ORDER

By majority the Court answers the reference in the following terms:

1. Taxes simpliciter are not within the contemplation of Part XIII of the Constitution of India. The word 'Free' used in Article 301 does not mean "free from taxation".

2. Only such taxes as are discriminatory in nature are prohibited by Article 304(a). It follows that levy of a non-discriminatory tax would not constitute an infraction of Article 301.

3. Clauses (a) and (b) of Article 304 have to be read disjunctively.

4. A levy that violates 304(a) cannot be saved even if the procedure under Article 304(b) or the proviso there under is satisfied.

5. The compensatory tax theory evolved in Automobile Transport case and subsequently modified in Jindal's case has no juristic basis and is therefore rejected.

6. Decisions of this Court in Atiabari, Automobile Transport and Jindal cases (supra) and all other judgments that follow these pronouncements are to the extent of such reliance over ruled.

7. A tax on entry of goods into a local area for use, sale or consumption therein is permissible although similar goods are not produced within the taxing state.

8. Article 304 (a) frowns upon discrimination (of a hostile nature in the protectionist sense) and not on mere differentiation. Therefore, incentives, set-offs etc. granted to a specified class of dealers for a limited period of time in a non-hostile fashion with a view to developing economically backward areas would not violate Article 304(a). The question whether the levies in the present case indeed satisfy this test is left to be determined by the regular benches hearing the matters.

9. States are well within their right to design their fiscal Legislations to ensure that the tax burden on goods imported from other States and goods produced within the State fall equally. Such measures if taken would not contravene Article 304(a) of the Constitution. The question whether the levies in the present case indeed satisfy this test is left to be determined by the regular benches hearing the matters.

10. The questions whether the entire State can be notified as a local area and whether entry tax can be levied on goods entering the landmass of India from another country are left open to be determined in appropriate proceedings.

SUPREME COURT OF INDIA

Jindal Stainless Ltd. & Anr.

Vs.

State of Haryana & Ors.

C.A.No.3453/2002

(T.S.Thakur,CJI., A.K.Sikri and S.A.Bobde,JJ., Shiva Kirti Singh and N.V.Ramana,JJ., R. Banumathi A.M.Khanwilkar,JJ Dr D.Y. Chandrachud Ashok Bhushan,JJ.,)

11.11.2016

JUDGMENT

T.S.Thakur.CJI., (for himself and A.K. Sikri and A.M. Khanwilkar. JJ.,)

1. These appeals bring to fore for our determination vexed questions touching the interpretation of Articles 301 to 307 comprising Part XIII of the Constitution which have been the subject matter of several Constitution Bench decisions of this Court, all but one, decided by majority. The questions assume in a great measure considerable public importance not only because the same deal with the powers of the State legislatures to levy taxes but also because any pronouncement of this Court is bound to impact the federal character of our polity and the Centre-State relationship in legislative and fiscal matters. There is no gainsaying that it is the importance of the questions that lies at the bottom of the present reference to a larger Bench made in the following circumstances.

2. In exercise of their legislative powers under Entry 52 of List II of the Seventh Schedule to the Constitution several States in the country, at least 14 of whom are parties to these proceedings, have enacted laws that provide for levy of a tax on the "entry of goods into local areas comprising the States". The constitutional validity of these levies was questioned in different High Courts by assesses/dealers aggrieved of the same, inter alia, on the ground that the same were violative of the constitutionally recognised right to free trade commerce and intercourse guaranteed under Article 301 of the Constitution of India. The levies were also assailed on the ground that the same were discriminatory and, therefore, violative of Article 304(a) of the Constitution of India. Absence of Presidential sanction in terms of Article 304(b) of the Constitution of India was also set-up as a ground of challenge to the levies imposed by the respective State legislatures. Writ Petition (Civil) No. 8700 of 2000 filed before the High Court of Punjab and Haryana was one such petition that assailed the constitutional validity of the Haryana Local Development Act, 2000. Relying upon the decisions of this Court in *Atiabari Tea Co. Ltd. v. State of Assam & Ors*[1]*.; Automobile Transport (Rajasthan) Ltd. etc. v. State of Rajasthan & Ors*[2]*.* M*/s. Bhagatram Rajeev Kumar v. Commissioner of Sales Tax, M.P. and Ors*[3]*. and State of Bihar and Ors. v. Bihar Chamber of Commerce and Ors*[4]*.* a Division Bench of the High Court of Punjab and Haryana dismissed the said

petition and connected matters on the ground that the levy was compensatory in character hence outside the purview of Article 301.

3. The correctness of the said order was assailed before this Court in *Jindal Stripe Ltd. and Anr. v. State of Haryana and Ors*[5]. A two-Judge Bench of this Court, however, referred the matter to a larger Bench as it noticed an apparent conflict between the pronouncements of this Court in Atiabari (supra) and Automobile Transport (supra) cases on the one hand and Bhagatram (supra) and Bihar Chamber of Commerce (supra) on the other. The Court after noticing the development of law on the subject observed:

> "25. To sum up: the pre-1995 decisions held that an exaction to reimburse/recompense the State the cost of an existing facility made available to the traders or the cost of a specific facility planned to be provided to the traders is compensatory tax and that it is implicit in such a levy that it must, more or less, be commensurate with the cost of the service or facility. The decisions emphasized that the imposition of tax must be with the definite purpose of meeting the expenses on account of providing or adding to the trading facilities either immediately or in future provided the quantum of tax sought to be generated is based on a reasonable relation to the actual or projected expenditure on the cost of the service or facility.
>
> 26. The decisions in Bhagatram and Bihar Chamber of Commerce now say that even if the purpose of imposition of the tax is not merely to confer a special advantage on the traders but to benefit the public in general including the traders, that levy can still be considered to be compensatory. According to this view, an indirect or incidental benefit to traders by reason of stepping up the developmental activities in various local areas of the State can be legitimately brought within the concept of compensatory tax, the nexus between the tax known as compensatory tax and the trading facilities not being necessarily either direct or specific.
>
> 27. Since the concept of compensatory tax has been judicially evolved as an exception to the provisions of Article 301 and as the parameters of this judicial concept are blurred, particularly by reason of the decisions in Bhagatram and Bihar Chamber of Commerce we are of the view that the interpretation of Article 301 vis-a-vis compensatory tax should be authoritatively laid down with certitude by the Constitution Bench under Article 145(3).
>
> 28. In the circumstances let all these matters be placed before the Hon'ble the Chief Justice for appropriate directions."

4. The matters were, pursuant to the above, placed before a Constitution Bench of this Court *in Jindal Stainless Ltd. (2) and Anr. v. State of Haryana and Ors.*[6], which resolved the conflict noticed in the reference order by holding that the working test propounded by seven Judges in Automobile Transport case (supra) was incompatible with the test of 'some connection' enunciated by the three Judge Bench in Bhagatram's case (supra).

The Court held that the test of 'some connection' as propounded in Bhagatram's case (supra) had no application to the concept of compensatory tax. The Court, accordingly, overruled the decisions rendered in Bhagatram and Bihar Chamber of Commerce cases and held that the doctrine of 'direct and immediate effect' of the impugned law on trade and commerce under Article 301 as propounded in Atiabari (supra) and the working test enunciated in Automobile Transport (supra) cases for deciding whether a tax is compensatory or not will continue to apply. The Court observed:

> "53. We reiterate that the doctrine of "direct and immediate effect" of the impugned law on trade and commerce under Article 301 as propounded in Atiabari Tea Co. Ltd. v. State of Assam and the working test enunciated in Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan for deciding whether a tax is compensatory or not vide para 19 of the Report (AIR), will continue to apply and the test of "some connection" indicated in para 8 (of SCC) of the judgment in Bhagatram Rajeevkumar v. CST and followed in State of Bihar v. Bihar Chamber of Commerce is, in our opinion, not good law. Accordingly, the constitutional validity of various local enactments which are the subject-matters of pending appeals, special leave petitions and writ petitions will now be listed for being disposed of in the light of this judgment."

5. The matters were, in terms of the above direction, listed before a two-Judge bench for hearing of the appeals in the light of the above pronouncement of the Constitution Bench. The two-Judge Bench, however, noticed that although the basic issue in the appeals revolved around the concept of compensatory tax, the High Courts had not examined the same as they had considered themselves bound by the view taken in Bhagatram and Bihar Chamber of Commerce cases (supra). The Court further found that in the absence of relevant data before the High Courts, the issue whether the levies were compensatory could not have been considered and accordingly referred the matter back to the High Courts to decide the said aspect. The appeals were, in the meantime, adjourned to await the finding from the High Courts on the question whether the levies were indeed compensatory in nature having regard to the decisions of this Court in Atiabari and Automobile Transport cases (supra).

6. The matters were accordingly taken up by the High Courts, after the remand, who came to the conclusion that the impugned levies were neither compensatory in character nor was the procedure stipulated by Article 304(b) and the proviso to the same followed. The levies were on that basis held to be in violation of Article 301 being an impediment to free trade, commerce and intercourse and accordingly struck down. The High Courts of Assam, Arunachal Pradesh, Jharkhand, Kerala and Tamil Nadu struck down the levies imposed by their respective States also on the ground that they were discriminatory in nature hence violative of Article 304(a) of the Constitution.

7. All these judgments and orders of the High Courts, passed after the remand, then, came to be challenged by the States concerned in the appeals filed against the same. These appeals initially came-up before a two-Judge Bench of this Court comprising Justice Arijit Pasayat and Justice S.H. Kapadia. Their Lordships referred the same to a Constitution Bench for an authoritative pronouncement on as many as ten questions

formulated in the reference order
(Jaiprakash Associates Limited v. State of Madhya Pradesh and Ors[7]*.* The Court noticed the arguments advanced on behalf of the assessees that entry taxes were, in essence and in the classical sense, in the nature of 'a fee' and not 'a tax'. It also noted the contention that all the cases on which the parties had placed reliance related to entry tax in the context of tax on vehicles in contradiction to taxes on entry of goods. The Court was of the view that while the Constitution Bench in Jindal Stainless Ltd. (2) (supra) had dealt with some aspects of the matter, certain other important constitutional issues remained to be examined especially because a conceptually and contextually different approach may be required vis-à-vis "transport cases" on the one hand and cases of "entry tax on goods" on the other. The questions formulated by the Court for determination by the Constitution Bench were in the following words:

> "(1) Whether the State enactments relating to levy of entry tax have to be tested with reference to both clauses (a) and (b) of Article 304 of the Constitution for determining their validity and whether clause (a) of Article 304 is conjunctive with or separate from clause (b) of Article 304?
>
> (2) Whether imposition of entry tax levied in terms of Entry 52 List II of the Schedule VII is violative of Article 301 of the Constitution? If the answer is in the affirmative whether such levy can be protected if entry tax is compensatory in character and if the answer to the aforesaid question is in the affirmative what are the yardsticks to be applied to determine the compensatory character of the entry tax?
>
> (3) Whether Entry 52 List II, Schedule VII of the Constitution like other taxing entries in the Schedule, merely provides a taxing field for exercising the power to levy and whether collection of entry tax which ordinarily would be credited to the Consolidated Fund of the State being a revenue received by the Government of the State and would have to be appropriated in accordance with law and for the purposes and in the manner provided in the Constitution as per Article 266 and there is nothing express or explicit in Entry 52 List II, Schedule VII which would compel the State to spend the tax collected within the local area in which it was collected?'
>
> (4) Will the principles of quid pro quo relevant to a fee apply in the matter of taxes imposed under Part XIII?
>
> (5) Whether the entry tax may be levied at all where the goods meant for being sold, used or consumed come to rest (standstill) after the movement of the goods ceases in the "local area"?
>
> (6) Whether the entry tax can be termed a tax on the movement of goods when there is no bar to the entry of goods at the State border or when it passes through a local area within which they are not sold, used or consumed?
>
> (7) Whether interpretation of Articles 301 to 304 in the context of tax on vehicles

(commonly known as "transport") cases in Atiabari case and Automobile Transport case apply to entry tax cases and if so, to what extent?

(8) Whether the non-discriminatory indirect State tax which is capable of being passed on and has been passed on by traders to the consumers infringes Article 301 of the Constitution?

(9) Whether a tax on goods within the State which directly impedes the trade and thus violates Article 301 of the Constitution can be saved by reference to Article 304 of the Constitution alone or can be saved by any other article?

(10) Whether a levy under Entry 52 List II, even if held to be in nature of a compensatory levy, must, on the principle of equivalence demonstrate that the value of the quantifiable benefit is represented by the costs incurred in procuring the facility/services (which costs in turn become the basis of reimbursement/recompense for the provider of the services/facilities) to be provided in the "local area" concerned and whether the entire State or a part thereof can be comprehended as local area for the purpose of entry tax?"

8. The matter was accordingly placed before a five-Judge Bench of this Court (*Jindal Stainless Limited and Anr. v. State of Haryana and Ors*[8]. who briefly referred to the decisions in Atiabari, Automobile Transport cases (supra) and *Keshav Mills Co. Ltd. v. CIT*[9] and a few others and referred the matters to a larger Bench for reconsideration of the judgment of this Court in Atiabari and Automobile Transport (supra). The Court noted that the correctness of the view taken in the said two cases had been doubted as early as in the year 1975 in *G.K. Krishnan v. State of Tamil Nadu*[10] The reference order briefly set out some of the questions that required consideration by a larger Bench. The Court said:

"11. Some of these aspects which need consideration by a larger Bench of this Court may be briefly enumerated. Interplay/interrelationship between Article 304(a) and Article 304(b). The significance of the word "and" between Articles 304(a) and 304(b). The significance of the non obstante clause in Article 304. The balancing of freedom of trade and commerce in Article 301 vis-a-vis the States' authority to levy taxes under Articles 245 and 246 of the Constitution read with the appropriate legislative entries in the Seventh Schedule, particularly in the context of movement of trade and commerce.

12. Whether Article 304(a) and Article 304(b) deal with different subjects? Whether the impugned taxation law to be valid under Article 304 (a) must also fulfil the conditions mentioned in Article 304(b), including Presidential assent? Whether the word "restrictions" in Article 302 and in Article 304(b) includes tax laws? Whether validity of a law impugned as violative of Article 301 should be judged only in the light of the test of non-discrimination? Does Article 303 circumscribe Article 301? Whether "internal goods" would come under Article 304(b) and "external goods" under Article 304(a)? Whether "per se test" propounded in Atiabari case should or should not be rejected? Whether tax

simpliciter constitutes a restriction under Part XIII of the Constitution? Whether the word "restriction" in Article 304(b) includes tax laws? Is taxation justiciable? Whether the "working test" laid down in Atiabari makes a tax law per se violative of Article 301? Interrelationship between Article 19(1)(g) and Article 301 of the Constitution? These are some of the questions which warrant reconsideration of the judgments in Atiabari Tea Co. Ltd. and Automobile Transport (Rajasthan) Ltd. by a larger Bench of this Court."

9. At the hearing before us learned counsel for the parties agreed after a day -long exploratory exercise that the questions that fall for determination by this Court could be re-framed as under:

> "1. Can the levy of a non-discriminatory tax per se constitute infraction of Article 301 of the Constitution of India?
>
> 2. If answer to question No. 1 is in the affirmative, can a tax which is compensatory in nature also fall foul of Article 301 of the Constitution of India?
>
> 3. What are the tests for determining whether the tax or levy is compensatory in nature?
>
> 4. Is the Entry Tax levied by the States in the present batch of cases violative of Article 301 of the Constitution and in particular have the impugned State enactments relating to entry tax to be tested with reference to both Articles 304(a) and 304(b) of the Constitution for determining their validity?

10. We have heard learned counsel for the parties at considerable length on the above questions which we shall now take up for discussion ad-seriatim.

Re: Question No. 1

11. Whether non-discriminatory fiscal measures also impede free trade, commerce and intercourse and thereby fall foul of Article 301 of the Constitution can be answered only if one keeps in view the Constitutional scheme underlying separation of powers in a federal system of governance like the one chosen by us. The answer would also depend upon the way we look at, understand and interpret the provisions of the Constitution and in particular the provisions of Parts XI, XII and XIII thereof. Interpretation of these and indeed every other provision must have due regard to what are recognised as the basic features of the Constitution. In doing so, the approach of the Courts can neither be rigid nor wooden or pedantic. Being a living and dynamic document, the Constitution ought to receive an equally dynamic and pragmatic interpretation that harmonizes and balances competing aims and objectives and promotes attainment of national goals and objectives. It must, as observed by this Court, in *Kihoto Hollohan v. Zachillhu*[11] be read as a logical whole. The Constitutional provisions cannot be read in isolation, nor can they be interpreted in a manner that renders another provision redundant declared this Court in T*.M.A. Pai Foundation and others v. State of Karnataka*[12] If words used in the provision are imprecise, protean or

evocative or can reasonably bear meaning more than one, it would be legitimate for the Court to go beyond the literal confines of the provision and to call in aid other well recognised rules of construction such as legislative history, the basic scheme and framework of the statute as a whole, the object sought to be achieved and the consequence flowing from the adoption of one in preference to the other possible interpretation observed this Court in Chief Justice of *Andhra Pradesh and others. v. L.V. A. Dixitulu and others*[13]. Reference may also be made to the decision of this Court in *Kesavananda Bharati v. State of Kerala*[14] where this Court quoted with approval Lord Greene's observations in the following words:

> "56 It is not right to construe words in vacuum and then insert the meaning into an article. Lord Green observed in *Bidie v. General Accident, Fire and Life Assurance Corporation*[15]*:* The first thing one has to do, I venture to think, in construing words in a section of an Act of Parliament is not to take those words in vacuo, so to speak, and attribute to them what is sometimes called their natural or ordinary meaning. Few words in the English language have a natural or ordinary meaning in the sense that they must be so read that their meaning is entirely independent of their context. The method of construing statutes that I prefer is not to take particular words and attribute to them a sort of prima facie meaning which you may have to displace or modify. It is to read the statute as a whole and ask oneself the question: 'In this state, in this context, relating to this subject-matter, what is the true meaning of that word.
>
> 57. I respectfully adopt the reasoning of Lord Green in construing the expression "the amendment of the Constitution....
>
> Xxxxxxxx
>
> 61. I may also refer to the observation of Gwyer, C.J., and Lord Wright:
>
> "A grant of the power in general terms, standing by itself, would no doubt be construed in the wider sense; but it may be qualified by other express provisions in the same enactment, by the implications of the context, and even by considerations arising out of what appears to be the general scheme of the Act." (Per Gwyer, C.J. — The Central Provinces and Berar Act, 1939, FCR 18 at 42 MR).
>
> "The question, then, is one of construction and in the ultimate resort must be determined upon the actual words used, read not in vacua but as occurring in a single complex instrument, in which one part may throw light on another. The Constitution has been described as the federal compact, and the Construction must hold a balance between all its parts." (Per Lord Wright — James v. Commonwealth of Australia, 1936 AC 578 at 613.)"

12. It is trite that a narrow interpretation that may have the potential or tendency to subvert the delicate balance which the framers of the Constitution had in mind while distributing legislative businesses including the sovereign power to levy taxes must be

avoided and a construction that is most beneficial for a harmonious relationship between different limbs of the State including that between the Centre and the States or States inter se adopted. This may, at times, involve ironing out of rough edges which exercise a Constitutional Court must necessarily undertake to avoid confusion and resultant negation of the Constitutional objectives.

13. Having said so, we must sail smooth on certain fundamentals before we address the question whether levy of taxes per se operate as an impediment or restriction on the right to free trade, commerce and intercourse. That is because a true and correct answer to Question No.1 can be found only if we constantly keep those fundamentals in mind while attempting to resolve what has been found to be somewhat difficult to resolve. For instance, whether levy of a tax is an attribute of sovereignty and if so whether Article 246 of the Constitution recognises the sovereign power of the State to make laws including the power to levy taxes on subjects enumerated in List II of the Seventh Schedule of the Constitution is an important dimension that must be addressed as a part of the interpretative exercise. So also, we must examine whether power to tax if held to be subservient to Article 301, shall have the effect of denuding the States of their sovereignty in the matter of levy of taxes and in the process affect the federal structure of the polity envisaged by the Constitution. If levy of taxes is always presumed to be reasonable and in public interest, whether such levies could be said to be within the contemplation of Article 304(b) when it provided for imposition of "reasonable restrictions in public interest" is yet another aspect that must be explored especially when the reasonableness of any restriction within the comprehension of Article 304(b) is not free from judicial scrutiny by Courts. These are some of the broad and fundamental issues that need to be examined before we attempt to answer the question whether levy of taxes per se acts as an impediment for free trade, commerce and intercourse. We may now briefly refer to these fundamentals before adverting to the provisions of Part XIII that fall for our interpretation. Power to Tax : an Attribute of sovereignty

14. Power to levy taxes has been universally acknowledged as an essential attribute of sovereignty. Cooley in his Book on Taxation - Volume-1 (4th Edn.) in Chapter-2 recognises the power of taxation to be inherent in a sovereign State. The power, says the author, is inherent in the people and is meant to recover a contribution of money or other property in accordance with some reasonable rule or apportionment for the purpose of defraying public expenses. The following passage from the book is apposite:

> "57. Power to tax as an inherent attribute of sovereignty. The power of taxation is an essential and inherent attribute of sovereignty, belonging as a matter of right to every independent government. It is possessed by the government without being expressly conferred by the people. The power is inherent in the people because the sustenance of the government requires contributions from them. In fact the power of taxation may be defined as "the power inherent in the sovereign state to recover a contribution of money or other property, in accordance with some reasonable rule or apportionment, from the property or occupations within its jurisdiction for the purpose of defraying the public expenses." Constitutional provisions relating to the power of taxation do not operate as grants of the power

of taxation to the government but instead merely constitute limitations upon a power which would otherwise be practically without limit. This inherent power to tax extends to everything over which the sovereign power extends, but not to anything beyond its sovereign power. Even the federal government's power of taxation does not include things beyond its sovereign power. But where exclusive jurisdiction over land is granted to another state or country, the land remains subject to the taxing power of the state within whose boundaries it is located."

15. To the same effect is the decision of this Court in *Raja Jagannath Baksh Singh v. State of U.P. & Anr*[16]. where this Cour observed:

"..... The power of taxation is, no doubt, the sovereign right of the State: as was observed by Chief justice Marshall in M'Culloch v. Maryland [4 Law Edn.579 p.607]
: "The power of taxing the people and their property is essential to the very existence of Government, and may be legitimately exercised on the objects to which it is applicable to the utmost extent to which the Government may choose to carry it." In that sense, it is not the function of the court to enquire whether the power of taxation has been reasonably exercised either in respect of the amount taxed or in respect of the property which is made the object of the tax. Article 265 of the Constitution provides that no tax shall be levied or collected, except by authority of law: and so, for deciding whether a tax has been validly levied or not, it would be necessary first to enquire whether the legislature which passes the Act was competent to pass it or not."

(Emphasis supplied)

16. Reference may also be made to *Dena Bank v. Bhikhabhai Prabhudas Parekh & Co*[17]. where this Court held:

"8. The principle of priority of government debts is founded on the rule of necessity and of public policy. The basic justification for the claim for priority of State debts rests on the well-recognised principle that the State is entitled to raise money by taxation because unless adequate revenue is received by the State, it would not be able to function as a sovereign Government at all. It is essential that as a sovereign, the State should be able to discharge its primary governmental functions and in order to be able to discharge such functions efficiently, it must be in possession of necessary funds and this consideration emphasises the necessity and the wisdom of conceding to the State, the right to claim priority in respect of its tax dues (see Builders Supply Corpn.[AIR 1965 SC 1061: (1965) 56 ITR 91])"

(Emphasis supplied)

17. In *Commissioner of Income Tax, Udiapur, Rajasthan v. MCdowell and Co. Ltd*[18]. where this Court reiterated the legal position in the following words:

"21. "Tax", "duty", "cess" or "fee" constituting a class denotes to various kinds of imposts by State in its sovereign power of taxation to raise revenue for the State. Within the expression of each specie each expression denotes different kind of impost depending on the purpose for which they are levied. This power can be exercised in any of its manifestation only under any law authorising levy and collection of tax as envisaged under Article 265 which uses only the expression that no "tax" shall be levied and collected except authorised by law. It in its elementary meaning conveys that to support a tax legislative action is essential, it cannot be levied and collected in the absence of any legislative sanction by exercise of executive power of State under Article 73 by the Union or Article 162 by the State.

22. Under Article 366(28) "Taxation" has been defined to include the imposition of any tax or impost whether general or local or special and tax shall be construed
accordingly. "Impost" means compulsory levy. The well-known and well-settled characteristic of "tax" in its wider sense includes all imposts. Imposts in the context have following characteristics:

(i) The power to tax is an incident of sovereignty.

(ii) "Law" in the context of Article 265 means an Act of legislature and cannot comprise an executive order or rule without express statutory authority.

(iii) The term "tax" under Article 265 read with Article 366(28) includes imposts of every kind viz. tax, duty, cess or fees.

(iv) As an incident of sovereignty and in the nature of compulsory exaction, a liability founded on principle of contract cannot be a "tax" in its technical sense as an impost, general, local or special. "

(Emphasis Supplied)

Power of Taxation under the Constitution:

18.We shall presently turn to the Constitutional limitations on the sovereign power to tax but before we do so we need to point out that while the power to levy taxes is an attribute of sovereignty, exercise of that power is controlled by the Constitution. This is evident from the provisions of Article 265 which forbids levy or recovery of any tax except by the authority of law. It reads:

"265. Taxes not to be imposed save by authority of law - No tax shall be levied or collected except by authority of law."

The authority of law referred to above must be traceable to a provision in the Constitution especially where the legislative powers are shared by the Centre and the States as is the case with our Constitution which provides for what has

been described as quasi federal system of governance.

The source of power to enact laws is contained in Articles 245 and 246 of the Constitution which read:

"245. Extent of laws made by Parliament and by the Legislatures of States - (1) Subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the Legislature of a State may make laws for the whole or any part of the State.

(2) No law made by Parliament shall be deemed to be invalid on the ground that it would have extra-territorial operation. 246. Subject-matter of laws made by Parliament and by the Legislatures of States - (1) Notwithstanding anything 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 anything in clause (3), Parliament and , subject to clause (1), 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 this 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."

19. Interpreting Articles 245 and 246, a three-Judge Bench of this Court in *M/s. Hoechst Pharmaceuticals Ltd and Ors. v. State of Bihar and Ors*[19]*.,* held on a review of the available decisions that the Constitution effects a complete separation of taxing powers of the Union and the States under Article 246 and that there is no overlapping anywhere in the exercise of that power. The sources of taxation are clearly delineated, observed the Court. The Court also held that there is a distinction between general subjects of legislation and taxation for the former are dealt within one group tax cannot be deduced from a general legislative entry. That view was approved by a Constitution Bench of this Court in *State of West Bengal v. Kesoram Industries Ltd*[20]*.* The propositions stated in the two decisions must therefore be treated to be fairly well settled. Reference may also be made to the decision of this Court in *State of Kerala and ors. v. Mar Appraem Kuri Co. Ltd. and Anr*[21]*.* where this Court explained the sweep and purport of Articles 245 and 246:

"35. Article 245 deals with extent of laws made by Parliament and by the legislatures of States. The verb "made", in past tense, finds place in the Head

Note to Article 245. The verb "make", in the present tense, exists in Article 245(1) whereas the verb "made", in the past tense, finds place in Article 245(2). While the legislative power is derived from Article 245, the entries in the Seventh Schedule of the Constitution only demarcate the legislative fields of the respective legislatures and do not confer legislative power as such. While Parliament has power to make laws for the whole or any part of the territory of India, the legislature of a State can make laws only for the State or part thereof. Thus, Article 245 inter alia indicates the extent of laws made by Parliament and by the State Legislatures.

36. Article 246 deals with the subject-matter of laws made by Parliament and by the legislatures of States. The verb "made" once again finds place in the Head Note to Article 246. This article deals with distribution of legislative powers as between the Union and the State Legislatures, with reference to the different Lists in the Seventh Schedule. In short, Parliament has full and exclusive powers to legislate with respect to matters in List I and has also power to legislate with respect to matters in List III, whereas the State Legislatures, on the other hand, have exclusive power to legislate with respect to matters in List II, minus matters falling in List I and List III and have concurrent power with respect to matters in List III. (See Subrahmanyan Chettiar v. Muttuswami Goundan)

37. Article 246, thus, provides for distribution, as between Union and the States, of the legislative powers which are conferred by Article 245. Article 245 begins with the expression "subject to the provisions of this Constitution". Therefore, Article 246 must be read as "subject to other provisions of the Constitution".

38. For the purposes of this decision, the point which needs to be emphasised is that Article 245 deals with conferment of legislative powers whereas Article 246 provides for distribution of the legislative powers. Article 245 deals with extent of laws whereas Article 246 deals with distribution of legislative powers. In these articles, the Constitution Framers have used the word "make" and not "commencement" which has a specific legal connotation. [See Section 3(13) of the General Clauses Act, 1897.]"

(Emphasis supplied)

Limitations on the Exercise of Power

20. Exercise of sovereign power is, however, subject to Constitutional limitations especially in a federal system like ours where the States also to the extent permissible exercise the power to make laws including laws that levy taxes, duties and fees. That the power to levy taxes is subject to constitutional limitations is no longer res-integra. A Constitution Bench of this Court has in *Synthetics and Chemicals Ltd. and Ors. v. State of U.P. and Ors*[22]. recognized that in India the Centre and the States both enjoy the exercise of sovereign power, to the extent the Constitution confers upon them that power. This Court declared:

"56 ... We would not like, however, to embark upon any theory of police power

because the Indian Constitution does not recognise police power as such. But we must recognise the exercise of Sovereign power which gives the State sufficient authority to enact any law subject to the limitations of the Constitution to discharge its functions. Hence, the Indian Constitution as a sovereign State has power to legislate on all branches except to the limitation as to the division of powers between the Centre and the States and also subject to the fundamental rights guaranteed under the Constitution. The Indian States, between the Centre and the States, has sovereign power. The sovereign power is plenary and inherent in every sovereign State to do all things which promote the health, peace, morals, education and good order of the people. Sovereignty is difficult to define. This power of sovereignty is, however, subject to constitutional limitations. "This power, according to some constitutional authorities, is to the public what necessity is to the individual. Right to tax or levy impost must be in accordance with the provisions of the Constitution."

21. What then are the Constitutional limitations on the power of the State legislatures to levy taxes or for that matter enact legislations in the field reserved for them under the relevant entries of List II and III of the Seventh Schedule. The first and the foremost of these limitations appears in Article 13 of the Constitution of India which declares that all laws in force in the territory of India immediately before the commencement of the Constitution are void to the extent they are inconsistent with the provisions of Part III dealing with the fundamental rights guaranteed to the citizens. It forbids the States from making any law which takes away or abridges, any provision of Part III. Any law made in contravention of the said rights shall to the extent of contravention be void. There is no gain saying that the power to enact laws has been conferred upon the Parliament subject to the above Constitutional limitation. So also in terms of Article 248, the residuary power to impose a tax not otherwise mentioned in the Concurrent List or the State List has been vested in the Parliament to the exclusion of the State legislatures, and the States' power to levy taxes limited to what is specifically reserved in their favour and no more.

22. Article 249 similarly empowers the Parliament to legislate with respect to a matter in the State List for national interest provided the Council of States has declared by a resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in national interest to do so. The power is available till such time any resolution remains in force in terms of Article 249 (2) and the proviso thereunder.

23. Article 250 is yet another provision which empowers the Parliament to legislate with respect to any matter in the State List when there is a proclamation of emergency. In the event of an inconsistency between laws made by Parliament under Articles 249 and 250, and laws made by legislature of the States, the law made by Parliament shall, to the extent of the inconsistency, prevail over the law made by the State in terms of Article 251.

24. The power of Parliament to legislate for two or more States by consent, in regard to matters not otherwise within the power of the Parliament is regulated by Article 252,

while Article 253 starting with a non-obstante clause empowers Parliament to make any law for the whole country or any part of the territory of India for implementing any treaty, agreement or convention with any other country or countries or any decision made at any international conference, association or other body.

25. Article 285 exempts the property of the Union from all taxes imposed by the States save in so far as the Parliament may by law provide. Article 286 places yet another Constitutional limitation on the State's power to collect any levy that imposes or authorises the imposition of a tax on the sale or purchase of goods where such sale or purchase takes place outside the State or in the course of import of the goods into or export of the goods outside the territory of India. It also makes any law of a State imposing tax on sale or purchase of goods of special importance in inter State trade or commerce or a tax on the sale or purchase of goods being a tax of the nature referred to in the relevant sub-clauses of clause 29(A) of Article 366 subject to such restrictions and conditions as to the system of levy, rates and other incidents of tax as the Parliament may by law specify.

26. Article 287 places a Constitutional limitation on the State's legislative power to enact laws in so far as imposition of tax on consumption or sale of electricity consumed by the Government of India or sold to the Government of India for consumption by the Government or for consumption of the construction, maintenance or operation of any railway by the Government of India or a rail company etc. Similarly, Article 288 contains a Constitutional limitation on the power of the State in so far as imposition of a tax in respect of any water or electricity stored, generated, consumed, distributed or sold by any authority established by any existing law or any law made by the Parliament is concerned.

