

IN THE HIGH COURT OF DELHI AT NEW DELHI

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Judgment delivered on: 22.07.2016

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W.P.(C) 4754/1995

M/S SML ISUZU LTD. & ANR.

..... Petitioners

Through: Mr L. Badri Narayanan, Mr Aditya
Bhattacharya & Mr Yogendra Aldak, Advocates.

versus

UOI & ANR.

..... Respondents

Through: Ms Meera Bhatia, Senior Standing
counsel, Mr Bhagvan Swarup Shukla, CGSC and
Mr Rachit Goel, Advocate for UOI.
Mr Satish Kumar, Senior Standing Counsel for
Central Excise.

WITH

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W.P.(C) 1824/2000

M/S SML ISUZU LTD. & ANR.

..... Petitioners

Through: Mr L. Badri Narayanan, Mr Aditya
Bhattacharya & Mr Yogendra Aldak, Advocates.

versus

UOI & ANR.

..... Respondents

Through: Ms Meera Bhatia, Advocate for UOI.
Mr Satish Kumar, Senior Standing Counsel for
Central Excise.

AND

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W.P.(C) 1826/2000

V.E. COMMERCIAL VEHICLE LTD.
& ANR.

..... Petitioners

Through: Mr L. Badri Narayanan, Mr Aditya
Bhattacharya & Mr Yogendra Aldak, Advocates.

versus

UOI & ANR.

..... Respondents

Through: Ms Meera Bhatia, Senior Standing
counsel and Mr Amit Mahajan, CGSC for UOI.
Mr Satish Kumar, Senior Standing Counsel for
Central Excise.

CORAM:
JUSTICE S.MURALIDHAR
JUSTICE VIBHU BAKHRU

JUDGMENT

VIBHU BAKHRU, J

Introduction

1. The Petitioners in WP(C) Nos.1824/2000 and 1826/2000 have filed the said petitions under Article 226 of the Constitution of India, *inter alia*, impugning Sections 131 (b), 132(1)(a), and 132 (2) of the Finance Act, 1999 as being *ultra vires* the Constitution of India.
2. By virtue of Section 131 (b) of the Finance Act, 1999, clause (xxviii) was introduced in Sub-section 2 of Section 37 of the Central Excise Act, 1944 (hereinafter referred as the Act), to specifically empower the Central Government to make rules to provide for the lapsing of credit of duty lying unutilised with the manufacturer from a specified date.
3. Section 132 (1) (a) and Section 132 (2) of the Finance Act, 1999

were enacted to validate Sub-rule (4A) of Rule 57F of the Central Excise Rules, 1944 (hereafter 'the Rules') which had been held to be beyond the rule making power of the Central Government by the Supreme Court in ***Eicher Motors Private Limited v. Union of India: 1999 (106) ELT 3 (SC)***.

By virtue of the said sub-rule, MODVAT credit in respect of Excise duties paid on inputs for manufacture of goods falling under the heading no. 87.01, 87.02, and 87.04 and 87.06 of the Schedule to the Central Excise Tariff Act, 1985 lying unutilised as on 16.03.1995, was mandated to have lapsed and consequently unavailable for payment of duty on excisable finished goods.

4. The Petitioners in W.P.(C) No.4754/1995 *inter alia* impugn the validity of Sub-rule (4A) of Rule 57F and seek an appropriate writ declaring the said Sub-rule to be *ultra vires* the Constitution of India.

Factual context

5. M/s SML Isuzu Limited and M/s V E Commercial Vehicles Limited (hereafter referred to as 'the Petitioners') are mainly engaged in the manufacturing of chassis for light commercial vehicles (hereafter 'LCVs') falling under sub-heading 8706.20 and 8706.40 to the Schedule to Central Excise Tariff Act, 1985(hereafter the Tariff Act) as well as motor vehicles

for carrying goods that fall within the sub-heading 8704 of the said Schedule. The Petitioners purchase raw materials/inputs for the manufacture of finished goods, from indigenous sources as well as from overseas. The Petitioners pay all applicable duties including Excise Duty, Customs Duty, Additional Duty and Countervailing Duty on raw material/inputs purchased by them. In terms of the MODVAT scheme, the Petitioners have been availing credit in respect of the duty paid by them on inputs for discharge of the Excise Duty payable on the finished products since 1986. It is stated that in 1993, the Excise Duty payable on the goods manufactured by the Petitioners was reduced from 20% to 15% but the duty chargeable on the parts used in manufacture of those goods was increased to 20% to 25%. In view of this duty structure, the Petitioners were unable to fully utilise the MODVAT credit available in respect of duties paid on inputs for discharging the Excise Duty payable on the finished goods.

6. The Petitioners assert that the said inverted duty structure - where the rate of duty payable on inputs was greater than the duty payable on finished goods - was only in respect of tractors and LCV manufacturing Industry. The said Industry comprises of only nine manufacturers including the Petitioners and only these manufacturers are adversely affected by the

said Rule 57F(4A) of the Rules.

7. The denial of credit for the duties paid by Petitioners is at the core of the disputes involved in these petitions. It is claimed that SML Isuzu Limited and VE Commercial Vehicles Limited were denied the benefit of accumulated credit of Rs. 4.88 Crores and Rs 8.21 Crores respectively; they, accordingly, claim refund of the said amounts.

Submissions

8. Mr. L. Badri Narayanan, learned counsel for the Petitioners, submitted that the effect of the impugned provisions of the Finance Act, 1999 is that the Petitioners are deprived of their vested rights and in the given circumstances, the impugned provisions are unreasonable and arbitrary and ultra-vires the Constitution of India. He further contended that validating Rule 57F(4A) with retrospective effect was unreasonable and violative of the Part III of the Constitution. He submitted that it is permissible to pass retrospective legislation in certain circumstances, but it would be unreasonable to resort to such legislation in cases where the Assessee had acted in accordance with rules. He referred to the opinion of Justice Sen in *Lohia Machines Limited v. Union of India* (1985) 2 SCC 197, wherein it has been held that the retrospective application of Section

80J of the Income Tax Act, 1957 would be invalid.

