

IN THE HIGH COURT OF JUDICATURE AT CALCUTTA

SPECIAL JURISDICTION (CENTRAL EXCISE)

ORIGINAL SIDE

RESERVED ON: 21.03.2023
DELIVERED ON: 31.03.2023

CORAM:

THE HON'BLE MR. ACTING CHIEF JUSTICE T.S. SIVAGNANAM

AND

THE HON'BLE MR. JUSTICE HIRANMAY BHATTACHARYYA

CEXA NO. 80 OF 2018

SATYAM IRON AND STEEL COMPANY PRIVATE LIMITED

VERSUS

THE COMMISSIONER, CENTRAL EXCISE AND SERVICE TAX - BOLPUR

Appearance:-

Mr. J.P Khaitan, Senior Advocate.

Mr. Ananda Sen, Advocate.

Ms. Anupa Banerjee, Advocate.

Mr. Dipak Dey, Advocate.

.....For the Appellant.

Mr. Vipul Kundalia, Senior Advocate.

Ms. Manasi Mukherjee, Advocate.

.....For the Respondent.

JUDGMENT

(Judgment of the Court was delivered by T.S.SIVAGNANAM, J.)

1. This appeal filed by the assessee under Section 35G of the Central Excise Act, 1944 (the Act) is directed against the order dated 25th January, 2018 passed by the Customs, Excise and Service Tax Appellate Tribunal, East Zonal Bench, Kolkata, (tribunal). The appeal was admitted on the following substantial questions of law:

- 1) Whether on the facts and in the circumstances of the case, the central excise duty can be demanded with reference to the installed capacity when the finished goods are not notified under Section 3A of the Central Excise Act, 1944 and there is no material to show any unrecorded manufacture or clearance of the finished goods?*
- 2) Whether on the facts and in the circumstances of the case the impugned order of the tribunal upholding the demand made on the above basis was perverse?*

2. We have heard Mr. J.P. Khaitan, learned Senior Advocate assisted by Mr. Ananda Sen, Ms. Anupa Banerjee and Mr. Dipak Dey appearing for the appellant and Mr. Vipul Kundalia, learned Senior Standing Counsel assisted by Ms. Manasi Mukherjee for the respondent department.

3. The appellant is engaged in the manufacture of excisable goods namely, sponge iron falling under Tariff Item No. 7203-1000 of the Central Excise Tariff Act, 1985 and holding Central Excise Registration since 2002. The basic raw material used in the manufacture of sponge iron, iron ore, coal, and iron ore palettes. The issue involved in this appeal is whether the appellant assessee manufactured and clandestinely cleared goods without payment of Central Excise duty. An audit was conducted during 2014 which ultimately led to the issuance of show-cause notices dated 20th August,

2014, 17th April, 2014 and 3rd February, 2016. It was stated that in the course of verification of ER-7 (Annual Installed Capacity Statement) filed in terms of Sub-Rule 2(A) of Rule 12 of the Central Excise Rules, 2002, it was found that the assessee's annual production capacity is 60,000 metric tonnes but the assessee as per the ER-1 returns during the period October 2009 to March 2014 has not reflected the production and clearance quantity as per their production capacity. It was alleged that the assessee has shown a substantial lesser quantity of production and clearance of the said goods than that of their installed capacity. After noting the relevant details, the assessee was called upon to clarify as to the deviation of the annual capacity of production and production reflected in their ER-1 returns. The assessee submitted their response stating that the production capacity of the plant is 60,000 metric tonnes annually (two kilns of 100 tonnes per day capacity). That during the period of dispute they operated only one kiln on an average and achieved production as reflected in the ER-1 returns and they were constrained to curtail the production due to non-availability of raw material, shut down of kiln for maintenance purposes, high cost of raw materials and increase of overall expenses and adverse market conditions and low demand of finished goods. The Commissioner, Central Excise and Service Tax, Bolpur (the adjudicating authority) did not accept the explanation given by the assessee and alleged that the assessee has suppressed the production and cleared goods clandestinely with an intent to evade payment of excise duty. Accordingly, the assessee was called upon to show cause as to why Central Excise Duty should not be demanded and recovered in terms of Section 11(A) of the Act; why interest at proper rate should not be charged

