

A M/S INDIAN PETROCHEMICALS CORPORATION LTD.

v.

COLLECTOR OF CENTRAL EXCISE, VADODARA

MARCH 5, 1997

B [A.M. AHMADI, CJI. AND SUJATA V. MANOHAR, J.]

C *Central Excise Tariff Act 1985—Chapters 27 and 29—Raw Naptha—Exempted from duty—By notification for manufacturing products enumerated in table subjected to Thermal cracking by-product Pyrolysis Gasolene—Collector levied excise duty—Tribunal held that pyrolysis Gasolene used for manufacture of Petroleum Resins not entitled for exemption—Held, raw naptha not diverted to manufacture Petroleum Resins—Pyrolysis Gasolene intermediate product—Totally exempted from payment of excise duty—Order of Tribunal set aside.*

D The appellant was engaged in the manufacture of Ethylene, Propylene, Benzene, Toluene and other products falling under chapters 27 and 29 of the Central Excise Tariff Act, 1985. The raw naphtha obtained by the appellant under the notification was exempted from payment of duty for manufacturing products specified in the table. The raw naphtha was subjected to thermal cracking and one of the by products obtained was pyrolysis gasolene. The Collector of Central Excise held that the entire quantity of pyrolysis gasoline was not entitled to concessional rate of duty as it was used for the manufacture of Petroleum Resins which were not enumerated in the said table.

F On appeal, the Tribunal held that Pyrolysis Gasolene used for manufacture of Benzene and Toluene was entitled to concessional rate of duty but pyrolysis Gasoline used for manufacture of Petroleum Resins was not entitled to concessional rate. Hence the present appeal.

G The contention of the appellant was that the entire quantity of raw naphtha obtained was subjected to fraction and other process to manufacture the products. One of the by products obtained was Pyrolysis Gasolene which was further processed to obtain Benzene and Toluene which were products mentioned in the table. According to the appellant there was no violation of the terms of the notification.

On the other hand the respondent contended that the appellant had diverted raw naphtha to the manufacture of petroleum Resin and therefore, not entitled to concessional rates of excise duty. A

Allowing the appeal, this Court

HELD : 1.1. The contention of the Collector of Central Excise that the appellant has diverted raw naphtha to the manufacture of Petroleum Resins is not correct. What the appellant obtained under the exemption notification was raw naphtha which was subjected to thermal cracking. The entire quality of raw naphtha was subjected to processing for the purpose of obtaining items enumerated in the table. The appellant did not set apart any quantity of raw naphtha for the purpose of obtaining petroleum Resin. It has merely subjected the residual Pyrolysis Gasolene for the manufacture of Petroleum Resins. This residual Pyrolysis Gasolene cannot be equated with raw naphtha which was obtained at concessional rate of duty. [724-E-F] B C

1.2. Explanation 2 of the notification provides that in cases where certain goods which are incidental, inevitable or involuntary to the process of manufacture of the products specified in the table are produced in the course of manufacture, the exemption under the notification shall not be denied on the ground that these goods are not products specified in the schedule. [724-G] D E

State of Haryana v. Dalmia Dadri Cement Ltd., [1987] Supp. SCC 679 and *M/s Steel Authority of India Ltd. v. Collector of Central Excise*; (C.A. Nos. 3406-11/90 with C.A. No. 3178/90 decided on 30.7.1995 by Supreme Court relied on. F

2. Pyrolysis Gasolene being an intermediate product which is produced in the factory of the appellant and it being utilised for the manufacture of other goods, it would be totally exempt from payment of excise duty under the second exemption notification. The appellant is not liable to pay any duty of excise on Pyrolysis Gasolene. The order of the Tribunal is set aside. [727-B-C] G

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 4914 of 1991.

From the Judgment and Order dated 19.9.92 of the Central Excise H

A and Gold (Control) Appellant Tribunal, New Delhi in A. No. E/268/91-C.

V. Lakshmi Kumaran, A.R. Madhav Rao, M.P. Devnath and Shekhar Vyas for P.H. Parekh for the Appellant.

B R.R. Mishra, and (S.D. Sharma) for V.K. Verma, for the Respondent.

The Judgment of the Court was delivered by

C MRS. SUJATA V. MANOHAR, J. The appellant is a Government of India Undertaking. The appellant is engaged, *inter alia*, in the manufacture of Ethylene, Propylene, Benzene, Toluene and other products falling under Chapters 27 and 29 of the Central Excise Tariff Act, 1985.

