
(2011) 02 KL CK 0095

In the High Court Of Kerala

Case No : S.T. Rev. No's. 30 and 69 of 2004

Enviro Chemicals

APPELLANT

Vs

State of Kerala

RESPONDENT

Date of Decision : 10-02-2011

Acts Referred:

Constitution of India, 1950 — Article 286, 366

Kerala General Sales Tax Act, 1963 — Section 2, 2(21), 5, 5(1), 5(3)

Citation : (2011) 1 KLT 1060 : (2011) 39 VST 434

Hon'ble Judges : J. Chelameswar, C.J.; K.M. Joseph, J.; A.K. Basheer, J

Bench : Full Bench

Advocate : V.V. Asokan and K.I. Mayankutty Mather, for the Appellant; K. Vinod Chandran, Spl. Government Pleader, for the Respondent

Judgement

K.M. Joseph, J.—The matter comes up before us on the basis of a Reference by a Division Bench. We extract the Order of Reference as hereunder:

The question raised is whether the service rendered by the Petitioner in the form of chemical treatment of effluent water for the awarder amounts to sale of goods in the execution of works contract. Petitioner has developed a chemical product by name "Envirofloc" which is used as a chemical for effluent treatment. During the years 1988-89 and 1989-90, for which the issue arises, the Petitioner carried out pollution control treatment for Madura Coats Limited, Koratty, which is a known company engaged in manufacture of yarn. There may be massive pollution of water on account of dye-application on yarn. In the course of effluent treatment entrusted to the Petitioner, the Petitioner applies the chemical Envirofloc and it either gets used up in the treatment of effluent water probably by neutralising colour, ordour, etc. Petitioner's case is that no transfer or sale has taken place in the execution of works contract. The department's case is that material is consumed in the process of effluent treatment and it gets transferred in the course of such treatment and there is sale of goods involved in the execution of works contract which under the definition includes processing,

preparing, improvement etc. Counsel for the Petitioner cited before us the decision of the Division Bench of this Court in *The Deputy Commissioner of Sales Tax (Law), Board Of Revenue (Taxes), Ernakulam v. M.K. Velu* (89 STC 40), wherein this Court following the decision of Patna High Court held that there is no sale of goods in the display of fireworks done by the contractor on behalf of the awarder. Even though this Court has followed the decision of the Patna High Court in the case of pest control, strangely the definition of works under KGST Act is not referred to by Division Bench in their judgment. Another decision of this Court cited by counsel for the Petitioner is that of a single Bench in *Dynamic Industrial And Cleaning Services (P) Ltd. v. State of Kerala and Anr.* 1994 (2) KLT 188 : (1995) 97 STC 564 which is case of cleaning of boiler with cleaning aids, which the Court found not taxable under the Act. The Government Pleader cited latest decision of the Supreme Court In *Tata Consultancy Services v. State of Andhra Pradesh* 2005 (1) KLTSU 13 SC : (2004) 137 STC 620, and *B.S.N.L and Anr. v. Union of India and Ors.* 2006 (3) KLT SN 45 SC : (2006) 145 STC 91 wherein the Supreme Court followed the case in *Associated Cement Companies Ltd. v. Commissioner of Customs* (2001) 124 STC 59 and the case reported in *Rainbow Colour Lab and Anr. v. State of Madhya Pradesh* 2000 (2) KLTSN 13 SC : (2000) 118 STC 9. It was held by the Supreme Court that in order to attract sales tax, there need not be transfer of any tangible goods. The contract of the nature arising in this case also involves two stages. One supply of goods and the other services rendered with such goods. The Petitioner utilises the chemical for treatment of the effluent and brings out an improvement of the effluent quality, conform it with the parameters prescribed by Pollution Control Board for the awarder to retain their licence. Certainly it is processing of the effluent done by the Petitioner with the materials used by him. The point of transfer of goods to the awarder is by way of appropriation to the contract that is the application of the materials in the water which brings out the desired result, though in the process it gets consumed. Petitioners cited a Division Bench decision of this Court in *Ajanta Colour Lab v. State of Kerala* 1999 (2) KLT 445 and Anr. judgment of this Court in *Southern Cable And Engineering Works v. State of Kerala* 2002 (1) KLT SN 56 . We feel these judgments do not reflect the correct law by virtue of later decisions of the Supreme Court referred above. Moreover, Petitioners' is a case where the product used in effluent treatment is not transferred to the awarder, but consumed in the course of treatment. Having regard to the importance of the issue and since Division Bench judgments above referred apparently are against later decisions of the Supreme Court referred above, we feel the matter requires to be decided by a Full Bench of this Court.

Accordingly these cases are referred for decision by Full Bench.

Registry will place the matter before the Chief Justice for posting the matter before a Full Bench.

2. The Petitioner in both these cases stands assessed to tax under the Kerala General Sales Tax Act, 1963 (hereinafter referred to as the Act) on the alleged

sale of materials involved in the execution of works contract. The works contract involved is one of effluent treatment at the Madura Coats Limited (hereinafter referred to as the Awarder). When the matter came up before us, the learned Counsel for the Petitioner produced before us an account of the actual process involved, according to him. It reads as follows:

The wastewater generated from various sections of the factory is first passed through a screen chamber for removing large particles. After screening, the wastewater is collected in a collection tank to make the characteristics of waste water uniform. Till this stage, the process is done by the Company itself.

From the collection tank, the wastewater is pumped at a uniform rate to the flash mixer and subjected to chemical treatment. The Chemical is a combination of Ferrous Sulphate, Ferrous Chloride and Sulphuric Acid. These Chemicals obtained by the Petitioner from effluents discharge from Travancore Titanium Products. An addition of required dosage of lime is also added. The chemical mixture is named by the Assessee as Envirofloc. Due to this, coagulation of the suspended particles and precipitation of dissolved organics take place. The solid particles settled at the bottom and the clear liquid overflows. The overflow from the Clariflocculator is taken to the aeration tank and subjected to activated sludge process. Oxygen is supplied by means of surface aerators.