MODVAT Scheme

9. On the presentation of the Annual Budget 1986-87 in the Lok Sabha on 28.02.1986, the then Finance Minister referred to the 'Modified Value Added Tax' MODVAT Scheme-I, which he stated was formulated to address the issues regarding the cascading effect of Excise Duty paid for the manufacturing of the products utilising excisable inputs. Conceptually, the scheme provided for a proforma credit for duties paid on inputs for discharging the excise liability on finished goods. The MODVAT Scheme initially introduced was applicable to all goods covered under 37 Chapters of the Tariff Act including motor vehicles. In terms of the above scheme, credit would be available to a manufacturer in respect of Excise Duty as well as Additional Duties of Customs (known as Countervailing Duty) for payment of the Excise Duty on finished products. The said scheme came into force on 01.03.1986.

10. Section AA of Chapter V of the Rules contain Rules 57A to 57E embodying the statutory framework of the MODVAT Scheme.

11. The circular dated 08.08.1988 reported in **1988 (37) ELT T-17** clarified that the accumulated credit of duties paid on inputs could also be

utilised for payment of the Excise Duty on finished products manufactured from the use of duty-exempted inputs. The relevant extract of the said circular is reproduced below:-

“The matter has been examined by the Board. It is observed that what Rule 57F(3) basically provides is that the credit of duty allowed in respect of any inputs may be utilised towards payment of duty on any of the final products in or in relation to the manufacture of which such inputs are intended to be used. This rule does not debar utilisation of excess (accumulated because of less duty on final products than on the Input's) for payment of duty on the same final products which are manufactured by non-duty paid inputs (whether procured under Chapter X procedure or otherwise exempt under any notification). Moreover, there is no 'one to one co-relation of inputs and final product under the MODVAT scheme for utilisation of credit. It has therefore been decided by the Board that the excess credit accumulated if any, can be utilised towards payment of duty on the same final products even if manufactured out of non duty paid inputs.”

12. The departmental clarification as published in the booklet ‘Guide to MODVAT’ also reiterated the above clarification. The clarifications published in the said guide are in the question-answer form. Question No. 20 and its answer is relevant and is reproduced below:-

“Question 20:

When can the credit of duty paid on the inputs be used for paying duty on the final product? Is there any one to one co-relation between the inputs used and the final product manufactured?

Answer:

The MODVAT scheme provides for instant credit. The credit of the duty paid on the inputs can be taken as soon as the inputs are received and the evidence of payment of duty is in hand and the same may be utilised immediately for payment of duty on the final products for the manufacture of which such inputs are intended to be utilised. There need not be any one to one co-relation between the input and the final product.

It may be mentioned that there is generally no provision for refund of the Modvat credit (except in case of exports) and such credit can be utilised only for the purpose of payment of duty;

- (i) on the finished excisable goods in the manufacture of which such inputs are intended to be used;
- (ii) on the waste arising in the course of manufacture of such final products;
- (iii) on the inputs themselves, if such inputs are cleared as such.[Rule57F(3)].

The input duty credit available in respect of final products which are exported under bond can also be utilised similarly.”

13. In terms of Rule 57G (2) of the Rules, the Petitioners are entitled to the credit of duties paid on the inputs immediately on the receipt of such inputs in the factory. It is not disputed that the excise duty structure of goods used as inputs for manufacturing the final product was always less than the excise duty payable on the final product. However, for a period of three years commencing from 1993 - that is, 1993-94, 1994-95, and 1995-96 - the said duty structure was inverted. In other words, the excise duty payable on inputs used for manufacturing certain goods including LCVs

ranged between 20% and 25% which was significantly higher than the excise duty payable on such finished goods which ranged between 10% and 15%. This was also coupled with the fact that the manufacturing of finished goods did not result in sufficient value addition to absorb the duties of excise paid on the inputs. Consequently, the manufacturers were unable to utilise the MODVAT credit in respect of specified duties paid on the inputs, for paying the duty on final product.

14. Admittedly, prior to the year 1995, the credit in respect of duty paid on any input could only be utilised for payment of excise duty on the finished product which were manufactured by use of such inputs. In 1995-96, the Government of India provided for liberalisation of the use of credit on account of duties paid on any inputs used for manufacturing of excisable goods by allowing such credit to be used for payment of excise duty on any other goods. In other words, it was not necessary that MODVAT credit available in respect of duties paid on inputs be utilised for payment of duties in respect of products manufactured by using such inputs. This was intended to provide the manufactures with flexibility to use the credit available on account of duties paid for discharge of duties payable on other finished goods as well. At the same time, the excise duty structure was rationalised and Government of India also decided to lapse

the un-utilised MODVAT credit other than the credit in respect of duties on inputs which were physically lying in the factory premises either as raw material or as incorporated in the finished products.

15. Accordingly by a notification No.11/95 CE(NT) dated 16.03.1995, sub Rule 4A was introduced in Rule 57F of the Rules which reads as under:-

“57-F. (4-A) Notwithstanding anything contained in sub-rule (4), or sub-rule (1) of Rule 57-A and the notifications issued thereunder, any credit of specified duty lying unutilised on the 16th day of March, 1995 with a manufacturer of tractors, falling under Handing No. 87.01 or motor vehicles falling under Heading No. 87.02 and 87.04 [or chassis of such tractors or such motor vehicles under Heading No. 87.06] of the Schedule to the Central Excise Tariff Act, 1985 (5 of 1986) shall lapse and shall not be allowed to be utilised for payment of duty on any excisable goods, whether cleared for home consumption or for export:

Provided that nothing contained in this sub-rule shall apply to credit of duty, if any, in respect of inputs lying in stock or contained in finished products lying in stock on the 16th day of March, 1995.”