D At the material time the appellant obtained raw naphtha from the Refinery in terms of Notification No. 27/89-C.E. dated 1.3.1989. Under this notification, raw naphtha falling under sub-heading No. 2710.14 of the schedule to the Central Excise Tariff Act, 1985 intended for use in the manufacture of products specified in the table annexed to the said notification, is exempt from payment of so much of the duty of excise leviable thereon as is in excess of the amount calculated at the rate of Rs. 60 per kilolitre at 15C on the quantity of naphtha consumed in the manufacture of the said products. The table of products which is annexed to the notification, *inter alia*, covers Ethylene, Propylene, Butadiene, Benzene, Toluene and Para-Xylene which are the products manufactured by the appellant from raw naphtha obtained by the appellant under the concessional rate of excise duty under the above notification. According to the appellant it has not violated any term of this notification.

F The text of the notification is as follows :

G "Concessional rate on naphtha used in the manufacture of specified chemicals. - In exercise of the powers conferred by sub-section (1) of Section 5A of the Central Excises and Salt Act, 1944 (1 of 1944), the Central Government, being satisfied that it is necessary in the public interest so to do, hereby exempts raw naphtha, falling under sub-heading No. 2710.14 of the Schedule to the Central Excise Tariff Act, 1985 (5 of 1986), intended for use in the manufacture of the products specified in the Table hereto annexed from so much of the duty of excise leviable thereon as is in excess of the

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amount calculated at the rate of Rs. 60 per kilolitre at 15 C on the quantity of naphtha consumed in the manufacture of the said products :

Provided that where the use is elsewhere than in the factory of manufacture the procedure set out in Chapter X of the Central Excise Rules, 1944 is followed.

Explanation :

1. The amount of naphtha consumed in the manufacture of the products shall be calculated by subtracting from the quantity of naphtha received by the factory manufacturing the products the quantity of naphtha returned by the factory to a refinery, declared as such under sub-rule (2) of rule 140 of the Central Excise Rules, 1944.

2. In cases where certain goods which are incidental, inevitable, or involuntary to the process of manufacture the products specified in the said Table are produced in the course of the manufacture, the exemption under this notification shall not be denied for the reason that the said goods are not products specified in the said Schedule.

TABLE	
1.	Ethylene
2.	Propylene
3.	Butadiene
4.
5.
6.	Benzene
7.	Toluene
8.	Para-Xylene

According to the appellant the entire quantity of raw naphtha obtained by it is subjected to thermal cracking and is further subjected to fraction and other processes to extract or manufacture these products. At an intermediate stage of manufacture, one of the by-products obtained is

A pyrolysis Gasolene. Pyrolysis Gasolene is further processed by the appellant to obtain Benzene and Toluene which are products enumerated in the Table. The residue left after this manufacture is further processed to produce Petroleum Resins. Petroleum Resins are not listed in the Table. What is left over is returned to the refinery.

B The Collector, Central Excise held that the entire quantity of Pyrolysis Gasolene which was presumed by him to be raw naphtha, was not entitled to concessional rate of duty as it was used for the manufacture of Petroleum Resins. He levied a duty of Rs. 24,41,99,988.77, ordered confiscation of land, building, plant, machinery with option to the appellant to redeem them on payment of Rs. 1 lac and imposed a penalty of Rs. 5 crores.

C In appeal the Tribunal held that Pyrolysis Gasolene used for manufacture of Benzene and Toluene was entitled to concessional rate of duty. But the residual Pyrolysis Gasolene used for the manufacture of Petroleum resins was not so entitled. It reduced the duty to Rs. 4.36 crores and reduced the penalty to Rs. 10 lacs. The present appeal is from this order.

D Broadly speaking, the process of manufacture adopted by the appellant is as follows :

E Raw Naphtha which is obtained by the appellant at a concessional rate of duty under the above notification is cracked at high temperature as a result of which (1) olefenic rich gas (2) pyrolysis fuel oil and (3) pyrolysis gasolene are produced. Out of these, olefenic rich gas is further processed for the purpose of obtaining ethylene, butadiene, propylene and other items enumerated in the Table. Residual gas is flared while the residue is returned to naphtha cracker. The products which are obtained by the further processing of olefenic rich gas are all covered by the table in the concession notification. Pyrolysis fuel oil which is the second resultant of the thermal cracking process is used internally as fuel and is also removed as carbon black feed stock.

