
(1965) 10 GUJ CK 0018
In the Gujarat High Court
Case No : Sales Tax Reference No. 14 of 1965

Bhogilal Laxmichand	Vs	APPELLANT
The State of Gujarat		RESPONDENT

Date of Decision : 15-10-1965

Acts Referred:

Bombay Sales Tax Act, 1959 — Section 2(28)

Citation : (1966) 18 STC 141

Hon'ble Judges : J.M. Shelat, C.J.; P.N. Bhagwati, J

Bench : Division Bench

Advocate : S.L. Mody, for the Appellant; A.D. Desai, Assistant Government Pleader and M.G. Doshit, Additional Government Pleader, for the Respondent

Judgement

Shelat, C.J.—The assessees at whose instance this reference is made are a firm holding a registration certificate. During the relevant period,

i.e., Samvat Year 2017 (from 31st October, 1960, to 8th November, 1961), the assessees entered into certain transactions with four persons to

finance purchases of certain motor vehicles from Messrs Prem Nath Motors (P.) Ltd. of New Delhi. In the case of three out of these four

transactions, the hirers paid all the instalments under their respective agreements with the assessees and as provided in those agreements exercised

thereunder the option to purchase the vehicles. The Sales Tax Officer assessed these three transactions, but not the fourth transaction, as sales of

motor vehicles, and both the Assistant Commissioner and the Sales Tax Tribunal in appeals filed against the assessment confirmed the order of

assessment.

2. The contentions urged by the assessees before the Tribunal were (1) that these transactions were merely financing agreements though the

agreements were in the form of hire-purchase agreements; (2) that therefore, they did not fall within the definition of "sale" as defined by section

2(28) of the Bombay Sales Tax Act, 1959, and (3) that even if these transactions were sales, the business of the assessee being in piece-goods

they were causal sales and therefore the assessee could not be said to be dealers in motor vehicles. All the three contentions were rejected by the

Tribunal and this reference challenges the correctness of that decision.

3. All the three transactions in question were evidenced by documents. Since the procedure followed in all these agreements was the same, it will

be sufficient if we examine one of them as typical of the rest.

4. Messrs N. B. Patel & Co., who may be described as hires, first selected a motor truck to be purchased from the said Messrs Prem Nath

Motors (P.) Ltd. and then made a proposal dated 11th August, 1960, in writing to the assessee to finance the purchase. The proposal inter alia

stated that "If you accept and agree to advance me/us a loan, I/we for security of the loan to be advanced to me/us hereby agree to sign the usual

agreement and to enter your name in R.T.O. records of my/our vehicle in specially hire-purchase clause as a matter of further security." The usual

agreement referred to in this proposal obviously was the usual hire-purchase agreement. On the same day, i.e., on 11th August, 1960, the

assessee and the said Messrs N. B. Patel & Co. entered into an agreement referred to in the said proposal which recited that the proposal was

to be the basis of the contract under which, as has already been stated, the assessee in consideration of their agreeing to finance the purchase

were to be treated as the owners of the vehicle to be purchased. Clause 1 of the agreement provided :- "The owners, being the owners of the

motor vehicle with fittings, tools and accessories and additions more particularly described in the schedule hereto and hereinafter collectively called

"the vehicle" agree to let and the hirer agrees to hire the vehicle from the date hereof subject to the terms and conditions herein contained and

hereto annexed and which shall be taken and read as part of this agreement." Clause 2 provided that on the execution of the agreement, the hirer

should pay to the owners in cash a sum of rupee one in consideration of option to purchase given to the hirer by clause 4 of the agreement. Clause

