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When an 'Exemption' Becomes a Tax: SEZ Electricity, Customs Duty and the Constitutional Discipline of Taxation

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1. Introduction

The judgment of the Hon'ble Supreme Court in **Adani Power Ltd. v. Union of India** (*2026-VIL-01-SC-CU*) is not merely a resolution of a fiscal dispute arising out of the Special Economic Zones Act, 2005. It is a constitutional exposition on the anatomy of a valid tax, the limits of delegated legislation, and the institutional discipline required of both the executive and the judiciary once a declaration of law has been rendered. The case is instructive not because it turns on technical construction of tariff entries, but because it exposes the consequences of attempting to impose a levy in the absence of a lawful charging event.

The controversy traverses three foundational planes of public law. First, it interrogates the extent to which the executive may use subordinate legislation, particularly an "exemption" notification, to impose what is in substance a tax. Secondly, it revisits the doctrine of precedent and the binding force of a declaration of law upon coordinate Benches. Thirdly, it reinforces the constitutional obligation of the State to give full effect to judicial pronouncements, rather than attempting to reassert, through altered form or reduced rate, a levy already declared to be without authority of law. The judgment thus situates itself at the intersection of fiscal jurisprudence and constitutional discipline.

2. Factual Background

The appellant operates a coal-based thermal power plant of approximately 5,200 MW capacity located within the Mundra Special Economic Zone in Gujarat, where it functions as a co-developer. Electricity generated from this plant is partly consumed within the SEZ and substantially supplied to purchasers in the Domestic Tariff Area, including State electricity utilities. This factual matrix is critical, for the movement of electricity in question is not transnational but entirely intra-national, albeit across a fiscally distinct zone.

The architecture of the SEZ Act accords a special fiscal treatment to notified zones with the objective of encouraging exports, manufacturing, and infrastructure creation. At the same time, the statute seeks to maintain parity between goods imported into India and goods cleared from an SEZ into the domestic economy. This parity is achieved through Section 30 of the SEZ Act, which provides that goods removed from an SEZ into the DTA shall be chargeable to customs duties "as if such goods had been imported into India."

Prior to 2009, electrical energy imported into India attracted customs duty at a nil rate under the Customs Tariff Act. Correspondingly, electricity generated within an SEZ and supplied to the DTA did not suffer any independent customs duty. The regulatory scheme already addressed concerns of misuse of duty-free inputs through Rule 47(3) of the SEZ Rules, 2006, which required neutralisation of the customs duty benefit on inputs proportionate to electricity cleared outside the SEZ. Importantly, the law did not impose a customs duty on electricity itself.

The controversy arose when Notification No. 25/2010-Cus. was issued on 27 February 2010. Though couched as an "exemption" notification under Section 25 of the Customs Act, it in effect introduced a customs duty of 16% ad valorem on electricity cleared from an SEZ to the DTA, with retrospective effect from 26 June 2009. On the basis of this notification, demands were raised upon the appellant not merely prospectively but for a past period, prompting the first round of constitutional challenge.

3. Decision 1: The 2015 Judgment and the Declaration of Law

In its judgment dated 15 July 2015 [*2015-VIL-645-GUJ-CU*], the Gujarat High Court undertook a detailed examination of the constitutional and statutory foundations of the levy. The Court held that the charging provision for customs duty lies in Section 12 of the Customs Act, read with Entry 83 of List I of the Seventh Schedule. Section 12 contemplates a levy on goods "imported into India." The Court found that electrical energy generated within India in an SEZ and transmitted to the DTA does not, in substance, constitute an import into India.

The High Court clarified that an SEZ, though fiscally distinct, is not a foreign territory. The deeming fiction in Section 30 of the SEZ Act allows ascertainment of the rate of duty applicable to comparable imports; it does not convert an intra-national supply into an act of import. In the absence of an identifiable taxable event, the levy failed at the threshold. This was not a case of procedural irregularity but a jurisdictional defect going to the very authority to tax.

The Court further examined the character of Notification No. 25/2010-Cus. It found that although framed as an exemption, the notification in truth operated as an instrument to impose and quantify a new levy. Section 25 of the Customs Act is a beneficent provision conferring power to relax or remit duty; it does not authorise the creation of a tax. To use it as a source of levy was held to be a colourable exercise of delegated power.

Equally significant was the Court's finding on retrospectivity. The fastening of a 16% ad valorem duty from 26 June 2009 through subordinate legislation violated Article 265 of the Constitution, which mandates that no tax shall be levied or collected except by authority of law. The High Court also found the levy to be arbitrary, as the scheme already ensured reversal of input duty benefits under Rule 47(3) of the SEZ Rules. Imposing customs duty again on the

electricity output resulted in a double burden. On these grounds, the levy was struck down for the period from 26 June 2009 to 15 September 2010. This judgment was affirmed by the Supreme Court, and the review petition was dismissed.

