
(2007) 07 MAD CK 0297

In the Madras High Court

Case No : Writ Petition No's. 15960, 16069, 16116, 16117, 16124, 16143, 16167, 16185, 16198, 16206, 16207, 16283, 16284, 16288, 16291, 16319, 16340, 16341, 16349, 16350, 16351, 16352, 16353, 16370, 16408, 16472, 16518, 16519, 16521, 16527, 16593, 16594, 16646, 166

R. Gandhi

APPELLANT

Vs

State of Tamil Nadu and Others

RESPONDENT

Date of Decision : 10-07-2007

Acts Referred:

Constitution of India, 1950 — Article 255, 301, 302, 303, 303(1)

Citation : (2008) 13 VST 390

Hon'ble Judges : A.P. Shah, C.J.; P. Jyothimani, J

Bench : Division Bench

Advocate : R. Gandhi for R.G. Narendhiran, K.M. Vijayan for La Law, N.S. Manoharan, V. Srinivasa Balu, T.S. Sivagnanam, K.K. Senthilvelan, G. Vijay Anand, P. Suseela Rani, K. Sukumaran, M.S. Subramanian, R. Ramesh, Bhavadharani, P.V. Rajeswari, S. Sundaragopal, R. Murari, V. Kalyana Raman, S. Subbiah, P. Sukumar, V.P. Sengottuvel, M.S. Ramesh, V. Viswanathan and M.B. Dorminique, for the Appellant; Raja Kulifulla, Government Pleader, Edwin Prabhakar, Additional Government Pleader and V.R. Thangavelu, Government Advocate, for the Respondent

Judgement

A.P. Shah, C.J.—All these writ petitions filed by the importers/dealers of motor vehicles challenge the constitutional validity of the Tamil Nadu Tax on Entry of Motor Vehicles into Local Areas Act, 1990 (Act 13 of 1990) (hereinafter, for brevity sake, will be referred to as "the Act"). The Act was in replacement of an Ordinance (No. 1 of 1990) promulgated by the Governor on February 19, 1990 and published in the gazette on February 20, 1990. The Act received the assent of the President on April 24, 1990, published in the gazette on the next day, and deemed to have come into force from February 20, 1990.

2. The challenge to the validity of the Act which was basically on the ground of infringement of Articles 301 and 304 of the Constitution was originally dealt with

and rebutted on the basis of the law laid down by the Supreme Court in Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others, and State of Bihar v. Bihar Chamber of Commerce : [1996]2SCR184 , wherein it was held that in order to establish the tax as compensatory, some connection between the tax and the trading facilities extended to the dealers directly or indirectly is sufficient to characterise it as compensatory tax. The judgment of the Division Bench is R. Gandhi and Another Vs. Union of India (UOI) and Others, . Special leave petitions were filed in the Supreme Court against the Division Bench judgment and those special leave petitions and certain connected matters were referred to a Larger Bench by order dated September 26, 2003 as the Bench hearing the matters doubted the correctness of the view expressed in the case of Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others, and Bihar Chamber of Commerce : [1996]2SCR184 . The matters were dealt with by the Constitution Bench in Jindal Stainless Ltd. and Another Vs. State of Haryana and Others, and the Bench concluded that the doubt expressed by the referring Bench about the correctness of the decision in Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others, followed by the judgment in Bihar Chamber of Commerce case : [1996]2SCR184 was well founded. The Bench held that the doctrine of "direct and immediate effect" of the impugned law on trade and commerce under Article 301 as propounded in Atiabari Tea Co., Ltd. Vs. The State of Assam and Others, and the working test enunciated in The Automobile Transport (Rajasthan) Ltd. Vs. The State of Rajasthan and Others, for deciding whether a tax is compensatory or not vide para 19 of the report (AIR), will continue to apply and the test of "some connection" indicated in (page 658 of STC; para 8 of SCC) the judgment in Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others, and followed in Bihar Chamber of Commerce case : [1996]2SCR184 is not good law. Accordingly, the special leave petitions and the writ petitions were directed to be listed for being disposed of in the light of the said judgment. In Jindal Stainless Ltd. and Another Vs. State of Haryana and Others, , a two-judge Bench noted that in all these matters, the High Courts concerned have not examined the issue in the proper perspective, as they were bound by the judgments in Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others, and Bihar Chamber of Commerce case : [1996]2SCR184 and granted liberty to the parties to place the relevant data in the writ petitions concerned and directed the High Courts to deal with the basic issue as to whether the impugned levy was compensatory in nature.

