

(1970) 11 GUJ CK 0007

In the Gujarat High Court

Case No : Sales Tax Reference No's. 21 and 22 of 1969

Ruby Laboratories

APPELLANT

Vs

Commissioner of Sales Tax

RESPONDENT

Date of Decision : 26-11-1970

Acts Referred:

Bombay Sales Tax Act, 1959 — Section 12, 12(1), 2(23), 25, 36
Central Sales Tax Act, 1956 — Section 10, 10A, 12(1), 8, 8(1)

Citation : (1971) 27 STC 326

Hon'ble Judges : T.U. Mehta, J;P.D. Desai, J

Bench : Division Bench

Advocate : S.L. Mody, for the Appellant; B.S. Shah, Assistant Government Pleader, M.G. Doshit and H.V. Chhatrapati, Additional Government Pleaders, for the Respondent

Judgement

Mehta, J.—The question involved in both these references is whether distribution of some of the manufactured goods as free samples amounts to any use, which is contrary to the purpose mentioned in the certificate issued in form No. 15 for the purpose of deduction contemplated by section 12(1)(b) of the Bombay Sales Tax Act, 1959 (hereinafter referred to as "the State Act") or in form "C" u/s 8(4) of the Central Sales Tax Act, 1956 (hereinafter referred to as "the Central Act").

2. Short facts leading to both these references are as under : The applicant in both references is a firm known as M/s. Ruby Laboratories. It is manufacturing medicines for sale and is registered under the State Act as well as the Central Act. It also holds recognition certificate contemplated by the section 12 of the State Act and, therefore, there is no dispute about the fact that it is a recognised dealer within the meaning of section 2(23) of the State Act. It is found that during the assessment period, the applicant made certain purchases by issuing "C" forms under the Central Act. These purchases were made by the applicant for the manufacture of taxable goods for sale. At the time of purchasing these goods for the purpose of manufacture, the applicant is also found to have given a certificate in form No. 15 as contemplated by section 12(1)(b) of the State Act.

3. After the manufacture, for which the goods were so purchased, the assessee-company distributed some free samples of the manufactured articles to different persons. Therefore, the question which arose before the Sales Tax Officer was whether the goods which were covered by the certificate contemplated by form No. 15 of the State Act and "C" form of the Central Act, were the goods which were utilised in manufacturing the articles "for sale". Since these samples were distributed free of charge, the Sales Tax Officer found that the goods utilised in manufacturing these free samples were not the goods meant for use in manufacture "for sale". In order to find out what was the actual quantum of such goods, the Sales Tax Officer estimated 3 per cent. of the total turnover of the manufactured articles to be the value of the total samples. Of this, 60 per cent. was taken to be the price of all the materials used during the process of manufacture. Of these 60 per cent., the Sales Tax Officer considered 50 per cent. to be the purchases of goods covered by form No. 15 of the State Act and "C" form of the Central Act. In the opinion of the Sales Tax Officer, the applicant-assessee, by distributing these samples freely committed a breach of the conditions embodied in the certificate in form No. 15 declaration in "C" form of the relevant statutes. The Sales Tax Officer, thereupon, came to the conclusion that in view of the breach of conditions embodied in these in these forms, the applicant-assessee had rendered itself liable to the payment of penalty u/s 36(1) of the State Act and section 10-A of the Central Act. He, therefore, levied the penalty of Rs. 128.60 u/s 36(1) of the State Act and Rs. 138.24 u/s 10-A of the Central Act.

4. Being aggrieved by this decision of the Sales Tax Officer, the applicant-assess preferred two different appeals before the Assistant Commissioner of Sales Tax but was not successful. It thereafter preferred two second appeals against each of the orders of penalty before the Tribunal but there also it failed.

