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# THE MUMMY RETURNS!

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The word "Mummy" has two meanings. Affectionate "Mother" as well as, a preserved "Corpse!" The Supreme Court decision in the case of Ujagar Prints is the mother of job work valuation. Like most of the Hollywood blockbusters, the "Ujagar prints" was a trilogy! To understand better, let us take a legal safari.

Exactly two decades ago, the Hon'ble Supreme Court, in the case of Empire Industries {1985 (20) E.L.T. 179 (S.C.)}, laid the ratio for the valuation of excisable goods, manufactured on job work basis. In this case, it was held that, for the goods manufactured on job work basis, Excise duty cannot be paid on the processing charges of the job worker – processor alone, but shall be paid on the price at which such goods are sold for the first time in the wholesale market (Para 47 of the said decision). In other words, as per this decision, the goods manufactured on job work basis, shall be assessed to Excise duty on the selling price of the principal. This judgement was rendered by a Bench constituting three Judges.

Then came the famous "Ujagar" series. The Hon'ble Supreme Court in the case of Ujagar Prints {1987 (27) E.L.T. 567 (S.C.)} (Ujagar I), felt that it would be appropriate, if duty is charged on the goods manufactured on job work basis, on the value of materials supplied by the principal plus the conversion charges. It felt and observed that the profit of the customer/principal need not have been taken into account (Para 5 of the judgement). However, in view of the contra decision by a Coordinate Bench in the Empire Industries case, the Bench referred the issue to a five member bench, thus giving birth to Ujagar II {1987 (27) E.L.T. 567 (S.C.)}. In that landmark decision, the Hon'ble Supreme Court upheld the ratio of the Empire Industries case that the duty cannot be charged on the processing charges alone (Para 31 of the judgement). But there was some lack of clarity as to what would be the assessable value, between the two, viz., (a) Intrinsic value of the processed goods i.e. landed cost of raw materials plus the labour charges of job workers or (b) the price at which such goods are sold for the first time in the wholesale market.

This resulted in Ujagar III – {1989 (39) E.L.T. 493 (S.C.)}. In Ujagar III, it was clarified that, in respect of the valuation of goods manufactured on job work basis, the assessable value shall be based on the landed cost of raw materials plus the conversion charges (which also includes the profit of the job worker) and not the ultimate selling price of the customer/principal! Thus, even though the Larger Bench of the Apex Court upheld the ratio of the "Empire Industries" in Ujagar II, while clarifying the same in Ujagar III, it upheld the ratio of Ujagar I. Thus the mummy "Ujagar" mummified the "Empire Industries!"

But there are two crucial elements in the above legal cruise! In all the above cases, (Empire industries and Ujagar I,II &III):

1. The job worker and the principal were **NOT RELATED** persons (or at least there was no allegation on that front!) and
2. There was no **SALE** of goods between the principal and the job worker.

After nearly twenty years, now comes the latest judgement of the Hon'ble Supreme Court in the case of S.Kumar's case { }. If Empire industries and Ujagar prints cases are the First and Second World Wars, the present one is nothing short of the Third World War in the job work valuation! By this present decision, the mummified "Empire Industries" has been given a partial resurrection!

In this recent judgement in the S. Kumar's case, the Hon'ble Supreme Court has written another important chapter on job work valuation. It has now been held by the Hon'ble Apex Court that, if the job worker is "related" to the customer/principal, the principles of Ujagar Prints would not apply and the valuation has to be done with reference to the selling price of the customer, thus partially reviving the Empire ratio! As the issue of job worker being "related" to the principal, had never been the subject

matter before the Hon'ble Apex Court in the Ujagar cases, no impropriety can be complained that the present two member Bench of the Hon'ble Apex Court has not followed the five member decision in Ujagar Prints case.

Now let us understand the applicability of the present decision.

As per section 4 (1) (a) of the Central Excise Act, 1944 the "transaction value" shall be the assessable value, if the following conditions are satisfied, namely,

- There is a sale.
- Delivery at the time and place of removal.
- Assessee and the buyer are not related.
- Price is the sole consideration for sale.

If any of the conditions are not satisfied, as per section 4 (1) (b), recourse has to be made to the Central Excise Valuation Rules, 2000. As in the job work transactions there won't be any SALE, involved, we have to take recourse to the Valuation Rules.

It is not in dispute that the valuation of goods manufactured on job work basis is done only by the residuary Rule of Valuation (Rule 11 – Best judgement). Even the Ujagar principle, owes its origin only to the residuary valuation Rule. Now, there are two landmark decisions on job work valuation. Ujagar – if the job worker is not related and S.Kumar – if the job worker is related. Once recourse is made to the residuary Valuation Rule, to arrive at the assessable value of goods manufactured on job work basis, either of the two decisions have to be applied.