3. The only issue which now falls for our consideration is whether the levy of entry tax under the Tamil Nadu Tax on Entry of Motor Vehicles into Local Areas Act, 1990 (Act 13 of 1990) can be justified as a compensatory tax?

4. The learned Counsel appearing on behalf of the petitioners submitted that the right of the State to impose entry tax has to be decided in the light of the decision of the Constitution Bench of the Supreme Court in Jindal Stainless Ltd. and Another Vs. State of Haryana and Others, . It was submitted that in Jindal

Stainless Ltd. and Another Vs. State of Haryana and Others, , it has been specifically held that the burden is on the State placing material before the court to prove that the payment of compensatory tax is reimbursement/re-compensate for the quantifiable/measurable services provided or to be provided to the payers. It was submitted that the essence of compensatory tax is that the services rendered or facilities provided should be more or less commensurate with the tax levied and tax should not be patently more than what was required to provide trading facilities. It was submitted that the tax imposed for augmenting general revenue of the State is not compensatory; that any tax law, which is designed or which has the effect of disrupting the trade movement in inter-State trade and commerce between States is contrary to the concept of freedom of trade embodied in Article 301 of the Constitution. It was urged that as seen from the Statement of Objects and Reasons of the Act, the Act has been enacted to curb the evasion of sales tax on the sale of motor vehicles which are purchased outside the State and brought into this State and the State has not discharged the burden to prove that the tax levied and collected under the impugned Act is for the purpose of providing trade facilities. It was submitted that entry 52, List II, indicates that the levy contemplated therein is on the entry of goods into the local area for consumption, use or sale therein. Therefore, if levy of entry tax is claimed to be compensatory in nature, such levy should be, in the first instance, confined to a local area, and secondly, the trade facilities sought to be provided also should be confined to such local area. It was submitted that the expenses for such facilities and the levy by which such expenses are to be met must bear reasonable and rationale relationship. It was submitted that the entry tax levied under the impugned Act lacks basic ingredients for a valid compensatory tax as neither under the impugned Act nor in connection with it, any specific facility, convenience or service is provided to the importers/dealers, who are required to pay the impugned tax nor is there any co-relationship between the quantum of tax recovered from the importers/dealers and the value of convenience/facility or services provided. The levy thus violates Articles 301 and 304 of the Constitution.

5. In reply, on behalf of the State Government, it was submitted by the learned Government Pleader that Act 13 of 1990 has received the Presidential assent as required under Article 255 of the Constitution and thus the Act is saved by Article 304(b) of the Constitution. Learned Government Pleader in the alternative submitted that the entry tax is compensatory in character, and therefore, the impugned levy, which is compensatory in nature, does not attract Articles 301 and 304 of the Constitution. He submitted that it is sufficiently demonstrated from the statistical data furnished by the State in relation to the expenditure involved for the maintenance of roads, construction of bridges, etc., that the levy is compensatory, and thus, the test laid down by the Constitution Bench in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, : stands fully satisfied. He submitted that if the statute fixes a charge for convenience or services provided by the State and imposes a tax upon those who avail

themselves of such services or convenience, freedom of trade and commerce would not be impaired. He submitted that it would be permissible to consider in the context of entry tax that the whole of the State is divided into local areas, and therefore, it is necessary to consider various facilities provided by the State in all local areas and it is enough, if the traders are provided substantial facilities as a class.

6. The Constitution Bench in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, concluded as follows (paras 49 and 50 in STC; paras 52 and 53 in SCC):

Conclusion:

49. In our opinion, the doubt expressed by the referring Bench about the correctness of the decision in *Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others*, followed by the judgment in the case of *Bihar Chamber of Commerce* case : [1996]2SCR184 was well founded.

50. We reiterate that the doctrine of "direct and immediate effect" of the impugned law on trade and commerce under Article 301 as propounded in *Atiabari Tea Co., Ltd. Vs. The State of Assam and Others*, and the working test enunciated in *The Automobile Transport (Rajasthan) Ltd. Vs. The State of Rajasthan and Others*, for deciding whether a tax is compensatory or not vide para 19 of the report, will continue to apply and the test of "some connection" indicated in para 8 (of SCC) (page 658 of STC) of the judgment in *Bhagatram Rajeev Kumar Vs. Commissioner of Sales Tax, M.P. and Others*, and followed in *State of Bihar v. Bihar Chamber of Commerce* [1996]2SCR184 is, in our opinion, not good law. Accordingly, the constitutional validity of various local enactments which are the subject-matters of pending appeals, special leave petitions and writ petitions will now be listed for being disposed of in the light of this judgment.

