
(1984) 11 BOM CK 0087

In the Bombay High Court

Case No : Sales Tax Reference No. 7 of 1979

Uni Abex Alloy Products Ltd.

APPELLANT

Vs

The State of Maharashtra

RESPONDENT

Date of Decision : 13-11-1984

Acts Referred:

Citation : (1985) 58 STC 37

Hon'ble Judges : Sujata V. Manohar, J; M.H. Kania, J

Bench : Division Bench

Judgement

Smt. Sujata V. Manohar, J.—The applicants Uni Apex Alloy Products Ltd., Bombay, manufacture, inter alia, alloy castings and reformer tubes. They have a factory at Thane. The applicants entered into a contract dated 11th April, 1975, with Gujarat State Fertilizers Company Limited, for fabrication, supply and erection of 208 reformer tube assemblies for the conversion of the ammonia plant of the Gujarat State Fertilizers Company Limited at Baroda from a cold bottom system to a hot bottom system.

2. The applicants are holders of a registration certificate both under the Central Sales Tax Act as well as the Bombay Sales Tax Act. On 17th November, 1976, the applicants applied to the Deputy Commissioner of Sales Tax, Bombay, u/s 52 of the Bombay Sales Tax Act seeking his determination as to the nature of the transaction represented by the said contract of 11th April, 1975. They annexed a provisional invoice dated 30th April, 1976, for Rs. 49,451.70. This invoice was in respect of one reformer tube assembly, exclusive of tube top assembly, catalyst support assembly and other fixtures to be supplied and billed later. It was charged for at the rate of Rs. 103.00 per kg. No sales tax was charged in the provisional invoice. The invoice, however, contains a printed certificate stating that the registration certificate under the Bombay Sales Tax Act is in force on the date on which the sale of the goods specified in the invoice is made, etc.

3. In respect of this application the Deputy Commissioner of Sales Tax by his order dated 31st December, 1976, held that the said agreement of 11th April,

1975, was a divisible contract, one for the sale of reformer tube assemblies and the other for the work of designing, drawing, erection and installation.

4. Against this decision the applicants preferred an appeal before the Tribunal. The Tribunal confirmed the finding of the Deputy Commissioner that the contract was a divisible contract, one for the sale of reformer tube assemblies and the other for work to be carried out.

5. In respect of this decision of the Tribunal the following question is referred to us for our determination :

Whether the agreement dated 11th April, 1975, entered into by the applicant with Gujarat State Fertilizers Company Limited, is a works contract or a divisible contract containing two agreements one for the sale of goods and the other for payment of remuneration for services and work done ?

The answer to this question depends on the terms and conditions of the contract and the intention of the parties. It is, therefore, necessary to analyse in the first place the terms of the contract entered into between the applicants and the Gujarat State Fertilizers Company Limited, which is dated 11th April, 1975. Under clauses 2.101 and 2.102 of the agreement it is provided as follows :

"2.101 : The SELLER shall engineer, fabricate and supply 208 Nos. of HK-40,25/20 Cr/Ni cast alloy steel reformer tube assemblies, duly inspected and passed by the BUYER's inspection authorities before despatch and erect and install them at the BUYER's premises at Fertilizernagar, District Baroda, in Ammonia-I Plant in place of existing tubes therein.

2.102 : The SELLER shall prepare the detailed engineering and fabrication drawings for the reformer tubes for converting the cold bottom system to hot bottom system as suggested by the BUYER. The SELLER shall within four months from effective date of this agreement deliver to the BUYER a set of modified reformer tube drawings incorporating the said change from cold bottom to hot bottom system."

Under article I of this contract clause 1.30 defined reformer tubes as follows :

"1.30 : "Reformer tubes" shall mean the reformer tube assembly from top flange up to bottom cast piece all welded together but excluding the inlet and outlet pigtails, manifolds, header, refractories and insulation."

The terms "erect and install" are defined in clause 1.50 of article I. They are as follows :

"1.50 : "Erect and install" shall mean putting the reformer tubes in the furnace and aligning the tubes, flanges and gaskets as per the BUYER's approved drawings and weld the two ends of the outlet pigtails to the reformer tubes and the manifolds."

