiar circumstances of this case.

13. The respondent firm is a licenced manufacturer of the India made liquor at Tumkur. It is running a distillery under a valid licence granted by the competent authorities of the Excise Department under the provisions of the Karnataka Excise (Distillery and Warehouse) Rules for the manufacture of the India made liquor. Manufacture, sale as also storage and transport of liquor are regulated by the Karnataka Excise Act and the Karnataka Excise (Distillery and Warehouse) Rules, Karnataka Excise (Excise Duties and Fees) Rules and the Karnataka Excise (Denatured Spirit and Denatured Spirituous Preparations) Rules and the Karnataka Excise (Sale of Indian and Foreign Liquors) Rules and certain other rules, all made under the Karnataka Excise Act. Excise duty as defined u/s 2(8) of the Karnataka Excise Act is leviable on the manufacture of liquor and the manufacturer cannot remove the same from the distillery unless the excise duty imposed under the Karnataka Excise Act has been paid. There could be no dispute that the rectified spirit is liquor within the meaning of this term as defined u/s 2(18) of the Karnataka Excise Act. The terms, liquor as defined u/s 2(18) of the Act includes spirits of wine, denatured spirits, wine, beer, toddy and all liquids consisting of or containing alcohol or wash and any other intoxicating substance which the State Government may by notification declare to be liquor for the purposes of the Karnataka Excise Act. The buyers of the India made

liquor from the distilleries including the distillery of the respondent firm have to obtain the distillery passes or permits for the release of liquor after making payment of the excise duty and present the same at the distillery, whereupon the bill of sale or invoice is prepared by the distillery showing the price of the liquor. Rule 34 of the Karnataka Excise (Distillery and Warehouse) Rules provides that no spirits shall be removed from the distillery except under a permit in Form 3 issued by the Distillery Officer. Further Rule 16 of the said rules provide that no spirit shall be received into distillery unless they are accompanied by the permits issued by the Deputy Commissioner and all such spirits shall be gauged and proved on their arrival in the presence of the distiller or his representative, who will be responsible for the quantity and strength of the spirits received and stored in the warehouse, which are under the joint lock and key of the Distillery Officer and the distiller. Rule 18 of the said rules provide that the Government shall not be responsible for the destruction or loss or damage to any spirit stored in a distillery by fire or theft or by gauging or proving or by any other cause whatever and in case of fire or other accidents, the Distillery Officer shall immediately attend and open it, if necessary, at any hour by day or night. Rule 21 of the said rules provides that no person other than the licensee or his authorised vendors or agents or employees of the distillery shall be allowed to enter the distillery premises without the permission of the Distillery Officer. Rule 24 of the said rules provides that the distiller shall maintain regular accounts in the forms required by the Commissioner from time to time and such accounts shall be open for inspection at all times, by the Distillery Officer or any officer duly authorised and that further spirits in the distillery shall, at all times be open to gauging and proving by the Distillery Officer or any officer duly authorised. Rule 25 of the said Rules provides that an account shall be taken of the stocks of spirit kept in the distillery at such intervals not exceeding three months and in such manner as the Deputy Commissioner may direct and the distiller shall pay such duty on all spirits which are not forthcoming and which could not be accounted for to the satisfaction of the Deputy Commissioner, in excess of an allowance of 1% of wastage. The wastage shall be calculated at the end of every 12 months or at the end of licence period, if it is shorter, for the purpose of calculating the duty on the excess as aforesaid. Rule 26 of the said Rules provides that the distiller shall be bound to report immediately to the Distillery Officer and the Deputy Commissioner any breaches committed by any person employed by him in the manufacture, storage, receipt, blending or issue of spirits and he shall be bound to comply with the directions of the Deputy Commissioner respecting the continued employment of such persons. It is to be seen from the relevant rules of the Karnataka Excise (Distillery and Warehouse) Rules, 1967 that no spirit or liquor manufactured or stored shall be removed from the distillery unless the excise duty specified in Rule 2 of the Karnataka Excise (ED and F) Rules has been paid by a holder of the licence before such removal. The licensee for wholesale vend of the IML shall purchase the liquor only from the licensed distillery, brewery or winery located within the State and/or from a licensed distributor having CL-11 licence and shall sell liquors to persons holding CL-2 to CL-7, CL-7-

A and C-7-B, CL-9 and CL-10, vide Rule 3 of the Karnataka (SOI and FL) Rules. In the instant case, it is not in dispute that the respondent herein is the holder of a licence under the Karnataka Excise (D and WH) Rules. Condition 5 of the said licence prescribes that the licensee is prohibited from manufacturing any of the spirits, save the ones specifically instructed. Conditions 6 and 7 of the said licence prescribes that the licensee is prohibited from issuing any of the spirits except with the permission of the distillery officer or a competent authority and the account of the transactions in the distillery relating to wash and spirits should be maintained in such forms and in such manner as may be prescribed by the Commissioner. Now we shall have a fresh look at Rules 20-A, 21, 24, 25, 26 and 34 of the Karnataka Excise (D and WH) Rules. Rule 20-A specifically provides that the distiller shall establish a well-equipped chemical laboratory to the satisfaction of the Excise Commissioner within the premises of the distillery to check the quality of raw materials used and the liquor produced in the distillery, which shall be manned by a chemist holding a degree in science with chemistry as one of the subjects, preferably organic chemistry or biochemistry or specialisation in alcohol technology and that the liquor produced in the distillery shall be released for sale only after the chemist referred to in sub-rule (1) certifies that such liquor is fit for human consumption. Rule 21 prescribes that no person other than the licensee or his authorised vendors or agents or employees of the distillery shall be allowed to enter the distillery premises without the permission of the distillery officer and a list of such employees of the distillery shall be furnished to the distillery officer by the distiller. Rule 24 prescribes that the distiller shall maintain regular accounts in the forms required by the Commissioner from time to time and such accounts shall be open for inspection at all times by the distillery officer or any officer duly authorised and Rule 25 prescribes that an account shall be taken of the stocks of the spirits kept in the distillery at such intervals not exceeding three months and in such manner as the Deputy Commissioner may direct and the distiller shall pay such duty on all spirits, which are not forthcoming and which could not be accounted for to the satisfaction of the Deputy Commissioner in excess of an allowance of 1% of wastage and the wastage shall be calculated at the end of every 12 months or at the end of licence period, if it is shorter, for purpose of calculating duty on the excess as aforesaid. Rule 26 casts an obligation upon the distiller to report breaches of law etc., committed by their servants and it prescribes that the distiller shall be bound to report immediately to the distillery officer and the Deputy Commissioner any breaches committed by any person employed by him in the manufacture, storage, receipt, blending or issue of spirits and he shall be bound to comply with the directions of the Deputy Commissioner respecting the continued employment of such persons. Then Rule 34 prescribes that no spirits shall be removed from the distillery except under a permit in Form III issued by the distillery officer. There could be no dispute that the respondent distiller is bound by all these Rules. Now a reference may be made to Sections 16, 22, 23, 36 and 45 of the Karnataka Excise Act. Section 16, which deals with the establishment of distilleries and warehouses prescribes that the Excise

