
(2002) 08 KL CK 0032
In the High Court Of Kerala
Case No : W.A. No. 3096 of 2001

Siemens Ltd.

APPELLANT

Vs

State of Kerala

RESPONDENT

Date of Decision : 05-08-2002

Acts Referred:

Kerala General Sales Tax Act, 1963 — Section 5, 7(7B)
Kerala General Sales Tax Rules, 1963 — Rule 22A, 22A(2)

Citation : (2002) 3 ILR (Ker) 289 : (2002) 125 STC 544

Hon'ble Judges : K.K. Denesan, J;J.B. Koshy, J

Bench : Division Bench

Advocate : Jose Joseph, for the Appellant; Raju Joseph, Government Pleader, Latha Krishnan and K. Anand, for the Respondent

Final Decision : Allowed

Judgement

J.B. Koshy, J.—This Writ Appeal is filed questioning the correctness of the judgment of the learned Single Judge upholding the validity of Sub-section (7B) of Section 7 of the Kerala General Sales Tax Act, 1963 and Rule 22A(2) of the Kerala General Sales Tax Rules, 1963. Before going into the merits of the legal contentions, we may look into the facts.

2. The appellant is a company registered under the Indian Companies Act, 1956 having its registered office at Mumbai. It is a dealer registered under the Kerala General Sales Tax Act, 1963 (for short "KGST Act" and under the Central Sales Tax Act, 1956 (for short "CST Act"). Appellant is a manufacturer-cum-dealer of electrical and electronic goods. A customer from Ernakulam placed an order with the appellant for supply of one Somatom Ar. Whole Body CT Scanner at a total cost of Rs.55 lakhs. As per the above order, appellant had to supply the CT Scanner from its factory at ex-Goa and carry out the installation of the equipment at free of cost at Cochin. Installation work was incidental. According to the appellant, transaction was in a sense in inter-State sale assessable at Goa. Appellant has remitted Rs. 1,07,843.14 as tax at Goa. Details of the contract can

be seen from Exts. P1 and P2 and Ext. P3 is the invoice. But, by Ext. P4 dated 21.10.1999, appellant's customer was issued with a notice directing them to deduct a tax at 8% on the bill amount and remit the same with 10% surcharge on it. By Ext. P5 dated 6.12.1999, appellant requested to issue a certificate for non-deduction of TDS as it is mainly a direct inter-State sale and appellant is a registered dealer. By Ext. P6, appellant was informed by the third respondent that provision of CST Act has no application since the appellant supplied the equipment and erected it and, therefore, pay tax under the KGST Act. Appellant's representation to fourth respondent was also rejected by a one line letter stating that no intervention is required at that stage.

3. Similarly, appellant entered into a contract with the 6th respondent, a Kerala Government undertaking for construction of 110 K.V. Sub Station for a sum of Rs. 3,93,90,523/-. Exts. P11 and P12 show the details of the contract. According to the appellant, after deducting the annual maintenance charges, local purchases, inter-State supply and specified goods and pure labour value tax payable under K.G.S.T. Act will only be Rs. 31,94,995.04 and, therefore, they requested tax deduction certificate for Rs. 1,59,750/- being 5% value of Rs. 31,94,995.04 by Ext. P13. But, that was also refused. According to the appellant, provision for payment of advance tax to the entire value of the contract amount irrespective of the fact whether it is taxable or not is illegal and unconstitutional.

4. Sub-section (7B) of Section 7 of the KGST Act, substituted by Act 19/94 with effect from 1.4.1994 reads as follows:

"(7B). Every awarder shall deduct tax at the rate of two per cent in respect of civil contracts and five per cent in respect of other contracts from the payments made by him to any contractor liable to tax u/s 5, at every time, including advance payments, and remit it to the Government within seven days from the date of such deduction in the prescribed manner".