The decision of the Supreme Court in Eicher Motors Pvt. Ltd.

16. The validity of Rule 57F(4A) of the Rules was challenged before the Supreme Court, *inter alia*, on the following grounds:-

“1. Modvat credit lying in balance with the assessee as on 16-3-1995 represents a vested right accrued or acquired by the

assessee under the existing law and such right is sought to be taken away by impugned Rule 57F(4A) and the Central Government has no powers under Section 37 of the Central Excise Act, 1944[hereinafter referred to as 'the Act'] or any other provision thereof to frame such a rule.

2. The impugned rule is arbitrary and unreasonable as the same has been framed without due application of mind to the relevant facts and it has been exercised on the basis of non-existent facts or which are patently erroneous.

3. Section 37 of the Act does not enable the Central Government to frame a rule enabling the lapsing of the balance in Modvat account and is therefore *ultra vires* the rule making power.

4. The rule is vitiated on the grounds of promissory estoppel and/or the doctrine of legitimate expectation.”

17. The Assessee, that is, the Petitioner therein contended that they had utilised the facility of the scheme by paying excess duty on inputs and had carried forward the accumulated credit for paying excise duties chargeable on finished product and, therefore, Rule 57F(4A) of the Rules in effect took away their vested rights. The respondents, on the other hand, countered the aforesaid argument by contending that Rule 57F(4A) of the Rules was only a part of the scheme for providing concessions and it was not necessary that the said scheme be continued for all times. It was contended that the power to frame Rules for such scheme would also include the power to vary or modify the scheme.

18. The Supreme Court held that for the purpose of utilisation of the credit, all vestitive facts or necessary incidents thereto had taken place prior to 16th March, 1995. The duty paid inputs had been utilised in manufacturing finished products which had been cleared thereafter. The Court observed that under the MODVAT scheme, the Assessee became entitled to credit of the input instantaneously on the input being received in the factory. In this view, the Supreme Court held as under:-

“The basic postulate, that the scheme is merely being altered and, therefore, does not have any retrospective or retro-active effect, submitted on behalf of the State, does not appeal to us. As pointed out by us that when on the strength of the rules available certain acts have been done by the parties concerned, incidents following thereto must take place in accordance with the scheme under which the duty had been paid on the manufactured products and if such a situation is sought to be altered, necessarily it follows that right, which had accrued to a party such as availability of a scheme, is affected and, in particular, it loses sight of the fact that provision for facility of credit is as good as tax paid till taxes adjusted on future goods on the basis of the several commitments which would have been made by the assessee concerned. Therefore, the scheme sought to be introduced cannot be made applicable to the goods which had already come into existence in respect of which the earlier scheme was applied under which the assessee had availed of the credit facility for payment of taxes. It is on the basis of the earlier scheme necessarily the taxes have to be adjusted and payment made complete. Any manner or mode of application of the said rule would result in affecting the rights of the assessee.

We may look at the matter from another angle. If on the inputs the assessee had already paid the taxes on the basis that when

the goods are utilised in the manufacture of further products as inputs thereto then the tax on these goods gets adjusted which are finished subsequently. Thus a right accrued to the assessee on the date when they paid the tax on the raw materials or the inputs and that right would continue until the facility available thereto gets worked out or until those goods existed. Therefore, it becomes clear that Section 37 of the Act does not enable the authorities concerned to make a rule which is impugned herein and, therefore, we may have no hesitation to hold that the rule cannot be applied to the goods manufactured prior to 16-3-1995 on which duty had been paid and credit facility thereto has been availed of for the purpose of manufacture of further goods.”

Impugned provisions

19. The impugned provisions of the Finance Act, 1999 were enacted to overcome the decision of the Supreme Court in ***Eicher Motors Pvt Ltd*** (*supra*) and to sustain the lapse of the accumulated MODVAT credit in respect of the goods falling under the specified headings.

20. By virtue of clause (b) of Section 131 of the Finance Act, Sub clause (xxviii) was introduced in Sub-section 2 of Section 37 of the Act. The said provision reads as under:-

“131.Amendment of section 37. - In section 37 of the Central Excise Act, in sub-section (2), -

(a) xxxx xxxx xxxx xxxx

(b) after sub-clause (xxvii), the following sub-clause shall be inserted and shall be deemed to have been inserted with effect from the 16th day of March, 1995, namely : -

“(xxviii) provide for the lapsing of credit of duty lying unutilised with the manufacturer of specified excisable goods on an appointed date and also for not allowing such credit to be utilised for payment of any kind of duty on any excisable goods on and from such date.”.