Commissioner may with the previous sanction of the State Government: (a) establish a distillery in which spirit may be manufactured under licence granted u/s 13 on such conditions as the State Government may impose; (b) discontinue any distillery so established; (c) licence on such conditions as the State Government deems fit to impose, the construction and working of distillery or brewery; (d) licence a private bonded warehouse (e) establish or licence a warehouse wherein intoxicants may be deposited and kept without payment of duty; and (f) discontinue any warehouse so established. Sub-section (2) of Section 16 prescribes that a warehouse established under sub-section (1) shall be for general accommodation to warehouse intoxicants subject to duty pending removal for local consumption or for export and sub-section (3) of Section 16 prescribes that without the sanction of the State Government, no intoxicant shall be removed from any distillery, brewery, warehouse or other place of storage established or licensed under this Act unless the duty, if any, imposed under this Act has been paid or a bond has been executed for the payment thereof. A warehouse established or licensed u/s 16(e) is also a warehouse within the meaning of that expression in Section 23 and excise duty can be levied on articles issued therefrom. Section 22 giving power to Government to fix rates of duty is not invalid for excessive delegation. Though the preamble may not give any guidance, the legislative control over the delegate may take several forms. Section 71 of the Act which provides for the Rule making power imposes necessary check upon the wide power given to Government to fix rates. The laying down of the rules u/s 71(4) is control over delegated legislation. The excise duty is primarily a duty on the production or manufacture of goods produced or manufactured within the State. Subject always to the legislative competence of the taxing authority, the said tax can be levied at a convenient stage so long as the character of the impost is not lost. The method of collections does not affect the essence of the duty, but only relates to the machinery of collection for administrative convenience. In order to be an excise duty, the levy must be upon the goods and the taxable event must be the manufacture or production of goods. Thus the incidence of excise duty is directly relatable to manufacture, but its collection can be deferred to a later stage as a measure of convenience or expediency. The duty is primarily a burden which the manufacturer had to bear and even if the purchasers paid the same under the Karnataka Excise (Distillery and Warehouse) Rules, the provisions are merely enabling and did not give rise to any legal responsibility or obligation for meeting the burden. Section 22 of the Karnataka Excise Act provides that an excise duty at such rate or rates as the State Government may prescribe, shall be levied on any excisable article manufactured or produced in the State under any licence or permit granted under this Act. Thus the payment of excise duty is that of the manufacturer. The employment of the supervisory staff at the distillery as contemplated under Rule 14 and the attendance of the Excise Officers deputed at the , distillery as contemplated under Rule 15 of the Karnataka Excise (Distillery and Warehouse) Rules, 1967 do not in any way militate against the conclusion that the payment of the excise duty is a liability exclusively of the manufacturer.

Detailed provisions have been made regarding obtaining of distillery pass or permit, correct calculation and full payment of excise duty, the manner of depositing such duty and ultimately issue of the spirit under the pass or permit from the distillery. These rules therefore do not detract from the position that the payment of excise duty is the primary and exclusive obligation of the manufacturer and if payment be made under a contract or arrangement by any other person, it would amount to meeting of the obligation of the manufacturer and nothing more.

14. In the case of McDowell and Co. Ltd. Vs. Commercial Tax Officer, , the Hon"ble Supreme Court has concluded as under:

"21. Manufacture, sale - wholesale and retail - as also storage and transport of liquor are regulated by the Andhra Pradesh Excise Act, 1968 ("Excise Act" for short) and the Andhra Pradesh Distillery Rules, the Andhra Pradesh Indian Liquor (Storage in Bond) Rules and the Andhra Pradesh Foreign Liquor and Indian Liquor Rules, all made under the Excise Act. "Excise duty" as defined in Section 2(10) of the Excise" Act is leviable on the manufacture of liquor and the manufacturer cannot remove the same from the distillery unless the duty imposed under the Excise Act has been paid. Buyers of Indian Liquor from the appellant's distillery as alleged by it, obtain distillery passes for release of liquor after making payment of excise duty and present the same at the distillery whereupon the bill of sale or invoice is prepared by the distillery showing the price of liquor but excluding the excise duty. The appellant's books of account also did not contain any reference to excise duty paid by the purchaser. The appellant paid Sales Tax payable by it under the Andhra Pradesh General Sales Tax Act, 1957 ("Sales Tax Act" for short), on the basis of its turnover which excluded excise duty. The company was assessed to sales tax on the basis of its returns but later the Commercial Tax Officer was of the view that the Company had failed to include the excise duty paid on the liquor sold by it to wholesalers. The taxing authority "accordingly called upon the Company to show cause why assessments made may not be re-opened. The appellant moved the High Court for quashing of such notice and having failed, carried the matter in appeal to this Court. A Division Bench of this Court in McDowell and Company Ltd. Vs. Commercial Tax Officer VII Circle, Hyderabad, , examined the provisions of the Excise Act and Rules made thereunder as also the provisions of the Sales Tax Act. This Court took the view:

"We hold that intending purchasers of the India liquor who seek to obtain distillery passes are also legally responsible for payment of the excise duty which is collected from them by the authorities of the excise department".

This Court then proceeded to determine whether excise duty-paid directly to the Excise authorities or deposited directly in the State Exchequer in respect of Indian Liquor by the buyers before removing the same from the distillery could be said to form part of the taxable turnover of the appellant-distillery. Precedents were referred to and the Court came to the conclusion that⁷ excise duty did not

go into the common till of the appellant and did not become a part of the circulating capital. Therefore, the Sales Tax Authorities were not competent to include in the turnover of the appellant the excise duty which was not charged by it but was paid directly to the excise authorities by the buyers of the liquor. The appellant, therefore, succeeded before this Court and the notices issued by the Sales Tax Authorities were quashed.

22. The judgment of this Court was delivered on October 25, 1976. Rules 76 and 79 of the Distillery Rules were amended with effect from August 4, 1981. Rule 76(a) now provides: "No spirit or liquor manufactured or stored shall be removed unless the excise duty specified in Rule 6 has been paid by a holder of D2 licence before such removal". It is "not disputed that appellant is the holder of a D2 licence under the law. Amended Rule 79(1) provides:

"79(1) On payment of the excise duty by the holder of D2 licence a distillery pass for the removal of spirit fit for human consumption may be granted in favour of any of the following persons only, namely:-

(a) A person holding a licence in the Andhra Pradesh or in other States for sale of spirit by wholesale or retail and when the spirit is to be transported or exported beyond the limits of the district in which the distillery is situated to a person holding a permit signed by the Excise Superintendent of the District of destination or an officer of that district authorised in this behalf.

(b) A person holding a permit signed by the Officer of any other States referred to in clause (a) above for the export of such spirit from the Andhra Pradesh into that State.

(c) A person holding a permit signed by an officer duly authorised in that behalf for export of such spirit to an Union Territory.

(d) A person holding a permit from the Excise Superintendent of any district in the Andhra Pradesh or from an officer referred to in clause (a) above of any other State to transport or export rectified spirits or wine, to such district or State".

23. On the basis of the amended provisions the respondent-Officer issued a notice to the appellant proposing to include a sum of Rs. 4,49,09,552.40 representing the excise duty paid directly by buyers of appellant's liquor in the appellant's turnover for a part of the year 1982-83. Thereupon, the appellant again moved the High Court for quashing of the notice. Reliance was placed on the earlier decision of this Court. The High Court very appropriately felt bound by the decision of this Court and considered the effect of the amended Rules and held that the primary liability to pay excise duty was indisputably of the holder of the D2 licence. It further found that the turnover related to liquor; excise duty which was payable by the appellant but had by amicable arrangement been paid by the buyer was actually a part of the turnover of the appellant and was, therefore, liable to be so included for determining liability for sales tax. On these

findings the High Court dismissed the writ petition. When leave was granted by a Division Bench of this Court to appeal against the judgment of the High Court, the correctness of the decision in appellant's case *Mis. McDowell and Company Limited* was doubted and the matter was referred to a larger Bench. That is how this appeal came to be heard by us.

25. *The Federal Court in Province of Madras v. Boddu Paidanna and Sons*, AIR 1942 FC 33 : 1942 FCR 90, held:

"There is in theory nothing to prevent the Central Legislature from imposing a duty of excise on a commodity as soon as it comes into existence, no matter what happens to it afterwards whether it be sold, consumed, destroyed, or given away. A taxing authority will not ordinarily impose such a duty, because it is much more convenient administratively to collect the duty (as in the case of most of the Indian Excise Acts) when the commodity leaves the factory for the first time, and also because the duty is intended to be an indirect duty which the manufacturer or producer is to pass on to the ultimate consumer, which he could not do if the commodity had, for example, been destroyed in the factory itself. It is the fact of manufacture which attracts the duty, even though it may be collected later.-

This view has been followed by this Court and the position has been put beyond doubt by a series of decisions. In *R.C. Jall Vs. Union of India (UOI)*, , it has been observed:

"The excise duty is primarily a duty on the production or manufacture of goods produced or manufactured within the country. Subject always to the legislative competence of the taxing authority, the said tax can be levied at a convenient stage so long as the character of the impost is not lost. The method of collection does not affect the essence of the duty but only relates to the machinery of collection for administrative convenience".

26. In *Re: The Bill To Amend S. 20 of The Sea Customs Act, 1878 and S. 3 of The Central Excises and Salt Act, 1944*, , this Court said:

"With great respect, we accept the principles laid down by the said three decisions AIR 1939 1 (Federal Court); AIR 1945 98 (Privy Council) , in the matter of levy of an excise duty and the machinery for collection thereof.

