

(2002) 12 KL CK 0008

In the High Court Of Kerala

Case No : O.P. No"s. 1322 and 4474 and connected cases

P.R.S. Hospital

APPELLANT

Vs

State of Kerala

RESPONDENT

Date of Decision : 20-12-2002

Acts Referred:

Kerala General Sales Tax Act, 1963 — Section 14, 2

Citation : (2003) 1 KLT 633

Hon'ble Judges : C.N. Ramachandran Nair, J

Bench : Single Bench

Advocate : C.K. Thanu Pillai, for the Appellant; Raju Joseph, Government Pleader, for the Respondent

Judgement

C.N. Ramachandran Nair, J.—The short question arising in these cases is whether a hospital is a "dealer" within the definition of that term contained in the K.G.S.T. Act, hereinafter called the "Act". The proceedings initiated against the petitioners by the Sales Tax authorities under the Act under challenge are issued on the basis that the petitioners are "Dealers" under the Act. While in some cases notices are issued to the hospitals directing them to take registration under the K.G.S.T. Act, in some cases hospitals are directed to produce books of accounts and in yet another category penalty is levied or proposed either for not registering or for non-compliance with other statutory provisions. The validity or otherwise of all these proceedings will depend on whether the concerned hospital can be treated as a "dealer" to subject it to all the disciplines provided under the Act and Rules. There is a standard pattern of service rendered in a hospital and distinguishing factors among the hospitals may be in regard to quality and volume of it, but essentially the activities in all the hospitals are one and the same. There is no case by any of the petitioner-hospitals that they are not supplying or selling medicines to the patients in the course of medical treatment which is the very basis on which sales tax authorities have issued notices calling them to take registration, to produce books of accounts, file returns and pay tax, if any due. Therefore, the essence of issue is whether the supply of medicine to

patients in the course of treatment constitute "sale" bringing the petitioners within the scope of "dealer" under the Act making them liable in take out registration, file returns and to pay sales tax if payable.

2. I heard counsel for the petitioners and also the Special Government Pleader for taxes.

3. Before proceeding to the main issue, an aspect to be clarified is the distinction between medical practitioners on the one side and the hospitals and dispensaries on the other side. Notification SRO 1090/99 as amended by SRO 802/2001 provides exemption to medical practitioners which is as follows:

Sl. No. Name of Dealer Turnover which is exempted Conditions and restrictions

13. Medical practitioners Turnover relating to Nil

dispensing medicines the medicines dispensed

from their own to the patients in the

dispensaries course of treatment

(Explanation:- For the purpose of this serial number the term "medical practitioners" shall not include any hospital or clinic.)

By virtue of the exemption provided under the above notification, there is no need to go into the question as to whether medical practitioners dispensing medicines are also "dealers" within the meaning of the Act because by virtue of the exemption available to medical practitioners that question is only academic in nature and I do not think there is any need for this Court to address such a question unnecessarily. The explanation to Entry 13 to the above notification was introduced with effect from 16.8.2001. However, notices are seen issued by some officers way back in 1997 itself directing hospitals to comply with statutory provisions. In fact exclusion of hospitals and clinics from Entry 13 above is only in the form of an explanation. Even prior to the introduction of the said explanation, entry 13 provided for exemption only to medical practitioners dispensing medicines from their own dispensaries who are different from hospitals and clinics. Therefore, even prior to the introduction of the explanation, such of the persons who generally come as medical practitioners dispensing medicines from their own dispensaries only can claim exemption under the said notification. All that item 13 of SRO 1090/99 exempts is a category of doctors supplying medicine in the course of rendering medical service or treatment from their dispensaries. Such cases have to be taken as dispensaries run by doctors where medicine is dispensed with as part of service. The term "hospital" in the dictionary is given a meaning to cover an institution or place where sick or injured persons are given medical or surgical care. "Dispensary" on the other hand is a place where medicines or medical or dental aid are dispensed to ambulant patients. While a dispensary is a place where medical care is rendered involving supply of medicines, hospital is a place where all facilities such as

