

UNION OF INDIA AND OTHERS

v.

ATIC INDUSTRIES LIMITED

June 22, 1984

[P.N. BHAGWATI, R.S. PATHAK AND

AMARENDRA NATH SEN, JJ.]

Central Excise and Salt Act, 1944—Clause (c) of sub-section (4) of section 4 as it stood after its amendment by sec. 2 of the Central Act 22 of 1973—Constitutional validity of.

Central Excise and Salt Act, 1944—The words “related person” occurring in clause (c) of sub-section (4) of sec. 4 as it stood after its amendment by sec. 2 of the Central Act 22 of 1973—Definition and applicability of.

Bank Guarantee—Whether the High Court was right in directing the costs of furnishing bank guarantee to be paid by the Revenue to the assessee in cases where the demand for duty is quashed as unjustified.

The respondent—assessee, a limited company, was engaged in the business of manufacturing dyes. Its 50 per cent share capital was held by Atul Products Ltd. and the remaining 50 per cent by Imperial Chemical Industries Ltd. London which also had a subsidiary company fully owned by it, called Imperial Chemical Industries (India) Pvt. Ltd. The Imperial Chemical Industries (India) Pvt. Ltd. ceased to be a subsidiary company wholly owned by the Imperial Chemical Industries Ltd. London on 13th March 1978, since 60 per cent of the share capital of Imperial Chemical Industries (India) Pvt. Ltd. was offered to the public in pursuance of the policy of the Government of India requiring that not more than 40% of the share capital of an Indian company should be held by a foreign shareholder. Consequent upon this dilution of foreign shareholding, the name of Imperial Chemical Industries (India) Pvt. Ltd. was changed to Crescent Dyes and Chemicals Ltd.

The assessee at all material times sold the large bulk of dyes manufactured by it in wholesale to Atul Products Ltd. and Imperial Chemical Industries (India) Pvt. Limited which subsequently came to be known as Crescent Dyes and Chemicals Ltd. at a uniform price applicable alike to both these wholesale buyers and these wholesale buyers sold these dyes to dealers and consumers at a higher price which inter alia included the expenses incurred by

them as also their profit. The transactions between the assessee on the one hand and Atul Products Ltd. and Crescent Dyes and Chemicals Limited on the other were as principal to principal and the wholesale price charged by the assessee to Atul Products Ltd and Crescent Dyes and Chemicals Ltd. was the sole consideration for the sale and no extra-commercial considerations entered in the determination of such price.

The assessee went on clearing the dyes manufactured by it after payment of excise duty as per the price list submitted by it on the basis of the wholesale price charged to Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. as the same was approved by the Asst. Collector on 29th October, 1975. The Superintendent of Central Excise, however, issued a notice to the assessee on 31st July 1976 calling upon the assessee to show cause why the earlier decision approving the price list should not be reviewed and the differential duty worked out on the basis of selling price charged by Atul Products Ltd. and Crescent Dyes & Chemicals Ltd. should not be recovered w.e.f. 1st October, 1975 on the ground that the assessee on the one hand and Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. on the other were "related persons" and the assessable value of the dyes manufactured by the assessee was therefore liable to be calculated on the basis of the price at which Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. sold the Dyes to the dealers and the consumers. The assessee in its reply dated 31st August 1976 pointed out that the assessee on the one hand and Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. on the other were not "related persons" within the meaning of the definition of that term contained in clause (c) of sub-section (4) of section 4 of the amended Central Excise and Salt Act 1944. The Asstt. Collector was however not satisfied with the explanation offered by the assessee and viewed his earlier order of approval of the price list and confirmed the demand of differential duty which came to an aggregate amount of Rs 1, 17, 77, 737.65 with retrospective effect from 1st October, 1975 and directed the assessee to file a fresh price list on the basis of the selling price charged by Atul Products Ltd. and Crescent Dyes and Chemicals Ltd.