21. By virtue of clause (a) of sub Section 1 of Section 132 of the Finance Act, 1999, Sub-rule 4A of Rule 57F of the Rules was validated and it was expressly enacted that said Sub-rule shall be deemed to have and to have always had effect from 16th March, 1995. Sub-section 2 of Section 132 was enacted to validate all actions taken pursuant to introduction of Sub-rule 4A in Rule 57F of the Rules. The said provisions impugned in these petitions and are set out below:-

“132. Validation of certain rules. - (1) In the Central Excise Rules, 1944, made by the Central Government in exercise of the powers conferred under section 37 of the Central Excise Act, in rule 57F, -

(a) sub-rule (4A), as inserted by the Central Excise (Fourth Amendment) Rules, 1995, shall be deemed to have and to have always had effect from the 16th day of March, 1995;

XXXX XXXX XXXX XXXX XXXX

(2) Any action taken or anything done or purported to have been taken or done at any time during the period commencing from the 16th day of March, 1995 and ending with the day the Finance Act, 1999 receives the assent of the President (hereinafter referred to as the said period) under the

Central Excise Act or any rules made thereunder in relation to the lapsing of credit of duty lying unutilised with the manufacturer of specified excisable goods and also for not allowing such credit to be utilised for payment of any kind of duty on any excisable goods shall be deemed to be, and to always have been, for all purposes, as validly and effectively taken or done as if the amendments made by sub-section (1) had been in force at all material times and, accordingly, notwithstanding anything contained in any judgment, decree or order of any court, tribunal or other authority, -

(a) the lapsing of credit of duty lying unutilised with the manufacturer of specified excisable goods and also for not allowing such credit to be utilised for payment of any kind of duty on any excisable goods, during the said period shall be deemed to always have been, as validly lapsed, as if the amendments made by sub-section (1) had been in force at all material times;

(b) no suit or other proceedings shall be maintained or continued in any court for allowing the credit of, and no enforcement shall be made by any court of any decree or order allowing the credit of duty which has been lapsed and not allowed to be utilised and which would have been validly lapsed and not allowed to be utilised if the amendments made by sub-section (1) had been in force at all material times;

(c) recovery shall be made of all the credit of duty, which have not been lapsed or, as the case may be, which have been taken or utilised but which would have been lapsed, or as the case may be, would not have been allowed to be taken or utilised, if the amendments made by sub-section (1) had been in force at all material times, within a period of thirty days from the day, the Finance Act, 1999 receives the assent of the President and in the event of non-payment of such credit of duties within this

period, in addition to the amount of credit of such duties recoverable, interest at the rate of thirty six per cent. per annum shall be payable, from the date immediately after the expiry of the said period of thirty days till the date of payment.

Explanation.-. For the removal of doubts, it is hereby declared that no act or omission on the part of any person shall be punishable as an offence which would not have been so punishable if this section had not come into force.”

Reasoning and Conclusion

22. As is apparent from the above, the Parliament enacted Rule 57F(4A) to be in effect from 16th March, 1995. Sub-section (2) of Section 132 contain express provisions for sustaining any action in relation to lapsing of credit of duty lying unutilised with the manufacturer, which was done or purported to have been done during the period commencing 16th March, 1995. Sub-clause (a) of sub section 2 reaffirmed that lapsing of accumulated credit would be deemed to have always been validly lapsed. Sub clause (c) of Sub-section 2 enacted express provisions for recovery of the credit duty which may have been utilised for payment of excise duty. The said sub clause also provides for charging interest at the rate of 36% per annum for a period commencing after expiry of 30 days from the enactment till the date of payment.

23. There are two aspects to the challenge laid by the Petitioners to the

impugned provisions of the Finance Act, 1999. The first aspect relates to the validity of retrospectively affirming Rule 57F(4A) of the Rules which had been held to be beyond the scope of Section 37 of the Act by the Supreme Court in *Eicher Motors* (*supra*). The second aspect relates to the challenge to the validity of the substantive import of the Rule 57F(4A) of the Rules as offending the rights guaranteed under Part III of the Constitution of India.

24. As indicated above, the only ground on which the Supreme Court held that Rule 57F(4A) could not be applied to MODVAT credit already accumulated with the manufacturers was that the same would affect the rights of parties which had crystallised and the Central Government was not empowered to frame any subordinate legislation for taking away the said accrued rights. Indisputably, the said defect has been cured inasmuch as the Parliament has by Section 131 of the Finance Act, 1999 specifically empowered the Central Government to frame Rules for lapsing of accumulated credit on a specified date. Thus, if we assume - for the purposes of considering the challenge to the retrospective affirmation of Rule 57F(4A) of the Rules - that there was no defect in Rule 57F(4A) at the time when it was initially made except that the Central Government lacked the power to do so, it is at once clear that the challenge to Section

132(2) of the Act is without merit. This is so, because it is now well settled that the legislature can enact laws to operate retrospectively and enforce an earlier invalid legislation provided: (i) the defect for which the earlier legislation had been invalidated is cured; and (ii) the legislature has the legislative competence over the object of the legislation. It is well established that to legislate on the object within the field of the legislative competence and to enforce the legislative policy - including by way of a retrospective legislation - is a perfectly permissible exercise of legislative power.

25. In ***Rai Ramkrishna v. The State of Bihar: (1963) 50 ITR 171 (SC)***, the Supreme Court considered the challenge to the validation of the retrospective operation of the Bihar Taxation on Passengers and Goods (Carried by Public Service Motor Vehicles) Act, 1961. The said Act essentially sought to validate the tax levied on passengers and goods carried by public service motor vehicles in Bihar which was initially sought to be levied by virtue of the Bihar Finance Act, 1950. The said law had been struck down as invalid for lack of assent by the President. The Court noted that there was no challenge to the prospective operation of the Bihar Taxation on Passengers and Goods (Carried by Public Service Motor Vehicles) Act, 1961. In the context of the challenge to the retrospective

operation of the law, the Court observed as under:-

“The other point on which there is no dispute before us is that the legislative power conferred on the appropriate legislatures to enact law in respect of topics covered by the several entries in the three Lists can be exercised both prospectively and retrospectively. Where the legislature can make a valid law, it may provide not only for the prospective operation of the material provisions of the said law, but it can also provide for the retrospective operation of the said provisions. Similarly, there is no doubt that the legislative power in question includes the subsidiary or the auxiliary power to validate laws which have been found to be invalid. If a law passed by a legislature is struck down by the Courts as being invalid for one infirmity or another, it would be competent to the appropriate legislature to cure the said infirmity and pass a validating law so as to make the provisions of the said earlier law effective from the date when it was passed. This position is treated as firmly established since the decision of the Federal Court in the case of *The United Provinces v. Mst. Atiq Begum* : (1940) F.C.R. 110.”