5. The Tribunal found, on consideration of the provisions contained in the relevant sections of both the Acts that when the assessee-applicant gave certificate contemplated by form 15 of the State Act and "C" form of the Central Act, it knew fully well that a fraction of the manufactured goods was bound to be utilised, not for sale but for distribution of samples and, therefore, to the extent to which the goods were likely to be utilised for these free samples, the assessee-applicant should be presumed to have committed breach of the recitals contained in those certificates. Taking this view, the Tribunal upheld the order of penalties.

6. Being aggrieved by this decision of the Tribunal, the assessee-applicant has preferred both these references. These separate references have been made by the Tribunal in view of the fact that the penalties have been imposed under the State Act as well as the Central Act. So far as Reference No. 21 of 1969 is concerned, it relates to the penalty imposed u/s 36(1) of the State Act. In this reference the Tribunal has referred the following question to this court for its opinion :

"Whether under the facts and in the circumstances of the case distribution of

some of the manufactured goods as samples without charging any price amounts to violation of the declaration in form 15 u/s 12(1) of the Bombay Sales Tax Act, 1959, so as to attract penalty u/s 38(1) of the Act."

7. In Reference No. 22 of 1969, which relates to the penalty imposed under the Central Act, the following question is referred to this court :

"Whether under the facts and in the circumstances of the case distribution of some of the manufactured goods as samples without charging any price amounts to violation of the declaration in form "C" under 8(4) of the Central Sales Tax Act, 1956, so as to attract penalty u/s 10-A of the Central Act."

8. The Tribunal has disposed of the matter by a common judgment and since the points of law and facts involved in both these references are the same, we also propose of both the references by a common judgment.

9. Before touching the merits of the points involved in both these references, it would be useful to make a reference to the relevant provisions of the State Act as well as the Central Act.

10. So far as the State Act is concerned, it is section 12 which contemplates the certificates required to be given by a recognised dealer. This section 12 is about the deduction, which are contemplated to be given to authorised dealers, recognised dealers or licensed dealers. Clause (b) of sub-section (1) of section 12 is enacted with reference to recognised dealers. Now according to section 2(23) of the State Act, a recognised dealer means "a registered dealer who holds recognition". The word "recognition" means "recognition granted u/s 25 of the Act". It is not necessary to reproduce the provisions of section 25, but it would be sufficient to state that it contemplates recognition to be given to a registered dealer, who manufactures taxable goods and the value of the goods so manufactured by him exceeds Rs. 2,500. Now when such a recognised dealer purchases goods for use by him in the manufacture of other articles for sale, he becomes entitled to the deductions contemplated by section 12, if he gives a certificate in a prescribed form. This will be evident by the following relevant portion extracted from section 12 of the State Act :

"12. (1) There shall not be deducted from the turnover of sales, sales of goods to an authorised dealer, recognised dealer or licensed or to a commission agent holding a permit purchasing on behalf of his principal, as provided in section 7, 8, 9 and 10, unless -

(a)

(b) the recognised dealer certifies in the prescribed form, that the goods not being goods described in Schedule B, or at entries 1 to 11 (both inclusive and 15 in Schedule C or at entries 1 to 4 (both inclusive) in Schedule D and at entries 1 and 2 in Schedule E or specified in the notification in issued u/s 25 sold to him are goods of the class specified in his recognition and are purchased by him for use by him in the manufacture or packing of taxable goods for sale by him."

The form, which is contemplated by the above-quoted clause (b) of section 12(1) is prescribed by rule 21 of the Bombay Sales Tax Rules, 1959. The relevant portion of that form given an undertaking that the goods purchased by a recognised dealer "will be used in the manufacture of taxable goods for sale". It is thus evident that by giving a certificate in form 15, the recognised dealer who gives that certificate undertakes to use the goods in question in the manufacture of taxable goods for sale.