accommodation for inpatients for treatment is also provided. In other words, dispensaries are essentially consulting places where medicines also are supplied. In the case of hospitals, inpatients are taken and medical services are rendered involving supply of medicines. Exemption appears to be of a limited nature and is applicable only to dispensaries managed by doctors dispensing medicine to their own patients. In other words, essentially consultant doctors are granted exemption on the supplies of medicine in the course of consultation. This category of persons are enjoying exemption on the turnover of sale of medicines. The nature of exemption is evident and clear when the description of the dealer and the turnover exempted are read together. It is specifically mentioned in entry 13 that what is exempted is turnover relating to medicines dispensed to their patients in the course of treatment. This clearly establishes that the exemption is only to a doctor for the sale of medicine to his patients. However, an organised activity involving engagement of doctors and staff for treatment and supply of medicine is not covered by exemption because there is no correlation between the medical practitioner, his patient and the supply of medicine. In other words, exemption is only to doctors who supply medicine as part of their consultancy and service. The decisions relied on by the petitioners are to establish that the medical practitioner dispensing medicine is not engaged in manufacture or supply of medicine in the course of treatment. This activity does not amount to manufacture and sale of medicine is the decision by the High Courts in *Kaviraj PT. Durga Dan Sharma v. The State of Punjab* (1974) 33 STC 479 *Commissioner of Sales Tax v. Dri Sukh Deo* (1969) 23 STC 385 and in *Dr. M. Narayanan v. Sales Tax Officer* 1969 KLJ 311.

4. The petitioners have a case that the hospitals are also run by medical practitioners and so much so, they are also entitled to exemption available under the notification. I do not think this position can be accepted because hospitals cannot be run by doctors alone even though doctors are engaged in medical treatment and may own it. Hospitals are owned by companies, partnership, Trusts etc. or by individuals who may or may not be medically qualified. It is such management which engages doctors and medical staff to run the hospitals. The scope of exemption as already explained is available only to medical practitioners supplying medicine in the course of consultation. However, the same does not cover an organised activity of running a hospital even if the owners of such hospital are doctors.

5. The next question is with regard to the liability of hospitals to take registration and pay tax on the turnover of sale, of medicines and supply of other items in the hospitals. The petitioners' contention is that hospitals are essentially engaged in medical service and supply of medicine is only incidental to the service which does not attract the definition of "dealer" under the Act. The definitions of various terms contained in Section 2 of the Act which are relevant in this context are extracted hereunder:

Section 2(vi) "Business" includes

a) any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture, whether or not such trade, commerce, manufacture, adventure or concern is carried on with a motive to make gain or profit and whether or not any profit accrues from such trade, commerce, manufacture, adventure or concern; and

b) any transaction in connection with or incidental or ancillary to such trade, commerce, manufacture, adventure or concern;

viii) "Dealer" means any person who carries on the business of buying, selling, supplying or distributing goods, (executing works contract, transferring 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-

(a) (xxxx)

(b) a casual trader;

(c) a commission agent, a broker, a del credere agent or an auctioneer or any other mercantile agent by whatever name called, who carries on the business of buying, selling, supplying or distributing goods (executing works contract, transferring right to use any goods or supplying by way of or as part of any service, any goods) on behalf of any principal;

(d) a non-resident dealer or an agent of a non-resident dealer or a local branch of a firm or company or (association or body of persons whether incorporated or not) situated outside the State;

((e) a person who, whether in the course of business or not sells;

i) goods produced by him by manufacture, agriculture, horticulture or otherwise; or

ii) trees which grow spontaneously and which are agreed to be severed before sale or under contract of sale;)

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

(1) transfers any goods, including controlled goods, whether in pursuance of a contract or not, for cash or deferred payment or other valuable consideration;

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

(3) delivers any goods on hire-purchase or any system of payment by instalments;

