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COMMISSIONER OF CENTRAL EXCISE, CHENNAI-I

v

CHENNAI PETROLEUM CORPN. LTD.

APRIL 19, 2007

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[S.H. KAPADIA AND B. SUDERSHAN REDDY, JJ.]

*Central Excise Tariff Act, 1985:*

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*Chapters 27, 28 and 29—Oil Refinery—Declared deemed warehouse—Using Refinery Fuel Oil to produce naphtha, sulphur and electricity—Major portion of electricity so generated captively consumed but a part thereof sold—Demand of duty raised on RFO—HELD: Tribunal was right in its view that naphtha and sulphur being petroleum products a assessee was entitled to exemption in respect of RFO used for producing these items—Similarly assessee was entitled to exemption as regards electricity captively consumed—But with regard to portion of electricity sold, Revenue was right in demanding duty on RFO for the period August 1998 to January 1999—To that extent adjudicating authority would determine duty amount afresh.*

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*Central Excise Act, 1944:*

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*s.11-A—Invoking of extended period of limitation for arrears of duty—Oil Refinery owned by Central Government—Declared deemed warehouse—Using Refinery Fuel Oil to generate electricity a portion of which sold—Revenue issuing show cause notices demanding arrears of duty for period December, 1993 to July, 1998 by show cause notice dated 22.12.1998—HELD : There was no suppression on the part of assessee—Revenue was not right in invoking extended period of limitation—Demand is beyond limitation.*

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**Assessee, a refinery, declared by the Central Government to be a “deemed warehouse”, used Refinery Fuel Oil, i.e. the residuary left after distilling crude oil, in producing petroleum products, namely, naphtha, sulphur and electricity, which fell under Chapters 27, 28 and 29 of Central Excise Tarriff Act, 1985. The major portion of the electricity so generated was captively consumed, and a part of it was sold to the Tamil Nadu Electricity Board. According to the Revenue none of these products, namely, naphtha,**

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sulphur and electricity were petroleum products and, therefore, the refinery was liable to pay duty. Accordingly, demands were raised to pay arrears of duty for the period 1993 to July 1998 under show cause notice dated 22.12.1998 and for the period August 1998 to January 1999 under show cause notice dated 17.7.1999. The Tribunal held partly in favour of the assessee and partly in favour of the Revenue which gave rise to the present appeals and cross appeals.

Disposing of the matters, the Court

**HELD: 1.1.** The Tribunal rightly held that naphtha and sulphur are petroleum products and, therefore, the assessee which was a “deemed warehouse” was entitled to exemption in respect of RFO used for producing naphtha and sulphur during the period in question. Consequently, the show cause notice dated 22nd December, 1998 demanding duty on RFO used by the assessee for the manufacture of naphtha and sulphur is not sustainable.

[Para 4 and 5] [325-F-H]

**1.2.** As regards the electricity produced by assessee from RFO and sold to Tamil Nadu Electricity Board, Revenue was right in demanding duty on RFO. The very purpose behind giving the status of “deemed warehouse” to the refinery is to provide exemption to the RFO which is used for producing petroleum products. The Deemed Warehouse status demands nexus to the final product cleared from it. Generation of electricity, if captively consumed, is exempted from duty. This is because electricity which is generated in the refinery is used to operate the various processes within the refinery. However, a portion of the generated electricity, in the present case, is sold to Tamil Nadu Electricity Board. To that extent alone, the Department was right in demanding duty on RFO. [Para 6] [326-A-D]

*Indian Oil Corporation Ltd. v. Collector of Central Excise, Baroda*, (2006) 202 ELT 37 SC, relied on.

**2.1.** So far as the question of Revenue invoking the extended period of limitation under Section 11A of the Central Excise Act is concerned, the assessee is a Public Sector Company owned by the Government of India. There was no suppression on the part of the assessee and, therefore, the Department was wrong in invoking the extended period of limitation under the show-cause notice dated 22nd December, 1998 for the period December 1993 to July 1998. The demand to that extent is beyond limitation. [Para-7] [326-F-G]

A 2.2. The second show cause notice dated 17th February, 1999 is within limitation. Assessee would be liable to payment of duty thereunder on the RFO used for producing electricity which was sold to Tamil Nadu Electricity Board. This will require recalculation. Accordingly, to that extent alone, the matter is being remitted to the adjudicating authority for fresh determination of the duty amount payable by the assessee during the period August 1998 to January 1999. [Para 8] [327-A-B]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 318-322 of 2006.