11. Now in cases where the goods are used contrary to the certificate given under form 15, the dealer in question incurs penalty contemplated by section 36. The relevant portion of this section 36 of the State Act says that where any dealer or commission agent purchases any taxable goods under a certificate given by him u/s 11 or 12, and contrary to such certificate the goods are used for another purpose, or are not resold or despatched in the manner and within the period certified, then the Commissioner may, after giving such dealer or commission agent a reasonable opportunity of being heard, by order in writing impose on him, in addition to any tax payable, a penalty as prescribed by the different clauses of that section, to which reference is not necessary in these matters. It is thus evident from this sub-section (1) of section 36 that if the goods "are used for another purpose" contrary to the certificate given in form 15, the dealer in question would be liable to the penalty contemplated by that section. Therefore, the contention of the department in these cases is that since the applicant-assessee has used the manufactured goods not for sale but for distribution of free samples, such a use of these articles is contrary to the certificate, which says that the goods purchased at the time of giving certificate were goods meant to be used in the manufacture "for sale". The contention of the department, in other words, is that if a portion of the manufactured articles is used for distribution of free samples, then there is an infringement of the undertaking given by form No. 15 inasmuch as the said distribution of free samples does not amount to "sale".

12. Now coming to the Central Act the relevant provisions as regards certificate are found in section 8 thereof. Sub-section (1) of section 8 provides for concessional rate of tax on turnover. Sub-section (1) is in the following terms :

"8. (1) Every dealer, who in the course of inter-State trade or commerce -

(a) sells to the Government any goods; or

(b) sells to a registered dealer other than the Government goods of the description referred to in sub-section (3);

shall be liable to pay tax under this Act, which shall be two per cent. of his turnover."

The rate of two per cent. referred to above was introduced with effect from 1st April, 1963, but before that the said rate was one per cent. The above sub-section refers to the description of goods as found in sub-section (3). It is,

therefore, necessary to see what are the relevant provisions of sub-section (3). It is clause (b) of sub-section (3) which is relevant for our purpose. The said clause is as under :

"(3) The goods referred to in clause (b) of sub-section (1) -

(b) are goods of the class or classes specified in the certificate of registration of the registered dealer purchasing the goods as being intended for resale by him or subject to any rules made by the Central Government in this behalf for use by him in the manufacture or processing of goods for sale or in mining or in the generation or distribution of electricity or any other form of power."

Sub-section (4) of this section of the Central Act provides for a declaration in order to avail of the benefit contemplated by sub-section (1) thereof. The relevant portion of this sub-section (4) is as under :

"(4) The provisions of sub-section (1) shall not apply to any sale in the course of inter-State trade or commerce unless the dealer selling the goods furnishes to the prescribed authority in the prescribed manner -

(a) a declaration duly filled and signed by the registered dealer to whom the goods are sold containing the prescribed particulars in a prescribed form obtained from the prescribed authority."

The prescribed form which is referred to above is "C" form and it contains an assurance that the goods purchased "are for use in the manufacture of goods for sale." It is thus evident from all these provisions of section 8 of the Central Act read together with "C" form that the goods purchased should be the goods to be used in manufacturing articles "for sale". These provisions are, therefore, in pari materia with the provisions of the State Act, referred to above.

13. It is further found that sections 10 and 10-A of the Central Act provide for penalties whenever a breach of the undertaking given in the declaration "C" form takes place. Section 10 says that if any person after purchasing any goods for any of the purposes specified in clause (b) of sub-section (3) of section 8 fails, without reasonable excuse, to make use of the goods for any such purpose, he shall be punishable as prescribed in the section. This section contemplates penalty by way of imprisonment and, therefore, also contemplates a prosecution. But section 10-A of the Central Act contemplates the imposition of penalty in lieu of prosecution. According to that section, if a person purchasing goods is guilty of an offence under clause (d) of section 10, the authority who granted him a certificate of registration under the Act, may after giving him reasonable opportunity of being heard, by order in writing, impose upon him penalty as prescribed in the section. The sales tax authorities have taken recourse to the provisions of this section at the time of imposing the above-stated penalty, for breach of undertaking given in form "C".

