COMMISSIONER OF CENTRAL EXCISE, NEW DELHI

v.

M/S. MODI ALKALIES AND CHEMICALS LTD.

AUGUST 18, 2004

[S.N. VARIAVA AND ARIJIT PASAYAT, JJ.]

Central Excise Rules, 1994:

Rules 9(2), 52-A, 173-Q and 209-A—Excise duty—Clubbing of units—Interdependence of units—Determination of—Assessee manufactured caustic soda—Hydrogen gas obtained as a byproduct—Assessee floated three companies with a share capital of only Rs. 200 each—Subsequently, heavy amounts advanced as loans to these companies by assessee—Assessee also rendered financial assistance to these companies through a finance company—Cylinders were subleased to the said companies by assessee—Assessee piped Hydrogen gas to the said companies at a certain rate—The said companies compressed and bottled the same at a much higher rate—The profit earned was paid to assessee as lease rent for cylinders—There was common staff for maintaining records and operation of the units—Directors of the three companies were employees of the assessee—CCE (Adjudication) held the said companies as dummies of the assessee and that the assessee evaded duty by resorting to undervaluation—CCE (Adjudication), therefore, imposed duty and penalty on the assessee by clubbing with the three companies, confiscated the assets, and imposed penalty on the Directors, of the three companies—Correctness of—Held: Whether there was interdependence of units and whether another unit is a dummy has to be adjudicated on the facts of each case—There cannot be any generalization or rule of universal application—Two basic features which prima facie showed interdependence were pervasive financial control and management control—Although the three companies were registered under the sales tax and income tax authorities but when the corporate veil is lifted then these companies had no independent existence—The three companies are dummies of the assessee and there is clear suppression of facts—Therefore, extended period of limitation for recovery of duty clearly applicable—Hence, CCE (Adjudication) justified in imposing duty and penalty on the assessee and penalty on the Directors of the said

three companies—Central Excise Act, 1944, Ss. 11A and 11—Central Excise Tariff Act, 1985, Sub-Heading 2804.90.

New plea—Assessee did not raise any plea regarding manufacturing before CCE (Adjudication)—But Appellate Tribunal held that there was no manufacturing—But assessee claimed exemption as manufacturer—Effect of—Held: Under these circumstances, the said plea rejected.

The assessee-respondent No. 1 was engaged in the manufacture of caustic soda of which Hydrogen gas was a byproduct. The assessee floated three companies with a share capital of only Rs. 200 and advanced substantially heavy amounts as loans to the said companies. The assessee also arranged loan to these companies through finance companies. The assessee obtained cylinders on lease and subleased the same to these companies and through pipelines sent Hydrogen gas at a certain rate to these companies for compressing and bottling the same. These companies, in turn, sold the bottled gas at a much higher rate. The said companies paid the entire profit to the assessee as lease rent of the cylinders. The assessee and the three companies had common staff for maintaining of records and operation of the units. The Directors of the three companies were the employees of the assessee.

The Commissioner of Central Excise (Adjudication) held the said companies as dummies of the assessee and that the assessee had evaded duty by resorting to under valuation. Accordingly, the CCE (Adjudication) imposed duty and penalty on the assessee by clubbing with the three companies, ordered confiscation of the assets of the companies and imposed penalty on their Directors.

In appeal, the Central Excise and Gold (Control) Appellate Tribunal (CEGAT) held that there was no manufacture involved in the process and, therefore, question of evasion of duty did not arise. The CEGAT further held that there was no interdependence as alleged by the Central Excise Authorities and set aside the order of CCE (Adjudication). Hence the appeals.

On behalf of the revenue, it was contended that though the issue whether there was manufacture was never agitated before the CCE

(Adjudication), the CEGAT on its own came to hold that there was no manufacturing which was not supported on facts and law.

On behalf of the assessee, it was contended that the three companies had separate corporate existence, were assessed separately to sales tax and income tax and had central excise registration and, therefore, these companies were not front or dummy companies of the assessee; that the question of clubbing was not permissible in view of Circular No. 6/92 dated 29-5-1992; and that the extended period of limitation was not applicable.

