REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO.6896 OF 2002

KESAR ENTERPRISES LTD. — APPELLANT

VERSUS

STATE OF U.P. & ORS. — RESPONDENTS

J U D G M E N T

D.K. JAIN, J.:

1. Challenge in this appeal, by special leave, is to the judgment and order dated 18th January, 1996, delivered by the High Court of Judicature at Allahabad in C.W.P. No.599 of 1994. By the impugned judgment, the High Court has come to the conclusion that although the State Government had no authority to levy Excise duty under Section 28 of the U.P. Excise Act, 1910 (for short "the Act") on rectified spirit (industrial alcohol) in question but it could impose penalty on the appellant under Rule 633(7) of the Uttar Pradesh Excise Manual, (for short "the Excise Manual").

2. The background facts, essential for disposal of the instant appeal, in brief, are that on 15th October, 1988, the Excise Commissioner, Uttar Pradesh, issued an order authorising nine distilleries in the State, including M/s Daurala Sugar Works, to export rectified spirit (industrial alcohol), outside India. Since the export consignment was to be routed through the appellant, as handling agent as also the owner of the bonded warehouse at Kandla Port, where the spirit was to be stored before export, the appellant was required to furnish an indemnity bond, in the prescribed form, in favour of the Excise Commissioner as the authorised nominee of the exporter. On 20th December 1988, the appellant executed an indemnity bond in favour of the Governor of Uttar Pradesh in relation to permission for removal by rail 67.77 lac bulk litres of rectified spirit of any strength ranging between 91.68% V/V @ 15.6^{0}C to 95% V/V @ 15.6^{0}C. One of the conditions in the indemnity bond was that if the said quantity of rectified spirit, after deducting such allowance for dryage and wastage, as may be sanctioned, is not delivered at the warehouse at Kandla, the authorised nominee, the appellant herein, shall indemnify the Governor for any loss of duty, which the Governor may suffer by reason of such non delivery or short delivery, by paying him on demand the duty @ `40/- per alcoholic litre, on spirit not so delivered, after making the allowances aforesaid.

3.On 8th January, 1989, M/s Daurala Sugar Works consigned a rake of 15 tank wagons, loaded with 3,54,413 bulk litres of rectified spirit under PD-25 pass for export against order dated 15th October, 1988. The said consignment was dispatched through the Northern Railway to Kandla Port. However, out of 15 tank wagons only 14 tank wagons reached the Kandla Port. On 16th January, 1989, it was discovered that the 15th tank wagon was lying empty at Gandhi Dham Railway Station.

4.On 2nd October, 1992, a notice was issued by the Excise Commissioner to the appellant alleging that since the pass in form PD-25, issued to the appellant by the concerned Collector in terms of Rule 633 of the Excise Manual had not been received back along with certificate from the Collector for due delivery, they were liable to deposit in the Government Treasury, Excise duty on the rectified spirit @ `40/- per alcoholic litre, which amounted to `8,71,744/- along with interest at the rate of 18% per annum (`5,49,199/-).

5.The appellant having failed to deposit the said amount, another notice was issued by the Commissioner requiring them to show cause as to why their name be not black-listed and in future, permission for export may not be granted, on account of default on their part in not depositing Excise duty as demanded earlier.

6. The appellant responded to the said show cause notice by their letter dated 11th February, 1993, in which it was stated that since the reason for non receipt of the said rectified spirit was being investigated, the matter may be deferred till 30th June, 1993. Finally, vide their letter dated 29th April, 1994, the appellant replied to the show cause notice, contesting Excise Commissioner's claim for payment of Excise duty on account of non-receipt of full quantity of rectified spirit at the Kandla Port. It was pleaded that since the entire rake of 15 tank wagons was handed over to the Railway authorities at Daurala station for its delivery at Kandla Port, it was the responsibility of the Railways to make safe delivery of the goods at the destination and, therefore, the appellant was in no way responsible for the disappearance of rectified spirit contained in one of the tank wagons. It was, thus, urged that no Excise duty was payable by the appellant as the State Government had not suffered any loss of duty by reason of non delivery or short delivery of the rectified spirit.

7. Not being satisfied with the explanation furnished by the appellant, vide letter dated 6th April, 1994, the Excise Commissioner directed the District Excise Officer, Bareilly to issue recovery certificate and take appropriate steps against the appellant for the recovery of Excise duty amounting to `8,71,744/- and interest thereon. By letter dated 22nd June, 1994, the Bank of Baroda, Mandwi Branch, informed the appellant that pursuant to an order dated 22nd June, 1994, issued by the Sub-Divisional

Magistrate, their bank account had been attached and a sum of `12,00,000/- had been earmarked from their account for payment of Excise duty.

