(1994) 06 KL CK 0005

In the High Court Of Kerala

Case No : O.P. No. 7976 of 1984-N

Moidoo and Others APPELLANT

Vs

State of Kerala and Others RESPONDENT

Date of Decision : 17-06-1994

Acts Referred:

Central Sales Tax Act, 1956 — Section 14, 15, 3, 4, 5
Constitution of India, 1950 — Article 269, 286, 366, 366(29)
Kerala General Sales Tax Act, 1963 — Section 2, 5, 5(1)
Kerala General Sales Tax Rules, 1963 — Rule 8(1), 8(4)

Citation : (1994) 06 KL CK 0005

Hon'ble Judges : V.V. Kamath, J;K.T. Thomas, J;K. Narayanakurup, J

Bench : Full Bench

Advocate : T.R.G. Wariyar and K.R. Jinan, in O.P. 7976/84, for the Appellant; V.C. James, Government Pleader, for the Respondent

Judgement

Thomas, J.—In these connected cases, the validity of certain provisions of the Kerala General Sales Tax Act, 1963, (for short ''the Act'') and the particular Rule framed under the Act has been challenged by different persons who have undertaken contract work in different areas. As per the impugned provisions sales tax has been levied on the sale of goods involved in what is called "works contract". Section 2(viii), Section 2(xxi) read with Explanation 3(A) Section 2(xxvii) read with Explanation 1(A), Section 2(xxvi), Section 2(xxv) and Section 5(1)(iii) of the Act and Rule 8(4) of the Kerala General Sales Tax Rules (for short ''the Rules'') are the provisions principally assailed herein. When these cases came up before a Division Bench on reference, it was felt that the issues involved are of far reaching importance and of substantial revenue and hence, the Division Bench referred these batch of cases to a Full Bench. It was thus that the cases have reached us.

2. The impugned provisions as such were brought into the Act by means of amendments carried out from 1st April 1584 to 1st July 1987. We make it clear that the challenge is confined to these provisions which remianed on the statute

book as on 1st July 1987. We state this because some further amendments to the same and other provisions have been brought out subsequently through Acts 23/91 and 8/92 etc. Such amendments have also been challenged in other Original Petitions, and we are told that a learned Single Judge (Mr. Justice T.L. Viswanatha Iyer) has disposed of such Original Petitions. We make it again clear that this Full Bench is not concerned with such amendments made after 1st July 1987. As on the said date, the impugned provisions remained as follows:

Section 2(viii) ''Dealer'' means any person who carries on the business of buying, selling, supplying or distributing goods executing works contract, transfers the right to use any goods or supplying by way of or as part of any service, any goods directly or otherwise, whether for cash or for deferred payment, or for commission, remuneration or other valuable consideration and includes-

* * * * * (f) a person who, whether in the course of business or not,-

* * * * * (2) transfers property in goods (whether as goods or in some other form) involved in the execution of a works contract.

Section 2(xii) ''Goods'' means all kinds of movable property (other than newspapers, actionable claims, electricity, stocks and shares and securities) and includes livestock, all materials, commodities and articles (including those to be used in the construction, fitting out, improvement or repair of immovable property or used in the fitting out, improvement or repair of movable property) and every kind of property (whether as goods or in some other form) involved in the execution of a works contract, and all growing crops, grass or things attached to, or forming part of the land which are agreed to be severed before sale or under the contract of sale.

Section (xxvi) ''Sale'' with all its grammatical variations and eognate expressions means every transfer (whether in pursuance of a contract or not) of the property in goods by one person to Anr. in the courses 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).-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 (4).-The sale or purchase of goods shall be deemed, for the purposes of this Act, to have taken place in the State whenever the contract of sale or purchase might have been made, if the goods are within the State.

Section 2(xxvii) ''turnover'' means the aggregate amount for which goods are either bought or sold, supplied or distributed by a dealer, either directly or through Anr. , on his own account or on account of Ors. , whether for cash or for deferred payment or other valuable consideration, provided that the proceeds of the sale by a person of agricultural or horticultural produce, grown by himself or gorwn on any 1 and in which he has an interest whether as owner, usufructuary mortgagee, tenant or otherwise, shall be excluded from his turnoverr

* * * * * Explanation 1(A)(i).-The turnover in respect of works contract shall be the-aggregate amount received or receivable by the dealer for the transfer or goods (whether as goods or in some other form) involved in the execution of such contract.