The assessee thereupon filed a writ petition in the High Court of Gujarat challenging the validity of the demand made by the Asstt. Collector on two grounds namely, (i) that the concept of "related person" occurring in clause (c) of sub-section (4) of section 4 of the amended Central Excise and Salt Act, 1944 was outside the legislative competence of Parliament under Art. 226 read with Entry 84 in the Union List and was therefore unconstitutional and void ; & (ii) that the assessee on the one hand and Atul Products Ltd. and Crescent Dyes & Chemicals Ltd. on the other were not "related persons" and the wholesale cash price charged by the assessee to Atul Products Ltd. and Crescent Dyes and Chemicals Ltd., and not the price at which the latter sold the dyes to the dealers or the consumers represented the true measure of the value of the dyes for the purpose of chargeability to excise duty. The High Court allowed the writ petition on these two grounds and also gave direction to the Revenue for paying the costs incurred by the assessee in

A connection with the bank guarantee furnished by it. Hence the appeal to this Court by certificate granted under Art. 132 and 133 (1) of the Constitution.

Allowing the appeal in part, the Court.

B HELD : (1) On a proper interpretation of the definition of "related person" in sub-section (4) (c) of sec. 4, the words "relative and a distributor of the assessee" do not refer to any distributor but they are limited only to a distributor who is a relative of the assessee within the meaning of the Companies Act, 1956. The definition of "related person" is not unduly wide and does not suffer from any constitutional infirmity. It is within the legislative competence of Parliament. The decision of the High Court holding that "the concept of related person occurring in amended section 4 is ultra vires the legislative competence of Parliament under Article 256 read with Entry 84 in the Union List and striking down clause (c) of sub-section (4) of sec. 4 as also the expression "the buyer is not a related person and" in clause (a) of sub-section (1) of sec. 4 and proviso (iii) to that clause must consequently be set aside and it must be held that these provisions are constitutionally valid. [937 E-H]

D *Union of India v. Bombay Tyres International Ltd.* [1984] 1 SCC 467 applied.

High Court judgment in Special Civil Appln. No. 119 of 1976 decided on 20 21 February 1979 reversed.

E (2) The first part of the definition of "related person" in clause (c) of sub-section (4) of sec. 4 defines 'related person' to mean "a person who is so associated with the assessee that they have interest directly or indirectly in the business of each other". It is not enough that the assessee has an interest, direct or indirect in the business of the person alleged to be a related person nor is it enough that the person alleged to be a related person has an interest, direct or indirect in the business of the assessee. To attract the applicability of the first part of the definition, the assessee and the person alleged to be a related person must have interest, direct or indirect in the business of each other. Each of them must have a direct or indirect interest in the business of the other. The quality and degree of interest which each has in the business of the other may be different; the interest of one in the business of the other may be direct while the interest of the latter in the business of the former may be indirect. That would not make any difference so long as each has got some interest, direct or indirect in the business of the other. [938 G—H; 939 A—B]

H (3) (i) In the present case Atul Products Ltd. has undoubtedly interest in the business of the assessee since it holds 50% of the share capital of the assessee and has interest as shareholder in the business carried on by the assessee. But, it cannot be said that the assessee, a Ltd. company, has any interest, direct or indirect in the business carried on by one of its shareholders,

namely Atul Products Ltd., even though the share-holding of such shareholder may be 50 per cent. Secondly, Atul Products Ltd. is a wholesale buyer of the dyes manufactured by the assessee but even then, since the transactions between them are as principal to principal, it is difficult to appreciate how the assessee could be said by virtue of that circumstance to have any interest, direct or indirect, in the business of Atul Products Ltd. The assessee is not concerned whether Atul Products Ltd. sells or does not sell the dyes purchased by it from the assessee nor is it concerned whether Atul Products Ltd. sells such dyes at a profit or at a loss. [939 C—F]

(ii) Perhaps the position in regard to Crescent Dyes and Chemicals Ltd. is much stronger than that in regard to Atul Products Ltd. Crescent Dyes and Chemicals Ltd. is not even a shareholder of the assessee and it has therefore no interest direct or indirect in the business of the assessee. Equally, the assessee has no interest, direct or indirect in the business of Crescent Dyes and Chemicals Ltd., which is just a wholesale dealer purchasing dyes from the assessee in wholesale on principal to principal basis. [939 G—H]