26. In *Virender Singh Hooda v. State of Haryana*: (2004) 12 SCC 588, the Supreme Court observed:

“It is well settled that if the legislature has the power over the subject-matter and competence to make a valid law, it can at any time make such a valid law and make it retrospectively so as to bind even past transactions. The validity of a validating law, therefore, depends upon whether the legislature possesses the competence which it claims over the subject-matter and whether in making the validation it removes the defect which the courts had found in the existing law.”

27. There are numerous decisions of the Supreme Court and High Courts where the Courts have rejected the challenge to validating acts which retrospectively validate a levy that has been struck down by the Courts. It is now well established that the legislature can frame laws retrospectively within the field of their legislative competence. It is also well established that validating acts which cure the defect that invalidated an earlier legislation cannot be impugned as being unreasonable solely on the ground of their retrospective operation (except, of course, where the period of retrospective operation is itself unreasonable and unjustified).

28. In *R.C. Tobacco Pvt. Ltd. v. Union of India: (2005) 7 SCC 725*, the Supreme Court referred to the decision of *Rai Ramkrishna (supra)* and held as under:

“A law cannot be held to be unreasonable merely because it operates retrospectively. Indeed even judicial decisions are in a sense retrospective. When a statute is interpreted by a court, the interpretation is, by fiction of law, deemed to be part of the statute from the date of its enactment. The unreasonableness must lie in some other additional factors. The retrospective operation of a fiscal statute would have to be found to be unduly oppressive and confiscatory before it can be held to be so unreasonable as to violate constitutional norms:

“Where for instance, it appears that the taxing statute is plainly discriminatory or provides no procedural machinery for assessment and levy of the tax, or that it is confiscatory, courts would be

justified in striking down the impugned statute as unconstitutional. In such cases, the character of the material provisions of the impugned statute is such that the court would feel justified in taking the view that, in substance, the taxing statute is a cloak adopted by the legislature for achieving its confiscatory purposes”. (Rai Ramkrishna v. State of Bihar: [1963] 50 ITR 171 (SC))”

29. In the case of *Lohia Machines Ltd.* (*supra*), Sen J delivering the dissenting opinion observed as under:

“The power and competence of the Parliament to amend any statutory provision with retrospective effect cannot be doubted. Any retrospective amendment to be valid must however be reasonable and not arbitrary and must not be violative of any of the fundamental rights guaranteed under the Constitution. The mere fact that any statutory provision has been amended with retrospective effect does not by itself make the amendment unreasonable. Unreasonableness or arbitrariness of any such amendment with retrospective effect has necessarily to be judged on the merits of the amendment in the light of the facts and circumstances under which such amendment is made. In considering the question as to whether the legislative power to amend a provision with retrospective operation has been reasonably exercised or not it becomes relevant to enquire as to how the retrospective effect of the amendment operates.”

The Gujarat High Court in *Niko Resources Limited v. Union of India*: (2015) 374 ITR 369 (Guj) reiterated the above view.

30. In *Shri Prithvi Cotton Mills Ltd. v. Broach Borough Municipality*: (1969) 2 SCC 283, the Supreme Court considered the challenge to the

validity of the Gujarat Imposition of Taxes by Municipalities (Validation) Act, 1963. The said enactment was impugned as being *ultra vires* Article 19(1)(f), 19(1)(g) and 265 of the Constitution of India. The said challenge arose in the context of rates imposed by Broach Borough Municipality (hereafter 'BBM') constituted under Section 8 of the Bombay Municipal Boroughs Act, 1925. BBM purporting to Act under Section 73 of the Bombay Municipal Boroughs Act, 1925 and the Rules made thereunder imposed rates on lands and buildings on the basis of percentage on the capital value of lands and buildings within the municipality. The levy of rates was challenged by way of writ petitions. While the petitions were so pending, the Gujarat Legislature enacted Gujarat Imposition of Taxes by Municipalities (Validation) Act, 1963 to validate the imposition of rates on open lands at one percent of the valuation based on the value of the property. It is presumed that the said validation Act was passed because the Supreme Court in ***Patel Gordhandas Hargovindas v. Municipal Commissioner, Ahmedabad: (1964) 2 S.C.R. 608*** had interpreted Section 73 of the Bombay Municipal Boroughs Act, 1925 as not contemplating levy of rates based on the capital value of the lands and buildings and accordingly had struck down Rule 350A - which provided for rate on land at a percentage of the capital value of the property - as *ultra vires* the Bombay Municipal Boroughs Act, 1925. In the aforesaid context, the

Supreme Court observed as under:-

“Before we examine Section 3 to find out whether it is effective in its purpose or not we may say a few words about validating statutes in general. When a legislature sets out to validate a tax declared by a court to be illegally collected under an ineffective or an invalid law, the cause for ineffectiveness or invalidity must be removed before validation can be said to take place effectively. The most important condition, of course, is that the legislature must possess the power to impose the tax, for, if it does not, the action must ever remain ineffective and illegal. Granted legislative competence, it is not sufficient to declare merely that the decision of the Court shall not bind for that is tantamount to reversing the decision in exercise of judicial power which the legislature does not possess or exercise. A court's decision must always bind unless the conditions on which it is based are so fundamentally altered that the decision could not have been given in the altered circumstances. Ordinarily, a court holds a tax to be invalidly imposed because the power to tax is wanting or the statute or the rules or both are invalid or do not sufficiently create the jurisdiction. Validation of a tax so declared illegal may be done only if the grounds of illegality or invalidity are capable of being removed and are in fact removed and the tax thus made legal. Sometimes this is done by providing for jurisdiction where jurisdiction had not been properly invested before. Sometimes this is done by re-enacting retrospectively a valid and legal taxing provision and then by fiction making the tax already collected to stand under the re-enacted law. Sometimes the legislature gives its own meaning and interpretation of the law under which the tax was collected and by legislative fiat makes the new meaning binding upon courts. The legislature may follow any one method or all of them and while it does so it may neutralise the effect at the earlier decision of the court which becomes ineffective after the change of the law. Whichever method is adopted it must be within the competence of the legislature and legal and adequate to attain the object of validation. If the legislature has the power over the subject-matter and

