

# **EXPANDING CONCEPT OF SALE THE TAXATION DILEMMA**

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Philosophy is the record of bonafide research carried out under my  
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## **DECLARATION**

I do hereby declare that this work, “**EXPANDING CONCEPT OF SALE: THE TAXATION DILEMMA**” has been originally carried out by me under the guidance and supervision of **Dr. G. Sadasivan Nair**, Rtd. Professor, School of Legal Studies, Cochin University of Science and Technology. This work has not been submitted either in part, or in whole, for any degree at any University.

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This is to certify that the important research findings included in the thesis, “**EXPANDING CONCEPT OF SALE: THE TAXATION DILEMMA**” have been presented in a Research Seminar at the Department of Law/ School of Legal Studies, Cochin University of Science and Technology on 7<sup>th</sup> August, 2009

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## **PREFACE**

*Being a specialized field, study on taxation system is a motivating endeavour. Present study is not directly on any tax system, but with reference to one of the incidences of levy of tax, namely 'sale of goods'. Sale of goods is an act of property acquirement and a corresponding gain of income. This can be subject to various kinds of tax, such as, the process of passing of property can be subject to indirect sales tax, the trader can be subject to direct levy of professional or employment tax and the gain from trading can be subject to direct income tax. The passage of property can be subjected to consignment tax. There is another kind of tax on commodity, namely excise duty, which is levied on commodity, when it is manufactured or produced. Consequently, taxing of production and sale of goods constitute a complex scenario.*

*What is the significance of the topic for a research in law? Being a researcher I have to answer this explicitly. Sales Tax is an indirect tax. The levy is on the consumption of goods by the end consumer, though it is collected from the collecting agents, namely dealers. Of course it is collected at different points, according to the kind of tax system, either single point of multi point or multiple points.*

*The character of sales tax differs from country to country. In the United States of America, sales tax is levied on retail sale only being a tax on end purchase of goods, leaving all other points, such as resale or for subsequent processing. In India, it*

*is levied at all the point of sale based on the value addition, after introduction of Value Added Sales Tax in 2005 as a uniform method of tax throughout the country. Formerly, there were different system of levy of tax, either on the first point of sale/ purchase or in the last point of sale/ purchase or both in the first and last sale/ purchase, suitably, depends on the potentiality and substance of the commodity. Thus a commodity, after its manufacturing and clearance from the factory, is subjected to sales tax, on the occasion of sale of goods.*

*What ever be the point of levy, who ever be the person administering the tax and where ever be the situs of sale, the incidence of tax is sale, either local sale, inter-state sale or export sale. Therefore, the research on the subject of sale is an infinite and general study on the topic. It is difficult to find out a proper method for analysing the general principles of subject without going to the aspects of special fields, either intra state sale, inter- state sale or overseas export sale. However, I am constraint to limit the area of study with respect to expanding concept of sale in the meadow of taxation.*

*Sale is a special form of contract, well defined in the Sale of Goods Act, 1930 detailing the required features to form a transaction as sale. When a general statute defines the expression, sale, it is obvious that it has well accepted meaning of the expression, either in popular or in legal sense. Nevertheless, sale is not only a commercial activity of passing of property, but also a major source of tax, compared to other sources of revenue. While limiting the scope of 'sale of goods' within provisions of the general statute, there are leading issues;*

*like tax evasion or erosion or tax avoidance by an intelligent tax planning. To curb this situation, the usual practice of the legislature is to enlarge the meaning of sale of goods, in taxing statutes, irrespective of the significance of the expression in general law.*

*Expansion of meaning of the expression, 'sale of goods', in the taxing statutes, had resulted in a flood of litigations in the last several decades. There were divergent opinions between the legislature and the judiciary regarding the competency of legislature to expand the statutory expression. Additionally, with regard to the device to interpret the scope of the statutory expression, they adopted different modes of interpretational techniques, according to the wants.*

*The post constitutional period of Indian taxation system faced the dilemma of inconsistent interpretation of legal expressions, particularly in relation to the term 'sale of goods', on quite a lot of occasions. Consequently, in the year 1981, an amendment was carried out in the Constitution of India by incorporating a definition clause, (29A), to Article 366, to define the sale and purchase of goods for the purpose of taxation. Nevertheless, while expanding the scope of taxation on the sale of goods, this endeavour could not achieve the objective entirely. The amendment could not resolve the inconsistency in interpretation of sales tax laws. Such a state of affairs inspires the present study, the ambit and scope of expression 'sale of goods', in pre-amendment and post amendment era.*

*The methodology of research has to be flexible with the subject of study. An empirical study is not viable when the subject is one, evolved by interpretation of principles by the Judiciary, focusing on different statutes dealing with the subject. The topic of sale of goods is developed in relation with divergent understanding of law, by the Judiciary, internationally, particularly in India. There are hundreds of judicial pronouncements dealing with the ambit and scope of sale; of course, all are mainly attached to issues of levy of sales tax.*

*Statutes are the main sources of inputs. There is a general statute on sale of goods. Indian Sale of Goods Act, 1930 deals with the general principles on sale of goods. The provisions of Indian Sale of Goods Act, 1930 are analogous with that of Sale of Goods Act, 1893 (England). The principles are in corollary with the general principles of contract, governed by the Contract Act, 1872, as sale is a special kind of contract. The provisions of the Transfer of property Act, 1882, also deals with the sale of immovable property, which is out of the subject of study, as the expression 'goods' does not take the immovable property. However, the principles of conveyance dealt with in Transfer of Property Act, 1882 are significant and persuasive, as the both of them deal with contractual obligations also.*

*Comparative study of statutes dealing with general principles of sale and statutes dealing with taxation of sale of goods is vital during the course of research. Since, generally, the taxation of sale of goods, is a subject appended to State's legislative power, there are several statutes dealing with tax on Sale of Goods, one in each States and also a Central Statute in*

*the domain of Government of India. The subject of 'sale of goods' is dealt in all these statutes, almost consistently. The sole aspiration of these statutes is, gathering utmost tax revenue from the sale or purchase taking place within their authority. Thus this endeavour is a contemporary analysis of judicial and legislative accomplishments to advance the subject of study.*

*My efforts are not intended to replace the settled academic out look on the subject. But being a person from the practicing field of law, I am deeply influenced by the real and practical complexities faced by the Judges and Lawyers, rather than the Academic Scholars. To that extent my study is a survey on judicial interpretation on tax issues, rather than an analysis of principles of taxation.*

*I am greatly indebted to my respected Guide, Prof. (Dr.) G. Sadasivan Nair, whose invaluable guidance assisted me to complete my thesis. I am also greatly indebted to my senior in the Bar, Smt. S.K. Devi, Advocate, High Court of Kerala, whose constant encouragement and support helped me to complete my venture, as per schedule.*

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*With great reverence and love, I dedicate this work to my beloved father the Late K. Krishnan Nair.*

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## CHAPTER I

# Introduction: Jurisprudential Basis of Taxation

Tax is a mandatory imposition of the sovereign without any guarantee of special benefits. The imposition of tax is a constitutional function<sup>1</sup>. Such an imposition may be either upon person or property or privileges or occupations or enjoyments of the people<sup>2</sup>. Obviously, the primary implication and object of taxation is raising money for the purpose of the Government by means of contribution from individual persons. According to Seligman<sup>3</sup>, a tax is a compulsory contribution from the citizens to the

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<sup>1</sup> *Commissioner of Central Excise v. Acer India Ltd*, 2004 (8) SCC 173 at para 31.

<sup>2</sup> The term 'Tax' is explained as " 'taxes' in its most enlarged sense embraces all the regular imposition made by the Government upon the person, property, privileges, occupations and enjoyments of the people for the purpose of raising public revenue." See *Cooley in Constitutional Law*, 4<sup>th</sup> edn. at p. 61, cited in A.C. Sampath Iyengar. *Three New Taxes*, Vol. I, 4<sup>th</sup> edn. (Central Law Agency, Allahabad) (1976) at p. 39.

<sup>3</sup> E.R.A. Seligman, *Essays in Taxation* (1921), cited in A.C. Sampath Iyengar. *Three New Taxes*, Vol. I, 4<sup>th</sup> edn. (Central Law Agency, Allahabad) (1976) at p. 19.

Government to defray the expenses incurred in the common interest of all, without reference to special benefit conferred.

The nature of taxing power differs from the other two sovereign functions, namely the police power<sup>4</sup> and the eminent domain<sup>5</sup>. State cannot extend its police power to mount up the revenue<sup>6</sup>, but a taxing power, of course, enables the Sovereign to accumulate the revenue for its developmental or welfare purposes<sup>7</sup>. Even if the purpose of levy is not for common utility, but for particular purpose, it

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<sup>4</sup> *Dwarakadas Shrinivas v. Sholapur Spinning & Weaving Co.*, AIR 1954 SC 119 at p. 137.

<sup>5</sup> *State of West Bengal v. Union of India*, AIR 1963 SC 1241 at p. 1258. Eminent Domain derives from American Law as a right inherent in every sovereign to take and appropriate private property belonging to individual for public use. The Constitution of India adopted the principle in Article 31, but subject to two limitations that the acquisition must be for public purposes and the owner must be compensated by payment of compensation. See also the Judgement of Mukherjea, J in *Charanjit Lal Chowdhary v. Union of India*, AIR 1951 SC 41 at para 48.

<sup>6</sup> *Amritsar Municipality v. State of Punjab*, AIR 1970 SC 2182 at p. 2190.

<sup>7</sup> *Dantuluri Ram Raju v. State of Andhra Pradesh*, AIR 1972 SC 828 at p. 830.

will not alter the character of tax, when there is benefit to public at least to some limited extent<sup>8</sup>.

In earlier times, when the state was considered essentially as a police state, the economic regulations by way of levies and recoveries are bare minimum. State involvement was minimum because the individual is considered the best person to look after his/her economic interests. If every individual cared for his economic welfare, the welfare of the state was taken for granted. However, with the advent of welfare era, there has been a fundamental change in the sphere of economy and financial thinking. The obligation of the State to look after the welfare increased the responsibility of the State. For the same, the State has to incur heavy expenses. Thus the tax is a necessary evil; equally it is a sacrifice of the people to contribute for the progress of the Country<sup>9</sup>.

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<sup>8</sup> *Vivian Joseph Ferreira v. Bombay Municipality*, AIR 1972 SC 845 at para 16.

<sup>9</sup> Kunwar Deo Prasad, *Taxation in Ancient India*, Mittal Publications, Delhi (1987) at p. 14.

## **1.1. Characteristics of Tax.**

While levying a tax, the State, to some extent, brings in measures to regulate the business activity or the consumption of a commodity or service<sup>10</sup>. However such regulatory control does not come out from the general power of 'regulation or control', but from the specific power of taxation.<sup>11</sup> The levy of tax has an object or aim in which the general interest of the community has the greater significance rather than the private interest<sup>12</sup>.

Levy of tax cannot be equated with collection of public debt, but it is a sort of obligations or liabilities towards the State by the taxpayer<sup>13</sup>. In the widest sense, it includes all money raised by taxation, including taxes levied by the Union or State Legislatures; rates or other charges levied by the local authorities under the statutory powers<sup>14</sup>.

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<sup>10</sup> *State of Tamil Nadu v. SDO Association*, AIR 1975 SC 1006 at p. 1010.

<sup>11</sup> *State of West Bengal v. Kesoram Industries*, 2004 (10) SCC 201 at para 76.

<sup>12</sup> *Hamabai Framjee Petit v. Secretary of States India*, 1915 ILR 39 Bom. 279 at p. 291.

<sup>13</sup> *Government of India v. Taylor*, [1955] AC 491.

<sup>14</sup> *Gouse D.G. v. State of Kerala*, AIR 1980 SC 271 at para 5.

The Constitution of India defines taxation<sup>15</sup> to include imposition of any tax or impost, in its widest connotations so as to include all the compulsory levies.

In the popular meaning, 'tax' explains it as a compulsory exaction of money by public authority for public purpose enforceable by law<sup>16</sup>. Thus the essence of taxation is the compulsion<sup>17</sup>. When the levy is enforced by law, there is no necessity of consent of the tax payers<sup>18</sup>. Levy of tax does not require any element of 'quid pro quo' between the tax payer and the public authority<sup>19</sup>. It is a common burden and the only return which the tax payer gets is the participation in the common benefits of the State. If the element of revenue for the general purpose of the State predominates, then the taxing element takes hold of the levy and it ceases to have any relation to the cost of administration of the law to which it relates it becomes a

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<sup>15</sup> *Constitution of India*, Art. 366 (28) defines taxation to include the imposition of any tax or impost, whether general or local or special, and "tax" shall be construed accordingly.

<sup>16</sup> *Mathews v. Chicory Marketing Board*, 60 CLR 263 at p. 276.

<sup>17</sup> *Commissioner of Hindu Religious Endowment v. Lakshmindra Thirtha Swaminar*, AIR 1954 SC 282 at para 43.

<sup>18</sup> *Lower Mainland Dairy v. Crystal Dairy Ltd.*, [1933] AC 168.

<sup>19</sup> *Jaganath Ramanuj v. State of Orissa*, AIR 1954 SC 400 at para 9.

tax<sup>20</sup>. Likely a fee become tax as a result of surplus accumulated in collection in each year<sup>21</sup>. However there are constitutionally approved differences in the nature of tax and fee<sup>22</sup>. The taxation is not intended to be comprised either in the general legislative power or power to levy fee, but is treated as a distinct matter for the purpose of legislative competence<sup>23</sup>.

There is clear distinction between a tax and fee. Particularly, when services are rendered to a specific area or to specific classes of persons or trade or business in a particular area, in such cases as a condition precedent for such services or in return for them, some charges are levied, not in the nature of tax, but as fee, though whole of the class or locality may ultimately or indirectly be benefited<sup>24</sup>.

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<sup>20</sup> *State of Madras v. Zenith Lamps*, AIR 1973 SC 724 at p. 733.

<sup>21</sup> K.K. Mathew, J. in *Delhi Cloth & General Mills Co. v. Chief Commissioner*, (1970) 2 SCR 348 at p. 354.

<sup>22</sup> *Corporation of Calcutta v. Liberty Cinema*, AIR 1965 SC 1107 at para 45.

<sup>23</sup> *Sundarameir & Co v. State of Andhra Pradesh*, AIR 1958 SC 468 at p. 493.

<sup>24</sup> *Hingir Rampur Coal Co. v. State of Orissa*, AIR 1961 SC 459 at p. 466.

However, imposition of tax can be a compensatory one, when the trade people are having the use of certain facilities for the better conduct of their business and paying not patently much more than what is required for providing the facilities<sup>25</sup>. It gives a quid pro quo for the service rendered. Even in some cases the expenditure for services rendered consequent to the collection of tax may be higher than the proceeds from levy of a compensatory tax<sup>26</sup>. Thus, the illustrious author H.M. Seervai, rightly pointed out that there is no generic difference between a tax and fee, and in fact they are only different forms in which the taxing power of a State manifests itself<sup>27</sup>.

There are some other special features appended to a conscientious taxation system, according to the canon of taxation<sup>28</sup>. It supposes that a tax should be levied with

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<sup>25</sup> *Automobiles Transport Ltd v. State of Rajasthan*, AIR 1962 SC 1406 at para 22.

<sup>26</sup> *State of Himachal Pradesh v. Yash Pal Garg*, 2003 (9) SCC 92 at p. 103.

<sup>27</sup> H.M. Seervai, *Constitutional Law of India*, 4<sup>th</sup> edn., Vol. 3, (N.M. Tripathi, Bombay) (1996) at p. 2373. Also see in *Sri Jagannath v. State of Orissa*, AIR 1954 SC 400 at p. 403.

<sup>28</sup> The maxims of taxation enumerates following principles;

equality and uniformity in accordance with the reasonable principle of apportionment so that each taxpayer may contribute in accordance with his respective ability<sup>29</sup>.

The flexibility, productiveness, simplicity, diversity and elasticity are some of the other characteristics of a feasible taxation system<sup>30</sup>. According to Manu, tax shall be charged in accordance with rules, ethics, social justice and principles of legitimacy<sup>31</sup>. But Kautilya suggests, tax should

- 
- i. The tax which each individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor and to every other person.
  - ii. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it.
  - iii. The subjects of every state ought to contribute the support of the Government, as early as possible, in proportion to their respective abilities.
  - iv. Every tax ought to be so contrived as both to take out and keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state.

See A.C. Sampath Iyengar. *Three New Taxes*, Vol. I, 4<sup>th</sup> edn. (1976) (Central Law Agency, Allahabad) at p. 5 and U.A. Upponi, *Tax Jurisprudence*, (Taxman, Delhi) (1982) at p. 29.

<sup>29</sup> *Spences Hotel Private Ltd v. State of West Bengal*, 1991 (2) SCC 154 at para 24.

<sup>30</sup> K. Parameswaran, *The Power of Taxation under the Constitution*, Eastern Book Company, Lucknow, (1989) edn. at p. 20.

<sup>31</sup> *Manu Smriti* VII 80, as cited in Dr Umesh Holani, "Ancient Taxation Policy", *Chartered Secretary* (1989) at p. 734.

not be uniform and the incidence of taxes must be made to vary according to the nature of commodity<sup>32</sup>.

Undoubtedly, the incidence of tax and burden or volume of tax should have reasonable certainty. Certainty, in a better degree facilitates co-operation of tax payers. Of course, a poor tax structure, definitely results in large-scale tax evasion and tax avoidance in its greater extent<sup>33</sup>. It is the real annoyance faced by the taxman while administering an irresponsible tax scheme<sup>34</sup>.

Equity is not a decisive factor in complaining against a tax structure<sup>35</sup>. Even if a retrospective taxation deprives the right to pass on the tax liability to the customer that by

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<sup>32</sup> Usha Mehta & Usha Thakkar, *Kautilya and His Arthashastra*, cited in U.A. Upponi, *Tax Jurisprudence*, (Taxman, Delhi) (1982) at p. 6.

<sup>33</sup> *Mc Dowell Co. v. Commercial Tax Officer*, AIR 1986 SC 649 at para 17.

<sup>34</sup> Prof. Kaldor recommends three pillars to a sound tax system

- i. A tax system should not contain bias in favour of any particular group of tax payers.
- ii. Tax system must have proper economic effect and should not weaken the incentive to work, save and to take risk.
- iii. Tax system must be comprehensive and simple and must make for efficiency of the administration and prevent large scale tax evasion

See U.A. Upponi, *Tax Jurisprudence*, (Taxman, Delhi) (1982) at p. 48.

<sup>35</sup> *Tata Iron & Steel Co. v. State of Bihar*, AIR 1958 SC 452 at p. 462.

itself will not invalidate the tax, unless the nature and character of tax is altered<sup>36</sup>. A retrospective taxation, though causes harshness but not arbitrary or discriminatory<sup>37</sup>.

Equally, the three components of tax, such as (i) the subject of tax, (ii) the person who is liable to pay tax and (iii) the rate at which the tax is to be paid are necessary ingredients to remove ambiguity in the tax scheme and these are essential to validate an obligation under a taxing statute<sup>38</sup>. In *Union of India v. Bombay Tyre International Ltd*<sup>39</sup>, the Supreme Court held that a tax has two elements; firstly, the person, thing or activity on which the tax is imposed and secondly the amount of tax.

There are always a distinction between the subject of tax and measure of tax. There may be possibility of adopting same standards for measuring two kinds of tax,

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<sup>36</sup> *J.K. Jute Mills & Co. v. State of Uttar Pradesh*, AIR 1971 SC 1534 at p. 1539.

<sup>37</sup> *Empire Industries v. Union of India*, AIR 1986 SC 662 at para 49.

<sup>38</sup> *Mathuram Agrawal v. State of Madhya Pradesh*, 1999 (8) SCC 667 at para 13.

<sup>39</sup> 1983 (4) SCC 210 at para 14.

which arises from distinct power of taxation. The nature of the mechanism by which the tax is to be assessed is not decisive of the essential characteristic of the particular tax charged, though it may throw light on the general character of the tax.<sup>40</sup> The methods adopted for measuring a tax may be relevant in considering the character of the impost but its effect must be weighed along with and in the light of the other relevant circumstances also<sup>41</sup>.

In *R.R. Engineering College v. Zillah Parishat*<sup>42</sup>, the Constitution Bench of the Supreme Court observed that for a matter of convenience a unique criterion may be adopted as a yardstick or measure for assessing the tax and the evolvement of such mechanism is not conclusive on the nature of tax. For example, the fundamental difference between the tax on "income" and a tax on "circumstances and property" is that income tax can only be levied if there is income and if there is no income, no income tax is payable, where as in the case of

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<sup>40</sup> *Ralla Ram v. Province of East Punjab*, AIR 1949 FC 81.

<sup>41</sup> *Hingir Rampur Coal Co. Ltd v. State of Orissa*, AIR 1961 SC 459 at para 21.

<sup>42</sup> 1980 (3) SCC 330 at para 15.

"circumstances and property" tax, where a man's status has to be determined, his total business turnover may be considered for purposes of taxation, though he may not have earned any taxable income<sup>43</sup>.

## **1.2. Legitimacy of Taxing Power.**

The power to tax is the one great power upon which the whole national fabric is based. Taxing power is coupled with the power to craft the State policy<sup>44</sup>. It has the definite purpose of maintaining distributive justice and for regulating capital mobilization. Legislation in the field of taxation and economic activities need special consideration and are to be viewed with larger flexibility in approach<sup>45</sup>. It is as necessary to the existence and prosperity of a nation as is the air he breathes to the natural man<sup>46</sup>.

Manu suggested, the revenues due to the King must be paid at all costs and that in return for the same, the king must ensure the safety of home and health of his

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<sup>43</sup> *District Board of Farrukhabad v. Prag Dutt*, AIR 1948 All. 382 (FB).

<sup>44</sup> *Gopal Narain v. State of Uttar Pradesh*, AIR 1964 SC 370 at p. 376.

<sup>45</sup> *R.K. Garg v. Union of India*, AIR 1981 SC 2138.

<sup>46</sup> *Nichols v. Ames*, 173 US 509 at p. 515.

subjects<sup>47</sup>. It reminds the significance of tax, in a welfare economy.

The legislature has wide discretion in selecting the persons and objects, it wants to tax and a statute cannot be held invalid on the mere ground of classifications made between the subjects<sup>48</sup>. The legislature is free to select the objects for imposing tax<sup>49</sup> and even if there is classification infringing the equality principles, the power to classify may be exercised so as to adjust the system of taxation in all proper and reasonable ways<sup>50</sup>. The State is allowed to pick and choose districts, objects, persons, methods, and even rates for taxation if it does so reasonably<sup>51</sup>. Such classification ought to be made to adjust the burden on a fair and reasonable degree of equality<sup>52</sup>.

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<sup>47</sup> R.K. Choudhary, *Studies in Ancient Indian Law & Justice*, (1953) at p. 48, cited in U.A. Upponi, *Tax Jurisprudence*, (Taxman, Delhi) (1982) at p. 5.

<sup>48</sup> *State of Assam v. Narsh Chandra Ghosh*, 2000 (1) SCC 265 at para 4.

<sup>49</sup> *Steelsworth Ltd v. State of Assam*, 1962 Supp 2 SCR 589 at p. 593.

<sup>50</sup> *Ravi Varma Rajah v. Union of India*, AIR 1969 SC 1094 at p. 1098.

<sup>51</sup> *Mafatlal Industries Ltd v. Union of India*, 1997 (5) SCC 536 at para 343.

<sup>52</sup> *Gorania Butchaya Chowdary v. State of Andhra Pradesh*, AIR 1958 Andhra 294 at p. 297.

The legislature can devise classes for the purpose of taxing or not taxing, exempting or not exempting, granting incentives and prescribing rates of tax, benefits and concessions<sup>53</sup>. Such devices are only to give flexibility in the matters of taxation and even a sub-delegation is possible to the executive, to legislate provisions for exemptions<sup>54</sup>.

No law can be guaranteed perfection by ensuring equality and equal consideration. Mathematical nicety and perfect equality are not required while enacting a tax law<sup>55</sup>. Rule of equality prohibits only discrimination of one person with another if as regards the subject matter of the legislation their position is the same<sup>56</sup>.

A method of equalization of burden by exempting small entrepreneurs from taxation, by differentiating medium and large entrepreneurs for levy of tax, cannot be

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<sup>53</sup> *State of Uttar Pradesh v. Kamala Palace*, 2000 (1) SCC 557 at para 12.

<sup>54</sup> *Orient Weaving Mills Ltd v. Union of India*, AIR 1963 SC 98 at p.103.

<sup>55</sup> Prof. Willis, *Constitutional Law*, 1<sup>st</sup> edn. at p. 579, as referred in *Charanjit Lal Chowdhary v. Union of India*, AIR 1951 SC 41 at para 8.

<sup>56</sup> *Southern Railway Co v. Greene*, 216 US 400 at p. 412.

held unlawful or arbitrary<sup>57</sup>. The authority of the legislature to fix different rates of tax in various states also cannot be narrowed down, when the legislatures in the appropriate states have independent power to choose the taxable subjects<sup>58</sup>. Although the levy of tax is universally applied through out the State, conversely, on the basis of different criteria in accordance with speciality of local authority, the classification cannot be held to be bad<sup>59</sup>.

The basis of the tax may be calculated in accordance with different laws in existence in different areas of jurisdiction. Taxing of consumption of goods by more affluent in society at higher rate and modest customers at lowest rate, shall not alter the reasonableness of classification<sup>60</sup>. The very basis of different rate of tax on lodging is the quality of residential accommodation enjoyed by the customers by virtue of their economic superiority, and is in accordance with the legislative wisdom and

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<sup>57</sup> *Indian Express News Papers v. Union of India*, 1985 (1) SCC 641 at p. 707.

<sup>58</sup> *Salar Jung Sugar Mills v. State of Mysore*, AIR 1972 SC 87 at para 46.

<sup>59</sup> *D.G. Gouse & Co. v. State of Kerala*, AIR 1980 SC 271 at para 24.

<sup>60</sup> *Kerala Hotel & Restaurant Association v. State of Kerala*, AIR 1990 SC 913 at para 32.

cannot be condemned as irrational by comparing the charges<sup>61</sup>. The State is empowered to differentiate the subjects for administrative convenience, by imposition of flat rate of tax to one group and commodity based tax for the other group<sup>62</sup>.

The parliament has the exclusive residuary power in addition to the power vested to them under Article 246<sup>63</sup>.

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<sup>61</sup> *Federation of Hotels & Restaurants v. Union of India*, AIR 1990 SC 1637 at para 21.

<sup>62</sup> *Avinder Singh v. State of Punjab*, 1979 (1) SCC 137 at para 5.

<sup>63</sup> *Constitution of India*, Article 246 reads as follows,

**Subject matter of laws made by Parliament and by the Legislatures of States.-** (1) Notwithstanding any thing in clauses (2) and (3) Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule (in this Constitution referred to as the “Union List).

(2) Notwithstanding any thing in clause (3), Parliament, and, subject to clause (i), the Legislature of any State also, have power to make laws with respect to any of the matters enumerated in List III in the Seventh Schedule (in this Constitution referred to as the “Concurrent List”).

(3) Subject to clauses (1) and (2), the Legislature of any State has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List II in the Seventh Schedule (in the Constitution, referred to as the “State List”).

(4) Parliament has power to make laws with respect to any matter for any part of the territory of India not included in a State notwithstanding that such matter is a matter enumerated in the State List.

This exclusive power also takes the power to enact laws for imposing taxes not mentioned anywhere in the Lists<sup>64</sup>.

Taxing power by and large is a means of economic regulation<sup>65</sup>. When the State enjoins the widest latitude with respect to the measures of economic regulations, the legislators are entitled to formulate diverse and quite often conflicting economic criteria, adjustment and balancing of various conflicting social and economic values and interests<sup>66</sup>. It is pertinent to note that no economic measures have yet been devised which is free from discriminatory impact and it cannot be possible to advise or to devise a perfect alternative to any of the economic issues<sup>67</sup>.

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<sup>64</sup> *Constitution of India*, Art. 248 reads,

**Residuary powers of legislation.-**

- (1) Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List.
- (2) Such power shall include the power of making any law imposing a tax not mentioned in either of those lists.

<sup>65</sup> *RMDC (Mysore) Pvt Ltd v. State of Mysore*, AIR 1962 SC 594.

<sup>66</sup> *Secretary to Government of Madras v. Sriramulu*, 1996 (1) SCC 345 at para 15.

<sup>67</sup> *Sociedade De Femento Industrial Pvt. Ltd v. Mormugo Dock Labour Board*, 1995 Supp (1) SCC 534 at para 16.

A taxing power derives from the specific entry in this regard not upon the general entries enumerated in the VIIth Schedule to the Constitution. It is subject to the legislative powers available in Article 246, and not beyond that. Constitution confers powers to the Parliament and State legislatures to make laws with respect to any of the matters enumerated in the exclusive lists notwithstanding the concurrent powers of Parliament and State legislature<sup>68</sup>.

An entry enabling legislation of taxing statute must be given widest possible interpretation so as to enable the legislature to make provisions for all incidental and ancillary purposes, which may be necessary to effectuate the law. A power to legislate as to the principal matter specifically mentioned in the entry shall also include within its expanse the legislations touching incidental and ancillary matters<sup>69</sup>. It is open to the legislature to enact a levy of tax and also to enact provisions which would check the evasion of tax<sup>70</sup>. A taxing law can be justified, when the legislature has

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<sup>68</sup> *Indu Bhussan v. Rama Sundari*, AIR 1970 SC 228 at para 12.

<sup>69</sup> *State of West Bengal v. Kesoram Industries*, 2004 (10) SCC 201 at para 31.

<sup>70</sup> *Board of Revenue v. Jhaver*, AIR 1968 SC 59 at para 13.

competence to enact the law under more entries than one in the relevant legislative lists or parts of it may be justified under one entry and parts under another<sup>71</sup>.

Unless there is transgression of constitutional principles, there is a presumption in favour of the constitutionality of a law passed by the appropriate legislature as the legislature understands and correctly appreciates the needs of its own people and society<sup>72</sup>.

### **1.3. Limitations on Taxing Power.**

Every power, be it a sovereign or an ordinary executive or legislative or judicial power, is subject to the limitations under the Constitution or under the statutes. Such powers are subject to inherent limitations also.

Power of taxing a subject has its own inherent limitations. Until the natural law or natural justice permits taxation, it can be made only through a State enacted law<sup>73</sup>. A legislature while imposing tax may choose to

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<sup>71</sup> H.M. Seervai, *Constitutional Law of India*, Vol. 3, 4<sup>th</sup> edn., Universal Book (1996) at p. 2320.

<sup>72</sup> *Middleton v. Texas Power Company*, 249 US 152 at p. 157.

<sup>73</sup> *A.K. Gopalan v. State of Madras*, AIR 1950 SC 27 at para 228.

impose the liability on persons from whom the collection of tax is most convenient<sup>74</sup>. But the decision of the legislature may not be final and adjudication is possible to see whether there was direct and intimate connection or nexus between the persons so chosen and the taxable event.

Enacting a taxing law is a most important and sacred trust known to the Civil Government and the representatives of the people are required to exercise their wise discretion and a sound judgement having due regards to the ability of the tax payers and general public welfare<sup>75</sup>.

It is beyond doubt to say that the imposition of tax might have social reflection, even the price escalation of essential commodities. Hence the taxing power can be invoked only in a reasonable way by understating its real impact on the society<sup>76</sup>. A legislative power to enact taxing laws cannot be fettered except by the express words of a

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<sup>74</sup> *Khyerbari Tea Co. Ltd. v. State of Assam*, AIR 1964 SC 925 at p. 935

<sup>75</sup> *Baker's Fundamental Laws of American Constitution*, Vol I at p. 287, as referred in *In re Article 143 of the Constitution of India and Delhi Laws Act*, AIR 1951 SC 332 at para 227.

<sup>76</sup> *Meenakshi v. State of Karnataka*, AIR 1983 SC 1283 at p. 1289.

Constitution and that it cannot be fettered by a contract or by a statute<sup>77</sup>.

#### **1.4. Constitutional Limitations.**

A taxing statute must satisfy the test of rule of arbitrariness or reasonableness and also the rule of reasonable classification as envisaged in Article 14<sup>78</sup> of the Constitution of India<sup>79</sup>. It is not an exception to the doctrine of equality<sup>80</sup>. A taxing legislation contrary to the due process of law is bad<sup>81</sup>.

The rule of reasonableness mandates fair, just and equitable treatment and an action in a manner that is reasonable, relevant and germane to effectuate the purpose of public good and in the general public interest<sup>82</sup>. The rule of reasonable classification permits a classification

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<sup>77</sup> *Kesavan v. State of Kerala*, AIR 1961 Ker. 36.

<sup>78</sup> *Constitution of India*, Art. 14 reads, **Equality before law**.- The State shall not deny to any person equality before law or the equal protection of the laws within the territory of India.

<sup>79</sup> *K.T. Moopil Nair v. State of Kerala*, AIR 1961 SC 552 at para 10.

<sup>80</sup> *Ashwathnarayana Setty v. State of Karnataka*, AIR 1989 SC 100.

<sup>81</sup> *Albert A Hoeper v. Tax Commission*, (1931) 76 Law Ed 248, as cited in *Balaji v. Income Tax Officer*, AIR 1962 SC 123 at para 10.

<sup>82</sup> *Life Insurance Corporation of India v. CE&RC*, 1995 (5) SCC 482 at para 27.

for legitimate purpose<sup>83</sup> and is not insisting that the legislative classification should be scientifically perfect or logically complete<sup>84</sup>. It only prohibits class legislation and not the reasonable classification for the purpose of legislation<sup>85</sup>.

The rule requires that to pass the test of permissible classification two conditions must be satisfied, that is (i) the classification must be founded on an intelligible differential which distinguishes persons or things that are grouped together from others left out of the group and (ii) that differential must have a rational relation to the object sought to be achieved by the Statute in question<sup>86</sup>.

Article 27 of the Constitution of India debars levy of tax for religious purposes<sup>87</sup>. But grant from consolidated

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<sup>83</sup> *State of Bombay v. Balsara F.N.*, 1951 SCR 682 at p. 708.

<sup>84</sup> *P.B Roy v. Union of India*, AIR 1972 SC 908.

<sup>85</sup> *Budhan Chowdhry v. State of Bihar*, 1955 (1) SCR 1045 at p. 1049.

<sup>86</sup> *Pathumma v. State of Kerala*, AIR 1978 SC 771 at para 41.

<sup>87</sup> *Constitution of India*, Art. 27, reads, **Freedom as to payment of taxes for promotion of any particular religion.**- No person shall be compelled to pay any taxes, the proceeds of which are specifically appropriated in payment of expenses for the promotion or maintenance of any particular religion or religious denomination.

fund is possible in case of certain religious institutions, by virtue of Article 290A<sup>88</sup>. Additionally the prohibition will not distress the beneficial scheme for the public, though the ownership is vested with the religious head or deity<sup>89</sup> or a scheme for even reconstruction of religious places damaged in a communal riot<sup>90</sup>.

The Constitution expressly forbids levy and collection of tax without authority of law<sup>91</sup>. This prohibition corresponds to Article 1, Section 8(1) of the Constitution of United States<sup>92</sup> and Section 51 (ii) of the Commonwealth of

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<sup>88</sup> *Constitution of India*, Art. 290 A reads, **Annual Payment to certain Devaswom.**- A sum of forty-six lakhs and fifty thousand rupees shall be charged on, and paid out of, the Consolidated Fund of the State of Kerala every year to the Travancore Devaswom Fund; and a sum of thirteen lakhs and fifty thousand rupees shall be charged on, and paid out of the Consolidated Fund of the State of Tamil Nadu every year to the Devaswom Fund established in that State for the maintenance of Hindu Temples and shrines in the territories transferred to that State on the 1<sup>st</sup> day of November, 1956, from the State of Travancore- Cochin.

<sup>89</sup> *Bira Kishore Mohanty v. State of Orissa*, AIR 1975 Orissa 8 at p. 11.

<sup>90</sup> *Raghunath v. State of Kerala*, AIR 1974 Ker. 48.

<sup>91</sup> *Constitution of India*, Art. 265 reads, **Taxes not to be imposed save by authority of law.** - No tax shall be levied or collected except by authority of law.

<sup>92</sup> *United States Constitution*, 1787, Art. 1, Section 8(1) reads, The Congress shall have power to lay and collect taxes, duties, imposts and excise, to pay the Debts and provide for the Common Defence and general welfare of the United States; but all duties, imposts and excises shall be uniform throughout the United States.

Australia Constitution Act, 1900<sup>93</sup>. The law referred in Article 265 is a valid law, which is enacted within the legislative competence of the legislature imposing the tax<sup>94</sup>. Equally, the expression law in Article 265 takes the characteristics of law, as referred in Article 21<sup>95</sup> also, which should not be arbitrary, unfair and unreasonable, as held in *Maneka Gandhi v. Union of India*<sup>96</sup>. As held in *Kochunni v. State of Madras*<sup>97</sup>, it is manifest that the law must satisfy two test before it can be a valid law, firstly, the appropriate legislature has competency to make the law; and secondly it does not take away or abridge any of the Fundamental Rights guaranteed in Part III of the Constitution of India.

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<sup>93</sup> *Commonwealth of Australia Constitution Act, 1900*, Section 51, reads, as follows

**Section 51. Legislative Powers of the Parliament.-** The Parliament shall, subject to this Constitution, have power to make laws for the peace, order and good government of the Commonwealth with respect to :

- i. ...
- ii. taxation, but so as not discriminate between states or part of states;

<sup>94</sup> *Balaji v. Income Tax Officer*, AIR 1962 SC 123 at p. 128.

<sup>95</sup> *Constitution of India*, Art. 21 reads, **Protection of life and personal liberty.-** No person shall be deprived of his life or personal liberty except according to procedure established by law.

<sup>96</sup> AIR 1978 SC 597.

<sup>97</sup> 1960 (3) SCR 887 at p. 911: AIR 1960 SC 1080.

These two constitutional riders are equally applicable to the taxing statutes also<sup>98</sup>.

After the decision of the Supreme Court in *Kesavananda Bharati v. State of Kerala*,<sup>99</sup> it has to satisfy that the law is not infringing any of the basis features of the Constitution. Thus validity of any law or change in law is essentially a matter to be judged by applying the test whether it alters the essential features or basic structure of the Constitution<sup>100</sup>.

A law may not be a valid one, only for the reason that it is enacted by the State, if the law suffers from the vice of excessive delegation or it constitutes a colourable exercise of the legislative power or if it is in vires with the parent statute or if it is in contravention of fundamental rights or if it is vague or if it violates natural justice. When the term law

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<sup>98</sup> *Supra*, n. 94 at para 13.

<sup>99</sup> (1973) 4 SCC 225 at p. 468: AIR 1973 SC 1461. In *Kesavananda Bharati's* case, the 13 Judges larger bench of the Apex Court overruled the ratio of 11 Judges Bench in *Golak Nath L.C. v. State of Punjab*, AIR 1967 SC 1643, in which it was held that the power to amend the Constitution being a constituent power cannot be held subject to any implied limitations and there is no basic features to the Constitution, which cannot be amended. (See at para 91 of the judgment)

<sup>100</sup> *Minerva Mills Ltd v. Union of India*, AIR 1980 SC 1789 at para 29.

is interpreted in tune with the definition of existing law, it is obvious that it primarily means statute law, including subordinate legislation like, rule, regulation or any order or notification made by the statutory authority<sup>101</sup>.

The taxing power of the State is subject to another limitation that a taxing legislation shall not invade a legislative field demarcated exclusively for the other field by the Constitution<sup>102</sup>. A matter which the Constitution makers had foreseen, were conscious of or had deliberated upon, could not be relegated to any residuary power or allowed to encroach upon others field<sup>103</sup>. Article 245 is the fountain source of the Legislative power.

The legislative fields between the Parliament and State legislatures are specifically demarcated in Article 246 of the Constitution of India. In the three list appended to VIIth Schedule, there is clear cut distinction and classification between the general legislative entries and

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<sup>101</sup> *Edward Mills Co. Ltd v. State of Ajmer*, AIR 1955 SC 25.

<sup>102</sup> *A.G. for Canada v. A.G. for Ontario*, [1937] AC 335 (PC).

<sup>103</sup> *Kesavanada Bharati Sripadgalvaru v. State of Kerala*, 1973 (4) SCC 225 at p. 468: AIR 1973 SC 1461.

entries relating to taxation<sup>104</sup>. These entries are only the legislative heads/ fields enabling the appropriate legislatures to enact the law subject to the power in Article 246, and not an independent power to legislate<sup>105</sup>. The power to tax cannot be deduced from a general legislative entry as an ancillary power<sup>106</sup>. It is a distinct matter for purpose of legislative competence<sup>107</sup>.

The Constitution effects a complete separation of the taxing power of the Central and State units of the federal system of Government. To maintain the harmony of the federal units, there are limitations provided under Arts. 285<sup>108</sup> and 289<sup>109</sup> prohibiting taxing of property of the Union

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<sup>104</sup> *M.P.V. Sudararamaier and Co. v. State of A.P.*, AIR 1958 SC 468 at p. 493.

<sup>105</sup> *Hoechst Pharmaceuticals Ltd v. State of Bihar*, 1983 (4) SCC 45.

<sup>106</sup> *State of West Bengal v. Kesoram Industries*, 2004 (10) SCC 201 at para 31.

<sup>107</sup> *Union of India v. H S Dhillon*, AIR 1972 SC 1061.

<sup>108</sup> *Constitution of India*, Art. 285 reads as follows;

**Exemption of property of the Union from State taxation.-**

- (1) The property of the Union shall, save insofar as Parliament may by law otherwise provide, be exempted from all taxes imposed by a State or by any authority within a State.

by State and exempting property and income of the State from central taxation, subject to the conditions.

As observed by the Supreme Court in *S.R. Bommai's* case<sup>110</sup>, though our Constitution guarantees a federal structure, with equally important units, Centre and States, the totality of the provisions in the Constitution unmistakably justifies that the founding fathers intended to create a strong centre. In the matters of finance and

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- (2) Nothing in clause (1) shall, until Parliament by law otherwise provides, prevent any authority within a State from levying any tax on any property of the Union to which such property was immediately before the commencement of this Constitution liable or treated as liable, so long as that tax continues to be levied in that State.

<sup>109</sup> *Constitution of India*, Art. 289 reads as follows;

**Exemption of property and income of a State from Union taxation.-**

- (1) The property and income of a State shall be exempt from Union Taxation.
- (2) Nothing in clause (1) shall prevent the Union from imposing, or authorising the imposition of, any tax to such extent, if any, as Parliament may by law provide in respect of a trade or business of any kind carried on by or, on behalf of, the Government of a State, or any operations connected therewith, or any property used or occupied for the purpose of such trade or business, or any income accruing or arising in connection therewith.
- (3) Nothing in clause (2) shall apply to any trade or business, or to any class of trade or business, which Parliament may by law declare to be incidental to the ordinary function of Government.

<sup>110</sup> *S.R. Bommai v. Union of India*, 1994 (3) SCC 1 at p. 217.

taxation, the State units are placed in a less favourable position, and having inbuilt limitations<sup>111</sup>. Several taxes are being collected by the Centre, subject to allocation of revenue to the State, of course guided by the constitutional principles and other material factors.

### **1.5. Judicial Restraints.**

Judicial review is permissible, as well, in the cases of taxing statutes<sup>112</sup>. The assumption that supports the theory of judicial review of all law making is that the Court acts as the interpreters of real will of the people<sup>113</sup>. The power of the State to enact the taxing statute and levy taxes is more extensive than any other Governmental functions. Such powers of taxation are normally exercised with great arbitrariness and unreasonableness which may impose liability of tax retrospectively or even in a confiscatory manner<sup>114</sup>. A public body may some times commit errors of

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<sup>111</sup> Setalvad M.C., “Union and State Relations under the Indian Constitution”, *Tagore Law Lectures*, Eastern Law House, Calcutta, (1974).

<sup>112</sup> *State of Andhra Pradesh v. Nalla Raja Reddy*, AIR 1967 SC 1458.

<sup>113</sup> See the observations of Beg, J in *Indira Nehru Gandhi v. Raj Narain*, AIR 1975 SC 2299 at para 394.

<sup>114</sup> *Mega Traders v. State of Kerala*, [1991] 83 STC 59 (Ker.).

judgement, while it's functioning and if it happens the citizen requires a remedy. Thus Judiciary has a greater role in avoiding the divergence of interest between the taxman and taxpayers.

There are occasions of ambiguity and conflicts when the entries in different list or in the same list are overlapping or may appear to be in direct conflict with each other. Thus it is the duty of the Courts to remove the ambiguity and the lacuna by a proper interpretation of its scope and by an authoritative declaration by the Apex Court under Article 141<sup>115</sup>.

In the last six decades of the Indian Judiciary, the Supreme Court and High Courts in India have made

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<sup>115</sup> *Constitution of India*, Article 141 reads as follows

**Art. 141. Law declared by Supreme Court to be binding on all courts.** - The law declared by the Supreme Court shall be binding on all courts within the territory.

In *State of U.P. v. Synthetics and Chemicals Ltd*, 1991 (4) SCC 139, the Supreme Court founded the inherent limitation in Art. 141 and held that a decision which is not express and is not founded on reasons nor proceeds on a consideration of the issue cannot be deemed to be a law declared to have a binding effect as is contemplated in Art. 141. In *Union of India v. Dhanwanti Devi*, 1996 (6) SCC 44 at para 9, the Supreme Court reiterated that only ratio decidendi is binding; the obiter dicta (general observations) have no binding force.

significant contributions to the advancement of Indian taxation system. There are as many principles of law in the tax regime, settled by the Courts in India interpreting the scope and ambit of the taxing statutes in relation to the general principles of taxation and constitutional provisions.

There are large numbers of principles evolved by the Judiciary in the field of interpretation of taxing statutes. In taxing matters it is advised to take a commonsense view to understand the scope of taxing entry as well as commodity which is subjected to tax.<sup>116</sup>

Chiefly, while interpreting the taxing subject, it is extensively understood in its popular meaning or its trade or commercial parlance<sup>117</sup>. However in certain unusual circumstances, it was held that while construing a word which is of a technical or scientific character, its technical or scientific meaning is required to be assigned.<sup>118</sup> To avoid inconvenience and absurdity in interpretation of taxing

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<sup>116</sup> *Rajasthan Roller Flour Mills Association v. State of Rajasthan*, [1993] 91 STC 408 (SC).

<sup>117</sup> *Plasmac Machine Manufacturing Co. Pvt. Ltd v. Collector of Central Excise*, [1992] 84 STC 107 (SC).

<sup>118</sup> *Akbar Badradin Tiwan v. Collector of Customs*, AIR 1990 SC 1579.

statute, it is permissible to look in to legislative intention behind the enactment.<sup>119</sup>

It was the consistent stand of the Apex Court that it is appropriate for the legislature to adopt proper method for measurement of tax and not for the court to advise the legislature to adopt a particular method<sup>120</sup>. It was also held that the reasonableness of rate of tax is outside the scope of judicial review<sup>121</sup>.

In many of the circumstances, the judicial interventions made reasons for a chunk on the affirmative responsibility of the legislatures. Inequality in taxing the same class of people was held unconstitutional on the ground of infringement of Article 14 of the Constitution of India, in several occasions<sup>122</sup>. While granting a fairly wide discretion to the legislature in the matter of fiscal adjustment, the Court, at the same time insists that the

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<sup>119</sup> *Directorate of Enforcement v. Deepak Mahajan*, AIR 1994 SC 1175.

<sup>120</sup> *D.G. Gouse & Co v. State of Kerala*, AIR 1980 SC 271.

<sup>121</sup> *S. Kodar v. State of Kerala*, (1975) 1 SCR 121.

<sup>122</sup> *Supra*, n. 79. See also in *State of Kerala v. Haji K. Kutty Naha*, AIR 1969 SC 378.

statute in question should not infringe the equality principles<sup>123</sup>.

Equally the Judiciary adopted a pragmatic approach in resolving the problems in the meadow of tax, rather than measuring the propositions by abstract symmetry. Once, the Supreme Court<sup>124</sup> highlighted, the guidelines of Frankfurter, J, to justify this self imposed limitations. It was also reminded that every effort should be made as far as possible to reconcile the seeming conflict between tax entries<sup>125</sup>.

The allocation of subject of taxation in various entries in the Seventh Schedule is not comprehensive or unambiguous. Thus in *Hoechst Pharmaceuticals Ltd's*

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<sup>123</sup> *Twyford Tea Co. Ltd v. State of Kerala*, AIR 1970 SC 1133 at para 33.

<sup>124</sup> R.C. Lahoti, J in *State of West Bengal v. Kesoram Industries*, 2004 (10) SCC 201 at para 32 reminded following observations of Frankfurter J, in *Morey v. Doud*, 354 US 457,

“In the utilities, tax and economic regulation cases, there are good reasons for judicial self-restraint if not judicial deference to legislative judgment. The legislature after all has the affirmative responsibility. The courts have only the power to destroy, not to reconstruct. When these are added to the complexity of economic regulation, the uncertainty, the liability to error, the bewildering conflict of the experts, and the number of times the judges have been overruled by events - self-limitation can be seen to be the path to judicial wisdom and institutional prestige and stability”

<sup>125</sup> *Supra*, n. 40.

case<sup>126</sup>, the Supreme Court held that the allocation of subjects in the list is not by way of scientific or logical definition, but by way of a mere simplex enumeration of broad categories. Thus the entries must receive a liberal construction inspired by broad and generous spirit and not in a narrow pedantic sense.

The only restriction, self imposed, on the judicial review in taxation matter is that the Courts normally treat the judicial review as a reserve power; a power to be used when there is no alternative procedure available which is equally convenient and effective<sup>127</sup>.

It is significant to note that the ever followed outlook of the Apex Court, declared in *R.K. Garg v. Union of India*<sup>128</sup> still hold the filed, in which it was held that the court should feel more inclined to give judicial deference to legislative judgment in the field of economic regulation than in other areas where the fundamental human rights are involved.

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<sup>126</sup> *Hoechst Pharmaceuticals Ltd v. State of Bihar*, 1983 (4) SCC 45.

<sup>127</sup> Simon James, *Taxation- Critical Perspectives on the World Economy*, Vol.II, (2002), Routledge, London & New York. at p. 344.

<sup>128</sup> AIR 1981 SC 2138 at para 8.

## CHAPTER II

### **Concept of Sale in Tax Regime**

The tax is the major source of public revenue. It would mean a compulsory contribution in support of the Government levied on persons, property, income, commodities, transactions etc<sup>129</sup>. There should be a character of imposition and subject of taxation in a progressive taxation policy<sup>130</sup>. The character of imposition refers to the taxable event. Sale of goods is one such taxable event, which contributes major part of the State's exchequer<sup>131</sup>.

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<sup>129</sup> *The History and Philosophy of Taxation*, Compilation of papers by Marshall-Wythe School of Law, published by College of William and Mary (1955)

<sup>130</sup> *Govind Saran Ganga Saran v. Commissioner of Sales Tax*, AIR 1985 SC 1041.

<sup>131</sup> Girish K. Srivastava, *Commercial Taxes in India*, Pitaliya Pustak Bhandar (1975) at p.23

## **2.1. Significance of Sales Tax.**

The sales tax is leviable on the commodity corresponding to the point of transactions<sup>132</sup> or on the turnover<sup>133</sup> of the traders. A sales tax is an excise in so far as it is imposed upon domestic transactions of commodities, and it may also have some of the aspects of customs duties because national sales taxes commonly fall upon importing and sometimes upon exporting<sup>134</sup>.

Not all excises are imposed upon sales or the privilege of selling, however, for they may be placed upon the purchase or use of commodities in some times, services too.

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<sup>132</sup> Sales Tax is a commodity tax on one hand and tax on transaction on the other hand. The very classification of sales tax law is based on the above characteristics. There are three kind of tax system based on the point of levy. Single point, Double points and Multi points or Multiple points. In a single point tax the incidence of sales tax levy is one point, either the first sale or the last sale. However in Double point taxation the incidence of taxation shall be both the first and last points of a chain of sales. In a multi point system, the points of levy are each incidence of sales in a chain of sales.

<sup>133</sup> Turnover tax is a kind of sales tax, but a different levy that it taxes the turnover of the dealer at a fixed rate.

<sup>134</sup> *Buehler's Public Finance*, 3<sup>rd</sup> edn. McGraw-Hill (1948) at p 410, referred in *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, [1963] 14 STC 316 at p. 337.

## **2.2. Historical Importance of Sales Tax: A Trans-national View.**

Even from the ancient times, the sales tax has major role in the King's revenue<sup>135</sup>. Sales tax is said to have been prevalent in ancient Athens, Egypt under Ptolemies and Ancient Rome under Augustus<sup>136</sup>. In Ancient Greece, there were both retail sales tax in the form of market transfer taxes and heavy taxes on the sales of whole sales merchants<sup>137</sup>. Even the exchanges of slaves were subject to sales tax during those periods.

In middle ages, merchants were subjected to sales tax in Germany, France, Spain and Italy<sup>138</sup>. A tax of five-twelfth percent on sales and purchases was levied in France in 1292 except small sales and sales of foodstuffs<sup>139</sup>.

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<sup>135</sup> Walter A Goffart, *Caput and Colonate: Towards a History of Late Roman Taxation*, University of Toronto Press (1974).

<sup>136</sup> "A history of taxation" published in <http://www.taxworld.org/history/taxhistory.htm>.

<sup>137</sup> C.V. Mahalingam, *A Historical Sketch of Sales Tax*, [1953] 4 STC 28 (Journal).

<sup>138</sup> Edwin Robert Anderson Seligman, *Progressive Taxation in Theory and Practice*, American Economic Association (1909).

<sup>139</sup> *Supra*, n. 137.

In Ancient India the sales tax in its real form was introduced during the age of Mauryas<sup>140</sup>. A trade tax, 'biyajji', was levied due on commodities sold by cubical measures as 1/16<sup>th</sup> of the quantity, by weighing balance as 1/20<sup>th</sup> of the quantity and in numbers as 1/11<sup>th</sup> of the total number<sup>141</sup>. Spain introduced an *ad valorem* tax namely "Alcavala" on all sales of property at 10 percent of the sale proceedings<sup>142</sup>.

The sale tax prevailed in ancient India is moderate one that the rate of tax is subject to the nature of commodity, the distance from which the commodity was brought and all expenses towards food and charges for securing the goods.<sup>143</sup> Some texts suggest that tax should

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<sup>140</sup> During the reigme of Chandragupta Maurya, an eminent ruler in the age of Mauryas, during 322-289 BC. Reference is made in Kautilya's *Arthasasthra*, Book II, Chapter 16 and in Rajendra Kumar Jain, *State Taxation in India*, Progress Publishers; Progressive Book Depot (1972). See also *supra*, n. 9 at pp- 78-100.