In 1998 it was further amended as follows with effect from 1.4.1998:

"(7B). Every awarder shall deduct tax at the rate of two per cent in respect of civil contracts and five per cent in respect of other contracts from the payments made by him to any contractor liable to pay tax u/s 5, and who is registered u/s 13 and at the rate of seventy percent of the rates shown in the Fourth Schedule against such contract where the transfer of goods involved in the execution of works contract is not in the form of goods or, as the case may be, at the rate applicable to the goods under this Act, where such transfer is in the form of goods, from any other contractor liable to tax u/s 5, at every time, including advance payments and remit it to the Government on or before the fifth day of the succeeding month from the date of such deduction in the prescribed manner."

5. Rule 22A of the Kerala General Sales Tax Rules, 1963 as amended in 1994 reads as follows:

"22A. Payment and recovery of tax in works contract:- (1) In the case of works

contract on which tax is payable in accordance with the provisions of the Act whether an option under Sub-section (8) of Section 7 is made or not, the tax shall be paid either by the contractor in accordance with the rules.

(2) Wherever payment is made by the awarder to the contractor either in lump sum for the whole contract or in instalments, the awarder shall withhold an amount equal to two per cent of such payment or payments in the case of civil contracts and five per cent in the case of other contracts where the contractor is registered u/s 13 and at the rate of seventy per cent of the rates shown in the Fourth Schedule against such contract where the transfer of goods involved in the execution of works contract is not in the form of goods, or, at the rate applicable to the goods under the Act, where such transfer is in the form of goods from such payment or payments and shall remit it to the assessing authority to whom the contractor is registered as a dealer and if he is not so registered, to the assessing authority having jurisdiction over the place of works contract, on or before the fifth day of the month succeeding the month in which the deduction is made along with a statement in Form No. 21C:

Provided that no amount under this sub-rule shall be deducted if there is no transfer of goods involved in the execution of the works contract.

(3) Notwithstanding anything contained in Sub-rule (2) above, any contractor who pays tax regularly in accordance with the rules, on production of a certificate issued to that behalf issued by the assessing authority shall be entitled to payment of the contract amount without deduction of sales tax due on the contract for the period and to the extent or for the works contract specified in the certificate.

(3A) Any contractor may apply to the assessing authority in Form No. 21CA for the issue of such a certificate. The assessing authority, if it is satisfied that the applicant complies with the requirement of Sub-rule (3), may issue a certificate in Form No. 21CB.

(4) Notwithstanding anything contained in Sub-rule (2), if the total turnover in respect of a contractor for a year does not exceed the assessable limit prescribed u/s 5, the amounts recovered and remitted by any awarder under Sub-rule (2) for the period shall be refunded or adjusted as the case may be by the assessing authority.

(5) Any awarder who effects any payment of any contract amount without deduction of the amount prescribed under Sub-rule (2), shall be liable to pay the said amount and shall be recovered from him as if it were a tax due from him. All provisions relating to recovery of tax including provisions relating to penalty and interest shall apply to such awarder as if he were a dealer liable to pay tax under the Act, irrespective of the limit of turnover prescribed u/s 5.

(6) The amount deducted by the awarder from the payments due to the contractor and remitted under Sub-rule (2) shall be adjusted against the amount

finally assessed on the contractor under Sub-rule (13) of Rule 21 and shall be dealt with in accordance with Sub-rule (14) thereof.

Provided that this rule shall not apply to any contractor whose total turnover in a year does not exceed the assessable limit prescribed in Section 5.

Provided further that when the contract amount does not exceed rupees fifty thousand in the year, the awarder may effect payment of the contract amount after getting a declaration in duplicate (one copy to be forwarded to the assessing authority) from the contractor to the effect that his total turnover for the year does not exceed rupees fifty thousand".

6. Sub-section (7B) of Section 7 of the Act as it stood prior to 1.4.1994 only provided for deduction of the tax u/s 5(1)(iv) or under Sub-sections (7) and (7A) from the payments made to the contractors and option was also allowed. But, Sub-section (7B) as inserted by the Finance Act, 1994 provides for deduction of tax at the rate of two per cent in respect of civil contracts and five per cent in respect of other contracts by the awarder from payments made to the contractor liable to pay tax u/s 5. Sub-section (7B) mandates the deduction of the amount specified therein which is a percentage of the contract amount. Sub-section (7B) clearly provides that the deduction must be made only from persons who are liable to pay tax u/s 5 of the Act. The measure of the tax under the said sub-section is the quantum of the contract amount without any deduction of the turnover of export sales, outside sales or inter-State sales which are outside the purview of the State legislation. The provisions of Rule 22A(2) also provides for the deduction of the amount specified in Sub-section (7B) from the payments made by the awarder every time.