27. It would thus appear that even when Article 246(2) and (3) confers exclusive power on the State legislatures to make laws with respect to matters in the Seventh Schedule such legislative power is exercisable subject to constitutional limitations referred to above. What is significant is that the power of the State legislatures to levy taxes is also subject to the limitations of Article 304(a) of the Constitution appearing in Part XIII thereof, which part regulates trade, commerce and intercourse within the territory of India and comprises Articles 301 to 307. The provisions of these Articles have been the subject matter of a series of decisions of this Court including several Constitution Bench decisions to some of which we shall presently refer. The language employed in the provisions and the non-obstante clauses with which the same start have all the same given rise to several contentious issues for determination by this Court over the past five decades or so. The fact that the present batch of cases had to be referred to a Nine-Judge Bench to once again examine the very same issues as have been debated and determined in the previous judgments of this Court only shows that the task of interpreting the provisions is by no means easy and has in fact become more and more difficult on account of the pronouncements of this Court taking different views not many of which have been unanimous. The marked difference in the approach adopted by learned counsel for the parties in these appeals is also a measure of the complexities of issues that fall for determination. This is specially so because the prevailing legal position in terms of the judgment of this Court in Atiabari and Automobile cases (supra)

holding that fiscal measures that are compensatory fall beyond the mischief of Article 301 has been questioned by both sides. Mr. Harish Salve who led the forensic exercise followed by M/s.Arvind Datar, Laxmi Kumaran, Ravindra Shrivastava, N. Venkataraman and others vehemently argued that the "Compensatory Tax Theory" propounded by the Seven Judges Bench of this Court in Automobile case (supra) had no legal basis or constitutional sanction and was neither acceptable nor workable. That is particularly so because the State legislatures had taken umbrage under the "Compensatory Tax Theory" and declared the fiscal levies imposed by them to be compensatory in character and claimed the same to be outside the mischief of Article 301 and consequently immune from any challenge on the ground that these taxes and levies were unreasonable restrictions on the right to free trade and commerce. The States who have enacted the laws providing for levy of taxes on the entry of goods into a local area within the meaning of Entry 52 of List II have, on the other hand similarly contended that the Compensatory Tax Theory is bereft of any legal basis and that the decision in Atiabari and Automobile cases (supra) need to be revisited to restore and protect the sovereign power of legislation of the States and the Federal character of our polity. Suffice it to say that except a feeble attempt made by some Counsel, there has been a general consensus that the compensatory tax theory deserves to be rejected and the issues examined afresh on a true and correct interpretation of the relevant constitutional provisions. We are mentioning all this only to show that even after fifty years and several illuminating pronouncements of this Court, the cleavage in the judicial opinion as to the true and correct legal position on the subject continues to loom large and haunt lawyers and litigants and, if we may say so, even Judges alike. The present reference to a larger Bench is in that backdrop expected to give a quietus to this raging legal controversy of considerable complexity, though given the perseverance of the litigants and the ingenuity of the bar a quietus is only a pious hope which has and may even in future elude us. Constitutional Limitations must be Express:

28. The power to levy taxes, being a sovereign power controlled only by the Constitution, any limitation on that power must be express. That proposition is well settled by the decisions of this Court in *Maharaj Umeg Singh v. State of Bombay*[23], *and Firm Bansidhar Premsukhdas v. State of Rajasthan*[24] In Umeg Singh's case (supra) this Court stated the legal position in the following words:

> "12 The legislative competence of the State Legislature can only be circumscribed by express prohibition contained in the Constitution itself and unless and until there is any provision in the Constitution expressly prohibiting legislation on the subject either absolutely or conditionally, there is no fetter or limitation on the plenary powers which the State Legislature enjoys to legislate on the topics enumerated in the Lists II & III of the Seventh Schedule to the Constitution.
>
> xxxx xxxx xxxx
>
> 13. The fetter or limitation upon the legislative power of the State Legislature which had plenary powers of legislation within the ambit of the legislative heads

specified in the Lists II & III of the Seventh Schedule to the Constitution could only be imposed by the Constitution itself and not by any obligation which had been undertaken by either the Dominion Government or the Province of Bombay or even the State of Bombay. Under Article 246 the State Legislature was invested with the power to legislate on the topics enumerated in Lists II & III of the Seventh Schedule to the Constitution and this power was by virtue of article 245(1) subject to the provisions of the Constitution. The Constitution itself laid down the fetters or limitations on this power, e.g., in Article 303 or article 286(2). But unless and until the Court came to the conclusion that the Constitution itself had expressly prohibited legislation on the subject either absolutely or conditionally the power of the State Legislature to enact legislation within its legislative competence was plenary. Once the topic of legislation was comprised within any of the entries in the Lists II & III of the Seventh Schedule to the Constitution the fetter or limitation on such legislative power had to be found within the Constitution itself and if there was no such fetter or limitation to be found there the State Legislature had full competence to enact the impugned Act no matter whether such enactment was contrary to the guarantee given, or the obligation undertaken by the Dominion Government or the Province of Bombay or even the State of Bombay.

29. Again in Bansidhar's case (supra) this Court reiterated the legal position in the following words:

"8... It is well-established that Parliament or the State Legislatures are competent to enact a law altering the terms and conditions of a previous contract or of a grant under which the liability of the Government of India or of the State Governments arises. The legislative competence of Parliament or of the State Legislatures can only be circumscribed by express prohibition contained in the Constitution itself and unless and until there is any provision in the Constitution expressly prohibiting legislation on the subject either absolutely or conditionally, there is no fetter of limitation on the plenary powers which the Legislature is endowed with for legislating on the topics enumerated in the relevant lists. This view is borne out by the decision of the Judicial Committee in Thakur Jagannath Baksh Singh v. The United Provinces [1946 FCR 111] in which a similar complaint was made by the taluqdars of Oudh against the United Provinces Tenancy Act (U.P. Act 17 of 1939). It was held by the Judicial Committee that the Crown cannot deprive itself of its legislative authority by the mere fact that in the exercise of its prerogative it makes a grant of land within the territory over which such legislative authority exists, and no court can annul the enactment of a legislative body acting within the legitimate scope of its sovereign competence. If therefore, it be found that the subject-matter of a Crown grant is within the competence of a Provincial legislature nothing can prevent that legislature from legislating about it unless the Constitution Act itself expressly prohibits legislation on the subject either absolutely or conditionally. Accordingly, in the absence of any such express prohibition, the United Provinces Tenancy Act, 1939, which in consolidating and amending the law relating to agricultural tenancies and other matters connected therewith in Agra and Oudh, dealt with matters within the

> exclusive legislative competence of the Provincial legislature under Item 21 of List 11 of the Seventh schedule to the Government of India Act, 1935, was intra vires the Provincial legislature notwithstanding that admittedly some of its provisions cut down the absolute rights claimed by the appellant taluqdar to be comprised in the grant of his estate as evidenced by the sanad granted by the Crown to his predecessor. The same principle has been reiterated by this Court *in Maharaj Umeg Singh and others v. The State of Bombay [1955 2 SCR 164].* It was pointed out that in view of Art. 246 of the Constitution, no curtailment of legislative competence can be spelt out of the terms of clause 5 of the Letters of Guarantee given by the Dominion Government to the Rulers of "States" subsequent to the agreements of Merger, which guaranteed, inter alia, the continuance of Jagirs in the merged 'States'. This principle also underlies the recent decision of this Court in Maharaja Shree Umaid Mills Ltd. v. Union of India [1963 Supp 2 SCR 5151 in which it was pointed out that there is nothing in Art. 295 of the Constitution which prohibits Parliament from enacting a law altering the terms. and conditions of a contract or of a grant under which the liability of the Government of India arises...."
>
> (Emphasis Supplied)

30. One other fundamental aspect which must always be kept in mind while interpreting the provisions of the Constitution is the federal structure envisaged by it. Whether or not the Constitution of India is truly federal in character has been the subject matter of debate not only in the Constituent Assembly but also in Courts for over 60 years. The character of the Constitutional scheme described in the Constituent Assembly Debates was that there were doubts expressed whether the Constitution really provided a federal structure in the governance of the country. The criticism was that the scheme underlying the Constitution was more unitary than federal, on account not only of several provisions in the Constitution that empowered the Centre to at times intervene and enact laws for the States but also on account of the Centre's power to take over the governance of the State. Repelling that criticism, Dr. B.R. Ambedkar speaking in the Constituent Assembly explained the true character of the Constitution of India in the following significant words:

> "There is only one point of constitutional import to which I propose to make a reference. A serious complaint is made on the ground that there is too much of centralisation and that the States have been reduced to municipalities. It is clear that this view is not only an exaggeration, but is also founded on a misunderstanding of what exactly the Constitution contrives to do. As to the relation between the Centre and the States, it is necessary to bear in mind the fundamental principle on which it rests. The basic principle of federalism is that the legislative and executive authority is partitioned between the Centre and the States not by any law to be made by the Centre but by the Constitution itself. This is what Constitution does. The States under our Constitution are in no way dependent upon the Centre for their legislative or executive authority. The Centre and the States are coequal in this matter. It is difficult to see how such a Constitution can be called centralism. It may be that the Constitution assigns to

the Centre too large a field for the operation of its legislative and executive authority than is to be found in any other federal Constitution. It may be that the residuary powers are given to the Centre and not to the States. But these features do not form the essence of federalism. The chief mark of federalism as I said lies in the partition of the legislative and executive authority between the Centre and the units by the Constitution. This is the principle embodied in our Constitution."

31. To the same effect was the answer given to the criticism by Shri T.T. Krishnamachari during the Constituent Assembly Debates on the draft Constitution, when he said:

"Sir, I would like to go into a few fundamental objections because as I said it would not be right for us to leave these criticisms uncontroverted. Let me take up a matter which is perhaps partly theoretical but one which has a validity so far as the average man in this country is concerned. Are we framing a unitary Constitution? Is this Constitution centralising power in Delhi? Is there any way provided by means of which the position of people in various areas could be safeguarded, their voices heard in regard to matters of their local administration? I think it is a very big charge to make that this Constitution is not a federal Constitution, and that it is a unitary one. We should not forget that this question that the Indian Constitution should be a federal one has been settled by our Leader who is no more with us, in the Round Table Conference in London eighteen years back."

"I would ask mv honourable friend to apply a very simple test so far as this Constitution is concerned to find out whether it is federal or not. The simple definition I have got from the German school of political philosophy is that the first criterion is that the State must exercise compulsive power in the enforcement of a given political order, the second is that these powers must be regularly exercised over all the inhabitants of a given territory, and the third is the most important and that is that the activity of the State must not be completely circumscribed by orders handed down for execution by the superior unit. The important words are 'must not be completely circumscribedwhich envisages some powers of the State are bound to be circumscribed by the exercise of federal authority. Having all these factors in view, I will urge that our Constitution is a federal Constitution. I will urge that our Constitution is one in which we have given power to the units which are both substantial and significant in the legislative sphere and in the executive sphere."

(Emphasis Supplied)

32. Whether or not the Constitution provides a federal structure for the governance of the country has been the subject matter of a long line of decisions of this Court, reference to all of which may be unnecessary but the legal position appears to be fairly well settled that the Constitution provides for a quasi federal character with a strong bias towards the Centre. The pronouncements recognised the proposition that even

when Constitution may not be strictly federal in its character as the United States of America, where sovereign States came together to constitute a federal union, where each State enjoins a privilege of having a Constitution of its own, the significant feature of a federal Constitution are found in the Indian Constitution which makes it a quasi federal Constitution, if not truly federal in character and in stricto sensu federal. The two decisions which stand out in the long line of pronouncements of this Court on the subject may, at this stage, be briefly mentioned. The first of these cases is the celebrated decisions of this Court in Kesavananda Bharati case
(supra), wherein a thirteen Judges Bench of this Court, Sikri CJ (as His Lordship then was), being one of them talks about whether the Constitution of India was federal in character and if so whether federal character of the Constitution formed the basic feature of the Constitution. Sikri CJ. summed up the basic feature of the Constitution in the following words:

> "292 The true position is that every provision of the Constitution can be amended provided in the result the basic foundation and structure of the Constitution remains the same. The basic structure may be said to consist of the following features:
>
> (1) Supremacy of the Constitution.
>
> (2) Republican and Democratic form of Government.
>
> (3) Secular character of the Constitution.
>
> (4) Separation of powers between the legislature, the executive and the judiciary;
>
> (5)Federal character of the Constitution.
>
> 293. The above structure is built on the basic foundation i.e. the dignity and freedom of the individual. This is of supreme importance. This cannot by any form of amendment be destroyed.
>
> 294. The above foundation and the above basic features are easily discernible not only from the preamble but the whole scheme of the Constitution, which I have already discussed."

To the same effect are the views expressed by Shelat and Grover JJ. who declared that the federal character of the Constitution is a part of its basic structure.

33. In *S.R. Bommai v. Union of India*[25], this Court had yet another occasion to examine whether the Constitution was federal in nature. Speaking for himself and Justice Kuldeep Singh, Sawant J. while referring to H.M Seervai's commentary on “Constitutional Law of India” held that the principle of federalism has not been watered down so as to make the Constitution unitary in character. The presence in the Constitution exclusive legislative powers conferred on the State and the provision that such powers may be exercised by the Parliament during an emergency may not affect

and dilute the federal character of the Constitution. So also, the provisions of Article 355 imposing the duty on the Union to protect a State against internal disorder are not inconsistent with the federal principles nor are the powers vested in the Central Government under Article 356 inconsistent with the federal character of the Constitution. The Court, in particular, dealt with the question whether List II contains unimportant matters thereby denuding the Constitution of its federal character. The Court observed that List II contains very important subjects assigned to the State including the power to levy taxes which powers are made mutually exclusive so that ordinarily the States have independent source of revenue of their own. The following passages from the decision are apposite:

> "97 (k) The view that unimportant matters were assigned to the States cannot be sustained in face of the very important subjects assigned to the States in List II, and the same applies to taxing powers of the States, which are made mutually exclusive of the taxing powers of the Union so that ordinarily the States have independent source of revenue of their own. The legislative entries relating to taxes in List II show that the sources of revenue available to the States are substantial and would increasingly become more substantial. In addition to the exclusive taxing powers of the States, the States become entitled either to appropriate taxes collected by the Union or to a share in the taxes collected by the Union.
>
> 99. The above discussion thus shows that the States have an independent constitutional existence and they have as important a role to play in the political, social, educational and cultural life of the people as the Union. They are neither satellites nor agents of the Centre. The fact that during emergency and in certain other eventualities their powers are overridden or invaded by the Centre is not destructive of the essential federal nature of our Constitution. The invasion of power in such circumstances is not a normal feature of the Constitution. They are exceptions and have to be resorted to only occasionally to meet the exigencies of the special situations. The exceptions are not a rule.
>
> 100. For our purpose, further it is really not necessary to determine whether, in spite of the provisions of the Constitution referred to above, our Constitution is federal, quasi-federal or unitary in nature. It is not the theoretical label given to the Const-itution but the practical implications of the provisions of the Constitution which are of importance to decide the question that arises in the present context, viz., whether the powers under Article 356(1) can be exercised by the President arbitrarily and unmindful of its consequences to the governance in the State concerned. So long as the States are not mere administrative units but in their own right constitutional potentates with the same paraphernalia as the Union, and with independent Legislature and the Executive constituted by the same process as the Union, whatever the bias in favour of the Centre, it cannot be argued that merely because (and assuming it is correct) the Constitution is labelled unitary or quasi-federal or a mixture of federal and unitary structure, the President has unrestricted power of issuing Proclamation under Article 356(1). If the Presidential powers under the said provision are subject to judicial review

within the limits discussed above, those limitations will have to be applied strictly while scrutinising the concerned material."

(Emphasis Supplied)

34. What is important is that B.P. Jeevan Reddy, J. speaking for himself and Aggarwal J., while holding the Constitution to be federal in character cautioned that the Centre cannot tamper with the powers conferred upon the States. States are not mere appendages of the Centre within the sphere allotted to them. The States are supreme and the Centre cannot tamper with their powers.

35. Justice K. Ramaswamy, speaking for himself also accepted federalism of the Indian Constitution as a basic feature. One other decision that has dealt with the federal character of the Constitution of India is *Kuldeep Nair v. Union of India and Ors*[26]. wherein this Court held that nature of federalism in the Indian Constitution is no longer res integra. Relying upon the Constituent Assembly Debates to which we have referred earlier. The Court declared:

"50. A lot of energy has been devoted on behalf of the petitioners to build up a case that the Constitution of India is federal. The nature of federalism in the Indian Constitution is no longer res integra.

51. There can be no quarrel with the proposition that the Indian model is broadly based on federal form of governance. Answering the criticism of the tilt towards the Centre, Shri T.T. Krishnamachari, during debates in the Constituent Assembly on the draft Constitution, had stated as follows:

36. While parting with this aspect we must also refer to the decision of this Court in Re: Under Article 143, Constitution of India (Special Reference No.1 of 1964) AIR 1965 SC 745 wherein this Court held:

"39. In dealing with this question, it is necessary to bear in mind one fundamental feature of a Federal Constitution. In England, Parliament is sovereign; and in the words of Dicey, the three distinguishing features of the principle of Parliamentary Sovereignty are that Parliament has the right to make or unmake any law whatever; that no person or body is recognised by the law of England as having a right to override or set aside the legislation of Parliament, and that the right or power of Parliament extends to every part of the Queen's dominions (1). On the other hand, the essential characteristic of federalism is "the distribution of limited executive, legislative and judicial authority among bodies which are coordinate with and independent of each other". The supremacy of the constitution is fundamental to the existence of a federal State in order to prevent either the legislature of the federal unit or those of the member States from destroying or impairing that delicate balance of power which satisfies the particular requirements of States which are desirous of union, but not prepared to merge their individuality in a unity. This supremacy of the constitution is protected by the authority of an independent judicial body to act as the interpreter of a scheme of

distribution of powers. Nor is any change possible in the Constitution by the ordinary process of federal or State legislation (2). Thus the dominant characteristic of the British Constitution cannot be claimed by a Federal Constitution like ours."

37. Before we turn to the provisions of Articles 301 to 307 comprising Part XIII of the Constitution, we need to also bear in mind the historical backdrop in which that part of the Constitution was enacted. While doing so we must at the threshold acknowledge that the historical perspective of Part XIII has been explored several times during the past in several pronouncements of this Court. The exposition of different stages of evolution and development of what comprises Part XIII today has been both extensive as well as incisive. The decisions of the Court have gone into great details while examining the history of Part XIII. It will, therefore, be presumptuous for us to suggest that the historical basis of Part XIII is a virgin area being traversed for the first time. In fairness to the scholarly pronouncements that have preceded the present batch of cases, we must acknowledge with gratitude the usefulness of the in-depth study and understanding of the Judges who have examined and traced the evolution of Part XIII while drawing their conclusions from the same, no matter such inferences and conclusions have more often than not been varied which is but natural when one examines history or the events that led to its making.

38. It is, in our opinion, unnecessary to refer to all the decisions that have till now traced the development of the jurisprudence concerning Part XIII from its inception. A reference to some of the decisions alone should, in our opinion, suffice. The first of these decisions to which we must make a reference is the Constitution Bench decision in M.P.V. Sunderaramier v. State of Andhra Pradesh, AIR 1958 SC 468. That was a case filed under Article 32 of the Constitution of India for a Writ of Prohibition restraining the State of Andhra Pradesh from imposing a tax on inter-State trade of sale and purchase of yarn. The levy and collection of any such tax was according to the petitioner contrary to the provision contained in Article 282 (6) of the Constitution of India. One of the questions that fell for consideration of the Court was whether the States could impose a tax on inter-State sales having regard to the provisions of Articles 246 and 301 of the Constitution of India. The argument was that the freedom guaranteed under Article 301 included freedom from taxation with the result that any tax on inter-State sales would offend that guarantee. The contention was rejected by this Court in unequivocal terms. The Court said:

"(50) This contention suffers, in our opinion, from serious infirmities. It overlooks that our Constitution was not written on a tabula-rasa, that a Federal Constitution had been established under the Government of India Act, 1935, and though that has undergone considerable change by wav of repeal, modification and addition, it still remains the framework on which the present Constitution is built, and that the provisions of the Constitution must accordingly be read in the light of the provisions of the Government of India Act."

(Emphasis supplied)

39. Three years later came the Constitution Bench decision of this Court in Atiabari Tea Company Ltd. case (supra). The petitioner in that case questioned the constitutional validity of Assam Taxation (on Goods Carried by Roads or Inland Waterways) Act, (Assam Act XIII of 1954), before the High Court. The Writ Petition having failed, the matter was brought up in appeal before this Court which was heard alongwith several petitions filed under Article 32 of the Constitution of India. The impugned legislation levied taxes on certain goods carried by road and inland waterways in the State of Assam. The levy under the legislation was challenged primarily on the ground that the same was ultra vires of the Constitution inter aila because of their repugnance with the provision of Article 301 of the Constitution. This Court by a majority struck down the Constitutional validity of the enactment holding that the impugned levy operated directly and immediately as a restriction on free trade, commerce and intercourse guaranteed under Article 301 of the Constitution of India. The decision propounded three different points of view, one each taken by B.P. Sinha, CJ. and J.C. Shah, J. and the third by majority comprising P.B. Gajendragadkar, K.N. Wanchoo and K.C. Das Gupta, JJ. We shall presently deal with the rationale underlying the three views but before we do so, we may gainfully extract from the decision rendered by Sinha, CJ., the historical perspective in which Part XIII of the Constitution was enacted. In Para 9 of the Report, Sinha, CJ., as His Lordship then was, traced the evolution of Part XIII in the following words:

> "9. In order to fully appreciate the implications of the provisions of Part XIII of the Constitution, it is necessary to bear in mind the history and background of those provisions. The Constitution Act of 1935 (Government of India Act, 26 ('Geo. 5, Ch. 2) which envisages the federal constitution for the whole of India, including what was then Indian India in contradistinction to British India, which could not be fully implemented and which also introduced full provincial autonomy enacted Section 297 prohibiting certain restrictions on internal trade in these terms:
>
> 297. (1) No Provincial Legislature or Government shall - (a) By virtue of the entry in the Provincial Legislative List relating to trade and commerce within the Province, or the entry in that list relating to the production, supply, and distribution of commodities, have power to pass any law or take any executive action prohibiting or restricting the entry into, or export from the Province of goods of any class or description; or
>
> (b) By virtue of anything in this Act have power to impose any tax, cess, toll or due which, as between goods manufactured or produced in the Province and similar goods not so manufactured or produced, discriminates in favour of the former, or which, in the case of goods manufactured or produced outside the Province, discriminates between goods manufactured or produced in one locality and similar goods manufactured or produced in another locality.
>
> (2) Any law passed in contravention of this section shall, to the extent of the contravention, be invalid."

10. It will be noticed that the prohibition contained in the section quoted above applied only to Provincial Governments and Provincial Legislatures with reference to entries in the Provincial Legislative List relating to trade and commerce within the Province and to production, supply and distribution of commodities. That section dealt with prohibitions or restrictions in respect of import into or export from a Province, of goods generally. It also dealt with the power to impose taxes etc. and prohibited discrimination against goods manufactured or produced outside a Province or goods produced in different localities. Part XIII of the Constitution has introduced all those prohibitions, not only in respect of State Legislatures, but of Parliament also. ....

11. In this connection it has got to be remembered that before the commencement of the Constitution about two-thirds of India was directly under British rule and was called 'British India' and the remaining about one-third was being directly ruled by the Princes and was known as "Native States". There were a large number of them with varying degrees of sovereignty vested in them. Those rulers had, broadly speaking, the trappings of a Sovereign State with power to impose taxes and to regulate the flow of trade, commerce and intercourse. It is a notorious fact that many of them had erected trade barriers seriously impeding the free flow of trade, commerce and intercourse, not only shutting out but also shutting in commodities meant for mass consumption. Between the years 1947 and 1950 almost all the Indian States entered into engagements with the Government of India and ultimately merged their individualities into India as one political unit, with the result that what was called British India, broadly speaking, became, under the Constitution, Part A States, and subject to certain exceptions not relevant to our purpose, the Native States became Part B States. We also know that before the Constitution introduced the categories of Part A States, Part B States and Part C States (excluding Part D relating to other territories), Part B States themselves, before their being constituted into so many units, contained many small States, which formed themselves into Unions of a number of States, and had such trade barriers and custom posts, even inter se. But even after the merger, the Constitution had to take notice of the existence of trade barriers and therefore had to make transitional provisions with the ultimate objective of abolishing them all. Most of those Native States, big or small, had their own taxes, cesses, tolls and other imposts and duties meant not only for raising revenue, but also as trade barriers and tariff walls. It was in the background of these facts and circumstances that the Constitution by Article 301 provided for the abolition of all those trade barriers and tariff walls. When for the first time in the history of India the entire territory within the geographical boundaries of India, minus what became Pakistan, was knit into one political unit, it was necessary to abolish all those trade barriers and custom posts in the interest of national solidarity, economic and cultural unity as also of freedom of trade, commerce and intercourse."

(Emphasis supplied)

40. The majority opinion offered by Gajendragadkar J., also traced the history of Part

XIII in the following words:

> "33. Let us first recall the political and constitutional background of Part XIII. It is a matter of common knowledge that, before the Constitution was adopted, nearly two-thirds of the territory of India was subject to British Rule and was then known as British India, while the remaining part of the territory of India was governed by Indian Princes and it consisted of several Indian States. A large number of these States claimed sovereign rights within the limitations imposed by the paramount power in that behalf, and they purported to exercise their legislative power of imposing taxes in respect of trade and commerce which inevitably led to the erection of customs barriers between themselves and the rest of India. In the matter of such barriers British India was governed by the provisions of Section 297 of the Constitution Act, 1935. To the provisions of this section we will have occasion later to refer during the course of this judgment. Thus, prior to 1950 the flow of trade and commerce was impeded at several points which constituted the boundaries of Indian States. After India attained political freedom in 1947 and before the Constitution was adopted the historical process of the merger and integration of the several Indian States with the rest of the country was speedily accomplished with the result that when the Constitution was first passed the territories of India consisted of Part A States which broadly stated represented the provinces in British India, and Part B States which were made up of Indian States. This merger or integration of Indian States with the Union of India was preceded by the merger and consolidation of some of the States inter-se between themselves. It is with the knowledge of the trade barriers which had been raised by the Indian States in exercise of their legislative powers that the Constitution- makers framed the Articles in Part XIII. The main object of Article 301 obviously was to allow the free flow of the stream of trade, commerce and intercourse throughout the territory of India."

41. Then came the decision of this Court in Automobile case (supra) wherein, this Court examined the challenge to the Rajasthan Motor Vehicles Act, inter aila, on the ground that levy of taxes imposed under the said Act were offensive to Article 301 of the Constitution of India. S.K. Das, J. speaking for the majority also traced the historical background of Part XIII in the following words:

> "7. So far we have set out the factual and legal background against which the problem before us has to be solved. We must now say a few words regarding the historical background. It is necessary to do this, because extensive references have been made to Australian and American decisions, Australian decisions with regard to the interpretation of Section 92 of the Australian Constitution and American decisions with regard to the Commerce clause of the American Constitution. This Court pointed out in the Atiabari Tea Co. case (1961) 1 SCR 809 : (AIR 1961 SC 232), that it would not be always safe to rely upon the American or Australian decisions in interpreting the provisions of our Constitution. Valuable as those decisions might be in showing how the problem of freedom of trade, commerce and intercourse was dealt with in other federal constitutions, the provisions of our Constitution must be interpreted against the

historical background in which our Constitution was made; the background of problems which the Constitution-makers tried to solve according to the genius of the Indian people whom the Constitution-makers represented in the Constituent Assembly. The first thing to be noticed in this connection is that the Constitution-makers were not writing on a clean slate. They had the Government of India Act, 1935 and they also had the administrative set up which that Act envisaged. India then consisted of various administrative units known as Provinces, each with its own administrative set up. There were differences of language, religion etc. Some of the Provinces were economically more developed than the others. Even inside the same Province, there were under developed, developed and highly developed areas from the point of view of industries, communications etc. The problem of economic integration with which the Constitution-makers were faced was a problem with many facets. Two questions, however, stood out; one question was how to achieve a federal, economic and fiscal integration, so that economic policies affecting the interests of India as a whole could be carried out without putting an ever-increasing strain on the unity of India, particularly in the context of a developing economy. The second question was how to foster the development of areas which were under-developed without creating too many preferential or discriminative barriers. Besides the Provinces, there were the Indian States also known as Indian India. After India attained political freedom in 1947 and before the Constitution was adopted, the process of merger and integration of the- Indian States with the rest of the country had been accomplished so that when the Constitution was first passed the territory of India consisted of Part A States, which broadly stated, represented the Provinces in British India, and Part B States which were made up of Indian States. There were trade barriers raised by the Indian States in the exercise of their legislative powers and the Constitution-makers had to make provisions with regard to those trade barriers as well. The evolution of a federal structure or a quasi-federal structure necessarily involved, in the context of the conditions then prevailing, a distribution of powers and a basic part of our Constitution relates to that distribution with the three legislative lists in the Seventh Schedule "

42. Hidayatullah J., in a separate dissenting opinion traced at great length the historical evolution of not only the federal structure of the Government of India Act, 1915 but also the recommendations made by the Simon Commission and the Joint Parliamentary Committee on the Evolution of such Federalism and for the protection of trade, commerce and intercourse. His Lordship referred to the backdrop in which the Government of India Act, 1935 was enacted, including the recommendations made by the Butler Committee, the Round Table Conference, the Federal Structure Committee, the Federal Legislature and Provincial Legislature Committee and the Joint Parliamentary Committee to eventually conclude that the avowed object underlying all these recommendations and constitutional framework was to ensure that the accession of the State to the federation implies its acceptance of the principle that it will not set up a barrier to free interchange so formidable as to constitute a threat to the future of the federation. Based on the historical developments decades before the enactment of Government of India Act, 1935, his Lordship concluded:

"95. The detailed examination of the history lying at the back of the Government of India Act, 1935 lays bare some fundamental facts and premises. It shows that the process through a whole century was the breakup of a highly centralized Government and the creation of autonomous Provinces with distinct and separate political existence, to be combined inter se and with the Indian States, at a later period, in a federation. To achieve this, not only was there a division of the heads of legislation, but the financial resources were also divided and separate fiscs for the federation and the Provinces were established. The fields of taxation were demarcated, and those for the Provinces were chosen with special care to make these units self-supporting as far as possible with enough to spare for "nation-building activities". In this arrangement, the door was open for the Indian States to join on the same basis and on terms of equality. The most important fact was that unlike the American and the Canadian Constitutions the commerce power was divided between the Centre and the Provinces as the Entries quoted by us clearly show. The commerce power of the Provinces was exercisable within the Provinces. The fetter on the commercial power of the Provinces was placed by Section 297. This was in two directions. Clause (a) of sub-section (1) banned restrictions at the barriers of the Provinces on the entry and export of goods, and clause (b) prohibited discrimination in taxing goods between goods manufactured and produced in the Province as against goods not so manufactured or produced and local discriminations.

(Emphasis supplied)

43. In the opinion of Hidayatullah J., as his Lordship then was, several pitfalls existed in the 1935 Act regarding trade and commerce which were sought to be remedied by the framers of the Constitution while maintaining its federal structure. The following passage is, in this regard, instructive:

"96. When drafting the Constitution of India, the Constituent Assembly being aware of the problems in various countries where freedom of trade, commerce and intercourse has been provided differently and also the way the Courts of those countries have viewed the relative provisions, must have attempted to evolve a pattern of such freedom suitable to Indian conditions. The Constituent Assembly realised that the provisions of Section 297 and the Chapter on Discriminations in the Government of India Act, 1935 hardly met the case, and were inadequate. They had to decide the following questions: (a) whether to give the commerce power only to Parliament or to divide it between Parliament and the State Legislatures; (b) whether to ensure freedom of trade, commerce and intercourse inter-State, that is to say, at the borders of the States or to ensure it even intra-State; (c) whether to make the prohibition against restrictions absolute or qualified, and if so, in what manner; (d) if qualified, by whom was the restriction to be imposed and to what extent; (e) whether the freedom should be to the individual or also to trade and commerce as a whole; (f) what to do with the existing laws in British India and more so, in the acceding Indian States; (g) whether any special provisions were needed for emergencies; (h) what should be

the special provisions to enable the States to levy taxes on sale of goods, which taxes were to be the main source of income for the States according to the experts. All these matters have, in fact, been covered in Part XIII, and the pitfalls which were disclosed in the Law Reports of the Countries which had accepted freedom of trade and commerce have been attempted to be avoided by choosing language appropriate for the purpose. In addition to this, the broad pattern of the political set-up, namely, a federation of autonomous States was not lost sight of. These autonomous conditions had strengthened during the operation of the 1935 Constitution and led to what Prof. Coupland described as "Provincial-patriotism", for which the reason, according to the learned Professor was:

"In the course of the last few years, moreover, the sense of Provincial patriotism has been strengthened by the advent of a full Provincial self-government. The people took a new pride in Governments that were now in a sense theirs." (The Constitutional Problem in India, part III p. 40)."