The overflow from the aeration tank is sent to the hopper bottom settling tank. The outlet of the secondary settling tank is the treated effluent is discharged to the river and it will be odorless. It will not contain chemicals or any pollutant.

3. We heard Shri K.I. Mayankutty Mather, learned Counsel for the Petitioner and Shri Vinod Chandran, learned Special Government Pleader for taxes, State of Kerala.

4. Learned Counsel for the Petitioner would contend that there is no transfer of property in the chemical as goods or in any other form to the Awarder. It is submitted that the chemical is used up or consumed and as is stated in the Petitioner's version of what transpires, the treated water is discharged into the river. It is contended that the chemical is not at all transferred to the Awarder. He would contend that while it is true that by the 46th amendment to the Constitution, Clause 29(A) has been added to Article 366, it does not empower a State to levy tax on a works contract. Unless there is a transfer of property in the goods as goods or in any other form involved in the execution of works contract, no sales tax is leviable. He relied on the decisions of this Court in *The Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. M.K. Velu* (89 STC 40), *Dynamic Industrial And Cleaning Services (P) Ltd. v. State of Kerala and Anr.* 1994 (2) KLT 188 : (1995) 97 STC 564 which have been referred to by the Division Bench in the Order of Reference, as laying down the correct law. He would further contend that the law laid down in *Tata Consultancy Services Vs. State of Andhra Pradesh*, *Bharat Sanchar Nigam Ltd. and Anr. v. Union of India and Ors.* 2006 (3) KLT SN 45 SC : (2006) 145 STC 91, *Associated*

Cement Companies Ltd. v. Commissioner of Customs (2001) 124 STC 59 and Rainbow Colour Lab and Anr. v. State of Madhya Pradesh and Ors. 2000 (2) KLT SN 13 (C. No. 15) : (2000) 118 STC 9, namely that there need not be transfer of any tangible goods, is inapplicable to the facts of this case. He would submit that he has no quarrel with the proposition (and he can have none) that sales tax can be levied even on the transfer of intangibles. He took us through the Judgments of the Apex Court in Builders Association of India and Ors. v. Union of India and Ors. (1989) 73 STC 370 and Bharat Sanchar Nigam Ltd and Anr. v. Union of India and Ors. 2006 (3) KLT SN 45 SC : (2006) 145 STC 91 and contended that there was no transfer of property in the chemical, and that the law does not permit a mere works contract to be taxed. He would submit that the principle "*quicquid plantatur solo, solo cedit*" which means that the property in all materials and fittings once incorporated or affixed to a building will pass to the free holder cannot apply to the facts of this case. He illustrates the principle by pointing out that if in the course of a building contract, a lock is fixed to a door, the property in the lock would pass to the employer and the taxing event has occurred and the completion of the construction need not be awaited for rendering the transaction exigible to tax. In this case, he would point out that the Petitioner uses the chemical in question which is consumed as there is no trace of the chemical in the effluent and what is more, the Awarder does not even get back the water, as the water containing effluents is, after treatment, discharged into the river.

5. Per contra, Shri K. Vinod Chandran, learned special Government Pleader would press for our acceptance the principle "*quicquid plantatur solo, solo cedit*". He would also submit that this is a case where, even going by the version of the Petitioner, property in the chemical is transferred to the Awarder, the moment it is put into the effluent. The fact that it is subsequently consumed, would not absolve the Petitioner of his liability to pay tax, as there is a transfer of property in the goods, as there is delivery of the chemical before it is consumed. He would also point out that the version of the Petitioner which we have extracted, would show that he has obtained the various chemicals from the effluent which are discharged from the Travancore Titanium Products. No doubt, there is an addition of the required dosage of lime. He would submit that it cannot be in the region of any doubt that the chemical in question is goods, within the meaning of the Act and since the only contention of the Petitioner is that there is no transfer of the said goods, the matter is covered by the Judgment of the Apex Court in Xerox Modicorp Ltd. v. State of Karnataka (2005) 142 STC 209. We shall refer to the said decision in greater detail as much turns on the applicability of the principle enunciated therein to the facts of this case.

6. Petitioner has been entrusted with a works contract. A works contract can be an indivisible contract consisting of components of labour and service, as also sale of goods. Entry 54 of List II of the VIIth Schedule to the Constitution enables the State Legislatures to enact legislation providing for levying and collecting tax in respect of sale or purchase of goods. A Constitution Bench of the

Apex Court in *State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd.* (1958) 9 STC 353 took the view that the expression "sale of goods" must be understood in the sense in which it is understood under the Sale of Goods Act. It was further held that if there was only an indivisible works contract, the State could not split up the indivisible contract and levy tax on any sale of goods which may take place thereunder. The matter finally engaged the attention of the Law Commission of India and acting upon its suggestions, the Parliament enacted the 46th Amendment whereunder Clause 29A was added to Article 366 of the Constitution. Clause 29A reads as follows:

(29A) : "tax on the sale or purchase of goods" includes:

(a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;

(b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;

(c) a tax on the delivery of goods on hire purchase or any system of payment by instalments;

(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

(e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;

(f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration,

and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made.

The Apex Court has held that the effect of the insertion of Clause 29 A is the enlargement of the concept of sale, so that State Legislatures were enabled to tax the transactions covered by Sub-clauses (a) to (e) of Clause 29A. However, the Apex Court has further held that any legislation providing for levying tax on such deemed sales will be subject to the trammels of Article 286 of the Constitution and any other law to which a law providing for sales tax is otherwise subject to See *Builders Association of India and Ors. v. Union of India and Ors.* (1989) 73 STC 370. There cannot be any sales tax on a works contract per se even after the 46th Amendment to the Constitution. There must be transfer of property in goods, as goods or in any other form. This alone can be the basis for

levying tax in respect of sale of goods involved in the execution of a works contract. No doubt, as held by the Apex Court, after the 46th Amendment, it is open to the Taxing Authority to split up an indivisible works contract and tax the transfer of property in goods, as provided for in the Amendment.