7. It is thus seen that the Constitution Bench decision in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, has re-affirmed the working test laid down in *The Automobile Transport (Rajasthan) Ltd. Vs. The State of Rajasthan and Others*, that for any tax to be compensatory, it is necessary to examine whether the trades people are having the use of certain facilities for the better conduct of business and paying not patently much more than what is required for providing the facilities.

8. At this juncture, it is necessary to take note of what has been stated about the scope of Articles 301, 302 and 304 vis-a-vis compensatory tax by the Constitution Bench in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, , which reads as follows (at pages 572 to 574 of STC; SCC pages 268 and 269):

42. To sum up, the basis of every levy is the controlling factor. In the case of "a tax", the levy is a part of common burden based on the principle of ability or capacity to pay. In the case of "a fee", the basis is the special benefit to the

payer (individual as such) based on the principle of equivalence. When the tax is imposed as a part of regulation or as a part of regulatory measure, its basis shifts from the concept of "burden" to the concept of measurable/quantifiable benefit and then it becomes "a compensatory tax" and its payment is then not for revenue but as reimbursement/recompense to the service/facility provider. It is then a tax on recompense. Compensatory tax is by nature hybrid but it is more closer to fees than to tax as both fees and compensatory taxes are based on the principle of equivalence and on the basis of reimbursement/recompense. If the impugned law chooses an activity like trade and commerce as the criterion of its operation and if the effect of the operation of the enactment is to impede trade and commerce then Article 301 is violated.

Burden on the State:

43. Applying the above tests/parameters, whenever a law is impugned as violative of Article 301 of the Constitution, the court has to see whether the impugned enactment facially or patently indicates quantifiable data on the basis of which the compensatory tax is sought to be levied. The Act must facially indicate the benefit which is quantifiable or measurable. It must broadly indicate proportionality to the quantifiable benefit. If the provisions are ambiguous or even if the Act does not indicate facially the quantifiable benefit, the burden will be on the State as a service/facility provider to show by placing the material before the court, that the payment of compensatory tax is a reimbursement/recompense for the quantifiable/measurable benefit provided or to be provided to its payer(s). As soon as it is shown that the Act invades freedom of trade it is necessary to enquire whether the State has proved that the restrictions imposed by it by way of taxation are reasonable and in public interest within the meaning of Article 304(b) [See: para 35 of (AIR) the decision in Khyerbari Tea Co. Ltd. and Another Vs. The State of Assam,].

Scope of Articles 301, 302 and 304 vis-a-vis compensatory tax:

44. As stated above, taxing laws are not excluded from the operation of Article 301, which means that tax laws can and do amount to restrictions on the freedom guaranteed to trade under Part XIII of the Constitution. This principle is well-settled in the case of Atiabari Tea Co., Ltd. Vs. The State of Assam and Others, . It is equally important to note that in Atiabari Tea Co., Ltd. Vs. The State of Assam and Others, , the Supreme Court propounded the doctrine of "direct and immediate effect". Therefore, whenever a law is challenged on the ground of violation of Article 301, the court has not only to examine the pith and substance of the levy but in addition thereto, the court has to see the effect and the operation of the impugned law on inter-State trade and commerce as well as intrastate trade and commerce.

45. When any legislation, whether it would be a taxation law or a non-taxation law, is challenged before the court as violating Article 301, the first question to be asked is : What is the scope of the operation of the law? Whether it has

chosen an activity like movement of trade, commerce and intercourse throughout India, as the criterion of its operation? If yes, the next question is: what is the effect of operation of the law on the freedom guaranteed under Article 301? If the effect is to facilitate free-flow of trade and commerce then it is a regulation and if it is to impede or burden the activity, then the law is a restraint. After finding the law to be a restraint/restriction one has to see whether the impugned law is enacted by the Parliament or the State Legislature. Clause (b) of Article 304 confers a power upon the State Legislature similar to that conferred upon Parliament by Article 302 subject to the following differences:

(a) While the power of Parliament under Article 302 is subject to the prohibition of preference and discrimination decreed by Article 303(1), unless Parliament makes the declaration under Article 303(2), the State power contained in Article 304(b) is made expressly free from the prohibition contained in Article 303(1) because the opening words of Article 304 contains a non obstante clause both to Article 301 and Article 303.

(b) While the Parliament's power to impose restrictions under Article 302 is not subject to the requirement of reasonableness, the power of the State to impose restrictions under Article 304 is subject to the condition that they are reasonable.