27. In *Shinde Brothers etc. Vs. Deputy Commissioner and Others, etc.*, , Sikri, J. (as he then was), spoke for the majority and stated the ratio thus: "These cases establish that in order to be an excise duty (a) the levy must be upon goods and (b) the taxable event must be the manufacture or production of goods. Further the levy need not be imposed at the stage of production or manufacture but may be imposed later".

28. In *Jullunder Rubber Goods Manufacturers" Association Vs. The Union of India (UOI) and Another*, , Grover, J. after extracting a part of the judgment in *Jail's* case, spoke for the Court thus:

"The above statement of law in no way supports the argument that the excise duty cannot be collected from persons who are neither producers nor manufacturers. Its incidence certainly falls directly on the production or manufacture of goods but the method of collection will not affect the essence of the duty".

29. In *A.B. Abdul Kadir and Others Vs. State of Kerala*, , this Court restated the position thus:

"Excise duty, it is now well-settled, is a tax on articles produced or manufactured in the taxing country. Generally speaking, the tax is on the manufacturer or the producer, yet laws are to be found which impose a duty of excise at stages subsequent to the manufacture or production".

Thus the incidence of excise duty is directly relatable to manufacture but its collection can be deferred to a later stage as a measure of convenience or expediency.

30. On an examination of the provisions of the Excise Act, the Rules framed thereunder and the pronouncements referred to above, we are of the view that the conclusion of this Court at page 921 of *Mis. McDowell and Company Limited*'s case of the report that intending purchasers of the India liquors who seek to obtain distillery passes are also legally responsible for payment of the excise duty is too broadly stated. The "duty" was primarily a burden which the manufacturer had to bear and even if the purchasers paid the same under the Distillery Rules, the provisions were merely enabling and did not give rise to any legal responsibility or obligation for meeting the burden. We do not propose, however, to examine this aspect any further for the change in Rule 76 of the Distillery Rules has clearly affirmed the position that liability for payment of excise duty is of the manufacturer. Provisions of Rules 80, 81, 82, 83 and 84 do not militate against the conclusion that the payment of excise duty is a liability exclusively of the manufacturer. In these rules detailed provisions have been made regarding obtaining of distillery pass, correct calculation and full payment of excise duty, the manner of depositing such duty and ultimately issue of the spirit under the pass from the distillery. These rules, therefore, do not detract from the position that payment of excise duty is the primary and exclusive obligation of the manufacturer and if payment be made under a contract or arrangement by any other person it would amount to meeting of the obligation of the manufacturer and nothing more".

15. Now in this context, we will refer to Rule 25 of the Karnataka Excise (D and WH) Rules, which reads thus:

"25. Distiller to account deficiency in stocks.-An account shall be taken of the stocks of spirits kept in the distillery at such intervals not exceeding three months and in such manner as the Deputy Commissioner may direct. The distiller shall pay such duty on all spirits which are not forthcoming and which could not be accounted for to the satisfaction of the Deputy Commissioner, in

excess of an allowance of one per cent of wastage. The wastage shall be calculated at the end of every twelve months or at the end of licence period, if it is shorter, for purpose of calculating duty on the excess as aforesaid:

Provided that if it is proved to the satisfaction of the Deputy Commissioner or any officer appointed by him that any deficiency in excess of the margin allowed could not have been prevented by the exercise of proper care and precaution, the payment of duty on such deficiency may be waived".

16. A reading of the provisions contained in Rule 25 would make it clear that the distiller shall pay such duty on all spirits which are not forthcoming and which could not be accounted for to the satisfaction of the Deputy Commissioner, in excess of an allowance of 1% of wastage. However, the proviso to Rule 25 says that if it is proved to the satisfaction of the Deputy Commissioner or any officer appointed by him that any deficiency in excess of the margin allowed could not have been prevented by the exercise of proper care and precaution, the payment of duty on such deficiency may be waived.

17. In the instant case, it is not in dispute that on 30-7-1994 when physical stock of rectified spirit found at the distillery of the respondent firm was inspected by the concerned officer, there was a shortage of 11,624 bulk litres of the rectified spirit. The said shortage was not accounted for by the distillery to the satisfaction of the officer concerned. That being so, there was contravention of the provisions contained under Rule 25 of the Rules. Besides this, the said act committed by the distillery will amount to violation of the conditions of the licence issued to the respondent firm and was also be liable for prosecution u/s 36 of the Act. Obviously under these circumstances, the offence committed by the respondent firm was sought to be compounded u/s 45 of the Karnataka Excise Act, 1965. It is not in dispute that the shortage of such huge quantity of rectified spirit found at the distillery of the respondent firm having been reported by the Superintendent of Excise in charge at Thirumala Distilleries to the Deputy Commissioner of Excise, an offence or the crime was registered against the respondent-firm in Case No. 1 of 1994-95 on 30-8-1994 and the same was reported to the Commissioner of Excise at Bangalore. The Managing Partner of the respondent firm prayed the authorities to compound the offence departmentally as provided u/s 45 of the Act. The respondent also offered to pay the duty on all spirits, which was not forthcoming and which could not be accounted for by him. It was also made clear that the respondent is willing to pay the duty as provided under the provisions of the Karnataka Excise (Excise Duties and Privilege Fees) (Amendment) Rules, 1993. A representation was also made before the Commissioner of Excise at Bangalore, once again offering to compound the offence. The true copies of the respective representations made before the Deputy Commissioner of Excise at Tumkur and the Commissioner of Excise at Bangalore were produced along with the writ petition as per Annexure-A and B respectively and their near true translation in English were also produced as per Annexure-AI and BI respectively. Under Annexure-AI, dated 24-9-1994 the

respondent firm by its managing partner has stated as under:

"With regard to the above subject, it may be re-called that the Commissioner of Excise, Government of Karnataka, Bangalore has been requested that Case No. 1 of 1994-95 may be decided within the Department and the compensation payable in respect of the deficit quantity of 11,624.00 litres of liquefied spirit vide Notification No. FD 11 EPS 93, dated 30-3-1993, would be paid as fee to the Government (copy enclosed).

Hence, I request you that the said mistake may be pardoned and the matter may be decided within the Department and direction may be issued to pay the compensation in respect of deficit liquefied spirit as per the above Government notification".

18. Further, under the representation at Annexure-BI made to the Commissioner of Excise, Bangalore, the Managing partner of the respondent firm has stated as under:

"I, D.S. Kumar, Thirumala Distilleries, Siddartha Nagar, Tumkur, submit that during the last week of July, I had gone on a pilgrimage, along with my family and during that period, in our distillery, it was found that there is a deficit of 11,624.000 litres of liquefied spirit in our Books of accounts and accordingly the Excise Inspector, Thirumala Distilleries, Siddartha Nagar, Tumkur had filed Case No. 1 of 1994-95. This mistake has been committed by my Manager during the time I was out of station. Hence, I request you to pardon the said mistake and settle the case within the Department and I am ready to pay the compensation fee in respect of deficit rectified spirit vide Notification No. FD 11 PN 93, dated 30-3-1993".

19. From the above representations made by the Managing Partner of the respondent firm, it is quite clear that apart from admitting the deficit of 11,624 litres of rectified spirit, he also admitted that the said deficit is on account of a mistake committed by their Manager. He also made an offer to compound the offence and agreed to pay the composition fee in respect of deficit rectified spirit. Thereupon, in exercise of the power u/s 45 of the Karnataka Excise Act, 1965 the order dated 12-12-1994 vide Annexure-D was passed by the Deputy Commissioner of Excise, Tumkur District, Tumkur compounding the said Criminal Case No. 1 of 1994-95 registered against the distillery of the respondent firm by imposing Rs. 5,000 as composition fee and further directed the payment of Rs. 27,52,000/- on account of current duty, sales tax and surcharge. The respondent firm paid a sum of Rs. 5,000/- to the Excise Department on 6-6-1995, but failed to pay the further amount demanded under the compounding order at Annexure-D. The respondent further challenged the said order in appeal u/s 61 of the Karnataka Excise Act, 1965 before the 2nd respondent-Commissioner of Excise, Bangalore, who by his order dated 20-4-1995 vide Annexure-E set aside the order of the 3rd respondent at Annexure-E, dated 12-12-1994 and remitted the matter back to the 3rd respondent with a direction to decide the matter afresh

