

CLASSIFICATION OF EXCISABLE GOODS

2.1 INTRODUCTION

The actual amount of excise duty payable on excisable goods is, *inter alia*, dependent upon the rate of duty. The rate of duty is determinable on the basis of classification of goods. The classification of goods consists of determining the headings or sub-headings of the Central Excise Tariff under which the said goods would be covered. The classification of goods is also required to be decided for the purposes of determining eligibility to exemptions, most of which are with reference to the Tariff headings or sub headings.

In *Reckitt & Colman of India Vs. CCE 1994 (71) ELT 1144*, Tribunal has held that for the purpose of classification of goods, the nomenclature, character and function of the product is required to be determined and thereafter the excisable product may be identified accordingly with one or the other headings or sub headings with reference to the relative Section Notes and Chapter Notes and Rules of Interpretation.

2.2 CENTRAL EXCISE TARIFF

Prior to 1986, the First Schedule to the Central Excises and Salt Act, 1944 contained a schedule of the goods. This Schedule contained bare descriptions of products, split up into number of items and sub-items relating to each type of commodity. The Central Excises and Salt Act, 1944 also did not provide any guidelines as to the manner in which the said goods were to be classified. Accordingly, the goods used to be classified as per the popular or trade understanding of the same in commercial parlance.

However, from 28th February, 1986, the Tariff Schedule was taken out of the Central Excises and Salt Act, 1944, and a new Tariff Schedule based on the Harmonised System of Nomenclature (popularly known as HSN) was brought into force under an independent enactment called the Central Excise Tariff Act, 1985. HSN is an internationally accepted product coding system formulated under the auspices of the General Agreement on Tariffs & Trade (GATT). This new Tariff Act is modelled along with international practices. The international practice of adopting a uniform classification was done to facilitate a common understanding of products across countries. It consists of two Schedules. First Schedule consists of 96 chapters which group similar class of products under broad sections and specific classes of products under specific chapters. The chapters are arranged classifying all

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goods of a kind beginning with the raw material and ending with the finished products, within the same Chapter. Also, it is designed to group all goods relating to the same industry and all goods obtained from the same raw material under one Chapter in, progressive manner.

The said 96 chapters are grouped into twenty sections. Each of these sections relates to a broad class of goods. For example, section I relates to Animal and Dairy products while Section V relates to Mineral products. Each of these sections has been divided into various Chapters and each Chapter contains goods of a particular class. Each Chapter has been further divided into various Headings, depending upon the different types of goods belonging to the same class of products. This Schedule provides the rates of basic excise duty (CENVAT) leviable on various products.

The Second Schedule specifies the items on which special excise duty is leviable. Second Schedule contains only few items. It has been clarified that the Tariff headings given in the Second Schedule will be interpreted in the same way as those in First Schedule.

Unlike the earlier Central Excise Tariff, the new Central Excise Tariff contains Rules of Interpretation, Section/Chapter Notes and Chapter Sub-Notes giving detailed explanation as to the scope and ambit of the respective Chapter. These notes have been given statutory backing and have been incorporated at the top of each Chapter. Residuary items have been provided separately for each class of goods under each Chapter.

With effect from 28.02.2005, the excisable goods are classified by using 8-digit system. The first two digits refer to the Chapter Number of the Tariff, the next two digits refer to heading of the goods in that Chapter, the next two digits indicate Chapter sub-heading and the last two digits refer to the Chapter sub-sub-heading. Description with eight digits is termed as 'tariff item'.

The 8-digit tariff has a triple dash (---) scheme. If the description of the articles is preceded by a single dash, it means that it is a sub-classification of the immediately preceding heading. If there is double dash or triple dash before a description, it means that it is a sub-classification of the immediately preceding item which has either a single dash or double dash.

Thus, to a considerable extent, the concepts of classification of goods on the basis of popular meaning, commercial parlance or trade understanding has been done away with but to the extent that the goods are not covered by the Section Notes and Chapter Notes specifically, resort must yet to be had to the commercial or trade parlance in order to determine the classification. In its decision in *Akbar Baruddin Jaiwani Vs. CC 1990 (47) ELT 161*, the Supreme Court has held that the express wordings of the Tariff Headings and relevant Section and Chapter Notes would take precedence over the commercial or trade parlance test for classifying excisable goods. However, if the specific headings and notes do not cover the excisable goods, then resort must be had to the commercial or trade understanding of the goods.

The Supreme Court has held in *CCE v. Wood Craft Products Ltd.* 1995 (77) E.L.T. 23 that HSN can be resorted to in case of ambiguity in classifying goods.