3 provided that the hirer shall pay to the owners in Ahmedabad (i.e., the

assessee) on execution of the agreement the sum of Rs. 9,620 as initial payment ""by way of hire which shall become the absolute property of the owners and will punctually pay to the owners at their address for the time being in Ahmedabad, and without previous demand the sums mentioned in the margin thereof by way of rent for the hire of the vehicle the first payment to be made on the date mentioned therein and the subsequent payments on or before the same date in the succeeding months unless the hirer shall have terminated this agreement as hereinafter provided."" Clause 4 provided that if the hirer were to duly perform and observe all the terms and conditions set out in the agreement and on his part to the performed and observed and were in manner aforesaid to pay to the owners monthly sums by way of rent together with the aforesaid amount of Rs. 9,620 to be paid on the execution of the agreement and pay to the owners all other sums of moneys payable under the agreement the hiring should come to an end and the vehicle should at the option of the hirer become his property and the owners would make over all their rights, title and interest in the same to the hirer; but until the owners made over all their rights, title and interest to the hirer the vehicle should remain the absolute property of the owners. The sums mentioned in the margin in the agreement aggregated to Rs. 20,000 payable as aforesaid by monthly instalments of Rs. 2,000 each and this amount was over and above the amount of Rs. 9,620, being the initial payment, the total payment thus to be made by the hirer being Rs. 20,000 plus Rs. 9,620 equal to Rs. 29,620. The rest of the agreement dealt with the guarantee for the performance of this agreement by a surety which we do not recite here as we are not concerned in this reference with that part of the transaction. The hirers also executed a promissory note in favour of the assessee for an amount of Rs. 22,000 as a collateral security, the amount of Rs. 22,000 consisting of Rs. 20,000 being the aggregate of the ten instalments and Rs. 2,000 being interest payable on that amount. Thus, the hirers in all would have to pay the amount of Rs. 22,000 over and above the sum of Rs. 9,620 payable by them as initial payment on the execution of the agreement. As shown by the sale voucher of Messrs Prem Nath Motors (P.) Ltd., the truck was purchased on the next day, i.e., 12th August, 1960, for an amount of Rs. 30,495. That voucher was issued in the name of Messrs N. B. Patel &

Co., but in view of the assesseees having financed the purchase on the aforesaid agreement dated 11th August, 1960, having been executed by the

assesseees on the one hand and Messrs N. B. Patel & Co. on the other, the voucher expressly stated that the purchase was subject to ""H.P. (i.e.,

hire-purchase) with Messrs Pari Bhogilal Laxmichand."" The sale price of Rs. 30,495 consisted of Rs. 28,500 being the price of the truck and Rs.

1,995 as the sales tax. The assesseees produced before the Sales Tax Officer a copy of the account of Messrs N. B. Patel & Co. in their books of

account. That account shows that Rs. 32,521 were debited to Messrs N. B. Patel & Co., that amount consisting of the aforesaid sum of Rs.

30,495, Rs. 2,000 being the finance charges and Rs. 26 being the stamp on the hundi drawn by the assesseees in favour of Messrs Prem Nath

Motors (P.) Ltd. The amount of Rs. 9,620 being the initial payment made by Messrs N. B. Patel & Co., was credited to them.

5. Mr. Mody who appears for the assesseees contended that the transaction entered into by the parties was a purely financing transaction though

the form adopted by the parties was a hire-purchase agreement and therefore the transaction could not amount to a sale and was wrongly assessed

to tax. The first question that we have to determine, therefore, is whether the transaction in question is a financing transaction or whether it is a hire-

purchase agreement as contended by the revenue.

6. A hire-purchase agreement, though in essence a contract of payment, is in actual practice something more than hiring simpliciter, for it contains

elements of both bailment and sale. Such a hire-purchase agreement is of two kinds, (1) where the contract is of hire conferring an option to the

hirer to purchase, and (2) it is in reality a contract to purchase a movable property by instalments subject to the condition that the property in the

chattel is not to pass until all instalments are finally paid. In the latter case, there is a binding obligation on the hirer to purchase, while in the former

there is merely an option to purchase. If there is reserved to the hirer power to return the goods, either during the hiring, thereby determining the

bailment, or after the conclusion of the hiring and before the payment of such further sum as is required to complete the purchase, the agreement is

not a contract of sale but an agreement to hire with an option to buy. A hire-purchase agreement thus is an agreement for the bailment of goods

under which the bailee may buy the goods or under which the property in the goods will or may pass to the bailee. When the property in the goods passes to the bailee on his exercising the option, the bailment comes to an end and the transaction then becomes one of sale. (See Halsbury's Laws of England, Third Edition, Volume 19, pages 510 to 511). But Mr. Mody's argument was that, though the form of the transaction adopted by the parties was the hire-purchase form, what the Court has to ascertain is the essence and substance of the transaction and not the form and if it was necessary to examine and ascertain the substance of the transaction entered into by the parties, it would be found that the transaction in substance was not a hire-purchase transaction but a financing agreement. The question then is, what in substance and essence the transaction in question amounts to ? Mr. Mody's contention was that Messrs N. B. Patel & Co. first made a proposal to purchase and the assessee entered into the agreement in question, not for the purpose of hiring out the vehicle to the hirer and ultimately selling it to them, but only for the purpose of securing repayment of the loan advanced by them to the hirers. Now it is true that the transaction was initiated with a proposal by the hirers for a loan to be advanced by the assessee but it must be remembered that the whole transaction was pushed through on that very day and the agreement between the parties was executed simultaneously with the aforesaid proposal so that it is not as if we can, in trying to ascertain the substance or the essence of the transaction, look at the proposal in isolation divorcing it from what the parties did at the same time and simultaneously. Looking at the transaction in that light, though Messrs N. B. Patel & Co. first selected the truck proposed to be purchased and made a proposal for a loan to put through that purchase and executed a promissory note for Rs. 22,000 in favour of the assessee, they also entered into on the basis of that proposal and agreement whereunder they agreed that though the purchase was to be made by them from Messrs Prem Nath Motors (P.) Ltd., the property in the truck was to pass to and remain in the assessee and the assessee was for all practical purposes and also for the road transport records to be the owners of the truck until all the instalments and other moneys due by them to the assessee were paid and they exercised the option to purchase the truck for which the consideration fixed under the agreement was Re. 1. The agreement thus in substance and essence was not merely