Allowing the appeals, the Court

HELD: 1. Whether there is interdependence and whether another unit is, in fact, a dummy has to be adjudicated on the facts of each case. There cannot be any generalization or rule of universal application. Two basic features which *prima facie* show interdependence are pervasive financial control and management control. In the present case facts clearly show financial control. [625-G-H; 626-A]

2. The whole show was controlled, both on financial and management aspects by the assessee. If these were not sufficient to show interdependence probably nothing better would show the same. The factors, which have weighed with the Central Excise and Gold (Control) Appellate Tribunal like registration of the three companies under the sales tax and income tax authorities, have to be considered in the background of the facts of the case. When the corporate veil is lifted what comes into focus is only the shadow and not any substance about the existence of the three companies independently. [626-F-G]

3. The Circular No. 6/92 dated 29-5-1992 has no relevance because it related to notification No. 175/86-CE dated 1-3-1986 and did not relate to notification No. 1/93. The extended period of limitation was clearly applicable on the facts of the case, as suppression of material features and factors has been clearly established. [626-G-H; 627-A]

4. The question whether there was manufacture or not was not in issue before the Central Excise Commissioner (Adjudication). The

plea that there was no manufacture has also to be rejected in view of the fact that exemption was claimed by the three companies as manufacturers to avail the benefit of Central Excise Notification No. 1/93. [627-A-B]

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos. 7827-7834 of 2002.

From the Judgment and Order dated 22.4.2002 of the Central Excise and Gold (Control) Appellate Tribunal, New Delhi in A. No. E/237-244/99-D in F.O. No. 134-141 of 2002-D.

Anoop G. Chaudhary, Sanjay Grover, Mrs. June Chaudhary, P. Parmeswaran, Rohit Singh and B. Krishna Prasad for the Appellant.

A.K. Jain, Rajesh Kumar and Rajesh Jain for the Respondents.

The Judgment of the Court was delivered by

ARIJIT PASAYAT, J. : The Custom, Excise and Gold (Control) Appellate Tribunal, New Delhi (for short 'CEGAT') by the common impugned judgment held that there was no inter-dependence so far as the respondent no.1-company and respondent nos. 2-4 companies are concerned.

Background facts in a nutshell are as follows:

Respondent no. 1 M/s Modi Alkalies & Chemicals Ltd. (in short 'MACL') is engaged in the manufacture of caustic soda of which Hydrogen gas is a by-product. The Central Excise Authorities noticed that in reality MACL was engaged in the manufacture of Hydrogen gas falling under sub-heading 2804.90 of the schedule of the Central Excise Tariff Act, 1988 (in short 'Tariff Act'). But with a view to evade payment of excise duty it floated three front companies, namely, respondent nos. 2 to 4 i.e. M/s Mahabaleshwar Gas & Chemicals Pvt. Ltd. (for short 'MGCPL'), Shri Chamundi Gas and Chemicals Pvt. Ltd. (for short 'SCGCPL') and M/s. Nippon Gas and Chemicals Pvt. Ltd. (for short 'NGCPL'). All the three front companies were in vicinity of the factory of MACL. What in reality happened was that through pipelines Hydrogen gas was sent to the three