(iii) The first part of the definition of related persons in clause (c) of sub-section (4) of section 4 of the amended Act is therefore clearly not satisfied both in relations to Atul Products Ltd. as also in relation to Crescent Dyes and Chemicals Ltd. and neither of them can be said to be a "related person" vis-a-vis the assessee within the meaning of the definition of that term in clause (c) of sub-section (4) of sec. 4 of the amended Act. Therefore, the assessable value of the dyes manufactured by the assessee cannot be determined with reference to the selling price charged by Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. to their purchasers but must be determined on the basis of the wholesale cash price charged by the assessee to Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. The demand made by the Asstt. Collector for differential duty must therefore be held to be rightly quashed by the High Court. [940 D-F]

(4) The High Court was not right in giving direction to the Revenue to pay costs incurred by this assessee in connection with the bank guarantee furnished by the assessee. The bank guarantee was required to be furnished by the assessee as a condition of grant of interim stay of enforcement of the demand for differential duty and if it is ultimately found that the demand for differential duty was not justified, the bank guarantee would certainly have to be discharged. But, it is difficult to see how the costs of furnishing the bank guarantee could be directed to be paid by the Revenue to the assessee. This direction of the High Court which directs the revenue to pay to the assessee the costs in connection with the bank guarantee furnished by it in pursuance of the interim order of the High Court is set aside. [940 H ; 941 A—B]

A CIVIL APPELLATE JURISDICTION ; Civil Appeal No. 3260 of 1979

From the Judgment and Order dated the 22/23rd day of February, 1972 of the Gujarat High Court in Spl. Civil Appln. No. 52/77.

B *R.N. Poddar* for the Appellants.

N.A. Palkhivala, Atul Setalved, F.H.J. Talyar Khan, Ravindar Narain, Kamal Mehta, A. Manjra, T.M. Ansari and Miss Rainu Walia for the Respondents.

C The Judgment of of the Court was delivered by

D BHAGWATI, J. This appeal by certificate granted under Articles 132 and 133 (1) of the Constitution raises a short question relating to the applicability of the definition of "related person" contained in clause (c) of sub-section (4) of section 4 of the Central Excise and Salt Act, 1944 as it stood after its amendment by section 2 of Central Act 22 of 1973 which came into force with effect from 1st October, 1975. The facts giving rise to this appeal are few and may be briefly stated as follows :

E The assessee is a limited company engaged in the business of manufacturing dyes and it has its factory situate in Atul near Bulsar in the State of Gujarat. The share capital of the assessee is held by two limited companies ; Atul products Limited holds 50 per cent of the share capital while the remaining 50 per cent of the share capital is held by Imperial Chemical Industries Limited, London. The assessee at all material times sold the large bulk of dyes manufactured by it in wholesale to Atul products Limited and Imperial Chemical Industries (India) Private Limited at a uniform price applicable alike to both these wholesale buyers and these wholesale buyers in their turn sold the dyes purchased by them from the assessee to dealers as well as consumers. Now, until 13th March 1978, Imperial Chemical Industries (India) Private Limited was a subsidiary company wholly owned by Imperial Chemical Industries Limited, London. But, in pursuance of the policy of the Government of India requiring that not more than 40 per cent of the share capital of an Indian company should be held by a foreign share-holder, 60 per cent of the share capital of Imperial Chemical Industries (India) Private Limited was offered to the public, with