7. In the case of *Tata Consultancy Services v. State of Andhra Pradesh* 2005 (1) KLT SN 13 SC : (2004) 137 STC 620 the question which arose was whether incorporeal or intangible property can be treated as goods. The Court held, *inter alia*, as follows:

The term "goods", for the purposes of sales tax, cannot be given a narrow meaning. Properties which are capable of being abstracted, consumed and used and or transmitted, transferred, delivered, stored or possessed, etc., are "goods" for the purpose of sales tax. The test to ascertain whether a property is "goods" for the purposes of sales tax is not whether the property is tangible or intangible or incorporeal. The test is whether the concerned item is capable of abstraction, consumption and use and whether it can be transmitted, transferred, delivered, stored, possessed, etc. In the case of software, both canned and uncanned all of these are possible. Intellectual property when it is put on a media becomes goods.

The Apex Court in this regard, followed the view taken in *M/s. Associated Cement Companies Ltd. Vs. Commissioner of Customs*, . In *BSNL and Anr. v. Union of India* and Ors. 2005 (1) KLT SN 13 SC : (2006) 145 STC 91, the Apex Court was again dealing with the question as to the scope of the word "goods". The Court quoted the decision in *Tata Consultancy Services v. State of Andhra Pradesh* 2005 (1) KLT SN 13 SC : (2004) 137 STC 620 with approval. In *Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. Thomas Stephen & Co. Ltd.* 1987 (1) KLT 161 : (1987) 66 STC 34, a Division Bench of this Court was considering a case u/s 5A(1)(b) of the Act providing for levy of purchase tax. Therein, the dealer, a manufacturer of tiles, purchased cashew shells for fuel for the kiln in the factory, and lime shells and certain stores described as consumed stores for use in maintenance of the kiln and factory. The Court took the view that goods used for ancillary purposes, like fuel or for maintenance were not comprehended within Section 5A(1)(a) of the Act. It was also held that it did not attract liability to tax u/s 5A(1)(d), as there was no transfer of title in the goods in question, as they could not be said to be disposed of otherwise than by way of sale in the State. Against the same, no doubt, the Apex Court dismissed the application for special leave by a speaking order in its decision in *Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. Thomas Stephen & Co. Ltd.* 1988 (1) KLT 568 (SC) : (1988) 69 STC 320. Section 5A(1)(a) and 5A(1)(b) of the Act read as follows:

5A : Levy of purchase tax:- (1) Every dealer who, in the course of his business, purchases from a registered dealer or from any other person any goods, the sale or purchase of which is liable to tax under this Act, in circumstances in which no tax is payable under Sub-sections (1), (3), (4) or (5) of Section 5 and either:

(a) consumes such goods in the manufacture of other goods for sale or otherwise; or

(b) uses or disposes of such goods in any manner other than by way of sale in the State.

In *The Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. M.K. Velu* ((1993) 89 STC 40), the Court was considering a case where the Assessee was a fire works manufacturer and exhibitor. He displayed fireworks. The transaction of display of fire works was sought to be brought to tax. The matter related to the assessment years 1984-1985 to 1988-1989. The Court held as follows:

So, we hold that the contract was for the display of fireworks. The only further question is whether the Appellate Tribunal was justified in holding that no transfer of property takes place in the display of fireworks. As the explosives are consumed, nothing tangible remains, in which property could be transferred. It is a matter of common knowledge that in the display of fireworks, the explosives are spent and do not remain, once the display takes place. In the process of execution of the work, the goods themselves (explosives) ceased to exist. No tangible property remains. So, there could be no transfer of property. We concur with the decision of the Patna High Court in *Pest Control India Ltd. v. Union of India* (1989) 75 STC 188. There can be no transfer of property unless the goods themselves exist. That is not the case herein.

8. In *Dynamic Industrial And Cleaning Services (P) Ltd. v. State of Kerala and Anr.* 1994 (2) KLT 188 : (1995) 97 STC 564, a learned Single Judge of this Court considered the question as to whether when chemicals were used by the Petitioner therein in the business of cleaning boilers in thermal power stations and fertilizer plants and the chemicals used as cleaning agent were extinguished in the process, sales tax could be levied in the matter. The Court found that the chemicals used were consumed in the process of cleaning and removing the impurities in the plants, no goods were produced or come into existence and thereafter the Court proceeded to hold as follows:

2. A bare perusal of the above Explanation is sufficient to show that transfer of property in goods (whether as goods or in some other form) is the sine qua non for its application. The mere execution of a works contract does not by itself attract liability for tax under the Act unless it is accompanied by transfer of property in goods, involved in the execution of the contract. The emphasis is on the transfer of property in goods - *Builders Association of India and Others Vs. Union of India (UOI) and Others*, . When goods used in the process of executing a works contract are consumed in the process, as in the case of the chemicals used by the Petitioner or fuel and power, there is no transfer of any goods from the contractor to the awardee of the contract attracting liability to tax. "I draw inspiration for this conclusion from the decision of this Court in *Deputy Commissioner of Sales Tax v. Thomas Stephen and Co. Ltd.* (1987) 66 STC 34 :

1987 (1) KLT 161 (paragraph 5) which was affirmed by the Supreme Court in Deputy Commissioner v. Thomas Stephen & Co. Ltd. (1988) 69 STC 320 : (1988 (1) KLT 568 (paragraph 12).