2.3 EXPLANATORY NOTES TO THE HSN

The Explanatory Notes to the HSN are the official notes issued by the Customs Co-operation Council, Brussels. They explain and clarify the scope and extent of each and every heading of the HSN, on the basis of which the present Central Excise Tariff has been patterned. It is to be remembered that the Explanatory Notes do not have legal backing, unlike the Chapter Notes and Section Notes contained in the Tariff. Consequently, these Explanatory Notes are only of persuasive value and can be used as an aid to classification of goods when there is ambiguity as to the scope of the entry.

2.4 POWER OF CENTRAL GOVERNMENT TO AMEND FIRST AND SECOND SCHEDULES OF THE TARIFF

The Central Government has the power to amend the Schedules by notification under section 5 of the Central Excise Tariff Act. This is subject to the condition that such amendment shall not alter or affect in any manner, the rates of duty. The provisions of this section are:

(1) Where the Central Government is satisfied that it is necessary so to do in the public interest, it may, by notification in the Official Gazette, amend the First Schedule and the Second Schedule. However, such amendment shall not alter or affect in any manner the rates specified in the First Schedule and the Second Schedule in respect of goods at which duties of excise shall be leviable on the goods under the Central Excise Act, 1944.

(2) Such notifications shall be laid before each House of Parliament, while it is in session, for a total period of thirty days as soon as it is issued. These thirty days may be comprised in one session or in two or more successive sessions. If before the expiry of the session, immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the notification or both Houses agree that the notification should not be issued, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be. However, any such modification or annulment shall be without prejudice to the validity of anything previously done under that notification.

2.5 INTERPRETATIVE RULES TO CENTRAL EXCISE TARIFF

The Central Excise Tariff Act, 1985, contains a set of five general rules for the interpretation of the Tariff Schedules. By and large, these rules for interpretation are identical to those contained in the HSN. Accordingly, the Explanatory Notes issued for these interpretative rules under HSN are also relevant for Central Excise purposes.

However, the Supreme Court in the case of *CCE Vs K.W.H. Heloplastics Ltd.*, 1998 (97) ELT 385 (S.C.) held that classification of goods under particular heading depends upon description, purpose and use of the goods. Therefore, before resorting to interpretative rules, one has to look at the nature, description, purpose and usage of the goods.

2.5.1 Rules for the Interpretation: Classification of goods in the First Schedule shall be governed by the following principles:

1. The titles of Sections, Chapters and Sub-Chapters are provided for ease of reference

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only; for legal purposes, classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and, provided such headings or Notes do not otherwise require, according to the following provisions.

2. (a) Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled.
- (b) Any reference in a heading to a material or substance shall be taken to include a reference to mixtures or combinations of that material or substance with other materials or substances. The classification of goods consisting of more than one material or substance shall be taken to include a reference to goods consisting wholly or partly of such material or substance. The classification of goods consisting of more than one material or substance shall be according to the principles of rule 3.
3. When by application of rule 2(b) or for any other reason, goods are, prima facie, classifiable under two or more headings, classification shall be effected as follows:
 - (a) the heading which provides the most specific description shall be preferred to headings providing a more general description. However, when two or more headings each refer to part only of the materials or substances contained in mixed or composite goods or to part only of the items in a set put up for retail sale, those headings are to be regarded as equally specific in relation to those goods, even if one of them gives a more complete or precise description of the goods.
 - (b) mixtures, composite goods consisting of different materials or made up of different components, and goods put up in sets for retail sale, which cannot be classified by reference to (a), shall be classified as if they consisted of the material or component which gives them their essential character, insofar as this criterion is applicable.
 - (c) when goods cannot be classified by reference to (a) or (b), they shall be classified under the heading which occurs last in numerical order among those which equally merit consideration.
4. Goods which cannot be classified in accordance with the above rules shall be classified under the heading appropriate to the goods to which they are most akin.
5. In addition to the foregoing provisions, the following rules shall apply in respect of the goods referred to therein:
 - (a) camera cases, musical instrument cases, gun cases, drawing instrument cases, necklace cases and similar containers, specially shaped or fitted to contain a specific article or set of articles, suitable for long-term use and presented with the articles for which they are intended, shall be classified with such articles when of a kind normally sold therewith. This rule does not, however, apply to containers which give the whole its essential character;

- (b) subject to the provisions of (a) above, packing materials and packing containers presented with the goods therein shall be classified with the goods if they are of a kind normally used for packing such goods. However, this provision does not apply when such packing materials or packing containers are clearly suitable for repetitive use.
- 6. For legal purposes, the classification of goods in the sub-headings of a heading shall be determined according to the terms of those sub-headings and any related sub-heading Notes and, mutatis mutandis, to the above rules, on the understanding that only sub-headings at the same level are comparable. For the purposes of this rule the relative Section and Chapter Notes also apply, unless the context otherwise requires.