8.Being aggrieved, the appellant filed a writ petition before the High Court, seeking quashing of notice of demand dated 6th April, 1994. Relying on the decision of a Bench of seven Judges in ***Synthetics And Chemicals Ltd. & Ors.*** *Vs.* ***State of U.P. & Ors.***[1], wherein it was held that the States are not competent to impose a tax or charge imposts in respect of rectified spirit for industrial purposes, having a strength not less than 95% by volume of ethyl alcohol, the High Court held that though the State of U.P. did not have jurisdiction to levy and demand Excise duty on the rectified spirit (industrial alcohol), which disappeared during transit, but Rule 633 of the Excise Manual empowered the State to impose penalty at the same rate at which the Excise duty was payable for breach of conditions in the Bond. The High Court also held that it could be presumed that the appellant had diverted the rectified spirit into potable alcohol on which penalty and penal interest could be levied and, therefore, it was not a fit case where it should exercise its jurisdiction under Article 226 of the Constitution of India and quash demand notice dated 6th April, 1994. Accordingly, the writ petition was dismissed. Being dissatisfied, the appellant is before us in this appeal.

[1] (1990) 1 SCC 109

9.We have heard learned counsel for the parties.

10. Assailing the decision of the High Court, Mr. D.K. Agarwal, learned senior counsel appearing for the appellant, strenuously urged that in light of decision of this Court in ***Synthetics And Chemicals*** (supra), which was duly noticed in the impugned judgment, the High Court exceeded its jurisdiction in converting the levy of Excise duty into penalty and interest under Rule 633 of the Excise Manual. It was argued that the High Court misread the Rule inasmuch as Rule 633(7) contemplates recovery of penalty under the bond in order to indemnify the Governor of the State for loss of Excise duty but when admittedly no Excise duty could be levied by the State Excise Commissioner on the entire consignment of rectified spirit, covered under the bond, there was no question of loss of Excise duty on that account, for which the Governor was to be indemnified. It was asserted that in any event imposition of penalty under the said Rule was *ex-facie* illegal as neither any show-cause notice was issued to the appellant before such levy nor any amount by way of penalty on account of the alleged non-compliance with the conditions of the bond was quantified and communicated to the appellant. It was thus, asserted that since an order under Rule 633, entails serious consequences the elementary principles of natural justice and fair play are required to be observed and consequently, an opportunity of hearing has to be afforded before an order under the said Rule is made, which was

admittedly not done in the instant case. In fact, the said Rule was invoked for the first time by the High Court.

11. Mr. Ravi Prakash Mehrotra, learned counsel appearing for the State, on the other hand, supporting the view taken by the High Court, submitted that Rule 633, does not postulate a show-cause notice before levy of penalty or interest because penalty or interest being compensatory in nature because of infringement of condition of an indemnity bond furnished by the appellant to the Collector or the Excise Inspector, the liability under the Bond is absolute. It was argued that since in the present case, admittedly, the discharge certificate in terms of Rule 633 had not been furnished by the appellant within the stipulated time, penalty under the said Rule was clearly exigible.

12. The precise question at issue is whether sub-rule (7) of Rule 633 of the Excise Manual postulates the requirement of hearing before steps for recovery of penalty under the said Rule are initiated?

13. Before addressing the issue, it is necessary to bear in mind the fact that in so far as the question of levy of Excise duty on the high strength rectified spirit in 15 tank wagons is concerned, parties are *ad-idem* that in view of the judgment of this Court in ***Synthetics And Chemicals*** (supra), the State was not empowered to levy Excise duty on the said consignment. In the said decision, while interpreting Entry 84 of List I,

Entry 8 and 51 of List II and Entry 33 of List III of the Seventh Schedule to the Constitution of India, it was held that the State legislature has no power to enact law levying duty on the spirit, which is not meant for human consumption. It was also held that the State has the power to impose duty only on spirit, which is meant for human consumption under Entry 51 of List II of the Seventh Schedule. In light of the said decision, it is clear that under Section 28 of the Act, the charging Section, an Excise duty or a Countervailing duty, as the case may be, can be imposed by the State on alcoholic liquor only when it reaches the stage of human consumption and not on high strength rectified spirit (industrial alcohol), a Central subject. Therefore, the High Court is correct in law in holding that the State did not have the jurisdiction to levy Excise duty on rectified spirit, loaded in 15 tank wagons.