If the job worker is not related – the assessable value shall be the landed cost of raw materials plus conversion charges of the job worker. (Ujagar ratio)

If the job worker is related – the assessable value shall be the selling price of his customer, subject to permissible abatements / deductions. (Empire ratio)

So far so good. But there is a grave threat in the above proposition. As per Section 4 (3) (b) of the Central Excise Act, 1944, the following four classes of persons / entities are considered to be related, namely,

a. Inter-connected undertakings.
b. Relatives (applicable for individuals).
c. Relative and distributor or sub-distributor of such relative distributor.
d. Persons / entities having mutuality of interest.

The said definition shall equally apply to the Valuation Rules and hence shall apply to determine as to whether the job worker is related to the customer/principal or not.

The definition of "inter-connected undertaking" is borrowed from the provisions of MRTP Act, which is sweeping in nature. As per Sec 2 (g) of the MRTP Act, even if one partner is common, then they are inter- connected undertakings. As per Sec 4 (3) (b) of the Central Excise Act, such "inter-connected undertakings" are deemed to be "related" persons. The Rule 10 of the Valuation Rules, which deals with the "interconnected undertakings", has included certain other additional conditions to make such "inter-connected undertakings" to attract the mischief of the "related" person valuation. But the present S.Kumar's judgement speaks only of a "related person" and there are no other conditions attached thereto. If so, as per the judgement, even a plain "inter-connected undertaking" is a "related" person without any additional conditions, which makes everybody under the Sun as "Colonial Cousins!"

No doubt, the Apex Court has held that if the job worker is "related" to the principal, the sale price of the principal has to be considered as the assessable value, at the hands of the job worker. But a careful

reading of the facts of the S.Kumar's case would reveal that, as always, there is a ray of hope seen at the end of the tunnel.

The subject matter of the present decision of the Apex Court is the Tribunal's decision reported in 2000 (117) ELT 439. The following observation from the judgement is very much relevant (Para 3 of the judgement)

> The demand made in the order is on the basis that several firms constituted the S. Kumar's group and these units being either related to S. Kumar's or being intermediary/dummy set up by the group, the transactions among these units cannot be treated as independent commercial transactions and the **prices charged among them** cannot constitute the basis for levy of Central Excise duty.

Now the following extract from Para 2 of the Apex Court decision is also relevant.

> The basis of the demand against the respondents was that they were all firms and companies having a common management and control with **some of them selling grey fabric to the respondent No.1 which, after processing the fabrics, sold the same to some of the other respondents.** The latter ultimately sold the processed fabrics to independent dealers.

From the above, it may be observed that the transaction in this case was **sale** of grey fabrics by the principal to the job worker and **re-sale** of processed fabrics by the job worker to the other units of the principal. **In other words, there was NO JOBWORK at all, in the present S.Kumar's case.** But the ratio of all the cases of Empire Industries and Ujagar Prints, there were no SALE of goods between the principal and the job worker but the goods were given by the principal only a conversion to the job worker. It is highly surprising as to why the Hon'ble Tribunal has applied the ratio of the Ujagar Prints in this case, when the foundation of the case itself is a SALE transaction between the parties and NOT JOB WORK mode at all! In such circumstances, the proper recourse for valuation should have been under Rule 7 of the erstwhile Central Excise Valuation Rules, 1975 (presently Rule 9), whereby, when the goods are sold by an assessee to a related person, as per the said Rule, the assessable value shall be the price at which the related person sells the goods.

Upon appeal, the Hon'ble Supreme Court has now held that the Ujagar principles of valuation are not at all applicable to the present case. As the transaction is by way of sale, only the provisions of Rule 7 of the Valuation Rules, 1975 would apply and not Ujagar Prints. As such, can it be safely concluded that the present decision, which has been rendered in the context of a **sale** transaction by the principal to the processor and a subsequent **resale** by the processor to the related buyers, cannot be applied to a case, where the transaction between the principal and job worker, is purely on a job work basis (i.e. on payment of conversion charges) and not on SALE. In such cases, only the ratio of the "Ujagar" shall apply, irrespective of the relationship!

**Before parting...**

If we go by the above proposition and argue that there shall be no impact of "relationship" in case of pure "job work" transactions but such impact would only be in "sale" transactions, then the term "job work" assumes vital significance! Even though the general meaning of the term " job work" means "to work/process upon the materials given by the principal", it is a common trade practice that the job worker would also be using some of his own raw materials in the processing. For example, in case of dyeing a fabric done on job work basis, the principal would give the grey fabric and the job worker would use the dyes and chemicals, to process the fabrics. It may also be observed that the Hon'ble Apex Court has already held in Prestige Engineering India Limited case – (1994 (73) ELT 497 SC) that if the job worker contributes his own materials, the transaction is not a "job work". In such cases, the transaction

is neither a job work nor a sale! Then which principle of valuation would apply, if the job worker in such cases is related?  Is it Ujagar or S. Kumar's or shall we have to wait for another two decades?