under Section 11AA of the Act and why penalty should not be imposed under Section 11AC of the Act. The show-cause notice also proposed as to why the extended period of limitation of 5 years under the proviso to Section 11 A(1) cannot be invoked. The assessee submitted their reply dated 28th December, 2014 along with copies of the statement of intimation addressed to the respondent department informing shut down of Kiln 1 and Kiln 2 during the period 2009-10 to 2013-14 along with the acknowledged copies of the letters/ intimation. Copies of the statement showing the due dates of filing each return and the date of filing such returns by the assessee were also furnished. The reply submitted by the assessee was divided under various sub-headings, the first with regard to submissions on facts, next dealing with the allegations of clandestine removal, the correctness of invoking the extended period of limitation, as to why the proposal for levy of penalty is arbitrary and without authority of law. The adjudicating authority by order dated 13th February, 2017 confirmed the proposal in the show-cause notices. Aggrieved by the same, the assessee preferred appeal before the Tribunal which has been dismissed by the impugned order.

4. The reason for issuing show-cause notice to the assessee was based on the quantity of production difference between the annual installed production capacity statement as declared in the ER-7 statement and the ER-1 return. The annual installed capacity of the assessee's unit is 60,000 metric tonnes which has been mentioned in the ER-7 statement.
5. The department alleged that the assessee suppressed their production by showing lesser production in the ER-1 return and removed the products clandestinely by intentionally evading the payment of Central Excise duty.

Before we examine the facts of the case and test the correctness of the order passed by the tribunal, it would be beneficial to take note of a few decisions as to how the allegation of clandestine production or removal has to be viewed and on whom does the burden lie to establish the case of clandestine production or removal. One of the earliest decisions of the Constitution Bench of the Hon'ble Supreme Court in the case of ***Oudh Sugar Mills Limited Versus Union of India***¹ would guide us as to how such matters have to be viewed and considered. In the said case, the appellant was manufacturing sugar from sugarcane. There was a report submitted that the quantity of sugar has been short accounted for on the basis of which the show cause notice was issued, which ultimately was adjudicated against the appellant therein and penalty was imposed. An appeal was preferred before the Central Board of Revenue which was dismissed after which leave was sought for from the Hon'ble Supreme Court to file appeal under Article 136 of the Constitution which was granted. It was contended by the appellant before the Hon'ble Supreme Court that the order of the Collector holding certain quantity of sugar were short accounted for and that the accounts had not been properly kept was based on assumptions for which there is no basis. It was further contended that the appellant therein cannot be held guilty of short accounting of sugar unless it is established that any part of the sugar manufactured in the factory has been removed from factory or there were some loopholes in the working of the factory which provide opportunities for clandestine removal of sugarcane. The only basis for the findings arrived at by the Collector was

¹ 1978 (2) ELT (J 172) (SC)

based on the calculations made by the Assistant Chemical Examiner which was challenged contenting that they were not based on factual data but on certain assumption. The Hon'ble Supreme Court examined the report of the Assistant Chemical Examiner and held that if any one of the assumptions, as assumed in the report, breaks down then the ultimate conclusion will have to be rejected as incorrect. It was further pointed out that it has to be borne in mind that human element is involved on certain stages of the operations such as time of commencement of the days working, rapidity or slowness in feeding cut sugarcane into the crusher and mills, accurately adding the same quantity of water in the crusher and mills etc. Thus, it was pointed out that the recovery of sugar must necessarily depend upon the performance, it cannot be assumed that even in an ordinary well run factory performance would be uniformly good or uniformly the same. Similarly, the value of the fibre percentage in the cane as mentioned in the report was also considered. Ultimately, it was held that the findings arrived at by the Collector that certain quantity of sugar were not accounted for by the appellant therein has been arrived at without any tangible evidence and is based only on inferences involving unwarranted assumptions and the findings is thus vitiated by error of law.

