

THE TWILIGHT ZONE

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*"When twilight drops her curtain down and pins it with a star,
remember that you have a **friend** though he may wander far."*

- Lucy Maud Montgomery

Statistics reveal that, this summer, the ratio between the honeymoon couples to that of the industrialists, who have visited Shimla, is 1:100. Same is the ratio between the pilgrims to that of the industrialists at Haridwar. And the reason for this surge of industrialists' invasion into the erstwhile tourist/pilgrim attracting States of Himachal and Uttranchal, could well be the two luring excise exemption notifications, which exempt the units located in certain specified areas. The two ONIDA notifications (*Neighbours' envy; Owners pride!*) are Notifications 49/2003 and 50/2003 dated 10/6/2003. In this piece let us analyse, as to whether it would be a hassle-free honeymoon, for the swarm of industrialists, rushing to those places with their multi-crore investments?

As on date, there are five major area-based Excise exemption notifications in India. They are for the seven-sisters of the North-East, JK, Kutch, Himachal and Uttranchal. Out of them, the exemption given to the units at the NE, JK and the Kutch are more beneficial than those of the Himachal/ Uttranchal. It is because of the reason that, whereas the goods manufactured in the specified areas of Himachal/Uttranchal are only exempted from payment of Excise duty leviable on the final products, the goods manufactured and cleared by the units in NE/JK/Kutch are both exempted from payment of Excise duty on the one hand and the buyer of such exempted goods can also avail the benefit of CENVAT credit of the duty paid (not paid!) on such goods, on the other hand! This double benefit makes the NE/JK/Kutch notifications more lucrative than the Himachal/Uttranchal notifications. But, despite this double-edge advantage, the patronage to the NE/JK/Kutch is lukewarm compared to that of the Himachal/Uttranchal, because of the terrestrial (maybe terrorist) hazards!

Coming to the Himachal/Uttranchal notifications, as per notification 49/2003, only certain specified goods are exempted from payment of Excise duty, which are manufactured from a unit located in the States of either Himachal or Uttranchal. As per Notification 50/2003, all goods except a few notified goods are exempted from payment of Excise duty, if manufactured from the units located in certain notified areas of those two States. But in both the notifications, the exemption are limited only to a period of ten years from the date of publication of these notifications (i.e from 10/6/2003) or from the date of commencement of commercial production, whichever is later. Further, in both the notifications, the exemption is available only to the units, which satisfy the following conditions, namely;

1. New industrial units, which have commenced their commercial production on or after the 7th day of January, 2003;
2. Industrial units existing before the 7th day of January 2003, but which have undertaken substantial expansion by way of increase in installed capacity by not less than twenty five per cent, on or after the 7th day of January 2003.

Prima facie, both the above conditions appear to be simple and straight. There appears to be no dispute in respect of either the new industrial units or the existing units, which have undertaken substantial expansion, as per the relevant norms. It is also amply clear that, in respect of both the new units as well as the substantially expanded units, the only condition to be satisfied is that the commencement of the commercial production of such units shall be between 7/1/2003 and 31/3/2007. But there are few interesting corollaries, which are the feedstock of this article.

1. If a unit, which has duly satisfied all the above conditions before the notified date and has started enjoying the benefit of the exemption, opts to increase the production capacity after the notified date of 31/3/2007, will the benefit of the exemption be extended to such expanded capacity also?

Illustratively, say the existing production capacity of a unit is 100 tonnes per shift. Let the manufacturer invests on automated machinery replacing the manual machinery, by which, the production capacity is increased to 200 tonnes per shift and let this automation happens on a date after 31/3/2007. Now the question is as to whether the excess production of 100 tonnes on account of modernisation/automation of machinery, which has been installed after 31/3/2007, is eligible for the exemption?

2. If a unit, which has duly satisfied all the above conditions before the notified date and has started enjoying the benefit of the exemption, opts to introduce a new manufacturing/production line to its existing unit, will the benefit of the exemption be extended to such new manufacturing/production line also?