14. These are the relevant provisions of the State Act as well as the Central Act, which are required to be considered in these references. The point to be noted is

that the undertaking, which is contemplated by section 12(1)(b) and form No. 15 of the Bombay Act (State Act) and the undertaking contemplated by section 8 and form "C" of the Central Act, are practically the same. Under the Bombay Act, the undertaking, which is contemplated, is that the goods should be "used in the manufacture of taxable goods for sale" while the undertaking contemplated by the Central Act is that they should be goods "for sale by the dealer in the manufacture of goods for sale". Thus, the nature of the undertakings being the same in both the statutes, the points for consideration, which arise at the time of interpretation of these undertakings, would also be the same.

15. We find that, on the other hand, the penalty which is contemplated by the relevant provisions of both the statutes for breach of undertaking is also practically the same with only one difference that the Central Act specifically exempts a dealer from penalty if he is able to show that the goods are not used in accordance with the undertaking for some "reasonable excuse". This will be evident if a reference is again made to the provisions contained in section 36 of the State Act and section 10(d) of the Central Act. It may be noted that while section 36 of the State Act contemplates penalty if the goods are "used for another purpose", 10(d) of the Central Act contemplates a penalty if a dealer "fails without reasonable excuse to make use of the goods for any such purpose."

16. Now the question which arises to be considered in both these references is whether the assessee-applicant has committed any breach of the undertakings given by it in form No. 15 of the State Act form "C" of the Central Act by distributing free samples of the manufactured articles to others. Can it be said that the goods covered by the free samples were not the goods used in the manufacture "for sale" ? It would be obvious from the above provisions of both the statutes that the breach which invites penalty consists in using the goods, which are purchased in form No. 15 and form "C" for any purpose other than the purpose of manufacture or for sale. It is not in dispute that the samples, which are distributed by the assessee free of charge to others, do belong to the lot of those articles in the manufacture of which, the goods purchased under form 15 and form "C" were utilised. But the argument of the department is that since these samples were not sold for a price, it must be presumed that the goods, which were utilised in the manufacture of these articles and which were covered by the undertakings in form No. 15 and form "C" were not the goods meant for sale.

17. In order to appreciate this contention of the department, one thing which should be borne in mind is that the above referred provisions of the State Act as well as the Central Act do not require that the articles manufactured must actually be "sold". What the law requires is that the goods covered by form No. 15 and "C" form should (1) be used in the manufacture of some articles and (2) such articles must be the goods "for sale" Now when a manufacturer manufactures some goods "for sale", the whole lot, which is so manufactured, is manufactured only "for sale". But if, for some reasons, the whole of such a lot is

not actually sold, the goods covered by the unsold lot do not cease to be the goods manufactured "for sale". Therefore, while considering whether a particular lot of manufactured articles was manufactured "for sale" or not, it is not relevant to consider whether the goods covered by the said lot are actually sold in the market. Sometimes, the actual sale of manufactured goods in the market becomes impossible for various reasons. Taking the instance of pharmaceutical goods, as in this case, if the manufacturer is not able to sell all these goods in the market within the date of expiry for use of the goods and if he thus finds that a portion of the manufactured goods has become useless for any purpose whatever, can it be said that the goods, which are utilised for the manufacture of these articles, were not meant for being manufactured "for sale". Taking another instance, if during the process of manufacture some of the goods purchased under form 15 or "C" form are wasted on account of some defect in the process of manufacturing, can it be said that these goods were not used in the manufacture of articles "for sale". In our opinion, a proper and correct answer to these questions would be in the negative, and if that is so, at the time of deciding the question whether the goods purchased after giving the undertaking contemplated by form 15 and "C" form, were purchased for being used in manufacturing articles "for sale", it is not at all relevant to consider whether the finished articles in manufactured form were actually sold or not.

18. In this view of the matter, it follows that the criterion to decide whether the goods were manufactured "for sale" is not the actual sale of the finished articles. Therefore, if the articles are in fact manufactured for sale and if the goods covered by form No. 15 and "C" form are used in the said manufacture, then, in our opinion, the undertakings given by the certificate in form No. 15 and form "C" are complied with irrespective of the question whether the goods are actually sold or not.