4. Decision 2: The Attempt to Confine a Declaration of Law

Despite the 2015 declaration, the Union continued to collect per-unit customs duty on electricity cleared from the SEZ to the DTA under Notification Nos. 91/2010-Cus. and 26/2012-Cus., albeit at reduced rates and prospectively. The appellant, having paid these amounts under protest, sought a declaration that no customs duty was leviable even for the subsequent period and sought refund.

In its 2019 judgment [*2019-VIL-317-GUJ-CU*], the High Court declined relief, holding that the 2015 judgment was confined to a particular notification and period. This approach effectively reduced a constitutional declaration of law to a notification-specific relief. Aggrieved, the appellant approached the Supreme Court.

5. Supreme Court's Analysis: Ratio Decidendi and Its Reach

The Supreme Court categorically rejected the narrow construction placed on the 2015 judgment. It held that the High Court in 2015 had rendered findings on four foundational aspects: the absence of a taxable event under Section 12 of the Customs Act; the misuse of the exemption power under Section 25; the impermissibility of retrospective levy; and the arbitrariness inherent in the structure of the levy. These findings collectively constituted the ratio decidendi.

The Court emphasised that the 2015 judgment was not temporal but structural. It did not merely strike down a particular rate or notification; it identified the absence of authority to levy customs duty on SEZ-to-DTA electricity clearances under the then-existing statutory framework. In the absence of any material

change in law or facts, that declaration governed all periods standing on the same footing.

6. Delegated Legislation and the Doctrine of Colourable Exercise

A central theme of the judgment is the reaffirmation of limits on delegated legislation. The Supreme Court reiterated that a delegate cannot do indirectly what it has no authority to do directly. The power to exempt is not a power to tax. Section 25 of the Customs Act cannot be used to enlarge the field of taxation or to invent a levy which Parliament has not imposed.

The Court underscored that delegated legislation is subject to judicial review not only for unreasonableness but also for purpose. Where the dominant purpose for which a power is conferred is departed from, the exercise is ultra vires. Subsequent notifications which merely alter the rate or prospective application of the levy cannot cure the foundational illegality. Where the root is bad, every derivative iteration is equally bad.

7. Section 30 of the SEZ Act and the Parity Principle

The Supreme Court clarified the true nature of Section 30 of the SEZ Act. It is a parity clause, not a charging provision. It mandates that goods cleared from an SEZ into the DTA bear the same customs duty as would be applicable if those goods were imported into India. If imported electrical energy attracts nil duty, SEZ-generated electricity must attract the same incidence. Any attempt to impose duty on SEZ electricity alone creates an artificial and constitutionally suspect classification, offending both Section 30 and Article 14.

8. Judicial Discipline and Coordinate Benches

The Court also addressed the discipline required of coordinate Benches. Once a Bench of equal strength has declared the law, a subsequent Bench is bound to follow it. If the later Bench doubts its correctness or applicability, the only permissible course is to refer the matter to a larger Bench. It cannot sidestep or

narrow the earlier declaration. The High Court's approach in 2019 was therefore held to be impermissible.

9. Restitution and Consequential Relief

Once it was held that the levy itself was without authority of law, the Supreme Court concluded that the State could not retain amounts collected under such levy. Restitution was held to be a necessary incident of illegality. The respondents were directed to refund the amounts collected for the period from 16 September 2010 to 15 February 2016, without interest.

10. Conclusion

The judgment in *Adani Power Ltd* stands as a decisive reaffirmation that the power to tax is not a matter of executive convenience but of constitutional command. It reminds us that taxation is anchored not in nomenclature or form, but in authority, substance, and statutory legitimacy. An exemption notification cannot be transformed into a charging instrument; a deeming fiction cannot be stretched beyond its purpose; and a levy once declared to be without authority of law cannot be resurrected through successive notifications bearing altered rates or prospective veneers.

Equally significant is the Court's insistence on judicial discipline and finality-constitutional courts must not permit executive re-litigation of settled questions under the guise of fresh instruments. In insisting upon restitution as a necessary incident of illegality, the Supreme Court restores equilibrium between State power and taxpayer rights. The decision therefore transcends the immediate dispute on SEZ electricity and customs duty, and emerges as a constitutional milestone-one that reinforces the rule that in fiscal matters, as in all exercises of public power, legality must precede levy, and authority must precede collection.

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