

(2006) 11 KAR CK 0046
In the Karnataka High Court
Case No : STRP No. 57 of 2004

State of Karnataka

APPELLANT

Vs

Narrain Mines Ltd.

RESPONDENT

Date of Decision : 10-11-2006

Acts Referred:

Income Tax Act, 1961 — Section 2 (f)
Karnataka Sales Tax Act, 1957 — Section 12 A, 12 A (1-A), 2 (1)

Citation : (2007) ILR (Kar) 1500 : (2007) 3 KCCR 194 SN : (2009) 19 VST 535

Hon'ble Judges : R. Gururajan, J;Jawad Rahim, J

Bench : Division Bench

Advocate : Sujatha, Government Pleader, for the Appellant; S. Prabhakar and M. Venkatesh, for the Respondent

Judgement

Jawad Rahim, J.—State is in appeal against the judgment and order dated 22-12-2003 by the Karnataka Appellate Tribunal, Bangalore in series of Sales Tax Appeal Nos. 943, 944, 945 and 946 of 2003.

2. The facts, which resulted in filling of this appeal by the State, are:

Respondent is a Company registered under the Companies Act, 1956, engaged in mining and sale of Iron Ore within the State of Karnataka. Mining activity of the respondent company are basically within the Chithradurga District. It is assessed under the Karnataka Sales Tax Act and has been periodically submitting its returns.

3. The assessment under KST Act for the year 1997-98, 1998-99, 1999-2000 and 2000-01 were reopened u/s 12-A of the Act by the Assessing Officer. He did so having noticed that the respondent company had engaged contractors for mining operation and during the course of such operation necessarily several vehicles were utilised by the contractors. The obligation of the respondent and the contractors has been recorded under a term of contract. Several terms and conditions and covenants have been agreed upon, inter alia, between them.

4. One of the covenants in the agreement dated 01-04-1997 binding parties is that the respondent would supply diesel for consumption by the contractors during the use of the vehicles for mining operations. Supply of diesel is subject to payment of costs of the diesel by the consumer, namely, contractors. Such amount quantified will be deducted from and out of the amount payable by the respondent - company to the contractors for the mining operation conducted by it. The interim return covered by the Taxation Department reveal certain aspects indicating evasion of tax. The assessment which was done u/s 12-A of the Act was initially at Rs. 11,25,96,024/- and Rs. 10,73,379/- for the assessment year 1997-98 and at Rs. 11,44,69,065/- and Rs. 12,27,759/- for the assessment year 1998-99; at Rs. 23,05,55,306/- and Rs. 21,20,421 for the assessment year 1999-2000 and at Rs. 9,86,61,276/- and Rs. 4,49,270/- for the assessment year 2000-01, being value of interstate purchase of diesel which had not suffered KST.

5. The mandatory covenant in the agreement regarding value of diesel and recovery of the costs from the contractors (consumers) is not disputed. In order to supply the diesel to the contractors for their consumption and utilisation of vehicles was effected after purchase of diesel locally as well as inter-State purchase. The diesel so purchased was stored commonly by the respondent in its pumping station. The Assessing Authority by virtue of reassessment order has levied tax on the diesel supplied by the respondent to the contractors. The same was challenged by the assessee before the first Appellate Authority unsuccessful. Second appeal against the said order was filed before the Tribunal and the Tribunal having considered the plea of the respondent that it had maintained separate accounts, negated the finding of the first Appellate Authority and allowed the appeal. Against that order dated 22-12-2003 the State is in appeal before this Court.

6. Smt. Sujatha, learned Government Pleader appearing for the State would contend that supply of diesel by the respondent to the contractors has not been disputed. Purchase of diesel by the respondent - assessee locally and through inter State purchase is also not in dispute. The respondent had stored the diesel so purchased in single tank and supplied it through its outlet, which has been installed after obtaining permission from the Indian Oil Corporation. Therefore, there is evasion of tax by the respondent, which was rightly brought to levy by the Tax Department. The first Appellate Authority has confirmed the assessment and levy of tax, but the second Appellate Authority misguided itself on certain facts.