(c) An additional requisite for the exercise of the power under Article 304(b) by the State Legislature is that previous Presidential sanction is required for such legislation.

9. In the light of the principles laid down in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, : we shall now proceed to examine whether the tax levied under the impugned Act is compensatory or not. The preamble of the Act states that the Act is to provide for the levy of tax on entry of motor vehicles into local areas either for use or sale therein. The Statement of Objects and Reasons attached to the Bill introduced in the Legislative Assembly in respect of the Act was as under:

In order to curb the evasion of sales tax on the sale of motor vehicles which are purchased outside the State and brought into this State, the Government have decided to levy tax on entry of motor vehicles into local areas of this State either for use or sale therein which is liable for registration in the State under the Motor Vehicles Act, 1988 (Central Act 59 of 1988). It has also been decided not to levy the tax in respect of vehicles registered in the Union Territory or in other States fifteen months prior to registration in the State and necessary provision has been provided for. In the case of dealers, entry tax shall be leviable on the entry of motor vehicles and the tax paid by them shall be adjusted with the tax payable by them under the Tamil Nadu General Sales Tax Act, 1959 (Tamil Nadu Act No. 1 of 1959).

10. It is thus seen from the Statement of Objects and Reasons that the Act has been enacted with a view to curb the evasion of sales tax on the sale of motor vehicles which are purchased outside the State and brought into the State. In

Jindal Stripe Ltd. and Others Vs. State of Haryana and Others, , the Supreme Court observed in para 13 (STC, at page 309; para 16 at pages 65 and 66 of SCC), thereof that the following propositions are deducible from the cases noticed therein:

...

4. Tax imposed for augmenting general revenues of the State such as sales tax is not compensatory....

11. In the wake of the decision of the Constitution Bench in Jindal Stainless Ltd. and Another Vs. State of Haryana and Others, , the State has filed an additional counter-affidavit in which the State has sought to project certain figures and expenditure incurred for construction and maintenance of roads and bridges for the period from 1991-92 to 2005-06. It was stated that in view of the increasing network of road and transport system it is necessary to augment the revenue of the State to compensate the expenditure to provide trading facilities including laying and maintenance of roads, bridges, flyovers, etc. It was stated that the total length of the road network in Tamil Nadu is 61,430 kms. It was stated that the roads in the State of Tamil Nadu are repeatedly relaid and maintained in good condition apart from widening the same as four-lane roads investing substantial sum of money. The comparative chart on collection of tax on vehicles and the expenditure on construction and maintenance of roads and bridges furnished in the affidavit reads thus:

					Year
Collection of	Collection	Total	Total	Difference	entry tax on of road tax collection
expenditure on	motor vehicles	of tax	construction and	maintenance of	roads
and					bridges

1991-92	24.84	248	272.84	55.73	217.11
1992-93	42.07	293	335.07	144.53	190.54
1993-94	69.51	314	383.51	131.46	252.05
1994-95	105.27	372	477.27	187.28	289.99
1995-96	157.77	392	549.77	207.81	341.96
1996-97	185.96	425	610.96	435.54	175.42
1998-99	182.63	523	705.63	604.1	101.53
1999-00	220.57	582	802.57	734.68	67.89
2000-01	276.33	631	907.33	1155.22	-247.89
2001-02	296.66	650	946.66	674.14	272.52
2002-03	324.01	700	1024.01	539.19	484.82

2003-04 388.91 1000 1388.91 657.44 731.47

2004-05 519.21 1028 1541.21 1196.51 350.7

2005-06 655.67 1131 1786.67 1825.48 -38.81

12. It was stated that apart from the overall expenditure made, certain significant and important expenditure incurred by the State is in respect of special repairs programme, coastal road improvement programme, east coast road and sugarcane road development programme and various other works of improvement of road undertaken under the flood relief works and the tribal area development programme. It was stated that the cost of maintenance of roads is increasing every year in view of (a) high cost of materials, (b) increase in wage structures and (c) allowances for mazdoors working on road maintenance. It was stated that substantial amounts have been spent on the construction and maintenance of roads and bridges. It is stated that part II schemes framed by the State Government relate to construction of bridges. Apart from that, there are several other schemes under which the State has incurred substantial expenses for the construction and maintenance of roads.