<sup>141</sup> Kautilya's *Arthasasthra*, Book II, Chapter 16. See the full text, digitalized and published in the website, <http://www.mssu.edu/projectsouthasia/history/primarydocs/Arthashastra/BookII.htm>, visited on 01-10-2008.

<sup>142</sup> The Cambridge, *Modern History*, Vol IV (1906) at p. 627.

<sup>143</sup> Manu, VII, 237. See the full text digitalized and published in <http://www.mssu.edu/projectsouthasia/history/primarydocs/manu/index.htm> visited on 01-10-2008.

be levied only on the net profit<sup>144</sup> and seller is not liable to pay sales tax in the absence of profit<sup>145</sup>. The places of levy of tax, 'sulka' are market places, roads and mines<sup>146</sup>. The Kings imposed sale tax on traders on goods carried by land and water<sup>147</sup>. Sale taxes on Import and Export<sup>148</sup> of goods also prevailed.

At some stage in the middle ages a form of sales tax was introduced, namely 'alcabala'/ 'sakabala', in Spain in 1342<sup>149</sup>. The same was followed till the middle of the 19<sup>th</sup> Century. Under this kind of tax on the sales of commodities, the rate was 5% to 10% on the entire business turnover subject to constant alteration in the rate<sup>150</sup>. During 18<sup>th</sup> Century, the sales tax was introduced in England to meet

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<sup>144</sup> Yajnavalkya, II, See the full text digitalized and published in [http://www.gutenberg.org/files/21918/21918-h/21918-h.htm#FNanchor\\_270\\_270](http://www.gutenberg.org/files/21918/21918-h/21918-h.htm#FNanchor_270_270), visited on 01-10-2008.

<sup>145</sup> Sukra, Ch. IV-II 109, referred in K.R. Sarkar, *Public Finance in Ancient India*, Abhinav Publications (2003).

<sup>146</sup> Sukra, Ch. IV-II 107- 108, *ibid*.

<sup>147</sup> Manu, VII, 127, referred in Rajendra Nath Sharma, *Ancient India According to Manu*, Nag Publishers, New Delhi (1980).

<sup>148</sup> Kautilya, pp 126-127, *The Kautiliya Arthasastra*, compiled by R. P. Kangle, Motilal Banarndsidass Publication (1997).

<sup>149</sup> John Huxtable Elliott, *Empires of the Atlantic World: Britain and Spain in America, 1492-1830*, Yale University Press, (2006) at p. 355.

<sup>150</sup> Adam Smith, *Wealth of Nations*, Prometheus Books (1991).

the heavy expenditure caused by the Wars with France<sup>151</sup>. In United States the sales tax was introduced during the Civil War<sup>152</sup>. In Mexico sales tax was introduced in the year 1893. Sales tax at the rate of 1/3<sup>rd</sup> % was introduced in Philiphense in 1905. In Burma 5/12<sup>th</sup> percentage sales tax was introduced in the year 1861.

After the First World War the sales tax was very familiar in many countries, as a result of heavy post war expenditure and the consequential inflation. The Sales tax particularly that imposed on goods introduced in different countries in different forms. Its levy was either on the turnover on the volume of wholesale and in some times on the retain sales.

In the year 1916 the German Republic invented the turnover tax known as '*Umsatzsteuer*'. The revenue collection by way of tax on goods and services was very successful in Germany and the concept of sales tax become very popular source of revenue among the

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<sup>151</sup> William Tayler, *The History of the Taxation of England*, Hope & Co., London (1853).

<sup>152</sup> Carl Copping Plehn, *Introduction to Public Finance*, The Macmillan Company (1897).

European Countries<sup>153</sup>. In France, a year later, a kind of transaction tax, namely, “*L’import sur le chiffré d’affaires*” was introduced. In French Taxation system the excise and sales tax were interchangeable, the former being a replacement tax on the turnover of the manufacturer. Though in Germany the tax included both goods and services, in France services were excluded unless there was a commercial element.

In Italy, the sales tax was introduced in 1919. In the year 1920 in Czechoslovakia, a law providing for the sales tax at the rate of 1% on the total selling price of a commodity was implemented. Canada also followed the European trend and introduced sales tax in the year 1920. The significant of the Canadian sales tax law is that it covers multi point sales tax at the rate of 1% each, on the Manufactures or Wholesalers at the first point and Retailers and Consumers at the second point. It was producers’ or manufactures’ tax almost in the nature of excise duty.

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<sup>153</sup> D.P. O’Brien, *History of Taxation*, Pickering & Chatto Publishers (1990).

Belgium introduced sales tax in the year 1921, in tune with Canadian experiences and followed similar tax pattern. Tax was collected by stamps from both the seller and the buyer according to their respective invoices. Rumania, Hungary, Russia and West Virginia introduced the sales tax in the year 1921<sup>154</sup>. Cuba and Luxemburg introduced sales tax in the year 1922. In Austria the sales tax was introduced in the year 1923 following the German Pattern of tax. Poland introduced sales tax in the year 1924 on the gross sales, turnover basis. Brazil also introduced sales tax in the year 1924. During 1929 to 1939 the sales tax was introduced by various states in USA<sup>155</sup>.

In USA, the sales tax was an excise in so far it is imposed upon domestic transaction of commodities. The popular name for American excises is sales tax<sup>156</sup>. There is no standard usage, for selected sales taxes are often called

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<sup>154</sup> Edgar Sydenstricker, *A Brief History of Taxation in Virginia*, Virginia Legislative Reference Bureau, Superintendent Public Printing (1915).

<sup>155</sup> W. Elliot Brownlee, *Federal Taxation in America: A Short History*, Cambridge University Press (2004).

<sup>156</sup> David R. Burton and Dan R Mastromarco, *Emancipating America from the Income Tax: How a National Sales Tax Would Work*, Cato Institute (1997).

sales taxes, limited sales taxes, selective sales taxes and special sales taxes, while general sales taxes may be called sales taxes, turnover taxes, manufacturers' sales taxes, retail sales taxes etc<sup>157</sup>.

The unanticipated financial dilemma faced by the different countries, due to the war and reconstruction expenses, obligated the nations to introduce the sales tax either on commodity basis or on turnover tax basis<sup>158</sup>. Australia in 1930, Netherlands, New Zealand and Norway in 1933, Britain in 1940, Finland and Switzerland in 1941, Chile in 1943, Pakistan and Japan in 1948 and Indonesia in 1950 introduced the sales tax to meet their increasing public expenses.

Sales Tax is an indirect tax; the levy is on the consumption of goods by the end consumer, though it is collected from the collecting agents, namely dealers, of course at different points, according to the kind of tax system, either single point or multi points or multiple points.

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<sup>157</sup> Billy Tauzin, *National Retail Sales Tax*, Claitors Publication Division (1998).

<sup>158</sup> Carolyn Webber, Aaron Wildavsky, *A History of Taxation and Expenditure in the Western World*, Simon and Schuster (1986).

In United States of America, sales tax is levied on retail sale only being a tax on end purchase of goods, leaving out all other points, such as resale or for subsequent processing<sup>159</sup>.

### **2.3. Sales Tax in India.**

In pre-independent India, the concept of sales tax first visualised in the Report of Taxation Enquiry Committee by suggesting a turnover tax on the retail merchants and a quarterly collection<sup>160</sup>. But the type of tax suggested by the Enquiry Committee as a modification of the octroi through the intermediate steps of taxing markets and slaughter houses. The aim behind such suggestion was that price competition would stop inclusion of tax in the price.

Following the recommendation of the Enquiry Committee, the Provinces were empowered to levy the tax on sales, in tune with the Government of India Act, 1935<sup>161</sup>.

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<sup>159</sup> *United States Sales Tax–Introduction*, published in [http://www.usa-sales-use-tax-e-commerce.com/Intro\\_sales.asp](http://www.usa-sales-use-tax-e-commerce.com/Intro_sales.asp).

<sup>160</sup> See *Report of the Taxation Enquiry Committee (1924-25)*.

<sup>161</sup> The Government of India Act, 1935 (25 & 26 Geo.5 c.42) was passed in August, 1935. It aimed to grant large measure of autonomy to the provinces of British India by ending the system of Diarchy introduced by the Government of India Act, 1919.

Introduction of an exceptional commodity sales tax system in India was a major task. Taxes on the sale of goods being a kind of commodity taxes had to be demarcated from other commodity taxes like excise, octroi, terminal tax, market duties etc. To resolve such a difficulty, the goods are treated as the subject of taxation in different stages, like production, movement, sale and consumption<sup>162</sup>. Taxes on production of goods, Excise entrusted with Centre<sup>163</sup>, Taxes on Sale of goods were given to Provinces<sup>164</sup> and taxes on movement of goods<sup>165</sup> were earmarked between Centre and Provinces. Taxes on the entry of goods in a Local Area for consumption, use or sale were allotted to the Provinces<sup>166</sup>.

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<sup>162</sup> Pramathanath Banerjea, *A History of Indian Taxation*, University of Calcutta, Macmillan and co. Limited (1930). See also in Sunil Rangan Sarkar, "Sales Tax has a History in India", *Indian Journal of Economics*, Vol.34 (Oct.1953) at p. 93.

<sup>163</sup> *The Government of India Act, 1935*, Entry 45, List 1 read with Entry 40, List II, Seventh Schedule.

<sup>164</sup> *The Government of India Act, 1935*, Entry 48, List II, Seventh Schedule.

<sup>165</sup> *The Government of India Act, 1935*, Entry 58, List I and Entry 52, List II, Seventh Schedule.

<sup>166</sup> *The Government of India Act, 1935*, Entry 49, List II, Seventh Schedule.

The Central Provinces introduced the sales tax in the year 1938<sup>167</sup>. Madras Province introduced sales tax in the year 1939<sup>168</sup> to make up the revenue loss caused due to the implementation of prohibition policy. In the year 1946, the State of Travancore Cochin introduced a multi point sales tax at three pies in rupee at all point of sale. It was introduced as the main source of revenue to the Provinces under the scheme of Provincial autonomy<sup>169</sup>.

The system of Sales tax prevailed among the different provinces were not identical<sup>170</sup>. In Madras, Mysore, Travancore- Cochin and Hyderabad, sale means transfer of property in the course of trade or business. By implication all other sales were excluded. Casual sales by

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<sup>167</sup> The Central Provinces Government implemented Central Provinces and Berar Sales of Motor Spirit and Lubricants Taxation Act 1938, to levy and collect tax from the retail dealers on the retail sale of motor spirit and lubricants at the rate of 5% on the value of such sales. See the discussion in *In re C.P. etc. Motor Spirit Taxation Act* reported in [1951] 1 STC 1.

<sup>168</sup> The Province of Madras enacted a multipoint general sales tax, The Madras General Sales Tax Act, 1939. See the discussion in *Province of Madras v. Boddu Paidanna* reported in [1951] 1 STC 104 (FC). The Federal Court, in the above case, decided the constitutional validity of the Act.

<sup>169</sup> A. K. Chawla, *Constitutional Study of Sales Tax Legislation in India*, N. M. Tripathi (1973).

<sup>170</sup> *Report of Taxation Enquiry Commission (1953-54)*, Vol.III at p. 10.

individuals, sales of food by hostels attached to educational institutions, sales of old furniture etc were not sale exigible to sales tax in these Provinces. In Bengal and Delhi sale was a transfer of property in goods for money consideration which accordingly excludes transfers of other consideration like exchange or barter.

In the matters of levy also the system of taxation was different among the States in pre- independent India<sup>171</sup>. In some States for the purpose of taxation the sale is deemed to have taken place in the territory of State, if at the time when the contract of sale or purchase was made, the goods were actually in those States. In Certain States, the transfer or property in goods supplied in the execution of a contract was also a sale for the purpose of taxation.

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<sup>171</sup> G. R. Rao, *Sales Tax Laws of India: Comparative Analysis of the Sales Tax System in Different States*, Hindustan Chamber of Commerce (1968).

For a detailed and comparative analysis of concept of sale in different State's sales tax statutes, see K. Chaturvedi & P. Kothary, *The Principles of Sales Tax Laws*, 5<sup>th</sup> edn. Vol.I, Wadhwa & Company (Nagpur) (1987) at p. 184.

After the independence and the introduction of the Constitution of India the sales tax law which prevailed in the princely states and provinces, immediately before the Constitution was made valid under the specific provisions of Article 277<sup>172</sup>. Later in 1956, the Parliament of India enacted the Central Sales Tax Act<sup>173</sup> to cover up the export or import sales and inter state sales. Under the legislative powers derived from the Article 246<sup>174</sup> of the Constitution of

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<sup>172</sup> Constitution of India, Article 277 reads, **Savings**. - Any taxes, duties, cesses or fees which, being lawfully levied by the Government of any State or by any municipality or other local authority or body for the purposes of the State, municipality, district or other local area may, notwithstanding that those taxes, duties, cesses or fees are mentioned in the Union List, continue to be levied and to be applied to the same purposes until provision to the contrary is made by Parliament by law.

<sup>173</sup> The Central Sales Tax Act, 1956 was enacted by the Parliament, which is a comprehensive legislation to formulate principles in determining when a sale or purchase of goods takes place in the course of inter-State trade or commerce or outside a State or in the course of import into or export from India with provisions for levy, collection and distribution of taxes and also enumerating the goods to be of special importance in inter-State trade or commerce. The Act was enacted in terms of the recommendations of Taxation Enquiry Committee.

<sup>174</sup> *Constitution of India*, Art. 246 (1).- Notwithstanding any thing in clauses (2) and (3) Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule (in this Constitution referred to as the "Union List).

India and the corresponding entry 54<sup>175</sup> in the State list, the different State Units enacted state sales tax laws<sup>176</sup> to

- (2) Notwithstanding any thing in clause (3), Parliament, and, subject to clause (i), the Legislature of any State also, have power to make laws with respect to any of the matters enumerated in List III in the Seventh Schedule (in this Constitution referred to as the “Concurrent List”).
- (3) subject to clauses (1) and (2), the Legislature of any State has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List II in the Seventh Schedule (in the Constitution, referred to as the “State List”).
- (4) Parliament has power to make laws with respect to any matter for any part of the territory of India not included in a State notwithstanding that such matter is a matter enumerated in the State List.

<sup>175</sup> *Constitution of India*, Seventh Schedule, List II, entry 54 reads,

“Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I.

Entry 92 in List I, reads, “Taxes on the sale or purchase of newspapers and on advertisements published therein.

Entry 92A in List I, reads, “Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade and commerce.

Entry 92B in List I, reads, “Taxes on consignments of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-state trade of commerce”.

<sup>176</sup> After the enforcement of Constitution of India, the Legislatures in the different States either followed the pre-constitutional laws or enacted new Sales Tax Acts, repealing the existing Acts.

Some of the Acts enacted after the enforcement of Constitution are, The Rajasthan Sales Tax Act, 1954 (Repealed by Rajasthan Sales Tax Act, 1994), The West Bengal Sales Tax Act, 1954 (Repealed by West Bengal Sales Tax Act, 1994), The Assam Finance (Sales Tax ) Act, 1956 (Repealed by Assam General Sales Tax Act, 1993), The Karnataka Sales Tax Act, 1957.....

enable levy of tax on the sales and purchase of goods carried with in the territorial jurisdiction of the state.

Presently, in India, sales tax is levied at all the point of sale based on the value addition, after introduction of Value Added Sales Tax in 2005 as a uniform method of tax through out the country. Formerly, there were different systems of levy of tax, either on the first point of sale/ purchase or on the last point of sale/ purchase or both on the first and last sale/ purchase, suitably, depending on the potentiality and substance of the commodity. Thus a commodity after the manufacture and clearance from the factory is subject to sales tax, on the occasion of sale of goods.

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The Andhra Pradesh General Sales Tax Act, 1957, Madhya Pradesh General Sales Tax Act, 1958, Bombay Sales Tax Act, 1959, Tamil Nadu General Sales Tax Act, 1959, Jammu & Kashmir General Sales Tax Act, 1962, Kerala General Sales Tax Act, 1963, Goa, Daman – Diu Sales Tax Act, 1964, Pondichery General Sales Tax Act, 1967, Nagaland Sales Tax Act, 1967, Himachal Pradesh General Sales Tax Act, 1968, Gujarat Sales Tax Act, 1969, Haryana General Sales Tax Act, 1973, Delhi Sales Tax Act, 1975, Tripura Sales Tax Act, 1976, Bihar Finance Act, 1981, Mizoram Sales Tax Act, 1989 and Manipur Sales Tax Act, 1990.

Some of these legislations are repealed by Value Added Tax Acts, in the States where the Uniform Value Added System of Tax is introduced replacing the single point levy of tax.

The imposition of sales tax is normally influenced by political and economical factors<sup>177</sup>. Firstly, it is a mode of raising government revenue and secondly it is regulatory in nature to regulate the trade of certain commodity by imposing higher rate of tax. In India, under the Constitution as originally framed, revenue from the sales tax was reserved to the States<sup>178</sup>, in furtherance of system of taxation introduced by the Government of India Act, 1935<sup>179</sup>. However, the taxing power was subject to

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<sup>177</sup> Shah J, in *State of Madras v. Nataraja Mudaliar*, [1968] 22 STC 376 (SC) at p. 389.

<sup>178</sup> *Constitution of India*, Entry 54, List II, Seventh Schedule originally stands, “tax on sale and purchases of goods other than news paper”, till the amendment carried out by Constitution (Sixth Amendment) Act, 1956.

<sup>179</sup> Government of India Act, 1935, Entry 48 in the Provincial List reserve the levy of tax on sale and purchase within the sphere of Provincial Units. In compliance of the power of taxation in 1938, the Central Province first enacted the Central Provinces and Berar Sales of Motor Spirit and Lubricants Taxation Act, 1938 and Province of Madras enacted Madras General Sales Tax Act, 1939. In view of Article 277 of the Constitution of India, these enactments were continued in force after introduction of Constitution of India. Bengal Finance (Sales Tax) Act, 1941, Bihar Sales Tax Act, 1944 (Replaced by Bihar Sales Tax Act, 1947), Bombay Sales Tax Act, 1946, Assam Sales Tax Act, 1947, Orissa Sales Tax Act, 1947, Central Provinces & Berar Sales Tax Act, 1947, Mysore Sales Tax Act, 1948, Punjab General Sales Tax Act, 1948, Uttar Pradesh Sales Tax Act, 1948 and United State of Travancore & Cochin Sales Tax Act were some of other general sales tax Acts enacted under Entry 48 of the Provincial List.

constitutional restriction under Article 286<sup>180</sup>, then in force, leaving the fields of inter-state sale and export-imports sales out of the State regime. The provision so enacted has

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<sup>180</sup> Constitution of India, Art. 286, as originally enacted, stands as follows,

- (1) No law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of goods where such sale or purchase takes place- (a) outside the State; or (b) in the course of the import of the goods into, or exports of the goods out of, the territory of India.

Explanation.- For the purposes of sub-clause (a), a sale or purchase shall be deemed to have taken place in the State in which the goods have actually been delivered as a direct result of such sale or purchase for the purpose of consumption in that State, notwithstanding the fact that under the general law relating to sale of goods the property in the goods has by reason of such sale or purchase passed in another State.

- (2) Except in so far as Parliament may by law otherwise provide, no law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of any goods where such sale or purchase takes place in the course of inter-State trade or commerce.

Provided that the president may by order direct that any tax on the sale or purchase of goods which was being lawfully levied by the Government of any State immediately before the commencement of this Constitution shall, notwithstanding that imposition of such tax is contrary to the provisions of this clause, continue to be levied until the thirty- first day of March, 1951.

- (3) No law made by the Legislature of a State imposing, or authorising the imposition of, a tax on the sale or purchase of any such goods as have been declared by the Parliament by law to be essential for the life of the community shall have effect unless it has been reserved for the consideration of the President and has received his assent.”

given more advantages to the importing State allowing them to tax on the Inter- State transaction of sale, along with the local tax under its local sales tax law<sup>181</sup>.

But the interpretation of Article 286, in *Bengal Immunity's* case<sup>182</sup> created a constitutional dilemma, as the Court held that in absence of a law made by the Parliament as provided in clause (2) of Article 286, there cannot be a tax on the goods transacted in inter-State sales, either by state where from sales originated or by the State where the commodity is consumed. Resultantly, the sale or purchase occurred in inter- State sale became out of the purview of levy of tax and a serious financial disequilibrium was occurred to provoke the Central Government to take immediate steps for promulgating the Validation Ordinance<sup>183</sup>. Subsequently a comprehensive law<sup>184</sup> covers

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<sup>181</sup> See *State of Bombay v. United Motors (India) Ltd*, [1953] 4 STC 133 (SC).

<sup>182</sup> See *Bengal Immunity Company Ltd v. State of Bihar*, [1955] 6 STC 446 (SC). See also the Judgement in *Ram Narain Sons Ltd v. Asst. Commissioner*, [1955] 6 STC 627 (SC).

<sup>183</sup> To negative the declaration of law in *Bengal Immunity Company Ltd v. State of Bihar*, [1955] 6 STC 446 (SC), the President of India promulgated Ordinance No 3 of 1956. The Ordinance was replaced by the Sales Tax Law Validation Act, 1956 (Act 7 of 1956) enacted by the Parliament of India.

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<sup>184</sup> On the recommendation of Taxation Enquiry Commission, the Parliament amended the Constitution by the Constitution (Sixth Amendment) Act, 1956 by amending entry 54 in State List and introducing entry 92A in the Union List. After amendment of the Seventh Schedule, Entry 54 in the State List reads “taxes on the sale or purchase of goods other than newspapers, subject to provisions of entry 92A of List I”. The entry 92A in the List I reads, “Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce.”

Further Article 269 (1) is also amended to include clause (g) which reads

“269 (1) The following duties and taxes shall be levied and collected by the Government of India but shall be assigned to the States in the manner provided in clause (2), namely, .....(g) taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter- State trade or commerce.”

In Article 286, also substantial amendment was carried out by omitting explanation to clause (1) and making substitution of clause (2) and (3) by new clause. After amendment Article 286 reads as follows,

“286. (1) No law of a State shall impose, or authorise the imposition of, a tax on the sale or purchase of goods where such sale or purchase takes place (a) outside the State; or (b) in the course of the import of the goods into, or export of the goods out of, the territory of India.

(2) Parliament may by law formulate principles of determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1).

(3) Any law of the State shall, in so far as it impose, or authorise the imposition of, a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce, be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify”

the inter-State sales/ purchase and Sales/ purchase in the course of Export or Import, granting the power of levy of tax on inter-State sale to Central Government and assigning the collection to the respective State Governments. As a consequence, in India, the sales tax is a two tier system, by sharing the power to levy of general sales tax by the States and inter- State sales tax by the Union.

To sum up, what ever be the point of levy, who ever be the person administering the tax and where ever be the situs of sale, the incidence of tax is sale, either local sale, inter-state sale or export sale. The introduction of sales tax and the levy is not a contemporary device of revenue collection; however, it has historical hold<sup>185</sup>. It was prevalent in the Olden times, live in the middle Ages and spread swiftly from nation to nation in the first half of the

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Consequently, the Central Sales Tax Act, 1956 was enacted by the Parliament, which is a comprehensive legislation to formulate principles in determining when a sale or purchase of goods takes place in the course of inter-State trade or commerce or outside a State or in the course of import into or export from India with provisions for levy, collection and distribution of taxes and also enumerating the goods to be of special importance in inter-State trade or commerce. See Statement of Objects and Reasons of Central Sales Tax Act, 1956 (Act No. 74 of 1956).

<sup>185</sup> Baijnath Prasad Khaitan, *Evolution of Sales Tax Laws in India*, Pahuja Brothers (1963).

20<sup>th</sup> Century<sup>186</sup>. The machinery of sales tax has today attained enormous proportion under a planned economy and proved to be an effective source of revenue placed in the annual budgetary allocation of the state. Since the State made out it as a potential source of revenue, obviously, legal measures were introduced to define the subject and character of sales tax and to provide the method of levy. On that point of view the extended legal measures inflicted on the concept of sale, irrespective of its traditional notion and significance in commerce and trade, invites a cardinal discussion.

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<sup>186</sup> A. Venkata Rayudu, *Taxation and Economic Development in India: Reference to Sales Taxation in India*, Chugh Publications (1985) at p. 25.

## CHAPTER III

# Evolution of Concept of Sale

A sale is nothing but a contract in between parties, the seller and buyer. Sale is a popular phrase among the business class and tax on sale is a major source of State revenue, being an incident of indirect tax. In the general or literal meaning, sale only means passing of property. However law says, in order to constitute a sale it requires certain significant features. The most essential thing is that there must be an exchange of property for a money price. A sale, in short, is a completed transaction involving transference of interest.<sup>187</sup>

The repealed section 77 of the Indian Contract Act, 1872 defined sale as

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<sup>187</sup> *Bharat Sabaigraaa Ltd v. Collector*, [1952] 3 STC 453 (Orissa) at p. 458.

*“Sale is an exchange of property for a price. It involves a transfer of ownership for the thing sold from the seller to the buyer”.*

Section 4 of the Sale of Goods Act, 1930 defines it, as follows;

*“A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. There may be a contract of sale between one part – owner and another”.*

Section 54 of the Transfer of Property Act, 1882 defines,

*“Sale is a transfer of ownership in exchange of price paid or promised or part paid and part promised.”*

### **3.1. Historical Background**

The concept of sale has its roots in the Roman law<sup>188</sup>. As per the Roman law, a sale, ‘*emptio venditio*’, is

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<sup>188</sup> James Mackintosh, *The Roman Law of Sale*, T. & T. Clark (Great Brittan) (1907) at p. 15.

an agreement by which one person agrees to transfer to another the exclusive possession of something for consideration<sup>189</sup>.

The ancient rules on sale suggest different kinds of sale, such as, sale by numbers, by weight, by measures, according to work, according to beauty and according to splendour. The nature of sale was depending upon the character of article, i.e., an artwork was valued and sold not upon its weight or measurement but upon its beauty.

In ancient ages, different modes of transfer were prevailed. The sale, '*Vikraya*' is defined as the acceptance of a price by the owner preceded by the offering of saleable property.<sup>190</sup> In the olden ages the other recognised modes of transfer was '*Parivartana*', which necessitated transaction by acceptance of one article for another of the same kind, instead of paying its price in gold or money. The exchange of articles of different kinds, '*Vinimaya*' and an exchange of articles with payment of differential value in

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<sup>189</sup> See observations of Sathyanarayana Rao, J. in *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.) at p. 226.

<sup>190</sup> Justice (Rtd.) M. Rama Jois, *Legal and Constitutional History of India*, Universal Law Publishing Co. (2004) at p. 143.

terms of money, 'Avakraya' were other forms of transfer of movables.<sup>191</sup>

The ancient manuscripts prescribe certain principles of sale. Manu cautioned a sale made by non-owner is null and void.<sup>192</sup> A sale by incompetent parties is invalid. A sale by persons, intoxicated or insane or under duress or by a dependent or an idiot is void ab initio.<sup>193</sup> A sale concealing its actual price or a sale by undervaluation cannot said to be a valid sale.<sup>194</sup> Delivery of goods to buyer and receipt of value by the seller are the chief requisites of sale.<sup>195</sup> At the moment the seller receives price of the goods, the sold article belongs to the purchaser<sup>196</sup>. Ownership of the transferor is the deciding factor of the legality of sale and the essential aspect of the ownership under ancient law was the title of the property.<sup>197</sup>

A sale by misrepresenting the facts or if the sale is of

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<sup>191</sup> For detailed discussion see *Vyavahara Nirnaya* at pp. 347 to 348.

<sup>192</sup> *Manu VIII*, 199. See *supra* n. 143.

<sup>193</sup> *Kat* 629. See also in *supra*, n 9 at pp. 78-100.

<sup>194</sup> *Narada* at pp. 144, 145.

<sup>195</sup> *Yajnavalkya II* 254 at p. 256. See *supra* n. 144.

<sup>196</sup> *Ibid.*

<sup>197</sup> *Supra*, n. 190 at p. 145.

defective goods representing it as the sound one gives the buyer the right to return the sale.<sup>198</sup> Such cancellation of sale or recession of sale is subject to return of articles sold within ten days of delivery.<sup>199</sup> However, such period allowed for sales return varies according to the nature of articles.<sup>200</sup> Recession of sale is permitted only on compensatory payment of one sixth of the value of goods.<sup>201</sup> If the purchaser failed to effect the delivery of goods sold, the sale is defective and seller is permitted to make a fresh sale to another<sup>202</sup>.

### **3.2. Trans-national Concept of Sale**

From the beginning of ancient civilised society, the sale and purchase became inevitable parts of life of the mass. The concept of the sale was deeply rooted among the commercial community either in local commerce or in out side. It is to be noted that the importance of trade and expansion of commerce, occasionally, developed

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<sup>198</sup> *Id.* at p 257.

<sup>199</sup> *Manu VIII*, 272. See *supra* n 143.

<sup>200</sup> *Supra*, n. 194 at p 150.

<sup>201</sup> *Supra*, n. 195 at p 258.

<sup>202</sup> *Narada*, pp. 148- 149.

transactions of sale and purchase that crossed international boundaries. In certain aspects, such international extension of commerce had resulted rise and falls of political powers and incarceration of autonomy, commercial and political, over the local masses and traders. The disintegration and collapse of feudal 'Rajas' and the break down of Muslim rule in India and invasion of French, Dutch and English traders in Indian Sub Continent are the best instances of the above observation.

The sale transactions cross the boundaries created diverse legal issues and conceptual difference in the field of commerce. Obviously, the concept of the sale, in transnational out look, is alike. However, an unequal approach was shaped in between the traders of different countries that the obligations and understanding in the country at one end of transaction might be unintelligible to the traders in the other countries. The difference is not on the point of concept, however on the point of standard of conducts and consequences. Such a dilemma was removed; in a limited extend, by introducing Uniform Laws on the International

Sales<sup>203</sup>. The Vienna Conference in 1980<sup>204</sup> took remarkable steps to eliminate the divergence among the international traders.<sup>205</sup>

### **3.3. Legal Control on Sale.**

Sale is one of the forms of special contract. The special features for a normal contract are highly essential for a valid sale. In India, the concept of sale is closely connected with the commercial transactions. Sale may relate to immovable property or movables. The legislations regulating the commercial contract of sale are subject to the constitutional limitations. The subject of contract is a

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<sup>203</sup> In the year 1964, a diplomatic conference attended by 28 nations at Hague, signed and adopted two international documents on uniform governing contracts for the sale of goods entered into between parties whose place of business or habitual residence are in the territories of different contracting states. These documents were named as *Uniform Law on International Sale of Goods* (ULIS) and *Uniform Law on the Formation of Contracts for the International Sale of Goods* (ULFIS).

<sup>204</sup> The United Nations Commission on International Trade Laws formulated a draft contract for the international sales of goods and the same was adopted at the United Nations Conference on the Contracts of International Sale of Goods held at Vienna in 1980.

<sup>205</sup> Dicey, Morris & Collins, *The Conflicts of Laws*, 14<sup>th</sup> edn, Sweet & Maxwell (London) (2007) at paras 33-123.

concurrent subject<sup>206</sup>. The transfer of property except the agricultural land falls also in the concurrent list.<sup>207</sup> Hence the legal or regulatory field regarding sale is purely in a concurrent field on which both the Parliament and the State Legislatures are empowered to make laws.

The regulatory measures on the Sale of immovable properties<sup>208</sup> are solely covered by the Transfer of Property Act<sup>209</sup>. On the other hand, the Sale of Goods Act lays down special rules of law which are peculiar to the sale of movables in the form of goods. In India the Indian Contract Act enacted in 1872 provided lengthy provisions<sup>210</sup> regarding the sale of goods. However, in 1930 a special

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<sup>206</sup> *Constitution of India*, Seventh Schedule, List III, Entry 7, reads, “Contracts, including partnership, agency, contracts of carriage, and other special forms of contracts, but not including the contracts relating to agricultural land”.

<sup>207</sup> *Constitution of India*, Seventh Schedule, List III, Entry 6, reads, “Transfer of property other than agricultural land; registration of deeds and documents”.

<sup>208</sup> Sec. 3 (26) of the General Clause Act defines immovable property, which reads, “‘Immovable property’ shall include land, benefits to arise out of land and things attached to the earth, or permanently fastened to anything attached to the earth”.

<sup>209</sup> The preamble of the T P Act, 1882, states, “Whereas it is expedient to define and amend certain parts of the law relating to the transfer of property by act of parties...”

<sup>210</sup> Ss. 76 to 123 of the Contract Act, 1872 are repealed by Act 1 of 1930.

enactment to define and amend the law relating to sale of goods was enacted, which came in to force on the 1<sup>st</sup> day of July 1930<sup>211</sup>. Though the provisions of the Indian Contract Act, 1872 were replaced by a special enactment on the sale of goods, yet, the contracts on sale of goods are subject to the provisions of Indian Contract Act<sup>212</sup>.

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<sup>211</sup> The Central Legislature passed the Indian Sale of Goods Act, 1930 and the Governor General gave assent for the same on 15th March 1930. Later the Indian Sale of Goods (Amendment) Act 1963, Act 33 of 1963, repealed the word 'Indian' from the title of the Act with effect from 22nd September 1963.

<sup>212</sup> The Sale of Goods Act, 1930, Section 66, reads,

**66. Savings.** - (1) Nothing in this Act or in any repeal effected thereby shall affect or be deemed to affect-

- (a) Any right, title, interest, obligation or liability already acquired, accrued or incurred before the commencement of this Act, or
  - (b) Any legal proceedings or remedy in respect of any such right, title, interest, obligation or liability, or
  - (c) Anything done or suffered before the commencement of this Act, or
  - (d) Any enactment relating to the sale of goods which is not expressly repealed by this Act, or
  - (e) Any rule of law not inconsistent with this Act.
- (2) The rules of insolvency relating to contracts for the sale of goods shall continue to apply thereto, notwithstanding anything contained in this Act.
- (3) The provisions of this Act relating to contracts of sale do not apply to any transaction in the form of a contract of sale, which is intended to operate by way of mortgage, pledge, charge or other security.

The basic rules of the laws on sale of goods were evolved by the English/Common Law Courts, subject to the modifications by the Court of Equity. Additionally, the Statute of Frauds in 1677, required certain principles to be followed in the cases of execution of contracts relates to sale of goods<sup>213</sup>. The Factors Act, 1889 also deals with some basic principles on the sale of goods. Equally in United States, Uniform Commercial Code is enacted for regulating the field of sale of goods.

### **3.4. Pre-requisites of Sale.**

A sale ordinarily takes place where the goods are by mutual agreement appropriated towards the contract<sup>214</sup>. There must be a transfer of property or an agreement to transfer it, from one party, the seller, to the other, the buyer, in consideration of a money payment or a promise thereof by the buyer<sup>215</sup>. In a sale as a result of transaction, which requires an agreement between parties, having capacity to

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<sup>213</sup> *Benjamin's Sale of Goods*, 7<sup>th</sup> edn, Sweet & Maxwell (London), The Common Law Library (United Kingdom) at para 1-9.

<sup>214</sup> *Anwarkhan Mehboob Co. v. Commissioner of Sales Tax*, AIR 1970 SC 1756.

<sup>215</sup> *Madholal Sindhu of Bombay v. Official Assignee of Bombay*, AIR 1950 FC 21.

contract, for the purpose of transferring the title to goods and supported by money consideration, the property must actually pass in the goods<sup>216</sup>.

In *Benjamin's Sale of Goods*<sup>217</sup>, the general law on sale is elaborated and the author suggested that in order to constitute a sale there must be an agreement to sell, by which alone property does not pass and an actual sale by which the property passes. An act of sale is in par with the contract for which certain qualifications are necessary such as competency of parties, mutual assent, a thing, the absolute or general property in which is transferred from the seller to the buyer and a price in money paid or promised<sup>218</sup>. The Supreme Court endorsed this view in *Poppatlal Shah v. State of Madras*<sup>219</sup> by considering the composite expression of sale of goods.

An agreement is required, to constitute a sale, in between at least two parties, a buyer and a seller. The

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<sup>216</sup> *State of Madras v. Gannon Dunkerley & Co Ltd.*, AIR 1958 SC 560.

<sup>217</sup> *Benjamin's Sale of Goods*, 8<sup>th</sup> edn, Sweet & Maxwell (London), The Common Law Library (United Kingdom) at p. 1.

<sup>218</sup> John Barker Waite, *The Law of Sales*, Callaghan & Co. (1921).

<sup>219</sup> *Poppatlal Shah v. State of Madras*, [1953] 4 STC 188 (SC) at p. 193.

buyer and seller must be different parties as there must be a complete exchange of property to constitute a sale. A person is disabled from making a contract with himself<sup>220</sup>.

An agreement may be express or implied, either in writing or in oral. However it must be enforceable by law. However the mere agreement to sell is some thing different from the real sale. Sale creates a *jus in rem* while a contract to sell is *jus ad rem*<sup>221</sup>.

An agreement to sale ripens into sale when the stipulated time elapses or conditions are fulfilled subject to which the property in the goods is to be transferred<sup>222</sup>.

A money consideration is one of the pre requisite to constitute a sale. The price is the consideration. For sale it is necessary that the price should be settled for, without price, there can be no purchase or sale and it ought to be

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<sup>220</sup> *Tarsem Singh v. Sukminder Singh*, AIR 1998 SC 1400 at para 12. Also see *Commissioner of Income Tax v. Hind Constructions Ltd*, 1972 (4) SCC 460.

<sup>221</sup> Manindra Nath Das, *B.B. Mitra on the Transfer of Property Act*, 1882, 14th edn., Eastern Law House, Calcutta (1982) at p. 303.

<sup>222</sup> *Tobacco Manufactures (India) Ltd. v. State of Bihar*, [1951] 1 STC 282 (Patna) at p. 293.

fixed and certain<sup>223</sup>. The price is an essential ingredient and that where it is neither ascertained nor rendered ascertainable; the sale is void for incompleteness and incapable of enforcement<sup>224</sup>. However there is no inevitable rule that price must be fixed<sup>225</sup>. The sale varies from an exchange that in a sale the price is paid in money<sup>226</sup>, whilst in an exchange it is paid for some thing other than money<sup>227</sup> or in goods, commonly known as barter.

In *Gannon Dunkerley's case*<sup>228</sup>, Venkitarama Ayyar, J of the Hon'ble Supreme Court observed that if merely title of goods passed but not because of any contract between the parties, express or implied, there is no sale. If the consideration for the transfer is not money but other

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<sup>223</sup> *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.) at p. 226.

<sup>224</sup> *Ram Sunder v. Kali Narain*, AIR 1927 Cal 889 at p. 893.

<sup>225</sup> *Kurapati Venkata Mallayya & Another v. Jhondepu Ramaswami Co & another*, AIR 1964 SC 818.

<sup>226</sup> *Ghulam Abbas v. Razia Begum*, AIR 1951 All 86 (FB).

<sup>227</sup> *Commissioner of Income Tax V. Motors and General Stores Ltd.* AIR 1968 SC 200.

<sup>228</sup> *State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd*, AIR 1958 SC 560.

valuable consideration, it may not be a sale, but may be exchange or barter. If under the contract of sale, title of the goods has not passed, then there is an agreement to sell only not a completed sale.

If other conditions in a sale are satisfied the mere non payment of purchase money does not prevent the passing of title of the property sold.<sup>229</sup> If the intention is that the title should pass immediately even though the consideration has not been paid, the title passes, except when there is an agreement that it should take effect only if the consideration is first paid. In a sale, it is seldom the intention of the parties to allow title to pass without the receipt of consideration and the intention can be gathered from the transfer document<sup>230</sup>.

An immediate transfer or agreement to transfer is another requisite for a sale. Where a property in the goods is passed immediately, the sale is completed. However if the contract contemplates that the property in the goods would pass on a future date or on the happening of some

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<sup>229</sup> *Gurubari Lnka v. Dulani Thakurani*, AIR 1971 Orissa. 147.

<sup>230</sup> *Shiba Prasad v. Upendra*, AIR 1935 Pat. 45.

contingencies it would become sale when the contingencies happens or the condition is fulfilled. The agreement so entered may be express or implied regarding the passing of title of goods. The agreement and the sale should relate to the same subject matter<sup>231</sup>. A transaction to be regarded as a sale there must be transfer of property in the goods. Where the goods are merely ordered but delivery is not given or taken and there is nothing from which it can be ascertained that the property in the goods has actually been transferred from, one party to another it cannot be said that there is a sale<sup>232</sup>.

The two ingredients of the sale that is the passing of property and the payment of consideration need not take place at an instance. Payment of consideration can be postponed or even adjust in different modes. When the awarder of a contract himself make available to the contractor, the materials of the contract and subsequently adjusted the price of the materials from the disbursement of

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<sup>231</sup> *State of Gujarat v. M/s Variety Body Builders*, AIR 1976 SC 2108 at p. 2112.

<sup>232</sup> *Punamchand v. State*, [1951] 2 STC 14 (Nag.).

the total award amount, there is a sale, though there is no passing of consideration in money but adjustment of price of materials, when the final bills are settled<sup>233</sup>.

The capacity of the parties to enter in a contract is an essential ingredient to compose a sale. Though the Sale of Goods Act is silent about the specific requirements to constitute the capacity of the parties, the general law is squarely applicable in this filed<sup>234</sup>. The general law on contract is very specific that debars a contract of minor or a person of unsound mind.

A capacity to enter in a sale or purchase is not inherent but subject to the legal barriers under the general law on contract and transfer and acquires property<sup>235</sup>. Of

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<sup>233</sup> *Karya Palak Engineer, CPWD v. Rajasthan Taxation Board*, 2004 (7) SCC 195; [2004] 136 STC 641 (SC).

<sup>234</sup> *Supra*, n. 212.

<sup>235</sup> Section 2 of the Sale of Goods Act, 1893 (England), reads,

2. **Capacity to buy and sell.** - Capacity to buy and sell is regulated by the general law concerning capacity to contract, and to transfer and acquire property.

Provided that where necessaries are sold and delivered to an infant, or minor, or to a person who by reason of mental incapacity or drunkenness is incompetent to contract, he must pay a reasonable price therefore.

course, it is also subject to the exemptions like 'necessaries'<sup>236</sup> and 'reasonable pricing'.

Mutual Assent is another constituent element of a sale transaction. For formation of a valid contract, there shall be two or more persons who give consent so as they agree on the same thing in the same sense<sup>237</sup>. The Hon'ble Supreme Court of India<sup>238</sup> held that a sale predicates a contract of sale of goods between persons competent to

Necessaries in this section mean goods suitable to the condition in life of such infant or minor or other person, and to his actual requirements at the time of the sale and delivery.

<sup>236</sup> English Law says if necessaries, means goods suitable to the conditions in life, sold and delivered to a minor the sale are not barred, as a minor is incompetent to enter into contract. See section 3 of the Sale of Goods Act, 1979 (England).

**3. Capacity to buy and sell.** - (1) Capacity to buy and sell is regulated by the general law concerning capacity to contract and to transfer and acquire property.

(2) Where necessaries are sold and delivered to a minor or to a person who by reason of mental incapacity or drunkenness is incompetent to contract, he must pay a reasonable price for them.

(3) In subsection (2) above 'necessaries' means goods suitable to the condition in life of the minor or other person concerned and to his actual requirements at the time of the sale and delivery.

<sup>237</sup> Contract Act, 1872, Section 13, reads as follows,

**13. Consent defined.** -Two or more persons are said to consent when they agree upon the same thing in the same sense.

<sup>238</sup> *Chittar Mal Narain Das v. Commissioner of Sales Tax*, [1970] 26 STC 344 (SC).

contract for a price paid or promised; it does not involve an obligation to enter in to a contract, which cannot be called a sale. A compulsory acquisition of goods in view of Levy Order, where in the violation results penal provisions, does not envisage any consensual arrangement and amounts to no sale. Unless the element of mutual assent, implicit or explicit, is in existence there is no freedom of contract<sup>239</sup> and the transaction cannot be termed as sale in its strict sense<sup>240</sup>.

The consensual relation is connoted by the word 'sale' and even the parties to a sale, entered in to an agreement, on the basis of some mistakes of facts, such agreements does not form a valid sale in view of the provisions of Contract Act, 1872<sup>241</sup>. Lord Toker in House of Lords opined that the contract or agreement to sell may

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<sup>239</sup> *Salar Jung Sugar Mills Ltd v. State of Mysore*, [1972] 29 STC 246 (SC).

<sup>240</sup> *Food Corporation of India v. State of Punjab*, [1976] 38 STC 144.

<sup>241</sup> The Indian Contract Act, 1872, Section 20, reads as follows,

**20. Agreement void where both parties are under mistake as to matter of fact.** - Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void.

**Explanation.** -An erroneous opinion as to the value of the thing, which forms the subject matter of the agreement, is not to be deemed a mistake as to a matter of fact.

precede the formal instrument or act of delivery under which the property passes, but to describe a transfer of property in a chattel, which takes place without the consent of transferor and transferee as a sale would seem to be a misuse of language<sup>242</sup>. Consensus of mind, being one of the major requirements to fulfil a contractual obligation, warrants consensus regarding the identity of goods under the transaction also. In a sale the buyer and seller must be quite clear about the identity of the goods in question and there should not be any ambiguity whatsoever on it<sup>243</sup>.

Element of bargaining is another essential to constitute a sale<sup>244</sup>. House of Lords in *Kirkness v. John Hudson & Co*<sup>245</sup> ruled out the possibility of a valid sale in compulsory transaction and held that mere transfer of property will not constitute actual sale in the event of want of bargaining on conditions of sale. The House of Lords declined to accept the contention of the Revenue that the word "sale" has a wider meaning than a contract and a

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<sup>242</sup> *Kirkness v. John Hudson & Co*, [1955] AC 696.

<sup>243</sup> *Provincial Automobile Co. Ltd v. State*, [1952] 3 STC 147 (MP).

<sup>244</sup> See *Graff v. Evans*, 8 Q.B.D. 373 in [1952] 3 STC 77 at p. 88.

<sup>245</sup> *Supra*, n. 242.

conveyance of property. The Revenue argued that in its legal meaning it did not involve a contract at all but just the transfer of property in or ownership of something for a money price and whether it is voluntary, effected by operation of law, or compulsory is immaterial. In common law a sale of personal property is usually termed a 'bargain' and 'sale of goods' and the bargain is a necessary element in sale<sup>246</sup>. By referring the observations of Venkitarama Ayyar, J in *Gannon Dunkerley's case*<sup>247</sup>, Mr. Shah, J in *New India Sugar Mill's case*<sup>248</sup> pointed out that in the scheme of Indian Contract Act, 1872, from section 1 to 75, bargain is an essential element to constitute a contract and even after the introduction of Indian Sale of Goods Act, 1930 that position had not been changed.

An action of transfer of title and ownership are specifically incorporated in the designation of sale. Whether an action of transfer is limited to the transfer of ownership

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<sup>246</sup> Cheshire, *Modern Law of Real Property*, 7<sup>th</sup> edn. (1972) at p. 631.

<sup>247</sup> *State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd*, AIR 1958 SC 560.

<sup>248</sup> *New India Sugar Mills Ltd. v. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC) at p. 350.

by way of transfer of title or along with a transfer of possession, which constitute the delivery of the sold goods, is a debatable issue. A mere transfer of goods by the owner from one place to another does not amount to sale<sup>249</sup>. A person who has no complete title to the goods transferred cannot be said to have made a sale to another person<sup>250</sup>. In a sale, the seller has to cease the ownership of the goods<sup>251</sup>.

In sales tax law, the situs of transaction is a relevant factor to decide the taxability of sale. When the parties to a sale contract are present in a particular place and executed the contract with an undertaking to deliver the goods also made in the place wherein the contract of sale executed, needless to say, the situs of sale is the place wherein the contract of sale was executed, as the sale must be deemed to have taken place in that place<sup>252</sup>.

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<sup>249</sup> *Food Corporation of India v. State of Punjab*, [1976] 38 STC 144 (P&H).

<sup>250</sup> *ONGC v. State Of Bihar*, [1976] 38 STC 435 (SC).

<sup>251</sup> *Marikar Motors Ltd v. Sales Tax Officer*, [1967] 19 STC 18 (SC).

<sup>252</sup> *Vakkan v. Government of the Province of Madras*, [1952] 3 STC 204 (Mad.).

This view was settled by the Privy Council in a catena of decision, particularly in *Lovell & Christmas Ltd. v. Commissioner of Taxes*<sup>253</sup>, in which it was held that the trade or business in question in cases ordinarily consists in making certain classes of contracts and in carrying those contracts into operation with a view to profit; and the rule seems to be that where such contracts, forming as they do the essence of the business or trade, are habitually made, there a trade or business is carried

However to constitute a sale for the purpose of taxation it is not necessary that all the ingredients of sale should be at a place or within the territory of the same taxing state<sup>254</sup>. The doctrine of nexus was extended to sales tax legislation<sup>255</sup> If there is sufficient nexus between the Province and taxable event, the sale, by fiction, the Province can assume completion of sale in that Province for the purpose of levy of sales tax.

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<sup>253</sup> [1908] AC 46 PC.

<sup>254</sup> *State of Bombay v. The United Motors*, [1953] 4 STC 133.

<sup>255</sup> See *Wallace Brothers & Co. v. Commissioner of Income Tax*, 16 ITR 240 (PC): AIR 1948 PC 118

The object of Sales Tax Acts in India is to impose a tax on all sales and it is a tax imposed on the occasion of sale. The term sale has the intricate meaning in its legal sense and ordinary meaning in its popular sense. In the legal sense, it imports passing of property in the goods and in its popular sense it signifies the transaction which results in the passing of property<sup>256</sup>. It is a never-ending enquiry as to whether a wider meaning is possible to the term sale? According to Lord Reid<sup>257</sup>, sale is a word, which has become capable in an appropriate context of having a meaning wider than its ordinary and correct meaning. But it is only permissible to give to a word some meaning other than its ordinary meaning if the context so requires.

According to Venkitarama Ayyar, J, while interpreting a Constitution, a liberal spirit should inspire the courts and the widest amplitude must be given to legislative entries and they should not be cut down by resort to legislative practice and the subjects of taxation in particular should be

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<sup>256</sup> Venkitarama Ayyar, J in *Poppatlal v. State of Madras*, [1952] 3 STC 396 (Mad.) at p. 399.

<sup>257</sup> See *Kirkness v. John Hudson & Co.*, [1955] AC 696.

taken in *rerum natura* irrespective of previous laws on the subject<sup>258</sup>. Sale is judicially defined as transfer of property in a thing from one person to another for a money price<sup>259</sup>. It was pointed in *Gannon Dunkerley's case*<sup>260</sup> that even in popular sense a sale is said to take place when the bargain is settled between the parties, though property in the goods may not pass at that stage.

On a comparison, in an Australian case<sup>261</sup>, it was held that the meaning of sale in a fiscal statute should not be construed in the light of general law, Sale of Goods Act, but in a commercial and business sense.

A sale is concluded in a commercial shop, when the buyer selects the goods, takes delivery or collects the goods by paying the price of the goods. Is it a valid objection that there is no sale when a seller display the goods in a super store, without offering the same to buyers, but the buyer takes the goods and leave the shop? In fact

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<sup>258</sup> *State of Madras v. Gannon Dunkerley*, [1958] 9 STC 353 (SC).

<sup>259</sup> *Ibid.*

<sup>260</sup> *Ibid.*

<sup>261</sup> *Nevile Reid & Co. Ltd v. Commissioner of Inland Revenue*, [1922] 12 Tax Case. 545.

as held in the English case<sup>262</sup>, even if the seller does not offer the goods for sale in his shop, but merely invites offer to buy, the sale is complete at the cashier's desk when the goods are paid for.

In the beginning period of taxation in India, among the textual interpretations on the basis of the Sale of Goods Act and different Sales Tax Statutes, the usual view was that the term 'sale' is used in the respective statutes, in its limited sense, in terms of the provisions of the general law of contract, which was subsequently incorporated in the Sale of Goods Act, 1930<sup>263</sup>.

Can a sale be understood in its restricted meaning as in the general law or in its widest possible meaning or extended meaning as in the taxing statutes? The debates on the scope of 'sale' in the taxing statutes and general laws of contract are still a dynamic one. The parameters of this special type of contract are unsettled even after the deliberations in the last eight decades.

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<sup>262</sup> *Pharmaceutical Society of Great Britain v. Boots Cash Chemists Ltd*, [1953] 1 QB 401.

<sup>263</sup> *New India Sugar Mills Ltd. v. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC) at p. 352.

## CHAPTER IV

# **“Sale and Deemed Sale”: Unique Problems in Interpretation**

A sale is a consensual transaction. It has a trans-national recognition in international law. It has a traditional and historical meaning recognised by the commercial community. On the other hand, the term sale is well defined under the statutes explicitly.

A transaction which does not conform to the traditional concept of sale cannot be regarded as one subject to taxation under sales tax<sup>264</sup>. The word ‘sale’ should be construed in a popular sense as the transaction of sale irrespective of a mere passing of property<sup>265</sup>.

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<sup>264</sup> *Bhopal Sugar Industries Ltd. v. D.P. Dube*, [1963] 14 STC 406 (SC) at p. 408.

<sup>265</sup> *Poppatlal Shah v. The State of Madras*, [1952] 3 STC 396 (Mad.).

#### **4.1. Restricted Meaning of Sale- Nature and Essence of Transaction.**

It was the traditional outlook in the interpretation of the concept that sale has its restricted connotations and not in otherwise. The essential perception necessary to understand the traditional notion of sale is based on the requirements of an ordinary contract, as covered by the provisions of the general laws on contract.

#### **4.2. Need for Concurrence of Different Elements.**

To constitute a valid sale, there must be a concurrence of the different elements<sup>266</sup>, such as, competent parties, mutual assent among them, a thing, the absolute or general property in which is transferred from the seller to the buyer and money consideration paid or

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<sup>266</sup> *Poppatlal Shah v. State of Madras*, [1953] 4 STC 188 (SC) at para 7: AIR 1953 SC 274. The Constitutional Bench of the Supreme Court per B.K. Mukherja, J., held “The expression sale of goods is a composite expression consisting of various ingredients or elements that are a bargain or contract of sale, the payment or promise of payment of price, the delivery of goods and the actual passing of title, and each one of them is to a transaction of sale though the sale is not completed or concluded unless the purchaser becomes the owner of the property.”

promised<sup>267</sup>. Different statutes on the subject also confirm these requirements. In common law<sup>268</sup> a contract of sale of

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<sup>267</sup> *Benjamin's Sale of Goods*, 8th edn., Sweet & Maxwell, The Common Law Library (United Kingdom) at p. 2.