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the result that since 13th March, 1978 only 40 per cent of the share capital of Imperial Chemical Industries (India) Private Limited was held by Imperial Chemical Industries Limited, London and 60 per cent came to be held by Indian citizens and Imperial Chemical Industries (India) Private Limited ceased to be a subsidiary company wholly owned by the Imperial Chemical Industries Limited, London. Consequent upon this dilution of foreign share holding, the name of Imperial Chemical Industries (India) Private Limited was changed to Crescent Dyes and Chemicals Limited. Atul Products Limited and Crescent Dyes and Chemicals Limited continued to be the wholesale dealers of the dyes manufactured by the assessee throughout the relevant period with which we are concerned in this appeal. It was common ground between the parties that the transactions between the assessee on the one hand and Atul Products Limited and Crescent Dyes and Chemicals Limited on the other were as principal to principal and the wholesale price charged by the assessee to Atul Products Limited and Crescent Dyes and Chemicals Limited was the sole consideration for the sale and no extra-commercial considerations entered in the determination of such price. Atul Products Limited and Crescent Dyes and Chemicals Limited, of course, sold the dyes purchased by them from the assessee at a higher price which *inter alia* included the expenses incurred by them as also their profit.
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On 15th September, 1975 the assessee submitted a price list showing the assessable value of the dyes manufactured by it on the basis of the wholesale price charged by it to Atul Products Limited and Crescent Dyes and Chemicals Limited. The Superintendent of Central Excise demanded certain information from the assessee with a view to satisfying himself as regards the correctness of the price list submitted by the assessee and the requisite information was furnished by the assessee by its letter dated 23rd September, 1975. Thereafter correspondence ensued between the assessee on the one hand and the Superintendent of Central Excise on the other and ultimately on 29th October, 1975 the Assistant Collector of Central Excise approved the price list submitted by the assessee. The assessee thereafter went on clearing the dyes manufactured by it after payment of excise duty on the basis of the price list submitted by the assessee and approved by the Assistant Collector. Then again some further correspondence took place between the assessee and the Central Excise Authorities by which certain information demanded by the Central Excise Authorities
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A was supplied by the assessee. The Superintendent of Central Excise, however, issued a notice to the assessee on 31st July, 1976 calling upon the assessee to show cause why the earlier decision of the Assistant Collector approving the price list should not be reviewed on the ground that the assessee on the one hand and

B Atul Products Limited and Crescent Dyes and Chemicals Limited on the other were "related persons" and the assessable value of the dyes manufactured by the assessee was, therefore, liable to be calculated on the basis of the price at which Atul Products Limited and Crescent Dyes and Chemicals Limited sold the dyes to the

C dealers and the consumers. The assessee was required to show cause why the differential duty worked out on the basis of the selling price charged by Atul Products Limited and Crescent Dyes and Chemicals Limited should not be recovered from the assessee with effect from 1st October, 1975. The assessee in its reply dated 31st August 1976 raised several contentions in answer to the show

D cause notice and pointed out *inter alia* that the assessee on the one hand and Atul Products Limited and Crescent Dyes and Chemicals Limited on the other were not "related persons" within the meaning of the definition of that term contained in sub-clause (c) of sub-section (4) of section 4 of the amended Central Excise and Salt Act, 1944. The Assistant Collector was, however, not

E satisfied with the explanation offered by the assessee and he ultimately by an order dated 10th December, 1976 reviewed his earlier order of approval of the price list and confirmed the demand differential duty with retrospective effect from 1st October, 1975 and directed the assessee to file a fresh price list on the basis of the

F selling price charged by Atul Products Limited and Crescent Dyes and Chemicals Limited. The demand for differential duty computed by the Superintendent of Central Excise for the period from 1st October, 1975 to 31st December, 1976 came to an aggregate amount of Rs. 1,17,77,737.65. The assessee thereupon filed a writ petition in the High Court of Gujarat challenging the validity of the demand made

G by the Assistant Collector and in the meanwhile also preferred an appeal before the Appellate Collector. The Appellate Collector rejected the appeal of the assessee without examining the merits of the grounds raised by the assessee since he took the view that all these grounds would be decided in the writ petition pending before the High Court and no useful purpose would be served by his

H considering the self-same grounds.

