Is Machino no more machismo?

By S Jaikumar & G Natarajan, Advocates

IF Mr Big B were to ask the final question of his famous *Kaun Banega Crorepati* on Central Excise, we feel the appropriate question may be,

Which is the most relied judgement in the history of Central Excise?

And the options would be:

- Delhi Cloth Mills - defining the concept of manufacture
- Ujagar Prints - defining job-work valuation
- Sri Chakra Tyres - prescribing cum-duty benefit or
- Machino Montell - waiving interest and penalties.

If liberalization is the most teasing misnomer, era of trust is the most prevalent hypocrisy in the tax world! We all have witnessed the deadliest penal clauses and draconian recovery measures being introduced into the tax laws, in this so-called era of liberalization and trust! There is a school of thought that freedom should be with discipline and hence this trust regime has inherited such penal and recovery provisions! But what we are really worried about is the utter indiscretion which has crept into the tax administration and quasi adjudication! We have already commented that "Self-assessment" under Central Excise is nothing but a **curse in disguise** ! After the introduction of this scheme, the nation witnessed a waterfall of allegations, right, left and centre, invoking the lethal larger period of limitation in all cases, just because of the reason that, the invoices are not given to the Department! In other words, this self-assessment scheme is often used as an ugly mask to camouflage the inefficiency of the department.

The Larger Bench of the Tribunal in the sensational case of CCE, Delhi III vs M/s Machino Montell (India) Pvt. Ltd (2004-TIOL-423-CESTAT-DEL-LB) came as an oasis to the Sahara-stricken trade, wherein it had been held that, there shall be a waiver of penalty and interest under Sections 11AC and 11AB of the Central Excise Act, 1944 (CEA), if the duty amount is paid before the issuance of the show cause notice! No doubt, in the tax world the ruling was bloom to some and gloom to some! In the case of **AL-FALAH (EXPORTS) Vs COMMISSIONER OF CCENTRAL EXCISE, SURAT I** (2006-TIOL-519-CESTAT-MUM-LB) the above ratio which was given under the Central Excise Act was made good for the provisions of the Customs Act also, considering the *pari-materia*. Even though all the Benches of the Tribunals followed the above said ratio and set aside the penalties in all cases where the duty amount has been paid before the issuance of show cause notice, the essence of this judgement has started percolating into the minds of the pro-revenue brigades only now that very recently the quasi-judiciary have started extending the benefit of this ratio in the original/appellate stages. And now comes the judgement of the High Court of Punjab and Haryana in the case of CCE, Delhi III vs M/s Machino Montell (India) Pvt. Ltd (2006-TIOL-276-HC-P&H-CX) . Does it topple the apple cart? Let us delve a bit deep!

In the present judgement, the High court has observed that after a perusal of the provisions of Section 11AC of the CEA, it shows that the said provision incorporates liability to pay penalty in the situations mentioned therein. It has also observed that once a case is covered by the situation mentioned in the Section, mere deposit prior to issuance of show cause notice under Section 11 A of the Act will not necessarily negate the situation mentioned in the said Section. The High Court has thus concluded that the applicability of Section 11 AC is not excluded at the threshold merely on deposit of the amount after having been caught and before the issue of show cause notice. The High Court has thus remanded the matter to the Appellate Commissioner for denovo consideration.

In this present case before the High Court, the learned counsel for the respondents, namely, M/s Machino Montell has referred to Sub-Section 2B of Section 11 A of the Act, wherein, the statute itself has provided a situation, that on deposit being made, the assessee will not be served notice under Section 11 A (1) of the Act. But the High Court has not gone into this question in view of Sub-Section 2C of Section 11 A of the Act, whereby, the said Sub-Section 2B is not applicable to cases where the duty has become payable prior to the date on which Finance Bill, 2001 was passed and as the present case pertains to a period prior to the same.

Thus the applicability of the ratio of this present High Court judgement to the cases pertaining to a period subsequent to the date of passing of Finance Bill, 2001 has to be seen afresh. We feel that there cannot be much substance in bringing Sub-Section 2B for rescue from levy of penalty under Section 11AC of CEA, as by virtue of the Explanation 1 appended thereto, the provisions of the said Sub-Section has been made inapplicable to the cases involving fraud, collusion, willful mis-statement and suppression of facts.

We feel that, in this present case before the High Court the following points have not been put forth, namely,

- The larger bench decision of the Tribunal in this impugned case is following the decision in the case of M/s Rashtria Ispat Nigam Limited vs CCE, Vishakapatinam (2002-TIOL-116-CESTAT-BANG), wherein, it was held that there shall be no imposition of penalty either under Section 11AC of CEA or under Rule 173Q of the Central Excise Rules, if the duty is paid before the issuance of show cause notice, which was affirmed by the Apex Court **{2004 (163) E.L.T. A53 (S.C.)}** .