and to pass a speaking order. Thereafter the matter was considered afresh by the 3rd respondent and after hearing the parties, the 3rd respondent passed a speaking order as per Annexure-G, dated 3-6-1995, rejecting the contention of the respondent and imposing the excise duty of Rs. 11,50,875, Sales Tax of Rs. 8,41,838 and Surcharge of Rs. 1,26,989, totaling Rs. 21,18,989 against the respondent. Aggrieved, the respondent challenged the same by preferring a writ petition before this Court and in the writ petition it was ordered that the respondent should exhaust the alternate efficacious remedy of appeal provided under the statute. Accordingly, the respondent preferred an appeal before the 2nd respondent and the 2nd respondent by an order dated 19-8-1999 vide Annexure-J agreeing with the conclusion of the respondent 3, dismissed the appeal. Thus the 2nd respondent- appellate authority confirmed the order made by the 3rd respondent which clearly gives the basis for imposition of such amount. A reading of the order made by the 3rd respondent which has been confirmed by the 2nd respondent in appeal would make it clear that the basis of levy is not the rectified spirit, but the IML that was manufactured out of the deficit rectified spirit found at the distillery. According to the 3rd respondent 11,624 litres of rectified spirit would yield 25,573 litres of blended IML and it is on this quantity of the blended IML the excise duty was levied by the excise authorities and not on the rectified spirit as sought to be made out by the respondent. It is to be seen therefore that the excise duty was sought to be levied and demanded not on the deficit rectified spirit, but on the manufactured IML, that had resulted or yielded out of the utilisation of the deficit rectified spirit as a raw material for the manufacture of such IML by the respondent-distillery. Therefore, the subject-matter of levy of excise duty was the IML that would yield by utilising the rectified spirit that was found deficit and not satisfactorily accounted for by the respondent. Furthermore, the respondent herein having accepted the deficit stock of 11,624 bulk litres of rectified spirit and having compounded the offence u/s 45 of the Karnataka Excise Act, could not have challenged the compounding order made by the 3rd respondent u/s 45 of the Karnataka Excise Act, 1965 more so, when he had already paid the composition fee and did not dispute the offence being compounded with the department u/s 45 of the Karnataka Excise Act, 1965. The very fact that the respondent herein has admitted the shortage of the rectified spirit to the extent of 11,624 bulk litres and compounded the offence u/s 45 of the Karnataka Excise Act, 1965 would show that he has no reasonable explanation to offer with respect to the stock that was found deficit at the distillery. In the fact situation, what the authorities have done is that they have calculated as to what could be the yield of IML by utilizing the deficit rectified spirit and on the basis of that, they have demanded the excise duty from the respondent firm on the IML and not on rectified spirit. The respondent-distillery having a duty to account for the deficit stock of rectified spirit at the distillery which was specially meant for the manufacture of the IML, did not give satisfactory account for the said deficit rectified spirit found at the distillery to the competent authorities, and on the other hand, having compounded such offence departmentally, he accepted the

mistake on his part. In the fact situation, treating the deficit rectified spirit as being used in the manufacture of the IML by the respondent herein and imposing the excise duty on such manufacture of the IML by clandestinely using the deficit rectified spirit and not being satisfactorily accounted for by the respondent, does not amount to levy of excise duty on the rectified spirit and on the other hand, it amounts to levy of excise duty on the IML that was manufactured by. using the deficit rectified spirit. Thus it was an excise duty on the IML that was manufactured clandestinely by the respondent herein by utilising the deficit rectified spirit which was meant for the manufacture of the IML. Therefore, it was not beyond the competence of the State Government to impose such levy of excise duty.

20. In the instant case, it is not at all in dispute that the respondent herein is a holder of a distillery licence issued under the Karnataka Excise (D and WH) Rules, for manufacture of the India made liquor. The rectified spirit is an ingredient used in the manufacture of the IML. It is not in dispute that on 30-7-1994 when the physical stock of rectified spirit at the distillery of the respondent herein was inspected or checked by the Distillery Officer, it was found that there was a shortage or deficit stock of 11,624 bulk litres of rectified spirit. The respondent herein failed to give a satisfactory account of the said deficit to the excise authorities. That is to say, the deficit stock of 11,624 bulk litres of rectified spirit could not be accounted for by the respondent to the satisfaction of the authority concerned. The said deficit found at the distillery of the respondent was reported by the Superintendent of Excise-in-charge at the distillery of the respondent and on the basis of such report, the Deputy Commissioner of Excise, Tumkur, registered the Crime in Case No. 1 of 1994-95, on 30-7-1994. Thereupon, the respondent herein, who did not dispute the said deficit of rectified spirit at the distillery prayed the authorities to compound the offence and offered to pay the duty on all spirits, which was not accounted for by him. The respondent made two representations in this regard and they would clearly show that the respondent owing his mistake, offered to compound the offence. In both the representations, the respondent herein while admitting the mistake on their part, offered to pay the compensation in respect of the deficit quantity of 11,624 bulk litres of rectified spirit and agreed to compound the offence with the department to avoid prosecution and other penal consequences including the cancellation of licence. Thereupon, the excise authorities accepted the offer made by the respondent for compounding the offence and suggested to the respondent to pay a sum of Rs. 27,52,000/- by way of excise duty, sales tax and surcharge with respect, to the said deficit quantity of rectified spirit and a composition fee of Rs. 5,000/- by an order dated 12-12-1994. Such duty was obviously demanded because the respondent had utilised the said rectified spirit for the manufacture of the IML and sold the same clandestinely and retained its value. Pursuant to which, and in acceptance thereof, the respondent paid a sum of Rs. 5,000/-, but did not pay the other amounts suggested in the order of compounding made by the excise authorities and challenged the same by filing

an appeal and a writ petition. In this context, it is pertinent to note that the process of compounding being over, is not disputed by the respondent and on the other hand, the respondent admits the same. The very fact that the respondent was a willing party to the order of compounding and paid a part of the amount thereunder, it could not have challenged the order of compounding made by the competent authority. That is to say, the respondent, in respect of whom, an order of compounding was made is not entitled to challenge the order in any circumstances by invoking the appeal provisions of the Karnataka Excise Act. The respondent was estopped from challenging the order on the ground of acquiescence. The respondent having agreed to compound the offence with the department and having avoided prosecution and other penal consequences, could not have subsequently turned round to contend that the amount demanded under the order of compounding is not legally payable by him. Under the circumstances therefore, it is difficult to see how an appeal could have been filed by the respondent against an order of compounding. In this connection, a reference may be made to a decision of this Court in the case of S.V. Bagi. This is one aspect of the case. Coming to the other aspect of the case, the respondent, who specifically admitted the deficit stock of rectified spirit at the distillery could not give an account of such deficit of rectified spirit meant for manufacture of IML. It has remained unexplained by the respondent till this day. Further, it is highly inconceivable or difficult to believe that such a huge quantity of rectified spirit, which was stored in a storage tank at the distillery, could have evaporated into the thin air. Apart from this, the respondent did not report to the concerned authority as to how the said deficit has occurred. It is only when such deficit was detected by the authority and a case was registered against the respondent, the respondent while admitting his mistake, made a request to compound the offence and accordingly, the offence was compounded. Thus it stands unexplained even to this day by the respondent as to what happened to such a huge quantity of rectified spirit, which was stored in the storage tank at the distillery of the respondent. The respondent does not attribute anything to the distillery officer with regard to such deficit. On the other hand, they admit that such a default has occurred due to the mistake committed by their manager. Thus, the respondent owns his mistake for such deficit, but fails to explain as to what happened to such deficit stock of rectified spirit. It is not in dispute that the respondent is a licensee for manufacture of the IML and the said stock of rectified spirit was an ingredient meant for manufacture of IML. It was meant only for that purpose and not for any other purpose. It is to be seen therefore that the respondent herein is a manufacturer of the IML and the rectified spirit, which had disappeared from the storage tank of the distillery and not accounted for by the respondent, was an ingredient meant for the manufacture of the IML. In view of such established facts and in the absence of any reasonable explanation, on the part of the respondent herein, as to what happened to such stock and how the said stock could disappear from the storage tank of the distillery, the one and the only reasonable inference that can be drawn from the proved and admitted facts of this case is that the said deficit of rectified spirit