C From the Final Order Nos. 63, 64, 65, 66 & 67 of 2005 dated 07.01.2005 of the Customs, Excise & Service Tax Appellate Tribunal, South Zonal Bench, Chennai in Appeal Nos. E/000364/2000, E/0000786/2001, E/000787/2001, E/001234/2001 and E/0012345/2001.

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D Civil Appeal Nos. 4607 & 4639 of 2005.

V. Shekar, Navin Prakash, Tufail A. Khan, Sudhir Kr. Sajwan, Pradeep Dubey, P. Parmeshwaran and B.K. Prasad for the Appellant.

V. Lakshmikumaran, Alok Yadav and M.P. Devanath for the Respondent.

E The Judgment of the Court was delivered by

F **KAPADIA, J.** 1. The above group of Civil Appeals and cross Civil Appeals are filed by the Department and the assessee, M/s. Chennai Petroleum Corporation Ltd. respectively under Section 35L(b) of the Central Excise Act, 1944.

G 2. The assessee manufactures petroleum products like naphtha from crude oil since 1969. These petroleum products fall under Chapters 27, 28 and 29 of the Central Excise Tariff Act, 1985. Basically, the assessee is a refinery. It uses Refinery Fuel Oil (RFO), being the residuary left after distillation of Bombay High Crude Oil as fuel for generation of high pressure steam which in turn is used for generation of electricity for their co-generation plant in which the high pressure steam moves a turbine which generates electricity. A part of that electricity is supplied to Tamil Nadu Electricity Board and the major portion of it is captively consumed.

H 3. In the present case, we are concerned with three products produced

by the assessee in their refinery from the said RFO. The three products are naphtha, sulphur and electricity. The assessee is a refinery. It is declared by the Central Government to be a "deemed warehouse". RFO is the material which remains in the refinery. The said RFO is not removed from the refinery. It is a residue which remains at the bottom of the columns in the refineries. It is like slurry. According to the Department, assessee had failed to declare to the Department that the said RFO was used to produce electricity. According to the Department, the assessee had failed to declare to the Department that a part of the electricity generated was sold to Tamil Nadu Electricity Board. According to the Department, sulphur was not a petroleum product and, therefore, to the extent that the said RFO was used to produce sulphur was dutiable and not exempted. According to the Department, none of the three products, namely, naphtha, sulphur and electricity were petroleum products and, therefore, the refinery was liable to pay duty. According to the Department, the refinery was a "deemed warehouse", but the above three products were not petroleum products and, therefore, the assessee was liable to pay duty. Accordingly, demands were made on the assessee to pay arrears of duty for the period December 1993 to July 1998 and for the period August 1998 to January 1999. It may be noted that the period December 1993 to July 1998 (five years) came under show-cause notice dated 22nd December, 1998 whereas the period August 1998 to January 1999 came under show cause notice dated 17th February, 1999. Consequently, in the present case, we are required to consider whether the Department was entitled to invoke the extended period of limitation under Section 11A with show cause notice dated 22nd December, 1998. However, that question did not arise in the case of show cause notice dated 17th February, 1999 since the demand fell within the period of limitation.

4. Having heard learned counsel on both sides, we are in agreement with the view expressed by the Tribunal in its impugned judgment by which it has been held that naphtha is a petroleum product and, therefore, the assessee which was a "deemed warehouse" was entitled to exemption in respect of RFO used for producing naphtha during the above period. Therefore, to this extent, the assessee succeeds. To this extent, the show cause notice dated 22nd December, 1998 fails.

5. We are also in agreement with the view taken by the Tribunal that sulphur produced on RFO is a by-product and consequently, the show cause notice dated 22nd December, 1998 demanding duty on RFO used by the assessee for the manufacture of sulphur is not sustainable. The assessee succeeds in this regard also.

A 6. However, the assessee produces electricity from RFO. That electricity is sold to Tamil Nadu Electricity Board. The major portion of the electricity produced is captively consumed. The entire generated electricity is not sold. A part of the generated electricity is sold. It was vehemently argued before us on behalf of the assessee that the refinery was a “deemed warehouse” and whatever is produced in the refinery from the RFO was entitled to exemption.

B It was vehemently urged that RFO is a residuary which remains at the bottom of the columns. That RFO was never removed from the refinery. Hence, the assessee was entitled to claim deduction for even the RFO used in generation of electricity. We do not find merit in this argument. The assessee is a refinery. It is a “deemed warehouse”. It is so recognised by the Central Government.