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The assessee urged several grounds in support of the writ petition before the High Court but it is not necessary to refer to them in detail, because the High Court ultimately decided the writ petition in favour of the assessee only on two grounds and it will, therefore, be enough if we refer to those two grounds alone and consider whether the decision of the High Court is correct in so far as it decided those two grounds in favour of the assessee. The first ground was that the concept of "related person" occurring in clause (c) of sub-section (4) of section 4 of the amended Central Excise and Salt Act, 1944 was outside the legislative competence of Parliament under Article 246 read with Entry 84 in the Union List and was, therefore, unconstitutional and void. This ground found favour with the High Court in view of the earlier decision given by the same Bench on 20/21 February, 1979 in Special Civil Application No. 119 of 1976. But, this decision of the High Court striking down clause (c) of sub-section (4) of section 4 of the amended Act cannot stand in view of the decision of the Court in *Union of India v. Bombay Tyres International Limited*⁽¹⁾ where an identical challenge to the constitutional validity of the definition of the term "related person" was negatived by this Court. The definition of the term "related person" was read down and it was held by this Court that "On a proper interpretation of the definition of "related person" in sub-section (4) (c) of section 4 the words "relative and a distributor of the assessee" do not refer to any distributor but they are limited only to a distributor who is a relative of the assessee within the meaning of the Companies Act, 1956. So read, the definition of "related person" is not unduly wide and does not suffer from any constitutional infirmity. It is within the legislative competence of Parliament. The decision of the High Court holding that "the concept of related person occurring in amended section 4 is *ultra vires* the legislative competence of Parliament under Article 246 read with Entry 84 in the Union List" and striking down clause (c) of sub-section (4) of section 4 as also the expression "the buyer is not a related person and" in clause (a) of sub-section (1) of section 4 and proviso (iii) to that clause must consequently be set aside and it must be held that these provisions are constitutionally valid.

• The second ground on which the assessee assailed the validity of the demand made by the Assistant Collector for differential duty

[1] [1984] 1 S.C.C. 467.

A related to applicability of the definition of "related person" in clause
(c) of sub-section (4) of section 4 of the amended Act. The Assistant
Collector took the view that the assessee on the one hand and Atul
Products Limited and Crescent Dyes and Chemicals Limited on the
B other were related persons within the meaning of the first part of
the definition of the term "related person" and the assessable value
of the dyes manufactured by the assessee for the purpose of excise
duty was, therefore, liable to be determined with reference to the
price at which the dyes were ordinarily sold by Atul Products
Limited and Crescent Dyes and Chemicals Limited. This view
taken by the Assistant Collector was set aside by the High Court
C on the ground that the assessee on the one hand and Atul Products
Limited and Crescent Dyes and Chemicals Limited on the other
were not "related persons" and the wholesale cash price charged
by the assessee to Atul Products Limited and Crescent Dyes and
Chemicals Limited and not the price at which the latter sold the
dyes to the dealers or the consumers, represented the true measure
D of the value of the dyes for the purpose of chargeability to excise
duty. This conclusion reached by the High Court was assailed
before us by the learned Attorney General appearing on behalf of
the Revenue. He fairly conceded that the only part of the defi-
nition of "related person" in clause (c) of sub-section (4) o
section 4 on which he could rely was the first part which defines
E "related person" to mean "a person who is so associated with the
assessee that they have interest directly or indirectly in the business
of each other." The second part of the definition which adds an
inclusive clause was admittedly not applicable, because neither
Atul Products Limited nor Crescent Dyes and Chemicals Limited
was a holding company or a subsidiary company nor was either of
F them a relative of the assessee, so as to fall within the second part
of the definition. But we do not think that even the limited
contention urged by the learned Attorney General on behalf of
the Revenue based on the first part of the definition can succeed.
What the first part of the definition requires is that the person
G who is sought to be branded as a "related person" must be a
person who is so associated with the assessee that they have
interest, directly or indirectly, in the business of each other. It is
not enough that the assessee has an interest, direct, or indirect in the
business of the person alleged to be a related person nor is it enough
that the person alleged to be a related person has an interest, direct
H or indirect, in the business of the assessee. It is essential to attract the
applicability of the first part of the definition that the assessee
and the person alleged to be a related person must have interest,