Learned Counsel for the Petitioner also brings to our notice the decision of this Court in Teaktex Processing Complex Limited v. State of Kerala 2003 (3) KLTSN 64 (C. No. 87) : (2004) 136 STC 435. Therein, the Court was dealing with a case of a Company engaged in the business of undertaking job works of bleaching and dyeing of yarn and fabrics obtained from its customers. The Court found that after the processing of fabrics by using dyes, the dyes existed in the form of colour and, therefore, the item dye could not be treated as a consumable u/s 5C(1)(c)(iii) of the Act. The Court, inter alia held as follows:

Section 5C(1)(c)(iii) of the Kerala General Sales Tax Act, 1963 specifically excludes the cost of consumables used in the execution of works contract not involving any transfer of property in goods and actually incurred in connection with the execution of the works contract. If the items which are used in the process are existing in any form in the resultant product, then there is a transfer of the item used as goods exigible to tax under the Act. But, if the item which is used in the process is not in existence in any form in the end-product, then it can be treated as a consumable. Section 5C itself makes the position clear by specifying "not involving any transfer of property in goods and actually incurred in connection with the execution of works contract.

In Ajantha Colour Laboratory v. State of Kerala 1999 (2) KLT 445, a Division Bench of this Court was dealing with cases of Photographers and the controversy was whether their activities could be subjected to sales tax under the Act. The Court divided the categories into three. They are:

- (1) take photograph of customer, develop the negative and supply positive prints in the desired size to the customer;
- (2) develop the exposed film brought by the customer, take positive prints from them and supply negative and the prints in the desired size to the customer,
- (3) take positive prints from the negative brought by the customer and supply the prints in the desired size to the customer along with negative.

The Court proceeded to hold that in the first category, there was no works contract, while the second and third categories would be works contract. Learned Counsel for the Petitioner also brings to our notice a recent decision of a Division Bench of this Court in Microtrol Sterilization Services Pvt. Ltd. v. State of Kerala 2009 (3) KLT SN 14 : (2009) 26 VST 213 (Ker.). Therein, the facts were as follows:

The Petitioner was engaged in sterilization of goods, i.e. goods were made free of germs. This was done with the use of ethylene oxide, a toxic, highly inflammable gas. The tools to be sterilized were exposed to the gas and then the gas was released after neutralising it with carbon-dioxide. The Court held as follows:

Consumables are items which are lost in the course of execution of works contract, In other words, they are used up in the process of executing the work. Admittedly, after sterilisation, the goods do not retain any trace of ethylene oxide which was completely released in the air, Therefore, there was no transfer of ethylene oxide from the Petitioner to the customers in the course of sterilisation of the goods, On the other hand, it was used up as a consumable in the service rendered by the Petitioner, the value of which had to be excluded in the determination of taxable turnover of works contract u/s 5C of the Act. No tax was leviable on the value of ethylene oxide used in sterilisation work.

The Court drew support from the decision of the Patna High Court in *Pest Control India Ltd. v. Union of India* (1989) 75 STC 188 and the decision of this Court in *Deputy Commissioner of Sales Tax v. Velu* (1993) 89 STC 40 (Ker).

9. Now, it is necessary to refer to certain provisions of the Act. Section 2(viii), inter alia, provides for the definition of "dealer" as including a person who carries on the business of executing works contract, inter alia, and Clause (f)(2) provides that a person who, whether in the course of business or not, transfers property (whether as goods or in some other form) involved in the execution of a works contract is also to be a dealer. "Sale" has been defined in Clause 2(xxi) as follows:

2(xxi) : "Sale" with all its grammatical variations and cognate expressions means every transfer, whether in pursuance of a contract or not of the property in goods by one person to another in the course of trade or business for cash or for deferred payment or other valuable consideration, but does not include a mortgage, hypothecation, charge or pledge.

Explanation (3A) has been inserted and it reads as follows:

A transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract shall be deemed to be a sale.

Explanation (1A) has been inserted in relation to the definition of the word "turnover" in Clause 2(xxvii) and it reads as follows:

Explanation (IA)(i): The turnover in respect of works contract shall be the aggregate amount received or receivable by the dealer for the transfer of goods (whether as goods or in some other form) involved in the execution of such contract).

"Works Contract" has been defined in Clause 2(xxix-a) which reads as follows:

"Works Contract" includes any agreement for carrying out for cash or for deferred payment or other valuable consideration the construction, fitting out, improvement, repair, manufacture, processing, fabrication, erection, installation, modification or commissioning of any movable or immovable property.

The Apex Court in *Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others*, held, inter alia, as follows:

The value of the goods involved in the execution of a works contract will, therefore, have to be determined by taking into account the value of the entire works contract and deducting therefrom the charges towards labour and services which would cover:

- (a) Labour charges for execution of the works;
- (b) amount paid to a sub-contractor for labour and services;
- (c) charges for planning, designing and architect's fees;
- (d) charges for obtaining on hire or otherwise machinery and tools used for the execution of the works contract;
- (e) cost of consumables Such as water, electricity, fuel, etc. used in the execution of the works contract the property in which is not transferred in the course of execution of a works contract; and
- (f) cost of establishment of the contractor to the extent it is relatable to supply of labour and services;
- (g) other similar expenses relatable to supply of labour and services;
- (h) profit earned by the contractor to the extent it is relatable to supply of labour and services.

The amounts deductible under these heads will have to be determined in the light of the facts of a particular case on the basis of the material produced by the contractor.

In the aftermath of the decision of the Apex Court in Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, , Section 5(C) was inserted. Section 5C of the Act reads as follows:

5C.(1) Deduction of certain amounts in arriving at the taxable turnover of a dealer in respect of transfer of property in the execution of works contract : The taxable turnover of a dealer in respect of the transfer of property involved in the execution of works contract shall, from the 1st day of April, 1984 be arrived at after deducting the following amount from the total amount received or receivable by the dealer for the execution of the contract

- (a) xxxxxxxx
- (b) xxxxxxxx
- (c) all amounts towards labour charges and other service charges such as
 - (i) xxxxxxxx
 - (ii) xxxxxxxx
 - (iii) cost of consumables used

(iv) xxxxxxxx

(v) xxxxxxxx

not involving any transfer of property in goods, and actually incurred in connection with the execution of the works contract; or such amounts calculated at the rate specified in column (3) of the Table below, if they are not ascertainable from the books of accounts maintained and produced by the dealer.