44. The historical backdrop painted by the decisions of this Court referred to above has not been challenged on a question of fact. Inferences drawn from the same may have, as noticed earlier, varied depending on the individual perspective of the Judges about the said backdrop. The common thread that runs through the historical narratives in the pronouncements of this Court however is discernible and may be briefly summed-up at this stage. The first of these threads that runs through the historical perspective is the fact that before commencement of the Constitution nearly 2/3rd of the country was ruled by the British while the remaining 1/3rd was ruled by the Princes also known as native States that enjoyed varying degrees of sovereignty over their respective territories. These rulers had the power to impose taxes and to regulate the flow of trade, commerce and intercourse. Some of them had erected trade barriers thereby impeding free flow of trade, commerce and intercourse. With the merger of these Princely States into the dominion of India to constitute one single political entity, that part of the country that was ruled by the British came to be known as Part-A State while the native States became Part B States. What is significant is that even after the merger of these States, the Constitution had to acknowledge the existence of trade barriers and make transitional provisions with a view to eventually abolishing the same. It was in that background that the Constitution by Article 301 provided for the abolition of all such trade barriers consequent upon the entire geographical boundaries of India being knit into one political unit. The whole object underlying the removal of such barriers was to facilitate free trade, commerce and intercourse in the interest of national solidarity and economic unity of the country. The evolution of Articles 301 to 307 comprising Part XIII of the Constitution is also punctuated by several events, twists and turns to which we may briefly refer at this stage, but, while we may do so, we need to remember that Section 297 of the Government of India Act, 1935 dealt with the subject that eventually came under the umbrella of Part XIII and prohibited provincial governments from imposing barriers on trade within the country. The said provision also prohibited levy of cess, tolls or other tax duties which discriminated between the goods manufactured in one locality as against similar goods manufactured elsewhere. It is because of the said provision that Venkatarama Iyer, J. in MPV Sunderaramier's case (supra) made the observation that the Constitution was not written on a tabula rasa.

45. The first germ plasma for Article 301 was located in what was introduced as Clause 13 in the draft submitted by the Sub-Committee on fundamental rights comprising Mr. K.M. Munshi, Sir Alladi Krishnaswami Ayyar and Sir B.N. Rau amongst others. The clause was in the following words:

> "Subject to regulation by the law of the Union, trade, commerce and intercourse among the units, whether by means of internal carriage or by ocean navigation, shall be free: Provided that any unit may by law impose reasonable restrictions thereon in the interest of public order, morality or health." From the note of Sir B.N. Rau it is evident that the first part of clause 13 (supra) was adopted from Section 92 of the Australian Constitution while the proviso at the end of the clause was new.

46. Sir Alladi Krishnaswami Ayyar in the Draft Report of 10th, 14th and 15th April, 1947 in relation to Clause 13 suggested that it must be made clear that:

> "(1) goods from other parts of India than in the units' concerned coming into the units cannot escape duties and taxes to which the goods produced in the units in themselves are subject.
>
> (2) It must also be open to the unit in an emergency to place restrictions on the rights declared by the clause."

47. The above suggestions were accepted and it was modified and incorporated as Clause 14 in the following words:

> "14. (1) Subject to regulation by the law of the Union trade, commerce and intercourse among the units by and between the citizens shall be free:
>
> Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in an emergency: Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject: Provided further that no preference shall be given by any regulation of commerce or revenue by a unit to one unit over another. [N.B. - A proviso will have to be added to meet the difficulty pointed out in para 6 of our report.]
>
> (2) Trade, commerce or intercourse within the territories of the Union by or with any person other than the citizens shall be regulated and controlled by the law of the Union."

48. The above clause then came up for consideration before the Advisory Committee where an elaborate debate ensued. What is of considerable importance is the statement of Sir Alladi Krishnaswami Ayyar where he explained the purpose of enabling a State to impose reasonable restriction in the interest of public order, morality, health or in an emergency:

"Chairman: Then let us take up clause 14

C. Rajagopalachari: I Think we should add to 14 (1) that this shall not be a bar to the imposition of taxes for genuine purposes of revenue. Many Members: That comes later on: "N.B. A proviso will have to be added to meet the difficulty pointed out in para 6 of our report."

C. Rajagopalachari: That is why I am adding it. Alladi Krishnaswami Ayyar: "Subject to regulation by the law of the Union, trade, commerce, and intercourse among the units by and between the citizens shall be free." That is the general principle. Then come the exceptions, "Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in an emergency." Suppose there is a general famine, and people are starved, that is what is meant here to be dealt with. And then "Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject." That is to say, we ought not to differentiate; but at the same time, goods coming in should not go scot-free; they should be subject to the same duty as goods produced in the area. And then "Provided further that no preference shall be given by any regulation of commerce or revenue by a unit to one unit over another." Now, kindly read paragraph 6 of the report, regarding adding a proviso. K.M. Panikkar: Rajaji (C. Rajagopalachari) has raised the question of the right of the units to raise taxes, and says this right should not be denied. I, however, think this is a dangerous power to be given to the units. This may result in the creation of so many competing units. We have allowed for two things. We have allowed the unit to tax its own industries. We also allow things brought in to be taxed, for the sake of parity. But our friends want to go a little further and say that the right to impose taxes, or transit duty or some other kind of duty must be given to the units. That I am afraid, will be a negation of the clause. There are certain rates and duties existing in Indian States which for budgetary and other reasons cannot now be extinguished immediately. It may be possible to extinguish them over a period of time, by agreement, but not immediately.

C. Rajagopalachari: If the States everywhere can impose taxes and duties for revenue, cannot the provinces also do so? Alladi Krishnaswami Ayyar: We do not give a carte blanche to the States. It has been pointed out that certain condition of things obtain at present in the States, and... K.M. Panikkar: Let me explain the position. The position with regard to the internal customs in the States is complicated. In a large number of States these customs or duties do not exist. For example for the whole of the Punjab States there is no right for internal customs. For Hyderabad they have the right to impose a tax up to 5% only, both on imports and exports. In Travancore and Cochin it is governed by what is called inter-portal convention. A large number of States have no right whatever even now for imposing customs duty, but a considerable number of them do enjoy this power and their budgetary position today is based on the customs duties they receive, both the maritime States and the internal States. Therefore

arrangements will have to be made with them by agreement and contract for setting this matter.

Alladi Krishnaswami Ayyar: The Union Powers Committee's attention was drawn to this matter and it was suggested by Sir V.T. Krishnamachari and Sir B.L. Mitter that some reference should be made to it in their report. We wanted to permit the States to enjoy the indulgence they have been enjoying. But we should guard against converting the country into competing units; that will be against the federation idea.

Chairman: What shall we do about the note? A proviso will have to be added to meet the difficulty pointed out in para 6 of the report. Shall we leave it as it is or shall we draft it?

C. Rajagopalachari: I would request members who have given thought to this subject to please inform me how the units will raise their revenue. As it is, the Union does not contemplate the distribution of subsidies to the provinces. The provinces or groups differ among themselves, some are rich and some are poor. Some are capable of managing with their existing resources; but others may have to increase their revenue for managing their affairs. If you impose so many limitations on them, how can they do that? It is all very well to say free trade is necessary; but how are the provinces to live? Alladi Krishnaswami Ayyar: So far as the provincial legislatures are concerned, there is provision in Sec. 297 of the present Government of India Act itself: (Reads)

"No Provincial Legislature or Government shall by virtue of entry *** have power to pass any law or take any executive action ***description..."

C. Rajagopalachari: But at present we have the receipts from customs and other receipts.
Alladi Krishnaswami Ayyar: The other day the Madras Premier said he could stop the import of textiles from Bombay and other places outside Madras: but it was pointed out to him that until the constitution is altered he cannot do so. This theory of self-sufficiency of different units is dangerous in our country, because we have to depend upon one another. Govind Ballabh Pant: There is unanimity about the body of this clause and it is clear that there should not be any discrimination against one unit by another unit. Otherwise we will be going against the very sense of a Union or a Federal Constitution. If the units are to be discriminated against, we will come to blows more often than otherwise. Therefore this should be avoided. The only thing to be considered is how to give effect to the suggestion made in para 6 of the President's letter which we have received through the chairman. Should we append a note to the effect that the Constituent Assembly may consider how best to give effect to this clause in relation to the States or shall we put up a draft. If we are not going to put up a draft, then the matter is simple enough."

49. The Advisory Committee accepted the recommendation of the Sub-Committee in

relation to Clause 14 with one change that the sub-clause providing for central regulation of trade by or with non-citizens was dropped as being vague and unnecessary. The Advisory Committee in its report submitted on 23rd April, 1947 incorporated the above provision as Clause 10. Certain amendments to the said clause were suggested and adopted by the Constituent Assembly.

50. In the first Draft Constitution of October, 1947, Clause 17 underwent further amendments and eventually appeared in the Draft Constitution of 1948 as Clause 16 incorporated in the Fundamental Rights Chapter in the following words:

> "16. Subject to the provisions of Article 244 of this Constitution and of any law made by Parliament, trade, commerce and intercourse throughout the territory of India shall be free."

51. It is noteworthy to mention here that Inter-State trade and commerce was dealt with in Articles 243, 244 and 245 in the Draft Constitution of 1948 which Articles were in the following terms:

> "243. No preference shall be given to one State over another nor shall any discrimination be made between one State and another by any law or regulation relating to trade or commerce, whether carried by land, water or air.
>
> 244. Notwithstanding anything contained in article 16 or in the last preceding article of this Constitution, it shall be lawful for any State - (a) to impose on good imported from other States any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and
>
> (b) to impose by land such reasonable Restrictions on the freedom of trade, Commerce or intercourse with that State as may be required in the public interests:
> Provided that during a period of five years from the commencement of this Constitution the provisions of clause (b) of this article shall not apply to trade or commerce in any of the commodities mentioned in clause (a) of Article 306 of this Constitution.
> 245. Parliament shall by law appoint such authority as it considers appropriate for the carrying out of the provisions of Articles 243 and 244 of this Constitution and confer on the authority so appointed such powers and such duties as it thinks necessary."

52. The Ministry of Industry and Supply expressed some reservation regarding clause (b) of Article 244 and demanded abolition of the said clause altogether. The Ministry appears to have argued that it was not possible to foresee the circumstances in which the freedom of trade, commerce or intercourse with a State will need to be interfered with by that State in the public interest, unless it be on the basis of discrimination between the residents of one State to another, and this would be wholly contrary to the spirit of the Constitution. [See: B. Shiva Rao; the Framing of India's Constitution,

53. The note in support of the proposed clause (b) to Article 244, however, clearly suggests that restrictions referred to in clause (b) were meant to be restrictions other than by way of taxation. The explanatory note which was appended by Sir B.N. Rau was in the following words:

> "Note: During a period of depression owing to destruction by flood or otherwise of crops in any particular State, it may be necessary for the State to impose restrictions on the export of any crop from such State in the public interests. Similarly on the outbreak of any epidemic disease, like plague, in a State it may be necessary for a neighbouring State to impose restrictions on the freedom of intercourse between the inhabitants of that State with the inhabitants of such neighbouring State. Clause (b) of Article 244 is intended to give power to the State to impose such restrictions."

54. On 8th of September, 1949, Dr. B.R. Ambedkar moved an amendment seeking to delete Articles 243, 244 and 245 and the same was adopted. Simultaneously, a new Part XA was introduced containing draft Article 274-A to E. Dr. Ambedkar informed the House that the Articles that were otherwise scattered were now brought together so as to ensure that members could get a holistic idea regarding trade and commerce. Article 274-A was a repetition of Article 16 and laid down the general principle. Article 274-B empowered Parliament to impose restrictions in public interest. Article 274-C prohibited Parliament and the State legislatures from making any law giving any preference to one State over another, or making any discrimination between one State and another, except when Parliament found it necessary to do so to deal with a situation arising from scarcity of goods; Article 274-D vested with the State legislatures the power to impose non-discriminatory tax qua external goods and to impose reasonable restrictions in public interest and Article 274-E provided for an Inter-State Commission.

55. The Constituent Assembly Debates suggests that the introduction of Articles 274A to 274E was severely criticized by several members of the Assembly including Thakur Das Bhargava and Dr. P.S. Deshmukh who moved several amendments to these clauses but the same were rejected and Articles 274-A to 274-E including Articles 274 DD and 274 DDD were adopted without any modification. These Articles are now renumbered and appear as Articles 301 to 307 of the Constitution of India.

56. It is in the above backdrop that question No.1shall have to be answered which turns on a true and correct interpretation of Article 301 of the Constitution. We must at the threshold say that while attempting to answer the question we are not on virgin ground, for this Court has in Atiabari Tea Company case (supra) examined the matter at great length. The decision of this Court in Automobile case (supra) has modified the view in Atiabari, by bringing in the concept of compensatory taxes which this Court held to be outside Part XIII of the Constitution.

57. While J.C. Shah, J. took the view that all taxes regardless whether they are discriminatory or otherwise would constitute an impediment on free trade and

commerce guaranteed under Article 301 of the Constitution of India, Sinha, CJ., held that taxes per se were totally outside the purview of Article 301 and could never constitute a restriction except where the same operated as a fiscal barrier that prevented free trade, commerce and intercourse. The view taken by Justice Shah, J. was not supported by any one of the counsel appearing for the parties for it was candidly accepted that the same was an extreme view that was legally unsupportable. What was all the same argued on behalf of the dealers/assesses was that the majority view that propounded the test of "direct and immediate" effect on free trade, commerce and intercourse was the correct view. Reliance, in particular, was placed by learned counsel for the dealers/assessees upon the following passages appearing in the majority judgment authored by Gajendragadkar, J. to contend that the same propounded the correct legal position:

> "50. Let us now revert to Article 301 and ascertain the width and amplitude of its scope. On a careful examination of the relevant provisions of Part XIII as a whole as well as the principle of economic unity which it is intended to safeguard by making the said provisions, the conclusion appears to us to be inevitable that the content of freedom provided for by Article 301 was larger than the freedom contemplated by Section 297 of the Constitution Act of 1935, and whatever else it may or may not include, it certainly includes movement of trade which is of the very essence of all trade and is its integral part. If the transport or the movement of goods is taxed solely on the basis that the goods are thus carried or transported that, in our opinion, directly affects the freedom of trade as contemplated by Article 301. If the movement, transport or the carrying of goods is allowed to be impeded, obstructed or hampered by taxation without satisfying the requirements of Part XIII the freedom of trade on which so much emphasis is laid by Article 301 would turn to be illusory. When Article 301 provides that trade shall be free throughout the territory of India primarily it is the movement part of the trade that it has in mind and the movement or the transport part of trade must be free subject of course to the limitations and exceptions provided by the other Articles of Part XIII. That we think is the result of Article 301 read with the other Articles in Part XIII.
>
> 51. Thus the intrinsic evidence furnished by some of the Articles of Part XIII shows that taxing laws are not excluded from the operation of Article 301; which means that tax laws can and do amount to restrictions freedom from which is guaranteed to trade under the said Part. Does that mean that all tax laws attract the provisions of Part XIII whether their impact on trade or its movement is direct and immediate or indirect and remote? It is precisely because the words used in Article 301 are very wide, and in a sense vague and indefinite that the problem of construing them and determining their exact width and scope becomes complex and difficult. However, in interpreting the provisions of the Constitution we must always bear in mind that the relevant provision "has to be read not in vacuo but as occurring in a single complex instrument in which one part may throw light on another". (Vide: James v. Commonwealth of Australia - 1936 A.C. 578 at pg. 613). In construing Article 301 we must, therefore, have regard to the general scheme of our Constitution as well as the particular provisions in regard to taxing

laws. The construction of Article 301 should not be determined on a purely academic or doctrinnaire considerations; in construing the said Article we must adopt a realistic approach and bear in mind the essential features of the separation of powers on which our Constitution rests. It is a federal constitution which we are interpreting, and so the impact of Article 301 must be judged accordingly. Besides, it is not irrelevant to remember in this connection that the Article we are construing imposes a constitutional limitation on the power of the Parliament and State Legislatures to levy taxes, and generally, but for such limitation, the power of taxation would be presumed to be for public good and would not be subject to judicial review or scrutiny. Thus considered we think it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Article 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Article 301. The argument that all taxes should be governed by Article 301 whether or not their impact on trade is immediate or mediate, direct or remote, adopts, in our opinion, an extreme approach which cannot be upheld. If the said argument is accepted it would mean, for instance, that even a legislative enactment prescribing the minimum wages to industrial employees may fall under Part XIII because in an economic sense an additional wage bill may indirectly affect trade or commerce. We are, therefore, satisfied that in determining the limits of the width and amplitude of the freedom guaranteed by Article 301 a rational and workable test to apply would be: Does the impugned restriction operate directly or immediately on trade or its movement? It is in the light of this test that we propose to examine the validity of the Act under scrutiny in the present proceedings."

58. On behalf of the respondent-States it was per contra argued that the power to levy taxes is a sovereign power that remains totally unaffected by Article 301 of the Constitution of India. Free trade, commerce and intercourse was not, according to the learned counsel, to be understood as free from any restrictions, leave alone free from taxes which the State legislatures were otherwise competent to levy. Enunciation of law by Sinha, CJ. was according to the learned Attorney General for India and learned Counsel appearing for the States, the correct view which ought to be accepted in preference to the other two contrary views propounded in the judgment. Reliance, in particular, was placed by Mr. Rohatgi and learned Counsel for the respondent-States upon the following passages appearing in Sinha, CJ.'s judgment:

> “14. Viewed in this all comprehensive sense taxation on trade, commerce and intercourse would have many ramifications and would cover almost the entire field of public taxation, both in the Union and in the State Lists. It is almost impossible to think that the makers of the Constitution intended to make trade, commerce and intercourse free from taxation in that comprehensive sense. If that were so, all laws of taxation relating to sale and purchase of goods on carriage of goods and commodities, men and animals, from one place to another, both inter-State and intra-State, would come within the purview of Article 301 and the proviso to Article 304 (b) would make it necessary that all Bills or Amendments of

pre-existing laws shall have to go through the gamut prescribed by that proviso. That will be putting too great an impediment to the power of taxation vested in the States and reduce the States' limited sovereignty under the Constitution to a mere fiction. That extreme position has, therefore, to be rejected as unsound.

15. In this connection, it is also pertinent to bear in mind that all taxation is not necessarily an impediment or a restraint in the matter of trade, commerce and intercourse. Instead of being such impediments or restraints, they may, on the other hand, provide the wherewithals to improve different kinds of means of transport, for example, in cane growing areas, unless there are good roads, facility for transport of sugarcane from sugarcane fields to sugar mills may be wholly lacking or insufficient. In order to make new roads as also to improve old ones, cess on the grower of cane or others interested in the transport of this commodity has to be imposed, and has been known in some parts of India to have been imposed at a certain rate per md. or ton of sugarcane transported to sugar factories. Such an imposition is a tax on transport of sugarcane from one place to another, either intra-State or inter-State. It is the tax thus realised that makes it feasible for opening new means of communication or for improving old ones. It cannot, therefore, be said that taxation in every case must mean an impediment or restraint against free flow of trade and commerce. Similarly, for the facility of passengers and goods by motor transport or by railway, a surcharge on usual fares or freights is levied, or may be levied in future. But for such a surcharge, improvement in the means of communication may not be available at all. Hence, in my opinion, it is not correct to characterise a tax on movement of goods or passengers as necessarily connoting an impediment, or a restraint, in the matter of trade and commerce. That is another good reason in support of the conclusion that taxation is not ordinarily included within the terms of Article 301 of the Constitution.

16. In my opinion, another very cogent reason for holding that taxation simpliciter is not within the terms of Article 301 of the Constitution is that the very connotation of taxation is the power of the State to raise money for public purposes by compelling the payment by persons, both natural and juristic, of monies earned or possessed by them, by virtue of the facilities and protection afforded by the State. Such burdens or imposts, either direct or indirect, are in the ultimate analysis meant as a contribution by the citizens or persons residing in the State or dealing with the citizens of the State, for the support of the Government, with particular reference to their respective abilities to make such contributions. Thus public purpose is implicit in every taxation, as such. Therefore, when Part XIII of the Constitution speaks of imposition of reasonable restrictions in public interest, it could not have intended to include taxation within the generic term "reasonable restrictions". This Court has laid it down in the case of Ramjilal v. Income Tax Officer, Mohindargarh(1951 SCR 127 at page 136) (AIR 1951 SC 97 at page 100), that imposition and collection of taxes by authority of law envisaged by Article 265 is outside the scope of the expression "deprivation of property" in Article 31(1) of the Constitution. Reasonable restrictions as used in Part III or Part XIII of the Constitution would in most cases

be less than total deprivation of property rights. Hence, Part XII dealing with finance etc. as already indicated, has been treated as a Part dealing with the sovereign power of the State to impose taxes, which must always mean imposing burdens on citizens and others, in public interest. If a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution-makers to abolish by Part XIII. The objections against the contention that taxation was included within the prohibition contained in Part XIII may thus be summarised: (1) Taxation, as such, always implies that it is in public interest. Hence, it would be outside particular restrictions, which may be characterised by the courts as reasonable and in public interest. (2) The power is vested in a sovereign State to carry on Government. Our Constitution has laid the foundations of a welfare State, which means very much expanding the scope of the activities of Government and administration, thus making it necessary for the State to impose taxes on a much larger scale and in much wider fields. The legislative entries in the three Lists referred to above empowering the Union Government and the State Governments to impose certain taxations with reference to movement of goods and passengers would be rendered ineffective, if not otiose, if it were held that taxation simpliciter is within the terms of Article 301. (3) If the argument on behalf of the appellants were accepted, many taxes, for example, sales tax by the Union and by the States, would have to go through the gamut prescribed in Articles 303 and 304, thus very much detracting from the limited sovereignty of the States, as envisaged by the Constitution. (4) Laws relating to taxation, which is essentially a legislative function of the State, will become justiciable and every time a taxation law is challenged as unconstitutional, the State will have to satisfy the courts a course which will seriously affect the division of powers on which modern constitutions, including ours, are based. (5) Taxation on movement of goods and passengers is not necessarily an impediment.

17. That conclusion leads to a discussion of the other extreme position that taxation is wholly out of the purview of Article 301. That extreme position is equally untenable in view of the fact that Article 304 contains, and Article 306, before it was repealed in 1956, contained, reference to taxation for certain purposes mentioned in those Articles. But Article 306, which now stands repealed, contained references to tax or duty on the import of goods into one State from another or on the exports of goods from one State to another. Such imposts were really in the nature of impediments to the free flow of goods and commodities on account of customs barriers, which it was the intention of Article 301 to abolish. Similarly, Article 304 while recognising the power of a State Legislature to tax goods imported inter-State, insists that a similar tax is imposed on goods manufactured or produced within the State. The Article thus brings out the clear distinction between taxation as such for the purpose of revenue and taxation for purposes of making discrimination or giving preference, both of which

are treated by the Constitution as impediments to free trade and commerce. In other words, so long as the impost was not in the nature of an impediment to the free flow of goods and commodities between one State and another, including in this expression Union territories also, its legality was not subject to an attack based on the provisions of Part XIII. But that does not mean that State Legislatures derive their power of taxation by virtue of what is contained in Article 304. Article 304 only left intact such power of taxation, but contained the inhibition that such taxes shall not be permitted to have the effect of impeding the free flow of goods and commodities."
Sinha, CJ. concluded as follows:

"18 Thus, on a fair construction of the provisions of Part XIII, the following propositions emerge: (1) trade, commerce, and intercourse throughout the territory of India are not absolutely free, but are subject to certain powers of legislation by Parliament or the Legislature of a State; (2) the freedom declared by Article 301 does not mean freedom from taxation simpliciter, but does mean freedom from taxation which has the effect of directly impeding the free flow of trade, commerce and intercourse; (3) the freedom envisaged in Article 301 is subject to non-discriminatory restrictions imposed by Parliament in public interest (Article 302); (4) even discriminatory or preferential legislation may be made by Parliament for the purpose of dealing with an emergency like a scarcity of goods in any part of India [Article 303(2)]; (5) reasonable restrictions may be imposed by the Legislature of a State in the public interest [Article 304(b)]; (6) non-discriminatory taxes may be imposed by the Legislature of a State on goods imported from another State or other States, if similar taxes are imposed on goods produced or manufactured in that State [Article 304(a)]; and lastly (7) restrictions imposed by existing laws have been continued, except insofar as the President may by order otherwise direct (Article 305)."

59. Before we examine the rival submissions, we must also refer to the decision of this Court in Automobile case (supra) which added a new dimension to the legal exposition in Atiabari case (supra) by declaring that taxes that were compensatory in nature fell outside Part XIII and could never be treated as restrictions offensive to Article 301 of the Constitution. S.K. Das, J. speaking for the majority explained the concept of compensatory taxes falling outside Part XIII in the following words:

"10... As the language employed in Article 301 runs unqualified the Court, bearing in mind the fact that that provision has to be applied in the working of an orderly society, has necessarily to add certain qualifications subject to which alone that freedom may be exercised. This point has been very lucidly discussed in the dissenting opinion which Fullagar, J. wrote in McCarter v. Brodie (1950) 80 CLR 432 an opinion which was substantially approved by the Privy Council in Hughes and Vale Proprietary Ld. v. State of New South Wales 1955 AC 241. The learned Judge gave several examples to show the distinction between what was merely permitted regulation and what was true interference with freedom of trade and commerce. He pointed out that in the matter of motor vehicles most countries have legislation which requires the motor vehicle to be registered and a fee to be

paid on registration. Every motor vehicle must carry lamps of a specified kind in front and at the rear and in the hours of darkness these lamps must be alight if the vehicle is being driven on the road. Every motor vehicle must carry a warning device, such as a horn; it must not be driven at a speed or in a manner which is dangerous to the public. In certain localities a motor vehicle must not be driven at more than a certain speed. The weight of the load which may be carried on a motor vehicle on a public highway is limited. Such examples may be multiplied indefinitely. Nobody doubts that the application of rules like the above does not really affect the freedom of trade and commerce; on the contrary they facilitate the free flow of trade and commerce. The reason is that these rules cannot fairly be said to impose a burden on a trader or deter him from trading: it would be absurd, for example, to suggest that freedom of trade is impaired or hindered by laws which require a motor vehicle to keep to the left of the road and not drive in a manner dangerous to the public. If the word "free" in Article 301 means "freedom to do whatever one wants to do", then chaos may be the result; for example, one owner of a motor vehicle may wish to drive on the left of the road while another may wish to drive on the right of the road. If they come from opposite directions, there will be an inevitable clash. Another class of examples relates to making a charge for the use of trading facilities, such as, roads, bridges, aerodromes etc. The collection of a toll or a tax for the use of a road or for the use of a bridge or for the use of an aerodrome is no barrier or burden or deterrent to traders who, in their absence, may have to take a longer or less convenient or more expensive route. Such compensatory taxes are no hindrance to anybody's freedom so long as they remain reasonable; but they could of course be converted into a hindrance to the freedom of trade. If the authorities concerned really wanted to hamper anybody's trade, they could easily raise the amount of tax or toll to an amount which would be prohibitive or deterrent or create other impediments which instead of facilitating trade and commerce would hamper them. It is here that the contrast, between "freedom" (Articles 301) and "restrictions" (Articles 302 and 304) clearly appears: that which in reality facilitates trade and commerce is not a restriction, and that which in reality hampers or burdens trade and commerce is a restriction. It is the reality or substance of the matter that has to be determined. It is not possible a priori to draw a dividing line between that which would really be a charge for a facility provided and that which would really be a deterrent to a trade; but the distinction, if it has to be drawn, is real and clear. For the tax to become a prohibited tax it has to be a direct tax the effect of which is to hinder the movement part of trade. So long as a tax remains compensatory or regulatory it cannot operate as a hindrance.

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14. After carefully considering the arguments advanced before us we have come to the conclusion that the narrow interpretation canvassed for on behalf of the majority of the States cannot be accepted, namely, that the relevant articles in Part XIII apply only to legislation in respect of the entries relating to trade and commerce in any of the lists of the Seventh Schedule. But we must advert here to

one exception which we have already indicated in an earlier part of this judgment. Such regulatory measures as do not impede the freedom of trade, commerce and intercourse and compensatory taxes for the use of trading facilities are not hit by the freedom declared by Article 301. They are excluded from the purview of the provisions of Part XIII of the Constitution for the simple reason that they do not hamper trade, commerce and intercourse but rather facilitate them.

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17. We have, therefore, come to the conclusion that neither the widest interpretation nor the narrow interpretations canvassed before us are acceptable. The interpretation which was accepted by the majority in the Atiabari Tea Co. case is correct, but subject to this clarification. Regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Article 301 and such measures need not comply with the requirements of the proviso to Article 304(b) of the Constitution."

60. Hidayatullah, J. in his dissenting judgment, however, took the view that even when a tax may be compensatory in character it would be a valid levy only if it goes through the process of presidential assent in terms of Article 304(b) of the Constitution of India and the proviso thereto. The following passage in this regard is relevant:

"125. That a tax is a restriction when it is placed upon a trade directly and immediately may be admitted. But there is a difference between a tax which burdens a trader in this manner and a tax, which being general, is paid by tradesmen in common with others. The first is a levy from the trade by reason of its being trade, the other is levied from all, and tradesmen pay it because everyone has to pay it. There is a vital difference between the two, viewed from the angle of freedom of trade and commerce. The first is an impost on trade as such, and may be said to restrict it; the second may burden the trader, but it is not a "restriction" of the trade. To refuse to draw such a distinction would mean that there is no taxing entry in Lists I and II which is not subject to Articles 301 and 304, however general the tax and however non-discriminatory its imposition. To bring all the taxes within the reach of Article 301 and thus to bring them also within the reach of Article 304 is to overlook the concept of a Federation, which allows freedom of action to the States, subject, however, to the needs of the unity of India. Just as unity cannot be allowed to be frittered away by insular action the existence of separate States is not to be sacrificed by a fusion beyond what the Constitution envisages. No doubt. Part XIII ensures economic unity to India and combines the federating States into the larger State called India. The Constitution also permits independent powers of taxation. What the Constitution does not permit is that trade, commerce and intercourse should be rendered "unfree". Trade and commerce remain free even when general taxes are paid by tradesmen in common with non-tradesmen. The question whether a tax offends Part XIII can only arise when it seeks to tax trade, commerce and intercourse.

Support for the contrary proposition is not to be found in 1936 AC 578 James v. Commonwealth. The Privy Council in James v. Commonwealth did not lay down:

"Every step in the series of operations which constitutes particular transaction is an act of trade, and control under the State law of any of these steps must be an interference with ifs freedom as trade" (p.629) This passage represents the view held in McArthur's case 1920 (28) CLR 530. That case was disapproved at p. 631. We have already dealt with this view at some length.

126. Thus, taxation laws and taxes must be divided into two kinds. Taxes which are general and for revenue purposes which fall on those engaged in trade, commerce and intercourse in the same way as they fall on others not so engaged cannot normally be within the reach of Part XIII. A motor transport owner cannot claim that he will not pay property tax in respect of his garage buildings or electricity tax for the electricity he consumes in lighting them, or income tax on his profits. Part XIII has nothing to do with such taxes even though they fall upon tradesmen.

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132. In our judgment, the first test to apply is what is the object and scope of the legislation? A regulation of trade and commerce may achieve some public purpose which affects trade and commerce incidentally but without impairing the freedom. Sometimes, however, the regulation itself may amount to a restriction, and if such a stage is reached, then under our Constitution the restriction must be reasonably in the public interest, and the President's prior sanction must be obtained, if the law imposing such restriction is made by the State Legislature, If, however, it does not reach the stage of restriction of trade and remains only a regulation incidentally touching trade and commerce, the regulation is outside the operation of Articles 301 and 304. It is on this ground that laws prescribing the rule of the road and like provisions already referred to as well as a regulation that the height to which trucks may be loaded must be such as not to endanger the overhead bridges or wires, do not have to go before the President, since they do not affect the freedom guaranteed. The object of such laws cannot be regarded as a restriction of trade and commerce. Freedom in Article 301 does not mean anarchy. Similarly, a demand for a tax from traders in common with others is not a restriction of their right to carry on trade and commerce. A system of licensing of motor vehicles is a regulation, but does not impair the freedom of trade and commerce unless the licensing is made to depend upon arbitrary discretion of the licensing authority. Similarly, a fee for administrative purposes may also be viewed as a part of regulation. Such licensing and fees fall outside Article 301, because they cannot be viewed as restrictions, and therefore do not need to be processed under Article 304. Such regulations are designed to give equal opportunity to everyone, subject to a certain standard. The object being a public object, such regulations cannot be questioned unless they amount to restrictions. A tax, however, which is made the condition precedent of the right to enter upon and carry on business at all is a very different matter. It is a restriction on the right

to carry on trade and commerce, and the restriction is released on the payment of the tax, which is the price of such release. It is from this point of view that the impugned provisions in this case must be examined."

61. Subbarao J. as His Lordship then was, agreed with the majority view but added the following passage to the same:

"37. The next question is, what is the content of the concept of freedom? The word "freedom" is not capable of precise definition, but it can be stated what would infringe or detract from the said freedom. Before a particular law can be said to infringe the said freedom, it must be ascertained whether the impugned provision operates as a restriction impeding the free movement of trade or only as a regulation facilitating the same. Restrictions obstruct the freedom, whereas regulations promote it. Police regulations, though they may superficially appear to restrict the freedom of movement, in fact provide the necessary conditions for the free movement. Regulations such as provision for lighting, speed, good condition of vehicles, timings, rule of the road and similar others, really facilitate the freedom of movement rather than retard it. So too, licensing system with compensatory fees would not be restrictions but regulatory provisions; for without it, the necessary lines of communication, such as roads, water-ways and air-ways, cannot effectively be maintained and the freedom declared may in practice turn out to be an empty one. So too, regulations providing for necessary services to enable the free movement of traffic, whether charged or not, cannot also be described as restrictions impeding the freedom. To say all these is not to say that every provision couched in the form of regulation but in effect and substance a restriction can pass off as a permissible regulation. It is for the Court in a given case to decide whether a provision purporting to regulate trade is in fact a restriction on freedom. If it be a colourable exercise of power and the regulatory provision in fact is a restriction, unless the said provision is one of the permissible restrictions under the succeeding articles, it would be struck down. This view is consistent with the principles laid down by the Australian High Court and the Privy Council in the context of interprelation of the words "absolutely free" in Section 92 of the Commonwealth of Australia Constitution Act, which is more emphatic than the word "free" in Article 301 of our Constitution.