competence to make a valid law, it can at any time make such a valid law and make it retrospectively so as to bind even past transactions. The validity of a Validating law, therefore, depends upon whether the legislature possesses the competence which it claims over the subject-matter and whether in making the validation it removes the defect which the courts had found in the existing law and makes adequate provisions in the Validating law for a valid imposition of the tax.”

After observing as above, the Supreme Court rejected the challenge to the validity of Bombay Municipal Boroughs Act, 1925 in the following manner:-

“The legislature in Section 73 had not authorised the levy of a tax in this manner but had authorised the levy of a rate. That led to the discussion whether a rule putting the tax on capital value of buildings answered the description of the impost in the Act, namely, 'a rate on buildings or lands or both situate within the Municipal borough'. It was held by this Court it did not, because the word 'rate' had acquired a special meaning in legislative practice. Faced with this situation the legislature exercised its undoubted powers of redefining 'rate' so as to equate it to a tax on capital value and convert the tax purported to be collected as a 'rate' into a tax on lands and buildings. The legislature in the Validation Act, therefore, provided for the following matters. First, it stated that no tax or rate by whichever name called and laid on the capital value of lands and buildings must be deemed to be invalidly assessed, imposed, collected or recovered simply on the ground that a rate is based on the annual letting value. Next it provided that the tax must be deemed to be validly assessed, imposed, collected or recovered and imposition must be deemed to be always so authorised. The legislature by this enactment retrospectively imposed the tax on lands and buildings based on their capital value and as the tax was already imposed, levied and collected on that basis, made the

imposition, levy collection and recovery of the tax valid, notwithstanding the declaration by the Court that as 'rate', the levy was incompetent. The legislature not only equated the tax collected to a tax on lands and buildings, which it had the power to levy, but also to a rate giving a new meaning to the expression 'rate', and while doing so it put out of action the effect of the decisions of the courts to the contrary. The exercise of power by the legislature was valid because the legislature does possess the power to levy a tax on lands and buildings based on capital value thereof and in validating the levy on that basis, the implication of the use of the word 'rate' could be effectively removed and the tax on lands and buildings imposed instead. The tax, therefore, can no longer be questioned on the ground that Section 73 spoke of a rate and the imposition was not a rate as properly understood but a tax on capital value. In this view of the matter it is hardly necessary to invoke the 14th Clause of Section 73 which contains a residuary power to impose any other tax not expressly mentioned.”

The facts in the above case are in one sense materially similar to the facts in the present case as in the present case also, the Supreme Court had earlier held Rule 57F(4A) to be beyond the rule making power of the Central Government as conferred under Section 37 of the Act.

31. As pointed out earlier, by virtue of Section 131(b) of the Finance Act, 1999, the Parliament had cured the defect on account of which Rule 57F(4A) had been read down. There is no dispute as to the legislative competence of the Parliament to enact such law. The provisions of Section 132(1) (a) and Section 132(2) of the Finance Act, 1999 are only directed to sustain Rule 57F(4A) as originally enacted. Thus, in our view, the

challenge laid by the Petitioners insofar as the aspect of the retrospective operation of the impugned provisions to the extent that Rule 57F(4A) is validated, cannot be sustained.

32. This brings us to the second aspect of the challenge laid by the Petitioners, that is, whether Rule 57F(4A) is invalid as being violative of Article 14, 19(1)(f) and 19(1)(g), of the Constitution of India. According to the Petitioners, Rule 57F(4A) offends the rights guaranteed under Part III of the Constitution of India, as the said Rule is arbitrary and unreasonable. A plain reading of Rule 57F(4A) indicates that the operation of the said Rule is inherently retrospective inasmuch as its effect is to lapse MODVAT credit which has been accumulated by the Petitioners on account of payment of Excise Duty in respect of goods which have already been utilised for manufacture of finished goods that have been cleared. The import of Rule 57F(4A) was considered by the Supreme Court in *Eicher Motors* (*supra*) and it clearly held that Rule 57F(4A) affects the rights of manufacturers which had already accrued on account of their paying duties in accordance with the scheme. In the circumstances, any modification in the scheme would affect the past transactions. The Supreme Court had proceeded to hold that the facility of credit was as good as tax paid till the same was adjusted on future goods. In the aforesaid

view, the central issue to be addressed is whether Rule 57F(4A) in view of its inherently retrospective effect renders the same unconstitutional.

33. It is now well established that tax legislations - like any other legislation are not immune from being assailed on the ground of being unreasonable and offending Article 14, 19(1)(f) and 19(1)(g) of the Constitution. The Supreme Court in the case of *Tata Motors Ltd. v. State of Maharashtra: AIR 2004 SC 3618* had observed as under:-

“It is no doubt true that the State has enormous powers in the matter of legislation and in enacting fiscal laws. Great leverage is allowed in the matter of taxation laws because several fiscal adjustments have to be made by the Government depending upon the needs of the Revenue and the economic circumstances prevailing in the State. Even so an action taken by the State cannot be so irrational and arbitrary so as to introduce one set of rules for one period and another set of rules for another period by amending the laws in such a manner as to withdraw the benefit that had been given earlier resulting in higher burdens so far as the assessee is concerned without any reason. Retrospective withdrawal of the benefit of set-off only for a particular period should be justified on some tangible and rational ground, when challenged on the ground of unconstitutionality..... ”

34. Thus, while it is recognised that the powers of the State to levy tax and enact fiscal laws are wide, the laws framed cannot be so irrational as to fall foul of Article 14 or 19(1)(g) of the Constitution. Particularly, in cases such as the present one, where the benefit of the scheme on the basis of

which the Petitioners had already acted is sought to be withdrawn, the enactment has to be justified on some rational basis.