- Secondly, there is a reference to the decision of the Tribunal in the case of JKON Engineering in this case. But the judgement of the High Court of Madras in the case of CCE, Madras vs JKON Engineering (P) Ltd, as reported in (2005-TIOL-155-HC-MAD-CX), wherein, the High Court of Madras has dismissed the petition of the department filed under Section 35(H)(1) of CEA following the ratio of M/s Rashtria Ispat Nigam Limited vs CCE, Vishakapatinam *supra* and upholding that there shall be a waiver of penalty under Section 11AC even if the duty amount is paid before the adjudication, has unfortunately not been put forth.

- Further in the case of CCE, Madras v. Jkon Engineering (P) Ltd. (2005-TIOL-155-HC-MAD-CX)**,** the High Court of Madras has held that penalty under Section 11AC of the Act can be waived if the duty is paid before the conclusion of the adjudication proceedings, i.e., before the passing of the Order-in-Original. When the High Court of Madras has been benevolent in waiving the penalty before adjudication itself,

waiving it in cases, where the duty amount is paid before the issuance of show cause notice is thoroughly justified.

- Last but not the least; if the duty is paid within 30 days from the date of receipt of the Order-in-Original, the penalty is **automatically** reduced to 25%, as per the proviso to Section 11AC of CEA. If so, is it so unreasonable or insensible to grant a waiver of penalty if the duty is paid before the show cause notice. After all, penalty is not a source of revenue for the Government! Also refer to our article titled as **CODE OF HAMMURABI!**

Before Parting...

In this case, though the larger bench of the Tribunal had given waiver of both penalty and interest under Sections 11AC and 11AB of CEA, the present judgement has dealt only with the penalty under Section 11AC of CEA. In respect of the interest under Section 11AB of CEA, the High Court has observed that the Tribunal shall take a fresh decision on the question as to the liability of payment of interest (It is also surprising as to why the case has been remanded to the Commissioner (Appeals) in respect of penalty and to the Tribunal in respect of interest!). A perusal of the judgement in the case of M/s Rashtriya Ispat Nigam Limited *supra* (which is the basis of the larger bench decision in this impugned case) would reveal that, the ruling is for the waiver of both interest and penalties, which had been subsequently affirmed by the Supreme Court!

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Sub: Machino is still machismo

Jai & Nuts,

First things first - your photograph is very impressive.

When the Hon'ble P & H High Court has not considered the decisions of Apex Court and Madras High Court affirming the Rashtriya Ispat decision, then this latest judgment from P & H High Court is "per incuriam" and may not hold fort on this subject.

Its very true that Government should not look at penalty or interest as a source of revenue. But unfortunately officers who work for the Government litigate on these very issues and the current topic of this article is the best example. This fact can be verified with a quick check of the statistics on the number of cases with appellate authorities on penalty and interest.

Moreover interest and penalty are the two pet themes of every officer working in Range, Audit and Intelligence. Whenever they make a spot recovery of any duty the next thing on their mind is interest which comes to their mouth as a natural 'reflex' action. The natural corollary is a SCN appropriating this duty and interest and imposition of penalty.

Its habitual and as we all know habits die hard. There is a proverb in Kannada which when translated reads as follows: "That which has come by birth does not even go when the funeral pyre is lit". (Huttu guna suttru hogolla). That's the fate of this Department.

Regards
Santosh Hatwar

Posted by **sbhatwar** Post Reply

Sub: Machino Montell looses charm

Sir,

One should agree that the photograph is indeed attractive, a good portfolio session done.

Comming to the main issue. Cases have already been reviewed based on the P&H High Court Decision and appeals have been filed.

The main question is even after the introduction of 100% penal provisions it is still not working as a detterant. The attitude is to keep doing the wrong thing and draw the benefits, if you are caught just pay the entire amount along with interest and go scott free. Is penalty not justified in such cases?

As regards self assessement i would like to submit that it was the demand from the trade that there should be self assessement as prevelent in Direct Tax and Sales Tax laws which the government has extended.

Saptharishi.

Posted by **saptharishi_iyer** Post Reply

Sub: No final word yet

It appears that no final word has been pronounced yet on the issue of waiver of penalty when duty is paid before issue of demand notice. Though the pertinent provision in Central Excise Act viz., Section 11AC relates to certain situations which can be broadly covered under the head 'evasion with intent', the distinction between normal cases and evasion cases seems to have not yet been made. In normal cases involving interpretation and attendant issues and where the dispute period is within normal period of limitition, the question of absolving the offending or potentially offending parties from penal liability may look reasonable and justified. But,where the attempt to evade is unearthed by the dept., and where the party comes forward to meet the liability not voluntarily but after such detection and when the threat of penal and interest liabilities stare at him, the question of waiver of penalty poses a grave question. If on detection by Dept., every (utopian as trade is mostly known to brow-beat the Revenue with battery of best legal brains in all the corridors of judiciary) assessee pays up the duty, and if all such cases are covered by such interpretative amnesty from penalty, then whey retain Section 11AC in the statute book? What purpose is it intended to serve then? Just because the Dept is highly inept in handling its cases and just because it invokes all the rules in the book at the drop of the hat, does it stand to reason to expect that tax frauds deserve positive diffential treatment? The issue needs to be looked by a Constitution Bench of the Supreme Court which can take a balanced and holistic view of the situation. While the Revenue can be blamed for thoughtless invocation of extended time period alleging suppression of facts even for subsequent period notices and quoting all relevant and non-relevant clauses of all relevant and non-relevant provisions to somehow net the offender, the trade in India has not conducted itself any better by which it can instill trust and confidence in itself. Tax evasion is a crime and when attempt to murder is punishable and preparation to smuggle contraband is punishable, so also should preparation to acts of evasion be. But point to the lack of discretion before, during and after initiation of proceedings - that merits consideration. And in the ultimate analysis, as my colleague has said, the we are discussing much about a decision which will shortly be consigned to history. Anyway, thanks to the great authors who provoke and get themselves provoked.