direct or indirect, in the business of each other. Each of them must have a direct or indirect interest in the business of the other. The equality and degree of interest which each has in the business of the other may be different; the interest of one in the business of the other may be direct, while the interest of the latter in the business of the former may be indirect. That would not make any difference, so long as each has got some interest, direct or indirect, in the business of the other. Now, in the present case, Atul Products Limited has undoubtedly interest in the business of the assessee, since Atul Products Limited holds 50 per cent of the share capital of the assessee and has interest as shareholder in the business carried on by the assessee. But it is not possible to say that the assessee has any interest in the business of Atul Products Limited. There are two points of view from which the relationship between the assessee and Atul Products Limited may be considered. First, it may be noted that Atul Products Limited is a shareholder of the assessee to the extent of 50 per cent of the share capital. But we fail to see how it can be said that a limited company has any interest, direct or indirect, in the business carried on by one of its shareholders, even though the shareholding of such shareholder may be 50 per cent. Secondly, Atul Products Limited is a wholesale buyer of the dyes manufactured by the assessee but even then, since the transactions between them are principal to principal, it is difficult to appreciate how the assessee could be said by virtue of that circumstance to have any interest, direct or indirect, in the business of Atul Products Limited. Atul Products Limited buys dyes from the assessee in wholesale on principal to principal basis and then sells such dyes in the market. The assessee is not concerned whether Atul Products Limited sells or does not sell the dyes purchased by it from the assessee nor is it concerned whether Atul Products Limited sells such dyes at a loss. It is impossible to contend that the assessee has any direct or indirect interest in the business of a wholesale dealer who purchases dyes from it on principal to principal basis. The same position obtains in regard to Crescent Dyes and Chemicals Limited. Perhaps the position in regard to Crescent Dyes and Chemicals Limited is much stronger than that in regard to Atul Products Limited. Crescent Dyes and Chemicals Limited is not even a shareholder of the assessee and it has, therefore, no interest direct or indirect in the business of the assessee. It is Imperial Chemical Industries Limited, London which holds 50 per cent of the share capital of the assessee and this foreign company also holds 40 per cent of the share capital of

A Crescent Chemicals and Dyes Limited. Imperial Chemical Industries Limited, London would admittedly have an interest in the business of the assessee in its capacity as a shareholder, but how
B can Crescent Dyes and Chemicals Limited of which 40 per cent of the shares are held by Imperial Chemical Industries Limited, London which in its turn is a shareholder of the assessee, can not be
C said to have any interest, direct or indirect, in the business of the assessee. Equally the assessee has no interest direct or indirect in the business of Crescent Dyes and Chemicals Limited, which is just
D a wholesale dealer purchasing dyes from the assessee in wholesale on principal to principal basis. It is obvious that for the same reasons which have prevailed with us while discussing the case of Atul Products Limited, the assessee has no direct or indirect interest in the business of Crescent Dyes and Chemicals Limited. The first part of the definition of related person in clause (c) of sub-section (4) of section 4 of the amended Act is, therefore, clearly not satisfied both in relation to Atul Products Limited as also in relation to Crescent Dyes and Chemicals Limited and neither of them can be said to be a "related person" vis-a-vis the assessee within the meaning of the definition of that term in clause (c) of sub-section (4) of section 4 of the amended Act. We, therefore, affirm the view taken by the High Court and hold that the assessable value of the dyes manufactured by the assessee cannot be determined with reference to the selling price charged by Atul Products Limited and Crescent Dyes and Chemicals Limited to their purchasers but must be determined on the basis of the wholesable cash price charged by the assessee to Atul Products Limited and Crescent Dyes and Chemicals Limited. The demand made by the Assistant Collector for differential duty must, therefore, be held to be rightly quashed by the High Court.

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H But there is one small matter on which the High Court has, in our view, erred in giving direction and it is in regard to payment of the costs incurred by the assessee in connection with the bank guarantee furnished by it in pursuance of the interim order made by the High Court. We do not think the High Court was right in giving this direction. The bank guarantee was required to be furnished by the assessee as a condition of grant of interim stay of enforcement of the demand for differential duty and if it is ultimately found that the demand for differential duty was not

justified, the bank guarantee would certainly have to be discharged, but it is difficult to see how the costs of furnishing the bank guarantee could be directed to be paid by the Revenue to the assessee. We would, therefore, set aside that part of the order made by the High Court which directs the Revenue to pay to the assessee the costs incurred in connection with the bank guarantee furnished by it in pursuance of the interim order of the High Court.

The appeal, therefore, fails except in regard to the direction for payment of costs of the bank guarantee. The Revenue will pay the costs of the appeal to the assessee.

S.R.

Appeal dismissed