(4) transfers the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

(5) supplies, by way of or as part of any service or in any other manner

whatsoever, goods, being food or any other articles for human consumption or any drink (whether or not intoxicating), where such supply or service is for cash, deferred payment or other valuable consideration;

Explanation:-(1) A society including a co-operative society, club or firm or an association or body of persons, whether incorporated or not] which whether or not in the course of business, buys, sells, supplies or distributes goods from or to its members for cash or for deferred payment, or for admission, remuneration or other valuable consideration, shall be deemed to be a dealer for the purposes of this Act;

Explanation:- (2) The Central Government or a State Government, which, whether or not in the course of business, buy, sell, supply or distribute goods, directly or otherwise, for cash or for deferred payment, or for commission, remuneration or other valuable consideration, shall be deemed to be a dealer for the purposes of this Act;)

(g) a bank or a financing institution which whether in the course of its business or not, sells any gold or other valuable articles pledged with it to secure any loan, for the realisation of such loan amount;

Explanation I:- Bank for the purpose of this clause includes a Nationalised Bank or a Scheduled Bank or a Co-operative Bank;

Explanation II:- Financing Institution means a financing institution other than a bank;

(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;

(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 (3C):- Any 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 shall be deemed to be a sale.

(xxvii) "turnover" means the aggregate amount for which goods are either bought or sold, supplied or distributed 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 consideration, provided that the proceeds of the sale by a person of agricultural or horticultural produce, grown by himself or grown on any land in which he has an interest whether as owner, usufructuary mortgagee, tenant or otherwise, shall be excluded from his turnover."

The main contention of the petitioners as stated above is that supply of medicine though conceded, is only incidental and essentially the hospital is rendering medical services with professionals namely doctors and nurses who are experienced in the medical field. The petitioners have relied on the decisions of the Supreme Court in *State of Tamil Nadu v. Board of Trustees of the Port of Madras* (1999) 114 STC 520 and in *Northern India Caterers (India) Ltd. LT, Governor of Delhi* (1978) 42 STC 386. Relying on the above two decisions the petitioners contended that the main activity being rendering of medical services, the supply of medicine is only incidental and it does not constitute "sale" to make the petitioners liable as a "dealer" under the Act. In this regard the petitioners have pointed out that the pattern of billing in the hospitals may vary from hospital to hospital. In some hospitals consolidated bills are raised including service charges, accommodation charges, charges for supply of medicine, food etc., whereas in some other hospitals separate bills are raised for medical services, supply of medicine, food, rent and other allied services like X-ray ECG etc. It may not be possible to bifurcate the amount charged to a patient for the various services rendered in hospital. However, there is no dispute that supply of medicine is an integral part of the services rendered and it is significant in terms of cost to the patient and charged separately. Therefore, the first question to be answered is whether the supply of medicine is only an incidental transaction or otherwise it is as important as any other service such as rendering medical service or other services. In the course of treatment except probably in surgical treatment, nobody can have a doubt that medicines account for the main cost along with consultancy charges for the doctor, expenditure in diagnosis etc. Therefore, from common knowledge it is clear that medicine is as important, if not more in terms of value and purpose as anything else in the medical treatment. Therefore, in the first place, the petitioners contention that supply of medicine is only incidental cannot be accepted at all. It is as important as medical consultation or other services in the hospital. Therefore, supply of medicine in the course of medical treatment either to inpatients or to outpatients has to be taken as one of the main activities in a hospital or in a clinic. The Supreme Court had occasion to consider as to when a person becomes a "dealer" in the decision in *The State of Gujarat v. Raipur Manufacturing Co. Ltd.* (1967) 19 STC 1 wherein it was held as follows:

"Whether a person carries on business in a particular commodity must depend upon the volume, frequency, continuity and regularity of transactions of purchase and sale in a class of goods and the transactions must ordinarily be entered into

with a profit-motive. By the use of the expression "profit-motive" it is not intended that profit must in fact be earned. Nor does the expression cover a mere desire to make some monetary gain out of a transaction or even a series of transactions. It predicates a motive which pervades the whole series of transactions effected by the person in the course of his activity. In actual practice, the profit-motive may be easily discernible in some transactions, in others it would have to be inferred from a review of the circumstances attendant upon the transaction. For instance, where a person purchases a commodity in bulk and sells it in retail, it may readily be inferred that he has a profit-motive in entering into the series of transactions of purchase and sale. A similar inference may be raised where a person manufactures finished goods from raw materials belonging to him or purchased by him and sells them. But where a person comes to own in the course of his business of manufacturing or selling a commodity, some other commodity which is not a by-product or a subsidiary product of that business and he sells that commodity, cogent evidence that he has intention to carry on business of selling that commodity would be required. Where a person in the course of carrying on a business is required to dispose of what may be called his fixed assets or his discarded goods acquired in the course of the business, an inference that he desired to carry on the business of selling his fixed assets or discarded goods would not ordinarily arise. To infer from a course of transactions that it is intended thereby to carry on the business ordinarily the characteristics of volume, frequency, continuity and regularity indicating an intention to continue the activity of carrying on the transactions must exist. But no test is decisive of the intention to carry on the business in the light of all the circumstances an inference that a person desires to carry on the business of selling goods may be raised."

Going by the above test, no one can have a doubt that the volume, frequency and continuity or regularity of transaction in regard to purchase and sale of medicine by a hospital will be such that it will answer the definition of "dealer" under the Act beyond any doubt. In this context it is worthwhile to take note of the amendment to the term "dealer" contained in Section 2(viii) of the Act above stated wherein supplying goods by way of or as part of any service is also treated as business to make a person involved in it a "dealer" under the Act. Of course the definition of "supply of goods as part of service" introduced in the Act is in the context of Article 366, 29A(f) of the Constitution of India which was introduced to get over the decision of the Supreme Court in the context of various decisions, particularly, in *Northern India Caterers*" case 42 STC 386 referred to above. The Constitution only provides for supply of food or any other article for human consumption to bring it within the extended definition of "sale". The petitioners contended that the definition introduced under the explanation (3C) to the term "sale" contained in Section 2(xxi) of the Act contemplates only food and articles of human consumption and the same does not take in "medicine". Even though the amendment was brought to cover hotels, the legislative intent is to enlarge the scope of the operation of the Act to cover sales

effected in the course of rendering services also. Moreover, in the definition clause of "dealer" the supply of goods in the course of rendering service is not limited to food and articles of human consumption alone. Further, it is also not possible to compare the case of supply of food as part of service in a hotel and supply of medicine in the course of medical treatment. There is substantial difference between these two transactions. While food served to a guest in a hotel is only incidental and part of service, the supply of medicine in the course of treatment is not just incidental, but it is the main and integral part of treatment and supply by itself or sale of medicine as such is part of business in the hospital. It is not disputed that the hospitals are independently billing and charging for the medicines supplied and as already stated, going by the value of medicines involved in treatment, it is the main component of the cost to the patient and it is not an incidental transaction at all. In other words, sale of medicine is in terms of volume, frequency, continuity, regularity and in all other aspects it is one of the main activities in the hospital. Therefore, such of the hospitals which are supplying medicines of the value in excess of the turnover for which registration is required i.e. Rs. 2 lakhs in an year are liable to be registered under the K.G.S.T. Act. The decisions referred to by the petitioners do not apply or are at least not relevant here. The decision in *State of Tamil Nadu v. Board of Trustees of the Port of Madras* 114 STC 520 was rendered by the Supreme Court in the context of statutory service rendered by the Port Trust and other services and the transaction involved there was only sale of scrap materials which is occasional and incidental. Whereas in the case of hospitals, as found earlier the sale of medicine is one of the main activities and it satisfies the test laid down by the Supreme Court in *The State of Gujarat v. Raipur Manufacturing Co. Ltd.* 19 STC 1 referred to above. The activity answers all the test laid down by the Supreme Court to make the hospital a "dealer". The decision in *Northern India Caterers*" case referred to above is also not comparable and is no longer relevant after the 42nd amendment to the Constitution of India and the consequent amendment to the Sales Tax Act.