7. Smt. Sujatha would contend that the fact that respondent - company has been supplying diesel to the contractors for utilisation of their vehicles and machines is subject to recovery of the costs of diesel from the amount payable by the respondent to the contractors. Therefore, "property" has passed from the respondent to the contractors for value. It falls within the definition of sale as defined under the provisions of Section 2(f) of the Income Tax Act. Once this is established that there is a sale in the manner aforesaid of the diesel by the

respondent to the contractor the tax become liable. If the diesel supplied to the contractors was of locally purchased the diesel could be construed as having suffered tax. But the diesel supplied by the respondent to the contractor is from inter-State purchase, which has not suffered tax, consequently the State tax becomes liable on second sale of diesel after initial purchase in Inter-State sale. This aspect has not been appreciated by the Appellate Tribunal.

8. Our attention was drawn to the reasoning made by the Tribunal in para-12 and 19 of its order, which is relevant, reads thus:

12. The authorities below have not disputed the quantity and value of diesel purchased by the appellant and supplied to the various contractors. Such being the case the allegation that the appellant has not disclosed the turnover willfully to evade tax is not sustainable. Further the total supply of diesel to the contractor in each assessment year is less than the quantity of diesel purchased locally. It is not the case of the authorities below that at any point of time the Supply is exceeded the purchase of diesel from local registered dealers. Therefore, the benefit of doubt should be given to the appellant and to be concluded that the diesel supplied to the contractors is only from the diesel purchased locally but not from interstate purchase. The appellant has produced both the registers, showing separately the purchases of diesel in the course of interstate as well as from local registered dealers. Both the registers have been verified and checked by the intelligence authorities. But neither the intelligence authority nor the authorities below were have rejected the registers nor any defects are pointed out to disbelieve the books of accounts. On the other hand the observations of the authorities below indicates that the appellant has maintained the books of accounts in a verifiable manner.

19. Therefore, we are of the opinion that there is no sale of diesel is involved in the executing the works contract and even the so-called sale is not first sale in the State. The entire supply of diesel to his contractor vehicle is for his own use and it is supplied out of diesel purchasing locally from the registered dealers. Diesel being consumable nothing was left for sale. As such, the assessment orders, treating the same as escaped sales turnover, are liable to be set aside in respect of all the assessment years under appeal. Consequently, the penalty orders passed u/s 12-A(1-A) are also do not survive. Accordingly, we answer the pint No. 1 in the Affirmative.

9. Smt. Sujatha, learned Government Pleader, would relay on the decision in the case of M/s. N.M. Goel and Co. Vs. Sales Tax Officer, Rajnandgaon and another, , wherein similar question had arisen for decision before the Appellate Court. The facts of the said case show that N.M. Goel & Co, a dealer registered under the Madhya Pradesh General sales Tax Act, 1958, made an item rate tender to the PWD for construction of food grain godowns and ancillary buildings. In that tender, prices of the materials used for the construction including cost of iron, steel and cement were included. PWD, however, agreed to supply from its stores the iron, steel and cement and to deduct the prices of the materials so supplied

and consumed in the construction, from the final bill of the appellant. Clause (10) of the contract binding them provided that "if it is required that the contractor shall use certain stores to be provided by the Engineer-in-Charge as shown in the Schedule of materials hereto annexed, the contractor shall be bound to procure and shall be supplied such material and stores as are from time to time required to be used by him for the purposes of the contract only and the value of the full quantity of materials and stores supplied at the rates specified in the said schedule of materials may be set off or deducted from any sums then due or thereafter to the security deposit, or the proceeds or sale thereof if the same is held in Government securities, the same or a sufficient portion thereof being in this case sold for the purpose. The Apex Court dismissing the appeal held thus:

(i) that since the PWD was not a registered dealer the presumption u/s 6(c) applied, that the entry of the goods had been effected by the appellant into the local area before they were purchased by the appellant;

(ii) that in order to attract entry tax not only the property in the goods had to pass from the PWD to the appellant but there had to be an independent contract-separate and distinct-apart from the mere passing of the property: mere passing of property from the PWD to the appellant would not suffice;

(iii) that, in this case, for the performance of the contract, the appellant was bound to procure the materials; but in order to ensure that quality material were procured, the PWD undertook to supply such materials and stores as from time to time were required by the appellant to be used for the purpose of performing the contract only. The value of such quantity of materials and stores so supplied was specified at a rate and got set off or deducted from any sum due or to become due thereafter to the appellant. Clause (10) of the contract read in proper light indicated that a sale inhered from the transaction. By the use or consumption of materials in the work of construction, there was passing of the property in the goods to the appellant from the PWD. By appropriation and by the agreement, there was a sale from the PWD to the appellant as envisaged in terms of Clause (10); and

(iv) that, therefore, the appellant was liable to pay entry tax on the materials supplied by the PWD.