35. The learned counsel for the Petitioners strongly relied on dissenting opinion of Justice Sen, in *Lohia Machines (supra)*. In that case, the Supreme Court considered the challenge to a legislative amendment to Section 80J of the Income Tax Act, 1961. The majority opinion was that the amendment was only clarificatory and, therefore, was held to be valid. However, Justice Sen was of the view that the amendment was not clarificatory and the introduction of Sub section (1A) in Section 80J had the effect of retrospectively withdrawing the benefit granted under Section 80J in certain cases. As rightly pointed out by the learned counsel for the Petitioners, the observations made by Justice Sen in respect of retrospective amendment - although forming a part of his dissenting opinion - is, nonetheless, binding. This is so as the effect of a substantive amendment by virtue of which a benefit granted earlier is retrospectively withdrawn, was not considered in the majority opinion. Accordingly, this Court in *Whirlpool of India Limited and Anr. v. Union of India and Ors: (2013) 355 ITR 51 (Delhi)* as well as the Bombay High Court in *Commissioner of Income Tax v. Hico Products Pvt. Ltd.: (1991) 187 ITR 517 (Bom)* have followed Justice Sen's view in regard to the effect of

withdrawal of benefit with retrospective effect. In his dissenting opinion,

Justice Sen held as under:-

“The withdrawal with retrospective effect of any relief granted by a valid statutory provision to an assessee, depriving the assessee of the benefit of the relief vested in the assessee, stands on a footing entirely different from the footing which may necessitate the passing of a Validating Act seeking to validate any statutory provision declared unconstitutional. When Parliament passes an amendment validating any provision which might have been declared invalid for some defect or lacuna However, the withdrawal or modification with retrospective effect of the relief properly granted by the statute to an assessee which the assessee has lawfully enjoyed or is entitled to enjoy as his vested statutory right, depriving the assessee of the vested statutory right has the effect of imposing a levy with retrospective effect for the years for which there was no such levy and cannot, unless there be strong and exceptional circumstances justifying such withdrawal or modification, be held to be reasonable or in public interest.”

36. Retrospective statutory amendments made to cure certain defects and to validate a law held to be invalid or retrospective amendments which are clarificatory in nature, stand on a completely different footing. They are materially different in their nature from legislative amendments which introduce substantive changes with retrospective effect and thereby introduce a levy for the first time from an anterior date and the legislations which have the effect of withdrawing benefits granted and availed of in the

past. Such legislations would have to be justified on rational basis and in absence of good reasons, would be liable to be declared as falling foul of the Constitution of India. A similar view was expressed by the Calcutta High Court in *Shew Bhagwan Goenka v. Commercial Tax Officer.*: (1973) 32 STC 368 (Cal) wherein the Court after referring to the various decisions of the Supreme Court including *Rai Ramkrishna* (*supra*) observed as under:-

“Different considerations may arise where by an amendment with retrospective operation a fresh tax is sought to be levied.....

It is necessary, therefore, to enquire as to the circumstances under which the amendment in question was introduced.”

37. To summarise, the legal position as now well established is that a legislature has the power to enact laws both prospectively as well as retrospectively. In the case where the legislature enacts laws for curing defects to validate an earlier enacted invalid law, or to clarify an earlier legislation, the same would not be unconstitutional solely for the reason that the said laws have been enacted with retrospective effect. However, in cases where a law is enacted to impose a fresh levy with retrospective effect or to take away a benefit granted under an earlier law, the same is required to be justified on rational reasons.

38. The question whether an enactment is reasonable has to be considered in the context of the relevant statute and the purpose for which it has been enacted. As held by the Calcutta High Court in *Shew Bhagwan Goenka* (*supra*), no abstract standard or general pattern of reasonableness can be laid down as applicable to all cases.

39. In *State of Madras v. V.G. Row: AIR (1952) SC 196*, the Supreme Court observed as under:-

“The nature of the right alleged to have been infringed, the underlying purpose of the restrictions imposed, the extent and urgency of the evils sought to be remedied thereby, the disproportion of the imposition, the prevailing conditions at the time, should all enter into the judicial verdict”

40. If we now look into the surrounding circumstances and the context in which Rule 57F(4A) was initially made, it is clear that the same was a part of rationalizing the Excise Duty structure. It is important to note that the Excise Duty structure existing prior to 1996 had resulted in the manufacturer paying a higher rate of excise duty on inputs as compared to the finished products; the duties payable on inputs was ranging from 20 to 25% while that of the finished product was 10 to 15%. The aforesaid duty structure coupled with the fact that manufacturing of the LCVs did not result in sufficient value addition to absorb the duties payable on the