The scope of work is defined under clauses 2.109 and 2.220, as follows :

"2.109 : The SELLER's scope of work shall exclude the supply, erection and installation of inlet and outlet pigtails, manifolds, headers, refractories, insulation bottom supports, top suspension gear and any other item not mentioned in ARTICLES 2.10 except that the outlet pigtails supplied by the BUYER shall be welded by the SELLER on one end to the reformer tubes and on the other end to the manifold, i.e., two welds for each outlet pigtail. Specification for welding outlet pigtail ends shall be mutually discussed and agreed to by the BUYER and the SELLER.

2.110 : The SELLER's scope of work shall exclude the removal of any item from the existing reformer furnace."

Clause 2.20 deals with deliveries :

"2.20 : DELIVERIES : The SELLER shall complete and despatch to the BUYER's plant all 208 reformer tubes complete with flanges, bottom static castings, gaskets bolts and catalyst supports as per the SELLER's scope of supply detailed in ARTICLES II, to the BUYER, before 12 months from the date of this agreement or 31st March, 1976, whichever is earlier. Part deliveries shall be permissible at the SELLER's discretion."

6. There are also detailed provisions in the contract relating to tests and inspection of the reformer tube assemblies at various stages of fabrication and installation. Complete details of the work relating to fabrication, supply, erection and installation are set out in Annexure A to the contract. A perusal of the contract makes it clear that the work of fabrication and installation involved is a highly specialised work for which detailed specifications have been laid down in the contract. All welds have to be radiographed and there are various types of checks and tests to be carried out under the contract. The applicants have to install the 208 reformer tube assemblies in the ammonia plant in the primary reformer furnace. From the details set out in Annexure A, from the drawings and from the terms of the contract it is clear that each reformer tube assembly requires insertion of a catalyst support grid assembly which forms a part of the reformer tube assembly. As specified in clause 2.306 of Annexure A, after the completion of welding of each reformer tube assembly, a GO DEVIL shall be passed down the full inside length of the assembly to check that adequate clearance has been obtained for insertion of the catalyst support grid assembly. The catalyst support grid assembly has to be inserted thereafter.

7. The contract also involves the work of preparation of detailed engineering and fabrication drawing for the reformer tubes for the purpose of converting the plant from a cold bottom system to a hot bottom system. These drawings and designs are required to be approved by the parties. Thereafter the applicants are required to fabricate the reformer tube assemblies as per the approved drawings and designs. These reformer tube assemblies are required to be erected and welded into the plant as per the details which are set out in the contract.

8. In respect of this work to be carried out, the buyer is required to pay to the

seller (under Article V) at the rate of Rs. 103 per k.g. of the weight of the reformer tube assemblies in black un machined condition, in consideration of their carrying out all obligations, in time and manner as stipulated in the agreement. This rate includes charges for design and drawing and for erection and installation of the tubes. The estimated total amount payable under the said clause is Rs. 98,55,040.00.

9. Article VII of the contract deals with the schedule of payment. Clauses 7.10, 7.20, 7.30, 7.40, 7.50 and 7.60 are as follows :

"7.10 : The total amount payable by the BUYER shall be paid to the SELLER in the following instalments : 10 per cent. of the total amount payable under ARTICLE V, i.e., Rs. 9,85,504.00 (Rupees nine lakhs eighty-five thousand five hundred four only) within 7 days of signing of the formal agreement between the BUYER and the SELLER against the SELLER's furnishing to the BUYER a bank guarantee issued by a schedule Bank or an insurance guarantee for the like amount in the form and manner acceptable to the BUYER.

7.20 : 5 per cent. of the total amount payable under ARTICLE V, i.e., Rs. 4,92,752.00 (Rupees four lakhs ninety-two thousand seven hundred fifty-two only) within seven days of approval of design drawings against the SELLER's furnishing to the BUYER a bank guarantee issued by a schedule Bank or an insurance guarantee for the like amount in the form and manner acceptable to the BUYER.

7.30 : 75 per cent. of the total amount payable under ARTICLE V, on pro-rate basis for the value of reformer tubes actually despatched to the BUYER against documents evidencing despatch of tubes, negotiated through a bank, partial deliveries being permissible at the discretion of the SELLER.