GENERAL EXPLANATORY NOTES

1. Where in column (2) of this Schedule, the description of an article or group of articles under a heading is preceded by “-“, the said article or group of articles shall be taken to be a sub-classification of the article or group of articles covered by the said heading. Where, however, the description of an article or group of articles is preceded by “- -“, the said article or group of articles shall be taken to be a sub-classification of the immediately preceding description of the article or group of articles which has “-“. Where the description of an article or group of articles is preceded by “- -“ or “- - -“, the said article or group of articles shall be taken to be a sub-classification of the immediately preceding description of the article or group of articles which has “-“ or “- -“.
2. The abbreviation “%” in column (4) of this Schedule in relation to the rate of duty indicates that duty on the goods to which the entry relates shall be charged on the basis of the value of the goods fixed, defined or deemed to be, as the case may be, under or in sub-section (2) read with sub-section (3) of section 3 (tariff value) or section 4 or section 4A (MRP) of the Central Excise Act, 1944, the duty being equal to such percentage of the value as is indicated in that column.

ADDITIONAL NOTES

In this Schedule,--

1. (a) “heading,” in respect of goods, means a description in list of tariff provisions accompanied by a four-digit number and includes all sub-headings of tariff items the first four-digits of which correspond to that number;
- (b) “sub-heading”, in respect of goods, means a description in the list of tariff provisions accompanied by a six-digit number and includes all tariff items the first six-digits of which correspond to that number;
- (c) “tariff item” means a description of goods in the list of tariff provisions accompanying either eight-digit number and the rate of the duty of excise or eight-digit number with blank in the column of the rate of duty;
2. the list of tariff provisions is divided into Sections, Chapters and Sub-Chapters

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3. in column (3), the standard unit of quantity is specified for each tariff item to facilitate the collection, comparison and analysis of trade statistics.

2.5.2 Analysis of Rules for Interpretation of the Tariff (Statutory Principles) : Rule 1 states that the titles of sections, chapters and sub-chapters are provided for ease of reference and the determination of where the goods will fall is dependent on the relevant section and chapter notes contained in the Tariff.

Where the Notes are silent, classification will be as per Note 2, 3, 4 and 5 of the Interpretative Rules. It would therefore be noted that Note 2, 3, 4 and 5 will have to be resorted to only if the Chapter does not contain any guide to classify the particular product.

The Tribunal held in *Rajasthan Synthetic Industries Ltd. v. CCE* 1989 (42). E.L.T. 24 that rules for interpretation are not invocable if the section and chapter notes clearly determine the classification.

In *Subhash Photographics Vs. U.O.I.* 1992 (62) ELT 270 it was held that classification has to be determined according to the terms of the headings read with the relevant Chapter Notes and Rules of Interpretation.

Rule 2(a) governs classification of incomplete or unfinished goods. It specifies that if the incomplete or unfinished goods have the essential characteristics of the complete or finished goods, then such goods will be classified in the same heading as the complete goods. Complete or finished goods will cover goods removed in unassembled or disassembled form.

It was held in *MICO Ltd. v. AC* 1992 (62) E.L.T. 13 (Mad.) that only goods requiring minor adjustments would be covered by this interpretative note and if major processes like turning, grinding, broaching, etc. are undertaken, the incomplete goods cannot be classified as complete goods.

Rule 2(b) consists of two parts - the first part relates to the mention of a material or a substance under any heading. The Rules states that the reference to a material or substance shall be taken to include a reference to mixtures of that material or substances. On the other hand, the second part of the rule deals with the goods of a given material or substance mentioned under any heading of the Tariff and states that a reference to a material or substance is to be taken to include a reference to goods consisting of such material or substance. This Rule further says that goods made of several materials or substances shall be classified according to Rule 3.

Rule 3 states that for the purposes of sub-rule (b) of rule 2 or where goods are *prima facie* classifiable under two headings, the following shall be done **sequentially**:

- a. Specific description will have to adopted in place of a general description. This has been adopted by the Supreme Court in *Moorco India Ltd. v. CC* 1994 (74) E.L.T. 5.

This rule further says that if the goods are made up of different materials or substances or parts against which each different headings refer to part only of the materials or substances contained in mixed or composite goods, in such case each of the headings are to be regarded as equally specific in relation to those goods,

even if one of them gives a more complete or precise description of the goods.