F Upto this stage the respondent has accepted that the appellant has complied with the requirements of the above notification. The difficulty in the present case has arisen on account of the third resultant of the thermal cracking processing, namely, pyrolysis gasolene. Pyrolysis gasolene which

arises in the process of thermal cracking is further processed by the appellant in order to obtain benzene and toluene which are also enumerated items. Since 1984 the appellant has put up a Petroleum resin plant. After the extraction of benzene and toluene, the residual pyrolysis gasolene is further processed in the petroleum resin plant of the appellant. The residual product is given a C8.C9 Cut which ultimately results in the manufacture of petroleum resins. Petroleum resins are not mentioned in the table annexed to the above exemption notification.

According to the respondent, the appellant has diverted pyrolysis gasolene for the manufacture of petroleum resins and, therefore, pyrolysis gasolene to the extent that it is used for the manufacture of petroleum resins cannot be granted concessional rates of excise duty. Accordingly under the impugned order of CEGAT, duty of excise must be calculated on the balance of residue of pyrolysis gasolene "diverted" for C8.C9 Cut and not on the entire pyrolysis gasolene as earlier held by the department. As a result the appellant has become liable to pay duty calculated approximately at Rs. 4.36 crores instead of Rs. 24,41,99,988.77 as earlier held by the department.

In order to decide whether the findings of Tribunal are correct, we must examine the terms of the notification in question. The notification exempts raw naphtha *intended for use* in the manufacture of products specified in the table attached to it from so much of the duty of excise as is in excess of the amount calculated at the rate of Rs. 60 per kilolitre at 15 C on the quantity of naphtha consumed in the manufacture of the said products. It is an accepted position that the appellant has used raw naphtha which was obtained by the appellant under the notification for the manufacture of products which are listed in the table.

The only contention of the department is that the appellant has not used the entire quantity of raw naphtha for this purpose. This contention does not appear to be correct. The entire quantity of raw naphtha which was obtained by the appellant under the exemption notification is subjected to thermal cracking for the purpose of obtaining ethylene, butadiene, propylene and other items which are incorporated in the said table. After the entire quantity of raw naphtha is subjected to thermal cracking, three items emerge; olefinic rich gas, pyrolysis fuel oil and pyrolysis gasolene. There is no way in which the appellant could have avoided this outcome.

- A Out of these resultants, olefinic rich gas is required to be further processed for the manufacture of items forming part of the table. One of the other resultant products, namely, pyrolysis gasolene is further processed to obtain some more products which are listed in the table, namely, benzene and toluene. For this processing of pyrolysis gasolene also the department has no objection because as a result of processing of pyrolysis gasolene the products which are obtained are listed in the table.
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- However, the further processing of residual pyrolysis gasolene after extraction of benzene and toluene in the petroleum resin plant on the appellant is objected to by the department. This further processing of pyrolysis gasolene residue results in production of petroleum resins which are not enumerated in the said table. There is no dispute that on petroleum resins so manufactured the appellant is paying duty of excise. The only dispute is as to the duty of excise to be levied on pyrolysis gasolene residue which is processed in the petroleum resin plant of the appellant to manufacture resins. According to the respondent the portion of the residual pyrolysis gasolene consumed in the manufacture of Petroleum resins should have been returned to the refinery.
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- In the first place the contention of the respondent that the appellant has diverted raw naphtha to the manufacture of petroleum resins is not correct. What the appellant obtained under the exemption notification was raw naphtha which was subjected to thermal cracking. The entire quantity of raw naphtha so obtained was subjected to processing for the purpose of obtaining items enumerated in the table. The appellant did not set apart any quantity of raw naphtha for the purpose of obtaining petroleum resins.
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- F It has merely subjected the residual pyrolysis gasolene to further processing in the petroleum resin plant for the manufacture of petroleum resins. This residual pyrolysis gasolene cannot be equated with raw naphtha which was obtained at concessional rate of duty. Explanation 2 of the notification provides that in cases where certain goods which are *incidental*, inevitable or involuntary to the process of manufacture of the products specified in the said table are produced in the course of manufacture the exemption under this notification shall not be denied on the ground that these goods are not products specified in the said Schedule. In fact, the respondent has issued a clarification with the concurrence of the Ministry of Law bearing G.I. (D.R. & D.) F. No. 03/15/72-Cx.3 dated 26.3.1976 setting out as follows
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- H :

"..... it is clarified that when raw naphtha is intended for use in the manufacture of any one or more of the products specified in the Schedule appended to the notification the production of other goods which are incidental/inevitable/involuntary in such production would not disturb the scheme of exemption and that the whole of the raw naphtha would be deemed to have been used in the manufacture of the product for the manufacture of which raw naphtha was obtained."

