

THE FIAT FIASCO - II

(S. Jaikumar, Advocate, Swamy Associates)

"Whereas it takes a whole box for a campfire, a careless match is enough for a forest fire."

Though this landmark judgement is primarily and predominantly for the period prior to 1/7/2000, wherein, Section 4 of the Central Excise Act (CEA) was under the "normal price" regime, the latter part of the decision tangents upon the "transaction value" regime, wherein, the Apex Court had approved the invocation of the provisions of the Valuation Rules 2000 for the period after 1st July, 2000, thus igniting a nation-wide furore.

The Department has already initiated enquiries across the right, left and center of the industry, asking for the details of the cost of production and profit margin and has started probing into the fact as to whether the adopted "transaction value" is over and above the "cost plus profit".

Here is an attempt to analyse the various contingencies, as formulated in Part – I.

Impact under the "transaction value" regime

In para 61 of the judgement, it has been observed as under:

"After amendment of Section 4 :- Section 4 lays down that the valuation of excisable goods chargeable to duty of excises on ad-valorem would be based upon the concept of transaction value for levy of duty. 'Transaction value' means the price actually paid or payable for the goods, when sold, and includes any amount that the buyer is liable to pay to the assessee in connection with the sale, whether payable at the time of sale or at any other time, including any amount charged for, or to make provisions for advertising or publicity, marketing and selling, and storage etc., but does not include duty of excise, sales tax, or any other taxes, if any, actually paid or payable on such goods. Therefore, each removal is a different

transaction and duty is charged on the value of each transaction. The new Section 4, therefore, accepts different transaction values which may be charged by the assessee to different customers for assessment purposes where one of the three requirements, namely; (a) where the goods are sold for delivery at the time and place of delivery; (b) the assessee and buyers are not related; and (c) price is the sole consideration for sale, is not satisfied, then the transaction value shall not be the assessable value and value in such case has to be arrived at, under the Central Excise Valuation (Determination of Price of Excisable Goods) Rules 2000 ('the Rules 2000' for short) which is also made effective from 1st July, 2000. Since the price is not the sole consideration for the period even after 1st July, 2000, in our view, the assessing authority was justified in invoking provisions of the Rules 2000."

Thus, the Apex Court had concluded that even under the "transaction value" regime, the valuation has to be resorted to the Section 4(1)(b) of CEA and therefore under the Valuation Rules, 2000.

Coming to provisions of the Valuation Rules, though the judgement had clarified and approved the application of the best judgement under Rule 7 of the erstwhile Valuation Rules, 1975 under the "normal price" regime, it had been silent as to the which would be the relevant Rule under the Valuation Rules, 2000 under the "transaction value" regime.

As discussed in Part I, in this judgement, the Apex Court had departed from Section 4(1)(a) of CEA and resorted to Section 4(1)(b) of CEA and the Valuation Rules because of three reasons, namely:

1. The "loss making price" cannot be considered as "normal price",
2. The goods are NOT ORDINARILY SOLD in the course of the wholesale trade and
3. The price is not the sole consideration for the sale.

The above three findings are rendered under the "normal price" regime, whereas, under the "transaction value" regime, the Apex Court had found that, only the third one *supra*, namely, the price is not the sole consideration, to be the reason for resorting to Section 4(1)(b) of CEA and therefore to Valuation Rules 2000.

In other words, the other two reasons, namely, "loss making price" is not the "normal price" and the sale is not "ordinary" are not the reasons under the "transaction value" regime to reject the value under Section 4(1)(a) of CEA. This is also supported by the reason that, under the "transaction value" regime, Section 4 of CEA does not incorporate or contemplate, either of the terms "normal price" or "ordinarily sold" in its definition.

This leaves us with a proposition that, post 'transaction value' regime, in the facts of the case, all other conditions contemplated under Section 4(1)(a) of CEA except the condition that the price is not the sole consideration for sale, are satisfied.

Now as per the ratio of the judgement, since the condition that the price is not the sole consideration for sale has not been met in the instant case, valuation has to be resorted to Section 4(1)(b) of CEA and therefore under the Valuation Rules 2000.