front companies for compressing and bottling the gas. The sole object was to avail benefit of exemption given to small scale industries under the Central Excise Notification No.1/93 dated 28.2.1993 and thereby evade payment of central excise duty. With a view to unravel the truth, Director General of Anti-Evasion (for short 'DGAE') searched the factory and office premises of MACL and the three front companies on 27.9.1996. It was found that all the three bottling units were located in one single shed and were separated from each other by small brick walls of about 4 ft. height. The Directors of the three front companies were employees of either MACL or other Modi Group of companies and they were frequently changed. They had common staff for maintenance of records and operation of the units. The main plant and machinery i.e. cylinders had been supplied only by MACL and the total finance was provided by MACL as unsecured loans or had been arranged by finance companies whose whereabouts were not even known to the Directors of the three front companies. Marketing of the products was done by one Ritesh Beotra, a so-called Director of SCGCPL who was working as Deputy Manager (Marketing) in M/s Modi Gas & Chemicals Sales Depot at Delhi. He was marketing various gases manufactured by a Modi group concern and was answerable as an employee of MACL. It was, therefore, concluded that MACL had control over Hydrogen gas even after the stage of bottling till it was sold to the customers. The Balance-Sheets and other financial statements of the three units revealed that whatever income they earned had gone to MACL in the form of lease rent of cylinders. One Mr. Sita Ram Goswami, Accountant of MACL and Mr. Ashok Kumar, Chief Operating Officer of MACL admitted that some amount of cash was also collected by MACL over and above the invoice prices of Hydrogen gas supplied by three companies. It was noted that while front companies were being supplied gas by MACL @ 0.50 per unit, till August 1996, the same gas was sold by the three companies @ Rs. 5 per unit. Keeping in view all these factors the authorities were of the view that MACL had created the three companies with the fraudulent intention to avail benefit of exemption granted under Central Excise Notification No.1/93 dated 28.2.1993 and has mis-declared the assessable value in the invoices with the intention to evade central excise duty.

Show-cause notice was issued requiring MACL to show-cause as to why the central excise duty of Rs. 20,58,732.65 for the concerned period

A i.e. 9.5.1995 to 27.9.1996 should not be recovered from it under the provisions of Rule 9(2) of the Central Excise Rules, 1945 (in short the 'Rules') read with Section 11 of the Central Excise Act, 1944 (in short the 'Act') by invoking the extended period of limitation. Further, penalty in terms of Rule 52A and 173Q of the Rules and Section 11 of the Act along B with interest to be determined under Section 11 A(2) was to be levied. It was also required to show cause as to why the land, building, plant and machinery installed in the three front units were not to be confiscated in terms of Rule 173Q of the Rules. Three officials were asked to show cause as to why penalty should not be imposed under Rule 209A of the Rules on each of them. On receipt of the show-cause, MACL replied that the C three companies were independent entities with corporate existence and were using their own machinery. The loans have been returned and on the cylinders lease rent had also been paid. Merely because MACL had taken the cylinders on lease and had supplied to the three companies, no adverse inference was to be drawn. Even if common staff maintained the records D and operated units that would not prove that the companies did not exist or that MACL was the company having manufacturing activities in their premises. Similar replies were filed by the three companies who denied that they were fake units or front companies. It was pointed out that all requisites of central excise laws were followed. There was nothing E suspicious in the transactions entered into by them with MACL.

After consideration the show-cause reply, the Commissioner of Central Excise (Adjudication), Delhi (for short the 'Commissioner') analysed the factual position and found that this is a clear case where the F three companies were dummies of MACL. Documents have been created to show existence of the bottling companies, whereas in reality MACL was in full control over the units and, therefore, MACL was treated to have evaded duty by resorting to under valuation. Duty and penalty as proposed were imposed. Confiscation was directed of land, building, plant & machinery of the three companies with option for redemption on payments G of fine of Rs. 20 lakhs, Rs.7 lakhs and Rs. 50,000 respectively. Penalty of Rs.1 lakh was imposed on each of the three companies and Rs. 50,000 on each of the three employees and the Director of the Company.

Eight appeals were filed before the CEGAT, which by the common H judgment set aside the order of the Commissioner. It came to hold, *inter*

alia, that (1) there was no manufacture involved in the process and, A
therefore, question of evasion of duty did not arise; (2) there was no inter-dependence as alleged by the Central Excise Authorities. Three companies had independent existence and the factual position did not indicate that they were front companies as alleged by the authorities.