10. The learned Counsel for petitioner also relied on the decision in the case of *Rashtreeya Ispat Nigam Ltd. v. State of Andhra Pradesh* reported in 102 STC 454, wherein following the above referred judgment the Division Bench of Andhra Pradesh High Court held thus:

that the supply of material by the petitioner company to the various contractors on condition of price of the material to be deducted or adjusted from bills payable to the contractors for the work done, would constitute sale of the goods supplied to the contractor. The cement and steel were supplied to the contractor to ensure quality of the material which would go into construction work entrusted to the contractor. The Tribunal was right in holding that the various clauses in the

agreement were introduced only with a view to see that there was no pilferage or misuse of the material so supplied at the control price as the market price was higher and that such condition in the agreement could not be interpreted to say that the petitioner itself remained the owner of the goods even after their supply and consumption as such there was no transfer of ownership and consequently there was no sale. The provision in the contract giving the petitioner the right to make inter unit transfer of goods was made to ensure smooth execution of the work. If on a true interpretation of the agreement it was found that supply of the goods to the contractor constituted sale, the mere fact that it was bound to return the goods after completion of the construction work, on pain and payment of penalty or prosecution, would not alter the nature of the earlier sale transaction.

11. Smt. Sujatha, learned Government Pleader, distinguished the judgment of this Court in the case of Bangalore Water Supply And Sewerage Board, Bangalore v. State of Karnataka reported in 1999(46) KAR.LJ. 1. Finally, she relied on the unreported decision of this Court in STRP 60-61/2002 DD 23-06-2004.

12. Per contra, the learned Counsel appearing for the respondent would contend that in the instant case contractual obligations cast upon the respondent required him to supply of diesel to the contractors for consumption during the utilisation of the vehicles and machineries in mining operations which was the purpose of engaging the contractors. The contractors were obliged under the contract to conduct mining operations had perforce to utilise the vehicle in the remote area where the availability of fuel was difficult. To mitigate the difficulties and unnecessary waste of time in procuring the fuel- diesel and to avoid unnecessary expenditure on such acquisition from the distant places, a covenant was entered into the agreement and agreed upon by the respondent. Accordingly to store the diesel within the nearest point from the mining site so as to make available the diesel. The said diesel was procured locally as also from the interstate sale. It was stored, no doubt, in the single tank in its out let, but the supply of diesel to the contractors was from and out of locally purchased registered dealers, which had tax suffered. The diesel which was procured from interstate sale was utilised by the respondent for its own vehicles and not supplied it to the contractors. In this regard, the assessee has maintained regular accounts and made it available to the Assessing Officer. The Assessing Authority has not found fault with such maintenance of records and has not questioned its authenticity. Therefore, the Assessing Officer was in error in considering the supply of diesel by the respondent to its contractors as "sale" of the diesel purchased interstate. Since, locally purchased diesel is tax suffered item of property no third taxation is permissible.

13. In this view of the matter, the grounds on which the Assessing Officer has levied tax is unsustainable. He also contended that under the Rules and Regulations governing permission to install pumping station do not permit sanction for grant of two pumps. He relies on the licence issued by the Indian Oil

Corporation to the respondent for installing single pump pumping station. Thus it was urged that there was no possibility feasibility of storing locally purchased and interstate purchased diesel in separate tanks. The embargo under the Rules being operative, in the matter of grant of licence, the respondent had no choice but to store the diesel in one tank. The assessee had maintained separate accounts regarding supply of diesel. The quantity of diesel supplied to the contractor was from the locally purchased diesel and hence no tax was leviable. He has placed reliance on the decision of this Court in the case of Bangalore Water Supply and Sewerage Board, Bangalore v. State of Karnataka reported in 1999(46) KAR.LJ. 1.

14. Having heard the learned Government Pleader Smt. Sujatha and learned Counsel for respondent-assesses Sri Prabhakar, we have examined the records as well.