Section 5 which is the charging Section reads, inter alia, as follows:

5. Levy of tax on sale or purchase of goods: (1) Every dealer (other than a casual trader or agent of a non-resident dealer) whose total turnover for a year is not less than two lakh rupees and every casual trader or agent of a non-resident, whatever be his total turnover for the year, shall pay tax on his taxable turnover for that year:

(iv)(a) : In the case of transfer of goods involved in the execution of works contract where transfer is in the form of goods at the rates and at the points specified against such goods in the First, Second or Fifth Schedule.

(b) In the case of transfer of goods involved in the execution of works contract (where the transfer is not in the form of goods but in some other form) specified in the Fourth Schedule, at the rate specified against such contract in the said Schedule.

10. Interestingly, we may notice that while Clause 29A of Article 366 which provides that the transfer of property in goods, whether as goods or in some other form, involved in the execution of a works contract, is followed up by incorporation of Explanation 3 A to Section 2(21) of the Act on similar lines and the concept of "sale" is so expanded, when it comes to Explanation 1A to Section 2(xxvii) defining the word "turnover" in respect of works contract to be the aggregate amount received or receivable for the transfer of goods, whether as goods or in some other form, involved in the execution of such contract. We notice that in Explanation 1 A, there is no reference to transfer of property in goods and what is provided for is transfer of goods, of course, whether as goods or in some other form, involved in the execution of such contract. Even in the charging Section, namely Section 5, Clauses 4(a) and 4(b), the words used are "transfer of goods involved in the execution of a works contract." Section 5, Clauses 4(a) and 4(b) do not contain the words "transfer of property in goods". But, we notice that in the definition of "taxable turnover", it is stated as follows:

Provided that the taxable turnover of a dealer in respect of transfer of property involved in the execution of works contract shall, from the 1st day of April, 1984 be arrived at after deducting the amounts mentioned in Section 5C.

Section 5(1) which really is the charging Section provides for levy of sales tax on the taxable turnover. In this case, since the transfer of goods is alleged to be in the form of goods, the Authorities have brought the Petitioner to tax as

"chemicals".

11. On the one hand, learned Counsel for the Petitioner would contend that the chemical in question must be treated as a consumable as it is consumed in the effluent treatment process, on the other hand, Shri K. Vinod Chandran, learned Special Government Pleader for taxes, would contend that it may not be accurate to describe the chemical in this case as a consumable, the value of which is liable to be deducted going by the decision of the Apex Court as also the provisions of Section 5C of the Act which we have adverted to. Shri K. Vinod Chandran would illustrate the principles by giving the following examples:

He would submit that if a builder make use of water while mixing cement with other components as a building material, it would partake the characteristic of a raw-material and it would become part of the structure itself. In other words, when water is so used, it cannot be treated as a mere consumable as the water when employed as aforesaid, it is transferred to the awardee. He would submit that if on the other hand, water were to be used for curing the structure, it could be said that water is used as a consumable. He would submit, in other words, that if goods are used as raw-materials, then the mere fact that it is consumed, that would not detract from the transfer of goods being exigible to tax. He would, of course, submit that the decisions rendered in *Tata Consultancy Services v. State of Andhra Pradesh* 2005 (1) KLT SN 13 SC : (2004) 137 STC 620 and *BSNL and Anr. Union of India and Ors.* 2006 (3) KLT SN 45 SC : (2006) 145 STC 91 really dealt with the question as to whether intangibles could be goods and the said principle may not really have a bearing on the issue to be decided by us. Learned Special Government Pleader would contend that the matter should be concluded with reference to the decision of the Apex Court in *Xerox Modicorp Ltd. v. State of Karnataka* (2005) 142 STC 209. The facts have been set out by the Apex Court as follows:

The Appellants are a public limited company doing business in Xerox machines, parts and accessories, as part of its business. After the Xerox machine is sold to a customer, if the customer so desires, the Appellants enter into one of the two types of agreements, namely, either a Full Service Maintenance Agreement (FSMA) or a Spares and Service Maintenance Agreement (SSMA). In FSMA the Appellants take on the responsibility of fully maintaining the machine, servicing it and if necessary replacing parts. The Appellants also supply material, like toners and developers. They charge at the rate of 0.27 paise per copy produced by the machine. Under the SSMA, the Appellants agree to maintain the machine including replacement of parts if necessary, for a lumpsum of Rs. 7,000 per annum. However, the costs of toners, developers, etc. are to be borne by the customer.

Thereafter, the Court proceeded to hold as follows:

16. We have considered the rival submissions. As set out hereinabove, the word consumable in Explanation 1 to Section 6(4) refers to such items which get

consumed before the property in the goods can pass. We are informed that toners and developers are liquids which are put in the Xerox machine. They perform, to put it simply, the same function as ink in printers.

17. Thus, for the extra stock, there is a provision which provides that it is left in trust. However, once the toner and developer are put into the machine, they are no longer in trust. This is because the property in the toner and developer passed the moment they are put into the Xerox machine. Now, they belonged to the customer. At this stage, they are tangible movables in which property can pass. This is clear from the provision that the Appellants will charge for unaccounted stock at prevailing prices. That they are goods in which property can pass is also clear from the fact that in the SSMA the customer has to buy the toner and developer, if as now claimed they are consumables in which property cannot be transferred how are the Appellants charging for toners and developers in our view. Mr. Iyer is right. The sale i.e. transfer of property takes place before the goods are consumed. The transfer takes place in respect of tangible goods. Just like petrol is consumed after sale or ink is consumed after sale, in this case also the toners and developers get consumed after sale. The property passes the moment they are put in the machine. At that stage, they are not consumed, but are tangible goods in which property can pass.