13. The short question is whether the material produced by the State is sufficient to establish that the levy is compensatory. In *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, , the court has categorically ruled that for a law to be compensatory, there has to be a rational nexus between the levy and the services provided. The decision proceeds to make a clear-cut distinction between the general taxing power of the State and the levy of compensatory tax. The essence of compensatory tax is that the services rendered or facilities provided should be more or less commensurate with the tax levied. Services provided will have a direct co-relation with the trade. The main basis of compensatory tax is the quantifiable and measurable benefit represented by the cost incurred in procuring the facilities/services. The cost in turn becomes the basis of reimbursement/recompense for provider of services/facilities. As held in *Jindal Stainless Ltd. and Another Vs. State of Haryana and Others*, , the compensatory tax is a charge for offering trade facilities and they are based on the principle of equivalence. Applying the above test, we are of the opinion that maintaining of roads, providing bridges, etc., cannot be said to be compensatory in nature so as to constitute special advantage to trade, commerce and intercourse. Even otherwise, a welfare State is bestowed with the responsibilities of providing good roads and bridges for the benefit of the tax-paying citizens and hence to contend that the impugned levy is being raised only for the said purpose is not justified. Maintenance of roads, bridges, etc., are generally met from the general funds or revenue. Whether goods are transported into the State or outside State or abroad, the State has got a duty to provide facilities like roads, bridges, etc., which are being enjoyed not only by the persons who bring the goods notified for levy of entry tax, but also by others.

14 The roads, bridges expenditure test, which was applied in Automobile Transport case AIR 1962 SC 1406 in respect of the vehicle tax cannot be made applicable to the impugned enactment which sought to levy the entry tax on the entry of motor vehicles into the local areas of the State. As to what could satisfy such a test in the context of an entry tax could be gathered from para 28 in the case of State of Karnataka and Another Vs. Hansa Corporation, , which is extracted below:

The State did not attempt in the High Court to sustain the validity of the impugned tax law on the submission that it was compensatory in character. No attempt was made to establish that the dealers in Scheduled goods in a local area would be availing of municipal services and municipal services can be efficiently rendered if the municipality charged with a duty to render services has enough and adequate funds and that the impugned tax was a measure for compensating the municipalities for the loss of revenue or for augmenting its finances. As such a stand was not taken, it is not necessary for us to examine whether the tax is compensatory in character.

14.1 As per the Statement of Objects and Reasons, the Act has been enacted with a view to curb the tax evasion and the tax recovered under the impugned enactment is liable to be adjusted with the general sales tax payable under the Tamil Nadu General Sales Tax Act, 1959. The additional counter of the State merely gives the statistics with regard to the total cost of building of roads and bridges and on the maintenance of roads that is incurred from year to year by the State. This expenditure only represents the expenditure incurred by the State from its general total tax revenue and other receipts including the World Bank grants and loans. The said roads and bridges which are constructed or maintained by incurring this expenditure cannot possibly be considered to be a facility or convenience of services, which is provided to a particular importer who imports the goods into a particular local area. In ITC Limited Vs. The State of Tamil Nadu, , a Division Bench of this court (to which I am a party) has held that tax levied under the Tamil Nadu Tax on Entry of Goods into Local Areas Act, 2001, is not compensatory tax within the meaning of Articles 301 and 304 of the Constitution. It was held that applying the principle of equivalence, as set forth by the Supreme Court in Jindal Stainless Ltd. and Another Vs. State of Haryana and Others, , it cannot be said that maintaining of roads, providing bridges, etc., is compensatory in nature so as to meet the outlay incurred for some special advantage to trade, commerce and intercourse. It was held that there is no connection or nexus with the collection of entry tax and its utilisation for the benefit of traders/ manufacturers from whom such tax is collected and that consequently the levy of entry tax is unauthorised and violative of Article 301 of the Constitution. To the same effect is the decision of the Division Bench of the Kerala High Court rendered on December 18, 2006 in O.P. No. 434 of 1996 [Thressiamma L. Chirayil Vs. State of Kerala, rep. by the Deputy Commissioner of Agricultural Income Tax and Sales Tax, Kottayam and another. This is again referred to in the recent decision rendered by a Division Bench of the Jharkhand

High Court in Tata Iron & Steel Co. Ltd., Jamshedpur v. State of Jharkhand [2007] 6 VST 587 [W.P. (T) No. 5354 of 2004, dated August 14, 2006]. A Division Bench of the Bombay High Court in Eurotex Industries and Exports Ltd. v. State of Maharashtra [2004] 135 STC 25 also took a similar view.

15. In view of the foregoing discussion, our finding on the issue is that the tax imposed under the Tamil Nadu Tax on Entry of Motor Vehicles into Local Areas Act, 1990 (Act No. 13 of 1990) is not compensatory in nature.