7.40 : 5 per cent. of the total amount payable under ARTICLE V, within 7 days of starting of installation of the reformer tubes by the SELLER or within 2 months of the completion of delivery of all the tubes at the BUYER's plant, whichever is earlier.

7.50 : 5 per cent. of the total amount payable under ARTICLE V, within 15 days of the completion of the installation of the reformer tubes in the BUYER's Ammonia-I Plant against the SELLER furnishing to the BUYER a bank/insurance guarantee for a like amount to cover the workmanship guarantee as provided in clause 4.10 and valid for the period thereof.

7.60 : The above payments enumerated in clauses 7.10 to 7.40 shall be treated as advance and such advances shall be cleared on the SELLER submitting final bills for :

(a) Design and drawings.

(b) Manufacturing, assembling, testing, supply, etc., of tubes.

(c) Erection and installations."

Under clause 5.50 of article V the total amount payable by the buyer to the seller as stipulated in clause 5.10 is divided into three parts. The said clause is as follows :

"5.50 : The total amount payable by the BUYER to the SELLER as stipulated in clause 5.10 shall constitute of the following :

5.501 Of the total amount payable the charge for design and drawings stated in clause 2.102 shall be Rs. 4,00,000 (Rupees four lakhs only).

5.502 Of the total amount the charge for erection and installation work stated in clauses 2.101 and 2.109 shall be Rs. 5,50,000 (Rupees five lakhs fifty thousand only).

5.503 The balance amount for manufacturing, assembling, testing, supply and other obligations of the SELLER stated in ARTICLE II."

It is on the basis of clause 5.50 that the department has levied sales tax on the total amount payable under the said contract less a sum of Rs. 5,50,000 which is described in clause 5.50 as charge for erection and installation.

10. These are the material terms of the contract on the basis of which the question raised before us requires to be answered. Contracts which are composite contracts for supply of material and work often raise difficult questions of construction. If the contract is predominantly a contract for the sale of goods and some work incidental to the supply of goods is required to be carried out, such a contract is normally considered as a contract for sale on which sales tax can be levied. Similarly where the contract is predominantly a contract for work to be carried out in the course of which certain material is incidentally supplied by the contractor, such a contract is usually considered as a contract for work and not as a contract for sale. But where a contract is both a contract for supply of material as well as for work to be carried out, and both these aspects of the contract are of importance, a question usually arises as to whether any part of this transaction can be separately looked upon as a transaction for sale on which sales tax can be levied. Obviously such a transaction of sale must be severable from the rest of the contract and be capable of being treated separately as a transaction of sale.

11. In Benjamin's Sale of Goods, Second Edition, para 42, it is stated as follows :

"Where work is to be done on the land of the employer or on a chattel belonging to him, which involves the use or affixing of materials belonging to the person employed, the contract will ordinarily be one for work and materials, the property in the latter passing to the employer by accession and not under any contract of sale. Sometimes, however, there may instead be a sale of an article with an additional and subsidiary agreement to affix it. The property then passes before the article is affixed, by virtue of the contract of sale itself or an appropriation made under it."

In order to constitute a sale, therefore, the property in the chattel must pass as a chattel and not by virtue of the fact that it is affixed either to the land of the buyer or to any chattel belonging to the buyer. In Halsbury's Laws of England, Fourth Edition, Volume 41, para 603, a contract of sale is distinguished from a contract for work and labour as follows :

"A contract of sale is a contract the main object of which is the transfer of the property in, and the delivery of the possession of, a chattel as such to the buyer. Where the main object of work undertaken by the payee of the price is not the transfer of a chattel as such, the contract is one for work and labour."

12. In the present case we have to see whether at any stage in the execution of the contract a transaction of sale has taken place and there has been a transfer of the property in the reformer tube assemblies as such to the purchaser.

13. Under the contract there is an obligation on the applicants to design, fabricate and supply 208 reformer tube assemblies. Each of these reformer tube assemblies consists of several parts which have to be assembled. These 208 assemblies in turn have to be assembled and fitted into the system of the ammonia plant of the purchasers. When one examines these specifications relating to assembly and erection of these reformer tube assemblies, it is clear that each one of these reformer tubes is not fully assembled when it is despatched from the applicants' factory at Thane to the purchaser's plant at Fertilizernagar at Baroda. Some parts of each reformer tube assembly, viz., the catalyst support grid assembly, have to be inserted in each reformer tube after it is welded to the plant of the buyer. Such insertion has to be carried out after elaborate tests as specified in the contract.

