State of Gujarat

Vs

M/s. Kailash Engineering Co.

Civil Appeal No. 945 of 1965

(J. C, Shah, V. Ramaswami-I, V. Bharagava JJ)

26.09.1966

JUDGMENT

BHARGAVA, J.

This appeal under special leave granted by this Court arises out of proceedings for assessment of sales-tax under the Bombay Sales Tax Act III of 1953. Messrs. Kailash Engineering Co. (hereinafter referred to as "the respondent") was an engineering concern having their workshop at Morvi on the meter gauge section of the Western Railway. They obtained a contract from the Western Railway Administration for construction of III class passenger coaches on certain conditions described as the conditions of tender. Under that contract which was reduced to writing and was described as an agreement, the respondent constructed three coaches and submitted a bill which was properly certified in accordance with the agreement by the Railway Administration on October 4, 1958. The net value of the work done by the respondent was certified at Rs. 1,22,035/-. After receipt of this money, the respondent wrote to the Additional Collector of Sales Tax requesting him under s. 27 of the Bombay Sales Tax Act, 1953, to hold that this was a works contract, and that the transaction, in respect of which the respondent received the money, did not amount to a sale, so that no sales-tax was payable under that Act. The Additional Collector held that two questions fell for determination before him :

(1) Whether the transaction covered by the bill dated 4th October, 1958, is a sale; and

(2) if it is a sale, whether any tax is payable in respect of the same.

The Additional Collector answered both the questions in the affirmative against the respondent. The appeal before the Gujarat Sales Tax Tribunal failed; and thereupon, the respondent sought a reference to the High Court of Gujarat. The Tribunal referred the following question for the opinion of the High Court :-

> "Whether on a proper construction of the agreement as a whole and its general conditions and specification, the work done and covered by Contract Certificates No. M/60(1)/B-PRTN, dated 4th October, 1958, for the performance of the works of building, erecting and furnishing 3 B.G. Coaches over the chassis supplied by the Railway is a works contract not amounting to sale, or whether it is a transaction of sale."

The High Court answered the question in favour of the respondent, holding that the transaction was a works contract carried out by the respondent and did not amount to a sale. Consequently, this

appeal has been brought up by the State of Gujarat challenging the correctness of the decision of the High Court.

The Tribunal, when dealing with the case, mentioned a few of the terms of the contract entered into between the respondent and the Western Railway Administration, and, though there was a provision in one of the clauses of the agreement that as soon as the plant and materials were brought on the site where the coaches were to be constructed, the ownership in them would vest in the Railway, the Tribunal held that the ownership in those materials never passed to the Railway because of the indication given by another clause which provided that on removal of contractor or on rescission of contract, the Railway Authorities would be entitled to take possession and retain all materials, tools, implements, machinery and buildings. On this basis, the Tribunal held that, from the general conditions of the contract, it appeared that the ownership of the coach bodies only passed to the Railway when completed and handed over to the Railway, so that the contract was for supply of coach bodies. It was on supply of these coach bodies that the respondent received the price of those bodies, and thus received the amount subjected to sales-tax as sale consideration for those bodies.

The High Court, however, in its judgment, reproduced the preamble of the contract as well as a large number of clauses of it to show that in the contract, at every stage, it was clearly mentioned that the contract was for performance of work of building, erecting and furnishing coach bodies on Broad Gauge underframes which already belonged to the Railway. The terms of the contract showed that as soon as the materials were taken by the respondent to the site of construction of the coaches, the ownership in those materials vested in the Railway and all that the respondent had to do was to carry out the work of erecting and furnishing the coach bodies. When the coach bodies were ready, the property in them vested in the Railway automatically without any further transfer of rights in it to the Railway. In fact, the ownership in the ready coach bodies did not vest in the respondent at all. No doubt, the materials for building the coach bodies had to be obtained by the respondent and brought to the site of construction, but the provision that the ownership in those materials would vest in the Railway as soon as those materials were brought to the site clearly indicated that the respondent, in purchasing those materials, was acting more or less in the capacity of an agent for the Railway. While the materials were at site, the effect of vesting of their ownership in the Railway was that if they were destroyed or damaged, the risk had to be borne by the Railway, even though the Railway might have been entitled to reimburse itself, because those materials and goods were in the custody of the respondent on behalf of the Railway. In fact, under clause 29, there was a specific provision for the contingency that the materials or plant may be lost, stolen, injured or destroyed by fire, tempest or otherwise. This special provision was to the effect that the liability of the contractor was not to be diminished in any way, nor was the Railway to be in any way answerable for loss or damage on the happening of such contingency. This special provision had to be made, because the ownership in the materials vested in the Railway, though the contractor was in actual physical possession of the materials and plant in order to carry out the works contract. It was for this reason that a specific provision had to be made that the contractor would be liable to the Railway if any such loss occurred.