7. Before the amendment, deduction of tax from payments made to the contractor at fixed rate was optional. Before the introduction of present Rule 22A(2), Rule 22A(1) of the K.G.S.T. Rules provided for payment of tax in accordance with the Rules in the case of works contract.

8. It is the main contention of the appellant that the charging provision under the K.G.S.T. Act is relatable to Article 366(29A)(b) of the Constitution of India, i.e., Section 5(1)(iv) of the K.G.S.T. Act authorises levy of tax only on the taxable turnover excluding turnover relatable to the sale in the course of inter-State trade, outside-State sale, sale in the course of import and other permissible deductions. The Supreme Court in *Steel Authority of India Ltd. v. State of Orissa and Ors.* ((2000) 118 STC 297) held that a provision designed to collect tax in advance without excluding transactions falling outside the purview of the State Act is not sustainable. Therefore, so long as the amended Sub-section (7B) authorises the State Government to deduct tax on the entire turnover including the turnover covered by inter-State sales and sales on import, it is unsustainable.

9. Sub-section (7B) of Section 7 of the Act as it stood prior to 1.4.1994 only provided for deduction of tax u/s 5(1)(iv) of the Act or under Sub-sections (7) and (7A) from the payments made to the contractors. But, Sub-section (7B) as

inserted by the Finance Act, 1994 provides for deduction of tax at the rate of 2% in respect of civil contracts and 5% in respect of other contracts by the awarder from payments made to the contractor liable to pay tax u/s 5. In other words, if a person is liable to pay tax u/s 5, deduction under Sub-section (7B) is compulsory. Sub-section (7B) mandates the deduction of the amount specified therein which is a percentage of the contract amount. Rule 22 A(2) also provides that if there is no transfer of goods at all in the execution of works contract, no tax is payable and in view of Rule 22A(6), any payment made as advance tax is adjustable after final assessment is over. It is true that the amount of deduction under Sub-section (7B) of Section 7 of the Act read with Rule 22A is only provisional and final assessment has to be done subsequently. Even under Sub-rule (3) of Rule 22A to get a certificate, assessment must be over to any tax; but, Sub-section (7B) mandates payment of advance tax without any option except in cases where there is no transfer of goods at all.

10. Now, we may consider the decision of the Supreme Court in *Steel Authority of India Ltd. v. State of Orissa and Ors.* ((2000) 118 STC 297. A three-member Bench of the Supreme Court was considering the provisions in the Orissa Sales Tax Act. Deduction of tax u/s 5 (Section 13AA of the Orissa General Sales Tax Act) which deals with deduction of sales-tax at source. Section 13AA of the Orissa General Sales Tax Act reads as follows:

"13AA. Deduction of tax at source from the payment to works contractors :- (1) Notwithstanding anything contained in Section 13 or any other law or contract to the contrary, any person responsible for paying any sum to any contractor (hereinafter referred to in this section as the "deducting authority") for carrying out any works contract, which involves transfer of properly in goods, in pursuance of a contract between the contractor and-

- (a) Central Government or any State Government, or
- (b) any local authority, or
- (c) any authority or corporation established by or under a statute, or
- (d) any company incorporated under the Companies Act, 1956 (1 of 1956) including any State or Central Government undertaking, or
- (e) any co-operative society or any other association registered under the Societies Registration Act, 1860 (21 of 1860),

shall, at the time of credit of such sum to the account of the contractor or at the time of payment thereof in cash or by issue of a cheque or draft or any other mode, whichever is earlier, deduct an amount towards sales tax equal to four per cent of such sum in respect of the works contract, if the value of the works contract exceeds rupees one lakh.