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39. But the more difficult question is, what does the word "restrictions" mean in Article 302? The dictionary meaning of the word "restrict" is "to confine, bound, limit". Therefore, any limitation placed upon the freedom is a restriction on that freedom. But the limitation must be real, direct and immediate, but not fanciful, indirect or remote. In this context, the principles evolved by American and Australian decisions in their attempt to reconcile the commerce power and the State police power or the freedom of commerce and the Commonwealth power to make laws affecting that freedom can usefully be invoked with suitable modifications and adjustments. Of all the doctrines evolved, in my view, the doctrine of "direct and immediate effect" on the freedom would be a reasonable

solvent to the difficult situation that might arise under our Constitution. If a law, whatever may have been its source, directly and immediately affects the free movement of trade, it would be restriction on the said freedom. But a law which may have only indirect and remote repercussions on the said freedom cannot be considered to be a restriction on it. Taking the illustration from taxation law, a law may impose a tax on the movement of goods or persons by a motor-vehicle; it directly operates as a restriction on the free movement of trade, except when it is compensatory or regulatory. On the other hand, a law may tax a vehicle as property, or the garage wherein the vehicle used for conveyance is kept. The said law may have indirect repercussion on the movement, but the said law is not one directly imposing restrictions on the free movement. In this context, two difficulties may have to be faced: firstly, though a law purporting to impose a tax on a property or a motor-vehicle, as the case may be, may in fact and in reality impose a tax on the movement itself; secondly, a law may not be on the movement of trade, but on the property itself, but the burden may be so high that it may indirectly affect the free flow of trade. In the former case, the court may have to scrutinize the provisions of a particular statute to ascertain whether the tax is on the movement. If the provisions disclose a tax on the movement, it will be a restriction within the meaning of Article 302. In the latter case, if the provisions show that the tax is on property, the reasonableness of the tax may have to be tested against the provisions of Article 19 of the Constitution. The question whether a law imposes a restriction or not depends on the question whether the said law imposes directly and immediately a limitation on the freedom of movement of trade. If it does, the extent of the impediment relates to the question of degree rather than to the nature of it. If it is a restriction, it must satisfy the conditions laid down in Article 302 of the Constitution.

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46. The foregoing discussion may be summarized in the following propositions: (1) Article 301 declares a right of free movement of trade without any obstructions by way of barriers, inter-State or intra-State, or other impediments operating as such barriers. (2) The said freedom is not impeded, but, on the other hand, promoted, by regulations creating conditions for the free movement of trade, such as, police regulations, provision for services, maintenance of roads, provision for aerodromes, wharfs etc., with or without compensation. (3) Parliament may by law impose restrictions on such freedom in the public interest; and the said law can be made by virtue of any entry with respect whereof Parliament has power to make a law. (4) The State also, in exercise of its legislative power, may impose similar restrictions, subject to the two conditions laid down in Article 304(b) and subject to the proviso mentioned therein. (5) Neither Parliament nor the State Legislature can make a law giving preference to one State over another or making discrimination between one State and another, by virtue of any entry in the Lists, infringing the said freedom. (6) This ban is lifted in the case of Parliament for the purpose of dealing with situations arising out of scarcity of goods in any part of the territory of India and also in the case of a State under Article 304(b), subject to the conditions mentioned therein. And (7) the State can

impose a non-discriminatory tax on goods imported from other States or the Union territory to which similar goods manufactured or produced in that State are subject."

62. The net effect of the decision in Automobile case (supra) is that taxes, if the same are compensatory in character, do not offend the guarantee of free trade, commerce and intercourse under Article 301 of the Constitution. The further question whether the compensatory character of a tax has to be determined by reference to the direct and substantial benefits/ facilities provided by the State to the tax payer was examined and answered in the affirmative in Jindal Stainless Steel case (supra), where this Court while overruling the decisions in Bhagatram and Bihar Chamber of Commerce cases (supra) declared that it is not just a remote benefit to the tax payer but only a direct and substantial benefit that would justify levy of compensatory taxes without offending Article 301 of the Constitution of India. Speaking for the Court, Kapadia, J. observed:

"49. The concept of compensatory taxes was propounded in Automobile Transport in which compensatory taxes were equated with regulatory taxes. In that case, a working test for deciding whether a tax is compensatory or not was laid down. In that judgment, it was observed that one has to enquire whether the trade as a class is having the use of certain facilities for the better conduct of the trade/business. This working test remains unaltered even today.

50. As stated above, in the post 1995 era, the said working test propounded in Automobile Transport stood disrupted when in Bhagatram case, a Bench of three Judges enunciated the test of "some connection" saying that even if there is some link between the tax and the facilities extended to the trade directly or indirectly, the levy cannot be impugned as invalid. In our view, this test of "some connection" enunciated in Bhagatram case is not only contrary to the working test propounded in Automobile Transport case but it obliterates the very basis of compensatory tax. We may reiterate that when a tax is imposed in the regulation or as a part of regulatory measure the controlling factor of the levy shifts from burden to reimbursement/recompense. The working test propounded by a Bench of seven Judges in Automobile Transport and the test of "some connection" enunciated by a Bench of three Judges in Bhagatram case cannot stand together. Therefore, in our view, the test of "some connection" as propounded in Bhagatram case is not applicable to the concept of compensatory tax and accordingly to that extent, the judgments of this Court in Bhagatram Rajeevkumar v. CST and State of Bihar v. Bihar Chamber of Commerce stand overruled.

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52. In our opinion, the doubt expressed by the referring Bench about the correctness of the decision in Bhagatram case followed by the judgment in Bihar Chamber of Commerce was well founded.

53. We reiterate that the doctrine of "direct and immediate effect" of the impugned law on trade and commerce under Article 301 as propounded in Atiabari Tea Co.

> Ltd. v. State of Assam and the working test enunciated in Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan for deciding whether a tax is compensatory or not vide para 19 of the Report (AIR), will continue to apply and the test of "some connection" indicated in para 8 (of SCC) of the judgment in Bhagatram Rajeevkumar v. CST and followed in State of Bihar v. Bihar Chamber of Commerce is, in our opinion, not good law. Accordingly, the constitutional validity of various local enactments which are the subject-matters of pending appeals, special leave petitions and writ petitions will now be listed for being disposed of in the light of this judgment."

63. The legal position that today holds the field in light of the above is that compensatory taxes would fall outside Part XIII of the Constitution only if tax payers receive benefits and facilities commensurate to the levy. Any and every benefit howsoever remote or distant, would not save the levy from an attack on the ground of violation of Article 301. Having said that we must mention to the credit of the learned counsel for the dealers/assessees that except a feeble attempt made by Mr.A.K. Ganguly, learned counsel appearing for Sony India Pvt. Ltd. and Mr. Bagaria, learned counsel appearing for Steel Authority of India Limited (SAIL) the rest of the counsel fairly accepted that there was no constitutional or juristic basis for the Compensatory Tax Theory propounded by the majority judgment in Automobile Transport case (supra). Mr. Salve, who led the team of lawyers appearing for the dealers/assessees also did not support the compensatory tax theory propounded in Automobile case (supra). Mr. Rohatgi, learned Attorney General for India and M/s. Rakesh and Dinesh Dwivedi who appeared for some of the States also argued that the Compensatory Tax Theory has no basis whatsoever and that the same ought to be abandoned not only because of lack of any juristic support but also because of the problems that beset the application of the said theory in practice. It may, in the light of the concessions made at the Bar, have become unnecessary for us to deal with this aspect at any length but since M/s. Ganguly and Bagaria have not fully subscribed to the views urged by their colleagues appearing for the dealers, we are left with no option but to squarely deal with the question whether the Compensatory Tax Theory is indeed sustainable. Three distinct aspects touching the question need be noticed straightaway. The first and the foremost of these aspects is that the concept of compensatory taxes is not recognised by the Constitution. A tax is a compulsory exaction of money for general public good and is defined as under by Thomas M Cooley in his book The Law of Taxation at page 61(Clark A. Nichols ed., 4th ed. 1924) as:

> "Taxes are the enforced proportional contributions from persons and property, levied by the state by virtue of its sovereignty for the support of government and for all public needs. This definition of taxes, often referred to as "Cooley's definition," has been quoted and endorsed, or approved, expressly or otherwise, by many different courts. While this definition of taxes characterizes them as 'contributions', other definitions refer to them as 'imposts', 'duty or impost', 'charges', 'burdens', or 'exactions', ; but these variations in phraseology are of no practical importance."
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The term is defined also in The Major Law Lexicon by P. Ramanatha Aiyar - Vol. 6 - 4th Edition - Page Nos.6678 and 6679 in the following words: The term "tax" and "taxes" have been defined as a rate or sum of money assessed on the person or property of a citizen by government for the use of the nation or state; burdens or charges imposed by the legislative power upon persons or property to raise money for public purposes, and the enforced proportional contribution of persons and property levied by authority of the state for the support of government and for all public needs.

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Taxes are public burdens, of which every individual may be compelled to bear his part, and that in proportion to the extent of protection he receives or the amount of property held by him, as the will of the Legislature may direct. The power of taxation is said to be an incident of sovereignty, and co-extensive with that of which it is incident."

Blackwell on Tax Titles as cited in 'Tata Iron & Steel Co. Ltd. v. State of Bihar, AIR 1991 Patna 75, 81 has the following to say about taxes: 'Taxes are defined to be burdens or charges imposed by the legislative power upon persons or property to raise money for public purposes.' Black's Law Dictionary, 7th Edn., P. 1469 defines tax as under:

"A monetary charge imposed by government on persons, entities or property to yield public revenue,"

If taxes are eventually meant to serve larger public good and for running the governmental machinery and providing to the people the facilities essential for civilized living, there is no question of a tax being non-compensatory in character in the broader sense.

64. Secondly, because the concept of compensatory tax obliterates the distinction between a tax and a fee. The essential difference between a tax and a fee is that while a tax has no element of quid pro quo, a fee without that element cannot be validly levied. The difference between a tax and the fee has been examined and elaborated in a long line of decisions of this Court. (See*: Commissioner, Hindu Religious Endowments, Madras v. Sri Lakshmindra Thirtha Swamiar of Sri Shirur Mutt(Supra), Mahant Sri Jagannath Ramanuj Das & Anr. v. State of Orissa & Anr*[28]*, The Hingir-Rampur Coal Co. Ltd. v. State of Orissa*[29]*, Corporation of Calcutta and anr. v. Liberty Cinema*[30]*, Kewal Krishna Puri and Anr. v. State of Punjab*[31]*, Krishi Upaj Mandi Samiti and Ors. v. Orient Paper and Industries Ltd*[32]*., State of Gujarat and Anr. v. Akhil Gujarat Pravasi V.S. Mahamendal*[33]*; State of West Bengal v. Kesoram Industries Ltd. & ors*[34]*.*

65. Thirdly, and lastly, the concept of Compensatory taxes being outside Part XIII, is difficult to apply in actual practice. Experience in the present batch of cases has amply demonstrated that difficulty. Most of the legislations enacted by the States in these

cases have described the entry tax levied under the same to be compensatory in character. This may have been done to take the levy outside the mischief of Article 301 of the Constitution. The question however is whether tax amount collected in terms of the said legislation is really used by the State for the purpose of providing or maintaining services and benefits to the tax payers and whether the Courts can follow the money trail to determine whether the State concerned has actually used the amount for the avowed purpose underlying the legislation. This process is fraught with serious difficulties, a fact that was not disputed by learned Counsel for the assessees/dealers. Actual application of the Compensatory Tax Theory, therefore, runs into difficulties to an extent that the theory at some stage breaks down. M/s. Salve, Rohatgi and Dwivedi were in that view perfectly justified in submitting that the Compensatory Tax Theory was legally unsupportable and deserved to be abandoned. We have no hesitation in agreeing with that submission, the arguments of M/s. Ganguly and Bagaria to the contrary notwithstanding.

66. With the Compensatory Tax Theory no longer found acceptable, we are left with only two competing view points, one expressed by Gajendragadkar, J. and the other by B.P. Sinha, CJ. Which one is the correct view is the critical question that falls for our determination having regard to the Constitutional scheme and the language employed in Articles 301 to 307 to which we must now turn for a closer look. Article 301 is as under:

> "301. Freedom of trade, commerce and intercourse.- Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free"
>
> A plain reading of the above would show that freedom of trade, commerce and intercourse is by no means absolute, the same being subject to the other provisions of Part XIII of the Constitution. Amongst those provisions are Articles 302, 303 and 304 which have a direct bearing on the nature and the extent of restrictions subject to which only is the right to freedom of trade, commerce and intercourse referred to in Article 301 exercisable. Article 302 reads thus:
>
> "302. Power of Parliament to impose restrictions on trade, commerce and intercourse.— Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part of the territory of India as may be required in the public interest."

67. The above leaves no manner of doubt that Parliament is empowered to impose such restrictions on the freedom of trade, commerce and intercourse between one State and another or within any part of the territory of India as may be required in public interest. Reading Articles 301 and 302 together, it is evident, that freedom of trade, commerce and intercourse is subject to restrictions which Parliament may by law impose in public interest.

The absolute character of the freedom of trade, commerce and intercourse is thus lost by reason of Article 302 itself empowering Parliament to impose such restrictions as it may consider necessary in public interest. Article 303, in turn, places restrictions on the

legislative powers of the Parliament and of the States, when it says :

> "303. Restrictions on the legislative powers of the Union and of the States with regard to trade and commerce.—(1) Notwithstanding anything in article
>
> 302, neither Parliament nor the Legislature of a State shall have power to make any law giving, or authorising the giving of, any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule. (2) Nothing in clause (1) shall prevent Parliament from making any law giving, or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India."

68. A careful reading of the above would show that notwithstanding the power vested in the Parliament under Article 302, it shall not make any law giving, or authorizing the giving of any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule. From Clause (2) of Article 303 (supra) it is manifest that the restriction on the power vested in Parliament in terms of Clause (1) of Article 303 shall not extend to Parliament making any law with a view to giving or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising out of scarcity. A conjoint reading of Clauses (1) and (2) of Article 303 would thus make it clear that while Parliament/ Legislature of a State shall have no power to make a law imposing restriction on trade, commerce and intercourse, by giving or authorizing the giving of any preference to one State over the other, such limitation on the legislative power of Parliament shall not extend to giving of any preference or making or authorizing any discrimination if it is declared by law that a situation has arisen out of scarcity of goods that makes it necessary to do so. In other words, while the Parliament may impose restrictions in public interest under Article 302, the restriction so imposed shall not be in the nature of giving preference or discrimination between one State or the other except when the law declares that scarcity of goods in any part of India necessitates such preference or discrimination.

69. That brings us to Article 304 of the Constitution which too like Articles 302 and 303 deals with restrictions on the freedom of trade, commerce and intercourse. It reads:

> "304. Restrictions on trade, commerce and intercourse among States.— Notwithstanding anything in Article 301 or Article 303, the Legislature of a State may by law— (a) impose on goods imported from other States or the Union territories any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and (b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may

be required in the public interest: Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President."

The Article starts with a "non-obstante" clause which has been the subject matter of forensic debates in several cases. We do not for the present propose to address the effect of the non-obstante clause at this stage or the interplay between the expression "subject to" appearing in Article 301 and the non obstante clause in Article 304. We shall turn to that aspect a little later. What we wish to examine is whether Article 304(a) treats taxes as a restriction so that any such levy may fall foul of Article 301. The answer to that question, we say without any hesitation is in the negative. Article 304(a) far from treating taxes as a restriction per se, specifically recognises the State legislature's power to impose the same on goods imported from other States or Union Territories. The expression "the legislature of a State may by law impose on goods imported from other States (or Union Territories) any tax" are much too clear and specific to be capable of any equivocation or confusion. It is true that the source of power available to the State legislature to levy a tax is found in Articles 245 and 246 of the Constitution but, the availability of such power for taxing goods imported from other States or Union Territories is clearly recognised by Article 304 (a). The expression 'may by law impose' is certainly not a restriction on the power to tax. That does not, however, mean that the power to tax goods imported from other States or Union Territories is unqualified or unrestricted. There are, in our opinion, two restrictions on that power. The words "to which similar goods manufactured or produced in that State are subject" impose the first restriction on the power of the State legislature to levy any such tax. These words would imply that a tax on import of goods from other States will be justified only if similar goods manufactured or produced in the State are also taxed. The second restriction comes from the expression "so, however, as not to discriminate between goods so imported and goods so manufactured or produced". The State legislature cannot in the matter of levying taxes discriminate between goods imported from other States and those manufactured or produced within the State levying such a tax. The net effect of Article 304 (a) therefore is that while levy of taxes on goods imported from others State and Union territories is clearly recognised as Constitutionally permissible, the exercise of such power is subject to the two restrictive conditions referred to above. That does not however detract from the proposition that levy of taxes on goods imported from other States is constitutionally permissible so long as the State legislatures abide by the limitations placed on the exercise of that power. To put it differently, levy of taxes on import of goods from other States is not by itself an impediment under the scheme of Part XIII or Article 301 appearing therein.

70. That brings us to the question whether Clauses (a) and (b) have to be read conjunctively. It was contended on behalf of the dealers/assessees that even when a tax in terms of Article 304 (a) is not forbidden being non-discriminatory, it may still constitute a restriction under Clause (b) thereof. The argument is that just because a tax passes muster under Clause (a) of Article 304 being non-discriminatory does not mean that the levy of such a tax is not a restriction on the freedom of trade, commerce and intercourse. It was contended that while a discriminatory tax must be treated as a restriction by itself the reasonableness of a non-discriminatory tax will have to be seen

by the President in terms of the Proviso to Clause (b). It was argued that Article 304(a) does not exhaust the universe in so far as levy of taxes is concerned for even when the law complies with the requirement of Clause (a), it may fail to pass the test of reasonableness and of public interest under Clause (b) in which event the President may decline the sanction for introduction of any Bill aimed at levying such a tax.

71. There is, in our opinion, no merit in any of the contentions noted above. Clauses (a) and (b) of Article 304 deal with two distinct subjects and must, therefore, be understood to be independent of each other. While Clause (a) deals entirely with imposition of taxes on goods imported from other States, Clause (b) deals with imposition of reasonable restriction in public interest. It is trite that levy of a tax in terms of Article 304(a) may or may not be accompanied by the imposition of any restriction whether reasonable or unreasonable. There is, in our opinion, no rationale in the contention that the legislature of a State cannot levy a tax without imposing one or more reasonable restrictions or that a law that is simply imposing restrictions in terms of Clause (b) to Article 304 must be accompanied by the levy of a tax on the import of goods. The use of the word 'and' between clauses (a) and (b) does not admit of an interpretation that may impose an obligation upon the legislature to necessarily impose a tax and a restriction together. The law may simply impose a tax without any restriction reasonable or otherwise or it may simply impose a reasonable restriction in public interest without imposing any tax whatsoever. It may also levy a tax and impose such reasonable restriction as may be considered necessary in public interest. All the three situations are fully covered and permissible under Article 304 in view of the phraseology used therein. The word 'and' can mean 'or' as well as 'and' depending upon the context in which the law enacted by the legislature uses the same. Suffice it to say that levy of taxes do not constitute a restriction under Part XIII except in cases where the same are discriminatory in nature. Once Article 304 (a) is understood in that fashion, Clause (b) dealing with reasonable restrictions must necessarily apply to restrictions other than those by way of taxes. It follows that for levy of taxes prior Presidential sanction in terms of the proviso under Article 304(b) will be wholly unnecessary. This view is reinforced on the plain language of proviso to Article 304(b), which is limited to law relating to reasonable restrictions referred to in clause (b).

72. The sum total of what we have said above regarding Articles 301, 302, 303 & 304 may be summarized as under:

1. Freedom of trade, commerce and intercourse in terms of Article 301 is not abso-lute but is subject to the Provisions of Part XIII.

2. Article 302 which appears in Part XIII empowers the Parliament to impose restrictions on trade, commerce and intercourse in public interest.

3. The restrictions which Parliament may impose in terms of Article 302 cannot however give any preference to one State over another by virtue of any entry relating to trade and commerce in any of the lists in the Seventh Schedule.

4. The restriction that the Parliament may impose in terms of Article 302 may

extend to giving of preference or permitting discrimination between one State over another only if Parliament by law declares that a situation arising out of scarcity of goods warrants such discrimination or preference.

5. Article 304(a) recognizes the availability of the power to impose taxes on goods imported from other States, the legislative power to do so being found in Articles 245 and 246 of the Constitution.

6. Such power to levy taxes is however subject to the condition that similar goods manufactured or produced in the State levying the tax are also subjected to tax and that there is no discrimination on that account between goods so imported and goods so manufactured or produced.

7. The limitation on the power to levy taxes is entirely covered by Clause (a) of Article 304 which exhausts the universe in so far as the State legislature's power to levy of taxes is concerned.

8. Resultantly a discriminatory tax on the import of goods from other States alone will work as an impediment on free trade, commerce and intercourse within the meaning of Article 301.

9. Reasonable restrictions in public interest referred to in Clause (b) of Article 304 do not comprehend levy of taxes as a restriction especially when taxes are presumed to be both reasonable and in public interest."

73. The inferences enumerated above are based on a textual interpretation of the provisions of Article 301 to Article 304. An interpretation which is both textual and contextual has always been found to be more acceptable. That is so because it is only when both the text and the context are kept in view that the statutory provisions can be best understood. An interpretation that makes the textual match the contextual meaning of the provision is preferred by Courts over one that prefers one at the cost of the other.

74. In *Reserve Bank of India v. Peerless General Finance and Investment Co. Ltd*[35]. this Court pithily summed up the law on the subject in the following words:

"33. Interpretation must depend on the text and the context. They are the basis of interpretation. One may well say if the text is the texture, context is what gives the colour. Neither can be ignored. Both are important. The interpretation is best which makes the textual interpretation match the contextual "

75. We may also refer to the following passage of Constitutional Law of India (4th Edition) by H.M. Seervai where the distinguished author has adverted to the golden rule of interpretation applicable to Constitutional provisions in the following words:

"2.12. The golden rule of interpretation is that words should be read in their ordinary, natural and grammatical meaning subject to the rider that in construing words in a Constitution conferring legislative power the most liberal construction

should be put upon the words so that they may have effect in their widest amplitude."

76. Let us then see whether the textual interpretation placed on Articles 301 to 304 matches the contextual. The contextual interpretation of Part XIII must, out of necessity, start with the historical perspective of that Part. We have with great advantage extracted in the earlier part of this Judgment the historical backdrop as set out in the decisions of this Court both in Atiabari and Automobile cases (supra). While it is unnecessary to recall the said passages over again, we need to remember that Part XIII had a historical precursor in the form of Section 297 of the Government of India Act, 1935 that governed what was then called the British India comprising the territory of India subject to British Rule. The rest of the territories were at that time Princely States who claimed sovereign rights within the limitations imposed by the paramount power. The power to levy taxes was one such power wielded by the Princely States which led to erection of customs barriers impeding the flow of trade, commerce and intercourse. Section 297 aimed at removing such trade barriers. It provided for a prohibition against enactment of any law or taking of any executive action by the provincial legislature that restricted the entry into or export from the province goods of any class or description.

77. More importantly, in terms of clause (b) of Section 297(1) of Government of India Act, 1935 no provincial legislature or Government could impose any tax, cess, toll or due which discriminated between goods manufactured or produced in the provinces and goods not so manufactured or produced or between goods manufactured or produced outside the province discriminated between goods manufactured or produced in one locality and similar goods manufactured or produced in another locality. With India attaining its freedom, Part XIII of the Constitution adopted by it, was aimed at bringing about economic unity. The object underlying Part XIII was to make movement and exchange of goods free throughout the territory of India. This was achieved by Article 301 to Article 304 adopting substantially the scheme underlying the 1935 Act. The only difference between the said provisions and Section 297 of the 1935 Act was that the principles enunciated in the latter were extended to the Union Government and the Union Parliament and to the territory which had after merger become a part of India. Notably, the essence of the freedom of trade commerce and intercourse as recognized in the 1935 Act and in the Constitution under Part XIII remained the same. It was for that reason that Justice Venkatarama Iyer had in M.P.V. Sunderaramier's case (Supra) observed and if we may say so rightly that the Constitution of India was not written on a tabula rasa. The common feature which the two provisions share is that the provincial legislature's power to impose taxes is recognized subject only to the limitation that there is no discrimination between goods manufactured or produced within the Province or State vis-a-vis those imported from outside. In Atiabari's case (supra), the majority speaking through Gajendragadkar, J. noticed the co-relation between Section 297 of 1935 Act, and Article 301 of the Constitution of India but concluded that Article 301 did not simply adopt Section 297 of the 1935 Act but widened and enriched the same in content. The Court did not, however, elaborate as to how much richer and wider did Article 301 make the freedom of trade, commerce and intercourse then what was envisaged under Section 297. The Court said :

"42 That is why we are inclined to hold that the broad and unambiguous words used in Article 301 are intended to emphasize that the freedom of trade, commerce and intercourse guaranteed was richer and wider in content than was the case under Section 297; how much wider and how much richer can be determined only on a fair and reasonable construction of Article 301 read along with the rest of the articles in Part XIII. In our opinion therefore, the argument that tax laws are outside Part XIII cannot be accepted."

(emphasis supplied)

78. We have with great respect to the distinguished Judges failed to persuade ourselves to subscribe to the above view. The argument that Article 301 had enriched and widened the content of trade, commerce and intercourse beyond what is evident from a comparison of the language between the two provisions namely (a) extending the prohibition against discrimination to the Union Government and the Parliament and (b) making the provision applicable to the territory of India as defined by the Constitution, has not impressed us. The textual interpretation placed by us upon Articles 301-304 instead gets considerable support from the contextual and the historical perspective of Part XIII.

79. We may now turn to yet another contextual feature that has a bearing on the true and correct interpretation of Part XIII namely the sovereign character of the power to tax available to the State legislature. It is now fairly well settled that the Constitutionally vested power to levy tax can be regulated or controlled only by specific Constitutional limitations, if any. We have in the earlier part of this judgment elaborated how the power to levy taxes is a sovereign power with several limitations specifically stipulated by the Constitution itself. We have also explained at some length how legislative competence of the State legislatures can be circumscribed only by express provisions of the Constitution and unless there is an express limitation on the plenary taxing power of the States, there is no other fetter on the exercise of that power.

80. Applying the above principle to the case at hand, we do not see any specific limitation on the State's power to levy taxes on the import of goods from other States except the one referred to in Article 304(a) of the Constitution. That limitation we have sufficiently explained is confined to levy of discriminatory taxes within the comprehension of Article 304(a). So long as taxes are non-discriminatory and, therefore, consistent with Article 304(a), there is no limitation leave alone any express limitation on the States' legislative power to levy any tax on the import of goods from another State. The power to levy a tax in terms of Articles 245 and 246 read with Entry 52 of list II not being in dispute in the cases at hand, the absence of any specific limitation forbidding the exercise of such power whether for the sake of free trade, commerce and intercourse or otherwise simply means that the State legislatures are free to levy taxes that are non-discriminatory in nature.

81. That brings us to the third contextual feature relevant to the interpretation of Part XIII. We have in the earlier part of this judgment referred to the decisions of this Court in Kuldip Nayyar's case and S.R. Bommai's case apart from the decisions of this Court in

Special Reference No. 1 of 1964 (supra) to hold that the Indian Constitution if not federal in the strict sense of the term is at least quasi federal in character. That proposition has not been disputed even by the counsel for the assesses/dealers, and must be held to be fairly well settled. Equally well settled is the proposition that India's federal structure is one of the basic features of the Constitution. Relying upon the settled legal position Mr. Mukul Rohtagi, Attorney General, followed by Mr. Rakesh Dwivedi, Mr. PP Rao, Mr. AK Sinha and Mr. Devdatt Kamath strenuously argued, and in our opinion rightly so that the provisions of our Constitution are aimed at vesting and maintaining with the States substantial and significant powers in the legislative and executive fields so that States enjoy their share of autonomy and sovereignty in their sphere of governance. This can in turn be done by interpreting the provisions of the Constitution including those found in Part XIII in a manner that preserves and promotes the federal set-up instead of diluting or undermining the same. In *ITC Limited v. Agricultural Produce Market Committee and Ors*[36]. this Court ruled that the Constitution of India must be interpreted in a manner that does not whittle down the powers of the State legislature. An interpretation that supports and promotes federalism while upholding the Central supremacy as contemplated by some of the Articles must be preferred. To the same effect is the nine judge Bench decision of this Court in S.R. Bommai's case (supra) where this Court cautioned against adoption of an interpretation that has the effect of whittling down the powers reserved to the States. This Court said:

> "276. The fact that under the scheme of our Constitution, greater power is conferred upon the Centre vis-a-vis the States does not mean that States are mere appendages of the Centre. Within the sphere allotted to them. States are supreme. The Centre cannot tamper with their powers. More particularly. the Courts should not adopt an approach. an interpretation. which has the effect of or tends to have the effect of whittling down the powers reserved to the States. It is a matter of common knowledge that over the last several decades, the trend the world over is towards strengthening of Central Governments be it the result of advances in technological/scientific fields or otherwise, and that even in USA the Centre has become far more powerful notwithstanding the obvious bias in that Constitution in favour of the States. All this must put the court on guard against any conscious whittling down of the powers of the States. Let it be said that the federalism in the Indian Constitution is not a matter of administrative convenience. but one of principle - the outcome of our own historical process and a recognition of the ground realities. This aspect has been dealt with elaborately by Shri M.C. Setalvad in his Tagore Law Lectures "Union and State relations under the Indian Constitution" (Eastern Law House. Calcutta. 1974). The nature of the Indian federation with reference to its historical background, the distribution of legislative powers, financial and administrative relations, powers of taxation, provisions relating to trade, commerce and industry, have all been dealt with analytically. It is not possible nor is it necessary for the present purposes to refer to them. It is enough to note that our Constitution has certainly a bias towards Centre vis-a-vis the States: Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan. It is equally necessary to emphasise that courts should be careful not to upset the delicately-crafted constitutional scheme by a process of interpretation."

(emphasis supplied)

82. Reference may also be made to Kesavananda Bharati's case (supra) where a Bench of thirteen Judges cautioned that the process of interpretation should not diminish or whittle down the provisions of the original contract upon which the federation was founded nor is it legitimate to impose by a process of judicial construction a new contract upon the federating states. To the same effect is the decision of this Court in *M/s. International Tourist Corporation & ors. v. State of Haryana and Ors*[37]. where this Court observed:

> "6A. There is a patent fallacy in the submission of Shri Sorabji. Before exclusive legislative competence can be claimed for Parliament by resort to the residuary power,
> the legislative incompetence of the State legislature must be clearly established. Entry 97 itself is specific that a matter can be brought under that entry only if it is not enumerated in List II or List III and in the case of a tax if it is not mentioned in either of those lists. In a Federal Constitution like ours where there is a division of legislative subjects but the residuary power is vested in Parliament, such residuary power cannot be so expansively interpreted, as to whittle down the power of the State legislature. That might affect and jeopardize the very federal principle. The federal nature of the Constitution demands that an interpretation which would allow the exercise of legislative power by Parliament pursuant to the residuary powers vested in it to trench upon State legislation and which would thereby destroy or belittle state autonomy must be rejected."

(emphasis supplied)

83. An approach which tends to dilute the federal character of our Constitutional scheme must, therefore, be avoided and one that supports and promotes the concept of federalism preferred by the courts while interpreting the provisions of the Constitution.

84. Dealing in particular with the scope and meaning of Article 304 (b) of the Constitution on a true and correct interpretation Seervai in his treatise Constitutional Law of India (supra) sounded a note of caution and observed that if Article 304(b) was interpreted in a manner that would include levy of taxes as a restriction within the meaning of that Article, it would totally dislocate the scheme under our Constitution. The celebrated author, in our opinion, was right in saying so for the taxing power of the Union and the States are mutually exclusive. While the Parliament cannot legislate on the subjects reserved for the States, the States cannot similarly trespass onto the taxing powers of the Union. If the Constitutional scheme does not allow the Parliament to usurp the taxing powers of the State Legislatures, such process of usurpation cannot also be permitted to take place in the garb of making Union executive's concurrence an essential pre-requisite for any taxing legislation. The following passage from Seervai's book (Vol. 3, Page 2607) is in this regard instructive:

> "23.43. Thirdly, the whole scheme of taxation in our Constitution would be

completely dislocated if Article 304(b) included a tax. The taxing powers of the Union and the States have been made mutually exclusive so that Parliament cannot deprive the States of their taxing powers as has happened in countries where the powers of taxation are concurrent. It would be surprising if the Union legislature, i.e. Parliament could not take away the taxing powers of the State legislatures and yet it would be open to the Union executive under Article 304(b) to deprive the State legislatures of their taxing powers."

85. To the same effect are the following observations made by Mathew's, J. in G.K. Krishnan's case (supra):

> "27 Article 304(a) prohibits only imposition of a discriminatory tax. It is not clear from the article that a tax simpliciter can be treated as a restriction on the freedom of internal trade. Article 304(a) is intended to prevent discrimination against imported goods by imposing on them tax at a higher rate than that borne by goods produced in the State. A discriminatory tax against outside goods is not a tax simpliciter but is a barrier to trade and commerce. Articled 304 itself makes a distinction between tax and restriction. That apart. taxing powers of the Union and States are separate and mutually exclusive. It is rather strange that power to tax given to states. say. for instance under entry 54 of List II to pass a law imposing tax on sale of goods should depend upon the goodwill of the Union executive."