Illustratively, say the existing production capacity of a unit is 100 tonnes per shift. Let the manufacturer invests on a separate set of machinery, thereby, introduce a separate production line, by which, the production capacity is increased to 200 tonnes per shift and this introduction of new production line happens on a date after 31/3/2007. Now the question is as to whether the excess production of 100 tonnes on account of the introduction of a separate production line, which has been installed after 31/3/2007, is eligible for the exemption?

3. If a unit, which has duly satisfied all the above conditions before the notified date and has started enjoying the benefit of the exemption, opts to introduce a new product after 31/3/2007, will the benefit of the exemption be extended to such new product also?

Illustratively, say a unit is manufacturing a product X. After 31/3/2007, the unit starts manufacturing a new product Y. This new product is manufactured either on account of new machinery or on account of the existing machinery. Now the question is as to whether the new product Y, which is manufactured after 31/3/2007, is eligible for the exemption?

Let us deal the situations *in seriatim*;

Situation 1. On a plain reading of the notification, it is clear that the exemption is for the industrial units, either new or substantially expanded, which have satisfied the condition laid down in the respective notifications. Once an industrial unit duly satisfy the said conditions and qualify for the said exemption, then the same cannot be restricted or altered subsequently. As long as the goods manufactured by that

unit is specified in the notification, the exemption is for all such specified goods manufactured by that industrial unit, for a period of ten years, either from the date of the notification or from the date of the commencement of commercial production, whichever is later. The increase in production may be on account of variety of attributes, namely, automation/modernisation of the existing machinery or by way of adopting prudent manufacturing practices or by improving the labour efficiency or by way of increasing the number of shifts, etc. These material factors can neither influence nor alter the entitlement of the benefit of the exemption to the unit. In other words, once the unit qualifies for the exemption, then any increase in the capacity, by whatever means, shall not deprive or curtail the benefit of the notification. Thus, in Situation 1 above, the benefit of the exemption shall be available for the additional production of 100 tonnes also.

Situation 2. Here the situation is slightly different. Whereas, in the above situation, the increase in production capacity is in the same production line, in this case, the increase is due to an addition of an extra production line. In other words, in the earlier case there will be a replacement of the existing machinery by automated/new machinery, whereas, in the instant case, there will be an addition of new machinery along with retention of the old machinery. Now the department may contemplate that, this new production line is a new unit, *per se*, and shall not be eligible for the exemption, as the same is installed after the deadline date, i.e 31/3/2007. For the reasons stated above, we are of the opinion that, the benefit of the exemption shall be available even in the cases of introduction of a new production line after 31/3/2007, as long as, the new production line is within the existing industrial unit. In other words, the new production line, by no stretch of imagination, can be construed as a separate industrial unit!

Situation 3. Here the situation is two-fold, namely, the unit manufactures a) similar goods but of different specifications/brands of the same category and b) dissimilar goods of different category. For example, a manufacturer of medicines, who is initially manufacturing pain killer tablets till 31/3/2007, can manufacture cough syrups after 31/3/2007. But both of them are classified as P or P medicaments under chapter heading 30 of the Central Excise Tariff, 2005 and are eligible goods for the exemption. In the second case, a manufacturer who manufacture iron castings falling under Chapter heading 73 prior to 31/3/2007, can start manufacturing aluminium castings after 31/3/2007, which fall under Chapter heading 76 of CETA,2005. Now the moot question is as to the eligibility of the exemption to the manufacturer in respect of the Cough syrups and the Aluminum castings, manufactured after 31/3/2007? Again for the reasons explained above, we are of the firm opinion that, the exemption shall be available for all the goods manufactured in the industrial units, which have duly qualified for the benefit of the exemption prior to 31/3/2007. In other words, any/all goods manufactured by the industrial units, which are eligible for the exemption before the notified date, are entitled for the exemption!