19. The next point which now arises to be considered in view of what we have said above, is whether in case where samples of manufactured goods are supplied free of charge, in order to effect the sale of the whole lot of manufactured articles, can it be said that the goods covered by such samples were not manufactured "for sale". While appreciating this point, one important fact which should be borne in mind is that in an economy which recognises private enterprise where sale of marketable is based on competition, supply of samples is inevitable in certain circumstances. In certain types of business such samples are required to be supplied free of charge in order to effect the sale. In this case we are concerned with pharmaceutical articles, which are manufactured by the assessee-applicant and, therefore, we would concentrate our attention on the nature of the said articles. In our opinion, it cannot be gainsaid that pharmaceutical articles, which are used as medicines cannot reach a customer unless they are recommended by doctors. It cannot also be gainsaid that the doctors would not prescribe these articles to the patients unless they are sure that they would prove to be effective in curing the concerned ailment. Under these circumstances, the manufacturers of such pharmaceutical articles, which

are used for medicines, cannot effect the sale of their products so long as free samples of such a product are not distributed amongst the doctors, who can test the potency and medical value of these articles. Therefore, speaking of the articles, which are manufactured by the assessee, we have no doubt in our mind that free supply of samples of these articles is an essential part of the sale of the rest of the articles of the lot manufactured. Unless the articles are thus supplied free of charge and unless the usefulness of the articles is proved, the rest of the articles of the lot manufactured cannot be sold in the market. In other words, in order that the sale of the lot manufactured with the aid of the goods covered by the undertakings contemplated by forms Nos. 15 and "C" can be effectively made, distribution of free samples is quite essential. Such a distribution of free samples, therefore, forms an integral part of the process of sale. The sale of the rest of the articles, which are supplied on price, is generally dependent upon such distribution of free samples. Moreover, when a manufacturer supplies a portion of the goods as free samples, the cost which that manufacturer has incurred in manufacturing these samples is always taken into account by him in fixing the price of the rest of the articles of that lot manufactured by him. Therefore, when that part of the lot, which is supplied on payment of price, is sold in the market, the value of that lot so realised, includes within itself even the value of the samples supplied without charge. This value being the turnover of sales, it becomes liable to the payment of sales tax to the Government. Thus, albeit indirectly, the revenue does get sales tax even on the value of the samples, which are freely supplied by the manufacturers. This aspect of the case further emphasises our view that free supply of samples of a particular lot of manufactured articles, forms an essential and an integral part of the sale, and if that be so, it is not possible to say that the goods, which were utilised in manufacturing the free samples were not used for manufacturing articles "for sale". In our opinion, therefore, it is not possible to hold that by supplying some of the samples of the manufactured lot freely, the applicant-assessee has committed any breach of the undertaking given by him either in form No. 15 or form "C" so as to attract the penal provisions of section 36 of the State Act and section 10-A of the Central Act.

20. Here we would like to add one more aspect so far as section 10-A of the Central Act is concerned. We have also noticed above that penalty u/s 10-A of the Central Act can be imposed only if there is a breach contemplated by clause (d) of section 10 of that Act. Now if again a reference is made to the said clause (d) of section 10, it will be found that the penalty contemplated by that section is invited only if the concerned dealer fails to make use of the goods in accordance with the undertaking without reasonable excuse. Now, looking to the facts of these cases, can it be said that the applicant-assessee has failed to make use of the goods covered by the undertaking in form "C" without reasonable excuse ? If once it is believed that distribution of free samples was a sine qua non of effecting sale of all the goods manufactured by him, it is not possible to contend successfully that such a distribution was without reasonable excuse.

21. In view of this discussion, our answers to the questions referred to us in both the references are in the negative. These references are accordingly disposed of. The opponent-Commissioner of Sales Tax shall bear the costs of the applicant-assessee in the both references.

22. References answered in the negative.