B

In support of the appeals, learned counsel for the appellant submitted that the CEGAT has fallen into grave error both while analyzing factual position and the applicable principles of law. Telltale features which clearly prove that the three companies were front companies have been lightly brushed aside by the CEGAT. It even failed to notice that transactions were done by companies with share capital of Rs. 200 each. The CEGAT has C
also recorded wrong findings as regards the management and marketing. Though the issue as to whether there was manufacture was never agitated before the Commissioner, the CEGAT on its own came to hold that there was no manufacturing. The conclusion is not supportable on facts and in law. D

In response, learned counsel for the respondents submitted that the CEGAT has rightly analysed the factual background and came to the right conclusions. It was submitted that the three companies have separate corporate existence, are assessed separately to sales tax and income tax and E
have central excise registration. They submitted records to the Central Excise Authorities which were being verified by them. In any event, the question of any clubbing was not permissible in view of circular no.6/92 dated 25.5.1992 issued by the Government of India, Ministry of Finance, Department of Revenue, Central Board of Excise and Customs, New Delhi. F
The same was, in fact, continuation of the notification No. CER 8(5) Central Excise dated 1.3.1956. It was pointed out that there was no suppression or evasion for applying extended period of limitation. The show-cause notice was issued on 26.6.1997 and the order was passed on 23.10.1998 relating to the period from 9.5.1992 to 27.9.1996. The whole proceedings were, therefore, beyond the prescribed period of limitation. G

Whether there is inter-dependence and whether another unit is, in fact, a dummy has to be adjudicated on the facts of each case. There cannot be any generalization or rule of universal application. Two basic features which *prima facie* show inter-dependence are pervasive financial control H

A and management control. In the present case facts clearly show financial control. Undisputedly, the share capital of each of the three companies was Rs.200. Though it was claimed that financial assistance was availed from the financial companies, it is on record that the unsecured loans advanced by MACL to the three companies were substantially heavy amounts as on B 1.4.1998. NGCPL received an amount of Rs. 1.55 crores. About 14 lakhs appeared to have been paid after the issue of show cause notice. Loans advanced to NGCPL was about Rs. 52 lakhs while to SCGCPL it was about Rs.65 lakhs. The finding of the Commissioner that the financial assistance from the financial institutions were availed with the aid and assistance of MACL has not been seriously disputed. Apart from that, the cylinders were C brought on lease by MACL from another concern and were sub-leased to the three companies. The cylinders bore the name of MACL. If the three companies had separate standing as contended it could not be explained why they could not get the cylinders directly from the lessors on lease basis and the need for introducing MACL as the lessee and then the three D companies becoming sub-lessees. As noted by the Commissioner, entire receipts were paid as lease amount to MACL. Here again, the under-valuation aspect assumes importance. While the supply by MACL to three companies was Rs. 0.50 per unit, the sale price by the three companies was Rs. 5 per unit. It is on record that accounts were kept by common staff E and marketing was done under the supervision of a person who belongs to the same group of concerns. The amounts have been collected by an employee of MACL. The so-called Directors of the companies were undisputedly employees of MACL. Almost the entire financial resources were made by MACL. The financial position clearly shows that MACL had F more than ordinary interest in the financial arrangements for companies. The statements of the employees/Directors show that the whole show was controlled, both on financial and management aspects by MACL. If these are not sufficient to show inter-dependence probably nothing better would show the same. The factors which have weighed with CEGAT like registration of three companies under the sales tax and income tax G authorities have to be considered in the background of factual position noted above. When the corporate veil is lifted what comes into focus is only the shadow and not any substance about the existence of the three companies independently. The circular no. 6/92 dated 29.5.1992 has no relevance because it related to notification no. 175/86-CE dated 1.3.1986 H and did not relate to notification no. 1/93. The extended period of limitation

was clearly applicable on the facts of the case, as suppression of material features and factors has been clearly established. If in reality the three companies are front companies then the price per unit to be assessed in the hands of MACL is Rs. 5 and not Rs. 0.50 as disclosed. The question whether there was manufacture or not was not in issue before the Commissioner. The plea that there was no manufacture has also to be rejected in view of the fact that exemption was claimed by the three companies as manufacturers to avail the benefit of Central Excise Notification no. 1/93.

The inevitable conclusion is that CEGAT's judgment is indefensible. Accordingly, the same is set aside and that of the Commissioner is restored, so far as it relates on the peculiar facts of the case, to levy of duty, penalty and interest on MACL are concerned.

The appeals are accordingly allowed with no order as to costs.

V.S.S. Appeals allowed.