must have been utilised by the respondent for manufacture of the IML clandestinely. No other inference can be drawn other than the one mentioned above from the proved and admitted facts of this case. This is the only conclusion that could be drawn from the proved facts of this case. Such inference in our view can be drawn under law.. The said fact in our view stands proved from the circumstances appearing in the case. A fact is said to be proved when, after considering the matters before it, the Court or authority either believes it to exist, or consider its existence so probable that a prudent man ought, under the circumstances of the particular case, to act upon the supposition that it exists. What is required is production of such materials on which the Court or authority can reasonably act to reach the supposition that a fact exists. Proof of the fact depends upon the degree of probability of its having existed. The standard required for reaching the supposition is that of a prudent man acting in any important matter concerning him. Proof does not mean proof to rigid mathematical demonstration, because that is impossible; it must mean such evidence as would induce a reasonable man to come to a particular conclusion. In reaching the conclusion, the Court or authority can use the process of inferences to be drawn from facts produced or proved. Such inferences are akin to presumptions in law and law gives absolute discretion to the Court or to the authority to presume the existence of any fact which it thinks likely to have happened. In that process, the Court or authority may have regard to common course of natural events, human conduct, public or private business, vis-a-vis the facts of the particular case. The discretion is clearly envisaged in Section 114 of the Indian Evidence Act, 1872. Presumption is an inference of a certain fact drawn from other proved facts. While inferring the existence of a fact from another, the Court is only applying a process of intelligent reasoning which the mind of a prudent man would do under similar circumstances. Presumption is not the final conclusion to be drawn from other facts. But, it could as well be final if it remains undisturbed later. Presumption in law of evidence is a rule indicating the stage of shifting the burden of proof. From a certain fact or facts, the Court or authority can draw an inference and that would remain until such inference is either disproved or dispelled. For the purpose of reaching one conclusion, the Court or the authority can rely on a factual presumption. Unless the presumption is disproved or dispelled or rebutted, the Court or authority can treat the presumption as tantamounting to proof. A presumption can however be drawn only from facts and not from other presumptions by a process of probable and logical reasoning. In the instant case, such inference which is possible from the proved or admitted facts has not been dispelled or rebutted by the respondent herein and on the other hand, it stands confirmed from the conduct of the respondent in compounding the offence departmentally in respect of the shortage of rectified spirit found in the distillery which was under the exclusive control and possession of the respondent. The respondent herein clearly admits the shortage of rectified spirit in the distillery when checked by the authorities concerned and that further while accepting such mistake on the part of his employee, offered to compound the offence and did in fact compounded the

offence departmentally. There was a duty cast on the respondent to account for the rectified spirit which was not forthcoming at the distillery and failing which, he was obliged to pay such duty on all spirits which were not forthcoming in the distillery. The respondent does not attribute anything to the supervisory staff that was found at the distillery, and on the other hand, he clearly admitted their mistake with regard to the deficit that was found in the distillery. Therefore the one and the only conclusion that can be drawn from the proved and admitted facts is that the respondent herein had used the said deficit raw product viz., the rectified spirit clandestinely for the purpose of manufacturing of the India made liquor and sold the same clandestinely. If that is not so, Section 114 of the Indian Evidence Act would become otiose, which in its own would make the laws ineffective. In fact we must have regard to the common course of natural events, to human conduct. Under the circumstances, therefore it is quite reasonable to conclude that the respondent herein had utilised the said deficit quantity of rectified spirit found in the distillery clandestinely to manufacture IML and sold the same as seconds. No doubt a supervisory staff would be deployed at the distillery. But, as we have already indicated, the respondent did not attribute anything to the said supervisory staff with regard to the deficit rectified spirit found in the distillery. Likewise it is also not his case that the supervisory staff deployed at the distillery had connived with him in such clandestine act. Even otherwise assuming that the supervisory staff deployed at the distillery had conn; red with the respondent in such clandestine act, that by itself will not absolve the respondent of the consequences of such illegal or fraudulent act. An illegality would not become a legality on inaction or connivance of the staff of the Excise Department. There cannot be any doubt that the respondent herein could not have indulged in such illegal or fraudulent acts at such a large scale in the distillery, if the concerned authorities had performed their functions and obligations in accordance with the relevant rules. But, the respondent who had indulged in such fraudulent or illegal acts cannot be absolved of the same only on the ground of inaction by the authorities concerned. Be that as it may be. The fact remains on record is that the respondent herein did not give any reasonable explanation with regard to the shortage of rectified spirit in such huge quantity in the distillery. Under the circumstances, therefore, the one and the only reasonable inference that can be drawn from the proved and admitted facts is that the respondent herein had used or utilised the said rectified spirit as a raw product or as an ingredient in the manufacture of the IML in the distillery belonged to him and sold the same clandestinely. When once such a conclusion is reached, the excise duty can be levied or imposed on such manufacture of the IML by the respondent. That is exactly what has been done in this case by the excise authorities. This is very clear from a detailed order passed by the competent authority at Annexure-G. A careful perusal of the said order would clearly indicate that the excise duty has been levied not on rectified spirit but on the quantity of the IML that could be manufactured by utilising the deficit rectified spirit which has not been properly accounted for by the respondent in his distillery. The respondent herein obtained the rectified spirit for the purpose

of manufacture of the IML and did not properly account for the deficit rectified spirit and on the other hand, he accepted his mistake by compounding the offence, which will entitle the excise authority to conclude that the said deficit rectified spirit had been utilised by the respondent in the manufacture of the IML and hence imposed the excise duty on such manufacture of the IML. Therefore, in this case, the excise duty has not been levied or imposed on the quantity of deficit rectified spirit found in the distillery and on the other hand, the said excise duty has been levied on the quantity of the IML that was manufactured clandestinely and sold by the respondent herein by utilising the deficit rectified spirit found in the distillery. What the excise authorities have done in this case is that they have worked out the assessable value of the EVIL which was manufactured clandestinely by the respondent by utilising the deficit rectified spirit. It does not mean that the excise authorities had either levied the excise duty on the rectified spirit or on any notational basis. Thus in the instant case, the excise duty has been levied not on the rectified spirit but on the IML manufactured clandestinely and sold by the respondent herein by utilising the said quantity of rectified spirit which was found deficit and has not been properly accounted for by the respondent. Therefore, the subject of levy here is not rectified spirit but the IML that was manufactured clandestinely by utilising the deficit quantity of rectified spirit found in the distillery. Therefore in the fact situation, the authorities were legally entitled to arrive at such conclusion from the admitted facts of this case and accordingly, the said authorities were right in computing and levying the excise duty etc., on such clandestine manufacture of IML by the respondent in his distillery. Under the circumstances, therefore, we are of the clear view that the authorities were justified in demanding such excise duty on all the spirits which was not forthcoming and which has not been accounted for to the satisfaction of the competent authority and the said deficit, in all probability, had been utilised in the manufacture of the IML in the distillery owned by the respondent. It was not a notional levy and on the other hand it was a levy on the basis of the actual loss of rectified spirit and utilisation of the same in the manufacture of the IML clandestinely by the respondent herein. Therefore none of the decisions relied upon by the learned Counsel for the respondent herein have any application to the facts and peculiar circumstances of this case. The decisions relied upon by the learned Counsel for the respondent are clearly distinguishable on the facts of this case. The facts here would clearly indicate that the respondent herein did not explain as to what happened to the huge quantity of rectified spirit that was found deficit in the distillery. The rectified spirit that was found, deficit in the distillery was meant only for the purpose of manufacture of the IML by the respondent in his distillery. He clearly admits that the said deficit has been caused either on account of his own default or on account of the default committed by his own employees. In the fact situation, the one and the only inference that can be drawn from the proved and admitted facts is that the respondent had utilised the said quantity of rectified spirit which was found deficit, in the manufacture of the IML clandestinely and sold the same as seconds. Having regard to these facts of the case at hand, the