The Court, we notice, has referred to the decisions of this Court in Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. M.K. Velu (1993) 89 STC 40 (Ker.) and Dynamic Industrial and Cleaning Services (P) Ltd. v. State of Kerala and Anr. 1994 (2) KLT 188 : (1995) 97 STC 564 (Ker). Explanation 1 to Rule 6(4) of the Karnataka Sales Tax Rules reads as follows:

For the purpose of Clauses (m) and (n) of Sub-rule (4), "labour" and other like charges include charges for obtaining on hire or otherwise machinery and tools used for execution of works contract, charges for planning, designing and architects, cost of consumables used in the execution of works contract, cost of establishment to the extent relatable to supply of labour and services and other similar expenses relatable to supply of labour and services.

The Apex Court has also referred to the decision in Pest Control India Ltd. v. Union of India and Ors. (1989) 75 STC 188 (Pat.).

12. Interestingly, in the Karnataka Sales Tax Act, 1957, the word "dealer" is defined as including a person engaged in the business of transfer of property in goods, whether as goods or in some other form, involved in the execution of a works contract (See Section 2(k), Clause (viii)). "Sale" is defined as including a transfer of property in goods, whether as goods or in some other form involved in the execution of a works contract (See Section 2(t)). "Turnover" is defined in Section 2(v) as meaning the aggregate amount for which goods are bought or sold or supplied or distributed or delivered or otherwise disposed of in any other ways referred to in Clause 2(t) by a dealer either directly or through another, on his own account or on account of others, whether for cash or for deferred

payment or other valuable considerations. There are other provisions which may not be relevant. Subject to such conditions and restrictions, if any, as may be prescribed in this behalf, Explanation (ii) includes any sum charged for anything done by the dealer in respect of the goods sold at the time of or before the delivery thereof.

13. After having considered the entire case law cited before us and on a conspectus of the provisions, we would think that the learned Special Government Pleader is right in his contention based on the decision of the Apex Court in Xerox Modicorp Ltd's case (supra). It is no doubt true that the contract as such is not placed before us, if it is one which is reduced to writing. But we will proceed on the basis that the process involved is substantially the same as has been indicated by the Assessee and which we have extracted. It is undoubtedly true that even after the 46th amendment sales tax cannot be levied merely because there is a works contract. There must be transfer of property in the form of goods or otherwise than in the form of goods. What is taxable is the transfer of property in goods (See the definition of sale in the Act in this regard). It does not matter whether the transfer of property takes place in the form of goods or in any other form. It is undoubtedly also true that in view of the decision of the Apex Court in Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, that the cost of consumables involved in works contract cannot be taxed.

14. That the chemical in question is goods, is beyond doubt. It cannot be disputed that the Assessee was the owner of the goods in question, namely the chemical. It is obviously the intention of the parties that the Assessee must use the chemical in the effluent treatment process. It is equally indisputable that the Assessee has actually used it. No doubt, in the Judgment of the Apex Court in Xerox Modicorp Ltd. v. State of Karnataka (2005) 142 STC 209, the Apex Court found that the toners and developers are liquids put into the Xerox machine and they perform essentially the same function as ink in the printers and the Court also relied on the provision in the contract that the Assessee in the said case would charge for the unaccounted stock at prevailing prices. By using the chemical, the Petitioner/Assessee rendered the effluent compliant with the standards. It could probably be said that in the case of the toner and developers as the function is that of ink in printers, it shows up in the final product of the xerox machines. But, the decision of the Apex Court is not based on there being any requirement that the items which are used should exist in any form in the resultant product which is the principle laid down by this Court in Teaktex Processing Complex Limited v. State of Kerala (2003 (3) KLT SN 64 : (2004) 136 STC 435 and also in Microtrol Sterilization Services Pvt. Ltd v. State of Kerala 2009 (3) KLT SN 14 : (2009) 26 VST 213 (Ker).

15. We would think that the principle "quicquid plantatur solo, solo cedit" is a principle which is apposite in the context of a building and engineering contract. We get the following Account of the principle "quicquid plantatur solo, solo cedit":

The well-known principle is that the property in all materials and fittings, once incorporated in or affixed to a building, will pass to the free-holder *quicquid plantatur solo, solo cedit*. As soon as materials of any description are used in a building or other erection, they cease to be the contractor's property and become that of the free holder. The employer under a building contract may not necessarily be the free-holder, but may be a lessee or licensee, or even have no interest in the land at all, as in the case of a sub-contract. However, once the builder has affixed materials, the property in them passes from him, and at least as against him, they become the absolute property of his employer, whatever the latter's tenure of or title to the lands. The builder has no right to detach them from the soil or building, even though the building owner may himself be entitled to sever them as against some other person - for example tenant's fixtures. Nor can the builder reclaim them if the building owner or anyone else has subsequently severed from the soil.

Materials worked by one, into the property of another, becomes part of that property. This is equally true whether it be fixed or moveable property. Bricks built into a wall becomes part of the house, thread stitched into a coat which is under repair, or planks and nails and pitch worked into a ship under repair, become part of the coat or the ship. Until, however, the materials are actually built into the work, in the absence of some stipulation intended to pass the property in them, when delivered on the site, they remain the property of the contractor, notwithstanding that they might have been approved by the employer or his agent or brought into the site unless the agreement between the parties evinces a clear intention to the contrary.

We would think that the said principle as such may not advance the case of the Revenue in a case where the works contract involves the effluent treatment process wherein chemical is poured into the effluent.