(2) While making deduction as referred to in Sub-section (1), the deducting authority shall grant a certificate to the contractor in the form prescribed and

shall send a copy thereof to the Sales Tax Officer within whose jurisdiction the works contract is executed.

(3) The amount deducted from the bills or invoices shall be deposited into the Government treasury within one week from the date of deduction in such form or challan as may be prescribed.

(4) Such deposit into the Government treasury shall be adjusted by the Sales Tax Officer towards the sales tax liability of the contractor and would also constitute a good and sufficient discharge of the liability of the deducting authority to the contractor to the extent of the amount deposited.

(5) (a) Where, on an application being made by the contractor in this behalf, the Commissioner is satisfied that any works contract of the nature referred to in Sub-section (1) involves both transfer of property in goods and labour or service, or involves only labour or service and, accordingly, justifies deduction of tax on a part of the sum in respect of the works contract or, as the case may be, justifies no deduction of tax, he shall, after giving the contractor a reasonable opportunity of being heard, grant him such certificate as may be appropriate, in the manner prescribed:

Provided that nothing in the said certificate shall affect the assessment of the sales tax liability of the Contractor under this Act.

(b) Where such a Certificate is produced by a contractor before the deducting authority, until such certificate is cancelled by the Commissioner, the deducting authority shall either make no deduction of tax or make the deduction of tax as the case may be, in accordance with the said certificate.

(6) If any person contravenes the provisions of Sub-section (1) or (2) or (3) or of clause (b) of Sub-section (5), the Sales Tax Officer shall, after giving him an opportunity of being heard, by an order in writing impose on such person penalty not exceeding twice the amount required to be deducted and deposited by him into Government treasury".

11. Sub-section (5)(a) takes no account of the fact that even if a works contract involves both the transfer of property in goods and labour or service, State sales tax may not be payable upon the entire value ascribable to the transfer of property in goods for the reason that it is in the course of inter-State sale, an outside sale or a sale in the course of import or export; nor is such account taken elsewhere in that section. The person responsible for paying any sum to the contractor is required by Section 13AA(1) to deduct towards the contractor's liability to State Sales Tax, 4 percent of such amount as he credits or pays to the contractor, regardless of the fact that the value of the works contract includes the value of goods transferred in the course of inter-State sale, or by way of outside sale or sale in the course of import, despite provision for issuing a certificate under Sub-section (5) similar to Rule 22A(3) of the K.G.S.T. Rules.

12. In *Bhawani Cotton Mills Ltd. v. State of Punjab*, (1967) 20 STC 290, the

Supreme Court said:

"If a person is not liable for payment of tax at all, at any time, the collection of a tax from him with a possible contingency of refund at a later stage, will not make the original levy valid; because, if particular sales or purchases are exempt from taxation altogether, they can never be taken into account, at any stage, for the purpose of calculating or arriving at the taxable turnover and for levying tax".

Like the Orissa Act wherein it was stated that the Act is applicable to the State of Orissa, the Preamble to the K.G.S.T. Act, 1963 also provides as follows:

"Whereas it is expedient to consolidate and amend the law relating to the levy of a general tax on the sale or purchase of goods in the State of Kerala."

13. Section 2(xxv) defines "taxable turnover" under the K.G.S.T. Act. We extract the same:

"(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;"

14. It is made clear that taxable turnover shall not include turnover for 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. Even though it is stated that only a person taxable under the K.G.S.T. Act need pay sales tax, the amount payable is for the entire turnover including non-taxable turnover. Accepting the provision that only a person liable to pay tax need pay advance tax, we see no difference between Section 13AA of the Orissa Act as amended in 1993 and the present amendment in the K.G.S.T. Act. While considering the above section of the Orissa Act, the Supreme Court in Steel Authority of India's case (supra) held as follows:

"13. There can be no doubt, upon a plain interpretation of Section 13AA, that it is enacted for the purposes of deduction at source of the State sales tax that is payable by the contractor on the value of a works contract. For the purposes of the deduction neither the owner nor the Commissioner who issues to the contractor a certificate u/s 13AA(5) is entitled to take into account the fact that the works contract involves transfer of property in goods consequent upon of an inter-State sale, an outside sale or a sale in the course of import. The owner is required by Section 13AA(1) to deposit towards the contractor's liability to State sales tax four per cent of such amount as he credits or pays to the contractor, regardless of the fact that the value of the works contract includes the value of inter-State sales, outside sales or sales in the course of import. There is, in our view, therefore, no doubt that the provisions of Section 13AA are beyond the powers of the State Legislature for the State Legislature may make no law

levying sales tax on inter-State sales, outside sale or sales in the course of import".

15. A contention was raised in the Steel Authority of India's case that advance tax payable is only 4% whereas for taxable turnover the rate of tax is 8%. Here, the very same contention was raised that in respect of civil contracts, advance tax payable is only 2% and 5% in the case of other contracts and it is finally adjustable also. The same contention was advanced and repelled by the Supreme Court in the above case as follows:

"It was then contended by the learned counsel for the State that the preamble of the Orissa Sales Tax Act took account of the fact that that statute was limited to the sale or purchase of goods in Orissa. Unfortunately, it would appear that the State Legislature overlooked its limitations, even as contained in the preamble, when enacting Section 13AA. It was also contended that the deduction that was required to be made u/s 13AA(1) was of four per cent of the amount credited or paid by the owner to the contractor, whereas the sale tax liability of the contractor thereon was eight percent. It was contended that this requirement proceeded on the assumption that half of the amount was not liable to tax being in respect of inter-State sales, outside sales and export sales. No such assumption based on the rate of tax at any given point of time can be made. Section 13AA should have been precisely drafted to make it clear that no tax was levied on that part of the amount credited or paid that related to inter-State sales, outside sales and sales in the course of import, particularly after the previous Section 13AA had been struck down by the Orissa High Court for the reason that it was couched in terms wider than were permissible to the State Legislature and that judgment was accepted."

16. Following the above decision, similar provisions in the Himachal Pradesh General Sales Tax Act (S. 12A and Rule 31A) were struck down by the Supreme Court in *Nathpa Jhakri Jt. Venture v. State of Himachal Pradesh and Ors.* (2000) 118 STC 306. In Himachal Pradesh case also, deduction was 2% and 4% like Kerala Act. In paragraph 4, the Supreme Court held as follows:

"4. A bare perusal of the two provisions will make it clear that in either provision there is an obligation to deduct from transactions relating to works contract on bills or invoices raised by the works contractor an amount not exceeding 4% or 2%, as the case may be. Though the object of the provision is to meet the tax in respect of the transactions on all works contract on the valuable consideration payable for the transfer of property in goods involved in the execution of the works contract, the effect of the provision is that irrespective of whether the sales are inter-State sales or outside sales or export sales which are outside the purview of the State Act and those transactions in respect of which no tax can be levied even in terms of the enactment itself, such deductions have to be made in the bills or invoices of the contractors. To say that if a person is not liable for payment of tax inasmuch as on completion of the assessment refund can be obtained at a later stage is no solace, as noticed in *Bhawani Cotton Mills Ltd. Vs.*

State of Punjab and Another, . Further, there is no provision for certification of the extent of the deduction that can be made by the authority. Therefore, we must hold that arbitrary and uncanalised powers have been conferred on the concerned person to deduct upto 4 per cent from the sum payable to the works contractor irrespective whether ultimately the transaction is liable for payment to any sales tax at all. In that view of the matter, we have no hesitation in rejecting the contention advanced on behalf of the State".