<sup>268</sup> Mackenzie Dalzell Edwin Stewart Chalmers, *The Sale of Goods Act, 1893: Including the Factors Acts, 1889 & 1890*, William Clowes & Sons, (1899).

The Sale of Goods Act, 1893 [England], Section 1 reads as follows,

- 1. Sale and agreement to sell.** -- (1) a contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a money consideration, called the price. There may be a contract of sale between one part owner and another.
- (2) A contract of sale may be absolute or conditional.
- (3) Where under a contract of sale the property in the goods is transferred from the seller to the buyer the contract is called a sale; but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled the contract is called an agreement to sell.
- (4) An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

The Act, 1893 was replaced in the year, 1979, by the Sale of Goods Act, 1979, and the new Act replaced the provisions of Old Act, 1893 and Section 2 of Act, 1979, reads as follows,

- 2.** (1) a contract of sale of goods is a contract by which the seller transfers or agrees to transfer the property in goods to the buyer for a money consideration, called the price.
- (2) There may a contract of sale between one part owner and another.
- (3) A contract of sale may be absolute or conditional.
- (4) Where under a contract of sale the property in the goods is transferred from the seller to the buyer the contact is called a sale.

goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for money consideration, called the price. There may be a contract of sale between one party and another. A contract of sale may be conditional or absolute. Where under a contract of sale the property in the goods is transferred from the seller to the buyer the contract is called a sale; but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell. An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred. Apparently, the law in India is analogous to that of the common law.

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(5) Where under a contract of sale the transfer of the property in the goods is to take place at a future time or subject to some condition later to be fulfilled the contract is called an agreement to sell.

(2) An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

### **4.3. Mutual Assent as an Essential Element.**

A sale is said to be made out of a contract<sup>269</sup>. It is an executed contract that is a contract plus a conveyance<sup>270</sup>. That contract may be oral or writing. Even from the conduct of the parties, a sale contract may be inferred. Nevertheless, the contract originates in an offer and corresponding acceptance<sup>271</sup>. The word sale, in its traditional meaning is not co-extensive with the expression of contract of sale as the contract of sale is a wider circle, which includes the sale and the agreement to sale<sup>272</sup>. A sale is by a transfer of property in goods, but in other the transfer is to take place in future subject to the conditions or not<sup>273</sup>.

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<sup>269</sup> *Calcutta C.S.O. & D Association Ltd. v. State of West Bengal* [1974] 34 STC 161 (Cal.)

<sup>270</sup> *Budh Prakash v. Sales Tax Officer*, [1952] 3 STC 185 at p. 191 (All.).

<sup>271</sup> *ARG Krishnamurthi & Co. v. Ramanujan*, AIR 1961 Andhra 408.

<sup>272</sup> *Tobacco Manufacturers (India) Ltd. v. State of Bihar*, [1951] 1 STC 282 (Patna) at p. 292.

<sup>273</sup> *Id.* at p.291.

#### **4.4. Nature of Transaction: Transfer of Rights.**

The essence of transfer<sup>274</sup> is passage of control over the economic benefits of property that results in terminating rights and other relations in one entity and creating them in another<sup>275</sup>. In its real sense, it is the transfer of rights of the owner, namely the right to possess, right to use and enjoy, right to usufruct, right to consume, right to dispossess by destruction, alienation etc. The Court has held that an act of sale is merely the means for putting the goods in the way of use or consumption<sup>276</sup>.

A mere nomenclature or description of the transaction a sale will not be conclusive<sup>277</sup>. Mere language of a contract cannot by itself make the transaction of goods a sale, if it is not one of sale in its nature and essence.

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<sup>274</sup> P.J. Fitzgerald, *Salmond on Jurisprudence*, 12<sup>th</sup> edn, Sweet & Maxwell (London) (1966) at p. 332 transfer is explained as follows: The common use of the word transfer is to denote the passing of title in property, or an interest therein, from one person to another, and in this sense the term means that the owner of property delivers it to another person with the intent of passing the rights which he had in it to the latter.

<sup>275</sup> *Corpus Juris Secundum*, Vol. 87, West Publishing (1997) at p. 892.

<sup>276</sup> *Burmah Shell Oil Storage & Distributing Co v. Belgaum Borough Municipality*, [1963] Supp. 2 SCR 216.

<sup>277</sup> *Sokkallal Ramasait Factory Pvt. Ltd v. Dy. CTO*, [1967] 20 STC 419 (Mad.).

That means the sale has its own special features and all contract for transfer of goods cannot be said to be a sale. But all sales are originated from a contract, either oral or written and implied or expressed. In determining the question whether a transaction is a sale or any other transfer, the real nature and essence of the transaction as a whole is to be considered<sup>278</sup>.

#### **4.5. Competent Parties: Natural or Artificial Persons**

Sale effected in between incapable parties amounts to invalid sale, even if it satisfies all other requirements of sale. A sale is a bilateral transfer divesting the ownership of the goods sold from the original owner to the other person. Any person, whether natural or artificial, can effect the sale subject to the rule of ultra virus. However, the sale by a human being is subject to the rule of majority and sound mind.<sup>279</sup>

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<sup>278</sup> *Central Finance and Housing Co. v. British Transport Co.*, AIR 1954 All. 195.

<sup>279</sup> The Indian Contract Act, 1872, Section 11, reads as follows,

The formal description of the parties in the contract, as buyer and seller is not a conclusive evidence to declare the transaction as sale<sup>280</sup>. The true relationship of the parties has to be gathered from the nature of the contract, its terms and conditions. The mere terminology used by the parties is not decisive of the said relationship<sup>281</sup>.

Transfer effected by agents or representatives are not sale, if the capacity of such persons fall beyond the limits of the authority. A sale by a minor is absolute nullity and a subsequent ratification after attaining majority would not upshot the nullity. However transfer of goods by a natural or de jure guardian of a minor, on behalf of him, for the legal necessity or for the benefit of the estate, constitute valid sale. A sale by a person in a state of unsound mind or too drunk is not a sale until he ratify the sale after become sound or sober.

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**Who are competent to contract:** - Every person is competent to contract who is of the age of majority according to the law to which he is subject', and who is of sound mind and is not disqualified from contracting by any law to which he is subject.

<sup>280</sup> *Bhopal Sugar Industries Ltd v. Sales Tax Officer*, [1977] 40 STC 42 (SC).

<sup>281</sup> *Sri Tirumala Venkateswara Timber & Bamboo Firm v. Commercial Tax Officer*, [1968] 21 STC 312 (SC).

The law suggests such incapacity to prevent abuse of process that in the case of minors the mind is immature and the person in unsound mind and a drunkard lacks to know what he is about in such a nature that their judgment is defective and more or less incapable of forming an accurate judgement or conclusion on matters which intimately concern their interests.

#### **4.6. Passing of Property: An Essential Element.**

Passing of property is an essential to compose a sale. Until and unless the property in the goods has been transferred from the seller to the buyer, there is no sale<sup>282</sup>. The question of passing of property is normally a question of intention and the intention of the parties must be gathered from the terms of sale contract<sup>283</sup>. In absence of

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<sup>282</sup> *Great India Rice and Oil Mills v. State of Bihar*, AIR 1957 Pat. 178.

<sup>283</sup> The Sale of Goods Act, 1930, Section 19, reads as follows,

**Property passes when intended to pass.** - (1) Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.

(2) For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.

specific provision in the contract about passing of property from the seller to buyer, the inference has to be drawn from conduct of the parties<sup>284</sup>. Mere despatch of goods by manufacturer to his own branches out side the State does not amount to sale.<sup>285</sup>

In *Rohtas Industries Ltd. v. State of Bihar*<sup>286</sup>, the Supreme Court held, for considering whether particular transaction was sale or not, what had to be considered was whether as a result of transaction, the property in the goods passed in return for a price coupled with the title of goods to the transferee. A mere passing of order for certain pamphlets from a printing press, without effecting the delivery to customer does not constitute sale, as there was no passing of property<sup>287</sup>.

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(3) Unless a different intention appears, the rules contained in Sections 20 to 24 are rules for ascertaining the intention of the parties as to the time at which the property in the goods is to pass to the buyer.

<sup>284</sup> *Hindustan Malleablas Forgings Ltd. v. Indian Furnace Co. Ltd*, AIR 1979 Pat. 146 at p. 150.

<sup>285</sup> *Goodyear India Ltd v. State of Haryana*, [1990] 76 STC 71 (SC).

<sup>286</sup> [1961] 12 STC 615 (SC).

<sup>287</sup> *Punamchand v. The State*, [1951] 2 STC 14 (Nag.) at p. 16.

A machine ordered as per the contract of sale and could not complete the delivery of machine due to the halt of the purchaser company and in such circumstances, the Privy Council held that there is no sale and exigibility of tax does not arise<sup>288</sup>. In case of a forward contract, being an agreement to sell cannot be brought within the ambit of tax on sales, as there is no completed sale. The sales tax is a levy on the price of the goods and the reason of the thing requires that such a levy should not be made, unless the stage has been reached when the seller can recover the price under the contract<sup>289</sup>.

In a contract for building construction, there are supplies of materials embedded in a building. Can it be said the contractor had an intention to sell those materials essential for construction of the building as bricks, doors, windows, cement, steels etc. In actual fact if sale of material is deemed to have taken place, it would invariably take place earlier when he builds the walls, roof, etc. and

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<sup>288</sup> *The King v. Dominion Engineering Co. Ltd*, [1952] 2 STC 67 (PC).

<sup>289</sup> *Sales Tax Officer v. M/s Budh Prakash Jai Prakash*, [1954] 5 STC 193 (SC) at p. 197.

even before the building is constructed. Until the building materials are actually fixed to the building, in the absence of an agreement to pass the property in the materials on delivery, the property therein remains in law in the builder, notwithstanding that they may have been brought on the site.

In *Jubilee Engineering Co.Ltd v. Sales Tax Officer*<sup>290</sup>, the Supreme Court held that if in the discharge of a contract of service, ownership of goods passes which is inseparably integrated with the contract of service, and the transaction is not a sale, though the finished product may be subject matter of a sale.

When the contractor, in advance, brought the materials for construction to the work site to satisfy the contractee with regards to the quality of the materials used in the contract, merely because of such an act on the part of the contractee, there cannot be a presumption of the sale, unless there is actual sale of materials to the customer. The act of approbation by the contractee is

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<sup>290</sup> [1956] 7 STC 423 (SC).

sufficient to constitute an acceptance of the materials brought before him, but that approbation is not given *eo animo* at all<sup>291</sup>. The purpose is only to ascertain that they are such materials as are suitable for the purpose.

However if the contracts include sale of goods in explicit terms, the levy of tax on the sale of materials is justified and if on the other hand the contract is only for a works contract with no element of sale of goods, as described in the general law on sales of goods, it would not be taxable under the Sales Tax Laws<sup>292</sup>.

A contract purely for the supply of labour and work is not a contract of sale of goods, as labour and work cannot be deemed to be goods in any sense of the term. In the case of a chattel, it has to be produced by the labour and work of the contractor and also by the supply of the necessary materials for finishing the work. When the material is fixed to the corpus by the contractor, the property

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<sup>291</sup> See *Tripp v. Armitage*, [1839] 4 M & W 687, cited by Venkitarama Ayyar, J, in *Firm of M/s Peare Lal Hari Singh v. State of Punjab*, [1958] 9 STC 412 (SC) at p. 416.

<sup>292</sup> *Sundaram Motors (P) Ltd v. State of Madras*, [1958] 9 STC 687.

passes when the property in the larger corpus itself passes to the contractee<sup>293</sup>.

When the thing to be produced under the contract is a movable property then any material incorporated into it might pass as a movable, and in such a case the conclusion that no taxable sale will result from the disintegration of the contract can be rested only on the ground that there was no agreement to sell the materials as such<sup>294</sup>.

While a contractor execute a contract of construction of building, it is usual to buy and use materials for construction. When the provision of the contract stipulates “all stores and materials brought to the site shall become and remain the property of the contractee and shall not be removed off the site without the prior approval of the contractee or his agent”, an apparent argument was raised that vesting the material with the contractee, it shall be presumed that the materials so brought in the site must be taken to have been sold to the contractee. The Hon’ble

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<sup>293</sup> *Gannon Dunkerley v. State of Madras*, [1954] 5 STC 216 (Mad.)

<sup>294</sup> *State of Madras v. Gannon Dunkerley*, [1958] 9 STC 353 (SC) at p. 386.

Supreme Court in such circumstances brushed aside such an argument and held that even if such stipulation is there to ensure that the materials of the right sort are used in the construction and the intention is not to sale the materials to the contractee. It was held that a lump sum contract for construction of building cannot be a contract for the sale of materials used there in<sup>295</sup>.

#### **4.7. Incidence of Risk and Passing of Property**

It is suggested that the incidence of risk is a good test for determining the stages of passing of property in a sale. The delivery obtained by the transferor from the transferee with an agreement to retain the risk in the goods, as the risk usually follows the property, the delivery constitutes sale<sup>296</sup>. The risk prima-facie attaches to the ownership of the goods and passes with the property, in absence of an agreement to the contrary<sup>297</sup>. If the loss as a

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<sup>295</sup> *Firm of M/s Peare Lal Hari Singh v. State of Punjab*, [1958] 9 STC 412 (SC).

<sup>296</sup> *Sreelal Agarwala v. State of Orissa*, [1962] 13 STC 446 (Ori.)

<sup>297</sup> The Sale of Goods Act, 1930, Section 26, reads as follows,

rule falls upon the buyer, it is a sale and if the loss falls on the seller, it cannot be a sale, but may be an agreement to sale<sup>298</sup>.

#### **4.8. Delivery of Goods**

In a valid sale, doing an act, which the parties agree to treat as delivery can be assumed as delivery<sup>299</sup>. If the subject of sale is capable of an actual delivery, such delivery must accompany and follow the sale. Nevertheless, the constructive delivery is sufficient, if the subject of sale is not reasonably capable or incapable of an

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**Risk Prima facie passes with property.** -Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk whether delivery has been made or not:

Provided that, where delivery has been delayed through the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss, which might not have occurred, but for such fault:

Provided also that nothing in this Section shall affect the duties or liabilities of either seller or buyer as a bailee of the goods of the other party.

<sup>298</sup> *Chalmers' Sale of Goods Act*, 17<sup>th</sup> edn., Butterworths at pp.4 and 12

<sup>299</sup> The Sale of Goods Act, 1930, Section 33, reads as follows,

**Delivery.** -Doing anything, which the parties agree, shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf, may make delivery of goods sold.

actual delivery. An act of appropriation of goods<sup>300</sup>, in the custody of the buyer, supported by mutual consent is sufficient to constitute delivery.

The delivery or possession taken by the purchaser may be symbolic<sup>301</sup> but, must be exclusive of the seller and must be open, visible, unequivocal, and exclusive in such nature that will show the seller has ceased to be the owner of the goods. Where there is a sale of goods generally no property in them passes till delivery because until then the very goods sold are not ascertained. But where by the contract itself, the vendor appropriates to the vendee a specific chattel, and the latter thereby agrees to take that specific chattel and to pay the stipulated price, it was observed by the Court in an old case that that the parties are in the same situation as they would be after a delivery

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<sup>300</sup> Appropriation of goods means a buyer who is possession of the things owned by the seller in bulk, out of which smaller quantity is sold to the buyer, he could make the selection of the goods, which will result possession and valid title. For detailed discussion see Justice K Ramamoorthy, *Mulla Sale of Goods Act*, Sixth edn. Butterworths (2002) at p. 192.

<sup>301</sup> *Commissioner of Income Tax v. Ram Chandra Gupta & Co.*, AIR 1968 Cal. 385.

of goods in pursuance of a general contract<sup>302</sup>. The very appropriation of chattel is equivalent to delivery by the vendor and the assent of the vendee to take the specific chattel and to pay the price is equivalent to his accepting the possession of the chattel.

In a sale, delivery must be a bilateral act and voluntary transfer.<sup>303</sup> However any mode of transfer that has the effect of putting the goods in the possession of the buyer or of any person authorised to hold the goods on his behalf amounts to delivery<sup>304</sup>, which corroborate the sale. In a 'Free on Rail' contract the delivery is effected at the time of delivering and loading the goods in the railway wagons<sup>305</sup> and the seller's liability is only to place the goods free on the rail at the place of delivery. Once that is done

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<sup>302</sup> The observations of Parke, J, in *Dixon v. Yates* [(1833) 5 B & Ad. 313 at p 340), quoted by Sapru, J, in *Budh Prakash Jai Prakash v. Sales Tax Officer*, [1952] 3 STC 185 at p. 191.

<sup>303</sup> The Sale of Goods Act, 1930 Section 2(2) defines,  
 "Delivery" means voluntary transfer of possession from one person to another."

<sup>304</sup> The Sale of Goods Act, 1930, Section 33, reads, "**Delivery**.- Doing anything, which the parties agree, shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf, may make delivery of goods sold."

<sup>305</sup> *Marwar Tent Factory v. Union of India*, [1990] 77 STC 221 (SC).

the risk belongs to the buyer<sup>306</sup> and the buyer cannot escape from the liabilities arising out of the contract of sale alleging that there is no completion of sale, as actual delivery is not effected to the buyer<sup>307</sup>.

In the sale of specific goods in deliverable state, the property passes when the contract is made, irrespective of the time of payment of price or time of delivery of goods.<sup>308</sup> Merely because of bringing the plates in to the ship owner's place for executing the contract to construct a ship, does not mean that there is a delivery of goods to the ship owners and sale of materials to them<sup>309</sup>. The House of Lords negated such a contention by observing that though the plates had been approved by the surveyors of the ship owner, that did not mean there is a contract of sale

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<sup>306</sup> *Girija Proshad Pal v. National Coal Co. Ltd*, AIR 1949 Cal. 472 at para 11

<sup>307</sup> *Commissioner of Sales Tax v. Husenali Adamji and Co.*, [1959] 10 STC 297 (SC); [1959] Supp 2 SCR 702.

<sup>308</sup> The Sale of Goods Act, 1930, Section 20 reads as follows,

**Specific goods in a deliverable state**-Where there is an unconditional contract for the sale of specific goods in a deliverable state, the property in the goods passes to the buyer when the contract is made, and it is immaterial whether the time of payment of the price or the time of delivery of the goods, or both, is postponed.

<sup>309</sup> See House of Lords in *Reid v. Macbeth & Gray*, [1904] A.C. 223.

of materials apart from the contract to construct a ship, and that the title to the materials did not as such pass to the ship owners.

Where the goods sold interstate and the consignment was named self-consignor, the point of passing of property can be assumed as the payment of sale price<sup>310</sup>. The dispute on passing of property is a question of facts and can be settled on in support of proper evidences.

#### **4.9. Sale of Goods: Existing or Future Goods**

The parties to the contract can be entering in to an agreement to transact the goods, either existing or future goods<sup>311</sup>. A contract to transfer future goods<sup>312</sup> does not

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<sup>310</sup> *Sri Rama Purchase & Sales Society Ltd V. State of Madras*, AIR 1959 Andhra 36.

<sup>311</sup> Section 6 of the Sale of Goods Act, 1930, enables contract of sale of future goods. Section 6 reads as follows,

**Existing or future goods. -**

- (1) The goods, which form the subject of a contract of sale, may be either existing goods, owned or possessed by the seller, or future goods.
- (2) There may be a contract for the sale of goods the acquisition of which by the seller depends upon a contingency, which may or may not happen.

satisfy the qualification of a sale<sup>313</sup>. A man cannot grant or charge what he does not have. A future good can be promised for a sale as per an agreement to sell<sup>314</sup>. In such cases, the sale is completed either on fulfilment of condition or on time lapses or on existence of goods promised to sell. The obligation to fulfil the condition reserves the right to compensation<sup>315</sup> or performance of contract, however negatives the claim of completion of sale.

A sale in transit is not a transfer of future goods that the goods exist at the time of sale and the title is passed on issuing the invoices, even though the intermediate purchaser does not obtain the possession. The general rule is that a delivery of goods to a carrier, pursuant to a

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(3) Where by a contract of sale the seller purports to effect a present sale of future goods, the contract operates as an agreement to sell the goods.

<sup>312</sup> The Sale of Goods Act, 1930, Section 2 (6) defines future goods, which means “goods to be manufactured or produced or acquired by the seller after making of the contract or sale”.

<sup>313</sup> *Moti Ram v. Khyali Ram* AIR 1967 All. 484.

<sup>314</sup> *Malcolm Angas Tullesh v. Revenue Commissioner*, [1958] 9 STC 799 (Orissa).

<sup>315</sup> *Hurnandrai v. Pragdas*, AIR 1923 PC 54. See also *Ganga Saran v. Firm Ramachandra* AIR 1952 SC 9.

contract of sale is a delivery<sup>316</sup> to the purchaser sufficient to pass title to the goods<sup>317</sup>.

In order to constitute a sale it is necessary that there should be an agreement between the parties, on the part of the buyer to sell and on the part of the customer to purchase<sup>318</sup>. It is necessary that there should be an

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<sup>316</sup>The Sale of Goods Act, 1930, Section 39, reads as follows,

**Delivery to carrier or wharfinger- (1)** Where, in pursuance of contract of sale, the seller is authorised or required to send the goods to the buyer, delivery of the goods to a carrier, whether named by the buyer or not, for the purpose of transmission to the buyer, or delivery of goods to a wharfinger for safe custody, is prima facie deemed to be a delivery of the goods to the buyer.

(2) Unless otherwise authorised by the buyer, the seller shall make such contract with the carrier or wharfinger on behalf of the buyer as may be reasonable having regard to the nature of the goods and the other circumstances of the case. If the seller omits so to do and the goods are lost or damaged in course of transit or whilst in the custody of the wharfinger, the buyer may decline to treat the delivery to the carrier or wharfinger as a delivery to himself, or may hold the seller responsible in damages.

(3) Unless otherwise agreed, where goods are sent by the seller to the buyer by a route involving sea transit, in circumstances in which it is usual to insure, the seller shall give such notice to the buyer as may enable him to insure them during their sea transit and if the seller fails so to do, the goods shall be deemed to be at his risk during such sea transit.

<sup>317</sup> *A. Ramaiya's Sale of Goods Act*, 3<sup>rd</sup> edn. The Law Book Company Pvt. Ltd., Allahabad (1985) at p. 411.

<sup>318</sup> *Sundaram Motors (P) Ltd v. State of Madras*, [1958] 9 STC 687 (Mad).

agreement between the parties for the purpose of transferring the title of goods with other features of capacity to contract, supported by money consideration and that as a result of the transaction property must actually pass in goods<sup>319</sup>.

In a sale agreement, the goods may be owned by the seller or possessed by him<sup>320</sup>. A seller has the ownership, but possessory rights vested with other party, shall have the right to offer the goods in a sale agreement. Goods pledged or let on hire by the seller, later offer for sale are some of such instances. Sale of Goods possessed by the agents, bailee, servants etc. are the other instances.

#### **4.10. Subject Matter be Real not a Mere Chance.**

The subject matter of sale shall be absolute or shall not be a mere chance. The parties can offer a sale on expectation of obtaining the subject of sale, which is only

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<sup>319</sup> *State of Madras v. Gannon Dunkerley*, [1958] 9 STC 353 at p. 365.

<sup>320</sup> The Sale of Goods Act, 1930, S. 6(1), See *supra*, n. 311.

an agreement to sell. A forward contract<sup>321</sup> becomes actual sale only when the goods promised to sell become real. Other wise it is only an executory contract. In a contingent contract of sale the seller is estopped from denying the ownership of the goods, if he represented himself as the owner and subsequently acquired the title. The sale become absolute on the part of the buyer on happening of such contingencies and the title so acquired by the seller vests in the buyer on completion of the sale.

Unless the property in the goods has passed from the seller to buyer, there is no sale<sup>322</sup>. To determine whether the property in the goods passed, the intention of the parties has to be ascertained and it is to be inferred from the terms of contract itself<sup>323</sup>. Like wise if the goods

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<sup>321</sup> A forward contract is an executory contract, consisting of two reciprocal promises between two parties, namely, the buyer and seller to sell or buy one person to another to be performed on a subsequent date fixed by the parties. The Forward Contracts (Regulation) Act, 1952, Section 2(c) defines “Forward Contract” means a contract for the delivery of goods and which is not a ready delivery contract. Forward Contracts are of three kinds, future contracts, transferable specific delivery contracts and non-transferable specific delivery contracts.

<sup>322</sup> *Punamchand v. State*, [1951] 2 STC 14 (Nag.).

<sup>323</sup> *Louis Dreyfus & Company Ltd v. The Province of Madras*, [1952] 3 STC 19 (Mad.).

indented to be sold have ceased to exist or perished or damaged or subjected to any kind of antecedent destruction, before entering the contract, there is no sale<sup>324</sup>.

A contract of sale is one whose main object is the transfer of property in and the delivery of the possession of a chattel as a chattel to the buyer. Where the principle object of work undertaken by the payee of price is not the transfer of chattel quo chattel, the contract is merely one of work and labour<sup>325</sup>.

A running contract for sale of coal ash, that might accumulate at a pump house under the railway administration amounts to agreement to sell and there is no sale<sup>326</sup>.

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<sup>324</sup> The Sale of Goods Act, 1930, Section 7, reads as follows,

**Goods perishing before making of contract.** -Where there is a contract for the sale of specific goods, the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract.

<sup>325</sup> *Assistant Sales Tax Officer v. B.C. Kame*, [1997] 39 STC 237 (SC).

<sup>326</sup> *Union of India v. Taracand*, AIR 1976 MP 101.

#### **4.11. Specified or Ascertained Goods**

As regards a contract for the sale of specified or ascertained goods, the property in the goods is transferred to the buyer at such time as the parties to the contract intend it to be transferred. Unless the parties to the contract identified the goods and agreed upon it at the time of the contract, it cannot be said that the sale is for specified goods<sup>327</sup>. Hence sale of standing tree cannot be sale of specified goods, as standing trees are merchantable and cannot be determined until the time of felling them as approached and also when the time for their measurement has arrived<sup>328</sup>. For the purpose of ascertaining such an intention, regard shall be had to the terms of contract, the conduct of the parties and circumstances of the case<sup>329</sup>.

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<sup>327</sup> The Sale of Goods Act, 1930, S. 2 (14) denies 'Specific goods' means "goods identified and agreed upon at the time a contract of sale is made."

<sup>328</sup> *Kursell v. Timber Operators and Contractors Ltd*, [1927] 1 KB 298.

<sup>329</sup> *Husenali Adamji v. Commissioner of Sales Tax*, [1956] 7 STC 88 (Nag.)

Occasionally unascertainable goods are also subject of sale contract<sup>330</sup>. Where there is a bargain for the sale of certain quantity of goods from larger quantity or where there is power of selection to the seller to deliver or to the buyer to take, what they think fit, the sale is completed only on the goods are ascertained or selection is made. Such kind of transfer of unascertained goods is a promise to sell. No property in the goods is passed unless and until the goods are ascertained<sup>331</sup>. As pointed out by Lord Loreburn,

“There must be added to it some act which complete the sale, such as delivery or the appropriation of specific goods to the contract

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<sup>330</sup> The Sale of Goods Act, 1930, Section 23 (1), reads as follows,

**Sale of unascertained goods and appropriation.** - (1) Where there is a contract for the sale of unascertained or future goods by description and the seller unconditionally appropriates goods of that description and in a deliverable state to the contract, either with the assent of the buyer or by the buyer with the assent of the seller the property in the goods thereupon passes to the buyer. Such assent may be expressed or implied, and may be given either before or after the appropriation is made.

<sup>331</sup> The Sale of Goods Act, 1930, Section 18, reads as follows,

**Goods must be ascertained.** -Where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained.

by the assent, express or implied, of both the buyer and seller.”<sup>332</sup>

A seller drew a bill of exchange upon the buyer, payable to their order and endorsed. The bill of exchange annexed along with the bill of lading with a condition that the goods deliverable to the buyer on the acceptance and payment of bill of exchange. The buyer accepted the bill of exchange however failed to pay. The transaction lacks the satisfaction of condition and no sale is said to be completed.

A contract of sale with conditions stipulated in the contract reserves the right of disposal<sup>333</sup> to its seller and

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<sup>332</sup> *Badische Anilin Fabrik v. Hickson*, [1906] AC 419 at p. 421.

<sup>333</sup> Section 25 of the Sales of Goods Act, 1930 reserves the right of disposal to the seller until certain conditions are fulfilled. Section 25 reads as follows,

**Reservation of right of disposal. -**

- (1) Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation, reserve the right of disposal of the goods until certain conditions are fulfilled. In such case, notwithstanding the delivery of the goods to a buyer, or to a carrier or other bailee for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled.

there is no absolute transfer of title or ownership. There might be competency of parties, transfer of property and money consideration, however it lacks passing of title, in absolute.

#### **4.12. Consideration: An Essential Element.**

When a party in intermediate get commission from the seller on sale price entitled by the seller and the title goes to the purchaser, there is no sale to or by the commission agent, though he received the price as consideration<sup>334</sup>.

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- (2) Where goods are shipped or delivered to a railway administration for Marriage by railway and by the bill of lading or railway receipt, as the case may be, the goods are deliverable to the order of the seller or his agent, the seller is prima facie deemed to reserve the right of disposal.
  - (3) Where the seller of goods draws on the buyer for the price and transmits to the buyer the bill of exchange together with the bill of lading or, as the case may be, the railway receipt, to secure acceptance or payment of the bill of exchange, the buyer is bound to return the bill of lading or the railway receipt if he does not honour the bill of exchange; and, if he wrongfully retains the bill of lading or the railway receipt, the property in the goods does not pass to him.

Explanation-In this section, the expressions “railway” and “railway administration” shall have the meanings respectively assigned to them under the Indian Railways Act, 1890.

<sup>334</sup> *Rudnap Export Import v. Eastern Associates Co.*, AIR 1984 Del 20 at p. 28.

Price is inevitable to complete a sale. It reflects the money consideration for a sale<sup>335</sup>. Price is the amount of consideration which a seller charges the buyer for parting with the title of goods. The cost of price of goods with the amounts paid by the purchaser on the various heads of accounts, freight, duties, handling charges, taxes, margin of profit etc. would constitute the consideration and this entire consideration constitutes the price of the goods sold<sup>336</sup>. Cost of the goods and price of the goods are distinguishable<sup>337</sup>.

Price in a sale shall be reasonable and definite<sup>338</sup>. The price may be fixed by the parties in the sale at the time

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<sup>335</sup> *Commissioner of Income Tax v. Motors & General Stores Pvt. Ltd*, [1967] 66 ITR 692 (SC).

<sup>336</sup> *Central Wines v. Special C.T.O*, [1982] 49 STC 83 (AP) at p. 90.

<sup>337</sup> *Mafatlal Industries v. Union of India*, [1998] 111 STC 467 (SC) at p. 594.

<sup>338</sup> The Sale of Goods Act, 1930, Section 9, reads as follows,

**Ascertainment of price.** - (1) The price in a contract of sale may be fixed by the contract or may be left to be fixed in manner thereby agreed or may be determined by the course of dealing between the parties.

(2) Where the price is not determined in accordance with the foregoing provisions, the buyer shall pay the seller a reasonable price. What is a reasonable price is it question of fact dependent on the circumstances of each particular case.

of bargain is made or in consensus with the market price or the price customarily charged by the seller. Price may not be fixed by a contract<sup>339</sup>; however, the parties in a sale must at least specify the method by which the price will be determined<sup>340</sup>. Volition in fixing of sale price is very limited, when the Government declares the basic price.

Mere inadequacy of price does not affect the sale and the completion of sale is to be judged in the light of the other attendant circumstances<sup>341</sup>. An underselling, sale of goods in a lower price than market price, will not hit the sale. Quantum of sale price is a matter depends on the facts and circumstances as in usual cases the discount and rebate over normal discount<sup>342</sup> or trade discount<sup>343</sup> does not form part of the sale price. It is also settled principles is that

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<sup>339</sup> *Indian Sugars & Refineries v. State of Mysore*, AIR 1968 Mysore 332.

<sup>340</sup> *Abdul Sathar Sait v. Kunju Varkey*, 1954 KLT 209 (Ker.)

<sup>341</sup> *Madholal v. Official Assignee*, AIR 1950 FC 21

<sup>342</sup> *State of Tamil Nadu v. Indian Cable Company Ltd.* [1984] 56 STC 192 (Mad.)

<sup>343</sup> *Deputy Commissioner of Law v. Advani Oerlikon (P) Ltd.*, [1980] 45 STC 32 (SC).

the quantum of consideration and sale price is depending on the conduct of the party relevant<sup>344</sup>.

Unless expressly explained the nature of other charges, the amount involved under that head is only to be treated as the commission which will form part of the sale price<sup>345</sup>. Charges levied for the belated returning of empty bottles<sup>346</sup> or empty cylinders or bags<sup>347</sup> are part of the sale price for the purpose of taxation. When goods is sold the incidental expenses such as carrying charges, postage, telephone charges, telegrams<sup>348</sup>, packing charges<sup>349</sup>, handling charges etc.<sup>350</sup> form part of the sale price. Expenses incurred towards handling charges prior to the

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<sup>344</sup> *Black Diamond Beverages Pvt. Ltd v. Commercial Tax Officer*, [1992] 87 STC 43.

<sup>345</sup> *Commercial Tax Officer v. Uttamal Gagumal*, [1987] 64 STC 428, Guj.

<sup>346</sup> *Kalyani Breweries Ltd v. State of West Bengal*, [1990] 78 STC 441

<sup>347</sup> See *Mahabir Rice Mills v. State of Orissa*, [1983] 54 STC 218.

<sup>348</sup> *Vimalchand v. Commissioner of Commercial Taxes*, [1987] 67 STC 74 (M.P.).

<sup>349</sup> *Commissioner of Commercial Taxes v. Rai Bharat Das & Brothers*, [1988] 71 STC 277 (SC).

<sup>350</sup> *Vallabh Glass Works Ltd. v. State of Gujarat*, [1982] 50 STC 352 (Guj.). See also in *Nemkumar Kesarimal v. Commissioner of Commercial Taxes*, [1955] 6 STC 222.

delivery of goods but of course in connection with sale do not form part of the sale price<sup>351</sup>.

High Court of Madhya Pradesh unambiguously held that when a dealer sold gift articles to the retailers under a Gift Scheme at fifty percent of its cost price and received the balance price from its principal, then the amount received from the principle shall not form part of sale price for determining the tax liability<sup>352</sup>. It was also held that every post sale charges, even if levied prior to the sale and charged in the invoice, will not form part of the sale price.<sup>353</sup>

However charges incidental in getting the forest produces cannot be treated as part of its purchase price<sup>354</sup>. Administrative surcharge and price equalisation charge due to the Government from the retail dealers of rationed articles not form part of sale price as that is a rate fixed by the Government in terms of the agency granted to the

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<sup>351</sup> *State of Andhra Pradesh v. Bengal Coal Company Ltd*, [1971] 27 STC 213 (Andhra).

<sup>352</sup> *Commissioner of Sales Tax v. Rita Sales Corporation*, [1986] 61 STC 240 (MP)

<sup>353</sup> *Hindustan Steels Ltd. v. State of Tamil Nadu*, [1984] 56 STC 70, (Mad.).

<sup>354</sup> *Tata & Co. v. Sales Tax Officer*, [1971] 27 STC 176 (Orissa).

retailers<sup>355</sup>. Statutory levies, though included in the invoices, but not collected in terms of incentive schemes, shall not be includable in the sale price, as it is not actually passing from the buyer to the seller<sup>356</sup>.

Price may not be passed at the time of delivery of sold goods. The time of payment of sale price is depending on the terms of sale or intention of the parties. The damage received for breach of contract cannot be considered as the sale price, which constitutes sale<sup>357</sup>. Unless there has been a transfer of property, there cannot be a sale, only because of the loss of goods were compensated with damages by the carrier<sup>358</sup>. It is immaterial if the amount received by way of damages should represent the full price of the goods lost.

A sale is incomplete if a seller invoked the right of stoppage in transit<sup>359</sup>. If the movement of the goods sold is

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<sup>355</sup> *Food Corporation of India v. State of Kerala*, [1988] 68 STC 1 (SC).

<sup>356</sup> *Andhra Conductors (P) Ltd v. State of Andhra Pradesh*, [1994] 95 STC 320 (Andhra).

<sup>357</sup> *Sales Tax Officer v. Budh Prakash*, [1954] 5 STC 193.

<sup>358</sup> *Newton Chikhli Collieries Ltd v. State*, [1952] 3 STC 243 (MP).

<sup>359</sup> The Sale of Goods Act, 1930, Section 50 reads as follows,

interfered by an unpaid seller or a seller having insolvent buyer, the effect is a voidable sale. Sale become immature till the consideration passes. Such an immature sale cannot be treated as sale in the legal sense as it lacks the requirements of mutual assent and passing of consideration. Taking of possession or constructive notice to the possessor are the methods to invoke the right to stoppage<sup>360</sup> and it reveals the intention of the seller to conclude the sale as cancelled until he rewarded. The seller

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**Right of stoppage in transit.** -Subject to the provisions of this Act, when the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until payment or tender of the price.

<sup>360</sup> The Sale of Goods Act, 1930, Section 52 reads as follows,

**How stoppage in transit is effected-** (1) The unpaid seller may exercise his right of stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods. Such notice may be given either to the person in actual possession of the goods or to his principal. In the latter case the notice, to be effectual, shall be given at such time and in such circumstances, that the principal, by the exercise of reasonable diligence, may communicate it to his servant or agent in time to prevent a delivery to the buyer.

(2) When notice of stoppage in transit is given by the seller to the carrier or other bailee in possession of the goods, he shall re-deliver the goods to, or according to the directions of, the seller. The expenses of such re-delivery shall be borne by the seller.

In *Harprashad Tulsi Ram v. Jindar Parshad Naim Kanwar*, AIR 1934 Lah. 191, the Court observed that the seller could not stop the goods in transit unless the property has passed to the buyer.

can exercise the right to stoppage even when property in the goods has passed to the buyer. Of course, if no property has passed, there would not be need to exercise the right at all.

These are some of the inherent problems in the interpretation of the concept of sale. There are other relative issues in the interpretation, which are normally connected with the position of the parties or the relations among the parties to the contract of sale.

## CHAPTER V

# **Supplementary Issues in Interpretations: Position of Parties Transacting**

Apart from the subject matter, nature and essence of the transaction of the sale in question, which was discussed in the previous chapter, there are various other problems regarding the status and position of the parties involved in the transaction, while interpreting the concept of sale. In modern times there are many circumstances which call for dynamic interpretations; here also the doctrines relating to mutual assent and passing of property are the guiding factors.

### **5.1. Transfer between Club and its Members**

A transfer in between a club and its member constitutes no sale<sup>361</sup>. Two requirements are absent in such cases; means the supply of refreshments to its

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<sup>361</sup> *Cosmopolitan Club v. Deputy Commercial Tax Officer*, [1952] 3 STC 77 (Mad.).

members by the club out of the club funds, composed of members' subscription does not constitute transfer of property as such<sup>362</sup>. There is no transfer of the general or absolute property to its members, who themselves constitutes the owners, but only a transfer of special interest<sup>363</sup>. A non-proprietary members club is usually not dealing in trade or business<sup>364</sup> and supply to its members is not a sale of the refreshment amendable to sales tax<sup>365</sup>. Want of profit motive of a members club is again a criteria to hold the transfer between club and member, if any, is not a sale.<sup>366</sup>

The basic principles laid down by the court is that a purely members' club which makes purchases through secretary or manager and supplies requirements to members at a fixed rate does not in law sell these goods to

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<sup>362</sup> *Young Men's Indian Association v. Joint Commercial Tax Officer*, [1963] 14 STC 1030 (Mad.)

<sup>363</sup> *Graff v. Evans*, [1882] 8 Q.B.D, 373 referred in H.R. Gokhale, *Pollock & Mulla on the Sale of Goods Act & Partnership Act*, 4<sup>th</sup> edn., N.M. Tripathi Pvt. Ltd, Bombay (1977) at p. 22.

<sup>364</sup> *Inland Revenue Commissioners v. Westleigh Estates Co. Ltd*, (1924) 1 KB 390.

<sup>365</sup> *Cole v. Merton Park Wimbledon Golf Club*, (1927) 43 TLR 400.

<sup>366</sup> *Deputy Commercial Tax Officer v. Cosmopolitan Club*, [1955] 6 STC 1 (Mad.)

members but merely distributes them, all the essentials of a sale in the transaction being wanting<sup>367</sup>. In the case of incorporated clubs, it is acting as agent of its members investing its own moneys for preparing things for consumption of the principal and later recouping himself of the expenses incurred<sup>368</sup>. Mere registration under a statute does not confer the status of incorporated body<sup>369</sup>, even if it could acquire property and entitles to enjoy certain other statutory privileges<sup>370</sup>.

Though a different view was expressed by a three Judge's Bench in *Enfield India Ltd Co-op. Canteen's case*<sup>371</sup>, a six Judges Bench of the Hon'ble Supreme Court, in *Young Men's Indian Association's case*<sup>372</sup> held that if a club, even though a distinct legal entity is only acting as an

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<sup>367</sup> *Supra*, n. 361.

<sup>368</sup> *Joint Commercial Tax Officer v. Young Men's Indian Association*, [1970] 26 STC 241 (SC).

<sup>369</sup> *Board of Trustees, Ayurvedic and Unani Tibia College v. State of Delhi*, AIR 1962 SC 458.

<sup>370</sup> *Taff Vale Railway Co. v. Amalgamated Society of Railway Servants*, [1901] AC 426.

<sup>371</sup> *Deputy Commercial Tax Officer v. Enfield India Ltd Co-operative Canteen Ltd*, [1968] 21 STC 317 (SC)

<sup>372</sup> *Supra*, n. 368.

agent for its members in the matter of supply of various preparations to them, no sale would be involved as the element of transfer would be completely absent. In *Enfield's case*<sup>373</sup> the Judges held that a society being a legal person, the property in the refreshments supplied to its members is vested in the society and when refreshment is supplied to its members for a price paid or promised, a direct transfer of property in the refreshments results to treat the transfer as sale.

While deciding the issues the Courts in India were greatly influenced by the foreign decisions, particularly, the principles evolved in *Trebanog Working Men's Club and Institute Ltd v. Macdonald*<sup>374</sup> and *New York Life Insurance Co. v. Styles*<sup>375</sup>. In *New York Life Insurance Case*<sup>376</sup> it was held that when a number of individuals agree to constitute funds for a common purpose, they could not be regarded as traders. A club may be juristic entity capable of holding

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<sup>373</sup> *Deputy Commercial Tax Officer v. Enfield India Ltd Co-operative Canteen Ltd*, [1968] 21 STC 317 (SC)

<sup>374</sup> [1940] 1 KB 576.

<sup>375</sup> (1881) 14 App. Cas 381

<sup>376</sup> *Ibid.*

property, but when it purchases articles for the consumption of its members and supplies the same to them against payment, no element of sale is involved in the transaction<sup>377</sup>. The clubs should be regarded only as holding the property for the benefit of its members and releasing them to its members.

## **5.2. Supply of Goods Incidental to Service.**

Whether service coupled with supply materials amounts to sale, unless there is an intention to have a transaction of sale in detach. Supply of meals by the hotelier to the resident guests is not sale of food<sup>378</sup>. Supply of food is essentially an indivisible transaction. The primary and real activity of the hotelier is to receive the customer in the hotel to stay or lodging. The Hon'ble Supreme Court in *Associated Hotel's case*<sup>379</sup> held that even if the indivisible transaction is to be disintegrated, there is no question of the supply of meals during the stay constituting a separate

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<sup>377</sup> *Trebanog Working Men's Club and Institute Ltd v. Macdonald*, [1940] 1 KB 576.

<sup>378</sup> *State of Himachal Pradesh v. Associated Hotels of India*, [1972] 29 STC 474 (SC).

<sup>379</sup> *Ibid.*

contract of sale. There is no intention to the parties to sell and purchase of food-stuffs supplied during the meal time. Supply of meals must be regarded as ministering to a bodily want or to the satisfaction of human need and it is integrated with the hospitality service of the hotelier<sup>380</sup>. But where food is supplied in an eating house or restaurant and if the substance of transaction in its dominant object is supply of foods and rendering service is merely incidental, the transaction would undoubtedly sale and not a service only<sup>381</sup>. Here the Apex Court once again gives stress on the dominant intention of the contracting parties too, whether it is service or supply of materials.

While operating the flights, the Airways supplies foods to its passengers and the travel cost is same whether or not a passenger availed the facility of food. Dealing with the case the Court of Appeal<sup>382</sup> held that there is only service of air transportation and flights catering is part of

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<sup>380</sup> *Northern India Caterers(India) Ltd v. Lt. Governor of Delhi*, [1978] 42 STC 386 (SC).

<sup>381</sup> *Northern India Caterers (India) Ltd v. Lt. Governor of Delhi*, [1980] 45 STC 212 (SC).

<sup>382</sup> *British Airways plc. v. Customs and Excise Commissioner*, [1990] Simon's Tax Cases 643.

and integral to the transportation and there is no separate intention to supply of foods to sale. Although each supply in a composite transaction might be an independent separate supply, the essential features of a transaction might show that one supply was ancillary to another. This supports with the common law principles which states that in fact that separate charges were identified in a contract or on an invoice did not on a consideration of all the circumstances necessarily prevent the various supplies from constituting one composite transaction or did it prevent one supply being ancillary to another supply<sup>383</sup>.

### **5.3. Non-voluntary or Statutory Transfer.**

A transfer is an intentional act to passing of property. It is the action where in the owner of the property delivers it to another person with the intent of passing the rights, which he had in it to the latter<sup>384</sup>.

A non-voluntary transfer or statutory transfer provided under the Act is not a sale. A statutory transfer is

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<sup>383</sup> *Customs and Excise Commissioner v. British Telecommunications Plc.* [1999] Simon's Tax Cases 758 (House of Lords)

<sup>384</sup> *20th Century Finance Corporation Ltd. V. State of Maharashtra*, [2000] 119 STC 182 (SC) at p. 216.

deficient in the consensual element, which forms the very basis of a contract.<sup>385</sup> The ordinary conception of sale is that something is handed over for a price as a result of negotiation and agreement.

The essential element of bargaining<sup>386</sup> or a voluntary act is lacking in a compulsory acquisition of property by the State or instrumentalities of State and it is not a sale as the word is ordinarily used.<sup>387</sup> A statutory transfer amounts to sale or not would depend upon whether the liberty of contract in relation to the fundamentals of the transaction is completely excluded by the provision of the statute or order<sup>388</sup>. In *New India Sugar Mill's*<sup>389</sup> Case the Supreme Court held that the mutual assent is lacking in a compulsory sale or statutory sale, hence it is not a sale in ordinary sense.

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<sup>385</sup> *Appleby V. Sleep* [1968] 2 All ER 265.

<sup>386</sup> *Poppatlal Shah v. State of Madras*, [1953] 4 STC 188. (SC)

<sup>387</sup> *Calcutta Electric Supply Corporation Ltd v. Commissioner of Income Tax* [1951] 19 ITR 406 (Cal.)

<sup>388</sup> K. Ramamoorthy, J, *Mulla: Sale of Goods Act*, 6<sup>th</sup> edn. Butterworths, New Delhi (2002) at p. 62.

<sup>389</sup> *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, AIR 1963 SC 1207.

In *Chittar Mal Narain Das v. Commissioner of Sales Tax*<sup>390</sup> the compulsory supplies of wheat under U.P. Wheat Procurement (Levy) Order, 1959 and in *State of Tamilnadu v. Cement Distributors (P) Ltd*<sup>391</sup> the supply of cement under State controlled scheme were held as no sale, in absence of volition. Compulsory acquisition of electricity plant was held not a sale since there is no volition and there is no consensus on the consideration of acquisition<sup>392</sup>. The ratio laid down by the Court in *Calcutta Electric Supply Corporation's case*<sup>393</sup> seems to be inspired by the House of Lords decision in *Kirkness's case*<sup>394</sup>.

This position was later subjected to reconsideration in various cases decided by the Apex Court. It is suggested that though the compulsory acquisition of property would exclude the element of mutual assent that is fundamental to a sale, so long as mutual assent, express or implied, is not totally excluded the transaction will amount to sale. It is

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<sup>390</sup> [1970] 26 STC 344 (SC).

<sup>391</sup> [1973] 31 STC 309 (SC).

<sup>392</sup> *Supra*, n. 387.

<sup>393</sup> *Ibid*.

<sup>394</sup> *Kirkness v. John Hudson & Co. Ltd*, [1955] AC 696

observed by Hidayathulla, J, in *New India Sugar Mill's Case*<sup>395</sup>, that a compelled sale would nevertheless be a sale. According to Cheshire<sup>396</sup> there are instances which necessitate the State to compel persons to make contracts for reasons like social security.

Though the parties in the statutory transactions are bound by the legal requirements strictly, there is an agreement between the parties to enter into the transaction on statutory terms, it is assumable to be consensual and there is sale.<sup>397</sup> Offer and Acceptance, the essentials required to constitute a contract, need not always be in the elementary form, nor must the consent to the contract always be expressed. Such elements can be spelt out from the conduct of the parties. The true relationships of the parties in each case have to be gathered from the nature of the contract, its terms and conditions and the terminology

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<sup>395</sup> See the dissenting Judgment of Hidayathulla, J, in *New India Sugar Mills Ltd. V. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC) at para 59.

<sup>396</sup> Cheshire, *Law of Contract*, 4<sup>th</sup> edn., Butterworths (1981) at p. 23.

<sup>397</sup> *Vishnu Agencies Pvt. Ltd v. Commercial Tax Officer*, AIR 1978 SC 449.

used by the parties is not decisive of the legal relationship<sup>398</sup>.

Conversely, to its earlier views, the Supreme Court held, the supplies of Iron and Steel in pursuance of orders made under the Iron and Steel (Control and Distribution) Order, 1941 are sales, even though it is in the nature of compulsory attainment<sup>399</sup>. This is the view taken by the Constitutional Bench of the Court in *Vishnu Agencies Case*<sup>400</sup> and overruled its earlier view in *New India Sugar Mills case*<sup>401</sup> where the majority two judges held that the supplies of sugar to different States and Sugar Mills by the Controller of Sugar under the Sugar and Sugar Products Control Order, 1946 constitutes no sale because it have not the mutual assent.

The different views of the Apex Court created a lot of confusion in deciding the nature of obligations in

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<sup>398</sup> *Tirumala Venkateshwara Timber & Bamboo Firm v. CTO*, [1968] 21 STC 312 (SC) at p. 316.

<sup>399</sup> *Supra*, n. 397.

<sup>400</sup> *Ibid.*

<sup>401</sup> *New India Sugar Mills Ltd. v. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC): AIR 1963 SC 1207.

compulsory supplies. In *State of Rajasthan v. Karam Chand Thapper*<sup>402</sup> the Court observed that the compulsory supplies of coal made under the Colliery Control Order, 1945 constitutes sale. The view was reiterated in *Oil and Natural Gas Commission v. State of Bihar*<sup>403</sup>, where it was held that Crude Oil supply by ONGC to Indian Oil Corporation made as per the directions of Central Government is sale. The supply of foreign liquor to the holders of permit issued under the Excise Act is held as a sale<sup>404</sup>, even though the supply requires statutory guidelines.

The freedom of contract and volition of the parties to the contract are, again, considered as the essential elements in a contract of sale. A full bench of the Punjab and Haryana High Court<sup>405</sup> upheld this view, even after, the decision in *Vishnu Agency' Case*<sup>406</sup>.

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<sup>402</sup> [1969] 23 STC 210 (SC).

<sup>403</sup> [1976] 38 STC 435 (SC).

<sup>404</sup> *State of Punjab v. Dewans Modern Breweries Ltd.*, [1979] 43 STC 454 (SC).

<sup>405</sup> *Krishna Rice Mills v. State of Haryana*, [1981] 47 STC 182 (P&H- FB).

<sup>406</sup> *Supra*, nn. 397 & 399.

## **5.4. Transfer between Principal and Agent**

The delivery of goods from a principal to the consignment agent for the purpose of sale by the agent for and on behalf of the principal lacks the features of sale, as there is no money consideration passing in between the Principal and Agent<sup>407</sup>. The essence of the agency to sell is the delivery of the goods to a person who is to sell, not as his own property but that of the principal.

In *Goverdhan Hathibhai and Co v. Appellate Assistant Commissioner*<sup>408</sup>, the Kerala High Court gave a live explanation in this regard. The agent obtained goods from the principal, pay for it and carry it at his risk with an obligation to maintain daily sales account subject to the supervision of the principal. The agent is obliged to return the delivered to goods with the infrastructures provided by the principal, on termination of relationship and entitled to get discount on the price of the goods obtained from the

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<sup>407</sup> *Standard Pharmaceutical Works v. Member, Board of Revenue*, [1954] 5 STC 327 (Cal.).

<sup>408</sup> [1961] 12 STC 464 (Ker.). The Supreme Court overruled this decision in *State of Kerala v. Goverdhan Hathibhai & Co.*, [1964] 15 STC 314 (SC).

principal. The principal has several like agents and entitled to fix the minimum delivery quota for each agent, the price of the goods and the restricted areas of operation of the agents. The principal has an obligation to provide the infrastructures required by the agents. The sale by the agent is held to be a sale by the principal and the delivery of the goods in between the principal and agent do not constitute sale<sup>409</sup>.

The Supreme Court held, the delivery of goods to an out station dealer by the supplier with a right to fix or alter the price of the goods and the outstation dealer is entitled to get a fixed remuneration for his exertion with an obligation to pay the price only after effecting the sale to customers, the delivery lacks the features of sale as there is no actual passing of ownership of the goods<sup>410</sup>.

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<sup>409</sup> *Hafiz Din Mohammad Haji Abdulla v. State of Maharashtra*, [1962] 13 STC 292 (SC).

<sup>410</sup> *Ibid.*

## **5.5. Loan Transaction, Whether Constitute Sale.**

The transaction on a joint venture<sup>411</sup> or loan transaction<sup>412</sup> will not constitute a sale. When the owner of the goods adjusted the security given for loan transaction, on default by the customer to return the goods, the realization by forfeiture of the security deposit cannot be payment of sale price. It can be only realization of liquidated damages of forfeiture under the contract<sup>413</sup>. When the farm growers entrusted the crops to the financier for selling it in the market and allow the financier to adjust the sale proceeds in the loan availed by the growers, it is only loan transaction and not a sale exigible to sales tax<sup>414</sup>.