- b. Mixtures, composite goods consisting of different materials (generally second part explained above) shall be classified as if they consist of that material or part which gives them their essential character.
- c. When goods cannot be classified in (a) or (b) above, they shall be classified under that heading which occurs last in the numerical order.

Rule 4 says where goods cannot be classified using the above principles, they would be classified under the head appropriate to the goods to which they are most akin. i.e. if a goods cannot be classified according to the above principle, then the goods shall be classified under the heading in which another goods which are mostly similar to the goods in question (akin goods) is classified.

Rule 6 says that after classifying the goods under a specific heading classification under sub-headings under such headings shall be made in accordance with terms of sub-headings, notes to sub-headings and applying the principles as explained above.

2.5.3 Rules for Interpretation – Non-statutory Principles : Apart from the above statutory principles of classification, the Courts have evolved certain non-statutory principles. But it must be understood that statutory principles will have precedence over non-statutory principles.

The Supreme Court in *CCE v. Wood Polymers Ltd.* 1998 (97) E.L.T. 193 held that Rules of interpretation will be preferred to the common parlance test.

In case of variation between section and chapter notes incorporated in the Tariff and in the HSN Explanatory notes, the Section and chapter will always prevail and the classification shall be made in accordance with the tariff only – *Amco Batteries Vs. CCE* 1993 (44) ECR 519 (Tri)

The burden of proving that a particular goods fall in a particular entry will be on the Department as per *Hindustan Ferodo Ltd. v. CCE* 1997 (89) E.L.T. 16 (SC).

Specific to be preferred to general as held in case of *Plasmac Machinery Mfg Co. Ltd. v. CCE* 1991 (51) E.L.T. 161 (S.C.)

Tariff Entry using commercial words to be interpreted as understood in the trade. A different approach may be required where strictly technical or scientific words are used - *Chemical and Fibres of India Ltd. v. U.O.I.* 1997 (89) E.L.T. 633 (S.C.)

Trade understanding to be resorted to if words not defined in the Act - *CCE v. Fenoplast P. Ltd.* 1994 (72) E.L.T. 513 (S.C.)

Goods to classified according to its popular meaning - *Shree Baidyanath Ayurved Bhavan Ltd v. CCE* 1996 (83) E.L.T. 492 (S.C.)

HSN a safe guide to interpretation - *CCE v. Wood Craft Products Ltd.* 1995 (77) E.L.T. 23 (S.C.)

ISI specifications not relevant as compared to circulars issued by trade associations and statutory control orders. - *Indian Aluminium Cables Ltd. v. U.O.I.* 1985 (21) E.L.T. 3 (S.C.)

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ISI specifications not ignorable in the absence of any material - *National Sales Corporation v. CCE* 1995 (78) E.L.T. 653 (S.C.)

Dictionary meaning have limited use and are not safe. - *CCE v. Krishna Carbon Paper Co.* 1988 (37) E.L.T. 480 (S.C.);

2.5.4 Trade parlance Test: According to the Trade Parlance test, if a product is not defined in the Schedules and Section Notes and Chapter Notes of the Central Excise Tariff Act, 1985, then it should be classified according to its popular meaning or meaning attached to it by those dealing with it i.e., in its commercial sense. However, where the Tariff headings itself uses highly scientific or technical terms, goods should be classified in scientific or technical sense.

The Supreme Court in *Akbar Badruddin Jiwani v. CC* [1990] 47 ELT 161 has held that the said doctrine of commercial nomenclature and trade understanding should be departed from in a case where the statutory context in which the Tariff entry appears, requires such a departure.

2.5.5 Burden to prove classification : In *Kirloskar Oil Engines Ltd. Vs. Union of India* (1991) (51) ELT-334, it was held that it is well settled that the burden to establish that certain goods can be classified and excise duty can be levied under a particular tariff item is entirely on the Department. Similarly, in *Union of India Vs. Sahney Steel And Press Works Ltd.* (1992) (58) ELT-38, it was held by the Tribunal that the burden was on the authorities to establish that particular goods fell within a particular item of the Tariff.

Under normal circumstances, it is the responsibility of the Department to establish the correct Tariff Heading under which the product falls. The onus is on the Department to establish the alternate classification, when the Department turns down the one claimed by the assessee. When certain goods are prima facie covered by the generic description, the burden to prove that they are not so covered would be on the person claiming so.

To sum up, the burden to prove a particular classification is initially on the Department and once it is discharged, the onus shifts to the assessee, because it is he who has exclusive and special knowledge about the product produced by him.