86. Suffice it to say that the interpretation of any provision of the Constitution will be true and perfect only when the Court looks at the Constitution holistically and keeps in view all important and significant features of the Constitutional scheme constantly reminding itself of the need for a harmonious construction lest interpretation placed on a given provision has the effect of diluting or whittling down the effect or the importance of any other provision or feature of the Constitution. So interpreted Article 301 appearing in Part XIII does not, in our opinion, work as an impediment on the States' taxing powers except in situations where such taxes fall foul of Article 304(a) of the Constitution. The contextual approach thus fully matches the textual interpretation which we have placed on Part XIII.

87. On behalf of the dealers/assessees it was contended with considerable amount of tenacity that since Article 304 starts with a non-obstante clause the inference was that the framers of the Constitution treated taxes as impediments for free trade, commerce and intercourse. The argument was that unless Article 301 was understood to mean that taxes could also be restrictions on free trade and commerce, there was no need for the framers of the Constitution to start Article 304 with a non-obstante clause inasmuch as a non-obstante clause is meant to be only an exception to the generality of the provision. Similar contentions urged in the past have been noticed by this Court and by jurists alike while attempting interpretation of Part XIII. This is evident from the passages which have dealt with the anomaly arising out of the use of the expression 'subject to' in Article 301 and the non-obstante clause in Article 304 of the Constitution. This Court has often found the use of the non-obstante clause in Article 304 to be either confusing or an unnecessary surplusage. But the problem with the use of non-obstante

clauses in Part XIII has been the subject matter of criticism even in the Constituent Assembly as is evident from the following passages from the debates: Constitution Assembly Debates (Vol. IX Page 1131):

> "Dr. P S Deshmukh: If we analyse the new articles that have been proposed. it is very difficult to understand them and I think the comment is absolutely justified that this is going to be a lawyers' constitution. a "paradise for lawyers" where there will be so many innumerable loopholes that we will be wasting years and years before we could come to the final and correct interpretation of many clauses. If we read this article 274. you will find. Sir. that this is one of the most wonderful articles in the whole Constitution. This is not the only one; there are many others. If we count the use of the word 'notwithstanding' in this Constitution. I am certain that the number of times that word is used will far exceed the use of the word 'Parliament' or 'Constitution' in the whole Constitution. If you will permit me. Sir. I will describe the situation a little graphically. We first of all provide and say or declare that a certain person is a man. Then. we say. notwithstanding this declaration. you shall wear a sari and nothing but a sari. Shri T.T. Krishnamachari: There is no bar to that. Dr. P.S. Deshmukh : Then, notwithstanding the fact that you are considered a man, and notwithstanding the fact that you wear nothing else but saris, you will wear a Gandhi cap also. Then we have another 'notwithstanding'. Notwithstanding that you are a man, notwithstanding that you shall wear nothing but a sari, notwithstanding that you shall also wear a Gandhi cap, you will be at liberty to describe yourself as a woman. (Laughter) Something of that sort, as funny and as amusing, is really the situation so far as this article 274 is concerned. If you read through it, you will see that as soon as the first part is over, we start with "notwithstanding whatever is said in the first part, such and such a thing will happen". In the next clause, we say not only notwithstanding what is contained in the first clause, together with notwithstanding what is contained in the other clauses' and then add something more. I think there is a better method of drafting. Even if it is necessary to cope with complex situations and to provide something on the lines proposed, there should be a simpler and more direct way of drafting and making a provision which is not so ununderstandable that only supermen could read this constitution, even assuming that only supermen are to be born in India hereafter. If this Constitution is made for the average man, if it is going to affect the rights and privileges of the ordinary common man, it is necessary that the drafters of this constitution should be more clear and use phraseology which is more easily understandable and simpler.
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> xxx xxx xxx xxx
>
> I hope therefore that the whole chapter will be made simpler. Instead of tying the hands of both the States as well as of Parliament, it would be far better not to commit ourselves to any policy, but to leave the whole thing to Parliament. Otherwise, the situation which has arisen already in respect of article 16 may arise in respect of article 274 itself. It is, therefore, better to have simpler provisions and I have given them the simplest form. I hope that this will appeal to

the drafters of the Constitution and if they accept it, I can tell them that they will be out of much of the trouble. But if they insist upon the draft that they have produced, it will be very difficult for trade and commerce not only to prosper but even to exist."

88. In Automobile Transport case (supra), S K Das, J. speaking for the majority noticed the anomaly arising out of the use of the non-obstante clause in Article 304 and described the same to be "somewhat inappropriate". The majority judgment in Automobile Transport case (supra) in fact took the view that the mix up of exception upon exception in the series of Articles in Part XIII makes a purely textual interpretation difficult. The following passage is in this regard apposite:

> "10. Art. 304 again begins with a non obstinate clause mentioning both Art. 301 and Article 303, though Article 304 relates only to the Legislature of a State. Article 303 relates to both the State Legislature and Parliament and again the non obstante clause in Article 304 is somewhat inappropriate. The fact of the matter is that there is such a mix up of exception upon exception in the series of articles in Part XIII that a purely textual interpretation may not disclose the true intendment of the articles."

89. Subba Rao, J., as His Lordship then was, in a separate judgment delivered in Automobile Transport case (supra) also found the use of the non-obstante clause to be a "defect in phraseology". His Lordship held that the non-obstante clause has no relevance to Article 303 even when the Article is mentioned alongwith the non-obstante clause. The importance of the non-obstante clause was then confined to Article 304(b) as is clear from the following paragraph of the judgment:

> "42 The non-obstante clause vis-a-vis Article 304(a) may have some relevance so far as Article 301 is concerned, for it enables the Legislature of a State to impose an impediment on the free movement of trade in spite of the freedom declared under Article 301. But it has no relevance to Article 303, which only prohibits the State Legislature from making a discriminatory law and it does not in any way prohibit the State Legislature from imposing a non-discriminatory tax permitted under Art. 304(a). But. with reference to Art. 304(b). the non-obstante clause has significance and meaning even in regard to Art. 303. as clause (b) lifts the ban imposed by Art. 303. subject to the limitation mentioned therein. Therefore. the non-obstante clause must be deemed to apply only to that part of Art. 304 appropriate to the said clause. If so read. the difficulty in the construction disappears. Art. 304(a) lifts the general ban imposed by Article 301 in respect of imposition of non-discriminatory taxes on goods imported. which indicates that but for the said provision the law of taxation in that regard would infringe the freedom declared under Art. 301."

90. Hidayatullah, J. also found the non-obstante clause in Article 304 to be somewhat anomalous and described the same as "inaccurate drafting of the Constitution".

91. Suffice it to say that the use of the non-obstante clause in Article 304 has had its

share of criticism from the very inception which criticism has to an extent been prophetic for the interpretation of Part XIII has indeed been a lawyer's paradise over the past fifty years or so. Seervai has in his treatise adverted to this anomaly arising from the use of the non-obstante clause and said that the same covers both the clauses (a) and (b) of Article 304. He argues with considerable forensic force that reference to Article 301 in the non-obstante clause is meaningless having regard to the fact that the freedom granted thereunder is itself subject to other provisions of Part XIII including Article 304. This would necessarily imply that Article 304 (a) and (b) do not subtract anything from Article 301. That appears to us to be the correct view on the subject. While it is true that legislature does not waste words and that no part of a legislation can be rendered a surplusage, the only rational meaning that can be attributed to the non-obstante clause appearing in Article 304 is that the same was used only as a manner of abundant caution and a possible reassurance that Article 301 is indeed subordinate to Article 304 which it was even otherwise without the use of that clause. The net effect of the discussion therefore is that the expression 'subject to other provisions of this Part' appearing in Article 301 and the non-obstante clause appearing in Article 304 do not traverse in different directions. There is no conflict in the two provisions on account of the use of the said expressions. Interpreted individually or conjointly, the said two expressions simply mean that Article 304 takes precedence over Article 301. While Article 304(a) recognizes the power of the State Legislatures to tax goods imported from other State, it also imposes limitations on the exercise of that power. On the other hand clause (b) to Article 304 permits imposition of reasonable restrictions subject to the proviso appearing below that clause. We have thus no hesitation in rejecting the argument that the use of the non-obstante clause in Article 304 is suggestive of the Constitution recognizing taxes as restrictions under Article 301 or that the power to impose a reasonable restriction under Article 304(b) is meant to include the power to levy taxes so that levy of taxes may be permissible only in case the procedure provided under the proviso is followed.

92. On behalf of the dealers/ assessee it was argued that the State legislatures may levy taxes that may operate as fiscal barriers and thereby prevent or restrict inter State trade, commerce and intercourse. It was urged that if such statutory fiscal barrier is also held not to be a restriction upon the freedom of trade, commerce and intercourse guaranteed under Part XIII, a citizen whose right under that Part is affected may have no redress against such levies. Relying upon the decision of this Court in Ramjilal v. Income Tax Officer, Mohindargarh, AIR 1951 SC 97, it was contended that a challenge to a fiscal statute shall not be maintainable even under Part III of the Constitution, thereby, not only violating the citizen's constitutional rights of free trade and commerce but also denying them the remedy against such violation. This according to the learned counsel was one among other reasons why levy of taxes ought to be treated as restrictions on free trade, commerce and intercourse.

93. In Ramjilal's case (supra), a petition under Article 32 of the Constitution was filed before this Court by the petitioner who was carrying on business in the State of Nabha. With the merger of Nabha into the State of Pepsu, the petitioner was required by the assessing authority to file return and pay income tax for the income earned by him during the previous years. Aggrieved, the petitioner challenged the proceedings inter

alia on the ground that the assessment of tax for previous year violated his right guaranteed under Article 14. This Court repelled the contention founded on Article 14 holding that there was reasonable classification of assessee under the relevant statute and that the petitioner's challenge to the proceedings under Article 14 was untenable. Having said that, the Court examined the question whether the taxing statute violated Right to Property guaranteed under Article 31 (1) of the Constitution. Repelling the contention this Court held that if collection of taxes amounted to deprivation of property within the meaning of Article 31 (1), there was no point in making a separate provision regarding the same as is made in Article 265. This Court declared that Article 31(1) must be regarded as a guarantee against deprivation of property otherwise, than by imposition of tax for otherwise Article 265 would become wholly redundant. The Court declared that the Constitution had treated taxation as distinct from compulsory acquisition of property and has made independent provisions giving protection against taxation.

94. Then came *Kunnathat Thathunni Moopil Nair v. The State of Kerala & Anr.*[38] , where again one of the questions that fell for consideration was whether Article 265 of the Constitution was a complete answer to the attack against the Constitutionality of a taxing statute. This Court held that in order that a taxing law may be valid, the tax proposed to be levied must be within the legislative competence of the legislature imposing the tax and authorizing the collection thereof and that the tax must be subject to the condition laid down under Article 13 of the Constitution. One of such conditions declared by this Court was that the legislature shall not make any law that takes away or abridges the equality clause in Article 14. The Court declared that the guarantee of equal protection of laws must extend even to taxing statutes. It clarified that every person may not be taxed equally but property of the same character has to be taxed, the taxation must be by the same standard so that the burden of taxation may fall equally on all persons holding that kind and extent of property. If the taxation, generally speaking, imposes similar burden on everyone with reference to that particular kind and extent of property on the basis of such taxation, the law shall not be open to attack on the ground of inequality even though the result of taxation may be that the total burden on different persons may be unequal. The Court summed up that taxing statute is not fully immune from an attack on the ground that it infringes equality clause under Article 14, no matter the Courts are not concerned with the policy underlying the taxing statute or whether a particular tax could have been imposed in a different way or a way that the Court might think would have been more equitable in the interest of equity.

95. To the same effect is the decision in *Laxmanappa Hanumantappa Jamkhandi v. Union of India*[39],. Reference may also be made to *Smt. Ujjam Bai v. State of Uttar Pradesh*[40], which took note of the pronouncements of this Court in the three cases mentioned above to examine whether there was any conflict between the view taken in Moopil Nair case on the one hand and Ramjilal and Laxmanappa cases on the other, the Court found on a closer examination that there was no such conflict and clarified that the observation made in Ramjilal and Laxmanappa cases must in the context bear reference to abrogation of Article 31 (1) only in so far as the admissibility of a challenge to taxation law with reference to Part III is concerned. The Court explained that in Moopil Nair's case this Court has held that a taxing statute was not immune from

challenge under Article 14 just because the legislature that imposed the tax was competent to levy the tax in terms of Article 265. This Court summed up the legal position in the following words:

> " The result of the authorities may thus be summed up:
>
> (1) A tax will be valid only if it is authorized by a law enacted by a competent legislature. That is Article 265.
>
> (2) A law which is authorized as aforesaid must further be not repugnant to any of the provisions of the Constitution. Thus, a law which contravenes Articles 14 will be bad, Moopil Nair's case.
>
> (3) A law which is made by a competent legislature and which is not otherwise invalid, is not open to attack under Article 31 (1). Ramjilal's case and Laxmanappa's case.
>
> (4) A law which is ultra vires either because the legislature has no competence over it or it contravenes, some constitutional inhibition, has no legal existence, and any action taken thereunder will be an infringement of Article 19 (1) (g) Himmatlal's case and Laxmanappa's case. The result will be the same when the law is a colourable piece of legislation.
>
> (5) Where assessment proceedings are taken without the authority of law, or where the proceedings are repugnant to rules of natural justice, there is an infringement of the right guaranteed under Article 19(1) (f) and Article 19(1)(g); Tata Iron & Steel Co. Ltd; Moopil Nair's case and Shri Madan Lal Arora's case."

96. The above statement of law in our view is legally unexceptionable. The argument that Ramjilal and Laxmanappa's cases place taxing statute beyond the purview of challenge under Part III has been correctly repelled and fiscal statutes are also held to be open to challenge on the touchstone of Article 14 of the Constitution. The contention that an aggrieved citizen may have no remedy against a taxing statute does not, therefore, hold good. Whether or not a challenge to such a statute succeeds is, however, a different matter. It is fairly well settled by now that Courts show considerable deference to the legislature in the matter of quantum of tax that may be levied as also the subjects and individuals upon whom the same may be levied. Just because room for challenge to a fiscal statute is limited is in our view no reason to hold that levy of taxes otherwise within the competence of the legislature imposing the same should be seen as a restriction on free trade and commerce guaranteed under Article 301 which Article does not either textually or contextually recognize levy of taxes as impediments except in cases where the same are discriminatory in nature thereby being offensive to Article 304 (a) of the Constitution.

97. On behalf of the States it was argued by the learned Attorney General, and M/s. Rao and Dwivedi that the decisions of this Court in Atiabari and Automobile Transport cases had drawn support for their conclusion on the Australian and American decisions.

It was urged that although the view taken by the majority decision in the former had recognized that decisions from other jurisdictions may not be helpful while interpreting the provisions of our Constitution, yet the Court had referred to and relied upon those decisions to buttress its conclusions. The Australian decisions relied upon by the majority have, it was contended, been reversed by subsequent pronouncements of the Australian High Court, which pronouncements are now gravitating towards the theory that discriminatory taxes alone will operate as restrictions against free trade, commerce and intercourse. It was in that view argued that the theoretical basis borrowed from the foreign judgments by this Court in Atiabari case stood demolished or atleast substantially eroded by the subsequent pronouncements of the Australian High Courts, thereby, rendering the correctness of the view taken by the majority in Atiabari's case open to serious doubts.

98. There is, in our view, considerable merit in that submission. In Atiabari's case (supra), Gajendragadkar J., speaking for the majority while referring to the American and Australian decisions observed:

> "59 We have deliberately not referred to these decisions earlier because we thought it would be unreasonable to refer to or rely on the said section or the decisions thereon for the purpose of construing the relevant Articles of Part XIII of our Constitution. It is commonplace to say that the political and historical background of the federal polity adopted by the Australian Commonwealth, the setting of the Constitution itself, the distribution of powers and the general scheme of the Constitution are different, and so it would not be safe to seek for guidance or assistance from the Australian decisions when we are called upon to construe the provisions of our Constitution. In this connection we have already referred to the note of warning struck by Venkatarama Aiyar, J., against indiscriminate reliance being placed on Australian and American decisions in interpreting our Constitution in the case of M.P.V. Sundararamier & Co. The same caution was expressed by Gwyer, C.J., as early as 1939 when he observed in The Central Provinces and Berar Sales of Motor Spirit and Lubricants Taxation Act, 1938. In the matter of AIR 1939 F. C. 1 at P.5; "there are few subjects on which the decisions of other Courts require to be treated with greater caution than that of federal and provincial powers, for in the last analysis the decision must depend upon the words of the Constitution which the Court is interpreting; and since no two Constitutions are in identical terms it is extremely unsafe to assume that a decision on one of them can be applied without qualification to another. This may be so even where the words or expressions used are the same in both cases, for a word or a phrase may take a colour from its context and bear different senses accordingly."
>
> (emphasis supplied)

99. Having said that Gajendragadkar J., referred to these decisions with a view to supporting his conclusions by reference to Judges in other jurisdiction responding to similar challenges posed by interpretation of what His Lordship described as "sister constitutions". He said:

"59 When you are dealing with the problem of construing a constitutional provision which is none-too-clear or lucid you feel inclined to inquire how other judicial minds have responded to the challenge presented by similar provisions in other sister Constitutions. It is in that spirit that we propose to refer to two Privy Council decisions which dealt with the construction of Section 92 of the Australian Constitution."

100. The Court, then, relied upon the decisions of the Australian High Court in James v. Commonwealth of Australia (1936) A.C. 578 and Commonwealth of Australia and others v. Bank of New South Wales and others [1950] A.C. 235 to hold that the test of direct and immediate effect evolved by the Australian High Court pronouncements, while interpreting Section 92 of the Australian Constitution, was the correct test applicable even to our Constitution including interpretation of Article 301 thereof. The Court said:

Commonwealth of Australia v. Bank of New South Wales

"61 In deciding the said question one of the tests which was applied by Lord Porter was: "Does the act not remotely or incidentally (as to which they will say something later) but directly restrict the inter-State business of banking", and he concluded that "two general propositions may be accepted, (1) that regulation of trade, commerce and intercourse among the States is compatible with its absolute freedom, and (2) that Section 92 is violated only when a legislative or executive act operates to restrict such trade, commerce and intercourse directly and immediately as distinct from creating some indirect or consequential impediment which may fairly be regarded as remote".

This decision thus justifies the conclusion we have reached about the scope and effect of Article 301."

(emphasis supplied)

101. In Automobile's case (supra) also Das, J. while speaking for the majority followed the direct and immediate effect test relying upon the pronouncements of the High Court of Australia in *Commonwealth of Australia and Ors. v. Bank of New South Wales and Ors*[41]. This is evident from the following passage:

"10 In Section 92 of the Australian Constitution the expression used was "absolutely free" and repeatedly the question was posed as to what this freedom meant. We do not propose to recite the somewhat chequered history of the Australian decisions in respect of which Lord Porter. after a review of the earlier cases. said in Commonwealth of Australia v. Bank of New South Wales that in the "labyrinth of cases decided under Section 92 there was no golden thread".

What is more important for our purpose is that he expressed the view that two general propositions stood out from the decisions: (i) that regulation of trade.

> commerce and intercourse among the States is compatible with its absolute freedom. and (ii) that Section 92 of the Australian Constitution is violated only when a legislative or executive act operates to restrict such trade. commerce and intercourse directly and immediately as distinct from creating some indirect or inconsequential impediment which may fairly be regarded as remote "

102. On behalf of the States it was contended and, in our opinion, rightly so that the "direct and immediate" effect test evolved by the pronouncement of the Australian High Court has itself been watered down and diluted. The current view in Australia is that only such taxes as are discriminatory introduced by way of a protectionist measure operate as restrictions on the freedom of trade, commerce and intercourse. This is evident from the decisions of the Australia High Court in Cole v. Whitfield (1988) 165 CLR 360. The Court in that case reviewed the case law on the subject and rejected the argument that if Section 92 of the Australian Constitution was interpreted to be forbidding only discriminatory burdens it would have the effect of denying the freedom of trade, commerce and intercourse. The Court said:

> " Plainly, however, the construction which treats Section 92 as being concerned to guarantee the freedom of inter-State trade and commerce from discriminatory burdens does not involve the consequence that the grant of legislative power with respect to inter-State trade and commerce is deprived of its essential content."

103. The Court noticed the evolution of the law on the subject and held that it is only discriminatory burdens that are forbidden by Section 92 and that the question whether a burden is indeed discriminatory is a question of fact and degree to be answered upon judicial interpretation and impressions. The following passage is, in this regard, instructive. " Departing now from the doctrine which has failed to retain general acceptance, we adopt the interpretation which, as we have shown, is favoured by history and context. In doing so, we must say something about the resolution of cases in which no impermissible purpose appears on the face of the impugned law, but its effect is discriminatory in that it discriminates against inter-State trade and commerce and thereby protects intra-State and commerce of the same kind. We mention first Commonwealth laws enacted under Section 51(i) which govern the conduct of inter-State trade and commerce. Such laws will commonly not appear to discriminate in a relevant sense if they apply to all transactions of a given kind within the reach of the Parliament. It is, however, possible for a general law enacted under Section 51(i) to offend Section 92 if its effect is discriminatory and the discrimination is upon protectionist grounds. Whether such a law is discriminatory in effect and whether the discrimination is of a protectionist character are questions raising issues of fact and degree. The answer to those questions may, in the ultimate, depend upon judicial impression."

(emphasis supplied)

104. The Court also held that it is only if the discrimination is of a protectionist character that Section 92 of the Australian Constitution would stand violated. The Court said:

"In the case of a State law, the resolution of the case must start with a consideration of the nature of the law impugned. If it applies to all trade and commerce, inter-State and intra-State alike, it is less likely to be protectionist than if there is discrimination appearing on the face of the law. But where the law in effect, if not in form, discriminates in favour of intra-State trade, it will nevertheless offend against Section 92 if the discrimination is of a protectionist character. A law which has as its real object the prescription of a standard for a product or a service or a norm of commercial conduct will not ordinarily be grounded in protectionism and will not be prohibited by Section 92. But if a law, which may be otherwise justified by reference to an object which is not protectionist, discriminates \against inter-State trade or commerce in pursuit of that object in a way or to an extent which warrants characterization of the law as protectionist, a court will be justified in concluding that it nonetheless offends Section 92."

(emphasis supplied)

105. The above passage signifies a paradigm shift in the judicial opinion in Australia as regards the interpretation of Section 92 of the Australian Constitution. The earlier view that any impediment including one in the nature of a tax which directly and immediately affects free trade, commerce and intercourse would violate Section 92 has been evidently abandoned by the Australian jurists. It follows that whatever support may have been available from the earlier decisions for the view taken in Atiabari (supra) and Automobile(supra) cases as to the true test applicable for interpreting Part XIII, has, if we may use that expression, "fizzled out" with the passage of time.

106. We may, at this stage, deal with yet another contention urged on behalf of the dealers in support of their case that taxes were, in the scheme of Part XIII, treated as restrictions. It was argued that the presence of Article 306 of the Constitution which now stands repealed by Constitution 7th Amendment Act, 1956 was itself suggestive of the fact that taxes were intended to be restrictions on free trade, commerce and intercourse, for otherwise, there was no reason why a provision like Article 306 should have been incorporated by the framers
of the Constitution. Article 306, as it stood, before its deletion, was in the following terms:

"Article 306. Power of certain States in Part B of the First Schedule to impose restrictions on trade and commerce. - Notwithstanding anything in the foregoing provisions of this Part or in any other provisions of the Constitution. any State specified in Part B of the First Schedule which before the commencement of this Constitution was levying any tax or duty on the import of goods into the State from other States or on the export of goods from the State to other States may. if an agreement in that behalf has been entered into between the Government of India and the Government of that State. continue to levy and collect such tax or duty subject to the terms of such agreement and for such period not exceeding ten years from the commencement of this Constitution as may be specified in the

agreement. Provided that the President may at any time after the expiration of five years from such commencement terminate or modify any such agreement if. after consideration of the report of the Finance Commission constituted under Article 280. he thinks it necessary to do so."

107. A careful reading of the above would show that the provision started with a non-obstante clause and made it constitutionally permissible for any State specified in Part B of the First Schedule to continue levying taxes or duties on the import of goods into the State from other States or on the export of goods from the State to other States, if an agreement in that behalf has been entered into between the Government of India and the Government of that State for such period not exceeding ten years as has been stipulated in the agreement.

108. The historic rationale behind incorporation of Article 306 lay in the fact that some States were imposing taxes/duties on the import of goods into their territory and on the export of goods from their territory, which taxes and levies were inconsistent with the Scheme of Part XIII, but, since the States were heavily relying upon the revenue so collected, the tax barriers set-up for such collection could not be completely taken away in one go. The framers of the Constitution in that view considered it necessary in the interest of stability of
revenue to preserve the power exercised by the States for a limited period subject to the conditions stipulated in Article 306. The true effect of Article 306, therefore, was that while the States had no power under the Constitutional Scheme to levy customs duties on the import and export of goods to and from a State and even when such taxes and levies were discriminatory vis-a-vis goods produced/manufactured from outside the State, the discriminatory duties and levies were in larger interest of stability of revenue of the concerned States permitted, but, conditionally for a limited period. The marginal note of Article 306, therefore, rightly mentions such levies and duties to be restrictions on trade, commerce and intercourse. The reason for such description being the discriminatory nature of such taxes and levies. Seen in the historical perspective, it is futile to argue that Article 306 lends any assistance for determining whether taxes act as restrictions on free trade, commerce and intercourse. Seervai has correctly summed-up the true import of Article 306 in the following passage from his treatise (supra):

"24.42. Again, Article 306 enabled the former Native States, which became Part B States, to continue to levy any tax or duty on the import of goods into such States from other States and to impose a duty on the export of goods out of such States for a limited period of time. The reason for enacting this provision is simple. First, Part B States claimed to be sovereign States vis-a-vis British India, and vis-a-vis other Native States so that the provinces of British India were in relation to Native States, and the Native States were foreign States to one another. The duties of import and export levied by Native States were thus duties of customs which are well known for creating tariff barriers. Thus a customs duty on the import of goods creates a tariff wall which the outside goods must surmount since there is no obligation on the Native State imposing such duty to impose any corresponding duty on similar goods manufactured and produced in the other States. And the same is true of duties of export for they can effectively

> prevent goods going out of the State by making them unsaleable in States where goods bear no such tax or bear a very much smaller tax. This scheme of taxation is basically opposed to the scheme of our Constitution because the States of India are not foreign States to one another, and no State can levy a duty or customs on goods imported from another, for no State has power to levy a duty of customs. That power belongs exclusively to Parliament in relation to foreign countries. Secondly, such duties would ordinarily contravene Article 304(a) so far as import from other States is concerned. However, as the revenues of the Native States were to a greater or smaller extent dependent on duties of customs, to have prohibited them at once would have dislocated the finances of those States. So, for a limited period of time, these duties were allowed to continue."

For all that we have said above we have no hesitation in rejecting the contention urged on behalf of the dealers.

109. It was next argued on behalf of the dealers that an unreasonably high rate of tax could by itself constitute a restriction offensive to Article 301 of the Constitution. This was according to learned counsel for the dealers acknowledged even in the minority judgment delivered by Sinha, CJ in Atiabari's case (supra). If that be so, the only way such a restriction could meet the constitutional requirements would be through the medium of the proviso to Article 304(b) of the Constitution. There is, in our opinion, no merit in that contention either and we say so for two precise reasons. Firstly, because taxes whether high or low do not constitute restrictions on the freedom of trade and commerce. We have held so in the previous paragraphs of the judgment based on our textual understanding of the provisions of Part XIII which is matched by the contextual interpretation. That being so the mere fact that a tax casts a heavy burden is no reason for holding that it is a restriction on the freedom of trade and commerce. Any such excessive tax burden may be open to challenge under Part III of the Constitution but the extent of burden would not by itself justify the levy being struck down as a restriction contrary to Article 301 of the Constitution.

110. Secondly because, levy of taxes is both an attribute of sovereignty and an unavoidable necessity. No responsible government can do without levying and collecting taxes for it is only through taxes that governments are run and objectives of general public good achieved. The conceptual or juristic basis underlying the need for taxation has not, therefore, been disputed by learned counsel for the dealers and, in our opinion, rightly so. That taxation is essential for fulfilling the needs of the government is even otherwise well-settled. A reference to "A Treatise on the Constitutional Limitations" (8th Edn. 1927 - Vol. II Page 986) by Thomas M Cooley brings home the point with commendable clarity. Dealing with power of taxation Cooley says:

> "Taxes are defined to be burdens or charges imposed by the legislative power upon persons or property. to raise money for public purposes. The power to tax rests upon necessity. and is inherent in every sovereignty. The legislature of every free State will possess it under the general grant of legislative power. whether particularly specified in the constitution among the powers to be exercised by it or not. No constitutional government can exist without it, and no

arbitrary government without regular and steady taxation could be anything but an oppressive and vexatious despotism, since the only alternative to taxation would be a forced extortion for the needs of government from such persons or objects as the men in power might select as victims."

111. Reference may also be made to the following passage appearing in McCulloch v. Maryland, 17 US 316 (1819) where Chief Justice Marshall recognized the power of taxation and pointed out that the only security against the abuse of such power lies in the structure of the government itself. The court said:

"43 It is admitted that the power of taxing the people and their property is essential to the very existence of government, and may be legitimately exercised on the objects to which it is applicable to the utmost extent to which the government may choose to carry it. The only security against the abuse of this power is found in the structure of the government itself. In imposing a tax, the legislature acts upon its constituents. This is, in general, a sufficient security against erroneous and oppressive taxation.

44. The people of a State, therefore, give to their government a right of taxing themselves and their property: and as the exigencies of the government cannot be limited, they prescribe no limits to the exercise of this right, resting confidently on the interest of the legislator, and on the influence of the constituents over their representative, to guard them against its abuse."

112. To the same effect is the decision of this Court in *State of Madras v. N.K. Nataraja Mudaliar*[42] where this Court recognized that political and economic forces would operate against the levy of an unduly high rate of tax. The Court said:

"16 Again, in a democratic constitution political forces would operate against the levy of an unduly high rate of tax. The rate of tax on sales of a commodity mav not ordinarily be based on arbitrary considerations, but in the light of the facility of trade in a particular commodity, the market conditions internal and external - and the likelihood of consumers not being scared away by the price which includes a high rate of tax. Attention must also be directed sub-Section (5) of Section 8 which authorizes the State Government, notwithstanding anything contained in Section 8, in the public interest to waive tax or impose tax on sales at a lower rate on inter-State trade or commerce. It is clear that the legislature has contemplated that elasticity of rates consistent with economic forces is clearly intended to be maintained."

113. Also apposite is the following passage from the said decision where this Court held that free flow of trade does not necessarily depend upon the rate of taxes but upon a variety of factors which the Court identified in the following words:

"14 The flow of trade does not necessarily depend upon the rates of sales tax: it

depends upon a variety of factors, such as the source of supply, place of consumption, existence of trade, channels, the rates of freight, trading facilities, availability of efficient transport and other facilities for carrying on trade. Instances can easily be imagined of cases in which notwithstanding the lower rate of tax in a particular part of the country goods may be purchased from another part, where a higher rate of tax prevails. Supposing in a particular State in respect of a commodity, the rate of tax is 2 per cent but if the benefit of that low rate is offset by the freight which a merchant in another State may have to pay for carrying that commodity over a long distance, the merchant would be willing to purchase the goods from a nearer State, even though the rate of tax in that State may be higher. Existence of long standing business relations, availability of communications, credit facilities and a host of other factors - natural and business - enter into the maintenance of trade relations and the free flow of trade cannot necessarily be deemed to have been obstructed merely because in a particular State the rate of tax on sales is higher than the rates prevailing in other States."

114. Reliance by the counsel for the dealers upon the judgment of Sinha, CJ is also, in our opinion, of no avail to them. After holding taxes to be outside the purview of Part XIII of the Constitution, His Lordship made the following observations:

"17 If a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade. commerce and intercourse. for example. by imposing a high tariff wall, or by preventing imports into or exports out of a State. such a law is outside the significance of taxation. as such. but assumes the character of a trade barrier which it was the intention of the Constitution makers to abolish by Part XIII."

115. A careful reading of the above would show that Sinha, CJ had two situations in mi-nd. One, where the State prevents imports into and exports out of the State and the other where the State imposes the high tariff wall with a view to imposing an impediment to the free flow of trade, commerce and intercourse. Insofar as the first category viz. laws that forbid imports into and exports out of a State are concerned, the same would work as a restriction in terms of restrictions within the contemplation of Part XIII and may be permissible in the manner and to the extent the said Part permits to do so, but, in the second case, viz. legislature imposing a high tariff wall so as to operate as an impediment to free flow of trade, commerce and intercourse, there are considerable difficulties. That is so because the judgment does not elaborate as to what would constitute a high tariff wall for the tax to operate as a restriction/impediment.