Posted by **GOKULKISHORE** Post Reply

Sub: Judicial discipline and the macho order

Dear JK / Nuts
Let me first congratulate you guys for this silver quick researched piece on the latest judgment !!! It just could not have got faster than this one (if the bench mark is based on the date of publishing of this judgment in a tax portal/ publication is taken)– especially in light of the quality of analysis provided. The importance of this judgment is best epitomized in your Big 'B' question. Needless to add, this judgment will be among those which will be fodder of revenue officers to continue the spate of unending litigations – may be add fuel to fire.

Few questions which however come to mind - If memory serves me right, The LB decision in Machino Montell was influenced by the Karnataka High Court decision in Shree Krishna

Pipe Industries which infact discussed the Apex Court dismissal of Revenue Appeal in Rashtriya Ispat Nigam Ltd. The said judgment had also referred to the Apex Court decision in the famous Nagarkar case to say that levy of penalty is mandatory. But the Larger Bench without attempting to differentiate or rather put in perspective why this Apex Court judgment would not apply in the said situation proceeded to rely upon the High Court decision and as you have put it, the decision of dismissal of Revenue Appeal. Will a judgment of such far reaching implications be fair if it only refers to an argument put forth (by any side for that matter) but does not discuss / counter or negate it ? It could have been understood if this case law was not placed before the Hon'ble Bench but it was and at best remained as referred. (I hope on the factual front I am not caught napping)

Another issue which remains unaddressed is whether the duty was paid voluntarily (before the issue was detected by the Department) or after the same was brought to the notice of the assessee. I say so because, the Tribunal in Surie Engg Works has addressed this issue and opined that the concept "penalty under Rule 173Q and Section 11AC would not be leviable when duty amount had been voluntarily paid before issue of SCN," is not attracted in such cases. The same view was propounded in Seiko Plast. Admittedly this is only one school of thought but if a debate rages on the acceptability of the judgment of Machino Montell, I think this judgment and the rationale behind it will have to be atleast taken note off. With due respect to the views of my dear friend (Santosh) above, simply stating that no penalty should be levied does bring rise to the larger question - Would such a judgment render the very provisions of Section 11AC redundant and non-operational?

I also recollect the judgment of Gujarat Travancore Agency (which I used to liberally quote while in Review Section) wherein the Hon'ble Apex Court held that -default in complying with the statute is sufficient for levy of penalty.

I am of the view the each judgment should be strictly an outcome of facts and circumstances of the concerned case and applying such rationale for deciding the levy of penalty in other cases should be after a thorough appreciation and analysis of the case laws relied upon. Apex Court in Sony India preferred not to interfere with the mandatory nature of penalty under Section 11AC and interest under Section 11AB. Though binding precedent is a legally accepted theory, if the same are so variedly and ambiguously used without strict compliance in the judicial sense inasmuch as it peters down to a matter of convenience, then revenue or for that matter the assessee will always pounce on the loop holes of such judgments. It in this context that I would appreciate that the powerful combo of you guys would crisply, analytically and quickly bring out deficiencies, such as in the present one, of even those cases which are pro-trade!!! May I add, it will be appreciated as your continued contribution to the field of taxation.

Posted by **nairsk**

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Dear Nuts and jai, With due respect for your deep analysis of the issue, I would just like to point out that a lot of confusion over the provisions of Section !!AB & 11AC. When 11AB was introduced along with Sec11AC, it was sort of penal interest as distingusihed from Interest on delayed payment under Section 11AA. The law

stipulated that no Courts / Appellate Authority have the powers to reduce the penalty or interest. But the only forum where penalties can get waived totally was Settlement commission by virtue of the provisions therein. But even Settlement Commn imposes interest at lesser rates though having powers to waive the interest fully.As the Tribunals started taking an active part in mitigating the penal liablities of the liablities of assessees with nil duty libality, the litigation is on. However, with the amendment of Section 11AB itis not clear as to how the assessees as well as legal fraternity wants waiver of interest even theough ther is a delayed payment of duty on the part of the assessee. This defies logic . But law knows no logic but we keep on fighitng over the issue.
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