2.5.6 Treatment of goods for the purpose of classification and exemption: The meaning of “for the purpose of classification” as well as “for exemption “ should be the same in view of the provisions of section 20 of the General Clauses Act, but the onus of proving dutiability is on the department while in the case of exemption, the burden is on the tax payer claiming the exemption.

In *Eskayef Ltd. Vs. CCE* 1990 (49) ELT- 649, the Supreme Court held that the exemption from payment of a excise duty which has been granted under a Notification is confined to goods falling under a particular Tariff Heading. Merely because a product can be used for the purposes as specified in the exemption notification does not qualify it for exemption, unless it also falls under the Tariff Heading specified in the Notification because the exemption cannot transfer product from one Tariff entry to another. Again, in *Mangalore Chemicals & Fertilisers Ltd. Vs. DC* 1991 (51) ELT 437, the Supreme Court held that the Rules for interpretation of the statute are the same for the purpose of classification and exemption. In *Naffar Chandra Jute Mills Ltd. Vs. Asst. CCE* the Calcutta High Court has held that the Rules for Interpretation of

the Central Excise Tariff are applicable for interpreting exemption notifications as well.

In *Maestro Motors Ltd. 2004 (174) E.L.T. 289*, the Supreme Court has held that if a tariff heading is specifically mentioned in exemption notification, the Rules for Interpretation will apply to such exemption notification. However, if an item is specifically mentioned without any tariff heading, then exemption would be available even though for purpose of classification, it may be something else.

Self-examination questions

1. Discuss briefly the Rules for Interpretation of the Schedules to the Central Excise Tariff Act, 1985.
2. How are the following goods classified under the Central Excise Tariff Act, 1985?
 - (i) Incomplete or unfinished goods having the essential characteristics of finished goods
 - (ii) Finished goods that are removed in an unassembled condition or in a disassembled condition such as semi-knocked down or completely knocked down condition.
3. Does the maxim "Latter the Better" apply in classifying the excisable goods?
4. Explain briefly the meaning of "Trade parlance test" in matters relating to classification under the Central Excise Tariff Act, 1985.
5. Vertex Ltd. manufactures a product known as "MICEL" which is used for killing lice in human hair. Vertex Ltd classifies their product under Tariff sub-heading 3808.10 as an insecticide. However, the Central Excise Officer is of the view that the product is classifiable under Tariff subheading 3003.10 as a medicament as it has therapeutic and prophylactic properties. Vertex Ltd.'s claim is supported by the reports of chemical examiners and the Department of Dermatology & Venereology, which confirm that "MICEL" is an insecticide. Further, various statements of dealers also state that in the market the product is considered to be an insecticide. The claim of the central excise officer is substantiated by the fact that Chapter Note 1(c) of Chapter 38 indicates that Chapter 38 would not cover "Medicaments under Heading No. 3003 or 3004". Chapter Heading 2(i) of Chapter 30 defines "Medicament", *inter alia*, as a product comprising of two or more constituents which have been mixed or compounded together for therapeutic or prophylactic use.

Give your opinion on the issue with the help of decided case laws, if any.

Answers

4. The Central Excise Tariff Act, 1985 incorporates five Rules of Interpretation. Rule 3(c) of the Rules for the Interpretation provides that when goods cannot be classified by reference to rule 3(a) or rule 3(b), they shall be classified under the heading which occurs last in the numerical order among those which equally merit consideration.

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Thus the maxim “Latter the Better” applies in determining the classification of the excisable goods.

5. The facts of the given problem are similar to the case of *Sujanil Chemo Industries v CC.Ex., & Cus., Pune 2005 (181) E.L.T. 206 (S.C.)* wherein the Supreme Court observed that even though, in normal parlance, a product might be considered to be an insecticide if that product had any therapeutic and prophylactic use, but for the purposes of classification, that product could not fall under Chapter 38. The Apex Court clarified that any medicine or substance which treats disease or is a palliative or curative is therapeutic. Therefore, since Licel cured the infection or infestation of lice in human hair, it was therapeutic. Further, it was also prophylactic in as much as it prevented disease which would follow from infestation of lice. Thus, the Apex Court held that ‘Licel’ was a product which was used for therapeutic and prophylactic purposes. It would thus be a Medicament within the meaning of the term “Medicament” in Note 2 of Chapter 30 and would be excluded from Chapter 38.

Applying the ratio of the above decision, “MICEL” will be classified as a medicament under Tariff subheading 3003.10 and not as an insecticide under Tariff sub-heading 3808.10.