6. The petitioners are also liable to take drug licence under the Drugs" Control Order for storing and selling drugs. Exemption is of course granted only to registered medical practitioners and Government hospitals and local bodies and hospitals and dispensaries run by Government or local bodies. Therefore, under the Drugs Control Order also hospitals and dispensaries are treated just like other dealers.

7. The petitioners have a case that medicine is, an item coming under entry 87 of the First Schedule to the Act which attracts tax at the point of first sale in the State and most of the petitioners are buying medicines within the State. Therefore, the Government gets no benefit by requiring the petitioners to take registration and comply with the formality by filing returns, as no tax is payable. It is one thing to say that the petitioners have no liability to pay tax and another to say that they are liable to conform to the discipline under the Act and Rules. If the medicines sold by the petitioners in the hospital are only second sales and

the petitioners have bills to prove purchase in Kerala showing payment of tax, necessarily they will get exemption in the course of assessment and they will have no liability to pay tax. However, the requirement of registration under the Act and the filing of returns and production of books of accounts in support of the same is to enable the Department to ensure that the claim is correct or otherwise to levy tax if the petitioners are found to be engaged in first sale of goods. It is to be noted that there is nothing barring the hospitals from sourcing medicine from outside the State or even from out of India. Therefore, unless the petitioners establish that the entire medicines sold by them or supplied in the course of treatment in the hospital are locally purchased for which tax is paid by the petitioners, exemption cannot be claimed by them. In other words, it is a matter of granting exemption in the course of assessment by the assessing officer when he is satisfied in this regard. Under the scheme of the Act registration is compulsory, if the dealer has turnover in excess of the minimum limit which is currently Rs. 2 lakhs; no matter, the turnover is non-taxable. Therefore, such of the hospitals having so much turnover, whether exempted or otherwise, are bound to apply for and take registration and establish exemption in the course of assessment after filing returns.

8. In some cases the petitioners are questioning the amendment to Section 14 of the Act increasing the fee for registration and renewal thereof going upto a maximum of Rs. 20,000/- based on turnover. The current rate of fee payable for registration u/s 14 of the Act is extracted hereunder;

"14. Procedure for registration:- (1) An application for registration shall be made to such authority, in such manner and within such period as may be prescribed and shall be accompanied by a fee as specified below:-

- (a) Where the total turnover is less than three lakh rupees Two hundred and fifty
- (b) Where the total turnover is three lakhs rupees and above but is less than ten lakh rupees Five hundred rupees
- (c) Where the total turnover is ten lakhs rupees and above but less than fifty lakh rupees Seven hundred and fifty rupees plus plus twenty five rupees for each lakh or part thereof above ten lakh rupees
- (d) Where the total turnover is fifty lakhs rupees and above One thousand seven fifty rupees plus fifty rupees for each lakh or part thereof above fifty lakhs rupees (so however that the total registration fee payable shall not exceed twenty thousand rupees).

9. There is no challenge against the constitutional validity of Section 14 of the K.G.S.T. Act as such which in any case will not stand in view of the powers conferred in the State under Entry 66 of the State list under Seventh Schedule to the Constitution. However, the increase of registration fee is challenged as arbitrary, unreasonable and hence violative of Article 14 of the Constitution. According to the petitioners, unlike tax there should be corresponding service for