several decisions relied upon by the learned Counsel for the respondent are clearly distinguishable on facts and hence they have no application to the facts and circumstances of this case. That being so, no individual reference is needed to each of the decisions relied upon by the learned Counsel for the respondent. Suffice it to say that, they have no application to the facts and circumstances of the case at hand. As has been rightly contended by the learned Government Advocate, there was an ingenious attempt on the part of the respondent herein for avoidance of the excise duty on the IML manufactured in the distillery owned by the respondent. When the deficit was detected by the excise authorities, the respondent cleverly avoided his prosecution and other penal consequences by compounding the offence and when once the offence had been compounded departmentally and the authorities have demanded the excise duty on the basis of the IML manufactured by him by utilising the said deficit quantity of rectified spirit found in the distillery, he sought to challenge the same by saying that the STATE has no authority to levy excise duty on the deficit rectified spirit and has been successful to a certain extent in his attempt before the learned Single Judge. What has been lost of by the learned Single Judge in this case is that the authorities had demanded the excise duty on the basis of the IML that was manufactured by utilising the deficit quantity of rectified spirit found at the distillery, and not, on the basis of the deficit rectified spirit found in the distillery, which was only a raw material that was meant for being used in the manufacture of the IML in the distillery. That further, this is neither a case of notional levy nor a case of levy on the basis of any assumption and presumption. But, on the other hand this is a pure and simple case of levying excise duty on the IML that was manufactured by the respondent clandestinely by utilising the rectified spirit which was found to be deficit in the distillery and meant for the manufacture of the IML by the respondent in his distillery. The one and only way in which the said stock of rectified spirit could have disappeared from the distillery is that it has been utilised in the manufacture of the IML clandestinely and may be with the connivance of the excise staff that were deployed there. We say so because, the respondent herein, who in fact admits such shortage of rectified spirit, has not come out with any reasonable explanation as to what happened to such huge stock of rectified spirit which was meant for use in the manufacture of the IML. It is only in the writ petition the respondent sought to project a theory of evaporation, which besides being highly imaginary, was clearly an after thought. In the absence of any such reasonable explanation on the part of the respondent, the only way in which such a huge stock of rectified spirit could escape from the distillery is by way of its utilisation as a product in the manufacture of the IML by the respondent. Non-explanation of the admitted or proved disappearance of a huge stock of rectified spirit meant for manufacture of the IML from the distillery owned by the respondent, who has a duty to account for the same, the necessary inference is that the respondent, who is admittedly a manufacturer of the IML must have utilised the said stock of raw material for the purpose of manufacture of the IML, more so when the respondent does not attribute any mala fides to the excise officers, who were

deployed there. This is the only conclusion that can be drawn from the proved and admitted facts of this case. When this is the only conclusion possible from the facts proved and admitted, the levy of excise duty was on the IML that was manufactured clandestinely by the respondent by utilising the rectified spirit, which was found deficit at the time of inspection by the competent authorities in the distillery. In that view of the matter, the excise authorities were right in demanding and levying excise duty on the manufactured IML, may be clandestinely, by utilising the deficit rectified spirit found at the distillery. On the facts and in the circumstances of the case as aforesaid, we are of the clear view that there was nothing wrong in demanding and imposing such a levy, on the basis that the rectified spirit that was found deficit had been used in the manufacture of the IML clandestinely by the respondent, more so when the offence committed by the respondent had been compounded departmentally by him thereby admitting his guilt. It may be stated even at the cost of repetition that this is not a case where the excise duty had been levied and demanded on the rectified spirit that was found deficit at the distillery owned by the respondent, but it is a case where the excise duty had been levied and demanded on the IML that was manufactured clandestinely by the respondent by utilising the rectified spirit, which was found deficit at the time of inspection at the distillery. The respondent herein very ingeniously attempted to avoid the payment of excise duty by saying that it is a levy on deficit rectified spirit and has in fact been successful in his attempt before the learned Single Judge. The learned Single Judge failed to discover the invisible line, which distinguishes the case of the respondent herein. As we have already indicated, this is a case where the demand of excise duty has been made on the IML, which has been manufactured clandestinely by the respondent by utilising the rectified spirit, which was found deficit at the time of inspection in the distillery and hence, the excise authorities were right in demanding such levy. The learned Single Judge while passing the impugned order did not consider all these aspects of the case and proceeded tangential to the real question in controversy and thus committed a serious error in quashing the orders of the authorities concerned. At this stage, it would be useful to refer to the observations made by the Hon'ble Supreme Court in the above case of *Mis. McDowell and Company Limited*, in paragraphs 3 to 18 which reads thus:

"3. Though initially the law was, and I suppose the law still is, "there is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied", During the period between the two World Wars, the theory came to be propounded and developed that it was perfectly open for persons to evade (avoid) Income Tax if they could do so legally. For some time it looked as if tax avoidance was even viewed with affection. Lord Sumner in *Inland Revenue Commissioners v. Fishers Executors*, 1926 AC 395 : 95 LJKB 478 : 10 Tax Cas 302, said:

"My Lords the highest authorities have always recognised that the subject is entitled so to arrange his affairs as not to attract taxes imposed by the crown so

far as he can do so within the law, and that he may legitimately claim the advantage of any expressed term or of any emotions that he can find in his favour in taxing Acts. In so doing he neither comes under liability nor incurs blame".

4. Lord Tomlin echoing what Lord Sumner had said observed in *Inland Revenue Commissioner v. Duke of Westminster*, 1936 AC 1 : (1935) All ERS (Rep.) 259 : 104 LJBK 383, as follows, typifying the prevalent attitude towards tax avoidance at that time:

"Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however, unappreciative the Commissioners of Inland Revenue or his fellow tax payers may be of his ingenuity, he cannot be compelled to pay an increased tax".

5. Then came World War II and in its wake huge profiteering and racketeering, something which persists till today, but on a much larger scale. The attitude of the Courts towards avoidance of tax perceptibly changed and hardened and in *Lord Howard De Walden v. Inland Revenue Commissioners*, (1942)1 KB 389 : (1942)1 All ER 287; in LJBK 273, Greene M.R. dealing with the construction of an anti-avoidance section said:

"For years a battle of manoeuvre has been waged between the legislature and those who. are minded to throw the burden of taxation off their own shoulders on to those of their fellow subjects. In that battle the legislature has been worsted by the skill, determination and resourcefulness of its opponents of whom the present appellant has not been the least successful. It would not shock us in the least to find that the Legislature has determined to put an end to the struggle by imposing the severest penalties. It scarcely lies in the mouth of the tax payer who plays with fire to complain of burnt fingers".

6. Expressing the same sentiment and dissertating on the moral aspects of tax avoidance, Lord Simon in *Latilla v. Inland Revenue Commissioners*, 1943 AC 377 : (1943)1 All ER 265 : 25 Tax Cas 107 (HL), said:

"My Lords, of recent years much ingenuity has been expended in certain quarters in attempting to devise methods of disposition of income by which those who were prepared to adopt them might enjoy the benefits of residents in this country while receiving the equivalent of such income without sharing in the appropriate burden of British taxation. Judicial dicta may be cited which point out that, however, elaborate and artificial such methods may be, those who adopt them are "entitled" to do so. There is, of course, no doubt that they are within their legal rights but that is no reason why their efforts, or those of the professional gentlemen who assist them in the matter, should be regarded as a commendable exercise of ingenuity or as a discharge of the duties of good citizenship. On the contrary, one result of such methods, if they succeed, is of course to increase pro tanto the load of tax on the shoulders of the great body of

good citizens who do not desire or do not know how, to adopt these manoeuvres".

7. In several cases, *Griffiths v J.P. Harrison Limited* 1963 AC 1, *Morgan v. Inland Revenue Commissioners*, 1963 Ch. 438 : (1963)1 All ER 481 : (1963)2 WLR 416, *Public Trustee v. Inland Revenue Commissioners*, 1965 Ch 286 : (1964)3 All ER 780 : (1964)3 WLR 1240, Lord Denning repeatedly referred to tax avoidance schemes and described them as magic performance by lawyer-tuned-magicians. Lord Harman, almost in the same words as Lord Denning described a tax avoidance scheme as one "which smells a little of the lamp" and said "it is a splendid scheme.....It is almost too good to be true. In law quite too good to be true. It won't do". (*Campbell v. Inland Revenue Commissioners* 1967 Ch. 651 : (1967)2 All ER 625 : (1967)2 WLR 1445, Stamp, J., *In re Wester's Settlements* observed:

".....There must be some limit to the devices which this Court ought? to countenance in order to defeat the fiscal intentions of the legislature. In my judgment these proposals overstep that limit. . . . I am not persuaded with this application represents more than a cheap exercise in tax avoidance which I ought not to sanction, as distinct from a legitimate avoidance of liability to taxation".

8. In *Greenberg v. Inland Revenue Commissioners*, (1971)3 All ER 136 : (1971)3 WLR 386 : 1972 AC 109 (HL), Lord Reid dealing with a scheme for tax avoidance by forward dividend stripping observed:

".....We seem to have travelled a long way from the general and salutary rule that the subject is not to be taxed except by plain words. But, I must recognise that plain words are seldom adequate to anticipate and forestall the multiplicity of ingenious schemes which are constantly being devised to evade taxation. Parliament is very properly determined to prevent this kind of tax evasion and, if the Courts find it impossible to give very wide meanings to general phrases, the only alternative may be for Parliament to do as some other countries have done, and introduced legislation of a more sweeping character which will put the ordinary well-intentioned person at much greater risk than is created by a wide interpretation of such provisions as those which we are now considering".