14. In fact, the invoice dated 30th April, 1976, on which the department has placed reliance, itself shows that what is despatched from the applicant's factory to the purchaser is not a complete reformer tube assembly but a reformer tube assembly exclusive of tube top assembly, catalyst support assembly and other fixtures which are to be supplied at a later date. Hence at no stage until the completion of erection and installation work, is there a delivery of a complete reformer tube assembly from the applicants to the purchaser. There is therefore no delivery of the complete reformer tube assembly as such from the seller to the buyer.

15. It is contended in this connection by Mr. Jetly, learned counsel for the department, that assembly of each reformer tube assembly is complete at the applicant's factory in Thane because there is an elaborate procedure for checking and inspection of each tube by the petitioners. This argument, however, cannot be accepted because there is a detailed provision in the contract relating to inspection and testing of the work to be done by the sellers at every stage. From this provision for inspection and testing, it is not possible to conclude that a fully assembled reformer tube is at any stage sold by the seller to the buyer.

16. The second factor which is relevant in this connection is the factor of price.

Under article V of the contract a lump sum price is payable by the buyer to the seller in respect of the entire work completed under the contract. The price is calculated at the rate of Rs. 103 per kg. of the reformer tube assembly as set out therein. The schedule of payment under article VII also deals with the percentages of the total amount which is payable at various stage of the contract. In fact, under clause 7.60 of that article, the payments up to the last 5 per cent. of the total amount are treated as advances to be finally cleared as set out in that clause.

17. The department, however, contended that the total amount so payable is split up into different parts by the parties themselves under clause 5.50 of article V. It is on the basis of this clause mainly that the sales tax authorities have come to the conclusion that the contract is a divisible contract and it is possible to construe a part of the contract as relating to the sale of reformer tube assemblies at a price equal to the total amount less Rs. 5.50 lakhs. An examination of clause 5.50 however, shows that under this clause the parties have not split up the total consideration into price for the supply of reformer tube assemblies and charges for the work of erection and installation. The total amount payable is divided into : (i) charge for design and drawings, (ii) charge for erection and installation and (iii) balance amount for manufacturing, assembling, testing, supplying and other obligations. Each of these obligations relates to the nature of the work to be carried out by the applicants under the contract. The first part, viz., charge for designing and drawings relates to design and drawings prior to the fabrication of reformer tube assemblies. The reformer tube assemblies are manufactured in accordance with the drawings. If one were to calculate the price of reformer tube assemblies, then this charge for designing the article would ordinarily be a component of the price of this article. It is, however, separately set out in clause 5.50. Charges for erection and installation work are separately specified in clause 5.50 and so are the charges for the balance work. In our view it is not possible to spell out from this clause any intention of the parties to divided the consideration into price for the materials supplied and charges for work. The separation appears to have been made for the purpose of calculation and determination of the amounts to be paid under the contract. The separation is not for the purpose of determining price of the goods supplied and charges for work and labour.

18. In this connection it is also necessary to refer to the provisional invoice of 30th April, 1976. Although the invoice relates to one reformer tube assembly less certain parts which are to be supplied and built later, the rate charged in the invoice is the full rate payable under article V for the entire work to be carried out under the contract. This would indicate that the invoice was merely a method of calculating part payment to be received by the applicants in the course of the work being done by them under the contract. If the invoice were in respect of the price of the reformer tube assembly, the price would have been much less. No sales tax is also charged under the invoice. It is also only a provisional invoice. All these factors go to show that the part payments received by the applicants

against delivery of partially assembled reformer tubes are not as and by way of price of the materials supplied. They are part payment against the total amount payable for the work to be done under the contract.

19. It is, therefore, not possible to divide the contract into a contract for the supply of reformer tube assemblies and a contract for work and labour. The contract is an integrated contract for supply of material as well as for work and labour. At no stage in the course of the contract work there is a sale of each reformer tube assembly as such to the buyers. It is true that the contract uses the terminology of "seller" and "buyer" to describe the parties. But the use of such terminology is not conclusive one way or the other when there is no transaction of sale as such involved under the contract. The department cannot therefore levy any sales tax.