6. In ***Continental Cement Company Versus Union of India***², it was held that to prove clandestine removal, evidence is required on purchase of raw materials, use of extra electricity, sale of final products, clandestine removal, transportation, payment, realization of sale proceeds, modes and flow-back of funds etc. It being a serious charge, it is required to be proved

² 2014 (309) ELT 411 (All)

by the revenue by tangible and sufficient evidence and mere statements of buyer based on their memory was insufficient without support of any documentary evidence.

7. In ***Commissioner of Central Excise, Kolkata - III Versus Sai Sulphonate Private Limited***³, it was held that the onus to prove clandestine removal is on the department and in the absence of any material on record establishing the charge of clandestine removal and trying to establish the charge by way of inference taking note of the ratio as adopted in the manufacturing process cannot be made.
8. As could be seen from the show cause notices issued to the appellant, the allegation of clandestine removal is solely based upon the annual installed capacity of the unit of the assessee as mentioned in the ER-7 return compared with the ER-1 statements.
9. The appellant in their reply to the show-cause notice after mentioning about their installed capacity, specifically pointed out that they were audited by the Audit Wing of the Department for the year 2009-10, 2011-12 and 2012-13 and at no point of time any objection was raised as regards under-statement of production or alleged clandestine removal of Sponge Iron. Further, for the very same period, the appellant was audited by the CAG/CERA and nothing adverse was pointed out. Therefore, it was contended except for the year 2012-13 no objection of any under-statement of production was ever raised. It was pointed out that the audit objection for the year 2011-13 is made the basis of the demand as mentioned in the show-cause notice. Nextly, the appellant mentioned about the period during

³ 2022 (380) ELT 441 (Cal)

which the Kiln 1 and Kiln 2 were shut down during the years 2009-10 to 2013-14 and relevant details were mentioned in an tabulated format and also specifically mentioning that the department was intimated periodically about the shutdown of the Kiln and those intimations were duly acknowledged by the department. Further for the period from October, 2009 to March, 2014, the appellant had furnished the quantity of Sponge Iron which was produced from their factory and they had disclosed the same in their statutory returns along with installed capacity. Furthermore, the manufacture/ clearance of Sponge Iron and particulars of payment of central excise duty was disclosed by the appellant in the statutory return prescribed by the Rule 12 of the Central Excise Rules, 2004 read with Rule 9/ 9A of the Cenvat Credit Rules and those returns were accepted by the Department without any demur or objection. With regard to the ER-1 return, it was submitted that it is a monthly return prescribed under Rule 12 of the Central Excise Rules and Rule 9(7) of the Cenvat Credit Rules and the return is to be filed within the 10th day from the close of the month to which it relates. In the said returns, the particulars of all the monthly production, clearance of excisable goods, rate of duty, value of excisable goods cleared and duty payable and payment particulars of such duty in cash and from Cenvat Credit account and claim/utilization of Cenvat Credit were disclosed. It was further stated that ER-4 return is prescribed under Rule 12(2)(a) of the Central Excise Rules and it is an annual financial information statement wherein the assessee discloses the value of raw material and other inputs, quantity/ value of manufactured excisable goods and details of the direct/indirect expenses incurred by the assessee during