demanding registration fee. In other words, there should be quid pro quo to justify the demand of registration fee. However, nobody has doubted that there is no service rendered by the Department and there has been always registration fee at all time in the statute. The question therefore is whether the increase in registration fee periodically made is justified or not and whether the present rate particularly, the maximum rate at Rs. 20,000/- is excessive or arbitrary. The principle of quid pro quo stands established and the settled position is that the dealers are getting services from the Department and there is nothing to indicate that the Government has to establish the correlation between fees and service exactly in court to sustain it. Various services are rendered by the Sales Tax Department to dealers. The petitioners contend that the form supplied such as delivery note declarations etc. are separately charged, though the charges are not very high. I find the registration fee fixed is directly related to turnover; that is in proportion to turnover and the maximum payable for an year is Rs. 20,000/-. It is because as the turnover goes on, of course the volume of department work also goes up. In the first place, the parties are entitled to departmentally issued declarations in form No. 26 for transport of goods, returns and other forms are also printed and supplied by the department including treasury challans for payment of tax, all of which are not charged on cost basis. Above all, there is a heavy burden on the Government to maintain various infrastructure facilities such as Check Posts, vehicles etc. for administration of the statute which has to be recouped by collection of fees. There are large number of dealers served by the Department who are not liable to pay any tax either being second or subsequent sellers of First Schedule items or dealers in exempted goods or exporters. The fee collected in proportion to turnover is therefore amply justified. Considering the inflation and cost increase in the course of last several years, I do not think the current levy of maximum registration fee at Rs. 20,000/- is exorbitant or arbitrary, since there is quid pro quo. I do not think this Court can go into the question whether there is service rendered in proportion to the fees charged. This is outside the scope of judicial scrutiny. So far as there is service rendered and the amount of fees charged for registration or renewal thereof is not exorbitant or unreasonable, the Section authorising such levy has to be upheld and I do so. The Supreme Court in *Municipal Corporation of Delhi and Others Vs. Mohd. Yasin*, held that Court need not assume the role of a cost accountant, while deciding the validity of the statute. It is further held that it is neither necessary nor expedient to weigh too meticulously the cost of the services rendered against the amount of fees collected so as to evenly balance the two. In short, even if the levy leads to a net gain for the State, the same does not affect the validity of the legislation so long as there is a relation between the fee charged and the services rendered. Therefore, the demand of registration fee in proportion to turnover with a maximum limit of Rs. 20,000/- a year is not excessive or arbitrary and is not a colourable legislation or "masked tax" as alleged by the petitioners. I feel the slab rates of fees with the upper limit are reasonable under the present conditions. Therefore Section 14 as amended is upheld and the O.Ps. on this

issue are dismissed.

10. The petitioners have pointed out that in respect of those dealers paying tax at compounded rate, registration fee cannot be related to turnover and therefore, there is lacunae in the statute. This is not going to invalidate registration fee provided on slab rate. So long as the petitioners are not enjoying any compounding facility, they cannot have a grievance in respect of registration fee charged on dealers paying tax at compounded rate. It is for them to challenge such demand, if there is a grievance.

11. In view of the pendency of the cases so far and consequently so far the provisions of the Act and Rules have not been enforced against the petitioners, and in view of the explanatory note introduced in the notification above referred, though the clarification is only prospective, I feel enforcement of the statute against the hospitals has to be made only with effect from the financial year 2001-2002. The petitioners are free to make application for registration, remit the registration fee, file returns and comply with statutory provisions. All the impugned proceedings stand vacated to enable the petitioners to comply with the statutory provisions of making application for registration, remitting registration fee, filing returns, etc. from 1.4.2001 onwards. The petitioners are granted three months from now to apply for registration, to file returns up-to-date, pay tax, if any, falling which the department is free to take coercive action including penal action. In view of the stay granted by this Court and continuously available to the petitioners and the introduction of explanation to the notification prospectively, I hold the petitioners cannot be called upon to pay penalty or interest for belated payment of registration fee or tax, if any payable, provided they comply with the above formalities in three months -from now. They need to register, file returns etc. only from the financial year 2001-2002 onwards.

The O.Ps. are disposed of with the above directions.