C This is not in dispute. The very purpose behind giving the status of “deemed warehouse” to the refinery is to provide exemption to the RFO which is used for producing petroleum products. That status is not meant for producing products which are not petroleum products. In other words, the Deemed Warehouse Status demands nexus to the final product cleared from it. Generation of electricity, if captively consumed, is exempted from duty. This

D is because electricity which is generated in the refinery is used to operate the various processes within the refinery. In the refinery, there exists large number of processes. Each process generates an item and, therefore, every refinery is given the status of “deemed warehouse”. However, a portion of the generated electricity, in the present case, is sold to Tamil Nadu Electricity Board. To that extent alone, the Department was right in demanding duty on RFO.

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7. The question still remains as to whether the Department was right in invoking the extended period of limitation under Section 11A of the Central Excise Act. In this connection, we are of the view that there was no suppression on the part of the assessee. As stated above, the assessee is a Public Sector

F Company. It is owned by the Government of India. The Department was aware that the assessee was a refinery. Nothing prevented the Department from visiting the site. Nothing prevented the Department from inquiring into the process within the refinery in the matter of production of naphtha, sulphur and electricity. Generation of electricity was also used for the running of the refinery. The electricity was supplied to Tamil Nadu Electricity Board (partly).

G In the circumstances, there was no suppression on the part of the assessee and, therefore, we are of the view that the Department was wrong in invoking the extended period of limitation under the show-cause notice dated 22nd December, 1998 for the period December 1993 to July 1998. The demand to that extent is beyond limitation. The assessee succeeds in that regard.

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8. The second show cause notice dated 17th February, 1999 is within limitation. It seeks to demand duty for the period August 1998 to January 1999 on the RFO used for producing electricity. We have held that the electricity generated from RFO which was captively consumed by the refinery was not liable to duty. To that extent, the demand made in the show cause notice dated 17th February, 1999 fails. However, as stated above, a part of the electricity produced from RFO was sold to Tamil Nadu Electricity Board during the period August 1998 to January 1999. To that extent alone, the assessee would be liable to payment of duty. This will require recalculation. Accordingly, to that extent alone, the matter is being remitted to the adjudicating authority for fresh determination of the duty amount payable by the assessee during the period August 1998 to January 1999.

9. We are also of the view that the penalty imposed on the assessee was unjustified since it has produced naphtha and sulphur which are petroleum products. Similarly, the assessee has produced electricity from RFO, the major portion of which has been used for captive consumption and a minor portion is sold to Tamil Nadu Electricity Board. In the circumstances, we are of the view that the Department had erred in imposing penalty.

10. Before concluding, we may quote hereinbelow paragraph 12 and paragraph 13 from the judgment of this Court in the case of *Indian Oil Corporation Ltd. v. Collector of Central Excise, Baroda*, (2006) 202 ELT 37 (SC)]:

“12. Apart from this, considering the appeal on merits as well, we find that the assessee would be entitled to the benefit in terms of entry 34 of exemption Notification No.75/84. The same reads as under :

Sl. No.	Description of goods	Rate of duty	Intended use/ Condition
34	Low Sulphur Heavy Stock	Nil	Intended for use as fuel in a refinery <i>Explanation.-</i> “Refinery” means a refinery wherein refining of crude petroleum or shale or blending of non-duty paid petroleum products is carried on.

The Board has issued a circular which reads as under :

A Eligibility of concession under Notification Nos.74/63-C.E., dated 18-5-63 @ 353/77-C-E, dated 16-12-77.

In supersession of the Board's instructions contained in F.No.3565-CX-3 dated 16-9-67 *it has been decided that since generation of electrical energy (electricity as an intermediate product is incidental in the process and manufacture of petroleum products falling under T.I. Nos. 6 to 11AA the exemption contained in the Notification No.352/77-C.E., dt. 16-12-77 as amended by Notification Nos.131/80-C.E., dt. 23-8-80 and 41/82-C.E., dt. 28-2-82 would be available to the quantity of intermediate product electricity. The exemption contained in this notification will, however, not be available to that quantity of petroleum products which is used in the generation of electricity which, in turn, is not used in the process and manufacture of petroleum products.*" [emphasis supplied]

[underline by us]

D 13. Low Sulphur Heavy Stock is used by the assessee as fuel in a Thermal Power Plant located within the refinery area for generating electricity which in turn is captively consumed for production of various petroleum products. Entry No.34 of Notification No.75/84 read with the clarificatory circular clearly spells out that the assessee would be entitled to the benefit of exemption on LSHS to the extent it is used in Thermal Power Plant located within the refinery area for generating electricity which in turn is used in the process of manufacture of petroleum products."

E 11. Accordingly, the above civil appeals and the cross appeals are  
F disposed of with no order as to costs.

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Appeals disposed of.