

Non-fulfilment of export obligation - No penalty sans relevant provisions under the FTDR Act – SC

27 May 2024



Summary

The Supreme Court (SC) has set aside a penalty under the Foreign Trade (Development and Regulation) Act, 1992 (FTDR Act), on account of non-fulfilment of export obligation (EO) under a license granted to the assessee. The SC observed that there was no attempt by the assessee to contravene any provisions under the FTDR Act or the Foreign Trade Policy (FTP). Therefore, the SC has held that the penalty, being a strict liability under the penal provision, is deemed unsustainable. Based on the examination of the sanctioned rehabilitation scheme under the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA), the SC noticed that the waiver of payment of specific amounts was for customs duty and not for failure to meet EO under the license granted.

Facts of the case

- Karnataka Malladi Biotics Limited ('the assessee') obtained an export promotion license to import capital goods at a concessional customs duty rate, subject to the condition of exporting finished goods and earning equivalent foreign currency within five years.
- In 1999, the Board for Industrial Finance and Reconstruction (BIFR) declared the assessee a sick unit under the SICA.
- Consequently, the assessee submitted a rehabilitation proposal to the operating agency.
- The commissioner issued a demand notice to demand the differential duty from the assessee because they had enjoyed the benefit of concessional duty.
- However, as the assessee could not pay the duty, the department recovered the amount by enforcing the bank guarantee.
- In 2003, the BIFR sanctioned a rehabilitation scheme for the assessee.
- Subsequently, a penalty was imposed on the assessee for non-fulfilment of the export obligation under the license.
- Aggrieved by the above penalty order, the assessee filed a writ petition before the HC.

- In 2009, the assessee was amalgamated with Emmellen Biotech Pharmaceuticals Limited.
- Consequently, the respondents challenged the writ petition by filing a writ appeal.
- The HC disposed of the appeal by granting permission to withdraw the writ petition with the liberty to file a fresh petition.
- The assessee (post-amalgamation entity) filed a writ petition before the HC, which was dismissed on the ground that the assessee had withdrawn the earlier petition without reserving any liberty to reargue the same issue.

Assessee's contentions

- The assessee contended that due to non-fulfilment of the EO, the rehabilitation scheme was sanctioned by the BIFR, which provided for a waiver of the custom duty and the interest accrued on it. Therefore, a penalty is not leviable in the present case.
- The assessee submitted that the Single Judge and the Division Bench ignored the fact that the assessee was granted the liberty to file a fresh writ petition after withdrawing the earlier.
- The assessee contended that non-fulfilment of the EO under the license is

not grounds for imposing a penalty under Section 11(2) of the FTDR Act. Therefore, the order passed was not valid under the law.

Respondent's contentions

- The respondent contended that the rehabilitation scheme did not include any clause granting a waiver of the penalty that could be imposed for non-fulfilment of the EO under the license.
- The respondent further contended that there was a contravention of the license terms.
- The respondent submitted that they acted within their legal authority by imposing the penalty, as there was a violation of the license terms.

SC's observations and judgement [Civil Appeal No. 6394 of 2024; Order dated 13 May 2024]

- **SC upheld the validity of the writ petition filed by the assessee before the HC:** The SC observed that the HC's Division Bench had explicitly granted the assessee the liberty to file a fresh writ petition on the same cause of action. Therefore, the Division Bench and the Single Judge erred in finding that the first writ petition was withdrawn without seeking permission to file a new one.
- **Penalty imposed is not sustainable:** The SC analysed Section 11(2) of the FTDR Act and observed that it is applicable when any import or export is made or attempted to be made in violation of the provisions of the FTDR Act, rules, orders, or FTP. However, in the present case, the assessee's predecessor had not made or attempted

to make any export or import in contravention of the FTDR Act, rules, orders, or FTP. The allegation was about the failure to fulfil the obligation to export the finished goods within the stipulated period of five years under the license. Since Section 11(2) of the FTDR Act is a penal provision and needs to be interpreted strictly, the demand for imposing penalty could not be sustained, as the alleged violation did not fall within the purview of this section.

- **Appeal allowed:** The SC allowed the appeal in favour of the assessee and set aside the impugned order imposing penalty on the assessee.

Our comments

This significant decision will provide much-needed relief to businesses facing financial challenges and undergoing rehabilitation. It highlights the necessity of exercising compassion and flexibility when enforcing trade obligations.

Earlier, the Delhi HC, in the case of Dencap Electronics Private Limited, had held that a penalty cannot be imposed under Section 11(2) of the FTDR Act in the circumstances where non-fulfilment of the EO was attributable to the factors beyond the control of the assessee and where there is no violation of the provisions of this Act at the time of importation.

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