## **5.6. Transaction between Branches.**

Amounts are given in loan for the purchase of machinery and the ownership in machinery is transferred

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<sup>411</sup> *Deputy Commissioner of Commercial Taxes v. Eswaran*, [1976] 37 STC 543 (Mad.).

<sup>412</sup> *Sri Rani Lakshmi Ginning v. State of Tamil Nadu*, [1981] 48 STC 406 (Mad.).

<sup>413</sup> *Southern Cable & Engineering Works v. State of Kerala*, [2002] 126 STC 178 (Ker.).

<sup>414</sup> *Provincial Government of Madras v. Mudukuru Munirathnam Chetti*, [1953] 4 STC 296 (Mad.).

after the repayment of the loan, is a hire purchase agreement cannot be termed as sale and only a loan agreement<sup>415</sup>. The transaction is merely with a contract for the purpose of security and there is no intention to purchase or sell the equipments.<sup>416</sup>

The transfer of goods from head office to branches or in between branches will not amount to sale, that such transportation is merely for conveniences in business and not for any transfer of ownership in the goods<sup>417</sup> or both the units are one and same entity in the eye of law<sup>418</sup>. Goods transferred from factory to its branches also constitute same position<sup>419</sup>. Any payments of commission or agency brokerage during such branch transfer would not amount to a transaction of sale in its ordinary meaning<sup>420</sup>.

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<sup>415</sup> *State of Kerala v. Modern Plastics Industries*, [1984] 57 STC 64 (Ker.).

<sup>416</sup> *Sundharam Finance Ltd v. State of Kerala*, [1966] 17 STC 489 (SC).

<sup>417</sup> *Bharat Sugar Mills Ltd. v. State of Bihar*, [1957] 8 STC 832 (Pat.).

<sup>418</sup> *International Cotton (Waste) Corporation v. Assessing Authority*, [1965] 16 STC 1045 (Punj.).

<sup>419</sup> *State of Madras v. Marshall Sons*, [1954] 5 STC 305 (Mad.).

<sup>420</sup> *Bengal Nagpur Cotton Mills Club v. STO*, [1957] 8 STC 781 (MP).

## **5.7. Transaction within Partnership.**

Two partnership firms, consists of same partners transfers goods from one to another would not constitute sale<sup>421</sup>. A firm has no separate legal existence apart from its partners collectively and the property of the firm vests in the partners jointly. Nevertheless the situation in case of transfer in between same set of partners to self is different from that of same partners constituting two different partnership firms. A person cannot sell goods to himself, but there may be sale between separate legal entities as, such partnership firms have separate legal existence in the eye of law<sup>422</sup>.

Movables belonging to the partnership firm or undivided family, later divided and allotted between the partners or members on its dissolution, amounts to no sale as there is no money consideration, no bargain, no agreement to sale, which are essentials of a sale<sup>423</sup>.

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<sup>421</sup> *Mahendra Kumar Ishwarlal & Co. v. State of Madras*, [1968] 21 STC 72 (Mad.).

<sup>422</sup> *Deputy Commissioner v. Kelukuty*, [1978] 42 STC 108 (Ker.).

<sup>423</sup> *State of Gujarat v. Ramanlal Sankalchand & Co.*, [1965] 16 STC 320 (Guj.).

Allotment of property of firm to a retiring partner in partial satisfaction of claim to his share in the firm amounts to no sale<sup>424</sup>.

### **5.8. Multiple Transfers in Combined Sale.**

Where the points of delivery of goods mixed or fused, each points of delivery can be considered as separate sales or not is a debatable issue. Here each point of deliveries is effected out of separate contracts, though there is only one point of effective transfer. However the transfer of goods between Non residents and a local dealer subject to the agreements between the non residents and intermediate dealer and the later with a local dealer with a condition to release the same to the nominee, the combined transaction was held as single sale in absence of passing of property between the non resident seller to the intermediate dealer<sup>425</sup>.

The combined sale, where two deliveries were synchronised in a point of time, but were separate in point

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<sup>424</sup> *Commissioner of Sales Tax v. Khurana & Co.*, [1980] 46 STC 39 (MP).

<sup>425</sup> *Saraswatha Corporation Pvt. Ltd. v. State of Kerala*, [1963] 14 STC 60 (Ker.).

of fact and in the eye of law, it was held that each deliveries are separate sales<sup>426</sup>. However there is only one physical delivery of goods and the other is only a supposition. The intermediate dealer entered agreement with the actual seller and before the date of delivery entered another agreement with a prospective buyer. The transfer is effected in between the seller and prospective buyer subject to the guidelines of the intermediate dealer. This combined sale consists of two deliveries, one is in between the seller and intermediate dealer and other is in between the inter mediate dealer and buyer, though the seller effects physical transfer of goods to the buyer on payment made by the buyer.

Here the buyer cannot claim a single sale in between the seller and him that there is no privity of contract with the seller and his agreement is only with the intermediate dealer. The delivery of goods in between

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<sup>426</sup> *Bayyanna v. Govt. of Andhra Pradesh*, [1961] 12 STC 147 (SC).

original seller to Kutcha delivery order holders amount to multi point sale<sup>427</sup>.

### **5.9. Test of Dominant Object of Parties.**

It is the dominant object of the parties to the contract, a predominant factor for deciding the nature of transaction, a sale or not<sup>428</sup>. Mere passing of property in an article or commodity during the course of performance the transaction in question does not render the transaction to be sale. The factors to be considered are primary object of the transaction and the intention of the parties to the contract<sup>429</sup>. In the customer supplied paper, the printer returns the 'printed goods' after the mechanically printing work, there is only application of printing ink owned by the printer, there is no sale of goods as such that no transfer of printer's ink, but only of the impressions made by it on paper with the help of printer's help. Such an intangible

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<sup>427</sup> *Thammana Gangadharan & Sons v. Board of Revenue*, [1959] 10 STC 560 (Andhra).

<sup>428</sup> *Maharashtra Mudran Parishad v. State of Maharashtra*, [2005] 139 STC 193 (Bom.).

<sup>429</sup> *Hindustan Aeronautics v. State of Karnataka*, [1984] 55 STC 314 (SC) at p. 322.

effect of printer's service cannot be considered as sale<sup>430</sup>.

However the transfer of printed goods after procuring the materials and by printing amounts to manufacture and selling a product, which amounts to sale<sup>431</sup>.

### **5.10. Contracts of Service and Labour.**

The service contracts of photography, photocopying, cyclostyling, typing and micro filming are not sale in the restricted connotation of sale, as it is only job works of technical persons having knowledge and skills of various machines installed for various purposes like photo developing, duplication of documents etc. Mere passing of property in an article or commodity during the course of performance of the transaction does not render the transaction to be sale. Even if a contract purely of service, it is possible that article may have to be used by the person executing the work and property in such articles or materials may pass to the other party. That would not

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<sup>430</sup> *In re Rajasthan Printing and Lith Works Ltd*, [1952] 3 STC 62.

<sup>431</sup> *Dominion Press Limited v. Minister of Customs and Excise*, [1928] AC 340.

necessarily convert the contract of service to sale of goods<sup>432</sup>.

The test is whether or not the work and labour bestowed end in anything that can properly become subject of sale; neither ownership of material nor value of skill and labour compared with the value of materials is conclusive although such matters may be taken into consideration in determining the circumstances of a particular case whether the contract in substance one for work and labour or one of sale of a chattel<sup>433</sup>.

### **5.11. Element of Sale in Works Contract.**

The fact that in the execution of a contract for work some materials are used and property in the goods so used passes to the other party, the contractor undertaking to do the work will not necessarily be deemed on that amount to sell the materials<sup>434</sup>. Where the main object of the work undertaken by the person to whom the price is paid is not

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<sup>432</sup> *Supra*, n. 429.

<sup>433</sup> *Asst. Sales Tax Officer v. B.C. Kame*, [1977] 39 STC 237 (SC).

<sup>434</sup> *Government of Andhra Pradesh v. Guntur Tobaccos Ltd*, [1965] 16 STC 240 (SC).

the transfer of a chattel as a chattel, the contract is not for sale, but one of work and labour<sup>435</sup>. The object of the payment of the price is to get a document copied, not to receive the paper, the media in which the document duplicated. The customer has no intention to purchase the paper for price and his interest is only if the paper bears the duplication of document. Supply of paper is only an incidental transaction to that of main activity of duplication of document<sup>436</sup>.

For deciding the nature of the contract, whether it is sale or labour it is necessary to determine the substance of the contract<sup>437</sup>. When the substance of the contract is that skill and labour that had been exercised for the production of the article and thus sale of material is only ancillary too that<sup>438</sup>.

Following the said principles of law, the argument that while duplicating a document by photo copying or

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<sup>435</sup> *Everest Copiers v. State of Tamil Nadu*, [1996] 103 STC 360 (SC).

<sup>436</sup> *Ibid.*

<sup>437</sup> *State of Tamil Nadu v. Anandam Viswnathan*, [1989] 73 STC 1 (Mad).

<sup>438</sup> *Commissioner of Sales Tax v. Uma Art Press*, [1984] 56 STC 300 (All.)

cyclostyling there is no element of sale only a labour work seems to be acceptable. The transfer of property in paper is a post-execution event, which does not take place during the course of execution of the job and such transfer is not a sale but an incidental event consequent to the dominant job of rendering service through the skilled operators of specially styled machines. The contract may be for work to be done for remuneration and for supply of materials used in the execution of works for a price, it may be a contract for work in which the use of materials is accessory or incidental to the execution of works. Such contract may not be for sale in the restricted connotation of sale.

When the contractor dealing printing accounts the value paper and labour charges on printing separately, there is no necessity to club the turnover of both together for the purpose of taxation, as the real intention of the contractor is to do the labour work according to the demand of the customer<sup>439</sup>.

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<sup>439</sup> *Ramaswami v. State of Madras*, [1954] 5 STC 250.

Apparently, in another decision<sup>440</sup>, it was held that whatever that when a person entrusts a press to print stationeries and the press itself supplies the material, the transaction is nothing but a works contract only. This view seems to be correct and acceptable in *Benjamin's Sale of Goods*<sup>441</sup>.

There it was opined that when there was a contract for printing and the printer was to find the materials including the paper, it was not a contract of sale of a thing to be delivered at a future time, nor was it a contract for making a thing to be sold when completed, but it was a contract to do work and labour, furnishing the materials. Means there is no contract of sale but a contract to execute work only. The principle object is to get the material printed and not to purchase the printed materials<sup>442</sup>.

Whether a contract for preparation and supply of photo blocks is a contract of sale or a contract of skill and

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<sup>440</sup> *State of Madras v. Vijayaraghavan*, [1955] 6 STC 237.

<sup>441</sup> *Benjamin's Sale of Goods*, 8<sup>th</sup> edn. Smith & Maxwell (London), The Common Law Library (United Kingdom) at p. 159

<sup>442</sup> *Sarvodaya Printing Press v. State of Maharashtra*, [1994] 93 STC 387 (Bom.) (FB)

labour was the question before the Kerala High Court in *Deputy Commissioner of Sales Tax v. Sreeni Printers*<sup>443</sup>. It is true that what the contractor supplied to its customers is a value added commodity but the process to prepare a photo block involve more labour and skills the value of the materials contained in the finished product. The Hon'ble High Court, in this case, held that the occupation of a block-maker is essentially one of skill and labour and if the substance of the contract between the buyer and the seller is that of skill and experience of the maker of the blocks require to be used for the production of blocks, then there is no sale, but the contract is only a works contract. It is immaterial that some materials also will pass to the customer along with the skill involved in the production of photo block<sup>444</sup>.

The activities undertaken by a photographer or photo studio can be enumerated in three ways. Firstly photographer taking photographs in his camera and supplying the prints to his customer.

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<sup>443</sup> [1987] 67 STC 279 (Ker.).

<sup>444</sup> *Commissioner of Sales Tax v. Vasudeo Rao*, [1981] 48 STC 447 (MP)

Secondly the customer brings the negatives, either taken by himself or by others and requests the photographer to enlarge the negatives to photo prints in the specified sizes.

Thirdly the photographer preparing the prints of same size from the negatives brought by the customers. The Hon'ble Supreme Court<sup>445</sup> has no doubt taken the view that when a photographer undertakes to photograph, develop the negative, or to do other photographic works and thereafter supplies the prints to his customers, he cannot be said to enter into a contract of sale of goods. The contract, on the contrary, is for use of skill and labour by the photographer to bring about a desired result.

Taking of photographs and supplying the prints thereof cannot be treated as sale of photographs for the reason that it is not the intention of the customer to buy a photograph from the photographer, as a photograph has no marketable value. When a photographer, using his skills and talent taking the photograph, developing and supplying

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<sup>445</sup> *Asst. Sales Tax Officer v. B.C. Kame*, [1977] 39 STC 237 (SC).

the print to an individual there is no such market value for the photograph, and it is not a saleable commodity<sup>446</sup>.

A customer going to a photographer for getting his exposed films developed does not ask to purchase the negative but asks to develop exposed film and to give him the negative obtained there from. Likewise, when a customer approaching a photographer with his negative for obtaining positive prints requests for giving him positive prints from his negative. Here exposed films and negatives are not marketable commodity. They have no market value for other persons. By the involvement of photo papers and chemicals, there is no accretion on the basic material, negative. Equally the intention of the work undertaken by the photographer is not the transfer of photo papers upon which the positive prints were under taken. By applying the test of dominant intention<sup>447</sup>, test of marketability and test of accretion, the activities of photographer is held not a

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<sup>446</sup> *Bavens v Union of India*, [1995] 97 STC 161 (Ker.).

<sup>447</sup> *Commercial Tax Officer v. Rajasthan Taxation Tribunal*, [2001] 124 STC 257 (Raj.).

sale<sup>448</sup>. The dictum was followed in *Golden Colour Lab's case*<sup>449</sup> and *Pro Lab's case*<sup>450</sup>. In *Rainbow Colour Lab's case*<sup>451</sup>, this view was reiterated by the Hon'ble Supreme Court and held that unless there is purchase or sale of goods, either in fact or deemed, and which sale is primarily intended not incidental to the contract, State cannot presume sale for taxing an activity which is purely a service contract and there was no element of sale involved.

However in an old reported decision of the Privy Council, based on Canadian Tax Law, in *Dominion Press v. Minister of C & E*<sup>452</sup>, it could be seen that a contract for printing and supplying of commercial stationary at an agreed price was held as contact of sale.

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<sup>448</sup> *Keshoram Surindranath v. Asst. Commissioner of Commercial Taxes*, [2001] 121 STC 175.

<sup>449</sup> *Golden Colour Lab v. Commissioner*, [2004] 134 STC 570 (Kar.).

<sup>450</sup> *Pro Lab v. State of Karnataka*, [2006] 144 STC 33 (Kar.).

<sup>451</sup> *Rainbow Colour Lab v. State of MP*, [2000] 118 STC 9 (SC).

<sup>452</sup> [1928] AC 340.

## **5.12. Test of Marketability.**

Marketability of the goods under consideration is one of the factors to decide the transaction as sale<sup>453</sup>. It only means saleable or suitable for sale, not in fact marketed or sold. The article should be, capable of being sold or being sold to the customers in the market, without any thing more<sup>454</sup> and without any change<sup>455</sup>. For articles to be marketable goods, they must be known in the market as such or must be capable of being bought and sold in the market as goods<sup>456</sup>.

It was held that there are distinguishable differences between the service contract and contract for sale. In the former, there is in the person performing or rendering service no property in the thing produced as a whole, notwithstanding that a part or even the whole of the material used by him may have been his property<sup>457</sup>.

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<sup>453</sup> *A.P. State Electricity Board v. Collector of Central Excise*, [1994] 95 STC 595 (SC).

<sup>454</sup> *Indian Cable Co. Ltd v. Collector of Customs*, [1995] 97 STC 307 (SC).

<sup>455</sup> *Union of India v. Indian Aluminium*, AIR 1995 SC 1580.

<sup>456</sup> *Bhor Industries v. Collector of Customs*, [1989] 73 STC 145 (SC).

<sup>457</sup> *Court Press Job v. State of Tamil Nadu*, [1983] 54 STC 382 (Mad.).

Printing and supply of question paper to the University is not a sale, as those question papers are not marketable in the general sense<sup>458</sup>. Equally, printing of lottery tickets which involve not only expertise but also confidentiality, does not amount to sale and use of paper and ink is only incidental and the ticket cannot be sold to any person in the market<sup>459</sup>. The end product is not a commercial commodity and cannot be sold in the market by the printer<sup>460</sup>. The printings are done at the risk of the printer and material could not be used as scrap if rejected and had to be destroyed. It is only a work of job printing<sup>461</sup>.

A duplicated paper using the Xerox machine has no marketability, in the general sense, and cannot be held as sale, when the paper upon which the duplication takes place is only incidental one<sup>462</sup>.

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<sup>458</sup> *State of Maharashtra v. Sarvodaya Printing*, [1989] 114 STC 242 (SC).

<sup>459</sup> *Thomson Press (India) Ltd v. State of Haryana*, [1996] 100 STC 417 (FB) (P&H).

<sup>460</sup> *Id.* at p 424.

<sup>461</sup> *All Assam Press Owner's Association v. Commissioner of Taxes*, [2006] 146 STC 21 (Gau.).

<sup>462</sup> *Girija v. State of Karnataka*, [1984] 56 STC 297 (Kar).

For the purpose of the taxing transaction of goods as sale, one of the requirements is it must be marketable<sup>463</sup> or a commercial commodity<sup>464</sup>. When the agency supplied additional prints of the advertising films to its customers, the prints supplied were not prints which could be sold in the market, nor there any utility of the same anyone other than the particular customer. It is not commercial commodity in the sense that it cannot be sold in the market to any other person. A printer after printing supplies cash books to the Electricity Board, according to the customer's specification held not a sale, as the goods have no commercial value for the person other than the Electricity Board and the printed cash books has no marketability in the general market<sup>465</sup>.

### **5.13. Relevance of Owner's Right to Sell.**

An essential element to constitute a sale is the title of the goods sold is in favour of the seller. A sale by non-

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<sup>463</sup> *Commissioner of Commercial Taxes v. Radio Advertising Services*, [1997] 106 STC 50 (Bom.).

<sup>464</sup> *Commissioner of Sales Tax v. Ratna Fine Arts Printing Press*, [1984] 56 STC 77 (MP).

<sup>465</sup> *Sarvodaya Printing Press v. State of Maharashtra*, [1994] 93 STC 387 (FB) (Bom.).

owner is not legitimate<sup>466</sup>. Yet, it is stated that an existing goods can be sell by the person who owned or possessed the goods<sup>467</sup> or by one of joint owners<sup>468</sup>. Of course, the person in possession shall be a mercantile agent acting in

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<sup>466</sup> The Sale of Goods Act, 1930, Section 27, reads as follows,

**Sale by person not the owner.** -Subject to the provisions of this Act and of any other law for the time being in force, where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner of the goods is by his conduct precluded from denying the seller's authority to sell:

Provided that, where a mercantile agent is, with the consent of the owner, in possession of the goods or of a document of title to the goods, any sale made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the buyer acts in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell.

<sup>467</sup> The Sale of Goods Act, Section 6 (1) reads, "The goods, which form the subject of a contract of sale, may either existing goods, owned or possessed by the seller, or future goods."

<sup>468</sup> The Sale of Goods Act, 1930, Section 28, reads as follows,

**Sale by one of joint owners.** -If one of several joint owners of goods has the sole possession of them by permission of the co-owners, the property in the goods is transferred to any person who buys them of such joint owner in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell.

the ordinary course of business<sup>469</sup> or should have the authority of the original owner to sell the goods.

There is an implied presumption on the part of the seller of goods that he has the right to sell in case of the ascertained goods and he will have the right to sell in case of unascertained goods<sup>470</sup>. Sale of goods by misrepresenting that the seller has the right to sell as the true trademark owner of the goods, later found incorrect, and it was held that the sale is with out the title<sup>471</sup>.

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<sup>469</sup> See *supra*, n. 466; proviso to section 27, The Sale of Goods Act, 1930.

<sup>470</sup> Section 14 (a) of the Sale of Goods Act, 1930. Section 14 reads as follows,

**Implied undertaking as to title, etc.-In a contract of sale, unless the circumstances of the contract are such as to show a different intention there is-**

- (a) an implied condition on the part of the seller that, in the case of a sale, he has a right to sell the goods and that, in the case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass;
- (b) an implied warranty that the buyer shall have and enjoy quiet possession of the goods;
- (c) an implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

<sup>471</sup> *Niblett v. Confectioner's Material Co.*, (1921) 3 KB 387.

The real owner of the goods enjoys the right of ownership coupled with right of possession, right of disposition and right of enjoyment. An auctioneer having no right to transfer of property simply invited the purchasers for purchase the goods of the owner cannot be held as a seller and there is no sale in between the auctioneer and purchaser, but only between the owner and purchaser<sup>472</sup>.

#### **5.14. Government Contracts.**

When the works are carried out for Government Department, lifting sand and gitti from the mine site, after paying the royalty to the Government, there is no sale by the contractor to government, who is the awarder too<sup>473</sup>. Without granting any lease the Government permitted the contractor to remove the minerals from the mines vested in them, it will not result in vesting of any rights to such goods in the contractors and there is no passing of ownership of minerals to permit the contractor to use the minerals freely.

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<sup>472</sup> *The Public Prosecutor v. M. Thommaia*, [1953] 4 STC 331 (Mad.).

<sup>473</sup> *Assistant Commercial Tax Officer v. R.K. Construction & Suppliers*, [2001] 124 STC 701.

### **5.15. No Sale in Delivery of Goods while Bailment**

The delivery of goods in due course of bailment<sup>474</sup> does not constitute any sale. The delivery of silver to the manufactures subject to return of manufactured articles for the wages and manufacturing charges. There is no sale as the property in silver never passed to the manufactures who were only acting as the bailees in respect of the silver delivered to them so long as they did not returned it in the form of finished goods<sup>475</sup>.

Supply of beer in barrels, with an undertaking to return the barrels and the price is separately charged for beer with a returnable deposit on return of barrels, the supply of barrels amounts to no sale as the relationship only that of a bailment<sup>476</sup>. A seller has the right to claim the

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<sup>474</sup> Indian Contract Act, 1872, Section 148 defines; the bailment is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.

<sup>475</sup> *Raju Chettiar & Bros. v. State of Madras*, [1955] 6 STC 131 (Mad).

<sup>476</sup> *Dyer Meakin Breweries v. Commissioner of Sales Tax*, [1972] 29 STC 69 (All.).

goods in return only he is unpaid; however the bailer has an absolute right to claim the goods in right<sup>477</sup>.

Whether a bailment can be termed as sale or deemed sale for the purpose of taxation was a question before the Bombay High Court in *20<sup>th</sup> Century Finance Corporation Ltd. v State of Maharashtra*<sup>478</sup>. The Court held that the transfer of right to use goods are in the nature of bailment and hence cannot be sale or deemed sale. The Court added that absence of transfer of ownership in favour of the hirer distinguishes transaction from sale. Since the substance of the right is enjoyment of the goods, the transfer is completed only upon the delivery of the goods. Such transfer may produces some of the effects of the sale and also achieve some of the objects for which the sale and purchase of goods are made. But that does not make the transaction as a proper sale and the right use goods transferred to hirer has only species of bailment, which is not a sale.

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<sup>477</sup> *South Australian Insurance Company v. William*, (1869) L.R. 3, P.C.101.

<sup>478</sup> [1989] 75 STC 217.

In bailment, obviously, there is transfer of goods, but for a particular period and thereafter the goods have to be returned to the person delivering them. It is a contract by which the hirer obtains the right to use the chattel hired in return for payment to the owner for the price of the hiring<sup>479</sup>.

### **5.16. Delivery while Transfer of Rights to Use.**

Installation of telephone as a part of facilitating telecommunication net work in a customer's house cannot be held as sale of telephone as it is coupled with service of telecommunication network<sup>480</sup>. The bimonthly rent received by the department is not the sale price. Rents are collected not for the use of telephone instrument but are being the charged as maintenance for the wire connecting the place of installation of phone with the system kept by the telecommunication network<sup>481</sup>. The instrument provided by the telecom department itself is useless unless it is connected with telecommunication network. It becomes

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<sup>479</sup> Halsbury's Laws of England, 4<sup>th</sup> edn at para 1551.

<sup>480</sup> *Union of India v. Government of Andhra Pradesh*, [1999] 113 STC 203 (Andhra).

<sup>481</sup> *Id.* at p 212.

service only once when it is connected to the network<sup>482</sup>. The Allahabad High Court<sup>483</sup> on different footing answered the same issue by endorsing the telecom department the status of Union of India to claim protection under Article 285 of the Constitution of India. The Hon'ble Supreme Court in *State of Uttar Pradesh v. Union of India*<sup>484</sup> overruled these decisions and held that the telephone apparatus supplied to the customers are goods and the transfer satisfies the requirements of deemed sale. Again in *BSNL's case*<sup>485</sup>, the Constitutional Bench of the Hon'ble Supreme Court diverted from its pro-revenue philosophy.

### **5.17. Delivery of Property for Hire**

Of course, when a sale occurs there is an absolute transfer of property in goods, but when there is only a delivery of property for hire<sup>486</sup> to use the property in certain

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<sup>482</sup> *Union of India v. State of Haryana*, [2001] 123 STC 539 (P&H).

<sup>483</sup> *Union of India v. State of Uttar Pradesh*, [1999] 114 STC 288 (All.).

<sup>484</sup> *State of Uttar Pradesh v. Union of India*, [2003] 130 STC 1 (SC).

<sup>485</sup> *Barath Sanchar Nigam Ltd v. Union of India*, [2006] 145 STC 91 (SC)

<sup>486</sup> The term hire is defined as follows:-

In **Webster's Dictionary**: means to obtain the use of something temporarily for an agreed payment, or to obtain the services for an agreed wage

specific purpose, can it be treated as sale? In one case the Court held no<sup>487</sup>. Machinery is supplied to a contractor for execution of works contract against collecting hire charges. The effective control of the machinery was with the owner and the contractor was not free to make use of the same for other works or move it out during the period the machinery was in his use. There was a condition also that the contractor would be responsible for the custody of the machinery while the machinery was in the site.

The Hon'ble Supreme Court also held that there is no transfer of right to use goods as such in favour of the contractor to treat the transaction as sale, as the effective control of the machinery even while the machinery was in

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In **Black's Law Dictionary** (2<sup>nd</sup> edn): means to purchase the temporary use of anything or to arrange for the labour or services of another for a stipulated compensation. An act of hiring means a bailment in which compensation is to be given for the use of a thing or labour and services about it.

In **Readers Digest, Great Encyclopaedia Dictionary** (2<sup>nd</sup> edn.): means contract under which movable property is taken for use in return for an agreed or a reasonable sum; the hirer must take reasonable care of the property.

<sup>487</sup> *Rashtriya Ispat Nigam Ltd v. Commercial Tax Officer*, [1990] 77 STC 182 (Andhra).

use of the contractor was with the awardee.<sup>488</sup> In absence of any evidence to support transfer of actual control coupled with custody and possession, hiring of sophisticated machineries designed for specific purpose can be treated as only lease and not sale<sup>489</sup>. In case of sale all the right, title and interest in the corpus is vested in the transferee, absolutely. However in the case of lease, the right and interest to enjoy the property is transferred<sup>490</sup>. It was held that accrual of the right to use goods within the meaning of Article 366 (29A) of Constitution of India necessarily involves delivery of possession<sup>491</sup>. It was also held that where a written contract exists whether in regard to ascertained goods or unascertained goods, the intention of the parties, as evidenced by the terms of contract, to transfer of right to use the goods is determinative of the fact

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<sup>488</sup> *State of Andhra Pradesh v. Rashtriya Ispat Nigam Ltd*, [2002] 126 STC 114 (SC) at p. 116.

<sup>489</sup> *Rungta Projects Ltd v. State of Bihar*, [1998] 108 STC 234 (Pat.).

<sup>490</sup> *Id.* at p. 254.

<sup>491</sup> *Saumya Mining Pvt Ltd v. Commissioner of Taxes*, [2006] 146 STC 343 (Gau.).

as to whom, how and where the right to use of the goods transferred<sup>492</sup>.

When the financial institutions, particularly commercial banks facilitate, its customer letting out of its lockers on hire or rentals, there is no transfer of right to use goods amounting to sale<sup>493</sup>. The lockers provided by the banks are the property of the banks specially equipped and fitted out for a special purpose and let out. There is no parting with possession of the property for the purpose of earning income and hirer has no right in the property<sup>494</sup>. Usually the lockers are not allowed to be opened by the customer and the bank has built a strong room, installed in a steel cabinet with safety lockers with sufficient security system and the same is part of their customer service. Additionally the bank has a lien on the goods stored in the locker for the rent payable by the customer. There is no

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<sup>492</sup> *Id.* at p. 349.

<sup>493</sup> *Bank of India v. Commissioner of Commercial Taxes*, [1987] 67 STC 199 (Cal.).

<sup>494</sup> *State Bank of India v. State of Andhra Pradesh*, [1988] 70 STC 215 (Andhra).

right to use goods and transfer to customer amounting to sale.

Similarly the Government hired the transport vehicle for conducting the general election and the transport owners are paid rent after the release of the vehicle by the Government Offices. The registration and insurance are still in the name of owners. The Court held that the authorities are forcing the transport operator to assist for the electoral purpose and to allow their vehicle to be used during the election on hiring basis with driver and fuel at the rate fixed by the Government and there is no transfer of right to use the goods to treat the transaction as sale<sup>495</sup>. The decision was later reversed in *State of Tripura v. Tripura Bus Syndicate*<sup>496</sup>. However in *Bahulayan's case*<sup>497</sup> the Kerala High Court held that by receiving hire charges by lorry owner, there cannot be any assumption that there is transfer of right to use the lorry?

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<sup>495</sup> *Tripura Bus Syndicate v. State of Tripura*, [1997] 105 STC 409 (Gau.) at 417.

<sup>496</sup> [2001] 122 STC 175 (Gau.).

<sup>497</sup> *Deputy Commissioner of Sales Tax v. S. Bahulayan*, (1992) 1 KTR 137 (Ker.).

By allowing the use of a hydraulic press installed in the premises of the owner by various customers on machine-hour basis cannot be said to be transfer of the right to use the hydraulic press to consider it as sale exigible to local sale tax<sup>498</sup>. It is at best a permission to use and no more, or a fruitful utilization of an asset otherwise lying idle<sup>499</sup>. Hence leasing out of plant and machinery is a lease of immovable property in its entirety and there cannot be presumption of taxable deemed sale, as transfer of immovable property is out of purview of sales tax<sup>500</sup>.

Yet again in *Commissioner of Sales Tax v. Bombay Sound Service*<sup>501</sup>, the Bombay High Court held that hiring of a recording studio for recording songs and dubbing sound cannot be treated as transfer of right to use the equipments and instruments embedded in the Studio and there cannot be a deemed sale to tax the hire charges as sale consideration. Alternatively, the Court held that Studio

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<sup>498</sup> *Deputy Commissioner of Sales Tax v. Bobby Rubber Industries*, [1998] 108 STC 410 (Ker.).

<sup>499</sup> *Id.* at 418.

<sup>500</sup> *Commercial Tax Officer v. Sadulshahar Krai Vikrai Sahakari Samiti*, [2004] 135 STC 90 (Raj.).

<sup>501</sup> [1999] 112 STC 290 (Bom.).

is an immovable property and any property embedded to the earth or attached to the earth in a manner essential for the beneficial user of the immovable property would also be immovable property. This view is supported either by reading of S. 3 of the Transfer of Property Act<sup>502</sup>, where the expression 'attached to earth' is defined and also the judicial dictums in *Hemendra Lal Roy v. Indo- Swiss Trading Co.*<sup>503</sup> and *Carborandum Universal Ltd. v. Commissioner of Income Tax*<sup>504</sup>. In *Sri Krishna Deo's case*<sup>505</sup>, the Court additionally held that machinery fixed to their bases with bolts and nuts although easily removable are not movable property when they have been set up with the definite object of running permanently and not with the intention of being removed after a temporary use.

When a service provider of audio visual services is engaged for any programme or event and the provider without delivering the equipment to customer, takes the

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<sup>502</sup> Transfer of Property Act, 1882, Section 3 reads, "Immoveable property" does not include standing timber, growing crops or grass.

<sup>503</sup> AIR 1955 Pat. 375.

<sup>504</sup> [1984] 146 ITR 1 (Mad.).

<sup>505</sup> *Official Liquidator v. Sri Krishna Deo*, AIR 1959 All 247.

equipment to the site and installs them, operates them and bring back the same after dismantling, there is no transfer of possession or passing of effective control to make the transfer as transfer of right to use goods and there is no deemed sale<sup>506</sup>.

However the situation is different if the provider hires the equipment to the customer without rendering the other service. There is passing of effective control as the equipments are transported, installed and operated by the customer after getting the possession<sup>507</sup>. When the owner of an excavator hires it to mines under a peculiar situation that it was operated by the person engaged by the owner and the operational expenses were incurred by the owner, there cannot be any transfer of right to use goods to make the transfer as deemed sale, as the effective control of the excavator rest with the owner<sup>508</sup>.

Charges received on over- detention of cylinders after the use of its contents shall not be treated as the

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<sup>506</sup> *Lakshmi Audio Visual Inc. v. Assistant Commissioner of the Commercial Taxes*, [2001] 124 STC 426 (Kar.).

<sup>507</sup> *Id.* at p. 428.

<sup>508</sup> *Alpha Clays v. State of Kerala*, [2004] 135 STC 107 (Ker.).

consideration for transfer of right to use goods and part of sale price<sup>509</sup>. The Court here diverted from the principles settled in other two decisions, namely, *Industrial Oxygen Co. Pvt. Ltd v. State of Andhra Pradesh*<sup>510</sup> and *Harbans Lal v. State of Haryana*<sup>511</sup>. The Kerala High Court<sup>512</sup> followed the decision in *Asiatic Gases's*<sup>513</sup> and held that incidental receipt of certain amounts by way of rent for the delayed return of cylinders will not fall within the meaning and expression of 'transfer of right to use goods' and cannot be deemed sale.

In comparison, in a Canadian case, the pawnbroker took articles from the customer on an agreement that the pawnbroker becomes the owner of the articles only if the customer failed to repay the amount or to redeem the

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<sup>509</sup> *Asiatic Gases Ltd v. State of Orissa*, [2001] 121 STC 405(Ori.)

<sup>510</sup> [1992] 86 STC 539 (Andhra).

<sup>511</sup> [1993] 88 STC 357 (P&H).

<sup>512</sup> *West Coast Industrial Gases v. State of Kerala*, [2003] 132 STC 177 (Ker.) at p. 181.

<sup>513</sup> *Supra*, n. 509.

articles. Such transaction is not to be a sale as held by the Canadian Court in the *Queen v. Morris*<sup>514</sup>.

### **5.18. Delivery in Hire Purchase Agreements.**

A hire purchase agreement is a special type of contract and a common and familiar instrument of mercantile social service<sup>515</sup>. It enables the hirer to own the article of his choice by paying on easy instalments and the dealer to provide the article to his customer for profit without minimum risk. The system was evolved at least in two stages. In the first stage, there was a transaction between the dealer and the customer, with a hire purchase agreement between them, where the dealer has to face the risk of full payment of price of chattel till the payment of last instalment<sup>516</sup>. This risk factor of the dealer necessitated the second stage through an intervention of the financier, in between the dealer and customer, who in turn pay the value of the chattel to the dealer and enter hire- purchase

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<sup>514</sup> 1953 Canadian Tax Cases 85.

<sup>515</sup> *Transport and General Credit Corporation Ltd v. Morgan*, [1939] 2 All ER 17 at p 28.

<sup>516</sup> See the minority Judgment of Subba Rao, J., in *Sundaram Finance Ltd v. State of Kerala*, [1966] 17 STC 489 at p. 492.

agreement with the customer. The main feature of these hire- purchase agreement, apart from small variations, is that the dealer or financier continued to be the owner till the terms of the agreement are fully complied with by the customer and the option to purchase the chattel was exercised by the customer. In another variation of the hire-purchase transaction, the customer purchases the chattel by paying the entire consideration to the dealer with the help of financier, and then he will enter the hire- purchase agreement with the financier, by way of a loan transaction.

A contract of sale is distinct from a contract of hire purchase. A contract of hire-purchase is, appropriately speaking, a contract of hire by which the hirer is granted an option to buy, but is not, as under a contract of sale, under a legal obligation to do so. The contract of hire-purchase is one of the variations of the contract of bailment, but it is a modern advance of mercantile life, and the rules with regard to bailment, which were laid down before any contract of hire-purchase was contemplated, cannot be applied simpliciter, because such a contract has in it not

only the constituent of bailment but also the element of sale.<sup>517</sup>

There can be two types of hire purchase contracts. Firstly, the contract of hire conferring an option to purchase and secondly contracts which are in reality agreement to purchase by instalments, subject to a condition that the property is not to pass until all instalments have been paid<sup>518</sup>. In the latter case, a most important distinction is that there is a binding obligation on the hirer to buy and the hirer can therefore pass a good title to a stranger to the hire-purchase contract.

The distinguishing feature of a typical hire-purchase agreement is that the property does not pass when the agreement is made but only passes when the option is finally exercised after complying with all the terms of the agreement<sup>519</sup>. The element of sale fructifies when the option is exercised by the intending purchaser after fulfilling the terms of agreement. As a result, when all the terms of

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<sup>517</sup> *The Instalment Supply Ltd. v. Sales Tax Officer*, [1974] 34 STC 65.

<sup>518</sup> *Halsbury's Laws of England*, 3<sup>rd</sup> edn. Vol.19, at pp. 510 - 511.

<sup>519</sup> *Johar & Co. v. Commercial Tax Officer*, [1965] 16 STC 213 (SC).

agreement are satisfied and the option is exercised then only a sale takes place of the goods which till then had been hired<sup>520</sup>. Pointing out the said legal proposition, in *Johar's case*<sup>521</sup>, the Hon'ble Supreme Court held that when the taxable event is the sale of goods, sales tax can be levied when the option is exercised after fulfilling all the terms of the hire-purchase agreement and that till the sale takes place there cannot be any liability of sales tax in cases of hire-purchase agreement.

The State legislature is not empowered to levy sale tax on the hire-purchase transactions, treating it as sale<sup>522</sup>. However the Supreme Court held in a case that even if hire-purchase agreement lacks the elements of sale of goods in its general sense, by virtue of inherent and residuary power to levy tax, the Parliament of India is justified in levying sales tax on hire-purchase transactions.<sup>523</sup> When the customer purchased vehicle directly from the dealer and obtained advance from the

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<sup>520</sup> *Ibid.*

<sup>521</sup> *Ibid.*

<sup>522</sup> *Ibid.*

<sup>523</sup> *Instalment Supply Ltd. v. Union of India*, [1961] 12 STC 489 (SC).

financer against the security of the vehicle, it was held that the transaction between the financer and the dealer is not sale<sup>524</sup>.

One of the significant features of the hire-purchase agreement is that the retention of title as the security for the amount paid<sup>525</sup>. When a vendor agreed to hire the chattel on payment of such instalments for the hire and until certain amounts are paid, the chattel were to become again the property of the vendor and this power was given to take possession of the chattel on default of payment. Only because of the retention of title as the security, a loan transaction cannot be termed as sale<sup>526</sup>.

### **5.19. Conclusion.**

It is a recognised rule of interpretation of statutes that the expressions used therein should ordinarily be understood in a sense in which they best harmonise with the object of the statute, and which effectuate the object of

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<sup>524</sup> *Sundaram Finance Ltd v. State of Kerala*, [1966] 17 STC 489 (SC).

<sup>525</sup> *In Re Watson, Ex parte Official Receiver in Bankruptcy*, [1890] 25 QBD 27.

<sup>526</sup> *Mass v. Pepper*, [1905] AC 102.

the Legislature. If an expression is susceptible of a narrow or technical meaning, as well as a wider popular meaning, it would be justified in assuming that the legislature used the expression in the sense which would carry out its object and reject that which renders the exercise of its powers invalid.

Thus, the Courts in India usually accept the narrow and technical concept of sale which justify the restricted meaning of 'sale' and discarded the extended meaning, which even supports the view that a sale includes transaction in which the property is transferred for consideration from one person to another without any previous contract of sale, which is one of the essential elements<sup>527</sup>. Furthermore the Rajasthan High Court in one of its illuminated decision in *Rajasthan Chemists Association v. State of Rajasthan*<sup>528</sup> held that even after insertion of extended scope for the definition of sale in Article 366 (29A) it includes certain transactions within its ambit, which had otherwise been held to be not falling

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<sup>527</sup> Majority view of Kapur and Shah, JJ in *New India Sugar Mills Ltd. v. Commissioner of Sales Tax*, [1963] 14 STC 316.

<sup>528</sup> [2006] 147 STC 475 (Raj).

within the precincts of sale of goods. The Court clarified the position that beyond that the principle still remains the same that the term “sale of goods” has the same meaning as “sale” defined in the Sale of Goods Act, 1930. The Apex Court in *State of Rajasthan v. Rajasthan Chemists Association*<sup>529</sup> has affirmed this view.

When under the statutes dealing with, taxation of sale, the subject of tax being sale, measure and levy of tax must retain nexus with sale, which has its general meaning under the Sale of Goods Act, 1930. The extended meaning of sale, such as “deemed sale”, has its limited application in terms of changes made in the Constitution by introducing the 46<sup>th</sup> Amendment Act, and not further.

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<sup>529</sup> [2006] 147 STC 542 (SC).

## CHAPTER VI

# Deemed or Fictional Sale: Evolution of the Concept

Sale in its strict sense is the consensual transaction that is defined in the Sale of Goods Act, 1930. However, in taxing statutes a wider meaning is imputed to the sale. Every sale under the Sale of Goods Act is certainly a sale under the General Sales Tax Act, but every sale under the General Sales Tax Act may not be strictly within the definition of the term 'sale' in the Sale of Goods Act<sup>530</sup>.

### 6.1. Departure from Laissez Faire.

The concept of sale has undergone a revolutionary change, having regard to the complexities of the modern times and the expanding needs of the society, which has made a departure from the doctrine of laissez faire<sup>531</sup> by including a transaction, which are not sale in its ordinary

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<sup>530</sup> Govinda Menon, J, *In re Jayaram Chettiar*, [1951] 1 STC 168 (Mad.) at p. 171.

<sup>531</sup> *Bhopal Sugar Industries Ltd. v. Sales Tax Officer*, [1977] 40 STC 42 (SC).

and popular meaning. Accordingly it was interpreted that sale for taxing purpose must be given widest possible meaning rather than technical meaning found in the Sale of Goods Act<sup>532</sup>.

## **6.2. Curative Amendment in the Constitution.**

The ever-large debates on tax avoidance in trade had resulted to the 46<sup>th</sup> Amendment to the Constitution of India, which amended the definition clause in Article 366 by the injection of Clause 29A. The said clause happened to be the part of the Constitution, right from the year 1984 widening the definition of sale irrespective of its traditional meaning approved in the Sale of Goods Act, 1930. The 46<sup>th</sup> Amendment<sup>533</sup> to the Constitution of India expanded the

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<sup>532</sup> *United Motors v. The State of Bombay*, [1953] 4 STC 10 at p. 22 (Bom.).

<sup>533</sup> Section 4 of the Constitution (Forty-Sixth Amendment) Act, 1982 introduced a new clause (29A) in Article 366.

Article 366 (29A) reads, “Tax on the sale or purchase of goods” includes-

- (a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;
- (b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;

meaning of sale by attributing an inclusive definition to the concept of sale.

To begin with, the Madras High Court<sup>534</sup> deviated from the traditional notion that supports a strict interpretation of sale in Sales Tax Act also. As per the Court, a transfer of property in any goods for cash, deferred payments or other valuable consideration when such transfer takes place otherwise than in pursuance of contract is a sale. If a person transfers the property in goods to another in the course of trade or business for

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- (c) a tax on the delivery of goods on hire-purchase or any system of payment by instalments;
  - (d) a tax on the 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;
  - (e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;
  - (f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration,

and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made.

<sup>534</sup> *In re Jayaram Chettiar*, [1951] 1 STC 168 (Mad.).

other valuable consideration it is a sale under the sales tax Act, though it lacks the characteristics of sale under the Sale of Goods Act<sup>535</sup>.

### **6.3. Issues in Execution of Works Contract.**

Generally, the transfer of property while carrying out works contract, either construction contract or contract of labour, did not consider as sale for the purpose of taxation. Several other deals like transfer of goods while executing a hire purchase or instalment arrangements, supply of foods in restaurants and canteens, transfer of right to use goods while executing the service or other contracts were also out of the tax net. The familiar view of the Courts in India was that mere passing of property in an article or commodity during the course of the performance of the transaction does not render the transaction as sale<sup>536</sup>. Even in a contract, purely of work or service, there are circumstances that articles or commodities may have to be used by the

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<sup>535</sup> *Id.* at p. 171.

<sup>536</sup> *State of Himachal Pradesh v. Associated Hotels of India Ltd.*, [1972] 29 STC 474 (SC).

person executing the work and the property in such article or materials may pass to other party.

Now, of course, the law has subjected to substantial changes. A transfer of property in goods involved in execution of works contract is a sale, after the 46<sup>th</sup> Amendment. The hire purchase or instalment transactions, transfer of right to use goods and supply of goods by any unincorporated association or body of persons to its member for valuable consideration etc are also included in the definition of sale as deemed sale<sup>537</sup>.

When the law creates the legal fiction, such fictions are amenable to populace. A transfer of property occasioned during the execution of works contract is a deemed sale. It is irrespective of the subject matter of the works contract, that is, either a contract of building, road or bridge construction or a contact of movables like motor vehicles, ships etc<sup>538</sup>.

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<sup>537</sup> *Supra*, n. 533.

<sup>538</sup> *Builders Association of India v. Union of India*, [1989] 73 STC 370 (SC).

#### **6.4. Is Works Contract differing from Sale?**

How far a sale is different from works contract was relevant at least in the pre-46<sup>th</sup> Amendment period. There are apparent differences in a sale and works contract. In sale of goods the things sold being more important, however, in works contract the skill of the persons entrusted with the work is vital. The payment for such services is much significant than the value of things transferred during the works. The primary test in between a contract of sale or contracts for work and labour is whether the contract is one whose main object is transfer of property in chattel as a chattel to the buyer, though some work may be required to be done under the contract as ancillary or incidental to the sale or its carrying out of work by bestowal of label and service and materials are used in execution of such works<sup>539</sup>.

Works done on a customer's chattel is a works contract, in its simplest meaning. It depends on the nature of chattel or holding of chattel. Whether works are done in

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<sup>539</sup> *Ram Singh & Sons Engineering Works v. Commissioner of Sales Tax*, [1979] 43 STC 195 (SC).

one's own chattel or of some other's is the criteria for deciding its nature. When works are done in one's own chattels and subsequently transferred to another, it is a sale of goods. However, if, works are done in a customer's chattel, of course it is nothing but a works contract.<sup>540</sup>

When and how the materials used by a contractor passes to its customer is an important factor to test the nature of a contract<sup>541</sup>. If it is a transfer at the time of delivery of finished article as a chattel, it is a sale. If it is during the process of work on affixture of fusion to the movable property of the customer it is a works contract<sup>542</sup>. Thus a contract for execution of fireworks does not include the transfer of property in goods<sup>543</sup>.

## **6.5. Theory of Accretion.**

The concept of addition, accretion or accession to goods belonging to persons other than the contractor is

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<sup>540</sup> *SV Motor Co. Ltd v. State of Mysore* [1964] 15 STC 771 (Mysore).

<sup>541</sup> *Commissioner of Sales Tax v. Purushotham Premji*, [1970] 26 STC 38 (SC).

<sup>542</sup> *T.V.Sundaram Iyyengar & Sons v. State of Madras*, [1970] 25 STC 160 (Mad). This decision was affirmed in *T.V.Sundaram Iyyengar & Sons v. State of Madras*, [1975] 35 STC 24 (SC).

<sup>543</sup> *Deputy Commissioner v. Velu*, [1993] 89 STC 40 (Ker.).

essential to form a works contract. Once it is held that property in goods used in the execution of the works contract passes incidentally or by theory of accretion, such passing, though not a sale in general sense, would be deemed sale in its extended meaning<sup>544</sup>.

An important ingredient of deemed sale by way of transfer of property in goods involved in the execution of works contract is supply of goods. Mere processing, treating or adapting is not sufficient. There should be supply of some goods in the course of such processing, treating or adapting resulting in transfer of property in those supplied goods. Such transfer should be from the contractor to the contractee.

The goods involved in a works contract cannot be regarded as appropriated to the contract, or as sold, unless these have been affixed to or made part of the corpus. Affixation or becoming a part of the corpus is the essence of deemed sale. The transfer of property by accession

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<sup>544</sup> *Commissioner of Sales Tax v. Matushree Textiles Ltd*, [2003] 132 STC 539.

inheres in deemed sale in a works contract and is an essential element<sup>545</sup>.

The test to identify the nature a works contract is that a contract by which one person promises to make something, which when made, will not be his absolute property, and by which the other person promises to pay for the work done, is a contract of work, although the payment may be called a price for the thing and although the materials, of which the thing is made, may be supplied by the maker<sup>546</sup>.

In its traditional concept, a sale is taxable if the goods in consideration are movable and sale is for a price subject to passing of property in pursuance of an agreement, either oral or written. In a contract for construction of building, it is entire and indivisible. The very fiction of sale is that the seller divests himself of all proprietary rights in the thing sold in favour of the buyer<sup>547</sup>.

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<sup>545</sup> *Appleby v. Myers*, 1867 LR (2) CP 651.

<sup>546</sup> *South India Corporation (P) Ltd v. Secretary, Board of Revenue*, 1961 KLT 782 (FB) (Ker.).

<sup>547</sup> Dezalute, *The Roman Law of Sale* at pp. 15 & 16.

In works contract the payee divests his skill and labour for a price consideration.

In the case of contract for sale the thing produced as a whole has individual existence as the sole property of the party who produced it, at the same time before delivery and the property therein passes only under the contract relating thereto to the other party for a price.

### **6.6. Theory of Dominant Intention.**

Whether a contract is one for purely sale of goods or for executing works or rendering services is largely on facts, depending upon the terms of the contract, including the nature of obligations to be discharged there under<sup>548</sup>. The nature of the transaction may vary depending on the output of the contract, as in the case of stitched suit or completed oil painting.<sup>549</sup> If the final product is regarded as separate goods belonging to the manufacturer and the property in the said final product remains with the manufacturer/ supplier at the time of its delivery, it is a sale

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<sup>548</sup> *Union of India v. Central India Machinery*, [1977] 40 STC 246 (SC) at p. 267.

<sup>549</sup> *Robinson v. Graves*, [1935] 1 KB 579.

of goods. But if the property in the materials used and also in the ultimate product remains with the person placing the order, it is a works contract.<sup>550</sup>

This view was reiterated by the Bombay High Court in *Maharashtra Mudran Parishad v State of Maharashtra*<sup>551</sup> where in it was held that in each case the nature of the contract and transaction has to be seen. This is possible only when the intention of the parties that too dominant intention is found out. The fact that in the execution of the contract for work some materials are used, and the property/goods so used, passes to the other party, the contractor undertaking to do the work will not necessarily be deemed, on that account, to sell the materials.

Whether or not and which part of the job-work relates to that depends as mentioned hereinbefore, on the nature of the transaction and what is the dominant intention has to be found in each case in the light of its own facts. Even if the dominant intention of contract is the provision of

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<sup>550</sup> *State of Gujarat v. Variety Body Builders*, [1976] 38 STC 176 (SC).

<sup>551</sup> [2005] 139 STC 193.

service, once there is a transfer of property within it, that property would be liable to payment of sales tax<sup>552</sup>.

## **6.8. Kinds of Works Contract.**

The performance of a works contract may be varying, subject to the conditions and actions. There may be different kinds of works contract like,

- i. A works contract to do all works subject to a lump sum payment of consideration.
- ii. A works contract to do all works subject to deferred payments for different parts of works.
- iii. A works contract without any pre conditional payments.
- iv. A works contract to do whole works for a price to be ascertained.

In the *Builder's Association case*<sup>553</sup>, the Supreme Court attempted to enumerate the kinds of works contract. Firstly, the work is done by the contractor on the property of the customer using the materials of the contractor, as in the case of construction contracts. Secondly, the property of

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<sup>552</sup> *Commissioner of Sales Tax v. Hari & Co*, [2006] 148 STC 92 (Bom.).

<sup>553</sup> *Builder's Association of India v. Union of India*, [1989] 73 STC 370 (SC).

the customer is given to the contractor for carrying out improvement thereon, as in the case of rethreading of tyres etc., Thirdly the customer passes his property in unprocessed form for a better and effective out put, as in the case of customer supplying negatives of films for developing and printing of positive copies by a contractor.

Normally a contractor does not transfer the materials used in the construction work as a commodity and therefore it could not be treated as a sale of the materials. There is no sale of materials and no contract of sale of materials. In certain works contract the sale of specified goods is divisible, that there shall be a separate agreement to transfer of materials in the form of goods for the price of the goods. An agreement to avail the service by way of labour is a secondary one in such contracts. The agreement between the parties is one to do a certain works and to supply certain materials and not an agreement for sale or delivery of the goods by way of sale<sup>554</sup>. However, the concept of “cost- plus contract” introduced in United

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<sup>554</sup> *Sydney Hydraulic & General Engineering Co v. Blackwood & Sons*, 8 NSWSR 10 (SC), referred in *Irvings Common Wealth Sales Tax Law & Practice*, (1950) at p. 7.

States as discussed in *Alamba v. King*<sup>555</sup>, says that even in a construction contract there is a distinction between the cost of the goods and the contract charges and it can be presumed that the cost of the materials be subject to taxation, as there is sale of goods.

### **6.9. Evolution of the Concept of Deemed Sale.**

The classical dictum laid down by the apex court in *Gannon Dunkerley's case*<sup>556</sup> settled the pre-amendment proposition of laws on works contract. The debate started when the State of Madras enlarged the definition of sale by enacting the Amendment Act in 1947. A transfer of property in goods involved in the execution of works contract was included in the definition of sale. The company, an assessee under the Sales Tax Act, carrying on business of execution of construction of building, roads, dams and bridges was assessed under the local Sales Tax Act levying sales tax on the turnover after deducting labour component. The debatable question was whether the

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<sup>555</sup> 314 U S 1.

<sup>556</sup> *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.): AIR 1954 Mad. 1130.

transfer constitutes sale of goods from the contractor to the awardee.