14. However, Rule 633 of the Excise Manual, which has been pressed into service by the High Court to sustain the demands raised against the appellant, reads as follows :

> "633. Any person may export in bond foreign liquor manufactured at a distillery in Uttar Pradesh to any place in India under a pass in form P.D.25 granted as provided in the following rules:
>
> (1) When any person desires to export in bond spirit manufactured at a distillery in Uttar Pradesh, he shall present a written application in form P.D. 58 to the Collector of the district in which the distillery of manufacture is situate.
>
> The application must specify—

(i) the name of the consignor;
(ii) the name of the consignee;
(iii) the description, quantity and strength of the spirit to be exported.

(2) Every application must be accompanied by—
(i) a permit from the Collector, Deputy Commissioner, or other officer specially appointed in this behalf of the district to which the spirits are to be exported authorizing the import of spirit; and
(ii) a duly executed special bond in form P.D. 16 or a reference to a general bond in form P.D. 15.

(3) The pass granted by the Collector of the exporting district or the Excise Inspector to whom the Collector may have delegated his power vide paragraph 58(c) of this Manual, shall be in triplicate in form P.D.-25.

One copy of the pass shall be delivered to the exporter, the second forwarded to the Collector, Deputy Commissioner, or *other* officer specially appointed in this behalf of the district to which the spirits are to be taken, and the third retained for record.

*NOTE-This will usually be the officer-in-charge of the bonded warehouse to which the spirit is consigned.

An advance in form P.D. 26 must also be sent by the officer-in-charge direct to the authority granting the import permit who will return the same duly filed in as soon as possible after receipt and verification of the consignment.

Within a reasonable time to be fixed by the Collector of the exporting district and specified in the bond or pass the importer shall produce before the Collector of the exporting district his copy of the pass endorsed with a certificate signed by the Collector, Deputy Commissioner or other officer specially appointed in this behalf, of the importing district certifying the due arrival or otherwise of the spirit at its destination;

(4) On each cask or other vessel containing spirit for export there shall be legibly cut or painted:

(i) the name and mark of the exporting distillery;
(ii) the number of the cask or other vessel and its capacity;
(iii) the nature, quantity and strength of its contents.

These particulars shall correspond with those entered in the pass.

(5) On a written application being made to the Collector of the exporting district establishing sufficient cause for the grant of an extension of time, or on the production before him of a certificate from the Collector, Deputy Commissioner, or other officer specially appointed in this behalf, of the district of destination, to the effect that there are good and sufficient reasons for extending the currency of the pass or bond, it shall be competent for the Collector of the exporting district, if he thinks fit, to extend the time specified in the pass or bond for the due arrival of the spirit at its destination.

(6) In the case of spirit exported under special bond the Collector of the exporting district shall discharge the bond on receipt of the pass in form P.D.-25 and certificate mentioned in clause (3), provided that none of the conditions of the bond have been infringed. The duty on consignment issued under a general bond shall be written off on receipt of the pass and certificate mentioned in clause (3), provided that none of the conditions of the bond have been infringed.

(7) If the certificate be not received within the time mentioned in the bond or pass, or if on receipt of the certificate it appears that any of the conditions of the bond have been infringed the Collector of the exporting district or the Excise Inspector who granted the pass shall forthwith take necessary steps to recover from executant or his surety the penalty due under the bond."

15. It is manifest that the said Rule, made in exercise of the rule-making power of the State under the Act, would apply only in relation to manufacture, import, export and transport of potable liquor, i.e. the liquor

which is capable of being consumed by human beings. Precisely for the aforesaid reason, in order to bring appellant's case within the scope of Rule 633, High Court went on to observe that it could be presumed that rectified spirit in the missing tank wagon was diverted for conversion into potable alcohol. Rule 633 is of regulatory character meant to ensure that the liquor being exported under a bond reaches its destination and is not misused or misutilized in transit. It contemplates that if the bond along with certificate signed by the Collector or other named officers of the importing district, certifying due arrival or otherwise of the liquor at its destination, is not furnished to the Collector of the exporting district, he would be entitled to presume that the liquor has been disposed of otherwise than by export and can proceed to take necessary steps as postulated in sub-rule (7) of Rule 633 of the Excise Manual. The said Rule provides for imposition of penalty, which may be equivalent to the Excise duty, leviable under the charging Section 28 of the Act on potable liquor. Bearing in mind the scope of Rule 633, we may now advert to the moot question, viz. whether the principles of natural justice demand that an opportunity of hearing should be afforded before an order under Rule 633(7) of the Excise Manual is made?

16. Before we deal with the question, it would be necessary to understand and appreciate the concept of natural justice and the principles governing its application.