116. Counsel for the parties were, in the course of arguments, repeatedly asked whether any objective standards and norms can be evolved to determine the height and the width of the wall referred to in the passage extracted above. They were, however, unable to suggest any such norms. They fairly conceded that it was difficult if not impossible to evolve any such norm applicable to myraid situations that would arise before the courts. This implies that the tariff wall theory actually breaks down and is not

amenable to judicially manageable dimensions. What may sound a high tariff wall or a fiscal barrier to one may not be so to the other. What may constitute a fiscal wall or barrier for one category of traders may not be so for other categories. So also, the tax at a given rate may be high on a particular commodity but reasonable qua another. Suffice it to say that the fiscal wall theory gets into serious difficulties when it comes to enforcement or effectuating the same. The logic behind the theory in fact cracks and gives-up. Such being the position, we have little hesitation in holding that the fiscal wall theory propounded in Sinha, CJ's minority judgment is not really workable and has not commended itself to us. It follows that simply because the tax is high is no reason for it to change its character and take the form of a restriction within the meaning of Part XIII, no matter any one aggrieved of such heavy burden shall have the liberty to assail the same on all such grounds as may be available to him under Part III of the Constitution. We are conscious of the fact that some decisions of this Court in *Raja Jagannath Baksh Singh v. State of UP*[43] *Federation of Hotel & Restaurant Assn. of India etc. v. Union of India & ors*[44]*. Y V Srinivasamurthy and ors. v. State of Mysore and Anr*[45]*. D G Gose & Co. (Agents) (P) Ltd. v. State of Kerala and anr.*[46]*; A Suresh and others v. State of TN and another*[47] have declared that just because a tax is heavy is no reason for it to be contrary to Part III, but we leave that question open to be examined in appropriate cases as and when any such challenge is mounted by anyone aggrieved of an unduly heavy tax rate.

117. That brings us to the question whether the use of the expression "by virtue of any entry relating to trade and commerce" appearing in Article 303 are wide enough to include entries relating to levy of taxes also. The argument advanced amongst others by Mr. Datar is that the expression "relating to trade and commerce" appearing in the said Article must be interpreted liberally so as to include not only Entry 42 in List I, Entry 26 in List II and Entry 33 in List III but also other entries that empower the Parliament and State Legislatures to levy taxes. By that logic it was contended that levy of taxes is also treated as a restriction within the contemplation of Part XIII making it necessary for the legislature to resort to Article 304(b) and the proviso for doing so. There is in our opinion no merit in that contention also.

118. We say so for two precise reasons. Firstly because entries relating to Trade and commerce by themselves are not sufficient to empower the legislature to levy taxes. The constitutional scheme is such that a taxing entry is distinct from other entries and a levy of tax is possible only if there is an entry which authorizes the competent legislature to levy the same. This distinction has for long been maintained by judicial pronouncements of this Court. We may in this regard refer to M.P.V. Sunderaramier's case (supra) where this Court has declared:

> "51. In List I, Entries 1 to 81 mention the several matters over which Parliament has authority to legislate. Entries 82 to 92 enumerate the taxes which could be imposed by a law of Parliament. An examination of these two groups of Entries shows that while the main subject of legislation figures in the first group, a tax in relation thereto is separately mentioned in the second. Thus, Entry 22 in List I is "Railways", and Entry 89 is "Terminal taxes on goods or passengers, carried by railway, sea or air; taxes on railway fares and freights". If Entry 22 is to be

construed as involving taxes to be imposed, then Entry 89 would be superfluous. Entry 41 mentions "Trade and commerce with foreign countries; import and export across customs frontiers". If these expressions are to be interpreted as including duties to be levied in respect of that trade and commerce, then Entry 83 which is "Duties of customs including export duties" would be wholly redundant. Entries 43 and 44 relate to incorporation, regulation and winding up of corporations. Entry 85 provides separately for corporation tax. Turning to List II, Entries 1 to 44 form one group mentioning the subjects on which the States could legislate. Entries 45 to 63 in that List form another group, and they deal with taxes. Entry 18, for example, is "Land" and Entry 45 is "Land revenue". Entry 23 is "Regulation of mines" and Entry 50 is "Taxes on mineral rights". The above analysis – and it is not exhaustive of the Entries in the Lists – leads to the inference that taxation is not intended to be comprised in the main subject in which it might on an extended construction be regarded as included, but is treated as a distinct matter for purposes of legislative competence. And this distinction is also manifest in the language of Article 248, clauses (1) and (2) and of Entry 97 in List I of the Constitution. Construing Entry 42 in the light of the above scheme, it is difficult to resist the conclusion that the power of Parliament to legislate on inter-State trade and commerce under Entry 42 does not include a power to impose a tax on sales in the course of such trade and commerce."

xxx xxx xxx

55. To sum up: (1) Entry 54 is successor to Entry 48 in the Government of India Act, and it would be legitimate to construe it as including tax on inter-State sales unless, there is anything repugnant to it in the Constitution and there is none such. (2) Under the scheme of the Entries in the Lists, taxation is regarded as a distinct matter and is separately set out. "

119. The above pronouncement is, in our opinion, the correct enunciation of the legal position in the light whereof it is difficult to appreciate how entries relating to trade and commerce could be understood to be including levy of taxes also. That apart, once taxes are held to be outside Part XIII for the reason that we have already set out earlier, there is no way we can bring them back into that Part by a tenuous interpretation or understanding of Article 303. As explained by us earlier, Article 303 is an exception to Article 302, inasmuch as it limits the power conceded to the Parliament under Article 302 to impose restrictions on freedom of Trade, commerce and intercourse in public interest. The power exercised by Article 302 cannot be so exercised as to give preference to one state over another except under a situation covered by Article 303(2) namely situation arising from scarcity of goods in any part of the territory of India. We cannot add to this Article any artificially extended meaning the ingenuity of the bar in coining any such interpretation notwithstanding.

120. Relying upon the decision in Mudaliar's case (supra) it was argued on behalf of the assessee that this Court has upheld the constitutional validity of the Central State Tax Act on the ground that such a tax was in public interest within the contemplation of Article 302 of the Constitution of India, hence, validly leviable. This, according to the

learned counsel, implied that the tax was recognised as a restriction which could be levied only if found to be in public interest as stipulated in Article 302. We have no difficulty in rejecting that contention. In Mudaliar's case, this Court was bound by and followed the pronouncement of the larger bench in Atiabari's case holding that taxes could also be restrictions on free trade and commerce if they directly and immediately impeded their free flow. We have, in the preceding part of this judgment, held that view to be legally unsustainable on a proper construction of the provision of Part XIII and the Constitutional scheme. Once the premise on which Atiabari's case was decided is held to be flawed, Mudaliar that simply followed the ratio of that decision cannot stand scrutiny. The argument that Central Sales Tax was valid in terms of Article 302 as such a tax was in public interest becomes academic if taxes are held to be outside the purview of Part XIII. This incidentally will be true in respect of every other pronouncement where benches of smaller strength have dealt with similar other legislations and taken a view following the ratio in Atiabari's case.

121. We may at this stage deal with yet another contention urged on behalf of the assesses who argued that while Article 304(a) forbids discriminatory fiscal legislation in respect of goods coming from another state there was no provision which prevented the States from levying discriminatory taxes within its territorial limits. The argument was that the absence of any provision against discriminatory taxation within a State must be understood to mean that taxes would generally be restrictions and unless the States take recourse to Article 304(b) they cannot levy such taxes upon trade and commerce within their territorial limits. The argument is, in our view, more in despair than substantial. It is true that Part XIII does not in terms forbid the levy of discriminatory taxes on goods produced within the States but the fact that there is no such prohibition does not necessarily mean that if such discriminatory taxation does indeed take place the same is constitutionally permissible. Whether or not there is hostile discrimination between goods from one part of the State and those from another part is a matter which will have to be judged on a case to case basis and on the touchstone of Article 14. Having said that we need to remind ourselves that Part XIII of the Constitution was aimed at addressing the mischief arising from fiscal and other barriers which the princely states had imposed and which gravely impeded free trade and commerce. The Constituent Assembly Debates show that framers of the Constitution were concerned with the removal of such barriers. Discrimination intra-State in terms of levy of taxes was never considered to be a challenge for presumably the Constituent Assembly never considered the same to be a real possibility necessitating a specific provision prohibiting levy of discriminatory intra-State taxes.

122. On behalf of the assessees-dealers, it was next argued that levy of entry tax on import of goods from outside the local area in the State will be per se discriminatory if goods so imported or similar are not produced or manufactured within the State. That is, argued the learned counsel, because the levy will fall unequally thereby violating the guarantee against discrimination contained in Article 304(a). We have no difficulty in rejecting that submission as well. The reason is obvious. Article 304(a), in our opinion, strikes at discriminatory taxation implying thereby that the levy falls unequally as between goods produced or manufactured within the State and those being imported from outside. The essence of the guarantee in Article 304(a) lies in the same or similar

goods being treated similarly in the matter of taxation. The question, therefore, is whether that guarantee is violated if the goods subjected to levy of entry tax are not produced or manufactured within the State levying the tax. Our answer is in the negative. This is because there is no question of any discrimination if goods from outside the State are not at a disadvantage vis-a-vis goods produced or manufactured within that State. It is true that a levy on goods that are not produced or manufactured in the State is likely to make such goods costlier but that is not enough for the levy to be considered unconstitutional. A responsive Government aware of the needs of its constituents will be under tremendous pressure to keep such taxes low enough for its constituents to be able to afford the same. Democratic processes and pressures within the system of governance that we have will itself take care of any aberration in this regard. What is absolutely clear, however, is that Article 304(a) will not frown at a levy simply because same or similar goods as are taxed are not produced or manufactured in the State. Reliance upon the decision in Kalyani Stores AIR 1966 SC 1686 does not, in our opinion, help the assessees. The majority judgment in that case looked at Article 304(a) as the source of power to levy a tax or duty. We have in the earlier parts of the judgment explained that the source of power to levy taxes/duties lies in Articles 245 and 246 of the Constitution read with the entries in the three lists contained in Schedule VII. Article 304(a), in that view, only places a constitutional restriction on the power to levy taxes or duties while recognizing the availability of such powers to the State legislatures. The restrictions as explained by us in the earlier paras to levy taxes/duties is confined to levy of discriminatory taxes and duties alone. To the extent, Kalyani Stores takes the view that the power to levy taxes is traceable to
Article 304(a) the decision, in our opinion, is not sound nor is it correct to say that since goods being taxed are not produced in the State, the power to levy a tax gets obliterated.

123. Appearing for some of the assessees Mr. Venkatraman argued that the Central Sales Tax Act was a classic example of the Union exercising its power under Article 302 of Part XIII. He contended that the restrictions so imposed signify that tax and restrictions are synonymous within the contemplation of part XIII.

124. The Central Sales Tax Act, 1956 was enacted pursuant to the Sixth Amendment Act, 1956 whereby taxes on sale and purchase of goods in the course of inter-state trade and commerce were expressly brought within the purview of the legislative competence of Parliament. This included the power to impose restrictions upon the power of the State legislature insofar as levy of taxes of sale or purchase of goods of special importance is concerned. Entry 92-A added by the Sixth Amendment Act 1956 empowered the Parliament to levy taxes on the sale and purchase of the goods other than newspapers in the course of trade and commerce. Entry 54 of the State List by the same amendment was redrawn to make the taxes on the sale and purchase of goods subject to Entry 92-A of List I. The two entries read as under:

> "92-A. 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.
>
> 54. Taxes on the sale or purchase of goods other than newspapers, subject to

the provisions of Entry 92-A of List-I."

125. The States' power it is evident is made subservient to the powers of the Parliament under Entry 92-A. Section 15 of the Central Sales Tax Act, therefore, has overriding effect vis-a-vis any State Law authorizing imposition of taxes on sale/purchase of declared goods. Seen in the above perspective, Parliament has limited the legislative power of the State insofar as taxes on declared goods are concerned. We find it difficult to read into such restrictions the meaning sought to be drawn by the learned counsel that taxes themselves are restrictions within the comprehension of Part XIII. The imposition of restrictions on the State's power of taxation in regard to declared goods is not, in our opinion, suggestive of taxes themselves being restrictions for purposes of Part XIII of the Constitution. Not only that, Article 286(3) provides the source of power for the Parliament to impose any restriction on the State authority to levy a tax on goods of special importance declared by Parliament. Article 286 (3) reads as:

> "286. Restriction as to imposition of tax on the sale or purchase of goods:
>
> (1)....
>
> (2)....
>
> (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 made by law specify."

126. In the light of what we have said above, we answer Question No.1 in the negative and declare that a non-discriminatory tax does not per se constitute a restriction on the right to free trade, commerce and intercourse guaranteed under Article 301. Decisions taking a contrary view in Atiabari's case (supra) followed by a series of later decisions shall, therefore, stand overruled including the decision in Automobile Transport (supra) declaring that taxes generally are restrictions on the freedom of trade, commerce and intercourse but such of them as are compensatory in nature do not offend Article 301. Resultantly decisions of his Court in *Jindal Stainless Limited(2) and anr. v. State of Haryana and ors.(Supra)* shall also stand overruled.

127. Re. Question No.2

In view of our answer to Question No.1, Question No.2 does not arise for consideration.

128. Re. Question No.3

In the light of what we have said in Question Nos. 1 and 2, this question also does not survive for consideration.

129. Re. Question No.4

This question touching the constitutional validity of the impugned State enactments can be split into two parts. The first part which can be briefly dealt with at the outset is whether the constitutional validity of the impugned legislations has to be tested by reference to both Articles 304(a) and 304(b) as contended by learned counsel for the assessees or only by reference to Article 304(a) as argued by the States. In the light of what we have said while dealing with question No.1 we have no hesitation in holding that Article 304(b) does not deal with taxes as restrictions. At the risk of repetition, we may say that restrictions referred to in Article 304(b) are non-fiscal in nature. Constitutional validity of any taxing statute has, therefore, to be tested only on the anvil of Article 304(a) and if the law is found to be non-discriminatory, it can be declared to be constitutionally valid without the legislation having to go through the test or the process envisaged by Article 304(b). Should, however, the statute fail the test of non-discrimination under Article 304(a) it must be struck down for the same cannot be sustained even if it had gone through the process stipulated by Article 304(b). That is because what is constitutionally impermissible in terms of Article 304(a) cannot be validated and sanctioned through the medium of Article 304(b). Suffice it to say that a fiscal statute shall be open to challenge only under Article 304(a) of the Constitution without being subjected to the test of Article 304(b) either in terms of the existence of public interest or reasonableness of the levy.

130. That brings us to the second part of question No.4 viz. whether the impugned State enactments violate Article 304(a) of the Constitution. That aspect will necessarily involve a careful reading of the impugned enactments and a proper appreciation of the scheme underlying the same. While we have at some length heard learned counsel for the parties on that aspect, we do not propose to deal with all the dimensions of that challenge based on Article 304(a) except two of them that were argued at great length by learned counsel for the parties. The first of these two dimensions touches upon the State's power to promote industrial development by granting incentives including those in the nature of exemptions or reduced rates of levy on goods locally produced or manufactured. On behalf of the assesses it was contended that grant of exemptions and incentives in favour of locally manufactured/produced goods is also one form of insidious discrimination which was impermissible in terms of article 304(a) for such exemptions and incentives had the effect of putting goods from another State at a disadvantage. Relying upon a decision of two-Judge Bench of this Court in *Shree Mahavir Oil Mills and Anr. v. State of Jammu and Kashmir and Ors*[48]. it was argued that exemptions in favour of locally produced goods from payment of taxes was constitutionally impermissible and offensive to article 304(a). That was a case where the State Government had totally exempted goods manufactured by small scale industries within the State from payment of sales tax even when the sales tax payable by other industries including manufacturers of goods in adjoining States was in the range of 8%. This exemption was questioned by manufacturers of edible oils from other States on the ground that the same was discriminatory and violative of Articles 301 and

304 of the Constitution.

131. This Court held that the exemption given to manufacturers of edible oil was total and unconditional, while producers of edible oil from industries in adjoining states had to pay sales tax @ 8%. Grant of exemption to local oil producing units thereby put the former at a disadvantage. Having said that, the Court exercised its powers under Article 142 of the Constitution and struck down the exemption by moulding the reliefs to suit the exigencies of the situation. The Court no doubt noticed a *three-Judge Bench decision in Video Electronics vs. State of Punjab*[49] in which notifications issued by the States of U.P and Punjab providing for exemptions to new units established in certain areas for a prescribed period of 3 to 7 years were assailed as discriminatory. The challenge to the exemption was in that case also based on the alleged violation of Articles 301 and 304. This Court however upheld the notifications in question on the ground that the same related to a specific class of industrial units and the benefit under the same was admissible for a limited period of time only. The Court observed that if an overwhelmingly large number of local manufacturers were subject to sales tax, it could not be said that the local manufactures were favored as a class against outsiders. Adverting to the decision in Video Electronics (supra) this Court in Mahavir (supra) held the same to be distinguishable on the ground that the Punjab and U.P notifications were qualitatively different from the one issued by the Government of Jammu and Kashmir in as much as while the former benefitted only specified units and limited the benefit to a specified period, the latter was not subject to any such limitations. This declared the Court resulted in discrimination vis-a-vis. outside goods. What is important is that in Video Electronics (supra) this Court recognized the difference between differentiation and discrimination and held that every differentiation is not discrimination. This Court noted that the word discrimination was not used in Article 14 as it has been used in Article 16, Article 303 and Article 304 (a). The use of the word in 304 (a) observed this Court involved an element of "intentional and unfavorable bias". So long as there was no such bias evident from the measure adopted by the state, mere grant of exemption or incentives aimed at supporting local industries in their growth, development and progress did not constitute discrimination.

132. We respectfully agree with the line of reasoning adopted in Video Electronics (supra). The expression "discrimination" has not been defined in the Constitution though the same has fallen for interpretation of this Court on several occasions. The earliest of these decisions was rendered in *Kathi Raning Rawat v. The State of Saurashtra*[50] where a seven-Judge Bench of this Court held that all legislative differentiation is not necessarily discriminatory. Relying upon the meaning of the expression in Oxford Dictionary, Patanjali Sastri, CJ (as His Lordship then was) explained:

> "7. All legislative differentiation is not necessarily discriminatory. In fact, the word "discrimination" does not occur in Article 14. The expression "discriminate against" is used in Article 15(1) and Article 16(2), and it means, according to the Oxford Dictionary, "to make an adverse distinction with regard to; to distinguish unfavourably from others". Discrimination thus involves an element of unfavourable bias and it is in that sense that the expression has to be understood

> in this context. If such bias is disclosed and is based on any of the grounds mentioned in Articles 15 and 16, it may well be that the statute will, without more, incur condemnation as violating a specific constitutional prohibition unless it is saved by one or other of the provisos to those articles. But the position under Article 14 is different. Equal protection claims under that article are examined with the presumption that the State action is reasonable and justified. This presumption of constitutionality stems from the wide power of classifi-cation which the legislature must, of necessity, possess in making laws operating differently as regards different groups of persons in order to give effect to its policies "

133. Fazl Ali J. in his concurring judgment explained the concept in the following words:

> "19. I think that a distinction should be drawn between "discrimination without reason" and "discrimination with reason". The whole doctrine of classification is based on this distinction and on the well-known fact that the circumstances which govern one set of persons or objects may not necessarily be the same as those governing another set of persons or objects, so that the question of unequal treatment does not really arise as between persons governed by different conditions and different sets of circumstances. The main objection to the West Bengal Act was that it permitted discrimination "without reason" or without any rational basis."

Any challenge to a fiscal enactment on the touchstone of Article 304(a) must in our opinion be tested by the same standard as in Kathi's case (supra). The Court ought to examine whether the differentiation made is intended or inspired by an element of unfavourable bias in favour of the goods produced or manufactured in the State as against those imported from outside. If the answer be in the affirmative, the differentiation would fall foul of Article 304(a) and may tantamount to discrimination. Conversely, if the Court were to find that there is no such element of intentional bias favouring the locally produced goods as against those from outside, it may have to go further and see whether the differentiation would be supported by valid reasons. In the words of Fazl Ali, J. discrimination without reason would be unconstitutional whereas discrimination with reason may be legally acceptable. In Video Electronic's case, this Court noted that the differentiation made was supported by reasons. This Court held that if economic unity of India is one of the Constitutional aspirations and if attaining and maintaining such unity is a Constitutional goal, such unity and objectives can be achieved only if all parts of the Country develop equally. There is, if we may say so, with respect considerable merit in that line of reasoning. A State which is economically and industrially backward on account of several factors must have the opportunity and the freedom to pursue and achieve development in a measure equal to other and more fortunate regions of the country which have for historical reasons, developed faster and thereby acquired an edge over its less fortunate country cousins. Economic unity from the point of view of such underdeveloped or developing states will be an illusion if they do not have the opportunity or the legal entitlement to promote industries within their respective territories by granting incentives and exemptions necessary for such growth and development. The argument that power to grant exemption cannot be used by the

State even in case where such exemptions are manifestly intended to promote industrial growth or promoting industrial activity has not appealed to us. The power to grant exemption is a part of the sovereign power to levy taxes which cannot be taken away from the States that are otherwise competent to impose taxes and duties. The conceptual foundation on which such exemptions and incentives have been held permissible and upheld by this Court in Video's case is, in our opinion, juristically sound and legally unexceptionable. Video Electronics, therefore, correctly states the legal position as regards the approach to be adopted by the Courts while examining the validity of levies. So long as the differentiation made by the States is not intended to create an unfavourable bias and so long as the differentiation is intended to benefit a distinct class of industries and the life of the benefit is limited in terms of period, the benefit must be held to flow from a legitimate desire to promote industries within its territory. Grant of exemptions and incentives in such cases must be deemed to have been inspired by considerations which in the larger context help achieve the Constitutional goal of economic unity.

134. Seen in the above context the decision in Mahabir Oil's case is indeed distinguishable in as much as the manufactures of edible oil were exempt totally and unconditionally while other manufacturers from outside the State were not so exempt. Whether or not the impugned enactments in the present batch of cases satisfy the tests referred to above and elaborated in Video Electronics case is a matter on which we do not propose to express any opinion for that aspect is best left open to be considered by the regular benches hearing these matters after the reference is disposed off.

135. The other dimension of what according to the assesses amounts to discrimination lies in goods coming from outside the State for sale, consumption or use within a local area of another State being subjected to an entry tax at a rate different from the one at which goods manufactured within the taxing State are taxed. We are not getting into the substantive or machinery provisions of the State enactments that levy entry tax on goods entering a local area. This can be done more appropriately by the bench hearing the matter after the reference has been answered. What we propose to examine is whether grant of exemption or adjustment/ setoff/ credit to goods produced or manufactured within the taxing State can vis a vis goods coming from outside the State constitute discrimination against such outside goods. According to the assessee it does constitute discrimination against such outside goods while according to the State any provision which is aimed at equalizing the impact of taxes on goods after their production/ manufacture is legitimate and constitutionally permissible.

136. The States argue that the grant of exemption to indigenous goods is aimed only at neutralizing the impact of entry tax on those goods, in cases where VAT/ Sales Tax payable on such goods is equivalent to the rate at which entry tax is chargeable. The exemption in such cases has the effect of rendering the locally produced goods free from entry tax liability. In cases where there is a difference in the rate of VAT/ Sales Tax and entry tax adjustment/credit of the amount paid towards VAT/ Sales tax has the effect of reducing the entry tax liability proportionately. It is argued that so long as similar credit/adjustment/setoff is made admissible to goods coming from another state there is no question of any discrimination qua them. The rate of tax paid on such goods

in the state from where they are brought including the Central Sales Tax, if any payable on the same may be equal to the entry tax payable under the relevant statute in which case such outside goods also enjoy the same advantage as goods manufactured in the taxing state, dispelling any misconceived impression about any discrimination qua such goods.

137. The legal position as to the approach that courts adopt towards fiscal measures while examining their constitutional validity is fairly well settled by a long line of decisions of this Court. The law on the subject is so well settled that it calls for no elaborate discussion of the same. Courts have almost universally accepted the principle that keeping in view the inherent complexities of fiscal adjustments and the diverse elements and inputs that go into such exercise a greater latitude is due to the legislature in taxation related legislations. It is unnecessary to refer to all the decisions in which this Court has conceded such play at the joints to the legislature. Reference to some of the decision of this Court should in our opinion suffice. In *Mafatlal v. Union of India*[51] in a separate but concurring opinion Paripoornan, J. held:

> "343 In the matter of taxation laws, the Court permits a great latitude to the discretion to the legislature. The State is allowed to pick and choose districts, objects, persons, methods and even rate for taxation if it does so reasonably. The Courts view the laws relating to economic activities with greater latitude than other matters. [See Collector of Customs v. Nathella Sampathu Chetty and Anr. AIR 1962 SC 316; Khyerbari Tea Company Ltd. and Anr. v. State of Assam and Ors. AIR 1964 SC 925; R.K. Garg v. Union of India and Ors. AIR 1981 SC 2138; Gauri Shanker and Ors v. Union of India and Ors. (1994) 6 SCC 349 and Union of India and Anr. v. A. Sanyasi Rao and Ors. (1996) 3 SCC 465]etc."

138. Reference may also be made to the Constitution bench decision of this Court in *Khandige Sham Bhat v. Agrl. ITO*[52], where this Court declared that a law may facially appear to be non discrimination and yet its impact on persons and property similarly situate may operate unequally in which event, the law would offend the equity clause. This implies that facial equality is not the only test for determining whether the law is constitutionally valid. What is equally important is the impact of the legislation. This Court held:

> "7...Though a law ex facie appears to treat all that fall within a class alike, if in effect it operates unevenly on persons or property similarly situated, it may be said that the law offends the equality clause. It will then be the duty of the court to scrutinise the effect of the law carefully to ascertain its real impact on the persons or property similarly situated. Conversely, a law may treat persons who appear to be similarly situate differently; but on investigation they may be found not to be similarly situate. To state it differently, it is not the phraseology of a statute that governs the situation but the effect of the law that is decisive. If there is equality and uniformity within each group, the law will not be condemned as discriminative, though due to some fortuitous circumstance arising out of a peculiar situation some included in a class get an advantage over others, so long as they are not singled out for special treatment. Taxation law is not an exception

to this doctrine vide Purshottam Govindji v. B.M. Desai, and Kunnathat Thathuni Moopil Nair v. State of Kerala. But in the application of the principles, the courts, in view of the inherent complexity of fiscal adjustment of diverse elements, permit a larger discretion to the legislature in the matter of classification, so long it adheres to the fundamental principles underlying the said doctrine. The power of the legislature to classify is of "wide range and flexibiliy" so that it can adjust its system of taxation in all proper and reasonable ways."

139. In *V. Guruviah Naidu and Sons and ors. v. State of Tamil Nadu and ors*[53], the Court was examining whether levy of sales tax on hides and skins from within or outside the State was discriminatory and offensive to Article 304(a) of the Constitution. Repelling the contention that it was violative of Article 304(a), this Court held:

"8. None of the circumstances which led this Court to strike down the relevant provisions in the abovementioned two cases exists in the present case. In Mehtab's case discrimination was found to exist because of the fact that tax was being levied at the same rate in respect of both raw hides and skins as well as dressed hides and skins, even though the price of dressed hides and skins was much higher. The position was worse in the case of Hajee Abdul Shukoor because in that case the sales tax was found to have been charged at a higher rate in respect of dressed hides and skins than that on the sale of raw hides and skins in spite of the fact that the price of dressed hides and skins was higher than that of raw hides and skins. The position in the present case is materially different, for here the rate of sales tax for raw hides and skins is 3 per cent, while that for dressed hides and skins is 11/2 per cent. It is plain that the lower rate of tax in the case of dressed hides and skins has been prescribed with a view to offset the difference between the higher price of dressed hides and skins and the lower price of raw hides and skins. No material has been brought on the record to show that despite the lower rate of sales tax for dressed hides and skins, the imported hides and skins are being subjected to discrimination. The onus to show that there would be discrimination between the hides and skins which were purchased locally in the raw form and thereafter tanned and the hides and skins which were imported from other States was upon the appellant. The appellant, we find, has failed to discharge such onus.

9. Article 304(a) does not prevent levy of tax on goods; what it prohibits is such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. The object is to prevent discrimination against imported goods by imposing tax on such goods at a rate higher than that borne by local goods since the difference between the two rates would constitute a tariff wall or fiscal barrier and thus impede the free flow of inter-State trade and commerce. The question as to when the levy of tax would constitute discrimination would depend upon a variety of factors including the rate of tax and the item of goods in respect of the sale of which it is levied. The scheme of Items 7(a) and 7(b) of the Second Schedule to the State Act is that in case of raw hides and skins which are purchased locally in the State, the levy of tax would be at the rate of 3 per cent at the point of last

purchase in the State. When those locally purchased raw hides and skins are tanned and are sold locally as dressed hides and skins, no levy would be made on such sales as those hides and skins have already been subjected to local tax at the rate of 3 per cent when they were purchased in raw form. As against that, in the case of hides and skins which have been imported from other States in raw form and are thereafter tanned and then sold inside the State as dressed hides and skins, the levy of the tax is at the rate of 11/2 per cent at the point of first sale in the State of the dressed hides and skins. This levy cannot be considered to be discriminatory as it takes into account the higher price of dressed hides and skins compared to the price of raw hides and skins. It also further takes note of the fact that no tax under the State Act has been paid in respect of those hides and skins. The legislature, it seems, calculated the price of hides and skins in dressed condition to be double the price of such hides and skins in raw state. To obviate and prevent any discrimination or differential treatment in the matter of levy of tax, the legislature therefore prescribed a rate of tax for sale of dressed hides and skins which was half of that levied under Item 7(a) in respect of raw hides and skins."

140. In *Malwa Bus Service (Private) Ltd. v. State of Punjab and others*[54] this Court held that a difference in the rate of tax by itself cannot be considered to be discriminatory and offensive to the equality clause:

"21. The next submission urged on behalf of the petitioners is based on Article 14 of the Constitution. It is contended by the petitioners that the Act by levying Rs 35,000 as the annual tax on a motor vehicle used as a stage carriage but only Rs 1500 per year on a motor vehicle used as a goods carrier suffers from the vice of hostile discrimination and is, therefore, liable to be struck down. There is no dispute that even a fiscal legislation is subject to Article 14 of the Constitution. But it is well settled that a legislature in order to tax some need not tax all. It can adopt a reasonable classification of persons and things in imposing tax liabilities. A law of taxation cannot be termed as being discriminatory because different rates of taxation are prescribed in respect of different items, provided it is possible to hold that the said items belong to distinct and separate groups and that there is a reasonable nexus between the classification and the object to be achieved by the imposition of different rates of taxation. The mere fact that a tax falls more heavily on certain goods or persons may not result in its invalidity. As observed by this Court in Khandige Sham Bhat v. Agricultural Income Tax Officer in respect of taxation laws, the power of legislature to classify goods, things or persons are necessarily wide and flexible so as to enable it to adjust its system of taxation in all proper and reasonable ways. The Courts lean more readily in favour of upholding the constitutionality of a taxing law in view of the complexities involved in the social and economic life of the community. It is one of the duties of a modern legislature to utilise the measures of taxation introduced by it for the purpose of achieving maximum social good and one has to trust the wisdom of the legislature in this regard. Unless the fiscal law in question is manifestly discriminatory the court should refrain from striking it down on the ground of discrimination. These are some of the broad principles laid down by this Court in

several of its decisions and it is unnecessary to burden this judgment with citations. Applying these principles it is seen that stage carriages which travel on an average about 260 kilometres every day on a specified route or routes with an almost assured quantum of traffic which invariably is overcrowded belong to a class distinct and separate from public carriers which carry goods on undefined routes. Moreover the public carriers may not be operating every day in the State. There are also other economic considerations which distinguish stage carriages and public carriers from each other. The amount of wear and tear caused to the roads by any class of motor vehicles may not always be a determining factor in classifying motor vehicles for purposes of taxation. The reasons given by this Court in G. K. Krishnan case for upholding the classification made between stage carriages and contract carriages both of which are engaged in carrying passengers are not relevant to the case of a classification made between stage carriages which carry passengers and public carriers which transport goods. The petitioners have not placed before the court sufficient material to hold that the impugned levy suffers from the vice of discrimination on the above ground."

141. Seen in the context of the above, we are inclined to accept the submission made on behalf of the State that so long as the intention behind the grant of exemption/adjustment/credit is to equalize the fall of the fiscal burden on the goods from within the State and those from outside the State such exemption or set off will not amount to hostile discrimination offensive to Article 304(a). Having said that, we leave open for examination by the regular benches hearing the matters whether the impugned enactment achieve the object of such equalization or lead to a situation that exposes goods from outside the state to suffer any disadvantage vis-a-vis those produced or manufactured in the taxing State.

142. We must, while parting, mention that learned counsel for the parties had attempted to raise certain other issues like whether the entire State can be treated as a local area and whether entry tax can be levied on goods imported from outside the country. We do not, however, consider it necessary in the present reference to address all those issues which are hereby left open to be decided by the regular bench hearing the matter.

143. With that observation the reference is answered. The Registry shall now place the matters before regular benches for an expeditious disposal of the same in the light of what has been observed by us above.