The sales tax assessment on the building contractors under the amended provision was challenged before the Madras High Court<sup>557</sup>, where it was held that the building contracts do not involve any element of sale of materials and so not in any sense a contract for sale of goods as understood in the law. In the same line, the High Court of Hyderabad<sup>558</sup> also held that in works contract where a person undertook to build a particular building or thing there couldn't be any sale of materials involved in making of the finished product, because there was no agreement to sell the materials nor was the price of the goods fixed.

### **6.10. Significance of *Gannon Dunkerley*.**

The core factor of the decision of the Madras High Court<sup>559</sup> was that while drafting the Constitution Act, 1935

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<sup>557</sup> *Ibid.*

<sup>558</sup> *Jubilee Engineering Co. Ltd v. Sales Tax Officer*, [1956] 7 STC 423 (Hyd.).

<sup>559</sup> *Supra*, nn. 556 & 557.

and the corresponding Entry 48, the draftsman must have intended to define the power of legislature to tax only the transaction of sale of goods, which was understood in law as meaning and as constituting those composite series of acts beginning with agreement of sale and ending with transfer of property for price, which constitute sale of goods. Accordingly, considering the sale defined in the Sale of Goods Act, 1930 and the Sale of Goods Act, 1893 (England), the Court held that the sale of goods being an incident for taxation cannot be interpreted beyond its meaning as defined in the General law.

It was also observed by the Court<sup>560</sup> that in a works contract, the property in the materials passes to the owner of the land not by virtue of the delivery of the materials as goods under and in pursuance of an agreement of sale, which stipulates a price for the materials. But the property in the materials passes to the owner of the land because they are fixed in pursuance of the contract to build, and along with the corpus, which ultimately results by the

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<sup>560</sup> *Id.* at p 238.

erection of the superstructure, the materials also pass to the owner of the land.

Conversely, in an identical case, the Kerala High Court<sup>561</sup> held that the building contracts are taxable and upheld the rules providing for apportionment and the determination of the taxable turnover on a percentage basis of materials used and labour employed. As well, identical issues were decided by the Mysore High Court<sup>562</sup>, Rajasthan High Court<sup>563</sup> and Nagpur High Court<sup>564</sup> against the assessee, declining to follow the ratio of Madras High Court<sup>565</sup> and held that determination of taxability of works contract, by picking out a sale from composite transaction of building contract is justified as there is transfer of property in materials and to the extent of the portion attributable to the cost of the materials the levy is legal.

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<sup>561</sup> *Gannon Dunkerley v. Sales Tax Officer*, [1957] 8 STC 347 (Ker.).

<sup>562</sup> *Mohamed Khasim v. State of Mysore*, [1955] 6 STC 211 (Mys.).

<sup>563</sup> *Bhuramal v. State of Rajasthan*, [1957] 8 STC 463 (Raj.).

<sup>564</sup> *Pandit Banarsi Das v. State of Madhya Pradesh*, [1955] 6 STC 93 (Nag.)

<sup>565</sup> *Supra*, n. 559

The justification for the contra view in *Pandit Banarsi Das's case*<sup>566</sup> is that when Entry 48 was framed, it conferred on the Provincial legislature powers of the widest amplitude to tax the sale of goods in all its aspects and forms. It is observed that the necessary conditions for the impost were that there should be a sale of goods and the selection of the taxable event and the severance of transactions of sale from other transactions in which they might be embedded was a necessary part of the power.

The matter went in appeal before the Apex Court<sup>567</sup> and the decision of the Madras High Court was affirmed. It was held that on a true interpretation of the expression 'sale of goods' it can only be understood that an agreement between the parties for the sale of the same goods in which eventually property passed. The Court added that in a building contract there is only an agreement between the parties and the contractor that the latter should construct the building according to the plan and specification

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<sup>566</sup> *Pandit Banarsi Das v. State of Madhya Pradesh*, [1955] 6 STC 93 (Nag.) at para 25

<sup>567</sup> *State of Madras v. Gannon Dunkerley*, [1958] 9 STC 353 (SC).

contained in the agreement and in consideration thereof and there was neither a contract to sell the materials used in the construction nor the property passed therein as movables.

The decision so rendered became final as the main dispute arose in *Gannon Dunkerley's*<sup>568</sup> was with regard to power of the State legislature to enact the law under Entry 54 of the State List in 7<sup>th</sup> Schedule. Alternatively, in *Mithan Lal and Others v. State of Delhi*<sup>569</sup>, the Apex Court examined the legality of the legislation enacted by Parliament for Part C States and held that the taxing of supplied materials while executing a construction contract is taxable.

### **6.11. Criticism of *Gannon Dunkerley*.**

It is a matter of fact that by the subsequent decision in *Mithan Lal's case*<sup>570</sup>, the Apex Court categorically clarified that while deciding the *Gannon Dunkerley's*<sup>571</sup>, the

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<sup>568</sup> *Ibid.*

<sup>569</sup> [1958] 9 STC 417 (SC).

<sup>570</sup> *Ibid.*

<sup>571</sup> *Supra*, n. 567

Court answered to the mooted question of the legislative competence only and not the wider question of expansion of scope of sale under the head of deemed sale.

Even if in *Gannon Dunkerley's case*<sup>572</sup> any restrictions were imposed by the Hon'ble Apex Court, it was only with respect to an indivisible or composite contract. Even after the decision, it is quite possible to assume a real sale where a contract entered into in connection with the construction of a building consisted of two parts. That is the first one is relating to the sale of materials used in the construction of the building by the contractor to the person who had assigned the contract and second one is dealing with the supply of labour and services. Sales tax is leviable on the goods, which were agreed to be sold under the first part of the contract<sup>573</sup>.

In a construction contract, the agreement between the parties is for the construction of the building or execution of the works according to the plans and

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<sup>572</sup> *Ibid.*

<sup>573</sup> *Builders Association of India v. Union of India*, [1989] 73 STC 370 (SC), AIR 1989 SC 1371.

specifications mentioned therein and in consideration thereof, receive payments provided for in it. Neither there is a contract to sell the materials used or consumed in the course of construction nor did the property over those materials pass to other party as movables.

In an agreement of the builders with the allottees, what the builder agrees is to sell the flat or apartment at a particular price and the undivided share in the land is transferred by a separate deed of assignment. It does not become a contract relating to sale of goods, but it is only a contract to build<sup>574</sup>. A works contract relating to building contract has multi optional phase, that is, it can be through a contract to build the structure in the awardee's own property or to build the structure in the property of the allottee. The passing of title and holding of title of the land property is relevant to decide its impact. In the former, it is sale of immovable property<sup>575</sup> and in the latter; it is a labour contract only.

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<sup>574</sup> *Supra*, n. 567.

<sup>575</sup> *SV Motor Co. Ltd v. State of Mysore* [1964] 15 STC 771 (Mysore).

It is obvious that in works contract the material that was supplied for construction or execution of contract merges in the immovable property and its value has to be apportioned for the purpose of taxation, treating the transfer as deemed sale. Thus the meaning of sale in the Sales Tax Statutes can neither be confined nor limited to the general meaning of that expression as understood in the Sales of Goods Act<sup>576</sup>.

In the case of composite contract, where the sale of goods is not separable or severable, no sale could have been carried out. However there could be distinct and severable contracts, one for the transfer of goods and other for rendering services, the former was held as sale subject to local taxation.<sup>577</sup> Thus the works contract, in general, is asserted as the deemed sale not in its composite form but in its separable form, in the pre- 46<sup>th</sup> Amendment period.

In an English case the Court held that if one orders another to make and fix curtains at his house the contract is

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<sup>576</sup> *Mohamed Kashim v. State of Mysore*, [1955] 6 STC 211.

<sup>577</sup> *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.): AIR 1954 Mad. 1130.

one of sale, though the work and labour is involved in the making and fixing<sup>578</sup>. The Court of Appeal annulled the contention that the contract is only for executing a work with service and not a sale. Though the contract is for making and fixing the curtains, the real effect of the contract is the transfer of property in the forms of curtain cloths and accessories to the awarder by the contractor that is noting but a sale for consideration. It is the primary object of the transaction and intention of the parties to enter in a contract are relevant factors to decide the nature of a sale<sup>579</sup>.

In contra, it was held that a contract for providing and fixing different types of windows of certain sizes according to the specification, designs, drawings and instructions set out in the contract, is a contract for work and labour and not a contract for sale<sup>580</sup>. When a contract stipulates that the equipment supplied was required to be erected and fitted at the site of the customer and the equipment, as such, a unit

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<sup>578</sup> *Love v. Norman Wright (Builders) Ltd*, [1944] All ER. 618.

<sup>579</sup> *State of H.P. v. Associated Hotels*, [1972] 29 STC 474 (SC) at p.481.

<sup>580</sup> *State of Rajasthan v. Man Industrial Corporation*, [1969] 24 STC 349 (SC).

came into existence only after its erection and commission, there cannot be a transfer of property in the goods by the manufacturer to the customer as a chattel and the contract is only for works and not for supply of goods<sup>581</sup>. It was also held that fabrication and supply of doors, windows, shutters etc. amounts to works contract and not sale of goods<sup>582</sup>.

### **6.12. Sale Element in Service or Labour Contracts.**

A contract to supply the dehydrated meat packed in containers to the Government of India is held as a sale discarding the claim of the contractor that there is no sale, only labour contract<sup>583</sup>. The Government provided the contractor the plant and machinery; a supplier as per the terms agreed between the supplier and the Government supplied the dressed meat. Though there is delivery of property in between the parties, the contractor claimed that no transfer of ownership over property occasioned that the

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<sup>581</sup> *RR Engineering v. Commissioner of Sales Tax*, [2008] 11 VST 353 (All).

<sup>582</sup> *Joseph Technical Institute v. State of Tamil Nadu*, [1993] 90 STC 27 (Mad.).

<sup>583</sup> *Mohammad Amin Bros. v. Province of Bihar*, [1951] 2 STC 55 (Pat.) at p. 61.

contractor was only entrusted to labour with cost of service. However the court found that as per the terms of the original contract, the contractor is entitled to receive the full payment from the Government according to the fixed scale for the dehydrated meat including the cost of packing and the contractor is paying to the supplier the cost of dressed meat out of the payment. Hence there is no compass to conclude the nature of contract as labour.

Similarly, when the contractor paid the seigniorage fee for extraction of the boulders, even according to the quarries specified by the Government, there may not be a sale. However, after extraction of the boulders, it becomes the property of the contractor, which he used in to the roadwork, particularly after resizing it and there is sale exigible to sales tax<sup>584</sup>. While considering a similar issue, whether there was sale of goods in view of the contract between the parties where under the custody and control of the goods remained with Government Department and goods were only used in the construction under the

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<sup>584</sup> *Seenaih & Co. v. Commercial Tax Officer*, [2001] 124 STC 248 (Andhra).

Contract, the Madhya Pradesh High Court held that by use or consumption of materials in the work, there is a passing of property in goods and there is a sale<sup>585</sup>. This view was affirmed in *N.M. Goel & Co. v. Sales Tax Officer*<sup>586</sup>, by the Supreme Court, and held that in order to be taxable, not only the property in goods should pass but with an independent contract of sale, which is separate and distinct.

When the contractor uses or consumes the materials in work of construction, there is passing of property and by virtue of receipt of value of such transferred property, of course, by way of adjustment in the award bill, the consideration has also passed over to treat the transaction as sale<sup>587</sup>. The Supreme Court in *CPWD's case*<sup>588</sup> reconfirmed this view by holding that the materials transferred by the CPWD to sub contractors and by

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<sup>585</sup> *N.M. Goel & Co. v. Sales Tax Officer*, [1989] 72 STC 368 (MP) (FB).

<sup>586</sup> [1989] 72 STC 375 (SC).

<sup>587</sup> *Rashtriya Ispat Nigam Ltd v. State of Andhra Pradesh*, [1998] 109 STC 425 (SC).

<sup>588</sup> *Karya Palak Engineer, CPWD v. Rajasthan Taxation Board*, [2004] 136 STC 641 (SC).

adjustment of price of materials in the bill; there is sale exigible to local sale tax.

It is immaterial that contractor consumed the Cement and Iron supplied by the Government for executing the public work. There is a deemed sale when the supply of materials to the contractor for agreed price as per the terms of agreement<sup>589</sup>. But, when the difference between the price of a coach and the cost of material could only be the cost of service rendered, as if the entire materials used in the construction belonged to the awarder, there could not be a sale, but a contract of works only<sup>590</sup>.

When an item is made under an order of the customer, usually called as a 'custom-made article' and sold as such, the same amounts to sale of a chattel as a chattel<sup>591</sup>. While fabricating a bus body and fixing on the chassis, can only be sale, not the contract of works as

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<sup>589</sup> *Hardeo Singh v. State of Bihar*, [2004] 137 STC 497 (Jhar.) (FB).

<sup>590</sup> *Commissioner of Commercial Taxes v. Hindustan Aeronautics*, [1972] 29 STC 438 (SC).

<sup>591</sup> *C.C. Sebastian v. State of Kerala*, [2007] 8 VST 798 (Ker.).

there is transfer of property in goods, explicitly<sup>592</sup>. The property in the materials used by the builder in constructing a bus body never passed to the customer during the course of construction but it would pass to the customer only when the complete bus with the body fitted to the chassis was delivered to him<sup>593</sup>.

If the parties intended that there should be delivery of bus bodies as units, or as bus bodies though fitted to the chassis that will be a case where the property passes only at the time of delivery and such a transaction will be sale of goods<sup>594</sup>. If the property in the materials used in the process of bus bodybuilding passes to the customer who supplied the chassis the moment the materials are affixed to the chassis it will be a contract for work and labour<sup>595</sup>.

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<sup>592</sup> *T.V.Sundaram Iyyengar & Sons v. State of Madras*, [1975] 35 STC 24 (SC)

<sup>593</sup> *T.V.Sundaram Iyyengar & Sons v. State of Madras*, [1970] 25 STC 160 (Mad). This decision was affirmed in *T.V.Sundaram Iyyengar & Sons v. State of Madras*, [1975] 35 STC 24 (SC).

<sup>594</sup> *Commissioner of Sales Tax v. Haji Abdul Majid*, [1963] 14 STC 435 (All.).

<sup>595</sup> *City Motor Service Pvt Ltd. v. State of Madras*, [1968] 22 STC 485 (Mad.).

In case of photocopying, as far as paper and ink are concerned, which are passed on, there is transfer of property to make the transfer, taxable being a deemed sale<sup>596</sup>.

When a printing press itself purchased stationary and did printing work upon it according to the orders of the individual customers and supplied the printed stationary to the customers at an agreed price the transaction is a pure sale and not a mere works contract<sup>597</sup>.

The goods prepared by the contractor which could not be exhibited for sale to the public is not decisive of the issue. It is also immaterial to say that the question paper after being printed are neither available commercially nor available to any community other than the candidates appearing at a particular time in an examination<sup>598</sup>. Even if the product is made to suit a particular customer, it cannot

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<sup>596</sup> *Commissioner of Sales Tax v. Hari & Co.*, [2006] 148 STC 92.

<sup>597</sup> *State of Andhra Pradesh v. Sri Krishna Power Press*, [1960] 11 STC 498 (Andhra).

<sup>598</sup> *State of Tamil Nadu v. Anandam Viswnathan*, [1989] 73 STC 1, (Mad.).

be treated as works contract, but only sale of goods as the price is charged on piece rate<sup>599</sup>.

While interpreting the contract, the clause relating to payment of price can be a decisive factor<sup>600</sup>, but mode of billing alone could not be a conclusive evidence of separate contract<sup>601</sup>. If the bulk of the material used in the construction belongs to the manufacturer, who sells the end-products for a price that will be a strong pointer to the conclusion that the contract is in substance one for the sale and not one for work and labour<sup>602</sup>.

If the substance of the contract is the production of something to be sold to the customer then there is sale of goods. If, on the other hand, the substance of the contract is that skill and labour have to be exercised for production of the article, and that it is only ancillary to that there will pass to the customer some materials in addition to the skill

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<sup>599</sup> *Johny v. State of Kerala*, [2007] 10 VST 19 (Ker.).

<sup>600</sup> *Patnaik and Co. v. State of Orissa*, [1965] 16 STC 364 (SC).

<sup>601</sup> *State of Madras v. Champion Motor Works*, [1974] 34 STC 338 (Mad.).

<sup>602</sup> *Union of India v. Central India Machinery Manufacturing Co. Ltd*, [1977] 40 STC 246 (SC).

involved, it is no doubt a contract of works or labour<sup>603</sup>. When it is established that the works carried out is manufacturing, the supply of the output is nothing but a sale and there is no contract of works or labour<sup>604</sup>. The decisive element in determining whether a particular deal is sale or works contract is the passing of the property in the manufactured product<sup>605</sup>.

### **6.13. Element of Sale in Photography Service.**

In *Kame's case*<sup>606</sup>, the Hon'ble Apex Court enumerated three kinds of photographic services rendered by a photographer and held that while taking a photograph, developing in to negative and taking photo prints for the customer, the photographer uses his artistic talent or skill which is required to take good photograph. Such kind of artistic skills are held not to result to sale of photographs to customers.

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<sup>603</sup> *Kanpur Journals Ltd v. Commissioner of Sales Tax*, [1956] 5 STC 661 (All).

<sup>604</sup> *Sardar Printing Works v. Sales Tax Commissioner*, [1958] 9 STC 75 (MP).

<sup>605</sup> *State of Gujarat v. Variety Body Builders*, [1976] 38 STC 176 (SC).

<sup>606</sup> *Assistant Sales Tax Officer v. B.C. Kame*, [1977] 39 STC 237 (SC). In this decision the Supreme Court affirmed the judgment in *B.C. Kame v. Assistant Sales Tax Officer*, [1971] 28 STC 1 (M.P.).

However regarding other two kinds, collecting negatives from the customers and enlarging in to different sizes or taking positive prints of same sizes from the negatives supplied by the customer, though the Hon'ble Kerala High Court in *Baven's case*<sup>607</sup> held that to the extent of value of the photographic paper, there is passing of property in the execution of works contract and there is a deemed sale exigible to sales tax. Such contracts cannot be termed as simply service contracts, as the artistic talent or skill which is required to take a good photograph is already invested by someone other than the contractor and he is only doing the processing work on the exposed film or the negative supplied by the customer which is purely a works contract<sup>608</sup>.

Distinguishing the declaration in *Rainbow Colour Lab's case*<sup>609</sup>, the Gauhati High Court<sup>610</sup> held that when a composite contract is made by the photographer that

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<sup>607</sup> *Bavens v Union of India*, [1995] 97 STC 161 (Ker.).

<sup>608</sup> *Classic Colour Lab v. Deputy Commissioner*, [1998] 110 STC 269 (Kar.).

<sup>609</sup> *Rainbow Colour Lab v. State of Madhya Pradesh*, [2000] 118 STC 9 (SC).

<sup>610</sup> *Live Tone v. State of Tripura*, [2001] 122 STC 115 (Gah.) at p. 123.

having not charging separate price for the materials passed to the customer and charge for his artistic skills, only available method is to treat the entire thing as deemed sale exigible to sale tax. In *Johny Joseph v. State of Kerala*<sup>611</sup>, the Kerala High Court after examining the precedents on the subject cleared out the controversy and held that enunciation of law in *Associated Cement Company's case*<sup>612</sup> which had been confirmed in *Bharat Sanchar Nigam Ltd's case*<sup>613</sup> fully settled the issue finally that activity of taking photographs and developing and printing films constitutes works contract and transfer of goods involved in the execution is liable to be taxed being it a deemed sale.

Likewise, while dyeing or bleaching and printing the contractor uses colours, dyes and chemicals, the goods that are eventually passed to the customer along with the finished product, it was held that accretion of coloured shade or chemicals on the fabrics during the process of

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<sup>611</sup> *Johny Joseph v. State of Kerala*, [2008] 13 VST 64 (Ker.).

<sup>612</sup> *Associated Cement Companies Ltd v. Commissioner of Customs*, [2001] 124 STC 59 (SC):2001 (4) SCC 593.

<sup>613</sup> *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 145 STC 91 (SC).

dyeing and printing represents the form of the goods used in the process and there is a transfer of goods within the meaning of deemed sale<sup>614</sup>.

After the 46<sup>th</sup> Amendment, to constitute a sale the test is whether the materials used in the execution of a works contract pass to the contractee either in its original form or in some other form?. If it passes, then there is a deemed sale of the materials used in the execution of the works contract even if there is no specific agreement between the parties for sale of materials, even if the price for such sale is not agreed between the parties and even though the materials are not delivered as materials<sup>615</sup>. This is a view far away from the traditional notion given to the concept of sale.

However, the Patna High Court<sup>616</sup> raised a mootable point to say that even after the 46<sup>th</sup> Amendment to the Constitution, the emphasis is on the transfer of property in goods, whether as goods or in some other forms, to mean

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<sup>614</sup> *Commissioner of Sales Tax v. Matushree Textiles Ltd*, [2003] 132 STC 539 (Bom) at. 561.

<sup>615</sup> *Ibid*.

<sup>616</sup> *Pest Control India Ltd v. Union of India*, [1989] 75 STC 188 (Pat.).

that goods existed shall be transferred to the other party either in its original form or in some other form and if the goods do not exist in any form whatsoever and are consumed in the execution of works contract, there cannot be any deemed sale.

This view was concurred by the Kerala High Court<sup>617</sup> and held that while executing the contract of display of fireworks, the explosives ceased to exist and there is no transfer of property in goods in its original form or in any other form to constitute a deemed sale.

#### **6.14. Scope of the Constitutional Amendment.**

The 46<sup>th</sup> Amendment to the Constitution was made precisely with a view to empower the State to bifurcate the contract and to levy sales tax on the value of the materials involved in the execution of the works contract, notwithstanding that the value may represent a small percentage of the amount paid for the execution of the works contract. Even if the dominant intention of the contract is the rendering of a service, which will amount to

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<sup>617</sup> *Deputy Commissioner v. M.K. Velu*, [1993] 89 STC 40 (Ker.).

a works contract, after the 46<sup>th</sup> Amendment the State would have now been empowered to levy sales tax on the materials used in such contract<sup>618</sup>.

The object of the Constitutional Amendment in 46<sup>th</sup> Amendment Act is in order to create a “legal fiction” of “transfer of goods within the works contract” that is in order to levy tax on the goods involved in the execution of a works contract. In the wider sacking, it also aimed to bring the transactions, though in which property in goods is passed but were not considered as sales<sup>619</sup>.

Irrespective of whether the transfer of property is incidental or accessory to a works contract, once a works contract involves transfer of property per se, the provision of the Article 366 (29A) of the Constitution of India are attracted to enable the State to extend the meaning of sale to deemed sale for the purpose of deciding incidence of taxation.

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<sup>618</sup> *Supra*, n. 596.

<sup>619</sup> Law Commission of India, *61<sup>st</sup> Report on certain problems connected with powers of the State to levy a tax on the sale of goods and with the Central Sales Tax Act, 1956*, Ministry of Law; Government of India (May, 1974) at p 174.

The Hon'ble Apex Court<sup>620</sup> rightly observed that if the legal fiction introduced by Article 366 (29A) is carried to its logical end it follows that even in a single and indivisible works contract there is a deemed sale of the goods which are involved in the execution of works contract.

Still, there cannot be a deemed sale for the purpose of state tax, when the transfer of property in good is a transfer in the course of inter-State trade or commerce or an outside transfer or transfer in the course of import or export, unless statutory changes are made in the appropriate legislation<sup>621</sup>.

In a fictional sale, what is taxable is the transfer of the property in the goods involved in the execution of contract and that only constitutes the taxable event. There is an inherent limitation to include the entire consideration as sale consideration. Thus the scope of the deemed sale cannot be extended to include the value of design<sup>622</sup> and cost of engineering while estimating the total sale consideration for the purpose of taxation.

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<sup>620</sup> *Larsen & Turbo Ltd v. Union of India*, [1993] 88 STC 204 (SC).

<sup>621</sup> *Id.* at p. 231.

<sup>622</sup> *Daelim Industrial Co. Ltd v. State of Assam*, [2003] 130 STC 53 (Gau.).

## CHAPTER VII

# Concept of Sale: Enlargement of Meaning

The 46<sup>th</sup> Amendment to the Constitution of India was not confined in its ambit to the fields of works contract or labour contract only, but in other areas also, such as, statutory- compulsory contracts, transfer of property during transfer of rights to use goods, transfer of property in hire-purchase, supply of goods in service contracts etc.

In effect, the attempt of Indian Parliament was to remove the ambiguity in law, mostly arisen due to the intrusion of the Court in to the legislative freedom, through various judgments like those in the cases of *Young Men's India Association*<sup>623</sup>, *Northern India Caterer*<sup>624</sup>, *K.L. Johar*<sup>625</sup> and *Meyiappan*<sup>626</sup>.

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<sup>623</sup> *Joint Commercial Tax Officer v. Young Men's Indian Association*, [1970] 26 STC 241 (SC).

## **7.1. Non-voluntary Transfer: Revisited.**

Even without having the traditional or statutory elements of sale, of course, in the facts and circumstances of each case, certain kind of transactions were held to be sale even in the foundation period. Compelled sale or sale by operation of law is one of its kind. Though bargaining and mutual assent are termed as special characteristics of sale, it was held by the House of Lords in *Newcastle Breweries's case*<sup>627</sup> that a compelled sale is nevertheless a sale. There are cases in which a sale takes place by the operation of law rather than strictly by mutual agreement either expressed or implied.

When the government procures sugar to common pool based on statutory orders, there is at least an implied contract out of an implied offer and implied acceptance by the parties. When the Government after receiving permit

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<sup>624</sup> *Northern India Caterers (India) Ltd v. Lt. Governor of Delhi*, [1978] 42 STC 386 (SC).

<sup>625</sup> *K.L. Johar & Co v. Deputy Commercial Tax Officer*, [1965] 16 STC 213 (SC).

<sup>626</sup> *Meyiappan v. Commissioner of Commercial Taxes*, [1967] 20 STC 115 (Mad.).

<sup>627</sup> *Newcastle Breweries v. Inland Revenue Commissioners*, [1927] 96 L.J.K.B. 735.

telegraphed instructions to despatch sugar and the mill despatched it, a contract emerges and consent must be implied on both sides though not expressed antecedent to the permit<sup>628</sup>. There are reasons as if social security measures mandate the State to compel persons to make contracts<sup>629</sup>. Under the economic compulsions, social control of many of economic activities is inevitable, to regulate the short supply of essential goods, even. This is one of the main reasons persuading the State to introduce statutory sales or compulsory acquisition.

Departing from the majority view in *New India Sugar Mill's case*<sup>630</sup>, the Hon'ble Supreme Court in *Andhra Sugars Ltd's case*<sup>631</sup> held that where one party to a contract of sale is compelled to enter into it on rigidly prescribed terms and conditions and has no freedom of bargaining, but the contract, nonetheless, is a contract of sale. The Court

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<sup>628</sup> Hidayathulla, J in *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, [1963] 14 STC 316 at p. 354. (Minority View)

<sup>629</sup> Cheshire, *Law of Contract*, 4<sup>th</sup> edn., Butterworths (1981) at p. 23.

<sup>630</sup> *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC).

<sup>631</sup> *Andhra Sugar Ltd v. State of Andhra Pradesh*, [1968] 21 STC 212 (SC).

ruled out the statutory mandate of freedom of contract, especially the requirements of mutual assent and voluntary actions to constitute a contract of sale.

The view of the House Lords in *Kirkness v. John Hudson & Co. Ltd*<sup>632</sup>, in which it was held that mutual assent is an element of a transaction of sale is distinguished in *Andhra Sugar Ltd's case*<sup>633</sup>, and according to Bachawat, J, it depends upon the facts of each case and the terms of the particular statute regulating the dealings whether the parties have entered into a contract of sale of goods<sup>634</sup>. In fact in *Kirkness's case*<sup>635</sup> the House of Lords was dealing with a compulsory acquisition and not a sale<sup>636</sup>. Consequently, it was asserted that the view taken by the House of Lords cannot be a precedent in all circumstances.

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<sup>632</sup> [1955] AC 696.

<sup>633</sup> *Andhra Sugar Ltd v. State of Andhra Pradesh*, [1968] 21 STC 212.

<sup>634</sup> *Id.* at p 223.

<sup>635</sup> *Kirkness v. John Hudson & Co. Ltd*, [1955] AC 696.

<sup>636</sup> *Indian Steel & Wire Products Ltd. v. State of Madras*, [1968] 21 STC 138 (SC) at p. 150.

The earlier view of the Hon'ble Supreme Court in *Chittar Mal Narain Das's case*<sup>637</sup> is that a sale predicates contract of voluntary actions and consensual arrangements and a transaction in which an obligation to supply of goods imposed or which does not involve an obligation to enter into a contract cannot be called a sale. The majority view in *New India Sugar Mill's case*<sup>638</sup> also supported this view where in it was held that the intimation by the State of its requirements of sugar to the Controller or the communication of the allotment to the Mills did not amount to an offer or mere compliance by the mills did not amount to acceptance to form the transaction a sale. It was held by the Court that sale of goods postulates a voluntary arrangement regarding the goods between the contracting parties. However while dealing with the matter in detail by a Seven Judges Bench of the Supreme Court in *Vishnu Agency's case*<sup>639</sup> the controversy was settled in a larger

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<sup>637</sup> *Chittar Mal Narain Das v. Commissioner of Sales Tax*, [1970] 26 STC 344 (SC); 1970 (3) SCC 809.

<sup>638</sup> *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, [1963] 14 STC 316 (SC); AIR 1963 SC 1207.

<sup>639</sup> *Vishnu Agencies (Pvt.) Ltd v. Commercial Tax Officer*, [1978] 42 STC 31 (SC); 1978 (1) SCC 520.

extend and the Court held that a regulatory law, even if it circumscribed the area of free choice, did not take away the basic character or core of sale from the transaction. It was added that the agreement between the parties under a statutory order despite considerable compulsive elements regulating or restricting the area of choice might, still, retain the basic character of a transaction of sale.

A statutory sale is a sale, which is done in the manner prescribed by law and having followed the procedure of law. Even though a forced requisition of vehicle is made from the vehicle owner for hire charges, if there is statutory right to the owner to get the relief through an arbitral proceedings for short payment of hire, it cannot say the price fixed is unilateral and without bargaining<sup>640</sup>. Likewise when the Statutory Order requires supplying rice that too, involuntarily to the Central or State Food Corporations, the compliance of obligatory terms of the Statutory Order treat the supply as sale<sup>641</sup>. The statute

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<sup>640</sup> *State of Tripura v. Tripura Bus Syndicate*, [2001] 122 STC 175 (Gau.) at p. 180.

<sup>641</sup> *Sri Dhanalakshmi Kanyaka Parameswari Rice Mill v. Commercial Tax Officer*, [1986] 63 STC 168 (Andhra).

brings the two parties together, restricting the area of consensual agreement, and however minimal it may be, property none the less passes on to the purchaser for a price, which is the essential feature of the sale.

In compulsory acquisition, the dissent is overridden by an assent supplied by the Statute. Whatever coercive force is used to bring about the transaction must be traced to the legislation not attributable to the Government, who is a party to the contract<sup>642</sup>. Supply of Indian Made Foreign Liquor by Distilleries and Brewery Company from its wholesale depots to permit holders on the permit issued by the authorities are held sale and the Court ruled out the contention that there is statutory fixed price and no volition in distribution of the liquor<sup>643</sup>.

In *Coffee Board's case*<sup>644</sup>, the Supreme Court considered an identical issue regarding the element of sale while delivering the coffee grown in the registered estates

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<sup>642</sup> *Food Corporation of India v. Commissioner of Sales Tax*, [1988] 69 STC 374 (All.).

<sup>643</sup> *State of Punjab v. Dewan's Modern Breweries*, [1979] 43 STC 454 (SC).

<sup>644</sup> *Coffee Board v. Commissioner of Commercial Taxes*, [1988] 70 STC 162 (SC); 1988 (3) SCC 263.

to the Coffee Board, as per the statutory mandate. The Court repelled the contention that there is no sale and only compulsory acquisition and held that while delivering the coffee to the Board though the growers does not actually sell the coffee, but there is a sale by operation of law, which was categorically cleared by the Hon'ble Supreme Court in *State of Kerala v. Bhavani Tea Produce Co.*<sup>645</sup>.

It is not only the supply or delivery out of a statutory order which forms the transaction a sale. When a company in compliance with the statutory obligation under the Factories Act and Mines Act, serves food through its canteen, it equally amounts to sale<sup>646</sup>. It is immaterial that the service is rendered in compliance of statutory requirements and the canteens are run on no profit no loss basis with subsidies required to be provided under the law.

## **7.2. Significance of Freedom of Contract.**

In short, while extending the scope of sale for the purpose of taxation, it is immaterial whether the freedom of contract is satisfied or not. So long as mutual assent is not

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<sup>645</sup> [1966] 2 SCR 96.

<sup>646</sup> *Tata Iron and Steel Co. v. State of Bihar*, [1985] 58 STC 302 (Pat.).

completely excluded in any dealing, in law it is a contract. Even if a Statutory Order reduces the scope of freedom of contract, there could be some kind of negotiation in respect of matters not controlled by the Order<sup>647</sup>. It is still open to the parties to settle their own terms regarding the manner and mode of payment of price.

Mere regulation or restriction of the filed of choice does not take away the contractual or essentially consensual binding core or character of the transaction. Under regulatory orders when there are mandates to deliver the produces in accordance with the regulation, there is volition or option, though minimal or normal to enter in to the trade or business to which the regulation concerns. Carrying of trade or business is not compulsory or there is no prohibition quitting out from the trade and only if any one decides to carry out or continue the trade, he must transact the trading in terms of the regulation<sup>648</sup>.

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<sup>647</sup> *Indian Steel & Wire Products Ltd. v. State of Madras*, [1968] 21 STC 138 (SC) at p. 148.

<sup>648</sup> *Coffee Board v. Commissioner of Commercial Taxes*, [1988] 70 STC 162 (SC) at para 28.

### **7.3. Essential Nature of Statutory Contracts.**

The Apex Court laid down certain elaborate propositions regarding the essential nature of statutory contracts in *Salar Jung Mill's case*<sup>649</sup>. Firstly, statutory orders regulating the supply and distribution of goods by and between the parties under Control Orders do not absolutely impinge on the freedom to enter into contract. Secondly, the directions, decisions and orders of agencies of the Government to control production and supply of commodities, may fix certain stipulations such as the parties to whom the goods are to be supplied, the price at which these goods are to be supplied, the time during which the goods are to be supplied and the person who has to carry out the directions. Still in such cases, it is not correct to say that compulsive directions rob the transactions of the character of the agreement. It is to be remembered that the transfer of property, which constitutes the agreement in spite of the compulsion of law, is neither void nor voidable, the transaction is not vitiated by any

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<sup>649</sup> *Salar Jung Mills Ltd v. State of Mysore*, [1972] 29 STC 246 (SC). The decision is rendered by a Seven- Judge's Bench headed by Ray, C.J., of the Supreme Court of India.

coercion and there is privity of contract between the parties. In addition, the statute supplies the consensus and the modality of consensus.

Thirdly, the proposition suggests, a transaction arising out of statutory order is neither a gift nor an exchange nor a hypothecation nor a loan, but absolutely a transfer of property from one person to another having capacity to enter into the contract. Yet, the price is fixed statutorily or by the authorities under the statute, there is consideration for the transfer. The law presumes the assent of the parties to the contract coupled with movement of goods in between them.

Furthermore, it is suggested that a sale may not require the consensual element and that there may, in truth, be a compulsory sale of property with which the owner is compelled to part for a price against his will and the effect of the statute in such case is to say that the absence of the consent of transferor does not matter and the sale is proceeded without it, due to larger interest. In fact, transfer is brought into being which *ex facie* in all its essential characteristics.

The propositions further suggest that delimiting areas of transactions or denoting parties or denoting price for transactions are all within the area of individual freedom of contract with limited choice by reason of ensuring the greatest good for the greatest number of achieving proper supply at standard or fair practice to eliminate the evils of hoarding and scarcity on the one hand and ensuring the availability on the other, which is uppermost interest of the welfare state. There is also proper appreciation for personal gains and interests. To be precise, after all the transactions in substance represent the outgoing of the business and the price would come into the computation of profits.

With the aid of these prepositions, the Courts in India took its predetermined stand to hold that compulsory delivery<sup>650</sup> or supply out of consensual arrangements and where with some sort of volition left untouched by the respective legislation amounts to sale, irrespective of the commodity, either, cement or cotton or coal or iron and

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<sup>650</sup> *Oil and Natural Gas Commission v. State of Bihar*, [1976] 38 STC 435 (SC).

steel or paddy or fertilizer or liquor or coffee etc<sup>651</sup>. The Court in *Food Corporation of India's case*<sup>652</sup> ruled out the argument that there is substantial difference in the nature of transaction arising out of a control order and levy order.

No one can ignore the reality that the concept of freedom of contract has undergone a great deal of change. Though, in earlier times, there were no freedom of contract, in its utter sense, the freedom of contract is now being confined gradually to narrower and narrower limits. There are several other instances like insurance contract to cover third party risk, hire purchase contracts etc. to justify this proposition<sup>653</sup>, which are best examples for standard form of contract, where there are less bargain and minimum freedom of contract.

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<sup>651</sup> *Food Corporation of India v. State of Kerala*, [1997] 105 STC 4 (SC) at p. 25.

<sup>652</sup> *Id.* at p. 24.

<sup>653</sup> Cheshire, *Law of Contract*, 4<sup>th</sup> edn., Butterworths (1981) at p. 23.

#### **7.4. Supply of Goods in Maintenance Contract: Deemed Sale.**

Whether an AMC (Annual Maintenance Contract) is a mere service contract or not? The Gauhati High Court<sup>654</sup> mooted this important question in premise of expanded meaning endorsed to the sale of goods in 46<sup>th</sup> Amendment. It was held that supplying of spare parts or replacing of the worn spare parts is not the essence of the service contract and the service contract merely provides for labour and expertise for maintenance of the machine or equipment to keep them workable. It was also held that wherever spare parts or other parts are supplied, it will amount to transfer of property in the goods from the supplier to the customer to treat the transfer as sale<sup>655</sup>. The Court did not give any general applicability of law regarding the AMC, but appreciated the variance in different kind of AMCs, such as contract in which supplier provides labour and service only

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<sup>654</sup> *HCL INFO System Ltd v. Commissioner of Taxes, Assam*, [2006] 146 STC 661 (Gau.). This view was upheld in *Xerox Modicorp Ltd v. State of Karnataka*, [2005] 142 STC 209: AIR 2005 SC 3336. Again in *State of Andhra Pradesh v. Kone Elevators (India) Ltd*, [2005] 140 STC 22: AIR 2005 SC 1581, the Supreme Court held that manufacture, supply and installation of lift in a building is equally a sale for levy of sales tax.

<sup>655</sup> *Id.* at p. 664.

and secondly along with supply of labour and service provides necessary spare parts also.

Analogous elucidation was given by the Apex Court in cases relating to warranty agreement also. The object of giving warranty is that the customer who has to make a heavy investment for the vehicle should be assured of a proper performance of the vehicle in a trouble free manner for reasonable length of time<sup>656</sup>. When manufacturer issue warranty to its purchaser and replaces the defective parts during the warranty period through the middle man dealer, and the dealer is receipt of the price of replaced parts from the manufacturer by way of issuance of credit notes, there is absolutely sale taking place and the dealer is liable to pay tax on the replacement and supply of spare parts<sup>657</sup>. The Apex Court while pronouncing the law differed from the earlier view in *Premier Automobile's case*<sup>658</sup> and also overruled the ratio laid down in the cases of *Prem Motors*<sup>659</sup>

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<sup>656</sup> *Premier Automobile Ltd. v. Union of India*, [1972] 2 SCR 526.

<sup>657</sup> *Mohd. Ekram Khan & Sons v. Commissioner of Trade Tax*, [2004] 136 STC 515 (SC).

<sup>658</sup> *Supra*, n. 656.

<sup>659</sup> *Prem Motors v. Commissioner of Sales Tax*, [1986] 61 STC 244 (MP).

and *Geo Motors*<sup>660</sup>, where in it was held that there is only compliance of contractual obligation and no sale exigible to tax.

The Apex Court judicially noticed the law declared by the Delhi High Court in *Prem Nath's case*<sup>661</sup> on different footing wherein it was held that in a case manufacturer offers warranty as a part of original sale and the customer pays fixed price consolidating the value of the equipment and the parts that may have to be supplied by way of replacement in pursuance of stipulations in the warranty, there can not be any sale on replacement of defective parts. In the case of extended warranty that is separately offered in addition to the generally offered warranty. If such extended warranty is optional and charged separate from the value of the commodity, it cannot be treated as sale<sup>662</sup>.

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<sup>660</sup> *Geo Motors v. State of Kerala*, [2001] 122 STC 285 (Ker.).

<sup>661</sup> *Commissioner of Sales Tax v. Prem Nath Motors (P). Ltd*, [1979] 43 STC 52 (Del.).

<sup>662</sup> *Commercial Tax Officer v. Weston Electroniks Ltd*, [1992] 87 STC 522 (Raj). Also see in *Commercial Tax Officer v. Kelvinator India*, [1993] 90 STC 336 (Raj.).

This view has been followed by the Allahabad High Court<sup>663</sup> and held that the additional warranty is only an optional one and thereby the same is not exigible to levy sales tax. The same principle was adopted by the Apex Court in *Kelvinotor India Ltd's case*<sup>664</sup>, relating to value assessment under Excise and found that such optional warranties are after sale facility separately accountable.

### **7.5. Supply of Goods in Hotel Service: Deemed Sale.**

Issues regarding indivisible contracts of service and supply of materials, in hotel industry, came for debates, again in view of the expanded meaning of sale, deemed sale in the 46<sup>th</sup> Amendment of Constitution. The argument that supply of meals in a hotel or restaurant in rendering of service is only in the satisfaction of human needs or ministering to the bodily want of human beings<sup>665</sup> is no more a defence for avoidance of tax. On a large-scale

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<sup>663</sup> *Commissioner of Sales Tax v. Kelvinator India Ltd*, [2006] 146 STC 651 (All.).

<sup>664</sup> *Collector of Central Excise v. Kelvinator India Ltd*, [1988] 69 STC 427 (SC).

<sup>665</sup> *Northern India Caterers (India) Ltd v. Lt. Governor of Delhi*, [1978] 42 STC 386 (SC).

representation made by the different States, Parliament enacted the Amendment Act by enlarging the scope of sale, by a legal fiction of deemed sale<sup>666</sup>, which would also include the supply, by way of, or as part of any service, of food or any drink for cash, deferred payment or other valuable consideration<sup>667</sup>. This legal proposition was followed in *Sree Annapoorna v. State of Tamil Nadu*<sup>668</sup> and *Damodarasamy Naidu v. State of Tamil Nadu*<sup>669</sup>, which was affirmed by the Hon'ble Supreme Court also<sup>670</sup>.

Equally, in the case of serving of refreshments by a club to its members, the ratio settled in *Young Men's Indian Association case*<sup>671</sup> is also no longer available after the

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<sup>666</sup> *Sangu Chakra Hotels Pvt. Ltd v. State of Tamil Nadu*, [1985] 60 STC 125 (Mad.).

<sup>667</sup> Article 366 (29A) (f) includes "a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration"

<sup>668</sup> [1986] 63 STC 18 (Mad).

<sup>669</sup> [1990] 76 STC 427 (Mad.).

<sup>670</sup> *Damodarasamy Naidu v. State of Tamil Nadu*, [2000] 117 STC 1 (SC) at p. 7.

<sup>671</sup> *Joint Commercial Tax Officer v. Young Men's Indian Association*, [1970] 26 STC 241 (SC).

expansion of meaning of sale in 46<sup>th</sup> Amendment Act<sup>672</sup>. The doctrine of mutuality, which supports the collective acquisition of goods and sharing of rights on goods or supply of goods in favour of the members of a collective organisation, has been done away with after the introduction of sub-clause (e) to Article 366 (29A)<sup>673</sup>. The commercial activities in any country are now carried on to a substantial extent by the incorporated bodies and supply of bulkily imported wattle extract to members of association for price is also deemed sale for the purpose of sales tax<sup>674</sup>.

### **7.6. Supply of Goods in Medical Service: Deemed Sale.**

When a hospital rendering medical service, supplies medicines to its patients in the course of medical treatment, as per the prescription of their own medical practitioner, it is

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<sup>672</sup> *Cosmopolitan Club v. Tamil Nadu Taxation Tribunal*, [2002] 127 STC 475 (Mad.).

<sup>673</sup> Article 366 (29A) (e) of Constitution of India, includes “a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;” in the definition of tax on sale and purchase of goods.

<sup>674</sup> *All India Skins & Hides Tanners and Merchant Association v. Commercial Tax Officer*, [2002] 127 STC 491 (Mad.).

a sale, not an incidental supply during the course of professional services<sup>675</sup>. The Court held that the supply of medicine in the course of treatment is not just incidental, but it is main and integral part of treatment<sup>676</sup>. Putting the goods in the way of use or consumption<sup>677</sup>, even supply<sup>678</sup>, can be treated as the sale in appropriate cases.

Barter is a system of exchange of property for property<sup>679</sup>. It cannot be said that it fulfils the features of sale. When the property in a finished silver article is transferred to a purchaser in exchange for an equivalent weight in silver along with a sum of money equal to the manufacturing or making cost, it was held that the sale is completed on passing of cash plus the quantity of silver being the valid consideration<sup>680</sup>. The reason stated by the learned Judge for ruling out the above transaction as barter

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<sup>675</sup> *Malankara Orthodox Syrian Church v. Sales Tax Officer*, [2004] 135 STC 224 (Ker.).

<sup>676</sup> *Id.* at p. 237.

<sup>677</sup> *Burmah Shell Oil Storage & Distributing Co. v. Belgaum Municipality*, [1963] Supp. 2 SCR 216.

<sup>678</sup> *Indian Aluminium Co. v. State of Kerala*, 1996 (7) SCC 637.

<sup>679</sup> *Wharton's Law Lexicon*, 9<sup>th</sup> edn., Stevens & Sons (1892) at p. 99.

<sup>680</sup> *In re Jayaram Chettiar*, [1951] 1 STC 168 (Mad.) at p. 171.

is that the exchange is of the same commodity in a different form not for a reciprocal transfer of different commodity as required in Barter<sup>681</sup>.

A similar legal position can be marked out from the Australian law of sales taxation, which provides that where the goods are supplied to the manufacturer wholly or in part by a customer and the former returned the goods as per the requirement of the latter, the goods shall be deemed to have been sold to the customer, though there is no transfer of money consideration equal to the value of the goods transferred<sup>682</sup>. It is apt to refer to the laws of Australia regarding the assessment of building contracts treating it as transfer of building materials, being the goods, from the contractor to awarder<sup>683</sup>.

The traditional approach regarding the ownership of goods has little relevance under the taxing statute as held

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<sup>681</sup> *Id.* at p.172.

<sup>682</sup> See Section 17A of the Australian Sales Tax Assessment Act, (No.1), 1930.

<sup>683</sup> *Deputy Federal Commissioner of Taxation v. Stronach* [55 CLR 305] and *M.R. Hornibrook (Pvt.) Ltd v. Federal Commissioner of Taxation* [62 CLR 272].

in *Staynor & Co. v. Commercial Tax Officer*<sup>684</sup>, wherein it was held, that an auctioneer though he is not the owner of the goods auctioned, is liable to be taxed as he has dominion and possession of goods auctioned. The transfer of property takes place and the ownership of the goods shift to the bidder who purchases the goods on the stroke of hammer by an auctioneer. That contemplates the real sale<sup>685</sup>.

### **7.7. Sale in Auctions.**

It was held that a sale by an auction is a sale as contemplated by the Sale of Goods Act, 1930, in view of Sections 4 and 64 of the said Act<sup>686</sup>. By the Act, a contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in the goods to the buyer for a price. Where under a contract of sale, the property in goods is transferred from the seller to buyer, the contract constitutes sale. In the case of sale by auction, where the goods are put up for sale in lots, each lot is deemed to be

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<sup>684</sup> *Staynor v. Commercial Tax Officer*, [1951] 2 STC 111 (Calcutta).

<sup>685</sup> *Ibid.*

<sup>686</sup> *Chowringhee Sales Bureau Pvt. Ltd v. Commissioner*, [1973] 31 STC 254 (SC).

subject of separate contract of sale. Where the transaction is one of sale of goods as known to law, the tax on auction sale is perfectly justifiable<sup>687</sup>.

Hence, State is not prevented from treating the auction of pledged article by the financial institution, as sale for the purpose of local taxation<sup>688</sup>. Financial institutions are not acting as the agent of the borrower, but as pledgees and by invoking the powers under S. 176 of the Contract Act, 1872<sup>689</sup> to sell the pledged articles in case of default<sup>690</sup>. When charge of pledge is enforced that enforcement is by way of sale of the pledged or

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<sup>687</sup> *Id.* at p. 258.

<sup>688</sup> *Federal Bank v. State of Kerala*, [2007] 6 VST 736 (SC).

<sup>689</sup> Indian Contract Act, 1872, S. 176 reads as follows,

**Pawnee's right where pawnor makes default.** - If the pawnor makes default of the debt, or performance, at the stipulated time, of the promise, in respect of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as a collateral security, or he may sell the thing pledged, on giving the pawnor reasonable notice of the sale.

If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the amount so due, the pawnee shall pay over the surplus to the pawnor.

<sup>690</sup> *Deputy Commissioner v. ARS Thirumeninatha Nadar*, [1968] 21 STC 184 (Mad.).

hypothecated goods, the sale is for valid consideration and it falls within the ambit of sale exigible to tax<sup>691</sup>. There is indeed transfer of general property to the buyer and it is not a special right which is transferred<sup>692</sup>.

### **7.8. Transfer of Right to Use Goods: Deemed Sale.**

The 46<sup>th</sup> Amendment to the Constitution made a hit on the traditional concept of sale, by including the transfer of right to use goods as a deemed sale. Thus transfer of right to use goods for any purpose for cash, deferred payment or other valuable consideration is a deemed sale. Such transfer is exigible to sales tax.

The Court held that when video cassettes are given to the members for being viewed on the hire charges, there is a transfer of right to use goods, which is a deemed sale after the introduction of Amendment Act to the Constitution of India<sup>693</sup>. It is material to note that the members of the

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<sup>691</sup> *Supra*, n. 688 at p. 754.

<sup>692</sup> *State Bank of Travancore v. Commercial Tax Officer*, [2008] 13 VST 562 (Ker.).

<sup>693</sup> *Rohini Panicker v. Additional Sales Tax Officer*, [1997] 104 STC 498 (Ker.).

Library has not the exclusive control over the cassettes for the period during which the cassettes are in his custody against the fixed hire charges. Even though the customer is forbidden from altering the recording in the cassette, the very purpose of hiring the cassette is for viewing the contents recorded in and there is an absolute transfer of that goods in favour of the customer which will make the transaction as deemed sale<sup>694</sup>.

While hiring the vehicle for the transport of food grains from railway yard to the godown, the Food Corporation of India maintains the actual control of operation of the vehicle. In such circumstances, it was held that during the period of carrying food grains remained with them, the hire charge of the vehicle is exigible to sale tax as there is a deemed sale arising out of transfer of right to use the vehicle by the vehicle owners to the Food Corporation of India<sup>695</sup>.

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<sup>694</sup> *Id.* at p 502.

<sup>695</sup> *Mahabir Transport Agency v. Food Corporation of India*, [1998] 109 STC 99 (Gau.).

The Court held that by transferring the possession of vehicle under a banner system allowing the hirer the effective and general control on the vehicle, there is sufficient acquisition of rights by the hirer than a mere custody and there is transfer of right to use goods which amounts to deemed sale<sup>696</sup>. Whether parting of goods is for a specified period or not is immaterial and the contention contrary that there is no parting of ownership of goods permanently and the requirement that the lessee is bound to return the goods to the lessor after the use of the goods for a specific period makes the contract as service contract is untenable<sup>697</sup>. When a towing vessel is hired by the Port Trust as per the charter party agreement with specific stipulation of handing over of possession and control in all respects, the transfer to port trust is a transfer of right to use goods and amounts to deemed sale<sup>698</sup>.

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<sup>696</sup> *Krushna Chandra Behra v. State of Orissa*, [1991] 83 STC 325 (Gau.) at p 330.

<sup>697</sup> *DCL Finance Ltd v. Union of India*, [2002] 126 STC 249 (Andhra).

<sup>698</sup> *Great Eastern Shipping Company Ltd v. State of Karnataka*, [2004] 136 STC 519 (Kar.).

When the owner of shuttering transferred it to builders and building contractors for use in the building construction, for consideration of hire charges, there is absolutely the transfer of right to use goods and where there is a transfer of a right to use goods for consideration, the requirement of deemed sale is satisfied<sup>699</sup>. It has been held that even if the Government for smooth functioning of election makes a forced requisition of vehicle for hire charges, a non voluntary act, it will come under the preview of extended meaning of deemed sale out of transfer of right to use goods<sup>700</sup>. The Court held that though it is correct to say that in common parlance sale is a voluntary act in transferring property in goods by the sellers to the buyers on a settled or negotiated price, paid or on credit, after the change undergone in the meaning of sale in view of 46<sup>th</sup> Amendment Act, the commercial meaning of sale in the Sale of Goods Act, 1930 is no more available<sup>701</sup>.

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<sup>699</sup> *Aggarwal Brothers v. State of Haryana*. [1999] 113 STC 317 (SC) at p. 318.

<sup>700</sup> *State of Tripura v. Tripura Bus Syndicate*, [2001] 122 STC 175 (Gah.)

<sup>701</sup> *Id.* at p. 178.

However, a different view is possible in view of the Constitutional Bench decision in *BSNL's case*<sup>702</sup>, regarding the rental charges collected by telecom department from the customers on rendering telephone service. On an earlier occasion, while deciding a batch of cases<sup>703</sup>, reversing the decisions of various high courts, the Hon'ble Supreme Court held that providing telephone service by the Department of Telecom which comprises of allotment of number, installation of an instrument/ apparatus and other appliances at the premises of a subscriber, which are connected with a telephone line to the area exchange to enable him to have access to the whole system, to dial and to receive the calls falls within the extended meaning of sale as it is a kind of transfer of right to use goods. By referring the decision in *Rashtriya Ispat Nigam's case*<sup>704</sup>, the Court held that handing over possession is not a sine qua non of completing the transfer of right to use any goods. This was followed in *Banda Test House*

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<sup>702</sup> *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 145 STC 91 (SC).

