



Supreme Court explains its earlier judgment of Dhamendra Textile and rules that the levy of penalty is not automatic in all the cases

Background

In October 2008, the Supreme Court of India (SC), in the case of *Dharmendra Textile Processors*¹ held that section 11AC of the Central Excise Act, 1944 (the Excise Act) dealing with imposing concealment penalty on persons who evaded payment of tax, should not be read to contain *mens rea*² as an essential ingredient and there was no scope for levying penalty below the prescribed minimum.

The SC further held that penalty under section 271(1)(c) of the Act was a civil liability and wilful concealment was not an essential ingredient for attracting civil liability but it was an essential ingredient to launch prosecution proceedings under section 276C of the Act.

This decision was being misinterpreted by the revenue to impose penalty in every case of short /non payment of excise duty. A similar approach has been adopted by the revenue to impose penalty under section 271(1)(c) of the Act. Despite the decision in some cases, penalty was being waived for the sole reason that duty was paid before issue of show cause notice. The way in which ruling of the SC in the case of *Dharmendra Textile Processors* was being interpreted is the backdrop to the current ruling.

On 12 May 2009, the SC, in the case of *Union of India v. M/s Rajasthan Spinning & Weaving Mills and Commissioner of Customs and Central Excise v. M/s Lanco Industries Limited*³ ruled on the conditions and circumstances under which penalty under section 11AC of the Excise Act would be attracted.

¹ UOI v. M/s. Dharmendra Textile Processors [2008] 231 ELT 3, 306 ITR 277 (SC)

² “Mens rea” is the mental state that produces criminal liability

³ Arising in Civil Appeals 3527 of 2009 and 3525 of 2009

In a decision having far reaching consequences, the SC observed that penalty under section 11AC would be applicable if conditions stated in that section are satisfied. Any other factor (payment of differential duty before issue of show cause notice) would not have a bearing in reaching this conclusion.

The SC further observed that in almost every case relating to penalty, the decision (Dharmendra Textile Processors) is referred to on behalf of the Revenue, as if it laid down the law that in every case of non-payment or short payment of duty the penalty clause would automatically get attracted and the authority had no discretion in the matter. There is no reason to understand or read that decision in that manner.

Facts of the case

Under different circumstances, both Rajasthan Spinning & Weaving Mills and Lanco Industries Limited were required to pay differential excise duty. In the case of Rajasthan Spinning & Weaving Mills, the same was paid before issue of show cause notice, based on the omission being pointed out by the central excise authorities. In case of Lanco Industries Limited, differential duty was deposited on the date of issue of show cause notice.

In both the cases, the adjudicating authorities issued a show cause notice seeking recovery of differential duty, interest and penalty and confirmed the same through their orders. Penalty in question was the penalty imposed under section 11AC of the Excise Act, being an amount equal to the amount of differential duty. However, the Customs, Excise and Service Tax Appellate Tribunal (Tribunal), for the reason that the assessee made payment of full duty before issue of notice, set aside the imposition of penalty.

Issue for consideration

What are the conditions and the circumstances that would attract the imposition of penalty under section 11AC of the Excise Act?

Taxpayer's contentions

- Though, demand for recovery of differential duty was untenable, the assessee made payment in order to buy peace and avoid litigation. In these circumstances, imposition of penalty was wholly unjust, unwarranted and unauthorized in law.
- Section 11A and 11AC not only operate in different fields, but, the two provisions are also separate by time. The penalty provision of section 11AC would come into play only after an order is passed under section 11A(2) with the finding that the escaped duty was the result of deception by the assessee by adopting a means as indicated in section 11AC.

Supreme Court's Ruling

- Main body of sub-section (1) of section 11AC lays down the conditions and circumstances that would attract penalty and the various provisos enumerate the conditions, subject to which and the extent to which the penalty may be reduced.
- The conditions that would extend the normal period of one year to five years would also attract the imposition of penalty. It, therefore follows that if the notice under section 11A(1) states that the escaped duty was the result of any conscious and deliberate wrong doing and in the order passed under section 11A(2), there is a legally tenable finding to that effect, then the provision of section 11AC would also get attracted. The converse of this is equally true.
- Penalty under section 11AC is punishment for an act of deliberate deception with the intent to evade duty by adopting any of the means mentioned in the section.
- In almost every case relating to penalty, the decision (Dharmendra Textile Processors) is referred to on behalf of the Revenue, as if it laid down the law that in every case of non-payment or short payment of duty the penalty clause would automatically get attracted and the authority had no discretion in the matter. There is no reason to understand or read that decision in that manner.
- The decision in the Dharmendra Textile Processors case must be understood to mean that though the application of section 11AC would depend upon the existence or otherwise of the conditions expressly stated in the section, once the section is applicable in a case, the concerned authority would have no discretion in quantifying the amount and penalty must be imposed equal to the duty determined under sub-section (2) of section 11A.

Our Comments

The SC's observation in the current case regarding the decision in the Dharmendra Textile Processors case is only in so far as section 11AC is concerned. Observations are not made regarding several other statutory provisions that came up for consideration in that case.

In view of the above, once conditions specified in section 11AC are satisfied, penalty under that section would have to be necessarily imposed and the concerned authorities would have no discretion – regarding whether or not to impose the penalty or regarding the amount of penalty. However, every case of non-payment or short payment of duty does not necessarily attract penalty under the said section.

Factors such as payment of duty before issue of notice etc are not relevant to determine if penalty under section 11AC can be imposed.

Though SC has given its ruling under section 11AC, it should be helpful while interpreting the provisions of section 271(1)(c) of the Act because it was pointed out in the ruling of Dharmendra Textile that both these provisions are pari materia. Therefore, even though the SC in this decision have not specifically dealt with section 271(1)(c) of the Act, it will certainly have persuasive value based on the similarity between both the provisions.

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