a financing agreement. Though the assesseees agreed thereunder to finance the purchase by giving to Messrs N. B. Patel & Co. a loan of Rs.

20,000, the agreement was something more than a financing arrangement, for under the agreement the hirers agreed that the property in the truck

was to vest in the assesseees and the assesseees were to be the owners of the truck and their name was to be in consequence recorded as owners in

the records of the road transport authorities and Messrs N. B. Patel & Co. were to be the merely hirers. The legal effect of this agreement, therefore,

was that so long as the hiring continued, though the truck in question was to be in possession of Messrs N. B. Patel & Co., they could not and

were not entitled to pass title thereunder to a third party. As already seen, the agreement then provided that if the hirers, over and above the initial

payment made by them to the assesseees, were to pay all the instalments set out in the margin in the agreement and other moneys payable

thereunder, they were to be entitled to exercise the option to purchase the truck. Thus, in fact and in substance though the transaction may be said

to have commenced with the proposal for financing, it was up to a certain stage a hiring agreement ultimately ending, on payment of all instalments

and the exercise of option provided therein by the hirers, in a contract of sale. On the happening of these events, the agreement thus would be a

contract of sale and would be then amenable to tax under the Sales Tax Act. This conclusion is reinforced by the manner in which the assesseees

maintained the account of Messrs N. B. Patel & Co. in their books of account. That account clearly demonstrates that the transaction was not

merely a financing transaction. Had it been so, the only amount actually advanced to Messrs N. B. Patel & Co. being Rs. 20,000 paid by draft,

that amount and Rs. 2,000 as interest calculated in advance would have been debited to Messrs N. B. Patel & Co. But what was done in the

account was to writ up the account of the transaction of purchase on the footing that the purchase was made by the assesseees. That was why the

whole of the price of the truck, namely, Rs. 30,495 was first debited to the hirers though actually only Rs. 20,000 were advanced. As against the

amount of Rs. 30,495, the sum of Rs. 9,620 was credited, that being the initial payment made by the hirers to the assesseees. Similarly, an amount

of Rs. 895 paid by the hirers in case was first credited and a corresponding debit entry had to be made, for, it would appear that that amount was

directly paid by the hirers to the vendors. The account thus clearly shows that the assesseees themselves did not treat the transaction as a mere financing transaction. Since the loan was made on the basis of hire-purchase agreement, the account had to be maintained and was in fact maintained on that basis. The ownership in the truck also was agreed to vest in the assesseees, not merely as security for the loan but because of the agreement by way of hire-purchase under which ownership was to remain with the assesseees until the conditions set out in the agreement were satisfied. There is no dispute that in terms of the agreement the name of the assesseees was entered in the records of the R.T.O. as owners of the truck. There is equally no dispute that Messrs N. B. Patel & Co. as hirers paid up all the instalments and other moneys due by them under the agreement to the assesseees and in terms of the agreement also exercised the option to purchase the truck. Therefore, on the happening of these events, there can be no manner of doubt, that they became the purchasers of the truck and the aforesaid agreement thus can be said to have matured into a contract of sale, the contract of bailment having come to an end on the exercise of the option by Messrs N. B. Patel & Co.

7. In a case on all fours with the present case in *Johar and Co. v. Deputy Commercial Tax Officer* ([1965] 16 S.T.C. 213.), the transaction in question was almost exactly similar to the one before us and the Supreme Court held that the transaction amounted to a sale which was assessable to the tax under the Madras General Sales Tax Act, 1939. The appellant there was a financing company, whose business was to advance moneys to persons to purchase motor vehicles but were themselves not in a position to find ready money to pay the price. A person desirous of acquiring a motor vehicle made a selection of the vehicle, fixed its price with the motor dealer and then approached the appellant for financial assistance on hire-purchase basis. The practice followed by the appellant was that sometimes an initial payment was made by the hirer to the motor dealer which was taken into account at the time of hire-purchase agreement, while in others the payment was made in a number of instalments to the appellant. In either case the appellant paid the price or the balance thereof to the dealer and thereafter the hire-purchase agreement was entered into between the appellant and the person purchasing the motor vehicle. The agreement provided, as did the agreement before us, that the owner (i.e., the

appellant) would let and the hirer, i.e., the person who wanted to purchase the vehicle, would take on hire the vehicle for a certain period. The

hirer had to pay, during the period of hire, the monthly instalments, keep the vehicle in good condition, pay all taxes, licence fees, and other charges

payable in respect of the vehicle and could not sell, charge, pledge or part with possession of the vehicle. If the hirer made default in the payment

of any rent for seven days, the hiring was to be determined immediately and the owner might, without notice, retake possession of the vehicle.