<sup>703</sup> *State of Uttar Pradesh v. Union of India*, [2003] 130 STC 1 (SC).

<sup>704</sup> *State of Andhra Pradesh v. Rashtriya Ispat Nigam Ltd*, [2002] 126 STC 114 (SC).

*Association's case*<sup>705</sup> and held that the fact that the goods remain within the ultimate control of the owner is irrelevant for deciding whether there was a transfer of use.

In *BSNL's case*<sup>706</sup> this verdict was doubted and reversed in certain extent and held that in telecom service the providers are dealing with electro magnetic waves, which are not goods and to that extent there is no transfer of right to use goods. Regarding the transfer of telephone apparatus, it depends on the conditions of transfer and there cannot be a general formula to decide whether the rent collected would form sale price. Likewise, though in *Asiatic Gases Ltd*<sup>707</sup> the Court held that the retention charges collected is in the form of penalty and not related to transfer of right to use goods, however in *North East Gases's case*<sup>708</sup> it was held that when the transfer of right to use the goods was not limited for any specified duration of time, and parties having intention to continue the transfer

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<sup>705</sup> *Banda Tent House Association v. State of U.P.*, [2006] 146 STC 355 (All.).

<sup>706</sup> *Supra*, n. 702.

<sup>707</sup> *Asiatic Gases Ltd v State of Orissa*, [2001] 121 STC 405 (Ori.).

<sup>708</sup> *North East Gasesa Pvt. Ltd v. State of Assam*, [2004] 134 STC 249 (Gau.) at p.255.

for an indefinite duration of time, subject to payment of rent, there is deemed sale.

Whether there is a transfer of right to use goods or not is essentially a question of fact depending on the facts and circumstances of the cases<sup>709</sup>. It depends on terms of contract and it is impossible to lay down any general principle<sup>710</sup>. However principally, it can be said that there is a conceptual distinction between sale and transfer of the right to use goods without being accompanied by transfer of the ownership in the goods in favour of the hirer. In transfer of right to use goods the proprietary rights in goods remain with the transferor. He has a bundle of rights such as right to possess, use and enjoy, usufruct, consume, transfer, alienate or even right to destroy the goods. In a conventional sale it has a double aspect. There is an acquisition of all these rights by the transferee and loss of it by the transferor, on receiving effective consideration<sup>711</sup>. For that reason, the Courts had excluded the mere transfer

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<sup>709</sup> *Harbans Lal v. State of Haryana*, [1993] 88 STC 357 (P&H).

<sup>710</sup> *Supra*, n 708. at p.254.

<sup>711</sup> P.J. Fitzgerald, *Salmond on Jurisprudence*, 12<sup>th</sup> edn., Sweet & Maxwell (London) (1966) at p. 332.

of right to use goods from the liability of sale tax in the pre-amendment period.

By the amendment in 46<sup>th</sup> Amendment Act, a fiction of sale was created with regard to goods involved or used in the execution of contract and also transferred right to use goods. The levy of tax is not on the use of goods but on the transfer of the right to use goods<sup>712</sup>. The taxable event in such transaction is the execution of the contract for the transfer of right to use goods<sup>713</sup>.

In the post- amendment period, if the transaction is one of leasing/ hiring/ letting simpliciter under which possession of goods with effective and general control is passing to the customer and the customer had the freedom and choice of selecting the manner, time and nature of use and enjoyment, there is transfer of right to use the goods to fall under the definition of deemed sale<sup>714</sup>. Handing over of

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<sup>712</sup> *Coromandal Finance Co. Ltd v. Commissioner of Commercial Taxes*, [2001] 122 STC 538 (Andhra).

<sup>713</sup> *20th Century Finance Corporation Ltd. v. State of Maharashtra* 119 STC 182 (SC) at p. 202.

<sup>714</sup> *Lakshmi Audio Visual v. Asst. Commissioner of Commercial Taxes*, [2001] 124 STC 426 (Kar.).

the possession is not sine qua non of completing the transfer of right to use any goods.<sup>715</sup>

### **7.9. Transfer of Goods while Hire-purchase: Deemed Sale.**

In a hire- purchase or instalment transaction, there is an obligation upon the hirer to buy the chattel from the party in other part. Such an obligation attaches on execution of the agreed terms and such an agreement is really an agreement to sell<sup>716</sup>. When the financier entered up on an agreed terms to advance the customer to purchase the vehicle and pay full price of the vehicle to the distributor, on the strength of the promissory note entered by the customer, no stretch of imagination, it is a sale between the parties<sup>717</sup>. A hire- purchase agreement is not a mere contract of bailment simply, but creates proprietary interest in the buyer<sup>718</sup>.

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<sup>715</sup> *State of Uttar Pradesh v. Union of India*, [2003] 130 STC 1 (SC) at p. 19.

<sup>716</sup> *Damodar Valley Corporation v. State of Bihar*, [1957] 8 STC 47 (Pat.).

<sup>717</sup> *Commissioner of Sales Tax v. Pashupati Trading Co.*, [1991] 80 STC 17.

<sup>718</sup> *Commercial Credit Corporation v. Deputy Commercial Tax Officer*, [1958] 9 STC 599 (Mad.).

In *Helby v. Mathews*<sup>719</sup>, two tests were invented by the Court to decide the nature of a contract, whether it is hiring or not? Firstly, to determine the question whether a particular agreement is a contract of mere hiring or whether it is a contract of purchase on a system of deferred payments of the purchase price, is whether there is any binding obligation on the hirer to purchase the goods. Other is whether there is a right reserved to the hirer to return the goods at any time during the subsistence of the contract. When there is no right reserved to the contractor to return the chattel at any time it is absolutely a sale not a mere hiring<sup>720</sup>. However there cannot be a straight jacket formula to decide the nature of hire- purchase contract and it is a complex contract transcending a mere bailment and conferring on the hirer a legal status<sup>721</sup>.

In *Johar's case*,<sup>722</sup> the Supreme Court categorically made the pronouncement on the salient features of hire

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<sup>719</sup> [1985] AC 471.

<sup>720</sup> *Damoder Valley Corporation v. State of Bihar*, [1961] 12 STC 102.

<sup>721</sup> *Karflex Ltd v. Poole*, [1933] 2 K B 251.

<sup>722</sup> *K.L. Johar & Co v. Deputy Commercial Tax Officer*, [1965] 16 STC 213 (SC).

purchase agreement to constitute a sale transaction. It was held that a hire- purchase agreement has two elements, such as element of bailment and element of sale. The element of sale fructifies when the intending purchaser exercises the option after fulfilling the terms of agreement. At the time when hire- purchase agreement is entered into there is no taxable event of sale taking place. The essence of a sale is that the property shall pass from the seller to the buyer when the contract of sale is made except in a case of conditional sale. Hire- purchase agreements are not conditional sale.<sup>723</sup> The declaration of law in *Johar's case* was reaffirmed in *Second Instalment Supply Ltd's case*<sup>724</sup>, by differentiating the characteristics of instalment sale and typical hire- purchase agreement.

However the situation is different when a financier is acting as an intermediary between the seller and buyer to advance the balance purchase price and in such a case the relationship between the financier and the car dealers is

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<sup>723</sup> *Marikar (Motors) Ltd v. Sales Tax Officer*, [1967] 19 STC 18 (SC).

<sup>724</sup> *The Instalment Supply Ltd v. Sales Tax Officer*, [1974] 34 STC 65 (SC).

only that of a mortgagee - mortgagor and transaction between the financier and customer is not a sale<sup>725</sup>. It is also material to note that the registration with authorities is made in the name of hirer and only an endorsement as to the hire-purchase is made in the registration certificate<sup>726</sup>.

When the obligation between the financier is only to pay the amount actually advanced and not to pay the full value of the vehicle, and there is no transfer of property from the financier to customer to constitute a sale<sup>727</sup>. To find out the true nature of transaction the Court has to look through or behind the documents leading to the transaction and to get at the reality<sup>728</sup>. Likely, it is well settled that for determining as to which category a particular contract comes under, the court has to look at the substance of the agreement and not at the mere words describing the category<sup>729</sup>.

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<sup>725</sup> *Union Credit Corporation Ltd v. State of West Bengal*, [1955] 6 STC 246 (Calcutta).

<sup>726</sup> *Dugar & Co. v. State of Tamil Nadu*, [1976] 37 STC 231 (Mad.).

<sup>727</sup> *Sundaram Finance Ltd v. State of Kerala*, [1966] 17 STC 489 (SC).

<sup>728</sup> *Polsky v. S & S Services*, [1951] All ER 185.

<sup>729</sup> *Supra*, n. 720 at p. 113.

In *Goodwill India Ltd v. State*<sup>730</sup>, it was held that a hire purchase agreement constitute sale when it is entered, irrespective of the factor that in general law on sale of goods it is not sale. However, the Court opined so, endorsing the competency of Parliament to legislate on the subject, not by a State legislature as in the case of *First Instalment Supply Ltd's case*<sup>731</sup>.

To settle these judicial controversies, the 46<sup>th</sup> Amendment to the Constitution, incorporated the hire purchase and instalment transaction to the sales tax net, by treating it as deemed sale. Moreover in modern times of commercial life, the hire purchase transactions are unique and the financiers usually enter into two kinds of transactions, first is with the distributors and other is with the customers<sup>732</sup>.

There can be transaction of purchase of goods by the financier, retaining the title of the goods until the last instalment is paid by the customer and secondly passes the

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<sup>730</sup> [1980] 45 STC 368 (Del.).

<sup>731</sup> *Instalment Supply (P) Ltd v. Union of India*, [1961] 12 STC 489 (SC).

<sup>732</sup> *Madras Credit & Investments Ltd v. State of Kerala*, [2004] 134 STC 264 (Ker.).

goods to the customer by way of a hire purchase agreement with delivery of goods. It is immaterial that the financier holds the title on the goods as security for the payment of price and there is a transfer of property and sale between the parties, to make the buyer as absolute owner<sup>733</sup>.

Anyway the expanded definition of sale in the State Sales Tax Statutes, in terms of the 46<sup>th</sup> Amendment to the Constitution of India, deals with transfer of property in goods and transfer of goods on hire-purchase. The principles enunciated in *Johar & Co's case*<sup>734</sup> is no more available in its restricted sense, as the ambit of deemed sale is expanded to include not only the transfer which takes place at the time of purchase when the option is exercised, but also to include the transfer of goods on hire-purchase<sup>735</sup>.

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<sup>733</sup> *Lloyds Finance Ltd v. Deputy Commercial Tax Officer*, [2006] 143 STC 625 (AP).

<sup>734</sup> *Supra*, n. 722.

<sup>735</sup> *Jay Bharat Credit & Investment Co. Ltd v. Commissioner of Sales Tax*, [2000] 120 STC 1 (SC).

After enlarging the compass of sale for the purpose of taxation, any kind of transfer of 'goods' and transfer of 'right to use goods' are turned into sale or deemed sale. Now the next issue appears for debate. For deciding a sale what constitute 'goods'. Is it tangible thing only? Or does it include incorporeal rights and other intangible property.

## **CHAPTER VIII**

# **Sale in relation to Tangibles and Intangibles**

Even from the ancient days, sale of goods by the trading community is one of the major revenue sources of the 'State'. However, the evasion of tax and avoidance of tax in the name of tax planning by the trading communities became the real headache for the tax administrators. Though the tax evasion can be controlled by strict implementation of provisions of law, the State still is incapable to control the tax avoidance, as it is legally permissible. Large volume of tax was thus, safely passed up by the trade community.

Consequently, the States are much eager to enhance the revenue, either by regulating tax avoidance or by extending the fields of taxation. As a consequence, Parliament of India, by 46<sup>th</sup> Amendment to the Constitution, had sheltered the State's interest in revenue enhancement, by way of expanding the ambit of "sale", which was,

previously, hardly curtailed in the celebrated decision of the Apex Court in *Gannon Dunkerley's case*<sup>736</sup>.

Nevertheless, a mere constitutional guarantee could not resolve the problems of tax avoidance. The issues again appear for discussions, when the trading community attempted to avoid the tax on transactions of intangible property and benefits, stating that these intangible properties and benefits does not appear the features of the “goods”, either statutorily defined or under common or commercial parlance. Their contention is that only personal chattels forms the expression, ‘goods’ and copyrights, patents and trademarks etc. are not personal chattel to fall within the definition of goods<sup>737</sup>.

### **8.1. Meaning of Goods.**

The term goods defined in the Constitution as “goods’ includes all materials, commodities and articles<sup>738</sup>.

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<sup>736</sup> *State of Madras v. Gannon Dunkerley & Co.*, [1958] 9 STC 353 (SC).

<sup>737</sup> Prof. P.S. Atiyah, *The Sale of Goods*, 8<sup>th</sup> edn. at p. 50.

<sup>738</sup> *Constitution of India*, Art. 366 (12) reads as “goods” includes all materials, commodities and articles.

In its wider meaning the “goods” is described as everything that is capable of ownership<sup>739</sup>.

“Goods” means all kinds of movable property and the term movable property when considered with reference to goods cannot be taken in to its narrow sense<sup>740</sup>. As well, any thing, material or immaterial, which can satisfy the human needs, is treated as goods in economic parlance<sup>741</sup>. In its wider connotation, the goods is defined as to include every kind of movable properties like stocks, shares, growing corps, grass and things attached to or forming part of the land, which are agreed to be served before sale or under the contract of sale other than actionable claims and money<sup>742</sup>. It means the substance of the expression ‘goods’

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<sup>739</sup> *Mohamed Kabir v. Government*, 15 Deccan L.R. 60, cited in *Nizam Sugar Factory Ltd. v. Commissioner of Sales Tax*, 8 STC 61 at p. 67.

<sup>740</sup> *Commissioner of Sales Tax v. M.P. Electricity Board*, [1970] 25 STC 188 (SC).

<sup>741</sup> *Nizam Sugar Factory Ltd. v. Commissioner of Sales Tax*, [1957] 8 STC 61 at p. 68.

<sup>742</sup> The Sale of Goods Act, 1930 S. 2 (7) defines **Goods** as follows,

‘Goods’ means every kind of movable property other than actionable claims and money and includes stocks and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be served before sale or under the contract of sale.

differs greatly according to the context where it is used for consideration<sup>743</sup> and it depends on the character and scope of the enactment in which the expression is used<sup>744</sup>.

## **8.2. Significance of Character of the Property.**

The definition of movable property is also very wide to include every description, except immovable property<sup>745</sup>. It includes corporeal property of every description, except land and things attached to the earth or permanently fastened to anything, which is attached to the earth<sup>746</sup>.

Of course, in sales tax law, taxable event is not only the traditional sale, but also the passing of movable goods in the course of fictional sale, in its wider ambit. The levy

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<sup>743</sup> Lord Sumner in *In re Noordam (No.2)*, [1920] AC 904 at p. 909.

<sup>744</sup> *R v. Dickinson*, [1920] 3 K.B. 552 at p. 555.

<sup>745</sup> The General Clauses Act, 1897, S. 3(36) defines “Movable Property” shall mean property of every description, except immovable property.

S. 3(26) defines “Immovable Property” shall include land, benefits arise out of land and things attached to the earth, or permanently fastened to anything attached to the earth.

<sup>746</sup> Indian Penal Code, 1860, S. 22 defines movable property, as follows,

The word “movable property” are intended to include corporeal property of every description, except land and things attached to the earth or permanently fastened to anything, which is attached to the earth.

depends on the nature and potentiality of commodity in transaction and the sales tax usually known as one of the methods of commodity taxation. Goods or commodity is interchangeable terms denote an article of trade, a movable article of value, something that one can buy and sell<sup>747</sup>.

A sale of movable property is subject to taxation if the property is transferred from the seller to buyer in the course of trade or business for cash or deferred payment or for other valuable consideration. It denotes every transfer of movable property is an incident of taxation under Sales Tax or Value Added Tax. However the Court refused to accept the wider connotation given to goods and movable property in the general statutes and held that the collocation of the words used in the general definitions apparently suggest only to include tangible goods or tangible movable property and not any kind of intangible right.<sup>748</sup> If we go for the definition in general statutes, it is beyond doubt, that it can include the tangible immovable properties also like standing

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<sup>747</sup> *U.S. v. Sisco*, D.C. Wash. 226 F. 1001 quoted in *Words and Phrases*, Volume 7A, Permanent Edition, West (1940) at p. 590.

<sup>748</sup> Per Sarjoo Prasad, J., in *State of Bihar v. Rameshwar Jute Mills Ltd*, [1953] 4 STC 179 (Pat.) at p. 185.

trees, but for the purpose of determination of sale for levy of tax, standing trees cannot be considered as goods.<sup>749</sup> But there cannot be a universal rule in this aspect that the law settled by foreign courts viewed it differently. In *Duppa v. Mayo*<sup>750</sup>, it was observed that wherever at the time of the contract it is contemplated that the purchaser should derive a benefit from the further growth of the thing sold from further vegetation and from the nutriment to be afforded by the land, the contract may be considered as for an interest in land. But, where the process of vegetation is over, or the parties agree that the thing sold shall be immediately withdrawn from the land, the land is to be considered as mere warehouse of the thing sold and the thing contracted takes the features of goods. Interestingly, from the definition of goods, in the sales tax statutes<sup>751</sup>, it can be

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<sup>749</sup> *Husenali Adamji & Co v. Commissioner of Sales Tax*, [1956] 7 STC 88 (Nag.).

<sup>750</sup> (1671) 1 Saund 287, The observations of Lord Coleridge, C.J., is quoted in *Sultan Ahmed Rowther v. State of Madras*, [1954] 5 STC 166 (Mad.) at p. 170.

<sup>751</sup> The Central Sales Tax Act, 1956, S. 2 (d) defines “goods” as follows,

“Goods” includes all materials, articles, commodities and all other kinds of movable property, but does not include news papers, actionable claims, stocks, shares and securities.

seen that the definition is narrower than the meaning of goods in the general statutes, that for the purpose of taxation, certain things are excluded from the purview of the goods.

However, in its wider connotation, it was explained that properties, which are capable of being abstracted, consumed and used, transmitted, transferred, delivered, stored or possessed, are goods for the purpose of sales tax<sup>752</sup>. Besides, evidently the connotation of 'goods' noted in the Constitution is also wider, as it is an inclusive definition to take all materials, commodities and articles.

### **8.3. Meaning of Property.**

The property is defined as 'things and rights considered as having a money value'<sup>753</sup>. It includes all property whether corporeal or incorporeal and subject matter of a right of property can be either a material or an

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<sup>752</sup> *Commissioner of Sales Tax v. Madhya Pradesh Electricity Board*, 1969 (1) SCC 200.

<sup>753</sup> *Vikas Sales Corporation v. Commissioner of Commercial Taxes*, AIR 1996 SC 2082.

immaterial thing<sup>754</sup>. The great author on Jurisprudence, Paton<sup>755</sup>, elaborately classified different ambits of a “thing” as it also mean a thing which exists in the physical world but is not material in the popular sense such as electricity and a thing which is nether material, corporeal nor tangible but is an element of wealth such as a copy right and a patent.

Property in its legal sense and constitutional dimension means an aggregate of rights, which are guaranteed and protected by law<sup>756</sup>. It extends to every

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<sup>754</sup> P.J. Fitzgerald, *Salmond on Jurisprudence*, 12<sup>th</sup> edn, Sweet & Maxwell (London) (1966) at pp. 156 and 461.

<sup>755</sup> Paton, *Jurisprudence*, 2<sup>nd</sup> edn., Charendon Press (1951) at p. 409 explains, A thing may mean

- (a) a thing in the material sense which is corporeal and tangible and has an organic or physical unity, e.g. a horse or a block of marble.
- (b) a thing which is corporeal and tangible, but consists of a collection of specific things, e.g. of flock of sheep;
- (c) a thing which exists in the physical world but is not material in the popular sense; e.g. electricity;
- (d) a thing which is neither material, corporeal, nor tangible but is an element of wealth; e.g., a copy right or a patent;
- (e) a thing which is not material and which is not directly an economic asset or element of wealth; e.g. a reputation.

<sup>756</sup> *Jilubhai Nanbhai Khachar v. State of Gujarat*, AIR 1995 SC 142.

species of valuable rights and interest, more particularly, ownership and exclusive right to a thing, the right to dispose of the thing in every legal way, to possess it, to use it and to exclude every one from interfering with it<sup>757</sup>. It is the most comprehensive of all terms which can be used, inasmuch as it is indicative and descriptive of every possible interest which a person can have<sup>758</sup>.

The extended meaning of the term 'property' is 'every species of valuable right and interest'. It includes everything that is subject to ownership and has an exchangeable value or which goes to make up wealth or estate irrespective of its nature that corporeal or incorporeal, tangible or intangible, visible or invisible or real or personal.<sup>759</sup> The ownership may be either legal and beneficial or even private<sup>760</sup> and it embraces a group of

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<sup>757</sup> *Dwarkadas Srinivas v. Sholapur Spinings and Weavings Co Ltd.*, AIR 1954 SC 119.

<sup>758</sup> Ramanatha Aiyer, *The Law Lexicon*, Reprint edn. (1987) at p. 1031.

<sup>759</sup> *Labberton v. General Gas Co. of America*, 53 Wash.2d 180.

<sup>760</sup> *Davis v. Davis*, 495 S.W. 2d. 607, 611.

rights to possess<sup>761</sup> to use and enjoyment for lawful purposes<sup>762</sup>.

Correspondingly, in *J.K. Trust v. Commissioner of Income Tax*<sup>763</sup>, the Supreme Court had an occasion to examine the meaning of property and observed that property is a term of the widest import and subject to any limitation or qualification, which the context might require; it signifies every possible interest which a person can acquire, hold or enjoy. It is observed in *Philco Exports case*<sup>764</sup> that it is a term of far-reaching conception and it is comprehensive enough to take in all types of proprietary rights. Property is a general term that has its widest interpretation to refer to the property of every kind tangible or intangible, debts and chose in action to include a right to receive the annual cash settlement<sup>765</sup>.

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<sup>761</sup> *Cereghino v. State*, 230 Or., 439, 370 P. 2d 694, 697.

<sup>762</sup> *Hoffmann v. Kinealy*, 389 S.W. 2d. 745.

<sup>763</sup> AIR 1957 SC 846 at p. 849: [1957] 32 ITR 535 (SC).

<sup>764</sup> *Philco Exports v. Sales Tax Officer*, [2001] 124 STC 503 (Del.).

<sup>765</sup> *Madan Mohan Pathak v. Union of India*, AIR 1978 SC 803.

#### **8.4. Relevance of Tangibility and Intangibility.**

The property in its larger import signifies things and rights as having money value, especially with reference to transfer or succession, which includes the rights such as trademarks and patents and other rights *in rem*<sup>766</sup>. Goodwill<sup>767</sup> and right to the proceeds<sup>768</sup> is property. An incorporeal right of copy right<sup>769</sup>, inventions and designs<sup>770</sup>, intangible thing of electric energy<sup>771</sup> and a mere chance for a prize or a right and beneficial interest to participate in a draw<sup>772</sup> are treated as property of which its transfer is

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<sup>766</sup> See *Black's Law Dictionary*, 6<sup>th</sup> edn. 1990.

<sup>767</sup> *Howell v. Bowden*, 368 S.W. 2d 842, 848. See also in *Commissioner of Income Tax v. B.C. Srinivasa*, AIR 1981 SC 972

<sup>768</sup> *Harris v. Harris*, 83 N.M. 441, 493 P. 2d 407 at p. 408.

<sup>769</sup> *Meyiappan v. Commissioner of Commercial Taxes*, [1967] 20 STC 115 (Mad.)

<sup>770</sup> *New Delhi Municipal Committee v. State of Punjab*, AIR 1997 SC 2847.

<sup>771</sup> *Commissioner of Sales Tax v. Madhya Pradesh Electricity Board*, 1969 (1) SCC 200; [1970] 25 STC 188, See *County of Durham Electrical Co. v. Commissioner of Inland Revenue*, (1909) 2 KB 604. See also *State of Andhra Pradesh v. NTPC Ltd*, 2002 (5) SCC 203, *Municipal Committee, Harda v. Harda Electric Supply Co. (P) Ltd*, AIR 1964 MP 101 at p. 106 and *Kumbakonam Electric Supply Corporation Ltd v. Joint Commercial Tax Officer*, [1963] 14 STC 600.

<sup>772</sup> *H. Anraj v. State of Tamil Nadu*, [1986] 61 STC 165.

exigible to the levy of tax under respective sales tax statutes, being the sale of goods.

Yet, an interesting aspect is that whether the gas or steam is tangible or intangible property. Of course the gas supplied in the containers or cylinders is an article of merchandise subject to taxation, however cannot be considered as tangible property in its real form. However, steam is held to be as tangible property subject to levy of sales tax, as 'it is visible, it has weight, and it can be felt at any rate to the detriment of the person venturing to feel it'<sup>773</sup>. In *Nizam Sugar Factory's case*<sup>774</sup>, the Andhra Pradesh High Court, considered the scope of goods in its widest amplitude to say that even some of the daily necessities, such as air and water, though freely available, in the economic point of view, are 'goods, when these are controlled and made available to the citizens for a cost'<sup>775</sup>.

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This ratio was doubted in *Sunrise Associates v. Government of NCT of Delhi*, 2000 (10) SCC 420 and referred to Larger Bench and finally overruled in *Sunrise Associates v. Government of NCT of Delhi*, [2006] 145 STC 576 (SC).

<sup>773</sup> *Supra*, n. 741 at p. 69.

<sup>774</sup> *Ibid.*

<sup>775</sup> *Id.* at p. 68.

According to Privy Council, the gas also takes the character of goods<sup>776</sup>. Additionally, in the scientific sense, anything that has weight, occupies space, offers resistance and capable to transfer by motion are goods, irrespective of its corporeal existence. The conclusion is that even transfer of intangible property is sale in the extended meaning rendered to the concept of sale, when the nature of thing is identified with its importance in the market.

### **8.5. Relevance of Physical Possession.**

As well, electricity is “goods”, though it is an intangible object, which is generated in projects and transmitted through sub-stations and housed in buildings.<sup>777</sup> Merely because electrical energy is not tangible or cannot be moved or touched like a piece of wood or a book it cannot cease to be movable property when it has all the attributes of such property<sup>778</sup>.

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<sup>776</sup> *Erie County Natural Gas & Fuel Co. Ltd v. Carrol*, [1911] A.C. 105 (PC).

<sup>777</sup> *State of Andhra Pradesh v. NTPC Ltd*, 2002 (5) SCC 203 (CB) (SC): [2002] 127 STC 280 (SC).

<sup>778</sup> *Commissioner of Sales Tax v. MP Electricity Board*, [1970] 25 STC 188 (SC): [1969] 2 SCR 939.

Possession or transfer of a thing need not be physical.<sup>779</sup>

As observed by an American Court, considering the scientific nature of electricity, it has been believed to be a highly subtle, imponderable fluid, identical with lightning, which pervades the pores of all bodies and is capable of motion from one body to another<sup>780</sup>. Electricity is movable in such a manner that continuity of supply and consumption starts from the moment the electrical energy passes through the meters and sale simultaneously takes place as soon as meter reading is recorded and the moment the electricity is supplied and recorded in the meter the consumption also take place concurrently<sup>781</sup>. All the three phases or steps, sale, supply and consumption take place without any interval and from the very nature of this transaction; it is worth to hold that it is a saleable commodity<sup>782</sup>.

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<sup>779</sup> *Kumbakonam Electric Supply Corporation Ltd v. Joint Commercial Tax Officer*, [1963] 14 STC 600.

<sup>780</sup> *Spensely v. Lancashire Ins. Co.*, 54 Wis. 433. 442, 11 NW 894).

<sup>781</sup> *Indian Aluminium Co. v. State of Kerala*, 1996 (7) SCC 637.

<sup>782</sup> *State of Andhra Pradesh v. NTPC Ltd*, 2002 (5) SCC 203 (CB) (SC): [2002] 127 STC 280 (SC) at p. 297.

## **8.6. Transfer of Technical Know-how.**

Differing from the above views, it was urged before the Supreme Court in *Associated Cement Companies* case that transfer of technical know how will not be subjected to taxability<sup>783</sup>. Further, the technical know how is in the forms of drawings and designs, though for valuable consideration in the money form or not, is only constituted ideas, is an intangible property and not “goods”. However rejecting the above contention, the Apex Court held that at the moment the information or advice is put in media, whether paper or diskettes or in any other thing, and sold in lieu of money, the things become a chattel, exigible to tax<sup>784</sup>. Identically, the contention that licence fee attached to the right to use the software cannot be regarded as goods, also was repelled by the Court in *State Bank of India’s case*<sup>785</sup>. The verdict is very obvious to say that the intellectual input is

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<sup>783</sup> See the arguments in *Associated Cement Companies Ltd v. Commissioner of Customs*, 2001 (4) SCC 593.

<sup>784</sup> *Associated Cement Companies Ltd v. Commissioner of Customs*, 2001 (4) SCC 593 at para 33.

<sup>785</sup> *State Bank of India v. Collector of Customs*, (2000) 1 SCALE 72 (SC).

not free from taxation if it transferred to others in a commercial transaction by acquiring its value.

The Kerala High Court in the case of *Mechanical Assembly System*<sup>786</sup> by following the ratio in *Associated Cement Companies case*<sup>787</sup> further added that transfer of technology in any manner either through a tangible media like floppy discs or CDs or even through a deputing personal would constitute sale for the purpose of levy of sales tax. It was further explained that technical know-how can also be transmitted, transferred, delivered, stored or possessed etc. and will constitute a “goods” in its wider connotation<sup>788</sup>. When technical material is supplied for value consideration, it takes the characteristics of goods and the transfer of such material is nevertheless sale for the purpose of taxation.

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<sup>786</sup> *Mechanical Assembly System (India) Pvt. Ltd v. State of Kerala*, [2006] 144 STC 536 (Ker.).

<sup>787</sup> *Supra*, n. 784.

<sup>788</sup> *Supra*, n. 786 at p. 544.

## 8.7. Intellectual Property and Software.

Series of instructions issued to the hardware of a computer enabling its performance, namely software, is nothing but an intangible thing<sup>789</sup>. It can certainly be sold to the customers, being housed in a tangible media such as floppy disk or CD ROM. Such encoded instructions and designed programs are perfectly goods<sup>790</sup>. Apparently, an intellectual property when it is put on a media becomes goods<sup>791</sup>. Computer programmes are the product of an intellectual process, but once implanted in a medium, it is inextricably linked with the corporeal object. Consequently, it is tangible, movable and available in market as goods<sup>792</sup>. For deciding identity of software as 'goods' it is immaterial that a software programme, both a system software or

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<sup>789</sup> A computer software or software can be defined as a general term primarily used for digitally stored data such as computer programme and other kind of information read and written by computers. See Sebastian Engelhardt, "The Economic Properties of Software", *Jena Economic Research Papers*, Vol.2, Max-Planck Institute of Economics, University of Jena, (2008) at p.5.

<sup>790</sup> *St. Albans City and District Council v. International Computers Ltd*, (1996) 4 All ER 481 at p. 493.

<sup>791</sup> *Toby Construction Products Pvt. Ltd v. Compura Bar (Sales) Pvt. Ltd*, (1983) 2 NSW 48.

<sup>792</sup> *Advent Systems Ltd v. UNISYS Corporation*, 925 F 2d 670.

application software is only used to achieve a certain result in a computer<sup>793</sup> and it cannot be an end product, like a music cassette. The fact that information can be transferred and then physically recorded on another medium does not make the computer software any different from any other type of recorded information that can be transferred to another medium like in film tapes, video and audio tapes, printed books etc.

Even though the information and instructions are put into an intangible form, software can be stored in the tangible medium, by several methods. The developer of the programme could program it manually at the location of the user's computer, working from his own instructions. A remote programming terminal located in far away place from the user's computer could programme the software, with the input information being transmitted by electro magnetic ways, through cable or cable less communication

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<sup>793</sup> *PSI Data Systems Ltd v. Collector of Central Excise*, 1997 (2) SCC 78. The Judgment was doubted in *Commissioner of Central Excise v. Acer India Ltd*, 2004 (10) SCC 111, and referred to a larger Bench. The Three Judges Bench in *Commissioner of Central Excise v. Acer India Ltd*, 2004 (8) SCC 173 affirmed the ratio in the case of *PSI Data Systems Ltd*.

device. A developer can store the programmed software by use of magnetic tapes or discs, which is a usual method in the trading of software. When a user buys the computer, usually it is pre-loaded with the systems software accompanied by a tangible device, in which the software is stored to enable the user to exploit it, for trouble-shooting and it is in the nature of after sale service. Even though there is no separate charging for the tangible device supplied along with the master computer, it is separate goods, marketable in economic parlance<sup>794</sup>.

According to the observations of American Courts, it is the intellectual process which is embodied in a physical manner; the logic or the intelligence of the program remains intangible property<sup>795</sup>. It is true that while transforming, converting, or organising some intangible ideas, plans, procedures, formulas etc, no manufacturing takes place that a material thing is not the subject of transformation or

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<sup>794</sup> *Commissioner of Central Excise v. Acer India Ltd*, 2004 (8) SCC 173 at para 67.

<sup>795</sup> *Northeast Datacom, Inc. et al v. City of Wallingford*, 563 A 2d 688.

conversion<sup>796</sup>. But such an arrangement of intangible ideas are more than a transfer of mere knowledge, but transfer of instructions physically recorded on some tangible media, to perform a desired function, which is nevertheless a corporeal thing<sup>797</sup>. Physical recording of software itself ceases its nature as incorporeal right.

A buyer of computer software acquires an intangible intellectual property right for limited use without having an absolute right or ownership, except to the particular copy of the software, as usually the copyright of the software is retained by the developer or marketer. The problems of piracy are also substantially regulated in the field of software, by sufficient cyber control devices through internet. What is transferred is an intangible knowledge recorded in physical medium for performance of the user's computer in a desired manner, to constitute a tangible personal property.

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<sup>796</sup> *Interactive Information Systems, Inc. v. Limbach*, [1985] 18 Ohio st. 3d, 311. [Supreme court of Ohio].

<sup>797</sup> *South Central Bell Telephone Co. v. Sidney J. Barthelemy*, 643 So. 2d 1240 [Supreme Court of Louisiana].

Though the supply of branded software in corporeal forms are held to be sale, in case of unbranded software, indeed the same is an intellectual property satisfying the test of capability, but a product of service contract amenable to works contract tax. The Andhra Pradesh High Court in the decision in *Tata Consultancy*<sup>798</sup> had observed that all intellectual properties may not be 'goods' and being an intellectual property, unbranded software might perhaps be outside the ambit of goods. However, the Apex court, approving the key issue in appeal, opined that the unbranded software too is capable of being abstracted, consumed and used and also can be transmitted, transferred, delivered, stored, possessed, etc. and may takes the characteristics of 'goods' when it is marketed or

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<sup>798</sup> *Tata Consultancy Services v. State of Andhra Pradesh*, [1997] 105 STC 421 (Andhra). The appeal against this judgment was considered by the Apex Court in *Tata Consultancy Services v. State of Andhra Pradesh*, [2001] 122 STC 198 (SC) and referring to a large number of case laws originated in different countries, the question was referred to a larger bench. The Constitution Bench in *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620 (SC), upheld the judgement of the Andhra Pradesh High Court *Tata Consultancy Services v. State of Andhra Pradesh*, [1997] 105 STC 421.

sold, but left this issue open for further scrutiny<sup>799</sup>. It is pertinent to note that in *Acer India Ltd's case*<sup>800</sup>, the Apex Court found that, even if the information contained in software is loaded in a hard drive, like operational software, it is also marketable commodities and does not lose its character as tangible goods.

### **8.8. Test to Determine Nature of Goods.**

In the strict interpretation of taxing statutes, the tangibility or intangibility of a thing is not a relevant criterion for the purpose of levying tax on the transaction of such things. In the taxing statutes, the test to determine a property as 'goods' for purposes of sales tax is not whether the property is tangible or intangible or incorporeal<sup>801</sup>. The Apex Court invented that the test is whether the thing is capable of abstraction, consumption and use and whether it can be transmitted, transferred, delivered, stored or

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<sup>799</sup> See majority judgment delivered by S.N. Variava, J in *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620 (SC) (CB) at para 26.

<sup>800</sup> *Commissioner of Central Excise v. Acer India Ltd*, [2004] 8 SCC 173 at para 83.

<sup>801</sup> *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620 at p. 633.

possessed<sup>802</sup> irrespective of its tangibility or intangibility. It is so, because, in India, the expression and context used in the Constitution with respect to the definition of 'goods' is very wide and to include all types of movable properties.

## **8.9. Test regarding Articles of Merchandise.**

### **(a) Music Disc or Cassettes.**

A music composed definitely as an intellectual work by the artistry of a musician by itself is not a good for sale, on the other hand when the same is hosted in media of disc or cassette, it becomes a readily mercantile commodity having the characteristics of property exigible to tax. A blank cassette, of course, is an article of merchandise. When an intellectual work of music is recorded in the blank cassette, a corporeal media, there is a value addition in the post recorded cassette and the value of the intangible artistry work is subjected to taxation, as held by the Apex Court in *Gramophone Co.'s case*<sup>803</sup>.

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<sup>802</sup> *ibid.*

<sup>803</sup> *Gramophone Co. of India Ltd v. Collector of Customs*, JT 1999 (9) SC 275.

**(b) R.E.P. Licences.**

Whether a licence is tangible or intangible is widely discussed in various case laws particularly with reference to the replenishment license. Replenishment licences, usually known as REP licences, are issued by the Controller of Imports and Exports to the manufacturer to enable them to import replenish materials used for the production of goods which are exported<sup>804</sup>. These licences are transferable to other parties by issuing a formal letter detailing the descriptions of the licence<sup>805</sup>. It was urged that the REP licence is an entitlement in the nature of a grant and is an actionable claim<sup>806</sup>. The Court ruled out this contention and held that the license has no physical existence however can be a bundle of rights<sup>807</sup>. It is not a mere beneficial right in respect of movable property and not

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<sup>804</sup> *Bharat Fritz Werner Ltd v. Commissioner of Commercial Taxes*, [1992] 86 STC 170 (Kar.).

<sup>805</sup> See *Import and Export Policy- 1990-93*, Ministry of Commerce, Government of India at para 199.

<sup>806</sup> *Supra*, n. 804.

<sup>807</sup> *Id.* at p. 174.

merely enables a person the right of indulging in a business of importing goods but also it excludes competition<sup>808</sup>.

The Court held that the right or privilege or entitlement of any right conferred by a license is crystallised or incorporated in a physical document, hence has a corporeal existence, thus taxable as an article of merchandise<sup>809</sup>. A licence generally may not assure any estate or interest absolutely<sup>810</sup> and it may permit an action lawful, which without it had been unlawful<sup>811</sup>. REP licences are goods, otherwise, because these licences are capable of buy and sell freely in the market as goods and even they have value of their own unrelated to the goods which can be imported there under<sup>812</sup>.

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<sup>808</sup> *Hemant Spices v. Assistant Commissioner*, [1994] 95 STC 336 (Ker.).

<sup>809</sup> *P.S. Apparels v. Deputy Commercial Tax Officer*, [1994] 94 STC 139 (Mad.).

<sup>810</sup> *Frank Warr & Co. v. London County Council*, [1904] 1 KB 713.

<sup>811</sup> *Thomas v. Sorrel*, [(1674) Vaugh 351] referred in *Frank Warr & Co. v. London County Council*, [1904] 1 KB 713.

<sup>812</sup> *Vikas Sales Corporation v. Commissioner of Commercial Taxes*, AIR 1996 SC 2082; [1996] 102 STC 106 (SC).

**(c) DEPB Licences.**

Likewise, transfer of Duty Entitlement Pass Book, commonly called as DEPB, which is a scheme allowing to neutralize the incidence of basic customs duty on the import content of the export product, by way of grant of duty credit against the export product, also held to be sale<sup>813</sup>, as it is a right to claim back credit which is freely tradable, like REP Licences. It is an article of merchandise and is treated and dealt with as such in the commercial world and in no

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<sup>813</sup> *Philco Exports v. Sales Tax Officer*, [2001] 124 STC 503 (Del.).

way it is a chose in action<sup>814</sup> or an actionable claim<sup>815</sup> and transfer of DEPB is sale exigible to sales tax.<sup>816</sup>

#### **(d) Lottery Tickets.**

Another controversial subject in sales tax is concerning the character of lottery tickets. Even from the initial stage of the controversy the main argument was that sale of lottery tickets does not amount to transfer of property in goods but only purchase of a chance of winning a prize and is an agreement by way of wager.<sup>817</sup>

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<sup>814</sup> Chose in Action means things of which the owner has no actual possession but has only right which can be realised by an action and includes a debt, the benefit of a contract and damages for wrong.

<sup>815</sup> Transfer of Property Act, 1882, defines actionable claim, as follows,

“Actionable claim” means a claim to any debt, other than a debt secured by mortgage of immovable property or by hypothecation or pledge of movable property, or to any beneficial interest in movable property not in the possession, either actual or constructive, of the claimant, which the Civil Courts recognise as affording grounds for relief, whether such debt or beneficial interest be existent, accruing, conditional or contingent.

This definition was incorporated in the Act by insertion by Act 2 of 1900.

<sup>816</sup> *Supra*, n. 813 at p. 514. See also in *Liberty Enterprises v. State of Haryana*, [2007] 5 VST 12 (P&H).

<sup>817</sup> *Commissioner of Commercial Taxes v. Shri Dipak Dhar*, [1986] 61 STC 131 (Calcutta).

Lottery is a scheme of distribution of prizes by lot or chance. Essential elements of a lottery are consideration, prize and chance and it includes any scheme or device by which a person for consideration is permitted to receive a prize<sup>818</sup>. In *Sesha Ayyar's case*<sup>819</sup>, the Madras High Court identified the elements of lottery as a prize or some advantage in the nature of prize, distribution thereof by chance and consideration paid or promised for purchasing the chance. Going by these propositions, essentially, lottery tickets are tokens of the right to participate in the scheme.

While purchasing a lottery ticket, offer is made which is based on the happening of some event, but, it was argued that, transfer cannot be said to be made or effected in pursuance of a contract for the sale or purchase of goods. While contesting in a lottery, a game of hazard in which small sums are ventured with the chance of obtaining a large value, either in money or things<sup>820</sup>, the only legal right remaining with the participant is the claim for the

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<sup>818</sup> *Bartlett v. Parker*, [1912] 2 KB 497.

<sup>819</sup> *Sesha Ayyar v. Krishna Ayyar*, AIR 1936 Mad. 225.

<sup>820</sup> *Horner v. United States*, 147 US 449.

return of his contribution in limited circumstances<sup>821</sup>. Lottery is a consolidation of prize, chance and consideration, as when one purchase a lottery ticket, he purchases for a prize, which is by chance and the consideration is the price of the ticket and that may be for receiving nothing<sup>822</sup>.

The beneficial rights under a contract are assignable unless the contract is personal in its nature or rights are capable of assignment either under a prescription of law or a contract<sup>823</sup>. Likely, the benefit due to be arrived from a lottery ticket would be assignable and there is a transfer of beneficial interest in movable property in favour of the purchaser while purchasing a lottery ticket.<sup>824</sup> The entitlement to a right to participate in the draw is an entitlement to beneficial interest, which is of incorporeal or intangible nature<sup>825</sup>.

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<sup>821</sup> *Barclay v. Pearson*, [1893] 2 Ch 154.

<sup>822</sup> *B.R. Enterprises v. State of U.P.*, [2000] 120 STC 302 (SC).

<sup>823</sup> *Khardah Company Ltd v. Raymon & Co. (India) Pvt. Ltd*, AIR 1962 SC 1810.

<sup>824</sup> *H.Anraj v Government of Tamil Nadu*, [1986] 61 STC 165 (SC): AIR 1986 SC 63.

<sup>825</sup> *Id.* at p 182.

Right to participate in the draw under a lottery ticket remains the valuable right till the draw takes place and it is for the reason the sellers are enabled to effect sales thereto till the draw actually takes place and therefore lottery tickets, not as physical article but as a memoranda evidencing the right to participate in the draw can be regarded as dealer's merchandise and goods which are capable of being bought or sold in the market<sup>826</sup>. It is immaterial that such lotteries are paper lotteries or on-line lotteries, as in both cases, the tickets are sold in retail outlet directly to the customers<sup>827</sup>.

It was held that sale of lottery ticket is a composite and divisible contract. There is transfer of a right to participate in the draw which takes place on the sale of lottery tickets, which is a transfer of goods as held in *Anraj II case*<sup>828</sup>. Concurring with the said view, in *Nirmal*

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<sup>826</sup> See concurring Judgment of Sabyasachi Mukharji, J., in *H.Anraj v Government of Tamil Nadu*, [1986] 61 STC 165 (SC) at para 47.

<sup>827</sup> *Pan India Network Infravest Pvt Ltd v. State of Kerala*, [2006] 144 STC 502 (Ker.)

<sup>828</sup> *Supra*, n. 825.

*Agency's case*<sup>829</sup>, the Karnataka High Court held that to the extent of sale of lottery that it involves the transfer of the right to claim a prize, depending on a chance, it is an assignment of an actionable claim and not a sale of goods.

Nevertheless, the decisions of foreign courts considered the right of a participant in lottery as chose in action. It was held by the High Court of Australia<sup>830</sup> that the person in whose name the lottery ticket issues obtains the legal title to what is a chose in action. In *Jones v. Carter*<sup>831</sup> it was held that what was assigned in a lottery is a chose in action. If it is a chose in action, then following the observation in *Philico Exporters's case*<sup>832</sup> it cannot be a goods exigible to sales tax. However the ratio in Anraj's case got approval in *Vikas Sales Corporation*<sup>833</sup> to hold that the transfer of beneficial rights amounts to transfer of property in goods.

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<sup>829</sup> *Niramal Agency v. Commercial Tax Officer*, [1992] 86 STC 450 (Kar.)

<sup>830</sup> *Van Rassel v. Kroon*, [1953] 87 CLR 298.

<sup>831</sup> [1845] 8 QB 134.

<sup>832</sup> *Supra*, n.813.

<sup>833</sup> *Supra*, n.812.

To summarise, the consequential legal position is that the physical existence of property or any beneficial rights is immaterial to attract the levy of tax. It is that every article of merchandise, even otherwise not excluded from the taxation, is subjected to sales tax. An article of merchandise whenever used in a taxation statute must always be understood in common parlance and must be given its popular sense, means the sense with which people are conversant and while dealing with the articles would attribute to it<sup>834</sup>.

### **8.10. Right to Use Intangible Goods.**

When transfer of intangible goods is sale, transfer of right to use the intangible goods is also sale, after the extension of scope of sale. Trademarks<sup>835</sup> are goods and

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<sup>834</sup> *Parle Biscuits (p) Ltd v. State of Bihar and Others*, [2005] 139 STC 204 at p. 214.

<sup>835</sup> S. 2(1)(v) of the Trade and Merchandise Marks Act, 1958 defines Trademark as,

“Trade mark” means (i) in relation to Chapter X (other than Sec.81), a registered trade mark or mark used in relation to goods for the purpose of indicating or so as to indicate a connection in the course of trade between the goods and some person having the right as proprietor to use the mark; and

all incorporeal rights including copyrights, patents, trademarks and other rights in personam which are capable of transfer or transmission are included in the ambit of

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- (ii) in relation to other provisions of this Act, a mark used or proposed to be used in relation to goods for the purpose of indicating or so as to indicate a connection in the course of trade between the goods and some person having the right, either as proprietor or as registered user, to use the mark whether with or without any indication of the identity of that person, and includes a certification trade mark registered as such under the provisions of Chapter VIII.

The Trade and Merchandise Mark Act, 1958 was repealed by the Trade Marks Act, 1999 and in Section 2(1) (zb), the Trade Mark is defined as follows, with some changes from its earlier definition.

“Trade Mark” means a mark capable of being represented graphically and which is capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colours; and

- (i) in relation to Chapter XII (other than Section 107), a registered trade mark or mark used in relation to goods or services for the purpose of indicating or so as to indicate a connection in the course of trade between the goods or services, as the case may be, and some person having the right as proprietor to use the mark; and
- (ii) in relation to other provisions of this Act, a mark used or proposed to be used in relation to goods or services for the purpose of indicating or so as to indicate a connection in the course of trade between the goods and services, as the case may be, and some person having the right, either as proprietor or by way of permitted user, to use the mark whether with or without any indication of the identity of that person, and includes a certification trade mark or collective mark.

It is relevant to note that in the Trade and Merchandise Mark Act, 1958, S. 2(1) (g) and the Trade Marks Act, 1999, S. 2(1) (j) the “Goods” is defined as “Goods” means anything which is subject of trade or manufacture.

goods<sup>836</sup>. When owner transferred the trademark to enable marketing of other's products under the terms of agreement receiving a consideration in return, by way of royalty there is transfer of right to use the trademark. For transferring the right to use the trademark, it is not necessary to hand over the trademark to the transferee or give him the control or possession<sup>837</sup>. Simply by retaining the right for himself to use trademark, the owner cannot say what he is transferred is only right to enjoy. It can be done merely by authorising the transferee to use the same in the manner required by the law and it is a deemed sale for the purpose of levy of sales tax. It is also relevant that the right to use the trademark can be transferred simultaneously to any number of persons<sup>838</sup>.

When the cases on the subject of the sale element in mobile services and supply of SIM cards to the customers came up for consideration, the large stress was on the contention that passing of intangible benefit cannot be

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<sup>836</sup> *Supra*, n. 833.

<sup>837</sup> *Commissioner of Sales Tax v. Duke & Sons Pvt. Ltd*, [1999] 112 STC 370 (Bom.).

<sup>838</sup> *SPS Jayam v. Registrar, TNTST*, [2004] 137 STC 117 at p. 124.

treated as sale but only services<sup>839</sup>. Though the supply of prepaid SIM cards is held as sale, the transfer of facilities and intangible right to use the wireless routes for the post paid customers are untouched by the Courts. If the capability test<sup>840</sup> invented by the Apex Court is functional, the transfer of right to use the mobile route by the post-paid customers, though it is intangible property of the mobile service providers, is necessarily a sale with valuable consideration. Consequently, the transfer of right to use the cyber ways to a customer, by an Internet service provider, is nothing but a transfer of right to use an intangible benefit, amounting to sale, as maintained by the capability test, evolved by the Supreme Court.

When some chemicals are consumed in the process of rendering services of anti-termite treatment, the out

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<sup>839</sup> *Escotel Mobile Communications Ltd v. Union of India and others*, [2002] 126 STC 475 (Ker.); (2002) 10 KTR 318 (Ker.). This decision was reversed in *BSNL v. Union of India*, [2006] 145 STC 91 (SC).

<sup>840</sup> See the concurring Judgement of S.B. Sinha, J in *Tata Consultancy Services v. State of Andhra Pradesh*, (2004) 137 STC 620 (SC) (CB) at p. 655. It was held, “A ‘goods’ may be tangible property of an intangible one. It would become goods provided it has attributes thereof having regard to (a) its utility; (b) capable of being bought and sold; and (c) capable or transmitted, transferred, delivered, stored and possessed.”

come is that there is no transfer of goods in identifiable form or in tangible form. Even after the introduction of 46<sup>th</sup> Amendment to the Constitution of India, the expanded definition of deemed sale covers only the transfer of goods in its original form or in some other form<sup>841</sup>. Here the appealing aspect is that goods do not exist in any form. The Court held that after the process of spraying and applying pesticides, nothing tangible remains in which property is transferred and there is no sale of chemicals during the service contract.<sup>842</sup> Likely, when explosives are consumed in the process of display of fire works, the explosives themselves ceased to exist and there no property in tangible form remains to constitute the transaction as sale<sup>843</sup>. Thus, the apparent suggestions of the courts are that if the goods alleged to be transferred is not in its identifiable or tangible forms, after consumption, there cannot be any transfer of property to constitute the sale.

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<sup>841</sup> Clause (29-A) inserted in Article 366 of the Constitution of India by the Constitution (Forty- sixth Amendment) Act, 1982. Clause 29 A (b) includes a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract.

<sup>842</sup> *Pest Control India Ltd v. Union of India*, [1989] 75 STC 188 (Pat.).

<sup>843</sup> *Deputy Commissioner v. M.K. Velu*, [1993] 89 STC 40 (Ker.).

### **8.11. SIM Cards and Lottery: Transformation in Judicial Thinking.**

The Judicial wisdom is a matter of random transformations. In the fifties of the last century, the Judiciary was very keen in restraining the 'meadow of commodity taxation', with strict interpretation of terms as per the traditional trade meanings. Resultantly, in *Rameshwar Jute Mills*<sup>844</sup>, the Court without any hesitation held that the transfer of quota of 'loom hours' by members of Jute Mills Association, to other member mills is not a sale, but only transfer of abstract rights of intangible incorporeal property. In series of cases, the Apex Court had showed its strict and conservative approach to put off the state actions to catch every transfer under the scheme of sales tax, treating the transfer as the sale. However, the Courts in current times are more conscious to sanctify the wider scope of tax incidence, as evidenced in the cases of *Associated Cement Companies*<sup>845</sup> and *Tata Consultancy*

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<sup>844</sup> *State of Bihar v. Rameshwar Jute Mills*, [1953] 4 STC 182 (Patna) at p. 185.

<sup>845</sup> *Associated Cement Companies Ltd v. Commissioner of Customs*, 2001 (4) SCC 593.

*Services*<sup>846</sup>. The legislature is also keen to elucidate the new areas to enlarge the tax revenue. Consequently, the new value added legislation has included all intangible goods<sup>847</sup> under the purview of VAT.

Further, it is to be noted that the pendulum of judicial consistency again collapsed the pro-revenue prescriptions laid down by the Apex Court in *Anraj*<sup>848</sup>, *Vikas Sales Corporation*<sup>849</sup>, *Associated Cements Companies*<sup>850</sup> and *Tata Consultancy Services*<sup>851</sup>. In *BSNL's case*<sup>852</sup>, the Apex Court, through the Constitution Bench held that not every transfer in subscription of telephone facilities amounts to sale. The Court overruled its earlier findings in *State of Uttar Pradesh v. Union of India*<sup>853</sup> wherein it was held that

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<sup>846</sup> *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620.

<sup>847</sup> Item 3 of the Third Schedule to the Kerala Value Added Tax Act, 2003 covers all intangible goods like copyright, patent, REP License, DEPB License etc. to levy VAT at the rate of 4%.

<sup>848</sup> *Supra*, n. 825.

<sup>849</sup> *Supra*, n. 833.

<sup>850</sup> *Supra*, n. 845.

<sup>851</sup> *Supra*, n. 846

<sup>852</sup> *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 145 STC 91 (SC).