the year. Similarly, ER-5 returns is an annual return of information relating to principal inputs wherein the assessee discloses similar information on monthly basis as disclosed in ER-5 return on yearly basis. With regard to the ER-7 return, the assessee pointed out the same is as prescribed under Rule 12(2)(A) of the Central Excise Rules, 2002 and it is the annual installed capacity statement wherein an assessee is obliged to disclose the installed capacity of the factory. The assessee thereafter set out in detail about the audit conducted in the factory of the assessee on various dates. With regard to the audit para alleging that the assessee has either short-utilized their production capacity or has suppressed the production of Sponge Iron and cleared the same with the intent to evade the payment of duty, the assessee pointed out that the audit officers were not sure whether it is a case of short-utilization of production capacity or it is a case of clandestine removal which could have been ascertained in the investigation. Furthermore, the assessee pointed out that copy of the audit objection is never handed over to the noticee at any point of time. Further, based on the audit para, the Superintendent, Central Excise issued letter dated 30th December, 2013 without conducting any investigation and without collecting any adverse material against the assessee and pre-decided the matter and directed the assessee to clarify as to why they have suppressed the actual production in the ER-1 return and why they should not be directed to pay the duty on the clearance of 29320 MT of Sponge Iron. The assessee by their reply dated 6th January, 2014 contended that during the material period, the Kilns were shut down for 679 days and 661 days respectively and submitted the necessary details in support of such contention. In spite of having furnished

such material, without conducting any enquiry or investigation, show-cause notice was issued merely based upon the audit objection. The assessee pointed out that the show-cause notice is wholly without jurisdiction as no duty can be demanded on deemed production of Sponge Iron on the basis of annual installed capacity of the Kilns in respect of excisable goods not notified under Section 3A of the Act. Further, there was no adverse material against the appellant revealing any clandestine production or clearance of Sponge Iron without payment of duty. It was further pointed out that Section 3 of the Central Excise Act provides that levy of central excise duty on actual production/ manufacture of excisable goods irrespective of the annual capacity of production whereas Section 3A of the Act provides for levy of duty of deemed production of notified excisable goods determined on the basis of capacity of production of the factory irrespective of the actual quantity of excisable goods manufactured/ produced. After pointing out this distinction, the assessee stated that Sponge Iron manufactured by the assessee is not notified goods under Section 3A and hence, no duty thereon can be demanded on the basis of annual capacity of production/ installed capacity. With regard to the charge of clandestine removal, the assessee pointed out that it is a very serious charge and must be proved with tangible, cogent and affirmative evidence, however, in the case of the assessee the entire demand is based on an audit objection without conducting any investigation, or enquiry, nor having any evidence on record. Thus, in the absence of any enquiry it has to be held that the allegation of clandestine production and removal is based on assumption, presumption, hypothesis and speculation.

10. The assessee referred to various decisions of the courts and that of the tribunal for the proposition that the charge of clandestine removal being a serious charge, the department must prove the same with tangible evidence and the standard of proof in such cases absolute proof and not preponderance of probabilities as the charge is quasi-criminal in nature.
11. Nextly, the assessee submitted that the major part of the demand is barred by the normal period of limitation. It is submitted that the disputed period is from October 2009 to March 2014 whereas show cause notice issued on 28.08.2014 and hence the major part of the demand is barred by period of limitation under Section 11A(1) of the Central Excise Act, 1944. Further it was submitted that the entire facts which led to the issuance of the show cause notice were those facts which are well within the knowledge of department and culled out from the return filed by the assessee and there is absolutely no material to allege any suppression of facts and consequently the extended period of limitation of five years could not have been invoked in the assessee's case. To support such proposition several decisions of the Hon'ble Supreme Court were referred to. With regard to the levy of penalty, it was submitted that the assessee has not contravened any of the rules, they had paid duty on excisable goods in accordance with the Rule 4 and Rule 8 upon assessment of duty under Rule 6 and they have maintained the detailed stock account in accordance with Rule 10, they have filed all their statutory returns in terms of Rule 12 read with Rule 9/9A of the CCR and in the absence of any contravention, there can be no case of suppression of facts, willful mis-statement, fraud, collusion or contravention of any provisions of the Act/Rules with an intent to evade payment of duty and

therefore penalty cannot be imposed. With the above submissions, the assessee prayed for dropping the proceedings.