[1]AIR 1961 SC 0232	[2]AIR 1962 SC 1406	[3](1995 Supp. 1 SCC 0673
[4](1996) 9 SCC 0136	[5](2003) 8 SCC 0060	[6](2006) 7 SCC 0241
[7](2009) 7 SCC 0339	[8](2010) 4 SCC 0595	[9](AIR 1965 SC 1636
[10] (1975) 1 SCC 0375	[11](1992) Supp 2 SCC 0651	[12](2002) 8 SCC 0481
[13](1979) 2 SCC 0034	[14](1973) 4 SCC 0225	[15](1948) 2 All E.R. 0995
[16]AIR 1962 SC 1563	[17](2000) 5 SCC 0694	[18](2009) 10 SCC 0755
[19](1983) 4 SCC 0045	[20](2004) 10 SCC 0201	[21](2012) 7 SCC 0106
[22](1990) 1 SCC 0109	[23]AIR 1955 SC 0540	[24]AIR 1967 SC 0040

[25](1994) 3 SCC 0001	[26] (2006) 7 SCC 0001	[27](AIR 1954 SC 0282
[28]AIR 1954 SC 0400	[29]AIR 1961 SC 0459	[30]AIR 1965 SC 1107
[31](1980) 1 SCC 0416	[32](1995) 1 SCC 0655	[33](2004) 5 SCC 0155
[34](2004) 10 SCC 0201	[35](1987) 1 SCC 0424	[36](2002) 9 SCC 0232
[37](1981) 2 SCC 0318	[38]AIR 1961 SC 0552	[39]AIR 1955 SC 0003
[40]AIR 1962 SC 1621	[41](1950) A.C. 0235	[42]AIR 1969 SC 0147
[43]AIR 1962 SC 1563	[44](1989) 3 SCC 0634	[45]AIR 1959 SC 0894
[46](1980) 2 SCC 0410	[47](1997) 1 SCC 0319	[48](1996) 2 SCC 0039
[49](1990) 3 SCC 0087	[50]AIR 1952 SC 0123	[51](1997) 5 SCC 0536
[52]AIR 1963 SC 0591	[53](1977) 1 SCC 0234	[54](1983) 3 SCC 0237

JUDGMENT

S.A.Bobde,J.,

1. I am in respectful agreement with the Judgment of the Chief Justice, on the question that taxes are not restrictions on the freedom of trade, commerce and intercourse guaranteed by Article 301.

Taxes are not restrictions on Trade

2. In addition to the reasons stated in the judgment, it appears that there is a more fundamental reason why tax is not liable to be viewed as a restriction on the freedom of trade, commerce and intercourse. On the contrary it seems that a tax, such as the one we are concerned with is predicated on the freedom of trade and commerce. This is particularly true of an entry tax. It is an impost levied on transactions which are entered into in the course of that freedom. In fact, but for such freedom of trade there would be no transaction and no occasion for the levy of a tax. The levy of a tax is a distinct event from the transaction. Trade and commerce must take place to attract a tax. Undoubtedly a tax may make the transaction less profitable to the extent of the tax. But that is far from being an impediment on the transaction which is part of trade, the freedom which is guaranteed under Article 301. It is not possible to readily conceive of a tax, which in itself, restricts or impedes the freedom of trade. The circumstances are much like the freedom of movement of an individual by a bus and the charge of a bus ticket for such movement. It can hardly be contended that the charge of a bus ticket impedes the freedom of movement.

3. The other related contentions have been adequately dealt with by the Judgment of the Chief Justice and I fully subscribe to the same. I would also agree in this regard with the view of Sinha, CJ, in Atiabari that a tax is not a restriction. Sinha, CJ, observed that " if a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution makers to abolish by Part-XIII". However, it is difficult to implement such a test since it does not disclose any objective standard for determining when such a law would assume the character of a trade barrier. In principle, a tax cannot constitute a restriction on the

freedom of trade, commerce and intercourse as held by Sinha, CJ. Therefore, it would not be possible to construe a tax as a trade barrier merely because the rates are high. As regards apprehensions expressed regarding high rates of taxation, it would be apposite to rely on the observations of *Marshall, CJ, in McCulloch v. Maryland*[1], that the only security against the abuse of such power lies in the structure of the government itself.

Article 304 (a)

4. In regard to the question whether the levy of entry tax on import of goods from outside the local area in the State will be per se discriminatory if goods similar to those imported are not produced or manufactured within the State, I find it difficult to agree with the conclusion that a tax on goods imported into a State can be levied even if similar goods are not manufactured or produced in the importing State. I would agree with the conclusion drawn by Ashok Bhushan, J., in this regard. Article 304 reads as follows:

> "Restrictions on trade, commerce and intercourse among States.- Notwithstanding anything in Article 301 or Article 303, the Legislature of a State may by law-
>
> (a) impose on goods imported from other States [or the Union territories] any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and
>
> (b)impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest:
>
> Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President."

5. The non-discriminatory principle is embedded in two provisions of Part XIII: Article 303 (1) - Parliament cannot impose restrictions under Article 302 and make a discriminatory law under any entry relating to trade and commerce; the other is Article 304 (a) which (unlike Section 297 of the erstwhile Government of India Act, 1935 which prohibited - through a negative mandate, discriminatory treatment) empowers State Legislatures to impose non-discriminatory taxes on goods. Thus, Article 304 (a) differentiates between discriminatory and non-discriminatory taxes. The premise underlying this provision is the paramount aim of Part XIII to establish and foster economic unity of the country. Non-discrimination, or parity of treatment is therefore at the core of its purpose, which Shri T.T Krishnamachari stressed, in his speech in the Constituent Assembly. He said that "restrictions by the State have to be prevented so that the particular idiosyncrasy of some people in power or narrow provincial policies of certain States should not be allowed to come into play and affect the general economy of the country." [Constituent Assembly Debates, 1139 (1949)].

6. The Article, therefore, recognizes the power of a Legislature to a State to impose the tax on the imported goods so, however, as not to discriminate between goods so imported and goods so manufactured or produced. While there is no doubt that this Article recognizes the power to legislate on a State, it equally qualifies that power with the condition that such a law must comply with. That condition is that the law which imposes a tax on imported goods cannot "discriminate" between goods so imported and the goods so manufactured or produced. It also postulates that the tax on import is a "tax to which similar goods manufactured or produced in that State are subject." The Article thus imposes two conditions: firstly, that a law may impose a tax on goods imported from other States, 'any tax' to which "similar goods manufactured or produced' in that State are subject. This clearly implies that the goods imported from other States may be subjected to a tax where similar goods are in fact, manufactured or produced in the importing State and are subjected to tax. In other words, (a) the goods imported from other States must be similar to (b) the goods manufactured or produced in the importing State and (c) the goods so locally manufactured or produced must be subject to tax. The second condition is the tax that is imposed on imported goods should not discriminate between the imported goods and goods manufactured or produced in the importing State.

7. The intention of the Article thus, clearly is that where a tax exists on goods imported into a State there should be no discrimination between such a tax and a tax on similar goods manufactured or produced in the importing State. The reference point for tax on imported goods is the tax on locally manufactured goods. It is not possible to construe the prohibition against discrimination where there is no tax upon similar goods manufactured or produced in the importing State. Undoubtedly, the effect of such a construction is that the imported goods cannot be taxed where similar goods are not manufactured or produced in the importing State and are therefore, not subjected to similar tax and that seems to be the clear intention of this Article.

8. In the normal course, a State in which certain goods are not manufactured would rely on the supply of such goods from other States and the effect of this provision would be to make the goods so imported available without the additional burden of tax. In sum, the premise on which tax can be imposed is the existence of not mere taxes on goods produced or manufactured locally, or the theoretical possibility of taxation, to avoid the prohibition under Article 304 (a), but the actual production or manufacture of similar goods, that are subject to like or similar tax. Absent this condition, the levy would fall foul of Article 304 (a) since it would constitute an additional burden (the goods already having suffered some form of taxation in the producing state). This interpretation, in my opinion would also further economic progress and the unhindered availability of goods in states which do not have manufacturing capacities and may not be able to develop it, having regard to lack of natural resources or other geographical limitations. It also furthers the aims underlying Article 301 of the Constitution of India.

Conclusion

9. I answer Question No.1 in the negative and I agree with the conclusions drawn by

the Chief Justice. I would also answer Question Nos. 2, 3 and 4 in agreement with the Chief Justice.

[1] 17 US 316 (1819)

JUDGMENT

Shiva Kirti Singh,J.,

1. Since I am in respectful agreement with the judgment by T.S. Thakur, CJI, I do not propose to go into whole gamut of documents, materials, relevant constitutional provisions and the precedents which have already been noticed not only by T.S. Thakur, CJI, but also by N.V. Ramana, R. Banumathi, D.Y. Chandrachud, and Ashok Bhushan, JJ. in their separate detailed judgments, which I had the privilege to go through.

2. While recording my agreement with judgment of T.S. Thakur, CJI and other similar views, in the light of some of the differing judgments, I feel it necessary to underline my understanding of the core issues and why they need to be answered in a particular way.

3. The basic issue which has generated the present litigation arises out of a challenge to various taxing statutes enacted by several States to impose Entry Tax on goods in exercise of specific power available to the State legislature under Entry 52 of List II in the 7th Schedule of the Constitution. If the Constitution Bench judgments in Atiabari's case and in Automobile Transport's case were not under doubt, then as per majority view in Atiabari's case one was required to apply the test of "direct or immediate" effect of Entry Tax. If it restricts freedom of trade and commerce, it had to be struck down. Since such a view did not permit certain levies imposed by the State legislature to provide better facilities for interstate trade and commerce, the concept of regulatory and compensatory taxation was advanced as a permissible exception, by the majority view in Automobile Transport case. The purpose was to reconcile the freedom of trade and commerce stipulated by Article 301 with the need of resources for the States through imposition of taxes on trade and commerce. Such tax was held permissible if it was to provide facilities which would improve and help freedom of trade and commerce through activities such as construction and upkeep of roads and other similar facilities.

4. As discussed in detail in the other judgments, ultimately States felt the need to exercise their legislative power to impose taxes even for general welfare measures and police duties. Resultantly it became more and more difficult to justify such tax as compensatory tax and such attempts brought excessive strain on the very concept of regulatory and compensatory tax. On the one side Trade and Industry seriously criticised such attempts, inter-alia, on the ground that it blurs the distinction between compensatory tax and regular tax. On the other hand, the States comprising the Indian Union are clearly unhappy with the law settled in Atiabari's case as well as in Automobile Transport case which permits them to impose taxes affecting freedom of trade and commerce but on the condition that it is actually by way of a fee, justified by some sort of quid pro quo.

5. In the above factual background the heavy burden that has befallen on this nine Judges Bench is to interpret Articles 301 to 304 comprising Part XIII of the Indian Constitution in a manner which is justified both by the text as well as the historical context and also effects the desired balance between the need of the country to have free movement of trade and commerce on one hand and the sovereign taxing powers of the States given to them by the Constitution on the other. Limitation on such power must be explicit in the Constitution. For safeguarding freedom of trade and commerce, such limitation is to be found only in Article 304(a) of Part XIII of the Constitution.

6. Answering the question No. 1 in the negative or in other words declaring that levy of a non-discriminatory tax per-se does not violate Article 301, in my opinion means that the majority view in respect of limits in imposition of tax through legislation in Atiabari case (supra) as well as in Automobile Transport case is no longer a good law. Since, in the matter of levy of taxes the compensatory theory is no more relevant, the State Legislatures are free to exercise their taxing powers without the need of declaring and showing that taxes imposed by them on outside goods are for the benefit of concerned traders or manufacturers. But such tax must be, in essence, non-discriminatory, both, in the ultimate tax burden and in machinery provisions. To muster compliance with Part XIII of the Constitution, the tax must pass the twin tests embodied in Article 304(a) - (i) Similar goods produced locally must also be subjected to similar tax and (ii) such state action should not attract the vice of discrimination between the two varieties of goods.

7. The entire discussion in my view leads to a fair conclusion that the views summarized by Sinha, CJI in paragraph 18 of his judgment in Atiabari case depict the law emanating from Part XIII of the Constitution in the correct perspective. However same cannot be said of observations in paragraph 16 where His Lordship used the expression - “If a law is passed by the legislature imposing a high tariff wall assumes the character of a trade barrier which it was the intention of the Constitution makers to abolish by Part XIII.” These observations do create practical difficulties of insurmountable proportions. Hence these deserve to be treated as obiter or interpreted in the light of the entire passage, to mean such taxes which impose an impediment to the free flow of trade, commerce and intercourse by creating discriminatory tariff wall/trade barrier (emphasis supplied). For Part XIII there can be no real impediment through tax unless the so called wall or barrier is one of hostile discrimination between local goods and outside goods.

JUDGMENT

N .V.Ramana,J.,

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PART - I : INTRODUCTION

1.1. I have had the privilege of going through the draft judgments prepared by the learned Chief Justice T.S. Thakur and my brother/sister judges. I am broadly in agreement with the conclusion of the learned Chief Justice on most of the issues. The erudite draft judgment of learned Chief Justice would in the usual course may not have warranted another concurring judgment. But when a Bench of nine judges of this Court has been assembled to consider the seminal issues that have been bothering the nation for about fifty years and such issues have been debated in the Court over a period of four weeks, many aspects having a bearing, canvassed about a constitutional question, a concurring judgment cannot be treated as a repetitive burden or a superfluous legal exercise[1]Therefore I propose to deliver a brief judgment concurring with the judgment of the learned Chief Justice, giving my own reasons.

1.2. As a caveat, I may mention that the contentious matter herein is important not only from the legal point of view but also for a common man who ultimately bears the tax burden. Secondly in constitutional matters, judgment with clarity is preferable to a judgment of wandering complexities. It is appropriate to quote ***Lord Denning***[2] He said- '...I avoid long

[1] *Journey Started from Atiabari Tea Co., Ltd. V. The State of Assam and Ors., A.I.R 1961 S.C 232 [hereinafter 'Atiabari']; continued in Automobile Transport (Rajasthan) Ltd. V. The State of Rajasthan, A.I.R 1962 S.C 1406 [hereinafter 'Automobile']. Doubted for first time in G. K. Krishnan v. State of Tamil Nadu, A.I.R 1975 S.C 583 [hereinafter 'GK Krishnan']. Dilution of compensatory took place in Bhagatram Rajeev Kumar v. CIT, MP, 1995 Supp. (1) S.C.C 673 [hereinafter 'Baghatram'] and State of Bihar v. Bihar Chamber of Commerce and Otr., (1996) 9 S.C.C 136 [hereinafter 'Bihar Chamber of Commerce']. Further went back to old formulation in Jindal Stainless Ltd. And Anr. V. State of Haryana and Ors., A.I.R 2006 S.C 2550 [hereinafter Jindal (2)]. Referred to larger Bench in JaiprakashAssosiates v. State of MP, 2009 (7) S.C.C 339 [hereinafter 'Jaiprakash']; further Constitution Bench has referred the matter before us in Jindal Stainless Ltd. And Anr. V. State of Haryana, 2010 (4) S.C.C 595 [hereinafter 'Jindal (3)']*

sentences like the plague: because they lead to obscurity. It is no good if the hearers cannot follow them... I refer sometimes to previous authorities. I have to do so because I know people are prone not to accept my views unless they have support from the books. But never at much length. Only a sentence or two. I finish with a conclusion -

and epilogue - again as the chorus does in Shakespeare. In it, I gather the threads together and give the result'.

(emphasis supplied)

Although I have tried in this Judgment to keep it as simple as possible yet sometimes legal jargon becomes unavoidable to keep the essence of the law.

1.3. As detailed by the learned Chief Justice below the referral order formulated as many as twelve (12) questions. Nonetheless on very first day with the consent of the learned counsels, we reframed these questions as under-

1. Can levy of a non-discriminatory tax per se constitute infraction of Article 301 of the Constitution of India?

2. If the answer to Question No.1 is in the affirmative, can a tax which is compensatory in nature also fall foul of Article 301 of the Constitution of India?

3. What are the tests for determining whether the tax or levy is compensatory in nature?

4. Is the entry tax levied by the states in the present batch of cases is violative of Article 301 of the Constitution and in particular have the impugned State enactments relating to entry tax to be tested with reference to Articles 304(a) and 304(b) of the Constitution for determining their validity?

PART II : CASE HISTORY

2.1 Let me take up the first case in the batch of appeals (Civil Appeal No. 3453 of 2002 (Jindal Stainless Steel Ltd. v. State of Haryana). On May 5, 2000, the State of Haryana issued the Haryana Local Area Development Tax Ordinance, 2000 (Ordinance No. 10 of 2000). The Ordinance was later replaced by the Haryana Local Area Development Tax Act, 2000. Therein, a provision was made for levy and collection of tax on entry of goods into local area. The validity of the said Act was challenged on the ground that it violated Articles 301 and 304 of the Constitution. C.W.P. No. 6630 of 2000 (Jindal Strips Limited v. State of Haryana) and connected petitions were dismissed by the ***High Court on December 21, 2001[3].*** Following the judgments of this Court, inter alia, in Bhagatram and Bihar Chamber of

[2] *Lord Denning, Family Story, p. 207 (1999) the hearers cannot follow them… I refer sometimes to previous authorities. I have to do so because I know people are prone not to accept my views unless they have support from the books. But never at much length. Only a sentence or two… I finish with a conclusion - and epilogue - again as the chorus does in Shakespeare. In it, I gather the threads together and give the result'.*

Commerce, the High Court upheld the validity of the said Act. It was held that the entry tax was compensatory as per parameters laid down by this Court in the said judgments and thus, did not violate Articles 301/304 of the Constitution. On appeal to this Court, the matter was referred to the Constitution Bench in Civil Appeal No. 3453 of 2002 vide order dated September 26, 2003. The said order is reported as Jindal Stripe Ltd. v. State of Haryana *[hereinafter 'Jindal (1)']* [4]. On April 13, 2006, the Constitution Bench

delivered its judgment in Jindal (2), and reversed the earlier judgments in Bhagatram and Bihar Chamber of Commerce. The Constitution Bench laid down the ingredients of compensatory tax as being value of direct, measurable and quantifiable special benefits provided by the State to tax-payers on the basis of equivalence. The matter was thereafter placed before a Division Bench of this Court for decision in the light of judgment of the Constitution Bench. On July 14, 2006, the Division Bench of this court in its order in *Jindal Stainless Ltd. v. State of Haryana*[5] , observed that relevant data had not been placed before the High Court for determining the nature of tax and asked the High Court to deal with the basic issue whether the levy was compensatory in nature. Accordingly, the State filed data by means of affidavits and vide order dated March 14, 2007 (reported as Jindal Strips Limited v. State of Haryana, a Division Bench of High Court held that the levy was not compensatory in character and amounted to restriction on free flow of trade and commerce and violated Articles 301 and 304 of the Constitution of India. On April 16, 2008, the State of Haryana repealed the 2000 Act and enacted the Haryana Tax on Entry of Goods into Local Areas Act, 2008, impugned in this Appeal. The High Court in *Indian Oil Corporation v. State of Haryana*[6], declared that the provisions of the Haryana Tax on Entry of Goods into Local Areas Act, 2008 to be unconstitutional and void. The Punjab and Haryana High Court invalidated the Haryana Act, the matters again came to this Court in a connected matter being Jaiprakash Associates[7] (A two judge bench) referred ten questions to the constitutional bench[8].

Questions are-

1.Whether the State enactments relating to levy of Entry Tax have to be tested with reference to both Clauses (a) and (b) of Article 304 of the Constitution for determining their validity and whether Clause (a) of Article 304 is conjunctive with or separate from Clause (b) of Article 304?

2.Whether imposition of Entry Tax levied in terms of Entry 52 List II of 7th Schedule is violative of Article 301 of the Constitution? If the answer is in the affirmative whether such levy can be protected if Entry Tax is compensatory in character and if the answer to the aforesaid question is in the affirmative what are the yardsticks to be applied to determine the compensatory character of the Entry Tax.

3.Whether Entry 52, List II, 7th Schedule of the Constitution like other taxing entries in the Schedule, merely provides a taxing field for exercising the power to levy and whether collection of Entry tax which ordinarily would be credited to the Consolidated Fund of the State being a revenue received by the Government of the State and would have to be appropriated in accordance with law and for the purposes and in the manner provided in the Constitution as per Article 266 and there is nothing express or explicit in Entry 52, List II, 7th Schedule which would compel the State to spend the tax collected within the local area in which it was collected?

4. Will the principles of quid pro quo relevant to a fee apply in the matter of taxes imposed under Part XIII?.

5. Whether the Entry Tax may be levied at all where the goods meant for being sold, used or consumed come to rest (standstill) after the movement of the goods ceases in the `local area'?

6. Whether the Entry Tax can be termed a tax on the movement of goods when there is no bar to the entry of goods at the State border or when it passes through a local area within which they are not sold, used or consumed?

7. Whether interpretation of Articles 301 to 304 in the context of Tax on vehicles (commonly known as `transport') cases in Atiabari's (supra) and Automobile Transport's case (supra) apply to Entry Tax cases and if so, to what extent.

8. Whether the non discriminatory indirect State Tax which is capable of being passed on and has been passed on by traders to the consumers infringes Article 301 of the Constitution?

9. Whether a tax on goods within the State which directly impedes the trade and thus violates Article 301 of the Constitution can be saved by reference to Article 304 of the Constitution alone or can be saved by any other Article?

10. Whether a levy under Entry 52, List II, even if held to be in the nature of a compensatory levy, it must, on the principle of equivalence demonstrate that the value of the quantifiable benefit is represented by the costs incurred in procuring the facility/services (which costs in turn become the basis of re-imbursement/recompense for the provider of the services/facilities) to be provided in the concerned `local area' and whether the entire State or a part thereof can be comprehended as local area for the purpose of Entry Tax?

2.2 One of the questions is whether State enactment relating to levy of entry tax has to

be tested with reference to both Articles 304 (a) and 304(b). When the matter was placed before the constitutional bench along with ***Jindal (3)***[9], the constitutional bench was confronted with the arguments by the State that the tests propounded by the Atiabari and Automobile failed to strike a balance between freedom of trade and commerce under Article 301 and taxing power of the State under Article 246 r/w relevant legislative entries to the Constitution of India. The constitutional bench, found merit to refer to suitable larger bench for reconsideration of Atiabari and Automobile. For doing so support was drawn from *Keshav Mills*[10] *, GK Krishnan, Dawoodi Bora*[11]*.* That's how the matter is before us.

2.3 Entry tax is levied by the State of Haryana under the provisions of Haryana tax on Entry of Goods into Local Areas Act, 2008. Section 3 of the Act contains the charging the provision which states that the tax is levied 'for the purpose of development of trade, commerce and industry and for creation and maintenance of infrastructure facilities for free flow of trade and commerce in State'. Section 25 of the Act provides that the proceeds of the levy shall be appropriated to a fund notified by the Government and shall be exclusively utilized for the development or facilitating the trade, commerce and industry in the State and also inter alia provides benefits towards which the proceeds may be applied. Most of the States in appeal have enacted similar provisions under the impugned enactments.

Part-III : Arguments canvassed

ARGUMENTS OF PETITIONERS/APPELLANTS (ASSESSEE(S))

3.1 Mr. Harish Salve, learned senior counsel argued as below¬ That taxes generally amount to restriction but it is only such taxes that directly and immediately restrict trade that will fall within the Article 301. Applying this test the court can strike down the law as violative of Article 301 unless saved by Article 304(b). The result of reading Article 304(a) and (b) together appears to be that a tax can be levied by State on goods manufactured/produced or imported in the State and thereby reasonable restrictions can be placed on the freedom of trade either with another State or between different areas of the same State. The vital federal safeguard provided in the proviso is pervious sanction of the President. Article 301 operates to restrict legislative power of State. Lastly, he argues that proviso of Article 304 can be read down in appropriate cases. In rejoinder he argues that as Article 304(a) of the Constitution envisages the rule of per se violation there is no question of impact test or comparative tax burden test under it as the text of the same does not accept such interpretation.

3.2 Mr. A. K. Ganguli, his main contentions are The Reference Order to a larger bench to 'reconsider' the decisions in Atiabari and Automobile is not warranted and runs contrary to the settled law laid down by this Hon'ble Court as it constitutes a binding precedent under Article 141 of the Constitution. Regarding the construction of Article 304 of the Constitution he submits that it is inherent in the drafting of the clause (a) itself that both clauses (a) and (b) of article 304 are not mutually exclusive. It is submitted that clause (b) acts as a gateway to protect those laws which don't satisfy the dual conditions laid down in clause (a). Further he supported the concept of compensatory

tax which has stood the test of time.

3.3 Mr. T.R. Andhyarujina, learned senior counsel argues as follows That there is no requirement of reference to a larger bench as there is no public mischief being caused by the prior Judgment. In alternative he submits that the compensatory taxes levied by the States would in a large measure negative the freedom of trade and commerce guaranteed by Article 301 because there is no proof that the State will utilize the tax for the improvement of trade facilities etc. Even assuming a State in the Act that the tax collected will be used for that particular purpose. A declaration to that effect would only mean a clever device to refute the abridgment of free trade. Hence, it is his submission that where a State claims to have imposed a compensatory tax, it should not be permitted to impose a tax without complying with the requirement of Article 304(b). Otherwise according to him all taxes would be outside the purview of the freedom of trade by mere assertion as is done by 22 States that the tax is compensatory.

3.4 Mr. Arvind P. Datar contends That Concept of compensatory tax may be confined to Entry no. 56 and 57 and not applied to any other tax/duty in State List. Further the working test contemplated in Automobile Case has not worked satisfactorily. Neither the "direct or immediate effect" test of Atiabari nor the "working test" of Automobile Case is feasible in practice. He suggested the bench to adopt "Appreciable Adverse Effect on Trade & Commerce [AAETC]" borrowed from section 3 of the Competition Act, 2002. The difference between enactment of AAETC before and after the impugned Law will provide the impact on Trade & commerce. The Burden of Proof will be on the petitioner to establish, prima facie, to prove actual or potential AAETC.

3.5 Mr. S.K. Bagaria, learned senior advocate, Mr. J. Dhankar, learned senior advocate, Mr. N. Venkatraman, learned senior advocate, Mr. R. Srivastava, learned senior advocates, Mr. Dhruv Aggrawal, learned senior advocate, Mr. Gopal Jain, learned senior advocate, Mr. Tushar Mehta, learned Additional Solicitor General, Mr. Dilip Tandon, Smt. Suruchi Aggrawal, Mr. V. Lakshmikumaran for assesses have either adopted the submissions made by the above named advocates or provided alternative reasons for the conclusions reached by the abovementioned advocates.

3.6 Mr. Mukul Rohatgi, learned Attorney General of India submits That that power to tax is an incident of sovereignty provided under specific entries in List II. It is to be noted that such power cannot be suppressed even by the Parliament of India under our Constitution. Part XIII generally does not deal with Taxes except in so far as Article 304(a). Part XIII is only concerned with deliberate discrimination. If discrimination is done for alleviation of economic condition than such a measure would not be covered under the mischief of Article 304(a). Furthermore 304(a) and 304(b) are disjunctive in which only (a) applies to taxes and (b) applied to non-fiscal measures. It is always assumed taxes are imposed in public interest and is reasonable. Therefore inclusion of taxes under Article 304(b) would be an exercise in redundancy which will never be the intention of our Constitution framers. Therefore, Sovereign power of the State cannot be made a plaything of Executive. Federalism is to be disjointed from economic unity. Part XIII and Part III are at different pedestal. Part III is individualistic in nature and has sufficient remedies to cover excessive taxation and other burdens. Moreover, Hon'ble

C.J Sinha's View in Atiabari has not required any reconsideration and the same should be followed even by this court. He submits that any test under article 301 will have to draw a line as to when taxes become Trade barriers. Such examination by Courts is not warranted. Part XIII has its origin in section 297 of Government of India Act 1935. It is to be noticed that earlier Article 301 was present as Article 16 under Part III of Constitution which was subsequently taken out. The source of Power to tax is present both under Article 245 as well as Article 246. We should not separate Article 246 and read taxing power only under 246. He argues that our Constitution is organic and flexible document which was considerate about providing level playing field to various States. He lastly argues that Video Electronic Case should be upheld.

ARGUMENTS OF RESPONDENTS (STATES/AUTHORITIES)

3.7 Mr. P. P. Rao, learned senior counsel contends that scope of Entry 52 of the State List cannot be reduced. Discrimination only arises if goods are available. If no tax can be imposed on the ground that there is no production that consumer state loses their revenue and the same is detrimental to the existence of very State itself. Therefore, the interpretation that sub-serves the intent and autonomy of State should be adopted in a Federal Constitution. that 304 (a) is not a part of 301 and the only restriction on imposition of tax is article 304(a) of Constitution. He argues that inclusion of taxes under article 304(b) was never argued before the bench of Atiabari. The observation in Atiabari is per in curium as there was no discussion or deliberation regarding the same.

3.8 Mr. Rakesh Dwivedi, learned counsel submits¬> That Part XIII is not a basic feature of the Constitution and every provision of Constitution though important cannot be elevated to the pedestal of basic feature. Economic Unity is not defined and for trade, commerce and intercourse political unity is equally important. If Article 19(1)(g) is explicitly given to citizens, Article 301 cannot be expanded to give same right to foreigners. "Free" in Art 301 does not mean free from Taxation. "Subject to" is the dominant expression in Art 301 and indicates subservience to at least Art 302, 303 and 304. Art 302-304 are mere restatement of powers under Art 246 r/w VII schedule with some limitations. Each restated power by itself overrides the freedom in Art 301. The equation between compensatory tax and fee is inconsistent with the Scheme of our Constitution which specifically draws distinction between two concepts.a m The judgments of Atiabari and Automobile erred in reaching the concepts of direct and immediate impediment and compensatory Tax. Further subjecting taxing power to executive clearance under Article 304(b) will not be justifiable as assent of the President cannot be reviewed.

3.9 Mr. Shyam Divan, learned senior counsel argues thatThe wordings of Article 301 are free from protectionist barriers. Tax is obviously a restriction which would require this court to examine the height of the barrier on a case to case basis.

3.10 Mr. Dinesh Dwivedi, learned senior counsel, Mr. S. V. Giri, learned senior counsel, Mr. A. K. Sinha, learned senior advocate, Mr. J. K. Gilda, learned Advocate General of State of Chhattisgarh, Mrs. Madhvi Divan, assisting the learned Attorney General of India, Mr. Devdutt Kamath, learned Additional Advocate General for the State of

Karnataka, Mr. S. S. Shamshery, learned Additional Advocate General for the State of Rajasthan, have either adopted the submissions made by the above named advocates or provided alternative reasons for the conclusions reached by the abovementioned advocates.

PART - IV : NEED FOR REVIEW

4.1 The learned counsel for the dealers/assesses argued for rejection of the reference itself. Shri T.R. Andhyarujina and Shri A.K. Ganguli, Learned Senior Counsel submitted that the doctrine of direct and immediate effect as well as compensatory tax which furnish a workable test vis-a-vis validity of a tax law in the context of inter-State trade are sound. Therefore, there is no need to review the decisions in Atiabari and Automobile. They would urge that these two decisions have been followed by this Court in half a dozen judgments and by various High Courts, and therefore, the ratio therein acquired the status of stare decisis. According to them, in the absence of any compelling changes in the Constitution or the law, the reference may not be necessary. They would point out that after the decision in Automobile, every State which made law for the levy of tax on entry of goods, declaring such tax to be compensatory so as to save such law from the effect of Articles 301 and 304 of the Constitution. We have given our earnest and anxious consideration to these submissions and are not able to agree with any of these contentions.

4.2 This Court has over-ruled approximately 60 Constitutional judgments in its 60 years of ***existence***[12]***,*** which is an impressive rate in itself, considering the fact that our nation is comparatively young and is developing jurisprudence in many aspects. Further it is interesting to note that there are only Seventeen Judgments of this Court with nine or higher ***bench strength***[13]. It is further important to note that most of the times nine judge bench decisions have led to change in law by legislative measure like ***Madhav Rao Scindia***[14] , ***R.C. Cooper***[15] etc. All this points out that the exercise of constituting higher bench strength has

[12] *A. Lakshminath, Precedent in India (3rd Ed.) p. 178 (2009)*

[13] *In re Sea Customs Act, A.I.R 1963 S.C 1760 (9 judge bench); State Trading Corp. of India Ltd. v. CTO, A.I.R 1963 S.C 1811 (9 judge bench); Golaknath v. State of Punjab, A.I.R 1967 S.C 1643 (hereinafter 'Golak Nath') (11 judge bench); Naresh ShridharMirajkar v. State of Maharastra, A.I.R 1967 S.C 1 (9 judge bench); Suptd. And Remembrancer of Legal Affair v. Corp. of Calcutta, A.I.R 1967 S.C 997 (9 judge bench); RC Cooper v. UOI, (1970) 1 S.C.C 248 (11 judge bench); Madho Rao JivajiScindia v. Union of India, (1971) 1 S.C.C 85 (11 judge bench); Kesavananda Bharti v. State of Kerala, 1973 4 S.C.C 225 (hereinafter Keshavananda Bharti) (13 Judge bench); Ahmedabad St. Xavier Collage Society v. State of Gujarat, (1974) 1 S.C.C 717 (9 judge bench); Indira Sawhney v. Uol, 1992 Supp. (3) S.C.C 215 (9 judge bench); Supreme Court Advocates on Record Association v. Uol, (1993) 4 S.C.C 441 (9 judge bench); SR Bommai v. Uol, (1994) 3 S.C.C 1 (hereinafter 'S.R. Bomnai')(9 judge bench); Attorney General of India v. AmritlalPrajvandas (1994) 5 S.C.C 54 (9 judge bench); Mafatlal Industries v. Uol, 1997 (5) S.C.C 536 (9 judge bench); NMDC v. State of Punjab, (1997) 7 S.C.C 339 (9 judge bench); TMA Pai Foundation Case, (2002) 8 S.C.C 481 (11 judge bench); I.R. Coelho v. State of TN, (2007) 2 S.C.C 1 (9 judge bench)*

taken place where there is grave need for settling the issue which caused grave mischief to the general-public at large. These numbers speak of restraint in over-ruling its own decisions. When Atiabari was decided, States sovereign power to levy tax within its permissible Constitutional competence stood curtailed. Probably, for this reason, two years after the decision in Atiabari came the decision in Automobile on the premise that the ruling in Atiabari was insufficient. Indeed, Automobile added new dimension to the

tax by introducing the doctrine of compensatory tax which is very conspicuous in the Constitutional scheme by its absence. The judicial innovation of compensatory tax was seemingly to unfetter the State's power to some extent the levy of taxes on entry of goods. There is no gainsaying that Part XIII nowhere, much less Article 301 either expressly or impliedly contemplate compensatory tax. The workable test of compensatory tax to comply with the Constitutional principle was doubted within a decade of the decision in G.K. Krishnan (1974), followed by the decisions in Bhagat Ram and Bihar Chamber of Commerce. From 1960 to 1996, there remained uncertainty with regard to the power of the State to levy tax as per entry 52 of the State List and principle of compensatory tax to immunize such entry tax from the perceived injunctive rigor of Articles 301 and 304(a). Thus, it would not be sound to argue that the principle laid down in Atiabarithat is "direct and immediate effect" and doctrine of "compensatory tax" evolved in Automobile attained any finality. Further even in Jindal (2), the aspect of compensatory tax was doubted by Justice S. H. Kapadia also (as his lordship then was). Therefore, this cannot be a ground to doubt the sound reasoning in the referral order of five Judges Bench of this Court in Jindal (3). Thus there is a need for review.