So far so good! But if the issue is so simple, why at all an article? Reference is drawn to an interesting correspondence between the Secretary (Industrial Development) & Director of Industries for the Government of Uttranchal and the CBEC, wherein, the Secretary to the Government of Uttranchal, vide his letter dated 31/1/2006, has enquired about the eligibility of the exemption under the above notifications to the Board, in respect of the following situations, viz.,

(a) a unit commences commercial production of items and registers under the excise classification of 87.02 & 87.03. Can the unit subsequently manufacture any product that falls under these excise classifications? Say, the unit commences with cars of less than 1000cc before 31/3/2007 but subsequently start manufacturing cars of more than 1000cc subsequent to 31/3/2007, both of which fall under the excise classification 87.03. Would both all types of vehicles falling under 87.03 qualify for the exemption as long as the 10-year period starts from the date of commercial production of the first vehicle and as long as all vehicles are cleared from the same unit?

(b) a unit commences commercial operations with a capacity of say 1,00,000 vehicles. 2 years down the line (after 31/3/2007) it increases the capacity to 2,00,000 vehicles using:

- (i) the same production line;
- (ii) setting up a new production line;

Will the exemption be available only for (b) (i) above or will it be available for (b) (ii) as well?

In response, the CBEC vide its letter dated 6/2/2006, has stated that there appears to be no bar in the notification, on setting up a new production line or manufacturing products under same excise classification, subsequent to 31/3/2007, provided that the conditions specified in the proviso to Paragraph 1 of the notification are satisfied. Subsequently, the CBEC modified the above clarification, vide its letter dated 21/3/2006, wherein it has clarified that, in cases where a new assembly / production line is installed after 31/3/2007, then the benefit of the exemption shall not be available for the goods manufactured out of such new assembly/production line. It has also been clarified that, in cases where the commercial production of a particular kind of specified goods have not commenced prior to 31/3/2007, then the benefit of the exemption shall not be available to such goods. In fine, it has summarily ruled out the benefit of the notifications to the situations in Para (a) and (b) (ii) above.

It appears that the above clarification issued by the Board inherits neither any logic nor any sound reasoning. It is also neither legally founded nor based on any judicial ratio. But, like any other issue, this clarification is also capable of creating a national furore. Further, there is every possibility that, the duty bound revenue brigade, with their microscopic interpretational skills, would proceed to read between the lines and allege to deny the exemption, even if there is a small design change in the products, after 31.3.2007.

With the sunset date of these notifications being hardly 10 months away, it is already a twilight zone. By this arbitrary clarification, the Board has just ignited a high-voltage bomb. It is sure that, someday, it shall explode on the aspiring industrialists, who are investing their fortune in the valley! We are really afraid that, whether the industrialists, who are busy planning and executing their plum projects, in these Excise-blessed States, would really have any clue about this clarification and its dreadful impact. Being a volatile issue, involving crores and crores of investment, we hereby earnestly appeal to the Board, to issue the above said clarification, by way of a Circular so that, even though it may be a rude shock to the multifarious industrialists, at least let them know, what is in store!

Before parting...

There are two more corollary issues, namely, whether the benefit of the above notifications shall be available to:

1. an unit, which has installed second-hand machineries and
2. an unit, which has shifted their existing unit, situated outside the exemption areas to the exempted areas?

Whereas the Board has clarified that the installation of second-hand machinery would not dis-entitle the unit from the benefit of the notification by its Circular No. 772/5/2004-CX dated 21/1/2004 **{2004 (164) E.L.T. T4}**, the Hon'ble Supreme Court has come to the rescue, in respect of shifting an existing unit. In a reasoned judgement in the case of **CCE, Shillong vs North-Eastern Tobacco Co. Ltd**, as reported in **2002 (146) E.L.T. 490 (S.C.)**, the Apex Court has ruled that the exemption notifications do not define that a new industrial unit would exclude the units that are shifted or transferred from one location to another from its ambit!