17. Rules of "natural justice" are not embodied rules. The phrase "natural justice" is also not capable of a precise definition. The underlying principle of natural justice, evolved under the common law, is to check arbitrary exercise of power by the State or its functionaries. Therefore, the principle implies a duty to act fairly i.e. fair play in action. As observed by this Court in ***A.K. Kraipak & Ors.*** *Vs.* ***Union of India & Ors.***[2] the aim of rules of natural justice is to secure justice or to put it negatively to prevent miscarriage of justice. These rules can operate only in areas not covered by any law validly made. They do not supplant the law but supplement it. (Also see ***Income Tax Officer & Ors.*** *Vs.* ***M/s Madnani Engineering Works Ltd., Calcutta***[3]).

18. In ***Swadeshi Cotton Mills*** *Vs.* ***Union of India***[4] R.S. Sarkaria, J., speaking for the majority in a three-Judge Bench, lucidly explained the meaning and scope of the concept of "natural justice". Referring to a catena of decisions, his Lordship observed thus:

> "Rules of natural justice are not embodied rules. Being means to an end and not an end in themselves, it is not possible to make an exhaustive catalogue of such rules. But there are two fundamental maxims of natural justice viz. *(i) audi alteram partem and (ii) nemo judex in re sua.* The audi alteram partem rule has many facets, two of them being (a) notice of the case to be met; and (b) opportunity to explain. This rule cannot be sacrificed at the altar of administrative convenience or celerity. The general principle--as distinguished from an absolute rule of uniform

[2] (1969) 2 SCC 262
[3] (1979) 2 SCC 455
[4] (1981) 1 SCC 664

> application—seems to be that where a statute does not, in terms, exclude this rule of prior hearing but contemplates a post-decisional hearing amounting to a full review of the original order on merits, then such a statute would be construed as excluding the *audi alteram partem* rule at the pre-decisional stage. Conversely if the statute conferring the power is silent with regard to the giving of a pre-decisional hearing to the person affected and the administrative decision taken by the authority involves civil consequences of a grave nature, and no full review or appeal on merits against that decision is provided, courts will be extremely reluctant to construe such a statute as excluding the duty of affording even a minimal hearing, shorn of all its formal trappings and dilatory features at the pre-decisional stage, unless, viewed pragmatically, it would paralyse the administrative process or frustrate the need for utmost promptitude. In short, this rule of fair play must not be jettisoned save in very exceptional circumstances where compulsive necessity so demands. The court must make every effort to salvage this cardinal rule to the maximum extent possible, with situational modifications. But, the core of it must, however, remain, namely, that the person affected must have reasonable opportunity of being heard and the hearing must be a genuine hearing and not an empty public relations exercise."
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> (Emphasis added)

19. In ***Canara Bank*** *Vs.* ***V.K. Awasthy***[5] the concept, scope, history of development and significance of principles of natural justice have been discussed in extenso, with reference to earlier cases on the subject. *Inter alia*, observing that the principles of natural justice are those rules which have been laid down by the courts as being the minimum protection of the rights of the individual against the arbitrary procedure that may be

[5] (2005) 6 SCC 321

adopted by a judicial, quasi-judicial and administrative authority while making an order affecting those rights, the court said:

> "Concept of natural justice has undergone a great deal of change in recent years. Rules of natural justice are not rules embodied always expressly in a statute or in rules framed thereunder. They may be implied from the nature of the duty to be performed under a statute. What particular rule of natural justice should be implied and what its context should be in a given case must depend to a great extent on the fact and circumstances of that case, the framework of the statute under which the enquiry is held."

20. The question with regard to the requirement of an opportunity of being heard in a particular case, even in the absence of provisions for such hearing, has been considered by this Court in a catena of cases. However, for the sake of brevity, we do not propose to refer to all these decisions. Reference to a recent decision of this Court in ***Sahara India (Firm), Lucknow*** *Vs.* ***Commissioner of Income Tax, Central-I & Anr.***[6] would suffice. In that case, the question for adjudication was whether in the absence of a provision in the Income Tax Act, 1961, an opportunity of hearing was required to be given to an assessee before an order under Section 142(2-A) of the said Act, directing special audit of his accounts was passed? A Bench of three Judges, speaking through one of us (D.K. Jain, J.), explaining the concept of "natural justice" and the principles governing its application, summed up the legal position as under :