Taking into account all the terms of the contract as a whole, the High Court came to the finding that the contract between the parties was one entire and indivisible contract for carrying out the works specified in full details in the agreement, and that it did not envisage either the sale of materials by the respondent to the Railway, or of the coach bodies as such.

In this connection, learned counsel for the appellant relied on the decision of this Court in Patnaik & Company v. State of Orissa ([1965] 2 S.C.R. 782.). In that particular case, the contract in question

was for the supply of bus bodies, and it was held that when the bus bodies were supplied by the contractor and money received by him, it amounted to a sale. It, however, appears that the facts and circumstances, on the basis of which the Court gave that opinion, do not find place in the case before us.

Three main circumstances were relied upon in that case for holding that the transaction amounted to a sale and not to a works contract. The first circumstance was that the bus bodies were, throughout the contract, spoken of as a unit or as a composite thing to be put on the chassis, and this composite body consisted not only of things actually fixed on the chassis but movable things like seat cushions, and other things which could be very easily detached. In the contract, with which we are concerned, the coach bodies are not separately described as units or components to be supplied by the respondent to the Railway. The language used in the contract everywhere describes the duty of the respondent to be that of constructing, erecting and furnishing coach bodies on the underframes supplied. At no stage does the contract mention that ready coach bodies were to be delivered by the respondent to the Railway. In fact, even during the process of construction of the coach bodies, the unfinished bodies in process of erection were treated, under the terms of the contract, as the property of the Railway.

The second circumstance found in that case was that if some work was not satisfactorily done and the body builder, on receipt of a written order, did not dismantle or replace the defective work or material at his own cost within seven days, the Controller was entitled to get the balance of the work done by another agency and recover the difference in cost from the body builder; and for this purpose, the Controller was entitled to take delivery of the unfinished body. In the contract before us, as we have already mentioned in the preceding paragraph, the unfinished bodies of the coaches were from the earliest stage treated as the property of the Railway, and there was no question of ownership of the unfinished body passing to the Railway only after its seizure by it as was the case in the other contract in which the property in the unfinished body did not pass to the Government till the unfinished body was seized.

The third circumstance taken into account in that case was the liability for the loss, if a fire took place and the bus bodies were destroyed or spoiled. In that case, there was a provision for insurance of the chassis, but there was no such provision regarding insurance of bus bodies, and the Court inferred that till delivery was made, the bus bodies remained the property of the appellant on whom the loss would fall. On the other hand, in the contract with which we are concerned, the terms envisaged the property in the unfinished bodies vesting in the Railway, and since those unfinished bodies were to be in charge of the respondent during construction, a special provision had to be made making the respondent responsible for the loss and throwing upon the respondent the liability to reimburse the Railway for loss by fire, etc. Thus, the terms of the contract in this case are markedly different from those which came up for consideration in that case. Here, we find that all the terms of the contract lead to the only inference that the respondent was not to be the owner of the ready coach bodies and that the property in those bodies vested in the Railway even during the process of construction. This was, therefore, clearly a works contract which did not involve any sale. The decision given by the High Court was correct. The appeal fails and is dismissed with costs.

R.K.P.S.

Appeal Dismissed.

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