15. It is not in dispute that the respondent and its contractors have entered into bilateral agreement and on their own volition agreed upon specific term that the respondent would supply to the contractors diesel for consumption for the vehicles and machinery used in mining operation by contractors.

16. It is pertinent to note that the costs of the diesel so supplied is recoverable from the contractors from out of the amount payable to the contractors for the work contract. In other words, supply of diesel is not for the vehicle and machines owned by the respondent but owned by the contractors in the mining operations for which the contract has been entered into. When the costs of the diesel is recoverable and does not form part of any incentive to the contract, the property, i.e., diesel, undoubtedly passes on to the contractor and they are consumers. The definition of "sale" as incorporated in the Sales Tax Act, undoubtedly, signifies that with it is grammatical variation and cognate expression sale means every transfer of the property in goods other than by way of goods mortgaged, hypothecated or pledged by one person to another in the course of trade or business for cash or for "deferred payment" or other valuable consideration and includes:

(i) a transfer otherwise than in pursuance of a contract of property in any goods for cash, deferred payment or other valuable consideration;

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

(iii) a delivery of goods on hire purchase or any system of payment by instalments;

(iv) a transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration.

17. Factual aspects admitted by the respondent establishes supply of diesel for value. Though the payment is not necessarily be paid by the contractor immediately on such supply but the value of the diesel being recoverable from

the amount payable to the contractors by the respondent, has to be considered as supply of diesel for deferred payment. We have, therefore, no hesitation in recording that the supply of diesel by the respondent to the contractors is a "sale" within the meaning of Sub-section (1) of Section 2 of the Act. Such an arrangement obviously may be for avoiding loss of time in procurement of diesel or avoidance of extra costs for acquisition by the contractors. The accrual benefit to the contractors may be a prompting factor to bind the respondent to supply diesel. But as far as respondent is concerned, in normal course it was not obliged to supply diesel but for the fact that it wanted smooth sailing of mining operations. Having thus held that the transaction comes within the ambit of the word sale, we shall now consider whether the tax is attracted.

18. Though the learned Counsel for respondent vehemently urged that the rules and regulations governing issuance of licence to install private pumping station, prohibits installation of more than two pumping stations, but no rules or regulations was brought to our notice which impasse such a restrictions. It all depends on the requirements of the licensee. Merely because in the licence it is mentioned that the permission is granted for installation of single pump no other condition is noticed in the licence which prohibits installation or grant of Licence for installation of two pumps.

19. Nextly, though the respondent contends it has maintained separate accounts regarding utilisation of local purchase and interstate purchase, necessary information as to self consumption of interstate diesel only by the respondent for its bonafide own use, is not established. Further, it is not established with acceptable evidence before the Assessing Authority that the respondent assessee's requirement of diesel was less or equivalent to interstate diesel purchased. Had the assessee been able to establish that interstate diesel has been utilised for its own use, it was possible to take a view based on the statement of accounts furnished. That has not been done by the respondent - assessee. The Tribunal, which has taken into consideration plea of the respondent appears to have weighed it in its favour only on the basis of the decision of this Court in the case of Bangalore Water Supply And Sewerage Board, Bangalore v. State of Karnataka reported in 1999(46) KAR.L.J. 1.

20. In this regard, it is necessary to mention that this Court in the said decision took note of the fact that the items like iron, steel, cast iron pipes and fittings, PVC pipes and fittings, etc., purchased by the Board from registered dealers, for use in execution of its work had not passed on to the contractor under terms of the contract. The said material has been utilised for a jot for which the contractors were engaged. Since passing of such items as properties had not passed to the contractors, this Court had held that there was no sale within the meaning of Sub-section 1 of Section 2 of the Act. On facts the said decision is certainly distinguishable. It was a case where consumer is a contractor and not an assessee but facts of that case discloses that assessee was a consumer. The decision in the case of N.M. Goel & Co, referred to supra, rendered by the Apex

Court mutadis mutandi applies to the facts of this case and we are satisfied that the impugned order passed by the Tribunal needs interference.

21. Consequently, we answer the question of law framed in favour of the State and against assessee and set aside the order passed by the Tribunal dated dated 22-12-2003 and confirm the order passed by the Assessing Authority.

Ordered accordingly. No costs.