The aggregate amount is the amount received for the transfer of goods and nor for carrying out the contract.

Section 2(xxvi) ''Total turnover'' means the aggregate turnover in all goods of a dealer at all places of business in the State, whether or not the whole or any portion of such turnover is liable to tax, including the turnover of purchase or sale in the course of inter-state trade or commerce or in the course of export of the goods out of the territory of India or in the course of import of the goods into the territory of India:

Explanation.-Notwithstanding anything, contained in any other provision of this Act, in the case of goods which are taxable at the point of last purchase in the State by a dealer liable to tax wider Section 5, and which are held as closing stock on the last day of any financial year, the amount far which such goods were purchased by the dealer shall be deemed also to be a part of his total turnover for the subsequent year or each of the subsequent years until such goods are either sold by him in the State or such purchase acquires the character of last purchase in the State in the hands of such dealer, and in case such purchase acquires the character of last purchase in the State in the hands of such dealer, the turnover in respect of such purchase shall be liable to tax in the year in which the purchase acquires the character of last purchase.

Section 2(xxv) ''Taxable turnover'' means the turnover on which a dealer shall be liable to pay tax as determined after making such deductions from his total turnover and in such manner as may be prescribed, but shall not include the turnover of purchase or sale in the course of inter-state trade or commerce or in the course of export of the goods out of the territory of India or in the course of import of the goods into the territory of India.

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

* * * * * (iii) in the case of transfer of the right to use any goods for any purpose (whether or not for a specified period) at the rate of five per cent at all points of such transfer on an aggregate turnover of fifty thousand rupees and above.

Rule 8 (4): For the purpose of Sub-rule (1) the amount for which goods are sold by a dealer shall, in relation to a works contract be deemed to be the amount payable to the dealer for carrying out such Contract less a sum not exceeding such precantage of the amount payable as may be fixed by the Board of Revenue from time to time for different areas, representing the usual proportion in such areas of the cost of labour to the cost of materials used in carrying out such contract, subject to the following maximum percentages.

Different rates relating to maximum percentages are shown in the Sub-rule.

3. A short reference to the history of the said amendments will be of advantage. After the Supreme Court delivered judgment in Bengal Immunity Company Limited''s case 1955 (6) S.T.C. 446 Entry 92-A was added in list L of the 7th Schedule of the Constitution which reads thus:

Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-state trade or commerce.

By the same amendment Entry 54 in List II was substituted as follows:

Taxes on the sale or purchase of goods other than newspapers, subject to the previsions of entry 92-A of List I.

Under Article 269 of the Constitution "Taxes" on the sale or purchase of goods (other than newspapers) where such sale or purchase takes place in the course of interstate trade or commerce could be levied and collected by the Central Government. Under Article 286 of the Constitution, it was enjoined that no law of a State shall impose or authorise the imposition of a tax on the sale or purchase of goods where such sale or purchase takes place outside India in the course of import of the goods into or export of the goods out of the territory of India. At the same time, Parliament was empowered to formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in the amendment. There was much controversy on the question whether cost of goods supplied by a building contractor in the course of construction of building could be subjected to payment of sales tax. The controversy was resolved by the Supreme Court in 1958 in State of Madras v. Gannon Dunkerley and Co. (Madras) Ltd. 1958 (9) STC 353. It was held that in a building contract which was one entire and indivisible, there was no sale of goods and it was not within the competence of the State Legislature to impose a tax on the supply of the materials for construction treating it as a sale. By virtue of the said decision, no sales tax could be levied on the amount received under a works contract even though he had supplied goods for the said work.