17. The State mainly relied on the earlier decision of the Supreme court in State of Kerala and Anr. v. Builders" Assn. of India and Ors., (1997) 104 STC 134. In that case, the Supreme Court upheld the earlier provision and Section 7A of the K.G.S.T. Act because payment of fixed percentage of the total contract amount before the amendment was optional. The Supreme Court held as follows:

"..... The impugned sub-sections have evolved a convenient hassle-free and simple method of assessment just as the system of levy of entertainment tax on the gross collection capacity of the cinema theatres. By opting to this alternate method, the contractor saves himself the botheration of book-keeping, assessment, appeals and all that it means. It is not necessary to enquire and determine the extent or value of goods which have been transferred in the course of execution of a works contract, the rate applicable to them and so on. For example, under Sub-section (7), the contractor pays two per cent of the total value of the contract by way of tax and he is done with all the abovementioned botheration. The rate of two per cent prescribed by Sub-section (7) is far lower than the rates in First, Second and Fifth Schedules referred to in Section 5(1)(iv) (a). In short, Sub-sections (7) and (7A) evolve a rough and ready method of assessment of tax and leave it to the contractor either to opt to it or be governed by the normal method. It is only an alternative method of ascertaining the tax payable, which may be availed of by a contractor if he thinks it advantageous to him." .

Therefore, the Supreme Court earlier upheld before the amendment of Sub-section (7B) because liability to pay fixed percentage of contract amount was optional. It was for the assessee to opt for the method. Here, under Sub-section (7B) of Section 7, there is no such option. There is no method of certification for excluding the turnover covered by a inter-State sales, import etc. on which State has no jurisdiction to assess sales tax. Therefore, we see that after the amendment, the present provisions are in pari materia the provisions of the Orissa Act and Himachal Pradesh Act which are struck down by the Apex Court. In the above circumstances, we are of the view that in view of the compulsory nature of payments under Sub-section (7B) of Section 7 which an assessee to pay sales tax to the State of Kerala for turnover inclusive of inter-State sales, sales by import etc. which are specifically outside the jurisdiction of the State is clearly illegal and, therefore, these sections are liable to be set aside.

18. Sub-section (7B) of Section 7 of the Act as amended is applicable only if the contractor is "liable to pay tax u/s 5". But, if he is liable to pay tax and there is

transfer of property in respect of even 1% of the total contract amount, he is bound to pay advance tax on provisional basis for the entire turnover including the turnover in respect of inter-State sales, outside sales and import sales. The principles laid down by the Constitution Bench of the Supreme Court in the decision in Bhawani Cotton Mills" case (supra) and in Steel Authority of India"s case (supra) is binding. Unlike the earlier provision, there is no option for the assessee to pay fixed percentage of contract amount or actual tax payable under the present Sub-section (7B) of Section 7. If part of the total amount involves in the transfer of goods, one is obliged to pay tax on the entire contract amount including the amount on which State Legislature has no power to tax. It is true that as held by the learned Single Judge that on the basis of the decision of the Supreme Court in Sardar Baldev Singh Vs. Commissioner of Income Tax, Delhi and Ajmer, , Commissioner of Commercial Taxes v. Ramakrishnan Shrikrishnan Jhaver, (1967) 20 STC 453 and Chaturbhai M. Patel Vs. Union of India (UOI) and Others, in the case of a taxing statute, it is open to the legislature to enact provisions which would check evasion of tax and that the power to tax includes the power to provide the means to make the realisation of the tax effective. But, that is not an excuse to collect tax on turnover which the State has no jurisdiction to collect tax as held by the Constitution Bench in Bhawani Cotton Mills Ltd. v. State of Punjab, (1967) 20 STC 290. But State Government cannot levy tax even provisionally on turnover which it has no jurisdiction at all to tax and, therefore, the same defect as noticed by the Supreme Court in the Orissa Act and Himachal Pradesh Act in (2000) 118 STC 297 and 306 is there in the amended Sub-section (7B) of Section 7 and consequent rules.

In the above circumstances, we declare that Sub-section (7B) fo Section 7 of the KGST Act and Rule 22A(2) of the KGST Rules brought into force on 1.4.1994 are ultra vires as beyond the legislative competence of the State so long as it enables the State to collect tax inclusive of turnover covered by inter-State sales, sales in the course of import, sales outside the State etc. for which State has no jurisdiction to collect sales tax. Revisional authorities are directed to dispose of the revision petitions filed by the petitioner as per the law declared.

The Writ Appealis allowed.