inputs, had resulted in accumulation of MODVAT Credit. Conceptually, the MODVAT scheme was introduced to prevent the cascading effect of tax. In other words, the object was that the finished product bears the duties as determined. This was sought to be implemented by providing credit for the duties paid on raw material/inputs used in manufacture of the finished product. This would ensure a certain and a determinative duty structure qua the final product. The duties paid on inputs were not available for discharge of Excise Duties on any other product other than the finished goods manufactured by use of the inputs in question. Although, it is not necessary that the duty paid on inputs in respect of which credit was claimed had to be used for discharging the duty on the very same finished product in respect of which the input was actually used; nonetheless, credit for discharge of the liability in respect of the finished goods was available only in respect of such goods that were manufactured using such inputs. Rule 57F(4) which provided that the credit of duty paid in respect of inputs be utilised was interpreted in a manner as not to require the same duty paid raw material to be used in the manufacture of final finished product in respect of which credit for the duty paid input was claimed. In that view, the MODVAT scheme as introduced worked on the principle that the duty paid inputs had a co-relation with the finished products even though such co-relation was not of a kind that required the

very same input to be used in the final product. It was clarified by the department in that sense that there was no one to one co-relation between duty paid on the inputs and the output. However, it was also clear that the duty paid on inputs was not available as a credit in respect of duties on any other excisable finished product. If this restriction was continued and the duty structure was not rationalised for higher duties (in absolute terms) then the duties paid on the inputs that resulted in the accumulated credit available with the Petitioners would remain as such and would be of no benefit to them (unless they changed their business model). Thus, although, the Petitioners had an accrued right in respect of duty paid by them, such right was limited and the Petitioners were not entitled to claim refund of such duties.

41. It is in the aforesaid context that the Central Government decided to rationalise the structure of excise duties and Rule 57F(4A) was an integral part of this rationalisation. One limb of the rationalisation was to reduce the duties paid on the finished product; this would ensure that the duties paid on inputs would be fully absorbed towards duties on the finished product. The second limb was to provide flexibility in use of the MODVAT credit available on account of payment of duties on raw material/input; such duties could now be used towards discharge of

finished products other than those in respect of which such raw material/inputs were used/intended to be used. The manufacturer was now no longer constrained to use this credit only towards the duties of the finished products manufactured by use of such inputs/raw material in respect of which the duty credit was available. The third limb was to start afresh and lapse the accumulated credit; Rule 57F(4) which provided for elapsing of credit was, thus, the third limb of this rationalisation. It is apparent that the Central Government did not want the accumulated credit to further reduce the collection of revenues.

42. It appears that in their wisdom, the Central Government sought to balance the rationalisation of duty structure and provide flexibility in the use of credit by lapsing the accumulated credit which was admittedly a product of the earlier duty structure.

43. Viewed from the aforesaid perspective, we are unable to hold that the making of Rule 57F(4A) was so irrational or unreasonable as to fall foul of the Constitution of India. As to how, a fiscal legislation is to be framed is not an area where any interference under Article 226 is warranted. Scope of judicial review in respect of fiscal legislation is limited to the extent of determining whether it is outside the legislative competence of the legislature to enact such legislation and/or whether such

enactment is so unreasonable and irrational so as to violate the rights guaranteed under the Constitution.

44. In the present case, we are unable to accept that the legislative policy in aid of which Rule 57F(4A) was made, is irrational or unreasonable. The fact that the Petitioners would have to bear additional burden can clearly not be a ground to challenge the legislative policy. In *J.K. Jute Mills Co. Ltd. v. The State of Uttar Pradesh: AIR 1961 SC 1534*, the Supreme Court had unequivocally held as under :

"And then it is argued that a sales tax being an indirect tax, the seller who pays that tax has the right to pass it on to the consumer, that a law which imposes a sales tax long after the sales had taken place deprives him of that right, that retrospective operation is, in consequence, an incident inconsistent with the true character of a sales tax law, and that the Validation Act is therefore not a law in respect of tax on the sale of goods, as recognised, and it is ultra vires entry 54. We see no force in this contention. It is no doubt true that a sales tax is, according to accepted notions, intended to be passed on to the buyer, and provisions authorising and regulating the collection of sales tax by the seller from the purchaser are a usual feature of sales tax legislation. But it is not an essential characteristics of a sales tax that the seller must have the right to pass it on to the consumer, nor is the power of the legislature to impose a tax on sales conditional on its making a provision for sellers to collect the tax from the purchasers. Whether a law should be enacted, imposing a sales tax, or validating the imposition of sales tax, when the seller is not in a position to pass it on to the consumer, is a matter of

policy and does not affect the competence of the legislature.”

Further, the Court also referred to the decision of *The Tata Iron & Steel Co., Ltd. v. The State of Bihar: (1958) 1 SCR 1355*.

45. The Supreme Court reiterated the aforesaid view in the case of *Krishnamurthi and Co. etc. v. State of Madras: (1973) 2 SCR 54*. In that case, Entry 47 of the First Schedule of the Madras General Sales Tax Act, 1959 was amended in 1964 to include all kinds of mineral oils including non-lubricant oils. An issue was raised as to whether furnace oil was included in the amended entry. The Madras High Court held that that was not included. In this context, the legislature passed an Act in 1967 which rectified the defect in the language of Entry 47 and also validated the past levy and collection of tax pursuant thereto. The Supreme Court upheld the validity of the amending and validating Act and held that for the purpose of making "small repairs", it was permissible for the legislature to enact a law with retrospective operation. The fact that levy of sales tax casts an additional burden on the dealers who could no longer pass the burden of retrospective tax to customers was held to be not consequential for the purposes of challenge to the legislative policy. In the present case too, the Petitioners and similarly placed manufacturers are mulcted with additional burden by virtue of Rule 57F(4A) of the Rules. However, that by itself

would not render the said Rule as unreasonable or arbitrary so as to fall foul of Article 14, 19(1)(f) and 19(1)(g) of the Constitution.

46. In the aforesaid view, the petitions are dismissed. The parties are left to bear their own costs.

VIBHU BAKHRU, J

S.MURALIDHAR, J

JULY 22, 2016
RK/MK