20. Several cases have been cited before us relating to such composite contracts for work and labour. In the case of *Richardson and Cruddas Ltd. v. State of Madras* reported in [1965] 16 STC 827 there was a contract for the fabrication and erection of steel structures on the site of the customer and there was also a contract for fabrication and installation of bottle cooler equipment. The Madras High Court construed the contract as a contract for erection and supply and held that it was not separable into a separate contract for sale of equipment and a contract for erection upon an analysis of the terms of the contract. It held that at no stage did the property in the materials pass as such materials to the customer. It was only when the material was affixed or installed in the customer's ground that the property in the goods passed to the customer. Hence there was no sale of the material to the customer. In that case also an all inclusive price was charged for the work of supply, fabrication and installation of the equipment. The Court said that the work of installation could not be considered as merely of an auxiliary nature or as incidental to the work of supply of equipment. The decision of the Madras High Court in that case was upheld by the Supreme Court in *State of Madras v. Richardson & Cruddas Ltd.* [1968] 21 STC 245 (SC).

21. In the present case also it is not possible to consider the work of erection and installation as merely of an auxiliary nature or as work incidental to the supply of material. In our view the contract in the present case is an integral one which cannot be separated into a contract for sale and a contract for work and labour.

22. In the case of *Sentinel Rolling Shutters and Engineering Company (Pvt.) Ltd. Vs. The Commissioner of Sales Tax*, the Supreme Court was required to consider a contract for manufacture and erection of rolling shutters. On the facts of that case the Supreme Court held that a rolling shutter came into existence only when it was assembled and affixed on the premises of the customer. There could therefore be no sale of a rolling shutter prior to its being so affixed. The Supreme Court in that case at page 417 held :

"The true nature of the contract cannot depend on the mode of payment of the amount provided in the contract. The parties may provide by mutual agreement that the amount stipulated in the contract may be paid at different stages of the execution of the contract, but that cannot make the contract one for sale of goods if it is otherwise a contract for work and labour."

Under the contract in the present case also payments made under the provisional invoices cannot be considered as a price for supply of material for reasons which we have set out earlier. The contract in the present case, like the contract in the case of Sentinel Rolling Shutters and Engineering Company (Pvt.) Ltd. Vs. The Commissioner of Sales Tax, , is essentially a contract for affixing reformer tube assemblies to the ammonia plant of the customer in order to convert the system of the plant from a cold bottom system to a hot bottom system. It is essentially a contract for work and labour as in the above case before the Supreme Court.

23. In the case of State of Rajasthan v. Man Industrial Corporation Ltd. reported in [1969] 24 STC 349 (SC) the contract was for fabricating and fixing certain windows in a building. The contract was to prepare the windows according to specifications, and to fix them to the building. The Supreme Court held that fixing the windows to the building was not incidental or subsidiary to the sale but was an essential term of the contract. The windows which were fabricated did not pass under the terms of the contract as windows. It was only on the fixing of the windows as stipulated that the contract was fully executed. The property in the windows passed on the completion of the work and not otherwise. In the present case also the property in the reformer tube assemblies does not pass under the contract as reformer tube assemblies. In fact, each reformer tube is fully assembled only in the course of completion of the work of installation under the contract. It is not possible to hold that there is a sale of reformer tube assemblies as such under the contract.

24. Similarly in the case of Otis Elevator Company (India) Ltd. v. State of Maharashtra reported in [1969] 24 STC 525 our High Court considered a contract for the supply and erection of passenger lifts in a building, for which an all inclusive price was quoted, as a works contract which was not capable of division into a contract for the sale of elevator and a contract for erection.

25. The latest case in this connection cited before us was the case of V.S. Raju and Sons Engineering Works Vs. The State of Andhra Pradesh, where a contract for delivery and erection of a boiler for a lump sum was considered as a contract for work and labour and not a contract for sale. The present contract is in line with the contracts in these above cases.