In this connection, our attention is drawn to a decision of this Court in the case of *State of Haryana v. Dalmia Dadri Cement Ltd.* [1987] Supp. SCC 679. In that case, cement required for use in the generation or distribution of electrical energy was exempted from sale tax. The Punjab State Electricity Board had obtained the cement and given certificates that it was for use in the generation or distribution of electrical energy. The Court said that the mere fact that some of the cement supply was, in fact, used by the Board for activities not directly connected with the generation or distribution of electrical energy cannot make any difference to the availability of the exemption. The intention of the board was that the cement was directly connected with the generation or distribution of electrical energy.

In the present case, the entire raw naphtha which is obtained at concessional rates of duty is made use of for the purpose of obtaining products permitted under the said exemption notification. Only some of the processed residue is used for the manufacture of other products. There is, therefore, no violation in the present case of the exemption notification.

In the case of *M/s. Steel Authority of India Ltd. v. Collector of Central Excise*, C.A. Nos. 3406-11/90 with C.A. No. 3178/90 decided by this Court on 30-7-1995, S.P. Bharucha and K.T. Thomas, JJ.) raw naphtha was subjected to a concessional rate of duty under an exemption notification provided that it was intended for use in the manufacture of fertilizers. Raw naphtha which was so obtained by SAIL was according to the revenue not used entirely for the manufacture of fertilizers. According to SAIL, because of abnormal operating conditions there was excessive consumption of raw naphtha on account of low load operation, interruption in the plant operations due to low, uncertain and fluctuating availability of power. Also consumption of naphtha was further high because gases produced out of

A raw naphtha had to be vented due to acute power crisis causing interruption/stoppages of down stream units of the plant. The Court said that although raw naphtha for reasons beyond the control of SAIL did not, in fact, result in the manufacture of fertilizer and had to be vented at an interim stage, nevertheless it could not be said that SAIL had violated any condition of the exemption notification because raw naphtha which was fed by SAIL into its plant was for the purpose and with the intention of manufacturing fertilizers. It was only because of supervening circumstances that the reformed gas produced during the interim stage of manufacture had to be vented out.

C In the present case, pyrolysis gasolene is an incidental product which has been further processed to obtain petroleum resin. This cannot be considered as a diversion of raw naphtha obtained at concessional rates for manufacture of other items.

D In this connection, the appellant has drawn our attention to another exemption notification being Notification No. 28/89-C.E. also dated 1.3.1989 which is as follows :

E "Exemption of goods other than blended or compounded lubricating oils and greases. - In exercise of the powers conferred by sub-section (1) of section 5A of the Central Excise and Salt Act, 1944 (1 of 1944), the Central Government, being satisfied that it is necessary in the public interest so to do, hereby exempts goods (other than blended or compounded lubricating oils and greases) falling under Chapter 27 of the Schedule to the Central Excise Tariff Act, 1985 (5 of 1986) produced in a factory and -

F (a) utilised in the factory in which the said excisable goods are produced, for the manufacture of other goods or as fuel for such manufacture (excluding fuel used for any internal combustion engine) or both; or

G (b) allowed to escape in the atmosphere by flare system or otherwise;

from the whole of the duty excise leviable thereon which is specified in the said Schedule."

H Under this notification pyrolysis gasolene which falls under chapter

27 is produced in the appellant's factory and it is utilised for the manufacture of goods. As such it would be exempt from the whole of the duty of excise leviable thereon assuming that any duty of excise is leviable on it. Therefore, we fail to see how any duty of excise can be levied on any part of pyrolysis gasolene manufactured in the factory of the appellant. A

Pyrolysis Gasolene being an intermediate product which is produced in the factory of the appellant, and it being utilised for the manufacture of other goods, it would be totally exempt from payment of excise duty under the second exemption notification. B

The appeal is, therefore, allowed. the appellant is not liable to pay any duty of excise on pyrolysis gasolene. The impugned order of Tribunal is, therefore, set aside. There will, however, be no order as to costs. C

S.V.K.I.

Appeal allowed.