4. It was in the aforesaid background that Parliament brought out the 46th amendment to the Constitution by adding a new definition clause in Article 366 of the Constitution which in effect changed the gamut of the sale of goods involved in works contract and certain other transactions. Commensurate changes were effected in Article 286 of the Constitution also. On the 46th amendment being passed various State Governments pushed through amendments in their sales tax enactments for the purpose of levying tax on the

goods involved in the works contract. Validity of 46th amendment was questioned in Builders'' Association v. Union of India 1989 73 STC 370. A Constitution Bench of the Supreme Court has upheld the validity in 1989 Builders Association of India and Others Vs. Union of India (UOI) and Others,

5. It was at the said stage that the Kerala State Legislature passed amendments to the Act and brought about the enactment containing the impugned provisions.

6. The State has filed a counter affidavit in support of the validity as well as legality of the provisions.

7. A development which took place during the pendency of these Original Petitions is the pronouncement of two decisions by the Supreme Court on 17th November 1992. One was in Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, (for convenience, hereinafter referred to as the ''second Gannon Dunkerley case'' and the second was in Builders'' Association v. State of Karnataka 88 S.T.C. 248 (for convenience, hereinafter referred to as the "second Builders'' Association case"). In the former case, a Constitution Bench of the Supreme Court considered the validity of certain provisions of the Sales Tax Law enacted by the State of Rajasthan etc. and in the latter the same Bench considered certain provisions of the corresponding enactments in the State of Karnataka. In the second Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, . Supreme Court laid down the following propositions:

(1) In exercise of its legislative power to impose tax on sale or purchase of goods under entry 54 of the State List read with Article 366(29A)(b), the State Legislature, while imposing 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 is not competent to impose a tax on such a transfer (deemed sale) which constitutes a sale in the course of inter-state trade or commerce or sale outside the State or a sale in the course of import or export.

(2) The provisions of Sections 3, 4, 5 and Sections 14 and 15 of the Central Sales Tax Act, 1956 are applicable to a transfer of proparty in goods involve in the execution of a works contract covered by Article 366(29A)(b).

(3) While defining the expression ''sale'' in the sales tax legislation it is open to the State Legislature to fix the situs of a deemed sale resulting from a transfer falling within the ambit of Article 366(29A)(b) but it is not permissible for the State Legislature to define the expression ''sale'' in a way as to bring within, the ambit of the taxing power a sale in the course of inter state trade or commerce, or a sale outside the State or a sale in the course of import and export.

(4) The tax on transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract falling within the ambit of Article 366(29A)(b) is leviable on the goods involved in the execution of a works contract and the value of the goods which are involved in execution of the works contract would constitute the measure for imposition of the tax.

(5) In order to determine the value of the goods which are involved in the execution of a works contract for the purpose of levying the tax referred to in Article 366(29A)(b), it is permissible to take the value of the works contract as the basis and the value of the goods involved in the execution of the works contract can be arrived at by deducting expenses incurred by the contractor for providing labour and other services from'' the value of the works contract.

(6) The charges for labour and services which required to be deducted from the value of the works contract would cover (i) labour charges for execution of the works, (ii) amount paid to a sub-contractor for labour and services; (iii) charges for obtaining on hire or otherwise machinery and tools used for execution of the works contract; (iv) charges for planning designing and architect''s fees; (v) cost of consumables used in execution of the works contract; (vi) cost of establishment of the contractor to the extent it is relatable to supply of labour and services; (vii) other similar expenses relatable to supply of labour and services; and (viii) profit earned by the contractor to the extent it is relatable to supply of labour and services.

(7) To deal with cases where the contractor does not maintain proper accounts or the account books produced by him are not found worthy of credence by the assessing authority the Legislature may prescribe a formula for deduction or cost of labour and services on the basis of a percentage of the value of the works contract but while doing se it has to be easured that the amount deductible under such formula does not differ appreciably from the expenses for labour and services that would be incurred in normal circumstances in respect of that particular type of works contract. It would be permissible for the Legislature to prescribe varying scales for deduction on account of cost of labour and services for various types of works contract.

(8) While fixing the rate of tax it is permissible to fix a uniform rate of tax for the various goods involved in the execution of a, work contract which rate may be different from the rates of tax fixed in respect of sales or purchase of those goods as a separate article.