<sup>853</sup> AIR 2003 (SCW) 695.

the activities of telecommunication department are sale exigible to sales tax.

Only if an apparatus is provided for the subscriber for consideration, it is definitely a sale of movable property. But mere transfer of electronic waves from the apparatus of the subscriber through the channels of the service provider will not come under the extended meaning of sale being the transfer of right to use the media of the service provider. It is merely a service provided by the telecommunication network provider and it was held that the sale of SIM cards and recharge cards are not exigible to sales tax, being it a supply of a medium to transfer of electronic waves.

Even if an apparatus is provided, if it is on rental basis, can it be a sale of apparatus or transfer of right to use the apparatus? Telephone facility is not merely installation of telephone instrument at the customer's residence; it is in fact maintenance of a system at an exchange which exchange is connected by way of the instrument, which is placed at the customer's place. The apparatus in itself is a useless thing unless it is connected to a system. It becomes only a service once it is connected

to a system by the Department and as such there is no transfer of any tangible thing to the customer, except providing the facility of telecommunication, which in no stretch of imagination contemplates elements of sale<sup>854</sup>.

The Court again departed from its earlier view of transfer of right during the participation in draw of Lottery. In *Sunrise Associate's case*<sup>855</sup> the two judge's bench of the Supreme Court doubted the views in *Anraj's case*<sup>856</sup> and opined that there was no good reason to split a lottery into separate rights, firstly right to participate in the draw and secondly right to win the prize depending on the chance. The reference made to a larger bench was decided in the affirmative in *Sunrise Associates v. Government of NCT of Delhi*<sup>857</sup> and found that the key reason for the *Anraj's*<sup>858</sup> decision is that an actionable claim is not assignable and lottery being it coupled with the assignable claim cannot be

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<sup>854</sup> *Union of India v. Government of Andhra Pradesh*, [1999] 113 STC 203 at para 22.

<sup>855</sup> *Sunrise Associates v. Government of NCT of Delhi*, 2000 (10) SCC 420.

<sup>856</sup> *Supra*, n. 825.

<sup>857</sup> [2006] 145 STC 576 (SC).

<sup>858</sup> *Supra*, nn. 825 & 856.

considered as actionable claim<sup>859</sup>. It was held that transferability is not the point of distinction between the actionable claim and other goods, which can be sold.

A lottery ticket, itself being a valueless piece of paper, was finally held as a token or evidence of the chance or a right to a conditional benefit of winning a prize of a greater value than the consideration paid for the transfer of that chance<sup>860</sup>. It is equally an actionable claim, which is assignable<sup>861</sup>, like negotiable instruments, right to claim any benefit of the contract<sup>862</sup>, a claim for arrears of rent,<sup>863</sup> etc.

The Apex Court later held, mere participation in a draw after paying the token for participation is not a transfer of right, consequently not a sale in its extended meaning. Consequently lottery is only an agreement by way of wager, which is permissible under S. 30 of the Indian

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<sup>859</sup> *Sunrise Associates v. Government of NCT of Delhi*, [2006] 145 STC 576 (SC) para 39.

<sup>860</sup> *Id.* at p 594.

<sup>861</sup> *Bharat Nidhi Ltd v. Takhatmal* [1969] 39 Comp Case 114 (SC): (1969) 1 SCR 595.

<sup>862</sup> *Union of India v. Sri Sarada Mills Ltd*, 1972 (2) SCC 877 at p. 880.

<sup>863</sup> *State of Bihar v. Maharajadhiraja*, [1952] SCR 889.

Contract Act<sup>864</sup>. It is only an actionable claim, which is specifically excluded from the definition of sale, which is exigible to tax under Sales Tax Statutes.

Following the judgment of the Apex Court in *Sunrise Associates case*<sup>865</sup>, the State is now prevented from expanding the tax net to catch the sale of tickets by Railway, Airlines Companies and Bus Agencies, as the purchase of tickets gives the right to a person to travel, which is nothing but a contract of carriage.

Nevertheless, the question of sale element in transfer of intangible beneficial rights is awfully problematical. What constitute a sale? The nature or physical existence, tangibility and intangibility of the commodity are immaterial to conclude a sale in the eye of taxation law. If a commodity is an article of merchandise or answer the capability test, of course the transfer constitute sale and such an incidence justify its taxation. Except in the case of telecommunication network and lottery, the concept of article of merchandise is

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<sup>864</sup> *Peter v. State of Kerala*, 2007 (2) KLT 532 at para 10. See also in *Subhash Kumar Manwani v. State of Madhya Pradesh*, AIR 2000 MP 109.

<sup>865</sup> *Supra*, n. 857.

approved as the best test to determine the taxability of intangible rights. With regard to the lottery, it is identified as actionable claim, which is out side the purview of taxable goods.

## CHAPTER IX

### **Sale under E- Commerce**

The concept of sale has a gradual growth by extending its meaning, either by judicial declarations or by legislative sanctions. As well, the growth of technology also contributed to the enlargement of its scope by adding some other incidence, which is lacking in the traditional requirements of sale.

#### **9.1. Evolution and Significance of E-Commerce.**

E-commerce is one of the latest contributions of technological growth. E-commerce consists of the buying, selling, marketing and servicing of products or services over the computer networks<sup>866</sup>. Originally, internet or “electronic commerce” facilitated commercial transactions, including sale, electronically. It is usually for limited purpose, by using technology like Electronic Data Interchange, to send the commercial documents like

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<sup>866</sup> Aashit Shah and Parveen Nagree, *Legal Issues in E-commerce*, Nishith Desai Associates, published in [www.nishithdesai.com](http://www.nishithdesai.com), (2005) at p. 3.

purchase orders or invoices electronically, in sale of goods. But, it has developed from a mere means of communication to a mode of carrying on commercial activity itself<sup>867</sup>.

The ongoing development in information technology facilitates sale and purchase of goods and services over the World Wide Web via secure servers, specially designed for confidential ordering data keeping customer protection<sup>868</sup>, and with the help of e-shopping cards and with electronic pay services, like credit and debit cards.

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<sup>867</sup> *Satyam Infoway Ltd v. Sifynet Solutions Pvt. Ltd*, AIR 2004 SC 2540 at para 12.

<sup>868</sup> The technology of exchange of things in Cyberspace is a unique one. Each host computer providing Internet services ("site") has a unique Internet address. Users seeking to exchange digital information (electronic mail ("e-mail"), computer programs, images, music) with a particular Internet host require the host's address in order to establish a connection. Hosts actually possess two fungible addresses: a numeric "IP" address such as 123.456.123.12, and an alphanumeric "domain name" such as microsoft.com, with greater mnemonic potential. *See* Internet domain names are similar to telephone number mnemonics, but they are of greater importance, since there is no satisfactory Internet equivalent to a telephone company white pages or directory assistance, and domain names can often be guessed. A domain name mirroring a corporate name may be a valuable corporate asset, as it facilitates communication with a customer base. *See* the discussion in *The Internet Unleashed*, Sams Publishing, 1994 and also in Philip Elmer-Dewitt, "Battle for the Soul of the Internet", *Time*, July 25, 1994 at p. 50.

Simply speaking, e-commerce is the mode of conducting business through electronic means. The wider definition of e-commerce includes all business activities conducted using a combination of electronic communications and information processing technology, that is the process of using electronic methods and procedures to conduct all forms of business activities. It is understood to mean the production, marketing, sale or delivery of goods and services by electronic means<sup>869</sup>.

## **9.2. Scope of E-commerce Sales.**

Any product that can be digitalised is amenable to sale and delivery, electronically. This would include books, newspapers, CDs, motion pictures, photographs, airline and movie tickets, and video and sound recordings. Even the saleable commodities like patent, designs and trademarks, that can be digitally converted, can also be the object of electronic commerce, whether in the form of a

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<sup>869</sup> *The Work Programme on Electronic Commerce: Background Note by the Secretariat of the Council for Trade Related Aspects of Intellectual Property Rights*, World Trade Organization. See also in A Didar Singh, *Electronic Commerce; Issues of South; Trade Related Agenda, Development and Equity, Working Paper*, South Centre, Oct.1999 at P.4.

total transfer or in the form of some limited transfer of rights only.

E-commerce has a vital role in the areas of entertainment industry. A wonderful movie having international recognition can be downloaded and seen through websites by paying charges. Any books attained worldwide popularity can be read in a website for its viewers by paying charges, in all over the world. A newly introduced song of an admired pop singer can be access and store by his admirers around the world, through the browsing and downloading. While watching such a movie or reading such a book or listening such a song, certainly transfer of information takes place.

Though it cannot be termed as sale in its traditional sense, but in the new technological era such traditional notion has little reverence. In the foregoing examples, the data can be down loaded and re-recorded in tangible media, too in the memories of hard drive for its future use or for a future transfer to others. Such valued information can be abstracted, consumed or used and capable for delivering and storing. Following the dictum in Tata

Consultancy's case<sup>870</sup> such delivery of information more less constitutes sale

### **9.3. Passing of Consideration and Digital Cash.**

Passing of value consideration is one of the other concerns of e-contracts. The debit<sup>871</sup> and credit card sales are very common, now a days and insertion of card numbers in the appropriate columns of website pages allows the payment of consideration. However, such payments are subject to allotment of security codes. Payments are accepted only on the unilateral consent of the seller and the buyer has no option. The instrumental growth in e-commerce has necessitated the evolution of

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<sup>870</sup> *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620 (SC).

<sup>871</sup> Debit Cards are pre paid cards issued by the Banks, in due course of its general banking transactions. The basic principle of prepaid cards is simple. You store a particular amount of money, which the owner of the card pays in advance to the issuing instance after storing value in it by cash or by debiting an account. The process of payment is marked by the fact that the party accepting the card (for example, retail merchant) debits the amount of money which owed from the card. Thus, the card owner remains anonymous, and there is no expensive and time-consuming process of authorization for the card issuer. An examination of the authenticity of the card takes place with the help of cryptographic processes directly at the payment recipient's terminal. The electronic units of value which are received do not have to be collected individually, but can be collected together from the card issuer by means a debit.

other electronic payment mechanisms also. Such a necessity opened the way of digital currencies, like CyberCash<sup>872</sup> and E-cash<sup>873</sup> that enables the sale and purchase of commodities over internet and or carrying on other commercial activities.

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<sup>872</sup> *CyberCash* permits secure transactions through complex routing transaction. The system was created by the CyberCash.inc founded in Reston of Virginia, 1994. For detail discussion and procedure see <http://www.paypal.com>.

<sup>873</sup> E- cash involves purchasing 'units' and 'credits' from a bank to a particular value in a particular currency which can be used to trade on Internet. The seller of goods can take e-cash units and either use it to buy some other goods on the Internet or redeem it at participating banks for its own country's currency. It is an electronic payment system introduced by a Netherlands based Company, DigiCash. E- Cash works as follows. Firstly a Customer places order at Merchant's web site and then Merchant securely transfers order information to E-Cash over the Internet via a proprietary Electronic Commerce Messaging Protocol (ECMP). E-Cash receives order information and performs requested services simultaneously. Then E- Cash routes transaction authorization request through payment processor to the appropriate card system. The card system contacts issuing bank (customer's bank) to request transaction authorization. Issuing bank returns authorization to card association, or if the transaction is not authorized, E-Cash returns a message to the merchant's system, to be requisitioned or cancelled. E-Cash receives transaction authorization and, if physical fulfilment is requested, sends an ECMP EDI message to the merchant or distribution centre authorizing order fulfilment. Merchant or distribution centre sends E-Cash an ECMP fulfilment notification to permit settlement, and E-Cash sends a settlement request to the issuing bank (customer's bank). If authorization is for the sale of a digitally delivered product or service, the settlement request is made synchronized with the authorization. Issuing bank approves transfer of money to acquiring bank (merchant's account).

E-cash is a computer-generated system, which allows items to be purchased by credit card, cheque or money order providing secure online transactions and processing. With the introduction of internet/ online banking, debit cards, online bill payments and internet business, paper money is becoming a thing of the past.

Being a part and parcel in the effective operation of E-commerce, banks now offer many services whereby a customer can transfer funds, purchase stocks and offer a variety of other services without having to handle physical cash or checks. Customers do not have to wait in lines; this provides a lower-hassle environment. Debit or Credit cards and online bill payments allow immediate transfer of funds from an individual's personal account to a business's account without any actual paper transfer of money. This offers a great convenience to many urban and business people alike<sup>874</sup>.

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<sup>874</sup> See *Report to the Council of the European Monetary Institute on Prepaid Cards*, The Working Group on EU Payment Systems, May, 1994. The report is published in the website <http://ecominfocenter.com/index.html?page=/services/merchants/legal.html> visited on 1-10-2008.

#### **9.4. Problems in Digital Cash.**

Nevertheless, in E-commerce sales, there are some hidden hazards, either in payment of consideration or in the quality and marketability of goods put for sale. Although there are many benefits to digital cash, there are also many significant disadvantages. These include fraud, failure of technology, possible tracking of individuals and loss of human interaction. Fraud over digital cash has been a pressing issue in recent years. Hacking into bank accounts and illegal retrieval of banking records has led to a widespread invasion of privacy and has promoted identity theft.

There is also a pressing issue regarding the technology involved in digital cash<sup>875</sup>. Power failures, loss of records and undependable software often cause a major setback in promoting the technology. Privacy questions

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<sup>875</sup> Edgar Meister, *Speech on Electronic Cash*, speech at the annual meeting of the Federal Association of German Money and Valuables Transport Companies on November 28, 1996 in Frankfurt. The speech is published in the website <http://ecominfocenter.com/index.html?page=/services/merchants/legal.html> visited on 1-10-2008

have also been raised; there is a fear that the use of debit cards and the like will lead to the creation by the banking industry of a global tracking system. Some people are working on anonymous e-cash to try to address this issue. It means the E-commerce sale, though now a days, universally accepted, is not a foolproof mechanism to substitute the traditional sale.

### **9.5. Relative Issues of E-Commerce Sale.**

E-commerce, either in E-shopping of physical things or intangible things, faces some challenging issues compared to the traditional sale. Whether any effective transfer is being done during the downloading of information while net surfing, is one of such issue which warrants debate. Transfer of 'goods' is essential for constituting the 'sale'. Transfer of intangible thing such as 'Technical know-how' is treated as the sale of goods, even if they are not in tangible form<sup>876</sup>. Transfer of intellectual property, either in tangible form like branded software or in intangible form like unbranded software developed in user's

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<sup>876</sup> *Associated Cement Companies Ltd v. Commissioner of Customs*, 2001 (4) SCC 593.

computer itself, takes the features of 'goods' for the purpose of taxation<sup>877</sup>. The principles of articles of mercantile quality or test of capabilities chiefly governs the field, as the apt test for deciding nature of a thing to satisfy the requirements of 'goods'

When an e-commerce service provider projects certain information to its customers, through the website, by charging money through credit card payments, and the customer only exploring such information to their mind only or even writing down it into their notebooks, can it be said that any transfer of goods are effected between the web site owners and customer. There is no intention to the viewers to purchase the information. The owners have no intention to sell their information to its viewers. There is only a momentary service by charging payments. There is no sale as such by transfer of any goods. Nevertheless, there are all other required elements to constitute sale. Information is not passing to the buyer in tangible media, unless it is recorded in Disks or in the Computer's Hard Drive.

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<sup>877</sup> *Supra*, n. 870.

It is as if a software is hosted in a client's computer from a remote programming terminal located in far away place to constitute transfer of intangible goods through communication devices. Too, it is the law that even if it is not recorded in tangible media, only passed through a deputing personal, there is transfer of property in goods exigible to the sales tax<sup>878</sup>. A momentary service of passing of information, which is a valuable intangible property, thus can be treated as sale for the purpose of taxation. The taxing authorities are seriously thinking to curb the situation of tax avoidance in like transactions.

### **9.6. Situs of Sale in E-commerce.**

While taxing a commodity, as an article of merchandise, there must be an incidence for tax, i.e., the sale. It is not that the commodity is subjected to tax, but it transfer as sale which is subjected to tax. In imposing the sales tax, one of the difficulties, which confront the Taxman, lies in the selection of the point of time at which the tax shall be attached and become due. In the case of

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<sup>878</sup> *Mechanical Assembly System (India) Pvt. Ltd v. State of Kerala*, [2006] 144 STC 536 (Ker.).

an ordinary retail sale for cash across the counter of shop, the stages of agreement, appropriation of the goods to the contract, delivery, payment of the price and passing of the property are all practically simultaneous<sup>879</sup>. On the other hand, in transactions like E- commerce, which are more complicated in nature, it is difficult to find out the stages in strict jacket.

When the act of sale is the subject of taxation, the place of sale has relevance. There must be a situs of sale. Sale consists of a number of ingredients, such as existence of goods which form the subject matter of the sale, a bargain or contract of mutual consent, which, when executed will result passing of the property in the goods for a price, the payment or a promise to pay the price and the passing of title<sup>880</sup>. When all take place in one place, there is no difficulty to ascertain the place of sale. When one or more ingredients take place at different places, it is difficult to find out the situs of sale.

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<sup>879</sup> *King v. Dominion Engineering Co. Ltd.*, [1951] 2 STC 67 (PC).

<sup>880</sup> *State of Bombay v. The United Motors (India) Ltd*, [1953] 4 STC 133 (SC) at p. 159.

In e-shopping, the situs of sale is not certain. It can be ordered from one place, payment can be effected from another place and the product can be accessed from a place other than the above two. 'Amazon.com', a well accomplished E-commerce Service Provider, registered its domain in United Kingdom advertised the product for sale through a link provided in an entertainment website hosted in Australia and an Indian Consumer purchased the product by accessing the website and by making payment through Credit Card provided by an International Credit Card Service Provider. There are cumulative incidents taking place to finalize the sale of the product. Can there be levy of sales tax in all places that is United Kingdom, Australia and India for a single occurrence of sale or in one of the places where the delivery effected. When the sale occurs with respect to a physical substance, and the sale being proximate cause of movement of goods from one place to another, there is a physical transfer of goods by way of delivery either by shipping or by a parcel agency or by an international courier agency. Can it be an Import with

respect to India and Export with respect to United Kingdom?

If the place of hosting the website and place of ordering the product are two places within India, whether such kind of transaction satisfies the requirement of inter-state sale under S. 3 of the Central Sales Tax Act, 1956<sup>881</sup>. The essential characteristics of an inter-state sale are no way debatable at least after NTPC's case<sup>882</sup> in which the

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<sup>881</sup> The Central Sales Tax Act, 1956, S. 3 reads as follows,

**When is a sale or purchase of goods said to take place in the course of inter-state trade or commerce.**- A sale or purchase of goods shall be deemed to take place in the course of inter-State trade or commerce if the sale or purchase,-

- (a) occasions the movement of goods from one State to another; or
- (b) is effected by a transfer of documents of title of goods during their movement from one State to another.

Explanation 1: Where goods are delivered to a carrier or other bailer for transmission, the movement of the goods shall, for the purpose of clause (b), be deemed to commence at the time of such delivery and terminate at the time when delivery is taken from such carrier or bailee.

Explanation 2: Where the movement of goods commences and terminates in the same State it shall not be deemed to be a movement of goods from one State to another by reason merely of the fact that in the course of such movement the goods pass through the territory of any other State.

<sup>882</sup> *State of Andhra Pradesh v. NTPC*, [2002] 127 STC 280 at para 25. In the judgment the essential ingredients of the Inter-state Sale are enumerated as follows,

law on inter-state sale is well settled by a larger bench of Apex Court.

Sale or purchase of goods shall be deemed to have been taken place in a particular place, wherever the contract of sale or purchase might have been made, if the goods are within such place at the time of contract of sale or purchase is made, in cases of specific and ascertained goods. However the law is laid down that in case of unascertained or future goods, sale takes place at the time of appropriation to the contract of sale or purchase by the seller or by the purchaser, whether or not the assent of the other party is prior or subsequent to such appropriation<sup>883</sup>. It is only when the transfer of ownership of goods passes the sale or purchase is completed. The sale or purchase occurs in the place where the transfer of ownership takes

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- (a) There must be a contract of sale, incorporating a stipulation, express or implied, regarding inter-State movement of the goods;
  - (b) The goods must actually move from one State to another, pursuant to such contract of sale; the sale being the proximate cause of movement; and
  - (c) Such movement of goods must be from one State to another State where the sale concludes.

<sup>883</sup> *Haji K. Moidoo Bros. v. State of Madras*, [1959] 10 STC 1 (Ker.) (FB).

place or the property in the goods passes under the law relating to sale of goods<sup>884</sup>.

When there is a sale by domestic supplier the liability to remit the tax almost always falls on such suppliers. But in cases of foreign supplier, such a liability cannot be insisted upon him and such tax administration is not possible.

### **9.7. Identical to Telephonic or VPP Sales.**

Such a problematic field can be tackled by adopting simple propositions. In cases dealing with telephone contracts, the recognised proposition is that the contract is concluded at the place where the acceptance is conveyed to the seller. That is the place where the seller is. The same proposition can apply to electronic contracts also. However, when a multi-place transfer takes place and the law compels that sale means a completed transaction by which property in goods passes, the place in which the

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<sup>884</sup> *Badische Aniline Un Soda Fabrik v. Basle Chemical Works*, [1898] A C 200.

property in goods passes would be the location of sale<sup>885</sup>. Before the property in goods passes the contract of sale is only executory and retains to the buyer a right of chose-in-action and there is no real sale<sup>886</sup>.

In E-shopping, the process is more or less identical to the VPP (Value Payable Post) sales, but there are substantial differences in certain aspects. The VPP system is designated to meet the requirements of persons who wish to pay for the articles sent to them at the time of the receipt of the articles or of the bills or railway receipts relating to them. It is also to meet the requirements of the traders or others who wish to recover through the agency of the Post Office, the value of the articles supplied to them<sup>887</sup>.

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<sup>885</sup> *India Copper Corporation Ltd v. State of Bihar*, [1961] 12 STC 56 (SC).

<sup>886</sup> *Burmah Shell Oil Storage & Distributing Company of India v. Commercial Tax Officer*, [1960] 11 STC 764 (SC).

<sup>887</sup> See Clause 186 of the Post Office Guide, Department of Posts, Director General of Posts, Government of India, (1985).

**186. Value Payable Post.** - The value payable system is designed to meet the requirements of person who wish to pay for articles sent to them at the time of receipt of the articles of the bills or railway receipts relating to them, and also to meet the requirements of traders and others who wish to recover through the agency of the Post Office the value of the article supplied by them.

In VPP Sales, the goods handed over to the post office by the seller and it can only be delivered to the buyer against payment received by the authorities of the post office, which is for and on behalf of the seller<sup>888</sup>. The payment to the post office is the payment to the seller under the agency relationship<sup>889</sup>. VPP sales are statutorily recognised<sup>890</sup>, the sale is completed on completion of certain stipulation and the seller retains control over the goods right up to the time the goods are delivered to the buyer against the payment of price. Sale is completed when the Post Office delivers the chattel to the buyer and payment is received by them on sellers' behalf<sup>891</sup>.

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<sup>888</sup> *Commissioner of Income- Tax v. P.M. Rathod & Co.*, [1959] 10 STC 493 (SC).

<sup>889</sup> *Mothi Rungaya Chetty v. The Secretary of State for India*, (1904) ILR 28 Mad. 213.

<sup>890</sup> VPP Sales are coming under the purview of the Section 25 (1) of the Sale of Goods Act, 1930, which says "Where there is a contract for sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation, reserve the right of disposal of the goods until certain conditions are fulfilled. In such case, notwithstanding the delivery of the goods to the buyer, or to a carrier or other bailee for the purpose of transmission to the buyer, the property in goods does not pass to the buyer until conditions imposed by the seller are fulfilled."

<sup>891</sup> *In re the Parchim*, [1918] AC 157 at p. 170.

In E-shopping, the delivery is effected, either through the Post or through other carriers. The payments are pre-paid at the time of order and the seller despatches the goods only after payment received. Until physical delivery is effected to the buyer by the carrier, no sale is completed. This factual position support the proposition that sale completed only at the place where the actual delivery occurs, that is the buyer's place. However, if the carrier is the agent of buyer, on his request, the position will be different, as the delivery of goods to the carrier at the place of the seller, completes the sale<sup>892</sup>.

### **9.8. Features in E-commerce Sale.**

Sale is an out come of a contract and formation of any contract would involve three main ingredients<sup>893</sup>. There has to be an offer, there has to be an acceptance of

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<sup>892</sup> *Badische Anilin Und Soda Fabrik v. The Basle Chemical Works*, [1898] AC 200.

<sup>893</sup> S. 3 of the Indian Contract Act, 1872, reads as follows,

**Communication, acceptance and revocation of proposals.-**  
The communications of proposals, the acceptance of proposals, and the revocation of proposals and acceptances, respectively, are deemed to have made by any act or omission of the party proposing, accepting or revoking, by which he intends to communicate such proposal, acceptance or revocation, or which has the effect of communicating it.

the said offer without any modification or revocation and there has to be some consideration for the contract. Of course, in e-commerce sale contracts also, the ingredients are essential to form a valid contract for legal enforceability. Since the e-commerce contracts are executed or in certain circumstances performed through internet communication, a direct communication between the proposer and proposee is not possible, unless it is through online chats. Usually the offer and acceptances are passing between the parties through e-mails as the ordinary means of communication.

A binding contract is constituted by acceptance of an offer. The acceptance must be reaching the seller and at that time the contract is completed. During an electronic offer and acceptance a number of questions will arise. Can a mere action of downloading be considered as the acceptance? The user may discard a surfed material, visuals, or writings. A clicking on the options in the websites cannot be a full acceptance of the information, though the sellers intended for an offer through the website. Without the use of encryption technology, the reliability and

acceptability of email, is an added difficulty<sup>894</sup>. In systems in which electronic messages are sent, over communication networks, it is certainly possible for someone to prepare and transmit an E-mail message and to make it appear that it came from someone other than the true maker

### **9.9. Jurisdictional Issues in E-commerce Sale.**

Another legal issue in internet contracts on sale is the Jurisdictional issue. When e-commerce enables transaction of sale, cross borders<sup>895</sup> there is unavoidable ambiguity regarding jurisdiction and law applicable, while terms of contract are violated or performance of e-contracts is breached. Parties to a contract formed through the internet may be located in different jurisdictions which may have implications for the interpretation and enforcement of the e-contracts. Is it the municipal law of the country or the law of other party having foreign jurisdiction covers the field

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<sup>894</sup> *Michael Doherty v. Registry of Motor Vehicles, Commonwealth of Massachusetts*. The case report is published in the website [http://ecominfocenter.com/index.html? page=/ services/emerchants/legal.html](http://ecominfocenter.com/index.html?page=/services/emerchants/legal.html), visited on 1-10-2008.

<sup>895</sup> For example Amazon.com, an e-commerce service provider has the chain of business covering 160 Countries, though they have situated in United States of America.

of litigation? According to the traditional rules of private international law, the jurisdiction of a country only extends to individuals who are within the country or to the transactions and events that occur within the natural boundary of the country<sup>896</sup>.

In e-commerce transactions, if a business derives customers from a particular country as a result of their web pages, it may be required to defend any litigation that may result in that country. The result is that any content placed on a website should be reviewed for compliance with the laws of any jurisdiction where the seller wishes to market, promote or sell its products or services as it may run the risk of being sued in any jurisdiction where the goods are brought or where the services are availed of.

### **9.10. Theory of Minimum Contacts.**

The theory of minimum contacts resolves the issues, which would mean that even if a person is not physically present in a country, he can be sued in that foreign court as long as his website has minimum contacts with that

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<sup>896</sup> Cheshire and North, *Private International Law*, 11<sup>th</sup> edn. at p. 188

country. Thus a seller should insert appropriate choice of law and choice of forum clauses in the online sale contracts, which should specify the jurisdiction to which the parties to the contact would be subject to and such clauses are binding upon the parties<sup>897</sup>.

### **9.11. The Source or Residence Principles.**

The principles of source or residence are the popular method to decide the jurisdiction of taxing subject, in direct taxation. Under the said principles, the income is subject to tax where the income is sourced or the subject has the residence. However in taxing of E-commerce application of the principles may hit the regional balances, at least in cases where major portion of goods are sourced in one region and largely consumed in another region. In cases of countries, which are having vital monopoly on software and other digital exports, the application of source principles in E-commerce sale will result in regional imbalance, if the sales are not attributable through a permanent establishment in the other country. The principle of

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<sup>897</sup> *Compu Serve.Inc v. Patterson*, 89 F.3d 1257 (6<sup>th</sup> Cir.1996).

residence is also inapplicable in E-commerce sales, since majority of e-commerce service providers exist in cyberspace only. Of course, in such cases the residence of such sellers can be attributable to the location of the server that hosts the home website of the seller.

### **9.12. Concept of Permanent Establishment.**

The concept of 'Permanent Establishment' suggests that if the activity passes the permanent establishment in the source country, that country would have the primary right to tax the activity. The permanent establishment is defined in the OECD Model Tax Convention<sup>898</sup> to mean, the fixed place of business through which the business of an enterprise is wholly or partly carried on. It may be a place of management, a branch, an office, a factory or a workshop<sup>899</sup>.

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<sup>898</sup> Organization for Economic Co-operation and Development (OECD), "Electronic Commerce: Taxation Framework Conditions", *A Report by the Committee on Fiscal Affairs* (Oct-1998) at p.3

<sup>899</sup> *Model Tax Conventions: Four Related Studies: Issues in International Taxation*, No.4 (1992) as cited in Catherine A. Brown, "The Canadian Income Tax Treatment of Computer Software Payments", *Canadian Tax Journal*, Vol.42, Issue 3, (1994).

Where a person is acting on behalf of an enterprise and has habitually exercised an authority to conclude the contracts in the name of such enterprise, it is deemed that such enterprises shall have a permanent establishment in such place. However if a broker, general commission agent or any other agent of an independent status is acting in the ordinary course of their business, it cannot be said that the enterprise is having a permanent establishment in such place merely because on the reason that the business is carrying through such persons.

By following the above principles, the South African Court held in *Secretary for Inland Revenue v. Downing*<sup>900</sup> that when a foreigner left the management of domestic share portfolio in the hands of a stockbroker in that country, such agency will not constitute a permanent establishment. Thus a website hosted on a server owned by a domestic independent agent like an ISP (Internet Service Provider), would not constitute a permanent establishment<sup>901</sup>. A

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<sup>900</sup> 1975 (4) SA 518 (A).

<sup>901</sup> Cigler J.D., Burrit H.C. & Stnnest S.E., *Cyber Space- the final formtier for international tax concepts*, Price Water House, United States (November, 1996).

vendor's home page on the internet and the access of the internet provided to that homepage do not give rise to a permanent establishment, since the vendor does not have control over any of the appliances necessary for data transmission, in a country<sup>902</sup>.

However according to Zak Muscovitch, a web page is likely to constitute a permanent establishment in the country where the host computer resides<sup>903</sup>. It is because a web page can have a physical presence, as it is made from binary or digital code and is housed on a magnetic surface, usually a disk of some kind. Such a binary code is viewable using the computer and communication device<sup>904</sup>.

### **9.13. Concerns of Taxing E-commerce Sale.**

How far the sale be scrutinised by the taxing authorities for the purpose of levy of tax during the e-commerce sales? Which is the enjoined point of the sale

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<sup>902</sup> Hey F E F, "Permanent Establishment- Remote Controlled Pipeline German Court Rulling", *International Tax Notes*, Vol 8, No.8 (1997) at p. 651.

<sup>903</sup> Zak Muscovitch, "Taxation of Internet Commerce", *First Monday*, (December, 2005). The article is published in the website [http://131.193.153.231/www/issues/issues2\\_10/muscovitch](http://131.193.153.231/www/issues/issues2_10/muscovitch).

<sup>904</sup> *Ibid.*

transactions? The massive growth of e-commerce business does not have been seen by the tax authorities. Realising the potentials of earning tax from e-commerce sales, tax authorities are examining the tax implications of e-commerce transactions and resolving mechanisms to tax such sales<sup>905</sup>. Thus, execution, performance and taxation of e-commerce sale open a new area for debates.

It is true that the e-commerce in the developed countries is fastly growing, but in the developing or under developed countries it is in its infancy. It represents only below 1% of its total retail sales in those countries<sup>906</sup>. The problems of tax erosion in e-commerce sale are a larger issue in the developed countries. In the absence of tax on e-commerce sales, prospect of tax evasion among the high income group of the society, who can afford the technology of online shopping, is a common phenomena. This resulted

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<sup>905</sup> Gordon, Roger, "An Optimal Taxation Approach to Fiscal Federalism", *Quarterly Journal of Economics*, XCIIIX (1983) at p 568.

<sup>906</sup> Annette Nellen, "Taxation of E-commerce- Part 2", *Introduction to E-commerce Tax Issue*, San Jose State University (September 2000) at p 3.

in the issues of discrimination in taxing, by taxing of ordinary customers and leaving the high income group.

An e-commerce sale is just like a mail order sale or tele-shopping. When the seller has no presence in the taxing state, the levy and collection of tax is invariably difficult, and the seller is enjoying the sale transaction as tax free one<sup>907</sup>. Therefore, lack of geography is one of the major problems in taxing an e-commerce sale, but the taxman suggests to substitute the point of levy from sale to use, as the consumer of the sold commodity is certain and within the geographical territory of the taxing state, like levy of tax on purchase<sup>908</sup> in case of sale effected by unregistered dealers.

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<sup>907</sup> Goolsbee, Austan. "In a World Without Borders: The Impact of Taxes on Internet Commerce", *Quarterly Journal of Economics*, Vol. 115, No. 2, 2000.

<sup>908</sup> Beth Cox, "Sales Tax Still a Mystery to E-tailers", (February 26, 2004). The article is published in the website; <http://www.ecommerce-guide.com/news/trends/article.php/3318671>.

The author certifies that in Florida, the law says in general, e-commerce businesses (and any business doing any portion of its sales on the Internet) currently are required to charge sales tax only on purchases made by in-state customers.

### **9.14. Theory of Physical Presence.**

Widely accepted and the primary determinative factor regarding exigibility of sales tax on e-commerce is the physical presence of seller in the customer's state.<sup>909</sup> For determining whether seller has physical presence, or a level of activity, the significant tests are either it may be owning or renting property in that state or having a warehouse or a fulfilment house that maintains inventory for seller in that state or having employees in that state or promoting his business in that state through something like a trade show. If seller is shipping merchandise to a state where his business does not have a location, his sale will not attract sales tax.<sup>910</sup>

The Courts in the United States maintained a sensible legal outlook in this regard. The Court has held that when the seller or service provider has no activity in the location, but merely having a web presence, it would

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<sup>909</sup> *Navigating Sales Tax Laws*, E-commerce Guide, the book is published in the website <http://www.ecommerce-guide.com/essentials/ebiz/article.php/3656806>.

<sup>910</sup> See the website; <http://www.allbusiness.com/sales/internet-e-commerce/2652-1.html>.

not bring them within the state's jurisdiction to proceed against the seller<sup>911</sup>. In *National Bellas Hess, Inc's* case<sup>912</sup>, the U.S Supreme Court has held that the sellers could be required to pay use taxes only in the states where they maintained a certain level of physical presence. This was a major hit on the state's power to tax on the inter-state mail order or catalogue sales. Later the U.S. Supreme Court in *Quill's* case<sup>913</sup> has held that it is for the Congress to decide the scope of nexus theory to protect the interest of State's revenue.

Nevertheless, exceptions are there, as in the case of levy of tax on shipments of 'Amazon.com' to residents of the State of New York. The state of New York began collecting sales tax from 'Amazon.com', which is based in Seattle, and many of the retailers who sell goods through Amazon are New York-based. Amazon has filed a suit in the New York Supreme Court challenging the

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<sup>911</sup> *Millennium Enterprises v. Millennium Music*, 33 F. Supp. 2d 907 (1999), cited in Annette Nellen, "Taxation of E-commerce- Part 2", *Introduction to E-commerce Tax Issue*, San Jose State University (September, 2000) at p. 12.

<sup>912</sup> *National Bellas Hess, Inc v. Illinois*, 386 U.S. 753 (1967) at p. 758.

<sup>913</sup> *Quill Corporation v. North Dakota*, 504 U.S. 298 (1992) at p. 318.

constitutionality of the levy on the theory of physical presence of the seller.<sup>914</sup> The impugned regulation suggesting for deeming physical presence in the State includes any website based in the state that earns a referral fee for sending customers to an online retailer. 'Amazon.com' has thousands of affiliates that feature links to its products. The defence of Amazon is that its affiliates are not agents, but simply sites on which it places advertising against payment of commissions for those advertisements.

Likewise, when a UK resident purchases a chattel through e-commerce from USA, it is material to see that he is not obliged to pay tax on sale to United States, as the seller has no physical presence in United Kingdom. However, on reaching the chattel, for physical delivery in United Kingdom, the resident purchaser is liable to pay tax on the sale to United Kingdom Inland Revenue. When an

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<sup>914</sup> Saul Hansell, "Amazon Sues Over State Law on Collection of Sales Tax", *The New York Times*, (2-5-2008). This article is published in the internet edition of the daily hosted in the website; <http://www.nytimes.com/2008/05/02/nyregion/02amazon.html?ex=1367467200&en=0bd37583e0401630&ei=5124&partner=digg&exprod=digg>.

overseas buyer is purchasing a chattel from a United Kingdom based E-commerce provider, such sales are taxable in United Kingdom also<sup>915</sup>.

### **9.15. Problems in Identification of Parties to Sale.**

Identity of parties to a contract is one of the keen issues to be resolved while performing the e-contracts. Unlike communications of offer and acceptance through postal means, in internet communications, it is not possible to locate the exact place of the parties, in the first instance. It can be possible only through decoding of protocol addresses and through other technological solutions, which are time consuming and highly technical.

Transactions on the internet, particularly consumer-related transactions, resulting in sale contracts, often occurs between parties who have no pre-existing relationship, which may raise concerns of the person's

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<sup>915</sup> Simon Sweetman, "A Short Practical Note on E-commerce and Tax". The article is published in the website; <http://www.taxationweb.co.uk/businessstax/article.php?id=106>.

identity with respect to issues of the person's capacity, authority and legitimacy to enter into a contract<sup>916</sup>.

However the Information Technology Act, 2000 resolves these problems to certain extent by legalising the concept of 'Digital Signature' to determine the identity of persons to the contract. As per the IT Act, 2000 digital signatures should be used for the purposes of authenticating an electronic contract and it must follow the Public Key Infrastructure, "PKI".

The physical supervisions over the movement of goods are one of the prime concerns in taxing of e-commerce sales. In e-commerce, the majority of sales are relating to intangible goods, that is without the need to provide tangible personal property to the customer; sale can be effected through transfer of intangible properties.

In the olden days, the sales tax laws were mainly concentrating on taxing of tangible personal property only and digitalized products often are not subject of sales tax,

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<sup>916</sup> Aashit Shah & Parveen Nagree, "Legal Issues in E-commerce", Nishith Desai Associates. The article is published in the website; [www.nishithdesai.com](http://www.nishithdesai.com) (2005) at p. 4.

for one or other reasons. However, the change in the state's approach resulted in the inclusion of at least some digitalized products, like software, in the tax regime, in the last decades<sup>917</sup>.

In the traditional system of trading, with respect to the main street-retailers, the administration of tax is easier. The tax on sale is, of course, an indirect tax and it is the primary duty of the traders to collect and remit the tax to the State ex-chequer. However, the e-commerce business man may not be obliged to comply with such statutory requirements in the absence of regular supervision of his business. The role of consumption tax is significant in such situations. The liability, in such cases can be fastened on the importer or the person who consumes the goods. Such a method is adaptable in cases of supply of tangible properties.

In cases of electronic supply of intangible goods, domestically, there is no much difference, as the domestic dealer has an obligation to collect the tax and such trades

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<sup>917</sup> *Supra*, n. 870.

are subject to tax audit also. But difficulty may arise when the trader destroys his back-up. In cases of electronic supply of intangible goods by a foreign supplier, such supplies satisfy the requirement of import sale and the tax can be levied on the importer, who consumes such goods. Such use tax is usual, when the seller is incapable of taxing the sale, because he has no nexus with the destination state<sup>918</sup>.

It is an undisputed fact that E-commerce is having a dramatic impact on almost all aspects of business. It opened a global market with global suppliers across the nations. Though regulatory measures were introduced to regulate and protect the issues of intellectual property rights in the field of cyber space, the law on tax administration is not yet fully developed.

The consequence is that the technologically advanced and high earning society, who made the e-commerce as parallel market, is out of tax administration. So either the concept of sale tax should further be modified

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<sup>918</sup> Debra S. Callihan, "How Will Sales and Use Taxation Change in Response to E-Business", *State Tax Today*, August- 28- 2000.

to cover the field or the taxation jurisprudence should advance further by developing alternative devices to fill the gap.

## **Dilemmas of Indecisive Law Making**

It was an enormous and multifarious deal to investigate on the meaning of 'sale' as understood by the lawmakers and law Interpreters. The investigation of the subject exposed the growth of judicial scrutiny of the area under discussion during the last six decades. Starting form *Budh Prakash*<sup>919</sup> ending to *Rajasthan Chemist Association*<sup>920</sup>, the observations and conclusions are noted appropriately and discussed within the frame of time and space.

The attempt was not for an empirical study of the subject, as it was impossible, and the endeavour is only to investigate on the growth of the subject in the hands of Courts and Lawmakers.

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<sup>919</sup> *Sales Tax Officer v. Budh Prakash Jai Prakash*, [1954] 5 STC 193 (SC).

<sup>920</sup> *State of Rajasthan v. Rajasthan Chemist Association*, [2006] 147 STC 542.

Law making is definitely depending on expertise and knowledge of the drafter. While drafting a law, the draftsmen and the legislature is expected to be well aware of consequences of each and every expression used in the statute book. It must be either dynamic or flexible to the wants of time.

For clarity and certainty of statutory expressions, it is only legitimate to presume that every expression is used in the sense in which it was or is understood by the legal community in the Origin State<sup>921</sup> or in the recipient State<sup>922</sup>.

The principle is the same in case of interpretation of legislative power also. When a power is conferred to legislate on a particular topic it is important, in determining the scope of the power, to have regard to what is ordinarily treated as embraced within that topic in legislative practice and particularly in the legislative practice of the State which has conferred the power<sup>923</sup>.

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<sup>921</sup> *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.).

<sup>922</sup> *Peterswald v. Bartley*, 1 Com. L.R. 497.

<sup>923</sup> *Croft v. Dunphy*, [1933] AC 156.

For that reason, it was held by the Court in *Sales Tax Officer v. Budh Prakash Jai Prakash*<sup>924</sup> that the expression sale of goods should receive the meaning, which it was understood to bear in legislative practice of England and India before the Constitution Act, 1935, which introduced the entry to enable taxing of sale and purchase of goods<sup>925</sup>.

It was also suggested that an expression in the statute may be attracting a meaning of the broadest connotation.<sup>926</sup> In other words, the expression should be read in their ordinary, natural and grammatical meaning<sup>927</sup> subject to the rider that in construing the words in a constitutional enactment conferring legislative power, the most liberal construction should be put upon the words so that it may have effect in the widest amplitude<sup>928</sup>. The Courts also counter attacked the propositions of legislative

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<sup>924</sup> [1954] 5 STC 193 (SC): AIR 1954 SC 459.

<sup>925</sup> *The Government of India Act, 1935*, Seventh Schedule, Provincial List, Entry 48 reads, "Taxes on the sale of goods and on advertisements.

<sup>926</sup> *Navinchandra Mafatlal v. Commissioner of Income Tax*, [1954] 26 ITR 758 (SC).

<sup>927</sup> *State of Bombay v. F.N. Balsara*, [1951] 2 SCR 682.

<sup>928</sup> *James v. Commonwealth of Australia*, [1936] AC 578.

practice, as it is helpful within limits, but not conclusive.<sup>929</sup>

Thus, the Court asserted that the legislature could not say that a contract of service amounted to a sale of service, but it could tax a genuine transaction of sale of goods whatever it was taken for<sup>930</sup>.

### **10.1. Interpretative Search for Solutions.**

There are various dilemmas of indecisive lawmaking in the field of taxation in the context of different theories and resultant multiplicity of meanings of legal concepts. Equally, there are several propositions regarding the interpretation of meaning of sale. The first theory says it should be the same meaning, which the general statute confers to the term 'sale of goods'. The theory supports

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<sup>929</sup> *Pandit Banarsi Das v. State of Madhya Pradesh*, [1955] 6 STC 93. For arriving an opinion regarding the applicability of legislative practice in interpretation of statutory expression, the Hidayathulla (J) had made a remarkable research work referring to Foreign Decisions, such as *In re Regulation and Control of Radio Communication*, [1932] AC 304, *Henrietta Muir Edwards v. Attorney General for Canada* [1930] AC 124, *Rex v. West riding of Yorkshire County Council* [1906] 2 KB 676, *Ex Parte Campbell* (1870) LR 5 Ch. 703, *Barras v. Aberdeen Steam Trawling & Fishing Co.* [1933] AC 402 and *Greaves v. Totfield* (1880) 14 Ch. D 563.

<sup>930</sup> *Pandit Banarsi Das v. State of Madhya Pradesh*, [1955] 6 STC 93 at para 25.

conferring of narrow meaning strictly in compliance with the provisions of Sale of Goods Act, 1930.

## **10.2. Proposition of Strict Interpretation.**

The theory first considered by the Allahabad High Court in *Budh Prakash Jai Prakash*<sup>931</sup>, wherein it was held that State legislature is not authorised to tax transaction which are not sales, regardless to the fact that whether there is transfer of property takes place or not, since transfer of property is one of the requirements to constitute a sale under the Sale of Goods Act, 1930.

The Apex Court affirmed the said ratio in *Sales Tax Officer v. Budh Prakash Jai Prakash*<sup>932</sup> holding that unless there is a completed sale under which price is paid or payable, the transaction did not constitute sale. However the Court here, declared the insertion of forward contract<sup>933</sup> for the purpose of sales tax, as ultra vires and regarding the

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<sup>931</sup> *Budh Prakash Jai Prakash v. Sales Tax Officer*, [1952] 3 STC 185 (All.).

<sup>932</sup> *Supra*, n. 924.

<sup>933</sup> The U P Sales Tax Act, 1948, Section 2 (h) says, 'sale' means, within its grammatical variations and cognate expressions, any transfer of property in goods for cash or deferred payment or other valuable consideration and includes forward contracts, but does not include a mortgage, hypothecation, charge or pledge:

expansion of definition of sale in UP Sales Tax Act, 1948<sup>934</sup>, the Court kept silence. On general reading of the above judgment, there is no specific finding with regard to the State power to enlarge the meaning of sale for the purpose of taxation, if the transaction did not satisfy the requirements under Sale of Goods Act, 1930 to constitute the sale. There, the forward contracts are declared as agreement to sell and in forward contracts, there is no actual delivery of goods to constitute sale. The decision does not effectively support or give any clarity on the theory of narrow or strict reading.

In *United Motors (India) Ltd's case*<sup>935</sup> though the subject of the dispute was concerning the impact of extra territorial jurisdiction of law, there was a suggestion from the Court that the expression 'sale' in the Sales Tax statute should construe only in its legal and technical meaning and

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<sup>934</sup> In Explanation II of S. 2(h) of the U.P. Sales Tax Act, 1948 the non- obstante clause says, "Notwithstanding anything in the Indian Sale of Goods Act, 1930, or any other law for the time being in force, the sale of any goods.- ....". The Apex Court in *Sales Tax Officer v. Budh Prakash Jai Prakash*, reported in [1954] 5 STC 193 (SC) did not refer to the non- obstante clause to hold the said explanation is ultravires.

<sup>935</sup> *United Motors (India) Ltd v. State of Bombay*, [1953] 4 STC 10 (Bom.) at p. 23.

not the wider meaning. In *Poppatlal Shah v. State of Madras*<sup>936</sup>, also the subject of dispute was extra- territorial operation of law, but the Court proposed to adopt the popular meaning of the expression sale, which means any transaction which results in the passing of property, irrespective of its legal meaning, that is passing of property in goods.

These two decisions of the respective High Courts were annulled by the Apex Court in *State of Bombay v. United Motors*<sup>937</sup> and in *Poppatlal Shah v. State of Madras*<sup>938</sup> to the extent of ratio regarding extra- territorial operation of laws under consideration and maintained the legal meaning of the term sale which supports the requirement of all essential elements to constitute a transaction as sale. The observations of Justice Mukherjea of Supreme Court in *Poppatlal Shah's case* more or less supports the theory of narrow and strict reading, alternatively called as legal and technical interpretation, by

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<sup>936</sup> [1952] 3 STC 396 (Mad.) at p 403.

<sup>937</sup> [1953] 4 STC 133 (SC).

<sup>938</sup> [1953] 4 STC 188 (SC).

overruling an interpretation on the basis of popular meaning<sup>939</sup>.

When the *Gannon Dunkerley's*<sup>940</sup> came up for deliberation, the Madras High Court emphasized on the theory of narrow or strict reading to hold that State legislature cannot go beyond the provisions of the Sale of Goods Act, 1930 to expand the field of taxation of sale of goods. The Court pointed out unless two requirements are satisfied, an agreement to transfer the property in goods to the buyer for a price and an actual sale by which the property in goods passes from the seller to buyer no transaction will constitute sale for the purpose of taxation

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<sup>939</sup> *Poppatlal Shah v. State of Madras*, [1953] 4 STC 188 (SC) at p 193. Justice Mukherjea observed as follows; “The expression “sale of goods” is a composite expression consisting of various ingredients or elements. Thus, there are the elements of a bargain or contract of sale, the payment or promise of payment of price, the delivery of goods and the actual passing of title, and each one of them is essential to a transaction of sale though the sale is not completed or concluded unless the purchaser becomes the owner of the property. The question is what element or elements have been accepted by the Madras Legislature as constituting a sale in the Province upon which it is the object of the statute to levy tax. Unmistakably the stress is laid down in this definition on the element of transfer of property in a sale and no other. The language gives no indication of the popular meaning of sale in which, according to the High Court, the word was used.”

<sup>940</sup> *Gannon Dunkerley & Co. v. State of Madras*, [1954] 5 STC 216 (Mad.).

also. Sale being a special kind of executed contract required all the essential elements of a contract, such as competent parties, mutual assent of the parties to the contract, a thing for which the absolute and general property is transferred from seller to buyer and a price consideration in money paid or promised<sup>941</sup>.

The benchmark settled by the Madras High Court in *Gannon Dunkerley's*<sup>942</sup> was approved by the Apex Court in appeal filed by the State of Madras<sup>943</sup> and also in the subsequent decision in *Pandit Banarasi Das's case*<sup>944</sup> holding that the expression of sale of goods in taxing statutes has the same meaning which it has in the Sale of Goods Act, 1930. By a 4:1 majority, another constitution bench in *Sindri Fertiliser's case*<sup>945</sup> reaffirmed the law in this regard. This point of law was followed constantly until the time, when the Apex Court sanctified legislative

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<sup>941</sup> *Id.* at p 227.

<sup>942</sup> *Ibid.*

<sup>943</sup> *State of Madras v. Gannon Dunkerley & Co*, [1958] 9 STC 353 (SC).

<sup>944</sup> *Pandit Banarsi Das Bhanot v. State of Madhya Pradesh*, [1958] 9 STC 388 (SC).

<sup>945</sup> *Carl Still G.M.B.H v. State of Bihar*, [1961] 12 STC 449 (SC) (CB).

competency of the Parliament to introduce the 46<sup>th</sup> Amendment to the Constitution of India<sup>946</sup>.

### **10.3. Counter to Strict Interpretation.**

The first counter attack against the proposition of narrow reading could be traced in the Madras High Court's decision in *in re Jayarama Chettiar*<sup>947</sup>. The Court found that the sale in its general meaning as defined under the Sale of Goods Act, 1930 is a contract whereby a seller transfers the property in goods for price and price denotes money consideration. However a sale in the sales tax Act, particularly in the Madras General Sales Tax Act, 1939<sup>948</sup> is much wider in scope and amplitude and it need not necessarily be that the money alone should be the consideration, but it may be cash, or deferred payment or other valuable consideration. Thus, in general, as a ratio, the court held that a transaction, which may not amount to

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<sup>946</sup> *Builders Association v. Union of India*, [1989] 73 STC 370.

<sup>947</sup> *In re Jayarama Chettiar*, [1950] 1 STC 168 (Mad.).

<sup>948</sup> Madras General Sales Tax Act, 1939 (Act III of 1939), S. 2(h) defines "Sale' with all its grammatical variations and cognate expressions means every transfer of property in goods by one person to another in the course of trade or business for cash or for deferred payment or other valuable consideration, but does not include a mortgage, hypothecation, charge or pledge."

sale under the Sale of Goods Act, 1930, could be a sale under the General Sales Tax Act.

In another instance, in *Vishnu Agency*<sup>949</sup>, the Apex Court deviated from the view endorsed by the Bench in *Gannon Dunkerley's*<sup>950</sup>, with respect to the element of bargaining in a transaction to constitute sale. By following the dictum of House of Lords in *Kirkness v. John Hudson & Co. Ltd*<sup>951</sup>, the Court observed that mutual assent and bargaining is essential to constitute the sale and compulsory acquisition or sale does not satisfy the requirements<sup>952</sup>.

However, when *Vishnu Agency*<sup>953</sup> came up for consideration, the Apex Court took a divergent stand stating that a transaction which was effected in compliance with the obligatory terms of a statute may nevertheless be a sale, even if the compulsory acquisition would exclude the

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<sup>949</sup> *Vishnu Agencies (P) Ltd v. Commercial Tax Officer*, AIR 1978 SC 449: [1978] 42 STC 31.

<sup>950</sup> *Supra*, n. 943.

<sup>951</sup> [1955] AC 696.

<sup>952</sup> *State of Madras v. Gannon Dunkerley & Co*, [1958] 9 STC 353 (SC) at p. 376.

<sup>953</sup> *Supra*, n. 949.

element of mutual assent and bargaining. The Court adopted the minority view of Justice Hidayathulla, in *New India Sugar Mill's case*<sup>954</sup>, as the correct proposition of law that the consensus of mind in a contract did not mean only expressed consent but also implied consent.

From a close reading of the minority judgment in *New India Sugar Mills*<sup>955</sup> and Judgment in *Vishnu Agency*<sup>956</sup>, it could be seen that, the Court did not rule out the requirement of the mutual consent or bargain. It was observed that regulatory law might specify the terms of contracts, but mere regulation or restriction of the field of choice did not take away the contractual or essentially consensual binding core or character of the transaction. The reasoning in the judgment also supported the essentiality of elements of contract to constitute a transaction as sale.