"I am inclined to think that the real explanation of these verbal difficulties may be that, in legislation of such extreme complexity as we have here, it is not humanly possible for a draftsman to preserve that consistency in the use of language which we generally look for. Indeed, I sometimes suspect that our normal meticulous methods of statutory construction tend to lead us astray by concentrating too much on verbal niceties and paying too little attention to the provisions read as a whole".

9. The march of the law against tax avoidance schemes continued and came a significant departure from the *Westminster* and the *Fisher Executors* principle. In *W.T. Ramsay v. Inland Revenue Commissioners*, 1982 AC 300 : (1981)1 All ER

865 : (1981)2 WLR 449, the House of Lords had to consider a scheme of tax avoidance which consisted of a series or a combination of transactions each of which was individually genuine but the result of all of which was an avoidance of tax. Lord Wilberforce, with great force, observed:

"Given that a document or transaction is genuine, the Court cannot go behind it to some supposed underlying substance. This is the well-known principle of *Duke of Westminster*'s case. This is a cardinal principle but it must not be overstated or overextended. While obliging the Court to accept documents or transactions, found to be genuine, as such, it does not compel the Court to look at a document or a transaction in blinkers, isolated from any context to which it properly belongs. If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine to prevent it being so regarded: to do so is not to prefer form to substance, or substance to form. It is the task of the Court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded. For this there is authority in the law relating to Income Tax and capital gains tax : see *Chinn v. Hochstrasser*, 1981 AC 533 : (1981)2 WLR 14 : (1981)1 All ER 189 (HC) and *Inland Revenue Commissioners v. Plummer*, 1980 AC 896 : (1979)3 WLR 689 : (1979)3 All ER 775 (HL)".

"For the Commissioners considering a particular case it is wrong and an unnecessary self-limitation, to regard themselves as precluded by their own finding that documents or transactions are not "shams", from considering what, as evidenced by the documents themselves or by the manifested intentions of the parties, the relevant transaction is. They are not, under the *Westminster* doctrine or any other authority, bound to consider individually each separate step in a composite transaction intended to be carried through as a whole".

Later again he observed:

". . . . For the tax payers it was said that to accept the revenue's wide contentions involved a rejection of accepted and established canons and that, if so general an attack upon schemes for tax avoidance as the revenue suggests is to be validated, that is a matter for Parliament. The function of the Courts is to apply strictly and correctly the legislation which Parliament has enacted : if the tax payer escapes the charge, it is for Parliament, if it disapproves of the result, to close the gap. General principles against tax avoidance are, it was claimed, for parliament to lay down. We were referred, at our request, in this connection to the various enactments by which Parliament has from time to time tried to counter-tax avoidance by some general prescription. The most extensive of these is, *Income and Corporation Taxes Act, 1970, Sections 460 et seq.* We were referred also to well-known sections in Australia and New Zealand (*Australia, Income Tax Assessment Act, 1936-51, Section 260, New Zealand, Income Tax*

Act, 1976, Section 99, replacing earlier legislation). Further it was pointed out that the capital gains tax legislation (starting with the Finance Act, 1965) does not contain any provision corresponding to Section 460. The intention should be deduced, therefore, it was said, to leave capital gains tax to be dealt with by "hole and plug" methods : that such schemes as the present could be so dealt with has been confirmed by later legislation as to "value shifting" : Capital Gains Tax Act, 1979, Section 25 et seq. These arguments merit serious consideration. In substance they appealed to Barwick, C.J. in *Feder Commissioner of Taxation v. Westraders Pty. Limited*, (1980)30 ALR 353".

"I have a full respect for the principles which have been stated but I do not consider that they should exclude the approach for which the crown contends. That does not introduce a new principle : it would be to apply to new and sophisticated legal devices the undoubted power and duty of the Courts to determine their nature in law and to relate them to existing legislation. While the techniques of tax avoidance progress and are technically improved the Courts are not obliged to stand still. Such immobility must result either in loss of tax, to the prejudice of other taxpayers, or to Parliamentary congestion or (most likely) to both. To force the Courts to adopt, in relation to closely integrated situations, a step by step, dissecting approach which the parties themselves may have negated, would be a denial rather than an affirmation of the true judicial process. In each case the facts must be established, and a legal analysis made : legislation cannot be required or even be desirable to enable the Courts to arrive at a conclusion which corresponds with the parties' own intentions".

"The capital gains tax was created to operate in the real world, not that of make belief.

10. The significance of *Ramsay* as a turning point in the interpretation of tax laws in England and the departure from the strings of *Westminster* were explained in *Inland Revenue Commissioners v. Burmah Oil Company Limited*, (1982)STC 30, where Lord Diplock said:

"It would be disingenuous to suggest, and dangerous on the part of those who advise on elaborate tax avoidance schemes to assume, that *Ramsay*'s case did not mark a significant change in the approach adopted by this House in its judicial role to a pre-ordained series of transactions (whether or not they include the achievement of a legitimate commercial end) into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax which in the absence of those particular steps would have been payable. The difference is in approach. It does not necessitate the overruling of any earlier decisions of this House; but it does involve recognising that Lord Tomlin's oft-quoted dictum in *Duke of Westminster*'s: "Every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Acts is less than it otherwise would be", tells us little or nothing as to what methods of ordering one's affairs will be recognised by the Courts as effective to lessen the tax what would attach to them if business transactions were conducted in a

straightforward way".

Lord Scarman said:

"First, it is of the utmost importance that the business community (and Ors., including their advisers) should appreciate, as my noble and learned friend Lord Diplock has emphasised, that Ramsay's case, marks "a significant change in the approach adopted by this House in its judicial role" towards tax avoidance schemes. Secondly, it is now crucial when considering any such scheme to take the analysis far enough to determine where the profit, gain or loss is really to be found".

11. The winds of change continued to blow and in *Furniss v. Dawson*, (1984)¹ All ER 530, Ramsay was reiterated. Lord Brightman observed:

"The fact that the Court accepted that each step in a transaction was a genuine step producing its intended legal results did not confine the Court to considering each step in isolation for the purpose of assessing the fiscal results". He further said:

"My Lords, in my opinion the rationale of the new approach is this. In a pre-planned tax saving scheme, no distinction is to be drawn for fiscal purposes, because none exists in reality, between (i) a series of steps which are followed through by virtue of an arrangement which falls short of a binding contract, and (ii) a like series of steps which are followed through because the participants are contractually bound to take each step seriatim. In a contractual case the fiscal consequences will naturally fall to be assessed in the light of the contractually agreed results".

12. In the same case Lord Fraser explained the principle of Ramsay's as follows.-

".....The true principle of the decision in Ramsay's case was that the fiscal consequences of a pre-ordained series of transactions, intended to operate as such, are generally to be ascertained, by considering the result of the series as a whole, and not by dissecting the scheme and considering each individual transaction separately". Lord Scarman in his characteristic style observed:

"The law will develop from case to case. Lord Wilberforce in *W.T. Ramsay's*, referred to "the emerging principle" of the law. What has been established with certainty by the House in Ramsay's case, is that the determination of what does, and what does not, constitute unacceptable tax evasion is a subject suited to development by judicial process. The best chart that we have for the way forward appears to me, with great respect to all engaged on the map-making process, to be the words of Lord Diplock in *Burmah Oil Company Limited's* case, which my noble and learned friend Lord Brightman quotes in his speech. These words have space in the law for the principle enunciated by Lord Tomlin in *Duke of Westminster's* case, that every man is entitled if he can to order his affairs so as to diminish the burden of tax. The limits within which this principle is to operate remain to be probed and determined judicially. Difficult though the task

may be for Judges, it is one which is beyond the power of the blunt instrument of legislation. Whatever a statute may provide, it has to be interpreted and applied by the Courts; and ultimately it will prove to be in this area of judge-made law that our elusive journey's end will be found".