16. When the assessee has used it, will it remain the owner of the chemical any longer? Will not the property in the goods pass to the awardee? We would think that the moment the Assessee pours the chemicals into the effluent, he will cease to be the owner and at that point of time the awardee must be deemed to have taken delivery of the same. In our view the fact that upon it being poured into the effluent, it loses its identity and that it is consumed will not detract from the fact that there is delivery of the same to the awardee. The Assessee does not have a case that the effluent belongs to the Assessee. We do not think that it can be their case that the effluent does not belong to the awardee. Let us pose a question, if a complaint by a third party is raised about the treated effluent, can the awardee absolve itself of the ownership of the same? We would think, it may not be possible. Therefore we would be justified in holding that the effluent and the treated effluent both belonged to the awardee. It is, therefore, into the property of the awardee, namely the effluent that the Assessee supplies the chemical. The Apex Court in its decision in *Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others*, had, inter alia, held that cost of consumables,

such as, water, electricity, fuel etc. used in the execution of the works contract, the property in which is not transferred in the course of execution of a works contract, is to be deducted. In Section 5C also, the words "not involving any transfer of property in goods" have been incorporated. Just like the toner and developer having been put into xerox machine becoming the property of the customer in the case before the Apex Court in Xerox Modicorp Ltd. case and the sale taking place before the goods are consumed, in the same way, the property in the chemical passed to the awarder the moment they are put into the effluent by the Assessee and its subsequent consumption is the consumption after sale and it does not detract from the factum of sale and consequently the exigibility to tax becomes unquestionable.

17. In both these Revision Petitions, no doubt, a question of law is raised concerning the correctness of the rate of tax applied. This is not mentioned in the Order of Reference as such. This was not argued before us by the learned Counsel appearing for the parties. In such circumstances, we answer the Reference by holding that there was indeed a sale of chemical involved in the execution of the works contract, in view of the Judgment of the Apex Court in Xerox Modicorp Ltd v. State of Karnataka (2005) 142 STC 209, as there is delivery of the same to the awarder by virtue of the chemical being poured into the effluent. The Revision Petitions will be posted before the concerned Bench for disposal of the same.

A.K. Basheer, J.

18. I have had the privilege of going through the Order prepared by esteemed brother Justice Joseph. But I am unable to concur with the view taken by my esteemed brother. Hence this separate Order.

19. As has been noticed already, the question that has cropped up for consideration is whether there is any "transfer of the property in goods" coming within the ambit of "sale" as defined under the Kerala General Sales Tax Act, 1963 (for short "the Act") in the course of treatment of waste water by applying a combination of some chemicals known as "Envirofloc" formulated by the Petitioner.

20. The Revenue contended that there was transfer of property in the chemicals used by the Petitioner in the process of effluent treatment and therefore the works contract undertaken by the Petitioner fell within the dragnet of Section 5 of the Act. According to the Revenue, it was immaterial that there was no tangible by-product other than the effluent-free water, but, going by the provisions contained Explanation (3A) in Section 2(xxi), it would be sufficient, if the transfer is either "as goods or in some other form". The Sales Tax Appellate Tribunal accepted the above contention raised by the Revenue and repelled all the contentions raised by the Petitioner.

21. There can be no controversy that the cost of consumables used in the execution of a works contract is not exigible to tax. Section 5(C)(1Xc)(iii)

introduced in the Act following the judgment of the Apex Court in Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, also postulates that the cost of consumables is liable to be deducted while arriving at the taxable turn over of a dealer in respect of transfer of property in the execution of works contract. But the Revenue lays heavy emphasis on the words "whether as goods or in some other form" employed in the Act in Explanation (3A) u/s 2(xxi) while defining "sale" and also in Explanation (1A) u/s 2(xxvii) which defines "turn over" and contends that the chemicals used by the Assessee being tangible goods, there occurs transfer of property when the chemicals react with the waste water for the purpose of cleansing it. It is contended by Sri. Vinod Chandran, learned Special Government Pleader (Taxes) that the chemicals used by the Assessee are not by any stretch of imagination, "consumables" as envisaged in Section 5(C)(1)(c)(iii) of the Act.

22. It has already been noticed that "Envirofloc" is a combination of a few chemicals like Ferrous Sulphate, Ferrous Chloride and Sulphuric Acid formulated by the Petitioner in a certain ratio for the purpose" of effluent treatment. According to the Petitioner, a small quantity of lime is also added to the above chemical combination in the course of the treatment process. I do not propose to refer to the actual process of waste water treatment being carried out by the Petitioner, yet again, since the procedure has been already extracted in the earlier part of the judgment.

23. It is on record that the polluted/impure water which comes out of the Plant in M/s. Madura Coats Limited is subjected to effluent treatment by the Petitioner on the strength of a works contract awarded to it. It is the admitted position that the waste water which is ridden off all impurities and pollutants after the treatment, is let out to the river. Admittedly the treated water does not contain any traces of chemicals. The case of the Revenue is that "the property in the chemicals" used by the Petitioner for the purpose of treatment gets transferred to the awarder and therefore such transfer falls within the ambit of Explanation (1A) of Section 2(xxvii) which defines "turn over" thereby attracting exigibility to tax u/s 5 of the Act.

24. It is contended by the Revenue that the chemicals used for the purpose of effluent treatment are totally consumed in the process. It is immaterial whether or not the transfer of goods in the chemicals is in a tangible or some other form. The fact that the chemicals used by the Petitioner/Assessee acted as the sole contributory or "reacting agent" for the purpose of cleansing the waste water cannot be denied at all. It may be true that the end product viz., the clean water is let out into the river after the process of elimination of the polluting agents; but still the awarder is benefited inasmuch as the obligation on his part not to pollute the river by the chemical agents from the plant and machinery in the factory is fulfilled. Thus it is contended by Sri. Vinod Chandran, the learned Special Govt. Pleader, that going by the definition clause of "sale" in Section 2(xxi) read with explanation (3A) and "turnover" in Section 2(xxvii) read with

Explanation (1A) thereunder, it is clear that the Petitioner is liable to be assessed under the Act.

25. Per contra, it is contended by Sri. Mayankutty Mather, learned Counsel for the Petitioner that the above proposition is totally misconceived and untenable. It is puerile for the Revenue to contend that the chemicals used by the Petitioner for treatment of the polluted water is not a consumable as envisaged u/s 5C(1)(c) (iii) of the Act. The chemical product (Envirofloc) that is being used by the Petitioner gets rid of all the pollutants in the contaminated water through a chain of chemical action and reaction. In that process, the chemicals get consumed and the polluting agents are removed. Resultantly, there will be no trace of any harmful chemical elements in the pollution free water that is let out to the river.