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<sup>954</sup> *New India Sugar Mills Ltd v. Commissioner of Sales Tax*, AIR 1963 SC 1207; [1963] 14 STC 316.

<sup>955</sup> *Ibid.*

<sup>956</sup> *Supra* n. 949.

In a series of decisions<sup>957</sup>, though the Apex Court approved the involuntary supplies out of statutory orders as sale, but consistently viewed that there are mutual consent or bargaining, though in a limited sense. Statutory orders may confine the freedom of contract to a narrow limit, but there were several matters, which the parties could decide by mutual assent. Provisions of a statute might vary the terms of an original contract, but it does not mean there is not a contract with a valid offer and acceptance. There is no absolute impinge of essential elements of contract, but the attempt of the State is within its realm of planning economic needs ensuring basic necessities of the community.

#### **10.4. Repugnancy between General Law & Sales Tax Acts.**

Another proposition is with respect to repugnancy of the legislative powers to enact on sale of goods. The Sale of Goods Act, 1930 and the general sales tax Acts of the

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<sup>957</sup> See *Indian Steel and Wire Products Ltd v. State of Madras*, [1968] 21 STC 138 (SC), *State of Rajasthan v. Karan Chand Thappar & Brothers*, [1969] 23 STC 210 (SC) and *Salar Jung Sugar Mills Ltd v. State of Mysore*, [1972] 29 STC 246 (SC).

States defines 'sale of goods'. When the term sale of goods is already defined by a Central Act, the theory supports that there cannot be any deviation from the definition in the Central Act, in no circumstances<sup>958</sup>, unless by invoking an equal legislative power<sup>959</sup>.

When the State Government lacks exclusive power to legislate on the subject 'sale of goods' and the Central enactment already occupied the field, the provisions of the General Sales Tax Act is repugnant to the provisions of the Sale of Goods Act, 1930<sup>960</sup>. However, the Court, though supported the theory of narrow and strict reading, ruled out the contention of repugnancy of two legislative powers.

In *Gannon Dunkerley's*<sup>961</sup>, the Apex Court specifically pointed this aspect to state that the Sale of Goods Act and

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<sup>958</sup> *Dukhineswar Sarkar & Brs. Ltd v. Commercial Tax Officer*, [1957] 8 STC 478 (Cal.) at p. 485.

<sup>959</sup> See *Mithan Lal v. State of Delhi*, [1958] 9 STC 417 (SC) and *Instalment Supply (Pvt.) Ltd v. The Union of India*, [1961] 12 STC 489 (SC). As per the above two decisions the expression 'sale' could be legally extended by the Central Legislature under the power conferred by them under Article 246 (4) of the Constitution of India, as then in force.

<sup>960</sup> *Constitution of India*, Art. 254. Article 254 is analogous to Section 107 of the Government of India Act, 1935.

<sup>961</sup> *State of Madras v. Gannon Dunkerley & Co*, [1958] 9 STC 353 (SC) at p. 380.

State general sales tax Acts are legislations in different fields. Sale of Goods Act, 1930 is a law relating to sale of goods and General Sales Tax Acts are laws relating to levy and collection of tax on sale and purchase of goods, obviously coming out of two different entries. It is the trite law that there could not be any question of repugnancy because the Act might encroach to a certain extent upon the items in the Concurrent List<sup>962</sup>. It was also observed that since Concurrent List does not contain any entry relating to taxing power the concept of occupied field or repugnancy cannot arise<sup>963</sup>.

However, it is also material to note that, while enumerating the entry with respect to taxing the sale and purchase of goods, there was no corresponding definition either in the Government of India Act, 1935 or in the Constitution of India.

Nevertheless the expression 'sale of goods' had the definite meaning in law and were governed by the

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<sup>962</sup> *Bengal Immunity Co. Ltd v. State of Bihar*, [1953] 4 STC 43 (Pat.).

<sup>963</sup> *State of Uttar Pradesh v. Synthetics and Chemicals Ltd*, [1992] 87 STC 289 (SC).

provisions of the Sale of Goods Act, 1930. It was clearly understood what in law amounted to sale of goods, and the intention in conferring power on the State legislature to legislate on taxing of sale and purchase of goods, meant no more than conferring power to impose taxes on what was understood in law as the sale of goods.

This proposition of law was the real provocation for the Law Commission of India to suggest for an amendment to eliminate the ambiguity by inserting a definition clause in the Constitution itself. Going on this proposition it is clear that the definition clause inserted by the 46<sup>th</sup> Amendment to the Constitution of India, cannot claim any retrospective operation prior to its introduction, though it is the settled principles of law that Sovereign can make legislations levying tax retrospectively<sup>964</sup>.

The validity of a statute is to be tested by the constitutional power of a legislature at the time of its enactment by that legislature and if the enactment is beyond the legislative power, without a re-enactment

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<sup>964</sup> *Empire Industries v. Union of India*, AIR 1986 SC 662 at para 49.

consequent to a constitutional amendment, which grants the necessary legislative power, it cannot be operated<sup>965</sup>.

The rule that support the view that there is no repugnancy between the provisions relating to sale of goods in Sale of Goods Act and General Sales Tax Acts does not seem striking. Though the Apex Court ruled it out, there is a clear repugnancy between the statutes, as the core subjects dealt by the two statutes are 'sale of goods'. One is general law on sale of goods and other is process and procedure of taxing the sale of goods.

The repugnancy is ruled out only when two fields were different and the legislature of highest hierarchy did not intend at all to cover the field, which the State legislature acted on<sup>966</sup>. The State being a lower unit in the federal setup cannot overlook the provision of law, which is enacted by the Central Legislature, which defines the specialities of an act to become sale of goods. It is true that in a federal system of governance in the fields of distributed powers the Federal and State Legislatures are supreme in

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<sup>965</sup> Willoughby, *Constitution of the United States*, Vol I (1910) at p. 11.

<sup>966</sup> *Tika Ramji v. State of Uttar Pradesh*, AIR 1956 SC 676.

their respective sphere<sup>967</sup>. The incidence of tax is sale of goods not any different sort of transaction. Here, obviously the State legislation is substantially transgressed on the field occupied by the Central legislature to define sale of goods. More or less for the same reason the Law Commission of India<sup>968</sup> strongly proceeded with an amendment to the Article 366 by incorporating the definition of sale leaving behind the other two alternatives of amendment of entry 54 in the State List or to insert a new entry in the State List.

Even though the 'Works Contract' is included in the fictional definition of sale, and subjects to taxation, after the 46<sup>th</sup> Amendment to the Constitution of India, the issue whether a particular dealing is a pure sale or a fictional sale is still an important one. It is obvious that both are taxable under Sales Tax Act. Nevertheless, for the purpose of other enjoyable benefits, like entitlement of composition tax etc.,

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<sup>967</sup> *State of Uttar Pradesh v. Synthetics and Chemicals Ltd*, [1992] 87 STC 289 (SC) at p 311.

<sup>968</sup> Law Commission of India, 61<sup>st</sup> Report on certain problems connected with powers of the State to levy a tax on the sale of goods and with the Central Sales Tax Act, 1956, Ministry of Law; Government of India (May, 1974) at p 174.

the identity of a deal, either sale or works contract is a controversial issue.

### **10.5. Constitutional Sanction to Deemed Sale.**

By introducing the 46<sup>th</sup> Amendment to the Constitution, the scheme of taxation of sale of goods could be rested, in a wider, not in its widest canvas. The definition introduced in the Constitution is an inclusive one. Without appraising the historical backgrounds<sup>969</sup> that necessitated

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<sup>969</sup> In series of cases, the Supreme Court of India negated the State actions to tax certain transactions, such as works contract (*State of Madras v. Gannon Dunkerley & Co*, [1958] 9 STC 353), supply of foods and drinks in clubs (*Joint Commercial Tax Officer v. Young Men's Association*, [1970] 26 STC 241), supply of foods and drinks in hotels attached to lodging (*Northern India Caterers (India) Ltd v. Lt. Governor of Delhi*, [1978] 42 STC 386), transfer of right to use goods (*A.V. Meyiappan v. Commissioner of Commercial Taxes*, [1967] 20 STC 115), transfer of goods in hire-purchase agreements (*K.L. Johar & Co. v. Deputy Commercial Tax Officer*, [1965] 16 STC 213).

All these decisions were rendered on a footing that State legislature has no power to tax these transaction as it lacks the elements of sale as defined in the Sale of Goods Act, 1930. This resultant large-scale tax evasion and revenue loss and the State Governments represented the matter to the Union of India. The problem relating to power of States to levy tax on the sale of goods was then referred to the Law Commission by the Government of India.

The Law Commission submitted its report in 1974 on a consideration of the scope of the levy of tax by the State Governments with respect to transfer of property in works contracts, hire- purchase agreement, transfer of controlled commodities out of statutory orders etc.

the amendments, it is sufficient to mention that each of those clauses was intended to get over the embargos settled in some of the decisions of the Supreme Court.

More particularly, those decisions by which the Court declared various transactions, dealt in sub-clause (a) to (f) to be not involving the transaction of sale of goods for the purpose of Entry 54 of the List II of the Seventh Schedule to the Constitution of India. Additionally, the amendment itself resolves the issue of repugnancy of Sale of Goods Act and the State General Sales Tax Acts, if any.

Sub clause (a) and (b) of Clause (29A) deal with the tax on the property in goods, of course, (b) in particular with respect to works contract. By insertion of sub clause (a) the transfer of property in goods, *otherwise that in pursuance of*

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The Law Commission noted that these transactions resembled sales in substance and suggested three drafting devices for conferring the power of taxing the transactions on the State, either by amending entry 54 in State List, or adding a fresh entry in the State List itself incorporating all these provisions or inserting a definition for sale in Article 366. In view of the final suggestion of the Law Commission of India, the Central Government acted accordingly and introduced the Constitution (46<sup>th</sup> Amendment) Bill, 1981 which was subsequently enacted as the Constitution 46<sup>th</sup> Amendment Act, 1982 by introducing clause (29A) to the Article 366 of the Constitution of India, though the contents of the amendment are different from the recommendations of the Law Commission.

*a contract*, is a fictional sale, irrespective of the stipulations in the Sale of Goods Act, 1930 and Contract Act, 1872. What it means is simple and logical, that the essential elements of sale and contracts are not fatal and a fictional sale is constitutionally recognised. As observed by Justice Ruma Pal in *BSNL's case*<sup>970</sup>, sub clause (a) covers a situation where the consensual element is lacking, as in an involuntary sale, like delivery of essential goods in compliance of a statutory order. By introducing the sub clause (a), the logical conclusion in *Vishnu Agency*<sup>971</sup> that the transaction shall contain the essential elements at least in its minimum level is also be sidelined. Resultantly, a compulsory sale is other wise a fictional sale after, insertion of sub clause (a). The basic character of the transaction of sale, as a special contract is exceedingly diluted in the definition, which obviously overrule all the prescriptions laid down by the Apex Court in the *Gannon Dunkerley's*<sup>972</sup> and

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<sup>970</sup> *Supra*, n. 852.

<sup>971</sup> *Supra*, n. 949.

<sup>972</sup> *Supra*, n. 952.

*Vishnu Agency*<sup>973</sup>, and all other inspired Foreign Judgments like *Kirkness*<sup>974</sup>.

By sub-clause (b), the ambit expanded to include the transfer of property during the execution of works contract, which was wisely restricted in *Gannon Dunkerley's case*.<sup>975</sup> As observed in *Builders Association's case*<sup>976</sup>, after the amendment the works contract, which was an indivisible one, is by a legal fiction altered into a contract, which is divisible into one for sale of goods and the other for supply of labour and services. Conversely, the 46<sup>th</sup> Amendment does not answer the deficiencies, which are pointed out in the decisions with respect to pesticide spraying contract<sup>977</sup> and Fireworks contract<sup>978</sup>. It is material to see that though property in goods in its physical form is consumed in a works contract, there is no transfer of property while executing the contract in its original form or other form.

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<sup>973</sup> *Supra*, nn. 949 & 971.

<sup>974</sup> *Supra*, n. 951.

<sup>975</sup> *Supra*, nn. 952 & 972.

<sup>976</sup> *Builders Association of India v. Union of India*, [1989] 73 STC 370 (SC).

<sup>977</sup> *Supra*, n. 842.

<sup>978</sup> *Supra*, n. 843.

There are no goods in any other form in existence, after execution of contract, and 46<sup>th</sup> Amendment to the constitution shall not assist the taxman to bring these types of contract under the tax net.

The reason of enacting of sub-clause (c) is evidently to rule out the decision in *Johar's case*,<sup>979</sup> which relates to transfer of property in hire-purchase agreement and instalment transactions. The Court, found that though there is passing of property to constitute sale in hire purchase transactions, that the elements of bailment and sale simultaneously occur, but prior to picking the option to purchase, there cannot be sale.

Sub-clause (d) relates to the fictional sale while transferring the right to use the goods from the owner to the user. A transfer of the right to use goods for any purpose for cash, deferred payment or other valuable consideration would be now a fictional sale, by the person making the transfer to whom such transfer is made. Objective of sub-clause (d) was obviously to neutralize the law declared in

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<sup>979</sup> *K.L. Johar & Co. v. Deputy Commercial Tax Officer*, [1965] 16 STC 213 (SC).

*Meiyappan's case*<sup>980</sup>, where the Madras High Court held that the grant of the lease for exploiting the film by distribution for the purposes of exhibition to the public does not constitute sale.

By virtue of this decision, the States were incapable of levying tax, when goods are hired for enjoyment by the hirer. It was held that while transferring goods for enjoyment, there is only a conferment of right to exploit, which is more valuable and supply of goods is ancillary to the exercise of that right.

While expanding the scope of fictional sale all transfer of right to use goods may not be placed in the sub-clause of Article 366 (29A). If the goods are not deliverable at all by the service providers to the user, there is no question of transfer of right to use goods. The Court in *BSNL's case*<sup>981</sup> explained the sub-clause that though actual delivery of goods is not necessary for effecting the transfer of the right to use the goods, the availability of goods for

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<sup>980</sup> *A.V. Meiyappan v. Commissioner of Commercial Taxes*, [1967] 20 STC 115 (Mad.)

<sup>981</sup> *Bharat Sanchar Nigam Ltd. v. Union of India*, [2006] 145 STC 91 at p 127.

delivery at the time of transfer and delivery of goods at certain stages are significant factors. Under sub-clause (d), the taxable event, fictional sale, is the transfer of right to use the goods regardless of when or whether the goods are delivered for use<sup>982</sup>.

Likewise, the effective control on the goods, to which the right relates, is also relevant. The dictum laid down in *Rashtriya Ispat Nigam Ltd's case*<sup>983</sup> states that if the user is not free to make use of the goods so transferred for the works other than the works mentioned in the contract of transfer and the effective control remains with the owner, sub-clause (d) will not be helpful to declare the transfer as fictional sale.

Apart from these, there is some thing more to create the transfer of right to use goods as fictional sale. There shall be consensus *as idem*, as to the identity of the goods transferred; the transferee should have the legal right to use the goods, during the period the transferee retains the

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<sup>982</sup> *20<sup>th</sup> Century Finance Corporation Ltd v. State of Maharashtra*, [2000] 119 STC 182 (SC).

<sup>983</sup> *State of Andhra Pradesh v. Rashtriya Ispat Nigam Ltd* [2002] 126 STC 114 (SC); 2002 (3) SCC 314.

legal right, a corresponding exclusion of transferor from using the goods, lack of authority to owner to make simultaneous transfer to some one else also are also contributes to decide the nature of a transaction coming under sub- clause (d) to clause (29A)<sup>984</sup>.

A transfer of right to use goods is a transfer without accompanying the transfer of ownership. Though a simultaneous transfer is prohibited the proprietary rights of the goods remains with the transferor. This precise feature maintains the view that transfer of right to use goods is in the nature of bailment<sup>985</sup>. Since the substance of right is the enjoyment of goods, the transfer of right to use goods only concludes when the delivery of goods effected.

The Apex Court<sup>986</sup> ruled out this proposition and held that transfer of right to use goods is not in the nature of bailment. It supports the theory that taxable event is not the

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<sup>984</sup> See concurring judgement of Justice (Dr.) A. R. Lakshmanan in *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 3 VST 95 (SC) at p. 133: [2006] 145 STC 91 (SC).

<sup>985</sup> *20<sup>th</sup> Century Finance Corporation Ltd v. State of Maharashtra*, [1989] 75 STC 217 (Bom.).

<sup>986</sup> *Supra*, n 982. The Apex Court overruled the Judgment of Bombay High Court in *20<sup>th</sup> Century Finance Corporation Ltd v. State of Maharashtra*, [1989] 75 STC 217.

use of goods but the transfer of right to use goods. When, the transfer of property in goods is obligatory to constitute sales, under Section 4 of the Sale of Goods Act, 1930, in case of transfer of transfer of right to use goods, it is the possible presumption that the yielding up of possession to the lessee for its use is also obligatory to constitute the fictional sale. Thus, it is proper to say, delivery and possession for enjoyment has relevance under sub-clause (d) to clause (29A), though the Apex Court ruled out this proposition.

Sub-clauses (e) and (f) plainly aim to overcome the impediments settled by the Apex Court in *Young Men's Indian Association's case*<sup>987</sup>, *Associated Hotel's case*<sup>988</sup> and *Northern India Caterer's case*<sup>989</sup>. In those decisions, supply of foods and beverages and other articles to the members and their guests by the club and supply of foods

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<sup>987</sup> *Joint Commercial Tax Officer v. Young Men's Association*, [1970] 26 STC 241 (SC): AIR 1970 SC 1212.

<sup>988</sup> *State of Himachal Pradesh v. Associated Hotels of India Ltd*, [1972] 29 STC 474 (SC): AIR 1972 SC 1131.

<sup>989</sup> *Northern India Caterers (India) Ltd v. Lt. Governor of Delhi*, [1978] 42 STC 386 (SC): AIR 1978 SC 1591. The Review Petition against this Judgment was dismissed and the same is reported in *Northern India Caterers (India) Ltd v. Lt. Governor of Delhi* [1980] 45 STC 212 (SC): AIR 1980 SC 674.

to their residents by the hotel as part of their lodging service were declared as not the situations to constitute sales.

After enacting sub clause (e), supply of goods by any unincorporated association or body of persons to a member for valuable consideration is sale, irrespective of the agency service rendered by the club to its members. Moreover supply of foods, drinks and other articles for human consumption during the service rendered by the hotels and restaurants also sale, after insertion of sub-clause (f), irrespective of the claim of essential facility attached to the main service contract. By introducing these two sub-clauses, the Legislature cleverly removed the lacuna, if any traceable in sub-clause (a).

However, in *Rainbow Colour Labs*<sup>990</sup>, though it referred to sub-clause (b) works contract, categorically observed that where the transfer of property in goods takes place as an incident of contract of service, it would not come under the purview of fictional sale. Applying this

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<sup>990</sup> *Rainbow Colour Lab v. State of MP*, [2000] 118 STC 9 (SC).

principles, unless, the law in *Rainbow Colour Labs*<sup>991</sup>, was clarified in *Associated Cements Companies*<sup>992</sup>, the taxman might have been suffered the incapacity to tax hotel sales, even if sub-clause (f) enables to do it.

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<sup>991</sup> *Ibid.*

<sup>992</sup> *Associated Cement Companies Ltd v. Commissioner of Customs*, [2001] 124 STC 59 (SC):2001 (4) SCC 593.

# Conclusions and Suggestions

While proposing an expanded meaning to sale for the purpose of taxation, the Law Commission of India was highly confident that either of their proposals in the Report<sup>993</sup> may extremely benefited to the taxman to resolve the current problems of tax avoidance, usual in a range of transactions like composite contracts for work, supply contracts etc. Such proposals were exceedingly significant; when the Courts in India had consistently viewed that sales tax could only be imposed on what could be regarded as a sale of goods under the general law on sale of goods.

It is pertinent to note that the Law Commission had never discussed or recommended to amend the Constitution by permitting an expansion in the concept of deemed sale, as done in 46<sup>th</sup> Amendment to the

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<sup>993</sup> Law Commission of India, *61<sup>st</sup> Report on certain problems connected with powers of the State to levy a tax on the sale of goods and with the Central Sales Tax Act, 1956*, Ministry of Law; Government of India (May, 1974) at p 174.

Constitution of India<sup>994</sup>. In the case of the so called 'sale' in the course of supply of materials in an un-incorporated club or association, the Commission recommended that no change be made because such a change may have the effect of discouraging the co-operative movement<sup>995</sup>.

Similarly the Law Commission did not recommend for taxing of transfer of right to use goods, though it had been inserted in the 46<sup>th</sup> Amendment to the Constitution of India. In that point of view and on other points also, there are wide range criticisms on the legislative exercise of 46<sup>th</sup> Amendment to the Constitution of India, which obviously permitted expansion of concept of deemed sale.

### **11.1. Critical Appraisal on Constitutional Amendment.**

By a general reading of the sub-clauses in Article 366 (29A), it can be seen that there are at least three occasions, and only three, when the Constitution permits to

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<sup>994</sup> Atul M Setalvad, *Law of Sales and Principles of VAT*, LexisNexis: Butterworths Wadhwa, Nagpur (2009) at p. 167.

<sup>995</sup> See Chapter ID of *Law Commission of India - 61<sup>st</sup> Report on certain problems connected with powers of the State to levy a tax on the sale of goods and with the Central Sales Tax Act, 1956*, Law Commission of India, Ministry of Law; Government of India (May, 1974) at p 45.

handle the composite contract for the purpose of taxation. Sub clauses (b), (c) and (f) in clause (29A) deal with, firstly, transfer of property in works contract, secondly, hire-purchase and instalment transaction and thirdly, transfer of property in the deals of hoteliers and caterers, respectively. Sub-clauses (b) and (f) are absolutely dealing with a situation where in contract of service and sale is involved. Sub-clause (c) deals with a situation, which takes in contract of bailment and sale.

The pre- amendment law permitted the taxman to levy tax on the divisible part of a works agreement, if the transaction in the instrument of contract in truth represented two distinct and separate contracts and prohibited in cases of indivisible contract, as there was no intention to deliver any property in goods and hence transaction constituted no sale. The theory of dominant intention held the field, during these periods. With regard to circumstances, relating to sub-clause (c), the pre-amendment law did not support taxation of hire-purchase agreement unless the option exercised by the hirer culminated in the transaction of sale.

Even after the 46<sup>th</sup> Amendment, only these three kinds of integrated contracts are coming under the purview of deemed sale. The requirement in one sub-clause cannot be projected into interpret another sub-clause and fiction upon fiction is not permissible.

As observed by the Apex Court in *Bengal Immunity Company's case*<sup>996</sup>, when each of the sub-clauses manifestly intended to deal with different topics, particularly six different kinds of transactions, one cannot be projected to read into another. If there is an instrument of contract, which may be composite, in any other form or in a case other than the exceptions in clause (29A) covers, the 46<sup>th</sup> Amendment does not appear a helpful device to hold the contract as sale. Thus, in the *BSNL's case*<sup>997</sup> the Constitution Bench, through Ruma Pal, J, rightly observed that the field of professional services, like lawyers and doctors, are out of the purview of 46<sup>th</sup> Amendment, even though there is contract coupled with delivery of goods.

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<sup>996</sup> *Bengal Immunity Company Ltd v. State of Bihar*, [1955] 6 STC 446 (SC).

<sup>997</sup> *Supra*, n. 981.

Additionally, another Constitution Bench, through Ruma Pal, J, in *Sunrise Associate's case*<sup>998</sup> held that the fields of conveyance service, like issue of Rail, Bus and Air tickets etc are also out of the purview of fictional sale.

Yet again, the *Rajasthan Chemist Association*<sup>999</sup> governs the field of law, under scrutiny. It laid down the proposition of law that expansion of expression "sale of goods" beyond the provisions of Sale of Goods Act, 1930 is impermissible even after the introduction of 46<sup>th</sup> Amendment to the Constitution of India. A transaction, which does not conform to its traditional concept of sale, cannot be regarded as sale, even after the amendment, except in the circumstances, enumerated in sub-clause (a) to (f) of Clause (29A) of Article 366<sup>1000</sup>. By devising a methodology in the matter of levy of tax on sale of goods, law prohibits taxing a transaction, which is not a completed sale and also confine sale of goods to mean sale as

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<sup>998</sup> *Sunrise Associates v. Government of NCT of Delhi*, [2006] 145 STC 576 (SC).

<sup>999</sup> *State of Rajasthan v. Rajasthan Chemist Association*, [2006] 147 STC 542 (SC).

<sup>1000</sup> *Id.* at p. 563.

defined, as per general law, except in limited circumstances<sup>1001</sup>. Thus, the law made it clear that even after the enactment of 46<sup>th</sup> Amendment Act of 1982, the taxman is not in a position to tax a transaction, which is not completed and which lacks the elements of contract and sales.

Thus, with regard to the definition of sale for the purpose of the Constitution in general and for the purpose of entry 54 of List II in particular, except to the extent that clauses (a) to (f) in Article 366 (29A) operates, the ratio in the celebrated decision *Gannon Dunkerley's*<sup>1002</sup> still holds the field. The ingredients of sale continue to be the same

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<sup>1001</sup> See the Judgment of Rajasthan High Court in *Rajasthan Chemist Association v. State of Rajasthan*, [2006] 147 STC 476. The Court elaborately discussing the settled principles of law observed as follows, "Certain transactions which were held to be not falling within definition of sale of goods and were held to be outside the purview of entry 54 of State List, as per the different judgments referred to above were brought under tax net within the competence of State Legislature. However, still the basic constrains remain that the State/ legislature does not has a power to levy taxation any transaction by extending the meaning of sale beyond the province/ provision of the Sale of Goods Act, 1930, except to the extent the provision has been made under clause (29A) of Article 366.". The Judgment was affirmed by the Supreme Court in *State of Rajasthan v. Rajasthan Chemist Association*, [2006] 147 STC 542 (SC).

<sup>1002</sup> *Supra*, n.943.

as defined in the Sale of Goods Act, 1930. The proposition is reaffirmed in *Rajasthan Chemist Association*<sup>1003</sup> and also by the Constitution Bench in *Bharat Sanchar Nigam Ltd*<sup>1004</sup>.

The expression “goods” have been understood according to its utility and capabilities<sup>1005</sup>. When it is marketed supply of intangible intellectual property will also come under the purview of sale of goods. This trite law was followed in a span of time to hold that electrical energy, licences, intellectual properties like, copyright, trademark, patent, technical know-how and intangible properties put in media like, software, movie and music are goods exigible to sales tax, being the transfer constitutes sale.

The theory supports that with out having delivery of any goods; the mere transfer of right to use goods itself will be covered by the 46<sup>th</sup> Amendment to the Constitution of

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<sup>1003</sup> *Supra*, n. 999.

<sup>1004</sup> *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 3 VST 95 (SC) at p. 118; [2006] 145 STC 91 (SC).

<sup>1005</sup> In *Tata Consultancy Services v. State of Andhra Pradesh*, [2001] 122 STC 198 (SC), the Court observed as follows, “‘goods’ may be a tangible property or an intangible one. It would become goods provided it has the attributes thereof having regard to (a) its utility; (b) capable of being bought and sold, and (c) capable of being transmitted, transferred, delivered, stored and possessed.”

India so as to attract tax on distribution of telephone activation attached to a Mobile SIM card being goods<sup>1006</sup>. The interpretation of the hypothesis goes beyond the limit to say that transfer of information through a deputed person constitutes sale of information<sup>1007</sup>.

The 46<sup>th</sup> Amendment of the Constitution elaborated only the field of 'sale' and 'purchase' of goods for the purpose of taxation. Sale and purchase has a direct nexus with the identity of the things transacted. The expression "goods" is untouched by the amendment and to that extent; there cannot be any extension of meaning for sale of goods by enlarging the scope of goods, to canvassing any tangible or intangible movable property.

Apparently, the inclusive definition in the Constitution itself, takes an exhaustive meaning to 'goods' to include not only the concrete articles, but also the incorporeal movable property. Nevertheless, the contention that supports, the

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<sup>1006</sup> *Escotel Mobile Communications Ltd v. Union of India and others*, [2002] 126 STC 475 (Ker.); (2002) 10 KTR 318 (Ker.). This decision was reversed in *BSNL v. Union of India*, [2006] 145 STC 91 (SC).

<sup>1007</sup> *Mechanical Assembly System (India) Pvt. Ltd v. State of Kerala*, [2006] 144 STC 536 (Ker.).

proposition that 'goods' takes all articles or things, may not strictly be available at least after *BSNL*<sup>1008</sup>, though the definition of 'goods', invented in *Tata Consultancy*<sup>1009</sup> was approved by the Apex Court in the former decision.

While using the expression 'any goods' and 'for any purpose', the Legislature may not have intended to enlarge the scope of goods, beyond "all materials, commodities and articles" without making any amendment in Article 366 (12). The scheme of the 46<sup>th</sup> Amendment aims to introduce a separate category of deemed sale and the meaning of the goods is not altered. The Court in *BSNL*'s case found that electromagnetic waves are not marketable commodities

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<sup>1008</sup> *Supra*, n.1004 at p. 122. In *BSNL*'s case the Constitution Bench of the Supreme Court held that *Tata Consultancy Services v. State of Andhra Pradesh*, [2001] 122 STC 198 (SC), took the correct approach to the question as to what are 'goods' and also adopted the meaning of goods as understood therein.

<sup>1009</sup> *Supra*, n. 1005.

and not goods, but only a mere medium of communication<sup>1010</sup>.

It is pertinent to note that the court noticed the significance of the theory which supports that, goods takes all articles of merchandise. In this context, the decision in *Sunrise*<sup>1011</sup> has little relevance, as the consideration in that case was with respect to nature or lottery tickets, whether it is actionable claim or not, which is purposely excluded from the expression of goods. .

The pro-state proposition that Article 366 (29A) enlarged the taxing power of the State with its largest amplitude and the State legislatures hold unlimited power to enlarge the ambit of fictional sale seems to be incorrect. This proposition was rightly negated in *Builders*

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<sup>1010</sup> *Supra*, n.1004 at p. 124. The Court observed as follows, “It is clear, electromagnetic waves are neither abstracted nor are they consumed in the sense that they are not extinguished by their user. They are not delivered, stored or possessed. Nor they are marketable. They are merely the medium of communication. What is transmitted is not an electromagnetic wave but the signal through such means. The signals are generated by the subscribers themselves. In telecommunication what is transmitted is the message by means of the telegraph. No part of the telegraph itself is transferable or deliverable to the subscribers.

<sup>1011</sup> *Supra*, n. 998.

*Association* case<sup>1012</sup>. The Court held that the 46<sup>th</sup> Amendment to the Constitution does not introduce a separate entry for legislation and only a co-reading is permissible between entry 54 in State List and clause (29A) in Article 366, not beyond it. This ratio was reiterated in Second *Gannon Dunkerley's* case<sup>1013</sup> to say that the scope of legislation can be extended to fix the situs of a deemed sale, not above that.

The amendment explains the meaning of tax on sale and purchase of goods. It is pertinent to note that entries in Seventh Schedule does not confer any power to legislate on the subject enumerated but only demarcated the areas of concerns of Central and State units under Federal setup. The legislative powers of Parliament and State legislatures derive from the legislative powers endorsed under Article 246, of course subject to other rules of legislative

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<sup>1012</sup> *Supra*, n. 976 at p. 400

<sup>1013</sup> *Gannon Dunkerley & Co. v. State of Rajasthan*, [1993] 88 STC 204 (SC) at p. 223.

competency including Articles 13<sup>1014</sup> and 286<sup>1015</sup> of the Constitution of India.

Finally, 46<sup>th</sup> Amendment Act is not a comprehensive legislation granting power to the taxman to resolve the upcoming issues in the tax regime. 46<sup>th</sup> Amendment to the Constitution creates a set of fictions and the fiction in each case must be confined to the transactions referred to in each clauses. There cannot be a fiction inside the fiction<sup>1016</sup>. Even though 46<sup>th</sup> Amendment to the Constitution had passed the judicial test, in *Builders Association's* case<sup>1017</sup> and in second *Gannon Dunkerley's* case<sup>1018</sup>, followed by detailed elucidations in the cases of 20<sup>th</sup>

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<sup>1014</sup> *Hari Krishna Bhargav v. Union of India*, AIR 1966 SC 619 at p. 623: For detailed discussion see Durga Das Basu, *Shorter Constitution of India*, 13<sup>th</sup> edn. Wadhwa (Nagpur) (2001) at p.52.

<sup>1015</sup> See *supra*, n.180, for details.

<sup>1016</sup> Atul M. Setalvad, *Law of Sales and Principles of VAT*, LexisNexis: Butterworth's, Wadhwa (Nagpur) (2009) at p. 169.

<sup>1017</sup> *Builders Association of India v. Union of India*, [1989] 73 STC 370 (SC).

<sup>1018</sup> *Gannon Dunkerley & Co. v. State of Rajasthan*, [1993] 88 STC 204 (SC).

*Century Finance*<sup>1019</sup> and *BSNL*<sup>1020</sup>, there are some issues left to be resolved in fields of tax evasion.

## **11.2. Techniques to Resolve the Conflicts.**

There are other emerging issues in the regime of taxation on sale, which are not covered by the 46<sup>th</sup> Amendment to the Constitution of India. Of course these issues were not live in the eighties of the last century, when the amendment proceedings were mooted by Indian Parliament. Obviously the 46<sup>th</sup> Amendment to the Constitution of India concentrated to overcome the barriers in the judicial decisions, which were instrumental to curtail the state interest in increasing the revenue. The major area, which is untouched by the 46<sup>th</sup> constitutional amendment, is the field of taxation on E-commerce.

## **11.3. Taxing of E-commerce.**

In E-commerce, being a technological oriented commercial activity, there are fewer prospects to supervise

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<sup>1019</sup> *20<sup>th</sup> Century Finance Corporation Ltd v. State of Maharashtra*, [2000] 119 STC 182 (SC).

<sup>1020</sup> *Bharat Sanchar Nigam Ltd v. Union of India*, [2006] 3 VST 95 (SC); [2006] 145 STC 91 (SC)

the trading. The cross- boarder elements in E- commerce hold the subject more intricate. It is the trite law that all the required elements of sale must be present to constitute a transaction as sale. If any one or more of them is absent, the conclusion invariably is that it is not sale. When E- shopping consists, multiple places of transactions, the finding of situs of sale is a complex issue. The law supports the proposition that it is the place wherein the property in goods passes is the location of sale. Only in that context, the sale seems to be completed<sup>1021</sup>. Taxing is a sovereign function and subject to the territorial limitation subject to Constitution of the country. Revenue interest of country may govern the fiscal policy of the sovereign and it is impossible to lay down a universal formula, in the absence of an International Charter.

#### **11.4. Framing of an International Charter.**

An international charter can save the countries to enable exchange of information that is either in its possession or obtainable by it when the information is

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<sup>1021</sup> *India Copper Corporation Ltd v. State of Bihar*, [1961] 12 STC 56 (SC).

needed to the taxmen in other countries. The co-ordination of countries can be ensured in an exchange of information agreements, as in the case of Organization for Economic Co-operation and Development (OECD). The OECD has promulgated a model information exchange agreement similar to the tax information exchange agreement negotiated by the United States of America, and developed countries. They had been experimented the scope of such an international covenant, in simplifying the tax structure of e-commerce. In the developing and third world countries also, a uniform international charter can be framed, to resolve this issue.

### **11.5. Theory of Physical Presence**

The theory of physical presence<sup>1022</sup> is suggested to resolve the phenomenon of tax evasion in e-commerce. The country where the seller has his physical presence is obliged to tax his sale, under the notion that the sale is

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<sup>1022</sup> This theory is based on the US Supreme Court ruling in *Quill v. North Dakota*, 504 U.S. 298 (1992). In this case the court ruled that state cannot require mail order businesses and by extension online retailers to collect sales tax unless they have a physical presence in the state. The theory of physical presence is further explained as theory of nexus, which means a dealer must have some sort of nexus with the state's territorial jurisdiction.

deemed to be completed in his hands. In the absence of a legislation, by international covenants, this can be declared as universal rule. Yet, the proposition of deemed physical presence generate further difficulties, as a universal rule is impracticable, if the countries are in habit of making legislation defining physical presence as fictional presence, to mean that any kind of presence enjoin physical presence for the purpose of taxation.

Mainly the taxman has to tackle two kinds of e-transactions, firstly, e-shopping by employing e-mail orders and secondly, downloading of goods like information, technical know-how, design, software, movie, books, artworks, music etc. from the cyber network. In the first instance, the sale is completed by delivery of goods to the buyer or his agent, like a mail order transaction, either through postal agency or through courier agency. Of course, with the assistance of the carrier, there is a wide scope for administering tax on the goods delivering through carrier.

In second instance, the sale is completed by downloading the goods, which of course, qualify the test of

article of merchandise invented in the cases of *Tata Consultancy*<sup>1023</sup> and approved in *BSNL*<sup>1024</sup>, but, the issue of tax supervision is a solemn issue. The consideration of downloaded materials is usually paid by way of e-cash, either with the assistance of debit cards or credit cards. The problems of tax administration can be tackled by supervising the bank transactions, but to what extent it can be successful is a real dilemma.

### **11.6. Introduction of BIT-tax.**

BIT-Tax is the new concept, evolved by the taxman to tackle these worries. This is a system of taxing Internet usage by volume. The bit tax would not discriminate between telephony, data, voice, images, or other content; it would apply based on the volume of data transferred. To move towards the system of bit tax, it is necessary to clarify whether internet access and usage, is a "good" or a "service." If access to the Internet or usage is deemed a service, in general no sales or use taxation applies,

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<sup>1023</sup> *Tata Consultancy Services v. State of Andhra Pradesh*, [2001] 122 STC 198 (SC) & *Tata Consultancy Services v. State of Andhra Pradesh*, [2004] 137 STC 620.

<sup>1024</sup> *Supra*, n. 1020.

separately, as the mere service is outside the regime of taxation of sales. But the collection of bit tax or byte tax is more convenient to the taxman that it can be implemented through the internet service providers as the collection agents of the tax.

It is the high time, that the countries like India, which is having complex tax structure and multiplicity of taxation, turns towards Goods and Service Tax (GST). When the GST replaces the traditional tax structure of multiple taxation, that is excise duty on manufacture, sales tax on sale of goods, use tax on consumption of goods, luxury tax on enjoyment of amenities and service, service tax on providing taxable services etc., there need not be any confusion on the significance of BIT tax, as it will form part of the GST, as it is levied on the event of providing internet service. In the GST regime, the elements of sale and services will merge into the taxable incidence of supply, and there need not be further issues of divisibleness of sale and service, in taxation.

## **11.7. Taxing of Tangible & Intangible Goods.**

Being a mercantile activity, sale relates to both movable and immovable property. However, in the traditional era, for the purpose of sales tax, significance is only on passing of property in goods, which is a movable property. There are drastic changes in the outlook of the taxman to limit the correlation of the expression, goods with movable tangible properties only. There are strong adherents on the theory of articles of merchandise to canvas a thing capable of merchandise will be subject to sale for the purpose of taxation<sup>1025</sup>. They argue extensively that the strict and narrow reading of goods as tangible movable property is no more available and the expression goods takes all things which are capable of being abstracted, consumed and used and/ or transmitted, transferred, delivered, stored or possessed<sup>1026</sup>. As we have seen, though the 46<sup>th</sup> Amendment to the Constitution has introduced an expanded definition clause to “tax on

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<sup>1025</sup> *Supra*, n. 1023.

<sup>1026</sup> *Commissioner of Sales Tax v. Madhya Pradesh Electricity Board*, [1970] 25 STC 188; [1969] 2 SCR 939.

purchase and sale of goods”, the law makers, did not touch the definition of goods, as defined under Article 366 (12).

### **11.8. Theory of Articles of Merchandise.**

This theory proposes that all things which are capable of being abstracted, consumed and used and/ or transmitted, transferred, delivered, stored or possessed can be goods in its wider sense and it includes all articles of merchandise. However the general law, the Sale of Goods Act, 1930 confined its scope to *“every kind of movable property other than actionable claim, money and includes stock and shares, growing crops, grass, and things attached to or forming part of the land, which are agreed to be served before sale or under the contract of sale”*. This is an exhaustive, but vague definition. To avoid this inconsistency and to make more clear, it is the time to amend the definition of the ‘goods’ in Sale of Goods Act, 1930 to define; *“‘goods’ means all materials, commodities, things which are capable of being abstracted, consumed and used and/ or transmitted, transferred, delivered, stored or possessed and includes every articles of merchandise”*.

### **11.9. “Sale”- Amendment in General Law.**

The amendment made in Article 366 (29A) of the Constitution expanded the scope of “sale and purchases” for the purpose of taxation, in relation to entry 54 of the State List in the Seventh Schedule to the Constitution of India. However such a Constitutional mandate does not cure the defect pointed by the Judiciary in its diverse pronouncements. Hence an amendment is inevitable in the general law itself, that is, the Sale of Goods Act, 1930 to expand the scope of definition of sale.

In the present law, a contract of sale of goods is articulated in such a way that a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price<sup>1027</sup>. There are essential ingredients for a contract of sale, such as offer to buy or sell goods for a price and acceptance of such offer<sup>1028</sup>. It can be made by providing delivery of goods or payment of price immediately or in future and even payments can be effected in

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<sup>1027</sup> The Sale of Goods Act, 1930, S. 4.

<sup>1028</sup> *Id.*, S. 5.

instalments<sup>1029</sup>. In contra, Central Sales Tax Act, 1956 defines it in terms of above explicit requirements, but added some other ingredients of deemed sale, incompatible with the scheme introduced in the 46<sup>th</sup> Amendment to the Constitution of India<sup>1030</sup>.

To avoid the complexities of deemed expansion of meaning, there must be a definite or accurate definition for sale in the Sale of Goods Act, 1930 by substituting subsection (13) of Section 2 as follows,

***Sale with its grammatical variations and cognate expressions means, any act of selling; by transfer of property or rights or any kind of interest, in goods; whether as goods or in its some other form; whether or not with ownership, whether or not for a definite period, from one person to another for cash or deferred payment or for any kind of valuable consideration, but does not include a mortgage or hypothecation of or a charge or pledge on goods; and***

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<sup>1029</sup> *Ibid.*

<sup>1030</sup> The Central Sales Tax Act, 1956, S. 2(g).

***seller means a person who sells or agrees to sell such goods;***

Thus, such a definition takes the aspect of deemed sale, sale of goods, either in tangible or intangible forms and the emerging issues of sales in e-commerce, in a greater extent, by avoiding the troubles of repugnancy of general law with the special taxation laws.



# Appendix

## **The Constitution (Forty-Sixth Amendment) Act, 1982.**

### **STATEMENT OF OBJECTS AND REASONS**

*Sales tax laws enacted in pursuance of the Government of India Act, 1935 as also the laws relating to sales tax passed after the coming into force of the Constitution proceeded on the footing that the expression "sale of goods", having regard to the rule as to broad interpretation of entries in the legislative lists, would be given a wider connotation. However, in Gannon Dunkerley's case (A.I.R. 1958 S.C. 560), the Supreme Court held that the expression "sale of goods" as used in the entries in the Seventh Schedule to the Constitution has the same meaning as in the Sale of Goods Act, 1930. This decision related to works contracts.*

- 2. By a series of subsequent decisions, the Supreme Court has, on the basis of the decision in Gannon Dunkerley's case, held various other transactions which resemble, in substance, transactions by way of sales, to be not liable to sales tax. As a result of these decisions, a transaction, in order to be subject to the levy of sales tax under entry 92A of the Union List or entry 54 of the State List, should have the following ingredients, namely, parties competent to contract, mutual assent and transfer of property in goods from one of the parties to the contract to the other party thereto for a price.*
- 3. This position has resulted in scope for avoidance of tax in various ways. An example of this is the practice of inter-State consignment transfers, i.e., transfer of goods from head office or a principal in one State to a branch or agent in another State or vice versa or transfer of goods on consignment account, to avoid the payment of sales tax on inter-State sales under the Central Sales Tax Act. While in the case of a works contract, if the contract treats the sale of materials separately from the cost of the labour, the sale of materials would be taxable, but in the case of an indivisible works contract, it is not possible to levy sales tax on the transfer of property in the goods involved in the execution of such contract as it has been held that there is no sale of the materials as such and the property in them does not pass as movables. Though practically the purchaser in a hire-purchase agreement gets the goods on the date of the hire-purchase, it has been held that there is sale only when the purchaser exercises the option to*

purchase at a much later date and therefore only the depreciated value of the goods involved in such transaction at the time the option to purchase is exercised becomes assessable to sales tax. Similarly, while sale by a registered club or other association of persons (the club or association of persons having corporate status) to its members is taxable, sales by an unincorporated club or association of persons to its members is not taxable as such club or association, in law, has no separate existence from that of the members. In the Associated Hotels of India case (A.I.R. 1972 S.C. 1131), the Supreme Court held that there is no sale involved in the supply of food or drink by a hotelier to a person lodged in the hotel.

4. In the New India Sugar Mills case (A.I.R. 1963 S.C.1207), the Supreme Court took the view that in the transfer of controlled commodities in pursuance of a direction under a Control Order, the element of volition by the seller, or mutual assent, is absent and, therefore, there is no sale as defined in the Sale of Goods Act, 1930. However, in Oil and Natural Gas Commission Vs. State of Bihar (A.I.R. 1976 S.C. 2478), the Supreme Court had occasion to consider its earlier decisions with regard to the liability of transfers of controlled commodities to be charged to sales tax. The Supreme Court held that where there are any statutory compulsions the statute itself should be treated as supplying the consensus and furnishing the modality of the consensus. In Vishnu Agencies vs. Commercial Tax Officer (A.I.R. 1978 S.C. 449), six of the seven Judges concurred in over-ruling the decision, in New India Sugar Mills case while the seventh Judge held the case to be distinguishable. It is, therefore, considered desirable to put the matter beyond any doubt.
5. The various problems connected with the power of the States to levy a tax on the sale of goods and with the Central Sales Tax Act, 1956 were referred to the Law Commission of India. The Commission considered these matters in their Sixty-first Report and, recommended, inter alia, certain amendments in the Constitution if as a matter of administrative policy it is decided to levy tax on transactions of the nature mentioned in the preceding paragraphs.
6. Device by way of lease of films has also been resulting in avoidance of sales tax. The main right in regard to a film relates to its exploitation and after exploitation for a certain period of time, in most cases, the film ceases to have any value. It is, therefore, seen that instead of resorting to the outright sale

of a film, only a leased or transfer of the right to exploitation is made.

7. There were reports from State Governments to whom revenues from sales tax have been assigned, as to the large scale avoidance of Central sales tax leviable on inter-State sales of goods through the device of consignment of goods from one State to another and as to the leakage of local sales tax in works contracts, hire-purchase transactions, lease of films, etc. Though Parliament could levy a tax on these transactions, as tax on sales has all along been treated as an item of revenue to be assigned to the States, in regard to these transactions which resemble sales also, it is considered that the same policy should be adopted.
8. Besides the above mentioned matters, a new problem has arisen as a result of the decision of the Supreme Court in Northern India Caterers (India) Ltd. Vs. Lt. Governor of Delhi (A.I.R. 1978 S.C.1591). States have been proceeding on the basis that the Associated Hotels of India case was applicable only to supply of food or drink by a hotelier to a person lodged in the hotel and that tax was leviable on the sale of foodstuffs by a restaurant. But over-ruling the decision of the Delhi High Court, the Supreme Court has held in the above case that service of meals whether in a hotel or restaurant does not constitute a sale of food for the purpose of levy of sales tax but must be regarded as the rendering of a service in the satisfaction of a human need or ministering to the bodily want of human beings. It would not make any difference whether the visitor to the restaurant is charged for the meal as a whole or according to each dish separately.
9. It is, therefore, proposed to suitably amend the Constitution to include in article 366 a definition of "tax on the sale or purchase of goods" by inserting a new clause (29A). The definition would specifically include within the scope of that expression tax on---
  - (i) transfer for consideration of controlled commodities;
  - (ii) the transfer of property in goods involved in the execution of a works contract;
  - (iii) delivery of goods on hire-purchase or any system of payment by instalments;
  - (iv) transfer of the right to use any goods for any purpose for cash, deferred payment or other valuable consideration;
  - (v) the supply of goods by an unincorporated association or body of persons to a member thereof for

*cash, deferred payment or other valuable consideration;*

- (vi) the supply, by way of or as part of any service, of food or any drink for cash, deferred payment or other valuable consideration. (See clause 4).*

*10. A new entry is sought to be inserted in the Union List in the Seventh Schedule, as entry 92B, to enable the levy of tax on the consignment of goods where such consignment takes place in the course of inter-State trade or commerce. (See clause 5).*

*11. Clause (1) of article 269 is proposed to be amended so that the tax levied on the consignment of goods in the course of inter-State trade or commerce shall be assigned to the States. Clause (3) of that article is proposed to be amended to enable Parliament to formulate by law principles for determining when a consignment of goods takes place in the course of inter-State trade or commerce. (See clause 2).*

*12. Clause (3) of article 286 is proposed to be amended to enable Parliament to specify, by law, restrictions and conditions in regard to the system of levy, rates and other incidents of the tax on the transfer of goods involved in the execution of a works contract, on the delivery of goods on hire-purchase or any system of payment by installments and on the right to use any goods. (See clause 3).*

*13. The proposed amendments would help in the augmentation of the State revenues to a considerable extent. Clause 6 of the Bill seeks to validate laws levying tax on the supply of food or drink for consideration and also the collection or recoveries made by way of tax under any such law. However, no sales tax will be payable on food or drink supplied by a hotelier to a person lodged in the hotel during the period from the date of the judgment in the Associated Hotels of India case and the commencement of the present Amendment Act if the conditions mentioned in sub-clause (2) of clause 6 of the Bill are satisfied. In the case of food or drink supplied by Restaurants this relief will be available only in respect of the period after the date of judgment in the Northern India Caterers (India) Limited case and the commencement of the present Amendment Act.*

*14. The Bill seeks to achieve the above objects.*

**R. VENKATARAMAN.**

*NEW DELHI; 18th March, 1981.*

**THE CONSTITUTION (FORTY-SIXTH AMENDMENT) ACT, 1982**

[2nd February, 1983.]

**An Act further to amend the Constitution of India.**

BE it enacted by Parliament in the Thirty-third Year of the Republic of India as follows:-

1. **Short title.**-This Act may be called The Constitution (Forty-sixth Amendment) Act, 1982.
2. **Amendment of article 269.**-In article 269 of the Constitution,-
  - (a) in clause (1), after sub-clause (g), the following sub-clause shall be inserted, namely:-
 

*"(h) taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce";*
  - (b) in clause (3), for the words "sale or purchase of goods", the words "sale or purchase of, or consignment of goods" shall be substituted.
3. **Amendment of article 286.**-In article 286 of the Constitution, for clause (3), the following clause shall be substituted, namely:-
 

"(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of,-

  - (a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or
  - (b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause (29A) of article 366,

Be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify."

4. **Amendment of article 366.**- In article 366 of the Constitution after clause (29), the following clause shall be inserted, namely:-

*“(29A) "tax on the sale or purchase of goods" includes-*

- (a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;*
- (b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;*
- (c) a tax on the delivery of goods on hire-purchase or any system of payment by instalments;*
- (d) a tax on the 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;*
- (e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;*
- (f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service is for cash, deferred payment or other valuable consideration, and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made;”*

5. **Amendment of Seventh Schedule.**- In the Seventh Schedule to the Constitution, in List I- Union List, after entry 92A, the following entry shall be inserted, namely:-

*"92B. Taxes on the consignment of goods (whether the consignment is to the person making it or to any other*

*person), where such consignment takes place in the course of inter-State trade or commerce.”*

**6. Validation and exemption.**-(1) For the purposes of every provision of the Constitution in which the expression "tax on the sale or purchase of goods" occurs, and for the purposes of any law passed or made, or purporting to have been passed or made, before the commencement of this Act, in pursuance of any such provision,-

(a) the said expression shall be deemed to include, and shall be deemed always to have included, a tax (hereafter in this section referred to as the aforesaid tax) on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating) for cash, deferred payment or other valuable consideration; and

(b) every transaction by way of supply of the nature referred to in clause (a) made before such commencement shall be deemed to be, and shall be deemed always to have been, a transaction by way of sale, with respect to which the person making such supply is the seller and the person to whom such supply is made, is the purchaser, and notwithstanding any judgment, decree or order of any court, tribunal or authority, no law which was passed or made before such commencement and which imposed or authorised the imposition of, or purported to impose or authorise the imposition of, the aforesaid tax shall be deemed to be invalid or ever to have been invalid on the ground merely, that the Legislature or other authority passing or making such law did not have competence to pass or make such law, and accordingly:-

i. all the aforesaid taxes levied or collected or purporting to have been levied or collected under any such law before the commencement of this Act shall be deemed always to have been validly levied or collected in accordance with law;

- ii. no suit or other proceeding shall be maintained or continued in any court or before any tribunal or authority for the refund of, and no enforcement shall be made by any court, tribunal or authority of any decree or order directing the refund of, any such aforesaid tax which has been collected;
  - iii. Recoveries shall be made in accordance with the provisions of such law of all amounts which would have been collected thereunder as such aforesaid tax if this section had been in force at all material times.
- (2) Notwithstanding anything contained in sub-section (1), any supply of the nature referred to therein shall be exempt from the aforesaid tax-
- a. where such supply has been made, by any restaurant or eating house (by whatever name called), at any time on or after the 7<sup>th</sup> day of September, 1978 and before the commencement of this Act and the aforesaid tax has not been collected on such supply on the ground that no such tax could have been levied or collected at that time; or
  - b. where such supply, not being any such supply by any restaurant or eating house (by whatever name called), has been made at any time on or after the 4th day of January, 1972 and before the commencement of this Act and the aforesaid tax has not been collected on such supply on the ground that no such tax could have been levied or collected at that time:

Provided that the burden of proving that the aforesaid tax was not collected on any supply of the nature referred to in clause (a) or, as the case may be, clause (b), shall be on the person claiming the exemption under this sub-section.

- (3) For the removal of doubts, it is hereby declared that,-

- a. nothing in sub-section (1) shall be construed as preventing any person-
  - (i) from questioning in accordance with the provisions of any law referred to in that sub-section, the assessment, reassessment, levy or collection of the aforesaid tax, or
  - (ii) from claiming refund of the aforesaid tax from him paid by him in excess of the amount due from him under any such law; and
- b. no act or omission on the part of any person, before the commencement of this Act, shall be punishable as an offence which would not have been so punishable if this Act had not come into force.

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