Lord Roskill put it even more forcefully:

"The error, if I may venture to use that word, into which the Courts below have fallen is that they have looked back to 1936 and not forward from 1982. They do not appear to have appreciated the true significance of the passages in the speeches in Ramsay's case of Lord Wilberforce and Lord Fraser, and even more important, of the warnings in the *Burmah Oil*'s case, given by Lord Diplock and Lord Scarman in the passages to which my noble and learned friend Lord Brightman refers and which I will not repeat. It is perhaps worth recalling the warning given, albeit in another context by Lord Alkin, who himself dissented in the *Duke of Westminster*'s case, in *United Australia Limited v. Barclays Bank Limited*, (1940) 4 All ER 20 : (1941) AC 1: 164 LT 139: "When these ghosts of the past stand in the path of justice, clanking their mediaeval chains, the proper course for the judge is to pass through them undeterred" 1936, a bare half century ago, cannot be described as part of the Middle Ages but the ghost of the *Duke of Westminster* and of his transaction, be it noted a single and not a composite transaction, with his gardener and with other members of his staff has haunted the administration of this branch of the law for too long. I confess that I had hoped that ghost might have found quietude with the decisions in Ramsay's and in *Burmah*'s. Unhappily it has not. Perhaps the decision of this House in these appeals will now suffice as exorcism".

13. Thus the ghost of Westminster (in the words of Lord Roskill) has been exorcised in England. Should it be allowed to rear its head in India?

14. I have referred to the English cases at some length, only to show that in the very country of its birth, the principle of Westminster has been given a decent burial and in that very country where the phrase "tax avoidance" originated the judicial attitude towards tax avoidance has changed and the smile, cynical or even affectionate though it might have been at one time, has now frozen into a deep frown. The Courts are now concerning themselves not merely with the genuineness of a transaction, but with the intended effect of it for fiscal purposes. No one can now get away with a tax avoidance project with the mere statement that there is nothing illegal about it.

15. Some years ago, a diverting attempt was made by a Correspondent to the London "Times" to defend tax avoidance. He said:

"The tax payer is merely bound to obey the law, but is not bound beyond the law, for apart from the law taxation would be blackmail or racketeering. There is not behind taxing laws, as there is behind laws against crime, an independent moral obligation. When, therefore, the tax payer has obeyed the law, he had done all that morality requires".

He had further said:

"It is said that by avoiding a tax he throws a load on to some other tax payer. But, this is not quite accurate, for the deficiency might be met by reducing expenditure.....is it not a good thing that there should be this last lawful remedy against oppressive taxation by a majority, that human ingenuity can always find a way by which the minority can escape from tyrannical imposts".

The correspondent was answered by another correspondent who described the former's defence of tax avoidance as "an amusing attempt to raise the art of tax avoidance to the moral level of political martyrdom and to make Hamden's of our modern tax dodgers". Nor, may we say, are our tax dodgers Gandhi is on the Dandi March to protest against the Salt Tax.

16. In Commissioner of Income Tax, Gujarat Vs. A. Raman and Company, , J.C. Shah, J., speaking for himself and Sikri and Ramaswami, JJ. repeating almost verbatim the observations in Westminster's case and Fishers Executors, 1926 AC 395 observed:

"Avoidance of tax liability by so arranging commercial affairs that charge of tax is distributed is not prohibited. A tax payer may resort to a device to divert the income before it accrues to arise to him. effectiveness of the device depends not upon considerations of morality, but on the operation of the Income Tax Act. Legislative injunction in taxing statutes may not, except on period (Pain?) of penalty, be violated, but it may lawfully be circumvented".

The same Judge, speaking for himself, Ramaswami and Grover, JJ., in Commissioner of Income Tax, Gujarat Vs. B.M. Kharwar, , expressly followed Westminster and observed:

"The taxing authority is entitled and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of relationship. But, the legal effect of a transaction cannot be displayed by probing into the "substance of the transaction".

17. We think that time has come for us to depart from the Westminster principle as emphatically as the British Courts have done and to dissociate ourselves from the observations of Shah, J., and similar observations made elsewhere. The evil consequences of tax avoidance are manifold. First there is substantial loss of much needed public revenue, particularly in a welfare State like ours. Next there is the serious disturbance caused to the economy of the country by the piling up of mountains of black money, directly causing inflation. Then there is "the large hidden loss" to the community (as pointed out by Master Sheatcroft in 18 Modern Law Review 209) by some of the best brains in the country being involved in the perpetual war waged between the tax-avoider and his expert team of advisers, lawyers and accountants on one side and the tax-gatherer and his perhaps not

so skillful advisers on the other side. Then again there is the "sense of injustice and inequality which tax avoidance arouses in the breasts of those who are unwilling or unable to profit by it. Last but not the least is the ethics (to be precise, the lack of it) of transferring the burden of tax liability to the shoulders of the guileless good citizens from those of the "artful dodgers". It may, indeed, be difficult for lesser mortals to attain the state of mind of Mr. Justice Holmes, who said, "Taxes are what we pay for civilized society. I like to pay taxes. With them I buy civilisation". But, surely it is high time for the judiciary in India too to part its ways from the principle of Westminster and the alluring logic of tax avoidance, we now live in a welfare State whose financial needs, if backed by the law, have to be respected and met. We must recognise that there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is a pretence to say that avoidance of taxation is not unethical and that it stands on no less moral plane than honest payment of taxation. In our view, the proper way to construe a taxing statute, while considering a device to avoid tax, is not to ask whether the provisions should be construed literally or liberally, nor whether the transaction is not unreal and not prohibited by the statute, but whether the transaction is a device to avoid tax, and whether the transaction is such that the judicial process may accord its approval to it. A hint of this approach is to be found in the judgment of Desai, J. in *In Re: Wood Polymer Limited*; *In Re: Bengal Hotels Pvt. Ltd.*, where the learned Judge refused to accord sanction to the amalgamation of companies as it would lead to avoidance of tax.

18. It is neither fair nor desirable to expect the legislature to intervene and take care of every device and scheme to avoid taxation. It is up to the Court to take stock to determine the nature of the new and sophisticated legal devices to avoid tax and consider whether the situation created by the devices could be related to the existing legislation with the aid of "emerging techniques of interpretation was done in the cases of *Ramsay*, *Burma Oil* and *Dawson*, to expose the devices for what they really are and to refuse to give judicial benediction".

21. In the light of the above observations made by the Hon^{ble} Supreme Court and having regard to the ingenious method adopted by the respondent herein to escape the levy of excise duty, and on the facts and in the circumstances of the case at hand, we find that the excise authorities were right in unraveling device and determining the true character of the levy and accordingly, demanding the excise duty which has escaped the levy. But unfortunately, the learned Single Judge has not been able to discover the device adopted by the respondent herein to avoid payment of the excise duty. We therefore, find that the learned Single Judge was not at all justified in interfering with the orders made by the excise authorities under the premise that it is a levy on rectified spirit, but in fact, it is not so and on the other hand, it was a levy on the IML manufactured clandestinely by the respondent by utilising the rectified spirit, which was found deficient at the time of inspection in the distillery owned by the respondent. That apart, the learned Single Judge could not have entertained the writ petition filed

by the respondent, in view of the fact that what was challenged in the writ petition was the order of compounding the offence by the respondent herein. When the respondent herein does not dispute the compounding of the offence, with the department, as per the impugned order at Annexure-D and G, then he cannot challenge the order of compounding the offence passed by the Competent Authority. Therefore, looking from any angle, the order of the learned Single Judge impugned in this appeal cannot be sustained in law. To confirm the order of the learned Single Judge is to encourage the distilleries, who are indulging in such nefarious activities of evasion of excise duty by resorting to such ingenious method. We are therefore of the clear view that the impugned order made by the learned Single Judge needs to be set aside on "the facts and in the circumstances of the case at hand.

22. In the result, therefore, this writ appeal filed by the appellant- State and its authorities is allowed. The impugned order made by the learned Single Judge dated 15-3-2002 in Writ Petition No. 40828 of 1999 is hereby set aside and that of the 3rd respondent dated 3-6-1995 at Annexure-G and confirmed by the 2nd respondent dated 19-8-2000 at Annexure-J are hereby restored. But in the circumstances of the case, there is no order as to costs.

B. Padrnaraj and H. Billappa, JJ. Dated 23-9-2004

ORDER

After the judgment was pronounced, the learned Counsel for the respondent made an oral application to grant a certificate of the nature referred to in clause 1) of Article 132 of the Constitution of India. It has to be pointed out that under clause (1) of Article 132 of the Constitution, there is no scope for granting a certificate unless the two conditions are satisfied namely, the case should involve a question as to the interpretation of the Constitution and the said question should be a substantial question of law. In the instant case, we find that no substantial question of law as to the interpretation of the Constitution is involved in the case and hence the oral application made by the learned Counsel for the respondent stands rejected.