26. The short question is whether or not the combination of chemicals known as "Envirofloc" used by the Petitioner for effluent treatment is a "consumable" as envisaged u/s 5(C)(1)(c)(iii) of the Act.

27. In *Dynamic Industrial and Cleaning Services (P) Ltd. v. State of Kerala and Anr.* 1994 (2) KLT 188 : (1995) 97 STC 564, the question that came up for consideration was whether there was any transfer of property in goods while cleaning of boilers in plants like Thermal Power Station, Fertiliser Complexes etc. by using chemicals like Citric Acid, Hydrochloric Acid etc. This Court after referring to various other decisions on the point held thus:

...It (the Petitioner) carries out the work of cleaning the boilers and accessories; using chemicals like citric acid, hydrochloric acid and the like after determining the precise type of cleaning agent to be used in the particular plant, by inspection or laboratory tests. The Petitioner employs its own machinery, labour and material for carrying out the work. The chemicals used are consumed in the process....

3. The chemicals are being used by the Petitioner only in aid of the work undertaken by it, as a cleaning agent for cleaning the boilers in the plant and they are extinguished in the process. They are not transferred to the awarder in any form, either as goods or otherwise. The work is more or less a labour contract, in which the Petitioner utilises the chemicals just as it uses any other item of its machinery or fuel or power in the performance of the work. There is no transfer of property in goods and no sale liable for tax under Explanation 3(A). It was further laid down in the above decision that transfer of property in goods (whether as goods or in some other form) is sine qua non for its application. It was held:

The mere execution of a works contract does not by itself attract liability for tax under the Act unless it is accompanied by transfer of property in goods/involved in the execution of the contract. The emphasis is on the transfer of property in goods. When goods used in the process of executing a works contract are consumed in the process, there is no transfer of any goods from the contractor to the awarder of the contract attracting liability to tax.

28. A Division Bench of the Patna High Court in *Pest Control India Ltd. v. Union of India and Ors.* (1989) 75 STC 188 had considered the question whether spraying of chemicals through machines to eradicate pests, rodents, termites etc. would involve transfer of any goods as understood in Sub-clause (b) of Clause (29-A) of Article 366 of the Constitution or under the provisions of the Bihar Finance Act, 1981. The Division Bench held thus:

...The chemicals are Sprayed through machines so that when the process ends, nothing tangible remains in which property is transferred. By the process of spraying or applying chemicals, a place is treated against insects and pests but in the process the chemicals are themselves consumed and there remains nothing in which property is transferred.

The Bench held that such a contract is a pure service contract and no sales tax is leviable in relation thereto under the provisions of the Bihar Finance Act 1981.

29. In a recent decision in *Microtrol Sterilization Services Pvt. Ltd. v. State of Kerala* (2009 (3) KLTSN 14 : (2009) 26 VST 213 (Ker.)), a Division Bench of this Court had occasion to consider the question whether in the process of sterilization of goods by using ethylene oxide gas there was transfer of any goods as envisaged under the Kerala General Sales Tax Act. It came on record that the goods to be sterilised were kept in a compact airtight room and thereafter they were exposed to ethylene oxide for around 6 hours. The gas would thereafter be allowed to escape through a chimney after neutralising it with carbon dioxide at a higher level. The Division Bench held that there was no transfer of ethylene oxide from the Petitioner to the customers in the course of sterilisation of the goods since it is used as a consumable in the service rendered by the Assessee. It was further held that ethylene oxide which was used as a consumable was therefore deductible from the total turnover of works contract u/s 5C of the Act. The Division Bench also took note of the decision of this Court in *Deputy Commissioner of Sales Tax v. Velu (M.K)* (1993) 89 STC 40 (Ker.), apart from the decision of the Patna High Court referred to above.

30. In *Velu* (supra) a Division Bench of this Court held that in display of fireworks no tangible property would remain once the display takes place. In the process of execution of the works contract, the goods themselves (explosives) cease to exist. The Division Bench relying on *Pest Control* (supra) held that there can be no transfer of property unless the goods themselves exist.

31. However Sri. Vinod Chandran, learned Special Government Pleader has placed heavy reliance on the decision of the Apex Court in *Xerox Modicorp Ltd. v. State of Karnataka* (2005) 142 STC 209 and contended that the Petitioner having admitted that he used a chemical compound for the process of cleaning the polluted water, it is immaterial that no tangible goods were available at the end of the process.

32. I do not propose to refer to the ratio decidendi in *Xerox Modicorp* (supra) yet again, since my esteemed Brother has already extracted the relevant portions of

the text in his judgment.

33. In my view, the dictum laid down in Xerox Modicorp has absolutely no relevance, particularly to the facts of this case.

34. In that case, under the Standards and Service Maintenance Agreement (SSMA), the Appellant/Company was bound to maintain the Xerox machines and supply the spare parts including toners, developers etc. as and when required. Obviously the cost of toners and developers to be supplied by the Appellant Company were to be borne by the customers. The short question that arose for consideration was whether the Appellant/Assessee would be liable to be assessed to sales tax for the sale of toners, developers, spare parts etc. Their Lordships held that transfer of property took place the moment the goods viz., toners, developers, spare parts etc. were put into the machine. In other words, tangible goods in toners, developers etc. were transferred as and when they were used by the customer.

35. Having considered the rival contentions of the parties, I have no hesitation to hold that there is no transfer of any goods in property whether as goods or in some other form attracting Explanation 3A u/s 2(xxi) of Act. Similarly, Explanation 1A u/s 2(xxv) is also not attracted. Still further, by virtue of the provisions contained in Section 5C(1)(c)(iii), the cost of the chemicals used by the Petitioner for the purpose of effluent treatment is liable to be deducted, they being consumables.

The reference is answered accordingly.

J. Chelameswar, C.J.

36. I had the advantage of reading the two opinions of both my learned brothers and I agree with the view taken by Justice K.M. Joseph.