12. The Commissioner who adjudicated the show cause notices confirmed the demand by order dated 13.02.2017. The discussion and findings are from page 17 of the order. After setting out the facts, the adjudicating authority opines that the appellant has fully utilized the production capacity and produced 3,65,000 metric tons of sponge iron but intentionally showed lesser production in the ER-1 return. What is conspicuously missing as to how the adjudicating authority came to such a conclusion. The allegation is one of the suppression of the production and clandestine removal of excisable goods without payment of excisable duty. Therefore the burden of proof is on the department to establish that the charge of clandestine removal for which there should be cogent and relevant material to pen down the assessee on a charge of clandestine removal. In the instant case, we find there was no material which was available with the Commissioner to come to such a conclusion. As pointed out earlier, the genesis of the entire matter is the audit objection. There are two known ways of dealing with an audit objection. Firstly, the respondent department will examine the objection and answer the audit para by giving an explanation. In the event, the same is found to be not acceptable and the findings are reiterated, then the department will have to conduct an enquiry into the aspect and satisfy itself that there are materials to proceed against the assessee and then issue the show cause notice clearly disclosing the case the assessee has to meet. Unfortunately the observation made in the audit objection was taken by the department as gospel truth and without conducting any enquiry or

investigation as the authority straight away proceeded to issue the show cause notice. In fact, the reply given by the assessee to the Superintendent, Central Excise department at the first instance was not even taken note of and mechanically the show cause notice was issued. When the assessee carried the matter on appeal to the tribunal, they reiterated the contention which was raised by them in reply to the show cause notice. In paragraph 8 of the impugned order, the tribunal noticed very briefly the contention raised by the assessee and then proceeded to decide the case against the assessee in one paragraphs, paragraph 9. The conclusion arrived at by the learned tribunal is solely based upon the annual production capacity. In the preceding paragraph, we had elaborately set out the stand taken by the assessee in their reply to the show cause notice, the documents which were annexed along with the show cause notice, unfortunately neither the adjudicating authority nor the tribunal adverted into any of these facts. The learned tribunal failed to see that the charge of clandestine removal is very serious charge and to establish the same there should be cogent and relevant materials. The learned tribunal has also not gone to into the aspect as to whether the extended period of limitation could have been invoked. Admittedly, the audit objection was based upon the information culled out from the return filed by the assessee and therefore there can be no charge of suppression or willful mis-statement and consequently the extended period of limitation could not have been invoked. The learned tribunal did not take enough effort to examine the facts of the case which are very crucial in the case on hand qua the allegations set out in the show cause notice. Thus, we are fully convinced that the adjudicating authority as well as the learned

tribunal committed a serious error in not accepting the case of the assessee. We reiterate that the department has not been able to establish the charge of clandestine removal by any tangible or cogent evidence. The show cause notice was mechanically issued without conducting any enquiry solely based upon audit objection. The documents filed by the assessee along with their reply were ignored. That apart, major part of the demand made in the show cause notice is barred by normal period of limitation. For invoking extended period of limitation, the revenue ought to have established willful mis-statement or suppression on the part of the assessee which has not been brought on record. Thus, the extended period of limitation could not have been invoked as well as the penalty could not have been imposed since there is no charge of willful mis-statement or suppression made against the assessee. The entire show cause notice has been built up on theory of assumption and presumption solely based upon the installed capacity of the two kilns in the assessee's factory without noting the factual details placed by the assessee, more particularly the period during which the kilns were shut down and as to how the department was fully aware of the shut down as the intimation given by the assessee were all acknowledged by the department. That apart, in the earlier audit inspections which were conducted no adverse report was drawn against the assessee even though they had not adopted the very same process. Thus, we hold that the department has failed to discharge the onus cast upon him to prove the charge of clandestine removal.

13. In the result, the appeal is allowed and the order passed by the tribunal as well as the adjudicating authority are set aside and the substantial questions of law are answered in favour of the appellant assessee.

**(T.S. SIVAGNANAM
ACTING CHIEF JUSTICE)**

I Agree.

**(HIRANMAY BHATTACHARYYA
JUSTICE)**

(P.A.- PRAMITA/SACHIN)