26. There are, of course, other decisions where the Courts have held the contract to be a divisible contract. The principles for deciding whether there was a sale involved in such a contract or not, were first laid down in the case of The State of Madras Vs. Gannon Dunkerley and Co., (Madras) Ltd., . The Supreme Court observed that :

"In order to constitute a sale it is necessary that there should be an agreement between the parties for the purpose of transferring title to goods, which presumption capacity to contract, that it must be supported by money consideration, and that as a result of the transaction property must actually pass in the goods."

Applying this principle in the case of *Sarvaiya & Co. v. State of Maharashtra* reported in [1976] 38 STC 86, our High Court considered a contract for the supply and laying of two underground cables. The contract set out separate charges for the supply of cable, for the supply of other equipment and for the work to be carried out. The extra 300 yards of cable which remained unutilised under the contract was retained by the customer. On this basis the Court came to the conclusion that there was clearly a sale of the cable to the customer under the contract and the contract was divisible into one for sale of cable and the other for the work to be carried out under the contract. In the present case there is nothing which would indicate such passing of property in the material at any time in the course of the contract. The ratio of this case, therefore, will not apply to the present contract.

27. In the case of *Union of India (UOI) Vs. The Central India Machinery Manufacturing Company Ltd. and Others*, there was a contract for the manufacture and supply of wagons for a price which was fixed, taking the wagon as a unit. In the course of manufacturing these wagons, certain material was supplied by the customer. It was contended before the Supreme Court that since some of the material used in the fabrication of the wagons was supplied by the customer, there could not be any transfer or sale of the wagons to the customer. This contention was negated by the Supreme Court. It held that the contract was expressly for the manufacture and supply of wagons for a price. It was a contract for sale and it should not be considered as a contract for work and labour. The issues before the Supreme Court were different from the issues in the present case. The ratio of that case has no application here.

28. The last case which was cited before us was the case of *State of Tamil Nadu v. Dunlop India Limited* reported in [1981] 48 STC 521. In this case the assessee who was a manufacturer and dealer in tyres entered into a contract with the Government of India for urbanisation of steel wheels and top rollers intended for use in the construction of tanks for defence purposes. The decision given by the Madras High Court in that case turned on the special facts of that case. Although the contract was for fitting or affixing a rubber compound over the wheels, the Madras High Court held that the terms of the contract were expressly for the supply of specific articles ordered. There was also a clause for payment of sales tax on the amount to be paid for each unit supplied. In all the relevant assessment years factually, the assessee raised invoices, claimed sales tax and recovered the same. A certificate was also given by the assessee with reference to the amounts claimed as sales tax in the invoices, to the effect that "the goods on which sales tax has been charged have not been exempted under the Central

Sales Tax Act or the State Sales Tax Act or the Rules made thereunder and the amounts charged on account of sales tax on these goods are not more than what is payable under the provisions of the relevant Act", etc. There was no separate charge relating to labour or the work of vulcanisation. In these circumstances the intention of the parties, as spelt out from the contract was an intention to enter into a contract for sale.

29. The ratio in that case can have no application here. The only similarity between the two cases relates to the certificate given relating to sales tax. But in that case the parties had actually paid the sales tax, and the dealer was assessed by the sales tax authorities in respect of the transaction in question. The certificate therefore shows an intention on the part of the parties to treat the contract as a contract for sale. In the present case the certificate is a printed certificate on the invoice form. There was no intention on the part of the parties to enter into any contract of sale at all and no sales tax was even collected by the seller. The decision of the Madras High Court therefore has no relevance to the present case.

30. It is not necessary to examine at length the various decisions on this point. Our decision must necessarily turn on the terms of the contract involved in the case. The principles, however, for determining whether there is a contract for sale which is a severable contract from the contract for work and labour, are well established. Applying these principles to the present case, in our view, for reasons which we have set out earlier, the present contract cannot be considered as a divisible contract, one for the sale of the material and the other for work and labour.

31. In the premises the question which is posed before us is answered as follows :

The agreement dated 11th April, 1975, entered into by the applicants with Gujarat State Fertilisers Company Limited is not a divisible contract containing two agreements, one for the sale of goods and the other for payment of remuneration for service and work done. It is essentially a works contract although it involves supply of materials.

The respondents will pay to the applicants costs of the reference.

The amount deposited by the applicants before the Tribunal to be refunded to the applicants.