Coming to the Valuation Rules 2000, Rule 6 of the said Rules reads as under:

"6. Where the excisable goods are sold in the circumstances specified in clause (a) of sub section (1) of section 4 of the Act except the circumstance where the price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee".

To me, this Rule is a simpliciter to the case on hand. As discussed above and as approved by the Apex Court, post “transaction value” regime, the situation is that the excisable goods are sold in the circumstances specified in Section 4(1)(a) of CEA except the circumstance where the price is not the sole consideration for sale, **which is an identical situation contemplated in Rule 6 *supra*.**

In the present case, in para 60 of the judgement, it has been held as under;

"In the instant case, the main reason for the assessees to sell their cars at a lower price than the manufacturing cost and profit is to penetrate the market and this will constitute extra commercial consideration and not the sole consideration".

Thus the additional consideration is held to be the advantage of the market penetration.

On application of Rule 6 of the Valuation Rules, in a situation where all other conditions of section 4(1)(a) of CEA are met except the condition that the price being the sole consideration, the value shall be **deemed** to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly **from the buyer to the assessee.**

In the instant case, firstly, there is no such additional consideration in terms of money value, and secondly, even if the market penetration is considered to be the additional consideration, then also such consideration **DOES NOT FLOW FROM THE BUYER TO THE ASSESSEE** as called for in Rule 6 *supra*, thus not warranting any addition to the transaction value.

Further, as the said Rule 6 “deems” the value by restricting it to the aggregate of the transaction value plus the money value of the additional

consideration flowing from buyer to the assessee, even if the department contends that there is an additional consideration by way of market penetration, the value cannot be enlarged any further, because its a "deemed value" under Rule 6 *ibid*.

Thus I am of the firm opinion that the application of the Fiat ratio in the "transaction value" regime shall have little impact due to the evangelical Rule 6 of the Valuation Rules.

In other words, under the "transaction value" regime after 1/7/2000, if the assessee sells their goods on a transaction value, which is lesser than the cost of production plus profit, be it for any reason including market penetration, then such goods shall be valued as per Section 4(1)(b) of CEA and correspondingly under Rule 6 of the Valuation Rules 2000, whereby, the value shall be *deemed* to be the aggregate of the transaction value plus the money value of the additional consideration flowing from the buyer to the assessee, thus resulting to the originally adopted transaction value only, for the reason that there would be no additional consideration flowing from the buyer to the assessee, in such cases.

Coming to the second poser as to whether the said ratio of this judgement would be restricted only to the automobile sector or shall be applicable across the industry, the ratio would be applicable to all excisable goods which are assessed to duty under Section 4 of CEA.

With regard to the poser that, considering the prevalent practice in trade wherein supplies made to OEM (Original Equipment Manufacturer) would be on a price much lesser than the cost plus profit (with a view of the handsome price margin in the spare market) what would be the impact on such OEM supplies, though there may be an impact on the goods cleared under the "normal price" regime, there would be little impact under the "transaction value" regime, for the reasons stated *supra*.

Regarding the other posers as to whether this ratio would affect the various discounts given by the manufacturers to penetrate/sustain in the market as well as the extra ordinary sales like distress sale, clearance sale etc, where the manufacturer clears the excisable goods at a price less than the cost plus margin to meet such contingencies, there is enough ammunition for the department to allege under the "normal price" regime, but, for the same reasons stated *supra*, there shall be little impact under the post "transaction value" regime, wherein, even on application of Section 4(1)(b) of CEA and Rule 6 of the Valuation Rules, ultimately the duty would be payable ONLY on the "transaction value."

Before Parting...

Apart from the above reasoning, the judgement has itself provided a little leeway. In the judgement, the Apex Court has also tacitly approved certain instances whereby the manufacturer would sell his goods at a price lesser than the cost. Reference is drawn to para 50 of the said judgement, wherein, it has been observed as under:

"There could be instances where a manufacturer may sell his goods at a price less than the cost of manufacturing and manufacturing profit, when the company wants to switch over its business for any other manufacturing activity, it could also be where the manufacturer has goods which could not be sold within a reasonable time. These instances are not exhaustive but only illustrative."