Clause 20 in that agreement was somewhat similar to clause 4 of the agreement before us and provided that if the hirer were to duly observe and

perform all the conditions and stipulations and were to duly pay to the owner all rents reserved under the agreement during the terms of hiring

together with all sums, if any, payable by him to the owner under the provisions of the agreement, then and at the termination of the hiring, the hirer

might purchase the vehicle from the owner for a sum of Re. 1. As in this case, the vehicle was registered in the name of the owner and the hirer

was forbidden to represent himself as the owner thereof. The Supreme Court held that the agreement was a hire-purchase agreement which on the

happening of certain events set out therein matured into a contract of sale. The Supreme Court observed that a hire-purchase agreement had two

elements, (1) element of bailment and (2) element of sale in the sense that it contemplated an eventual sale. The element of sale fructified when the

option was exercised by the intending purchaser after fulfilling the terms of the agreement. The taxable event under the Act would be the sale of

goods and until that taxable event took place, there could be no liability to pay tax. Mr. Mody, however, tried to distinguish this decision by urging

that there was not in the initial stage a proposal made by the hirer, that is to say the intending purchaser, for financing the purchase. In principle,

however, that fact does not make any material difference, for what we have to ascertain in this reference is what was the transaction in its

substance and in essence. As has already been stated, the transaction has to be looked into in its entirety. It may be that the transaction had its

genesis in the proposal for financing but what the parties ultimately did and agreed to was to enter into the usual hire-purchase agreement, the terms

whereof provided that on the hirer exercising the option and paying all instalments and other moneys due under the agreement, he would purchase

the truck in question, the transaction thus maturing or ending in actual sale of the motor truck in question. That being so, it is not possible to accept

the contention raised by Mr. Mody that the transaction in question did not amount to a hire-purchase agreement ending in a sale. Questions Nos. 1

and 2, therefore, must be decided against the assesseees.

8. As regards question No. 3, Mr. Mody argued though somewhat faintly that even if the transactions were to be held as sales, the business of the

assesseees being in textile goods it would not be possible to treat the assesseees as dealers in motor trucks and that the transactions in question

should be held as casual transactions. He also argued, relying upon our decision in *Ambica Mills Ltd. v. State of Gujarat* ([1964] 15 S.T.C. 367.),

that the test of volume and degree of frequency was not a conclusive test and that the transactions in any event being very few, it would not be

possible to hold that the assesseees were dealers in motor trucks. The three transactions which were brought to assessment by the Sales Tax

Officer in all aggregated to the amount of Rs. 96,000. These transactions cannot be held to be casual sales as they were made in pursuance of

regular dealings with parties who desired to purchase motor trucks but at the moment were not in a position to pay the entire sale price therefor.

Unlike the case in *Ambica Mills Ltd.* ([1964] 15 S.T.C. 367.), the trucks in the present case were not purchased with the original intention on the

part of the assesseees either to use them for their personal needs or for their use in the normal business carried on by them as dealers in piece-

goods. Besides, there can be no gainsaying that these agreements were entered into so that a fairly considerable amount of interest could be earned

on the amounts deployed by the assesseees in these transactions. Therefore, there was a consistent course of dealings perceived in each one of

them showing how these amounts and interest thereon were secured first by making the hirers to apply for a loan, then making purchases of motor

trucks, retaining ownership therein till the entire amounts together with interest thereupon were eventually paid up and then transferring property

therein to the hirers on such hirers exercising their option. The transactions thus had features giving to them the distinctive character of a business

and therefore they cannot be regarded as merely occasional sales. Nor would it be incorrect to say that the assesseees were dealers in motor trucks

in so far as these transactions were concerned. The third question, therefore, also has to be decided against the assesseees.

9. For the reasons set out above, our answers to the questions are as follows :-

Question No. 1 : The transactions were hire-purchase agreements and not financing agreements.

Question No. 2. in the affirmative.

Question No. 3 also in the affirmative.

10. The assesseees will pay to the State of Gujarat costs of this reference.

11. Reference answered accordingly.