[6] (2008) 14 SCC 151

> "Thus, it is trite that unless a statutory provision either specifically or by necessary implication excludes the application of principles of natural justice, because in that event the court would not ignore the legislative mandate, the requirement of giving reasonable opportunity of being heard before an order is made, is generally read into the provisions of a statute, particularly when the order has adverse civil consequences for the party affected. The principle will hold good irrespective of whether the power conferred on a statutory body or tribunal is administrative or quasi-judicial.
>
> We may, however, hasten to add that no general rule of universal application can be laid down as to the applicability of the principle audi alteram partem, in addition to the language of the provision. Undoubtedly, there can be exceptions to the said doctrine. Therefore, we refrain from giving an exhaustive catalogue of the cases where the said principle should be applied. The question whether the principle has to be applied or not is to be considered bearing in mind the express language and the basic scheme of the provision conferring the power; the nature of the power conferred and the purpose for which the power is conferred and the final effect of the exercise of that power. It is only upon a consideration of all these matters that the question of application of the said principle can be properly determined."

21. Having considered the issue, framed in para 12 supra, on the touchstone of the afore-noted legal principles in regard to the applicability of the principles of natural justice, we are of the opinion that keeping in view the nature, scope and consequences of direction under sub-rule (7) of Rule 633 of the Excise Manual, the principles of natural justice demand that a show-cause notice should be issued and an opportunity of hearing should be afforded to the person concerned before an order under the said Rule is made, notwithstanding the fact that the

said Rule does not contain any express provision for the affected party being given an opportunity of being heard. Undoubtedly, action under the said Rule is a quasi-judicial function which involves due application of mind to the facts as well as to the requirements of law. Therefore, it is plain that before raising any demand and initiating any step to recover from the executant of the bond any amount by way of penalty, there has to be an adjudication as regards the breach of condition(s) of the bond or the failure to produce the discharge certificate within the time mentioned in the bond on the basis of the explanation as also the material which may be adduced by the person concerned denying the liability to pay such penalty. Moreover, the penalty amount has also to be quantified before proceedings for recovery of the amount so determined are taken. In our view, therefore, if the requirement of an opportunity to show-cause is not read into the said Rule, an action thereunder would be open to challenge as violative of Article 14 of the Constitution of India on the ground that the power conferred on the competent authority under the provision is arbitrary.

22. Thus tested, in the instant case, vide his letter dated 2nd October 1992, the Excise Commissioner called upon the appellant to deposit an amount of `14,20,943/- towards Excise duty and interest on account of default on their part to furnish PD-25 pass duly certified by the competent authority at Kandla Port. The letter /notice does not indicate the exact quantity of

rectified spirit on which duty @ `40/- per alcoholic litre has been charged, though the total amount of duty payable is mentioned. Similarly, in the final show-cause notice dated 6th April 1994, threatening action for black listing for future exports on account of non-payment of the aforenoted amount, there is not even a whisper as to how and why rectified spirit in question was being subjected to Excise duty by the State. As stated above, this Court having categorically held in ***Synthetics And Chemicals*** (supra) and in catena of subsequent decisions that the State Legislature had no legislative competence to impose Excise duty on rectified spirit (industrial alcohol), the Commissioner of Excise could not demand Excise duty on rectified spirit contained in the tank wagon which, later on, was found to be empty, without returning a finding that the said spirit had been diverted/converted into potable alcoholic liquor fit for human consumption, on which the State was empowered to impose duty. It bears repetition that such a finding could not be recorded by the Commissioner without affording due opportunity to the appellant to explain its stand in this regard for which, the onus lay on them as transporter and the executant of the bond. We may, however, add that in the absence of any reasonable explanation regarding disappearance of rectified spirit, the Commissioner would have reason to presume that the same has been disposed of otherwise than by way of export outside the country, for which purpose it was being transported. We are convinced that in the present case, before imposing the impugned demand of penalty

and interest, there was absolutely no adjudication by any authority as regards the breach committed by the appellant, except the allegation that the appellant had failed to furnish the PD-25 pass certified by the Collector. In our opinion, therefore, the action of the respondents for the recovery of penalty and interest, being violative of principles of natural justice, is null and void.

23. In the afore-said premises, we allow the appeal; set aside the impugned demand raised by the Commissioner of Excise vide notice dated 2nd October 1992, as well as the judgment of the High Court, sustaining the demand by invoking Rule 633 of the Excise Manual and remit the matter to the jurisdictional Excise Commissioner to decide the question of levy of Excise duty and/or penalty and interest on the subject consignment of rectified spirit, after affording adequate opportunity of hearing to the appellant.

24. In the facts and circumstances of the case, the parties are left to bear their own costs throughout.

…….J.
(D.K. JAIN)

…….J.
(H.L. DATTU)

NEW DELHI;
JULY 6, 2011.

RS