8. In view of the aforesaid propositions, the Supreme Court struck down some of the impugned provisions of the State bales Tax Acts and considered the validity of the Karnataka Sales Tax Act in the second Builders Association case 88 S.T.C 248.

9. Shri T.R.G. Warrier, Senior learned Counsel, who appeared for some of the Petitioners addressed the main arguments in these Original Petitions. He took us through the entire decisions in the second Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, as well as in the second Builders Association''s case 88 S.T.C. 248 besides taking us through the other relevant decisions and contended that in view of the propositions laid down by the Supreme Court, the provisions impugned in these Original Petitions cannot be supported and consequently the assessments and/or various other steps resorted

to by the authorities under the Act as against the Petitioners are liable to be quashed.

10. After hearing the arguments of Shri T.R.G, Warrier, we thought it fit to ascertain from the Government whether in view of the decision in the second Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, Government would persist in defending the provisions impugned. As the Advocate General was not in station then, Shri. Cyriac Joseph, Additional Advocate General, was called by us to ascertain the position from the Government. Learned Additional Advocate General in deference to what we wanted to know from the Government, promptly contacted the Government and conveyed the stand of the Government to us. A statement signed by the Secretary (Taxes), Board of Revenue of the State of Kerala has been filed. We are extracting below the nub of the Government stand as recorded in the said statement.

It is respectfully submitted that in view of the judgment of the Honourable Supreme Court in Gannon Dunkerley and Co. and Others Vs. State of Rajasthan and Others, the State of Kerala will not make assessment or levy tax acting upon the provisions in Rule 8(4) of the Kerala General Sales Tax Rules, 1963 as it stood prior to the amendment effected by S.R.O. 92/91, dated 19th January 1991. This however will be without prejudice to the right of the State to take appropriate action in accordance with the provisions of the K.G.S.T. Act, 1963 and in conformity with the principles laid down by the Honourable Supreme Court in the judgment in Gannon Dunkerley and Co. and Ors. v. State of Rajasthan and Ors. reported in 88 S.T.C. 204.

11. As a counter to the said stand a statement was filed by the Counsel for the Petitioners in O.P. No. 3219/89 in which the Petitioners expressed their reluctance to be satisfied with the offer made by the Government. It is pointed out in the statement and reiterated by Shri T.R.G. Warrier at the bar that in spite of such undertakings made by the Government, the authorities under the Act are bound to proceed with the enforcement of the impugned provisions and therefore, the court may be pleased to decide the question of validity of the provisions challenged.

12. We considered the position in view of the clear cut stand adopted by the Government. Whatever be the validity or invalidity of the impugned provisions, we have absolutely no doubt that without existence of a rule prescribing for deductions for arriving at the taxable turnover as provided in Section 2(xxv), no taxable turnover can be determined by any authority under the Act. The corollary is that so long as Government will not male assessments or levy tax on the strength of Rule 8(4) of the Rules as it stood prior to the amendment effected by S.R.O. 92/91, dated 19th January 1991, the impugned provisions will remain in the statute book unenforced. None of the Petitioners will be affected by any action taken pursuant to the formulation of Rule 8(4) of the Rule as it stood then. In such a situation, it is not necessary for us to decide the question

whether the impugned provisions are unconstitutional. We are not interested in making any academic or advisory exercise regarding the constitutionality of any provision. We may examine the constitutionality of a provision when it is absolutely necessary for protecting the rights and interest of the persons approaching the Court.

13. Learned Government Pleader requested us to make it clear that it is open to the State to bring-forth the provisions in consonance with the parameters evolved by the Supreme Court in second Gannon Dunkerley''s case 88 STC 204. We are not inclined to make any such observations or reservations particularly since learned Counsel for the Petitioners expressed the apprehension that any such observation would be treated as prompting (if not directing) the Government to bring-forth such amendments. That is not the function of the Court.

14. We make it clear that in the light of the definite stand of the Government and to prevent any possible mischief in the matter we interdict all authorities under the Act from resorting to Rule 8(4) of the Rules as it stood prior to the amendment effected by S.R.O. 92/91 or to pursue with any action already adopted in exercise of the said sub-rule.

With the said directions and observations, we dispose of the Original Petitions.