PART-V CONSTITUTIONAL INTERPRETATION

RBI v. Pearless General Finance, A.I.R 1987 S.C 1023

5.1 The resolution of constitutional litigation ultimately rests upon the plain language of the text. In the event of vagueness in the language or when the language is capable of two different meanings it is not a bar to ***analyze the context***[16]**.** In interpreting the constitutional text the court may not feel shy of using all the tools and employing all the aids of construction. The Learned Chief Justice has elaborately analyzed various provisions in Part XIII and dealt with contextual aspects to see whether the contextual aspects match the textual. I am in respectful agreement with the nine postulations summarized by the Learned Chief Justice regarding the purport of Article 301, 302, 303 and 304.

5.2 Apart from the general principles of interpretations in my considered opinion, the relevant provisions of the Constitution especially those relating to legislative powers, the provisions limiting those powers, the external aids like Constituent Assembly Debates, other documents and the precedents are required to be considered. Be that as it is, it is a settled proposition that generally the construction of the Constitution must be most beneficial and widest possible amplitude. The court must gather from the spirit of the Constitution and the language must not be construed in a narrow and pedantic manner. In re CP and Berar Act, 1938[17], Gwayer CJ., summed up this principle in the following manner - the Court should seek to ascertain the meaning and intention of Parliament from the language of the statute itself; but with the motives of Parliament it has no concern.... The Constitution is not to be construed in any narrow and pedantic sense.... A broad and liberal spirit should inspire those whose duty it is to interpret it; but I do not imply by this that they are free to stretch or pervert the language of the enactment in the interests of any legal or constitutional theory, or even for the purpose of supplying omissions or of correcting supposed errors.

5.3 Equally important point is that legislative powers especially taxing powers cannot be tested by implication. Unless there is express limitation on the power of the State to enact the State law, it is not the province of the court to curtail the power of the state by interpretative process. We have reached a stage that every law must be tested with reference to preamble and Directive Principles of State Policy. As held in *Atam Prakash v. State of Haryana [herein after 'Atam Prakash'*[18]*] ,* if preamble is the guiding light Directive Principles of State Policy is the book of interpretation, this was lucidly explained in Atam Prakash.

> "The Preamble embodies and expresses the hopes and aspirations of the people. The Directive Principles set out proximate goals. When we go about the task of examining statutes against the Constitution, it is through these glasses that we must look, 'distant vision' or 'near vision'. The Constitution being sui-generis, where Constitutional issues are under consideration, narrow interpretative rules which may have relevance when legislative enactments are interpreted may be misplaced. Originally the Preamble to the Constitution proclaimed the resolution of the people of India to constitute India into 'a Sovereign Democratic Republic' and set forth 'Justice, Liberty, Equality and Fraternity', the very rights mentioned in the French Declarations of the Rights of Man as our hopes and aspirations. That was in 1950 when we had just emerged from the colonial-feudal rule. Time passed. The people's hopes and aspirations grew. In 1977 the 42nd amendment proclaimed India as a Socialist Republic. The word 'socialist' was introduced into the Preamble to the Constitution. The implication of the introduction of the word 'socialist', which has now become the center of the hopes and aspirations of the people a beacon to guide and inspire all that is enshrined in the articles of the Constitution, is clearly to set up a "vibrant throbbing socialist welfare society" in the place of a "Feudal exploited society". Whatever article of the Constitution it is that we seek to interpret, whatever statute it is whose constitutional validity is sought to be questioned, we must strive to give such an interpretation as will promote the march and progress towards a Socialistic **Democratic State.' "**[19]

5.4 Our constitutional history shows that we at one point had rigorously defended individualistic rights [for ex. Right to Property]. Slowly we have moved towards community rights by invoking Directive Principles of State Policy as a tool to judicially interpret Part III of the Constitution. Directive Principles of State Policy is a normative goal in the Constitution. Such important part cannot be restricted to only Part III interpretation and reduced to two wheels of ***Chariot***[20] rather it is like a bright sun which should shine in every part of the Constitution.

[19] Ibid.

5.5 Before consideration of legal aspects, we need to passingly refer to certain factual scenarios which may be pertinent to the issues of economic unity, balanced growth and development of all regions of India. India that is Bharath is said to be a Country with economic unity. But such assertion cannot be sustained for the reason that 82.5° Meridian or Indian Standard Time line seems to starkly divide India broadly as affluent

West and destitute East. Top 5 states share 44.87% of **India's total economy**[21]. Five states of South **India share 25.98%**[22]. Eight States of North-East India share only 2.64% of **economy**[23]**.** 13 States/UTs have Gross State Domestic Product less than ***Rs. 1 lakh Crore***[24]***.*** While the growth in 2013-14 in Maharashtra was pegged at 8.71% while Rajasthan recorded mere 4.6% growth at **2004-2005 prices**[25]**.** As per Tendulkar formulation Bihar has 54.4% population below poverty line while ***Jammu Kashmir has only 13.2%***[26]. Population in Uttar Pradesh was pegged at 199,812,341 while Kerala is 33,406,061, as ***per Census 2011***[27]***.*** Literacy Rate in Kerala is 94% while in ***Bihar its 61%***[28]***.*** Sex ratio in Kerala is 1084 while in ***Haryana is 879***[29]***.*** In Andhra Pradesh 12.04% live in slums whereas in Assam only 0.63% live in ***slums.***[30] The Utility of the Union to attain political and economic prosperity does not reflect in the figures or statistics so portrayed above. All is not lost in what we have achieved. We have stood with each other and for what is right? We have enacted laws and struck them down for right reasons. We have been beaten down but never gave up. We have braved poverty and hunger. We have cared about neighbors and have strived to be a welfare State. We have constructed great many things and achieved many more. We have advanced on scientific fronts and reached distances in universe which were unfathomable five decades back. We have earned a respectable name in the international scenario. We have produced great artists, many leaders and great men. We were not scared so easily by any adverse situation. First step in solving any problem troubling the present is recognizing that there is one India but India as a union of States. States being independent entities under the Constitution require resource to perform their duties under the Constitution.

[21]NITI Aayog (last visited on 15.10.2016):
http://niti.gov.in/state-statistics . Relevant table is
http://niti.gov.in/content/gsdp-constant-2004-05 prices-2004-05-2014-15

[22]Ibid.

[23]Ibid.

[24]Ibid.

[25]NitiAayog, GSDP and at constant prices, percent growth available at table (last visited on 15.10.2016):
http://niti.gov.in/content/gsdp-constant2004-05 prices-percent-growth-2004- 05-2014-15

[26] Tendulkar committee report. The table is available at PRS website (last visited on 15.10.2016), http://www.prsindia.org/theprsblog/? tag=tendulkar-committee

[27] Uttar Pradesh, Census of India (last visited on 15.10.2016)
http://censusindia.gov.in/2011census/censusinfodashboard/stock/profil es/en/IND009_Uttar%20Pradesh.pdf
Kerala http://censusindia.gov.in/2011census/censusinfodashboard/stock/profil es/en/IND032_Kerala.pdf

[28] (last visited on 15.10.2016)
http://censusindia.gov.in/2011-prov-results/data_files/india/Final_PPT_2011_chapter6.pdf

[29] Kerala State Profile, Census of India (last visited on 15.10.2016)
http://censusindia.gov.in/2011census/censusinfodashboard/stock/profiles/en/IND032_Kerala.pdfHaryana state profile, Census of India
http://censusindia.gov.in/2011census/censusinfodashboard/stock/profiles/en/IND006_Haryana.pdf

[30] (Last visited on 15.10.2016) http://www.census2011.co.in/slums.php.

5.6 Before a detailed discussion on legal fronts of this Case it is necessary to consider certain Constitutional principles and ethos. On considering the scheme of the Constitution, the power of Union and State are parallel. The Parliament as a super-

legislature over State assemblies cannot be accepted. On legislative front, demarcation of power is apparent from the language of Article 246 read with VII Schedule of the Constitution. People have vested the power in States to administer and provide welfare measures. For this process it is the State Government which has been elected by the people to administer by taking into consideration priorities and peculiarities of that particular region.

5.7 This Constitutional principle should not be ignored while imposing restrictions on the State. While feeling happy that we are one nation, we must not ignore the State rights. The facts and realities cannot be forgotten in the first place. The Union does not exist in isolation rather it is a co-operative association of the States. Taking into consideration of various problems faced and differences which exists between the States, importance of State's power to tax cannot be ignored or stifled. Poverty, unemployment, backwardness and adverse climate etc. are running amok within our Country. Natural calamities, insurgencies and
extremism are confronted by certain States. Over-growth and industrialization have taken place only in some places whereas rest of the country is reeling under under-development because of various facts such as geographical positioning, colonial establishments and discriminatory policies that have resulted in concentration of wealth in only certain affluent areas. No State, in this grand Union, should be made to feel discriminated and embarrassed because of the mere fact that history has not been congenial to them and have remained
under-developed. Any restriction imposed should not come in the way of natural development of a State on the ground that it creates barriers for free movement of the goods and trade. All States must be provided an equal level playing field for development and opportunities. This was the grand intention of the framers of our Constitution to not make a ***lassiez faire State***[31] Determined to make our Country a co-operative federalist, our framers set definite rules to achieve the objective. Through interpretation, Constitution cannot be re-constructed so that the goal envisaged by our framers will be more fully achieved by such construction. Such measure would not be justified in light of clear demarcation of functions bequeathed by our Constitution.

Constituent Assembly Debate, Vol. IX, September 8, 1949.

5.8 The Union and the States are co-equal in the Indian Federal structure. Our framers created a unique federal structure which cannot be abridged in a sentence or two. The nature of our federalism can only be studied having a thorough understanding of all the provisions of the Constitution. Confirmation that the Union and States are co-equals in the Indian federal structure. can be found in the speeches of Hon'ble P.S. Deshmukh, Shri T. T. Krishnamachari and Hon'ble ***Dr. B. R. Ambedkar***[32] before the Constituent Assembly. Common

[31] *Constituent Assembly Debate, Vol. IX, September 8, 1949.*

philosophy which runs through our Constitution is that both Center and States have been vested with the substantial powers which are necessary to preserve our unique federation with clear demarcation of power. Calling India as quasi-federal might not be advisable as our features are unique and quite different from other Countries like United States of America etc. Courts in India should strive to preserve this unique balance

which our framers envisaged, any interference into this balancing act would be detrimental for grand vision ***proscribed by our makers***[33]***.*** Amphibious nature of our federalism has been even noted by the SarkariaCommission Report on Center-State relationship. Co-operative federalism envisaged under our Constitution is a result of pick and choose policy which our framers abstracted from the wisdom of working experience of other Constitutions. Some Judgments which are illustrative of nature of federalism in India are (i)West Bengal (6 Judge Bench), a case relating to the power of Union to acquire land and right in and over the land, which are vested in State. This case produced two opinions, one by C. J. B.P. Sinha (majority opinion) and other by K. Subba Rao J. (dissenting opinion). As per the majority, there is undoubtedly distribution of powers between the Union and the States in matters legislative and executive; but distribution of powers is not always an index of political sovereignty. The exercise of powers legislative and executive in the allotted fields is hedged in by numerous restrictions, so that the powers of the States are not coordinate with the Union and are not in many respects independent. Minority Judgment held that the Indian Constitution accepts the federal concept and distributes the sovereign powers between the co-ordinate constitutional entities, namely, the Union and the States. This concept implies that one cannot encroach upon the

governmental functions or instrumentalities of the other, unless the Constitution expressly provides for such interference. In (ii) *Kesavanada Bharathi v. State of Kerala [hereinafter 'Keshvanada Bharathi']*[34]*,* majority held that the power conferred under Article 368 of the Constitution was not absolute. They took the view that by an amendment, the basic structure of the Constitution cannot be damaged or destroyed. And, as to what are the basic structures of the Constitution, illustrations were given by each of these Judges. They include supremacy of the Constitution, democratic, republican form of Government, secular

[32] *There is only one point of Constitutional import to which I propose to make a reference. A serious complaint is made on the ground that there is too much of centralization and that the States have been reduced to Municipalities. It is clear that this view is not only an exaggeration, but is also founded on a misunderstanding of what exactly the Constitution contrives to do. As to the relation between the center and the States, it is necessary to bear in mind the*

fundamental principle on which it rests. The basic principle of Federalism is that the legislative and executive authority is partitioned between the center and the States not by any law to be made by the center but the Constitution itself.This is what the Constitution does. The States, under our Constitution, are in no way dependent upon the center for their legislative or executive authority. The center and the States are CO-EQUAL in this matter.It is difficult to see how such a Constitution can be called centralism. It may be that the Constitution assigns to the center too large a field for the operation of its legislative and executive authority than is to be found in any other Federal Constitution. It may be that the residuary powers are given to the center and not to the States. But these features do not form the essence of federalism. The chief mark of federalism, as I said lies in the partition of the legislative and executive authority between the centre and the Units by the Constitution. This is the principle embodied in our Constitution.

(Emphasis Supplied)

[33] *State of West Bengal v. Union of India, [1964] 1 S.C.R 371 [hereinafter 'West Bengal'], S. R. Bommai, State of Karnataka v. Union of India and Anr., [1978] 2 S.C.R1, (Special Reference No. 1 of 1964) AIR 1965 SC 745, ITC Ltd. v. Agricultural Produce Market Committee and Ors, (2002)1 S.C.R 441 [hereinafter 'ITC'].*

character of the Constitution, separation of powers among the legislature, executive and judiciary, the federal character of the Constitution, Rule of Law, equality of status and of opportunity; justice, social, economic and political; unity and integrity of the nation and the dignity of the individual secured by the various provisions of the Constitution. In (iii) S.R. Bommai, this Court while determining the constitutional validity of emergency

proclamations issued by the Centre in various States observed that federalism, as understood by the American Scholars is absent in Indian Constitution which is more of a hybrid of pure federalist character and pure unitary character. However, the distribution of powers must not be rubbished out as being absent. It was observed by Ahmadi J. that in order to maintain the unity and integrity of the nation our founding fathers appear to have leaned in favour of a strong Centre while distributing the powers and functions between Centre and the States. But the essential characteristics can be understood by knowing the "effects" of such a system. As per Sawant and Kuldip Singh JJ: The features in the Constitution which provide the Centre with overriding powers over the states is only an exception and are not normal features of the Constitution. K. Ramaswamy J., observed that Indian Federalism places the nation as a whole under control of a national Government, while States are allowed to exercise their sovereign power within their legislative sphere. As per Jeevan Reddy and Agrawal, JJ. the bias in favour of the Centre does not make the states mere appendages of the Centre. States are supreme in the sphere allotted to them. The ultimate conclusion reached by this Court was that the fundamental feature of federalism being that irrespective of each list, each legislature is supreme. In (iv) ITC, the majority led by Justice Ruma Pal held that the Constitution of India deserves to be interpreted in a manner that it does not whittle down the powers of State Legislatures and preserves the federalism while also upholding the central supremacy as contemplated by some of the Articles. In (v*) State of West Bengal v. Kesoram Industries Ltd.*[35], it was concerned with Entries 52, 54 and 97 in List I and Entries 23, 49, 50 and 66 in List II of the Seventh Schedule to the Constitution of India as also the extent and purport of the residuary power of legislation vested in the Union of India. Wherein it was observed therein that federalism is one of the basic pillars of the Indian Constitution and that having regard to Articles 245, 248, 250, 256, 257, 356 and Entry 97 in list I of the seventh Schedule of the Constitution, it is not possible to say that India is not a subscriber to federalism but although having unique federal character it can, be said to be quasi-federal or hybrid federal State. Thus constitutional courts have interpreted that India has a federal polity and that each State has independent constitutional existence assigned with important role of Constitutional governance.

5.9 In view of these aspects, we need to consider the controversies in these cases and interpret relevant provisions of the Constitution in light of following rules and principles, which are-

> "1. That Directive Principles of State Policy should be utilized for interpreting every part of the Constitution. and
>
> 2.In a federal Constitution, an interpretation which preserves the State's power should be preferred."

PART-VI :INTRODUCTION TO TAXATION AND ITS IMPORTANCE

6.1 The States in the modern era are not strictly confined to political activities and law making functions. They function in a welfare society. Such working of States was visualized by our framers also, who were aware of responsibilities a State must

shoulder and discharge. This is the very reason for existence of Directive Principles of State Policy and which sets normative and positive standards for the Government. When the State is burdened with such normative goals as its primary responsibility, such activities are inevitably dependent on availability of monitory resources. The definition of Sovereignty has acquired a new flavor in the recent past, 'Sovereignty is responsibility'. In a democratic system the elected Governments are always responsible for its people. If there is any high taxation which is affecting their life, this puts pressure on the Governments to reduce taxes and elected Governments are answerable to public every five years. No Government can raise tax which would cause public inconvenience. In this context, Sovereignty is no more endless power, rather it is responsibility. A responsible government in a democracy should always strive to keep taxes as low as possible, so that no heavy burden is placed on the individuals. Although States are empowered to tax under the Constitution, it does not necessarily mean that they should tax at exorbitant rates. Tax is a way of apportioning the cost of government among those who in some measure are privileged to enjoy the benefits and must therefore bear its burdens. Fundamentally the exercise of sovereignty also includes lawful taxation as its incident. Assesses/dealer on the other hand stated that all powers exercised by the state such as police powers, power of eminent domain and power to tax are also incidents of ***sovereignty***[36]. There is nothing which mandates this Court to deny latitude in use of taxing powers in comparison to other similar powers. Although all powers exercised by State are incidents of sovereignty, there is need to treat taxation on a different pedestal to sustain the Government at the current level and to achieve the Constitutional goals set by our framers.

6.2 A tax is a burden or charge imposed by a competent legislature upon persons or property, to raise money for ***public purposes***[37]. Important elements of a tax may be said to be first, that it is a compulsory exaction; secondly, it is payable to the State or to some public authority on its behalf; and thirdly, that it is an exaction for purposes of public interest. Our Constitution has demarcated the taxing powers between the Center and States. Taxing power of the Union as well as the States resides in Article 245 read with 246 of the Indian Constitution. The Article 246 of the Constitution, lays down that Parliament has exclusive power to make laws with respect to any matter enumerated in Union List (List I of schedule VII). The States

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have complete power to make laws with respect to any matter enumerated in the State List (List II of schedule VII) and both Parliament and State Legislature have power to make laws with respect to any matter enumerated in the Concurrent List (List III of schedule VII). As per Article 265, no taxes shall be levied or collected except by the authority of law. It is important to note that taxation entries are to be found only in lists I and II, indicating that in

[36] *Jaganathbaksh Singh v. State of UP, (1963) 1 S.C.R 220; Dena Bank v. BhikhabhaiPrabhudas Parekh & Co., (2000) 5 S.C.C 694; Commissioner of Income Tax, Udaipur, Rajasthan v. McDowell and co. Ltd., (2009) 10 S.C.C 755.*

[37] *Cooley on taxation-volume 1, 4th ed., Ch. 2.*

our Constitutional scheme, taxation powers of the Centre and the States are mutually exclusive. There are no Entries in the Concurrent List which gives power of taxation. This being the case, the moment the levy contained in a taxing statute transgresses into a prohibited field, it is liable to be struck down.

PART-VII :FREEDOM OF TRADE, COMMERCE AND INTERCOURSE

7.1 To consider the question as to whether the tax laws come under the ambit of Article 301 vis-a-vis freedom of trade, commerce and intercourse, it is necessary to refer to the constitutional provisions, Constituent Assembly Debates and precedents. To begin with, I will first consider the relevant Articles, by extracting Part XIII verbatim.

PART XIII
TRADE, COMMERCE AND INTERCOURSE WITHIN THE TERRITORY OF INDIA

301. Freedom of trade, commerce and intercourse.— Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.

302. Power of Parliament to impose restrictions on trade, commerce and intercourse.— Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part of the territory of India as may be required in the public interest.

303. Restrictions on the legislative powers of the Union and of the States with regard to trade and commerce.—

(1) Notwithstanding anything in article 302, neither Parliament nor the Legislature of a State shall have power to make any law giving, or authorising the giving of, any preference to one State over another, or making, or authorizing the making of, any discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

(2) Nothing in clause (1) shall prevent Parliament from making any law giving, or authorizing the giving of, any preference or making, or authorizing the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India.

304. Restrictions on trade, commerce and intercourse among States. Not with sta-nding anything in article 301 or article 303, the Legislature of a State may by law—
(a) impose on goods imported from other States or the Union territories any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and

(b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest: Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President.

305. Saving of existing laws and laws providing for State monopolies.— Nothing in articles 301 and 303 shall affect the provisions of any existing law except in so far as the President may by order otherwise direct; and nothing in article 301 shall affect the operation of any law made before the commencement of the Constitution (Fourth Amendment) Act, 1955, in so far as it relates to, or prevent Parliament or the Legislature of a State from making any law relating to, any such matter as is referred to in sub-clause (ii) of clause (6) of article 19.

306. [Power of certain States in Part B of the First Schedule to impose restrictions on **trade and commerce.]**[38] Rep. by the Constitution (Seventh Amendment) Act, 1956, s. 29 and Sch.

307. Appointment of authority for carrying out the purposes of articles 301 to 304.—
Parliament may by law appoint such authority as it considers appropriate for carrying out the purposes of articles 301, 302, 303 and 304, and confer on the authority so appointed such powers and such duties as it thinks necessary."

7.2 Needless to mention that when the language of the provision is clear and unambiguous that, the intention of the law makers should be inferred from a plain reading of the provision itself. Ordinarily, we need not go beyond the clear language of the provision to interpret the Statute.
7.3 The freedom of trade, commerce and intercourse throughout the territory of India is assured, but such freedom of trade is subject to Part XIII of the Constitution. When we

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evaluate the impact of Article 301 on the plenary taxing power of the Sovereign State, the opening words become

[38] *Repealed Article 306-*
"Notwithstanding anything in the foregoing provisions of this Part or in any other provisions of this Constitution, any State specified in Part B of the First Schedule which before the commencement of this Constitution was levying any tax or duty on the import of goods into the State from other States or on the export of goods from the State to other States may, if an agreement in that behalf has been entered into between the Government of India and the Government of that State, continue to levy and collect such tax or duty subject to the terms of such agreement and for such period not exceeding ten years from the commencement of this Constitution as may be specified in the agreement : Provided that the President may at any time after the expiration of five years from such commencement terminate or modify any such agreement if, after consideration of the report of the Finance Commission constituted under article 280, he thinks it necessary to do so."

significant. Be that as it may, Article 301 only guarantees throughoutness of trade and commerce, the freedom, however, is not absolute freedom nor is it free from regulations.

7.4 The dissection of Article 301 shows that it has three significant parts or phrases. These are, 'subject to other provisions of this part', and 'Trade, Commerce and Intercourse throughout territory of India', 'shall be free'. Which everway one reads, the plain meaning of this is that trade, commerce and intercourse, shall be free, subject to Articles 302 to 307 of the Constitution. The two sets of the provisions which are mainly

contemplated in the phrase ‘subject to other provisions' are Articles 302, 303 and 304 (a) and (b). Article 303. The Parliament may by law restrict the freedom of trade in public interest and such law would be free from Article 301.

7.5 Article 301 of the Constitution begins with the phrase ‘Subject to other provisions of this Part'. This phrase gives an initial indication as to what to expect? The position of this phrase should be taken into consideration. Even before the declaration of freedom of Trade, Commerce and Intercourse, it is being subjected to limitations. Further the opening words of Article 301, namely, ‘subject to the provisions of this part' require that all the Articles of the Part XIII have to be read together so as to understand the width and meaning of the Part XIII. ‘Subject to' is the dominant expression so far as Article 301 is concerned. It indicates subservience to at least Articles 302, 303 and 304. Articles 302 to 304 embody a restatement of powers under Article 246 r/w the State List under the VII Schedule. Each restated power by itself overrides the freedom of trade in Article 301.

7.6 Article 301 loses its prime place, if States make laws under any of the taxing entries, erecting reasonable restrictions or imposing tax on the free trade. Such power over-rides freedom of trade and commerce. Thus, the general declaration by Article 301 is relaxed in favor of Parliament by Article 302 and in favor of the States by Articles 303 and 304. It is interesting to note that Article 304 starts with a non-obstante clause whereas Article 302 does not have a non-obstante clause. As the freedom of trade in Article 301 is itself subject to 302 and 304, the intention of the framers, to my mind, appears to be clear. The Constitution guards and protects the State legislations under Article 304(a) and (b) from overemphasized effect on freedom of trade under Article 301.

7.7 It is a sound principle of jurisprudence that entire statute has to be construed as a whole and not in isolation. While doing so, no clause in any provision can be ignored especially when we interpret the Constitution which is 'suprema lex’. The difference between the power of the Union and the States vis-a-vis Article 301 is that Article 302 does not have application to tax laws like Article 304(a), but under Article 304(a), tax can be imposed on the goods imported from other States. From the understanding of the Articles 301, 302, 303 and 304, what emerges is summarized below-

> “1. Article 302 is an exception to Article 301.
>
> 2. The limitation under Article 302 is again subject to Article 303.
> 3. Articles 302 and 303 do not refer to laws under taxing entries.
>
> 4. Article 304 can be an exception to be generally construed as dealing with non-tax discriminatory tax and restrictions.”

7.8 In addition to plain reading, an analysis of the relevant provisions and the legislative history of Article 301, is also relevant, in understanding the free trade clause in our Constitution. This can be considered also with reference to Constituent Assembly Debates and the legislative history which are equally important external aids.

7.9 In this connection, it has to be remembered that before the commencement of the Constitution, about two-thirds of India was directly under the British rule and was called 'British India' and the remaining about one third was being directly ruled by the native Princes and was known as 'Native States'. There were a large number of them with varying degrees of sovereignty vested in them. Those rulers had, broadly speaking, the trappings of a Sovereign State with power to impose taxes and to regulate inter-State trade. It is well known fact that many of them had erected trade barriers seriously impeding the free flow of trade, commerce and intercourse, thereby not only shutting out but also shutting in commodities meant for mass consumption. Between the years 1947 and 1950, almost all the Indian States entered into agreements with the Government of India and merged into India as one political unit, with the result that what was called British India, broadly speaking, came under the Constitution. The native States became Part 'B' States. These Part 'B' States, in turn, were some sort of unions of small States or individual princely States. They erected, more often than not, trade barriers and customs posts even amongst themselves. It was in this background, India for the first time, was constituted as one political unit. Hence, it was necessary to abolish all those trade barriers and custom posts in the interest of national solidarity, economic and cultural unity as also of freedom of trade.

7.10 One of the early tasks to engage the attention of the Constituent Assembly in 1947 was freedom of trade and commerce within territories of the Union. It is important to note that in the Draft Constitution, the freedom of trade, commerce and intercourse which was a part of fundamental right, was dropped as such. Basic principles were formulated in the notes submitted to the sub-committee on Fundamental Rights by ***Dr. K.M. Munshi***[39] and SirAlladi ***Krishnaswami Iyer***[40]**.**The Sub-Committee discussed Sir B.N. Rau's draft provision on the subject on March 29, 1947 and was adopted in the following form: Subject to regulation by

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[39] *B. Shiva Rao, The Framing of India's Constitution, Vol.II, p. 69 (1967). [hereinafter 'B. Shiva Rao'] Extract from the Note and draft Articles on Fundamental Rights by Dr. K. M. Munshi, dt. March 17, 1947 – Article V- (1) Every Citizen within the limits of the law of the Union and in accordance therewith has :*
(i)The right of free movement and trade within the territories of theUnion.

[40] *B. Shiva Rao, p. 68 Extract from the Note on Fundamental Rights by Alladi Krishnaswami Iyer, dt. March 14, 1947-*
'The Union powers being restricted in scope, care will have to be taken to bring in (a) the freedom of Inter-state and inter-provincial trade,

(b.) inter-state and inter-provincial movement…'

the law of the Union, trade, commerce, and intercourse among the units, whether by means of internal carriage or by ocean navigation, shall be free: Provided that any unit may by law impose reasonable restrictions thereon in the interest of public order, morality or health.

7.11 Commenting on the Clause when the draft of the sub-committee's report was under Consideration. Sir Alladi Krishnaswami Iyer suggested that goods entering a particular unit from other units of the Union should not escape duties and taxes to which

goods produced in the concerned unit itself were subjected to. These suggestions were accepted by the Sub-committee and incorporated in the report submitted to the Advisory Committee on April 16, 1947. On April 21, 1947 the clause came up for debate before the Advisory Committee. Shri C. Rajgopalchari expressed his view that the units must be allowed to raise some kind of custom duties for genuine revenue purposes, for which the reply of Shri K. M. Panikkar is
relevant for our discussion:

> "K. M. Panikkar: Rajaji (C. Rajgopalchari) has raised the question of the right of the units to raise taxes, and to say this right should not be denied. I, however, think this is dangerous power to be given to the units. This may result in creation of competing units. We have allowed two things. We have allowed the unit to tax its own industries. We also allow things brought in to be taxed, for sake of parity. But our friend wants go little further and say that the right to impose taxes or transit duty or some kind of duty must be given to the units. That, I am afraid, will be a negation of **the clause. "**[42]

7.12 In the interim report of the Advisory Committee dt.23.04.1947 placed by Shri Sardar Vallabhai Patel, the following recommendations were made:

> "While agreeing in principle with this clause we recommend that instead of being included in Fundamental Rights, it should find a place in some other part of the Constitution."

7.13 Taking into consideration above deliberations and decisions of the Assembly, Sir B.N. Rau incorporated the following clause in his draft Constitution of October, 1947 under Part III-Fundamental Rights including Directive Principles of State Policy [42]:-

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[41] *B.Shiva Rao.p.253*

[42] *B.Shiva Rao, p.701*

17. Provided that nothing in this section shall prevent any unit from imposing on goods manufactured or produced in that unit are subject, so however, as not to discriminate between goods so imported and goods so manufactured or produced : Provided further that no preference shall be given by any regulation of trade, commerce or revenue to one unit over another : Provided also that nothing in this section shall preclude the Federal Parliament from imposing by Act restrictions on the units in the interests of public	Freedom of trade, commerce And intercourse among the units. [Cf. Common wealth of Australia Constitution Act. Ss. 92 and 99, Government of India Act, 1935, s. 297

order, morality or health or in cases of emergency. freedom of trade, commerce and intercourse among the	

7.14 With some modifications, this clause was retained in the Fundamental Rights chapter in the draft Constitution of February 21, 1948. The proviso was redrafted and included as an independent Article under a separate heading, namely, "Inter-state trade and commerce" in Part IX of the Draft Constitution pertaining to relations between the *Union and the States*[43].

7.15 Further when the draft Constitution was published and circulated for suggestions and opinions, Sir Alladi Krishnaswami Iyer commented in the following manner:-

> "Comments of AlladiKrishnaswamiAyyar: In this regard to interstate trade there are three main provisions in the Draft Constitution : I. The freedom of inter-state trade secured by Article 16;
>
> II. Subject to an interference by federal law
>
> III. An interference by a provision or state law to the extent *provided in item 33,*[44] ,
> List II. The power of interference under Sub-clause (b) of the Article 244 is too drastic and much wider than that provided in the Original Draft. Would not this provision practically nullify the freedom of trade secured by the Article 16 as the expression 'interests of public is vague and uncertain and cannot be subject to judicial review."

7.16 Draft Articles relating to trade and commerce were scattered in different parts of the draft Constitution (i.e., Clause 16 and Articles 243 to 245) and the purpose was to string together all these scattered provisions under one head. Dr. Ambedkar stated before the Constituent Assembly that :

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[43] *B. Shiva Rao, p. 524 and p. 610*

[44] *Draft of Constitution, February 21, 1948-Seventh Schedule, List II- State List*
33. Regulation of trade, commerce and intercourse with other states for the purposes of the provisions of Article 244 of this Constitution.

> Sir, all that I need do at this stage is to inform the House that originally the articles dealing with freedom of trade and commerce were scattered in different parts of the Draft Constitution. One article found its place in the list of Fundamental Rights, namely, article 16, which said that trade and commerce, subject to any law made by Parliament, shall be free throughout the territory of India. The other articles, namely, 243, 244 and 245 were included in some other part of the Draft Constitution. it was found in the course of discussion that a large number of members of the House were not in a position to understand the

implications of articles 243, 244 and 245, because these articles were dissociated from article 16. In order, therefore, to give the House a complete picture of all the provisions. relating to freedom of trade and commerce the Drafting Committee felt that it was much better to assemble all these different articles scattered in the different parts of the Draft Constitution into one single part and to set them out seriatim, so that at one glance it would be possible to know what are the
provisions with regard to the freedom of trade and commerce throughout India. I should also like, to say that according to the provisions contained in this part it is not the intention to make trade and commerce absolutely free, that is to say, deprive both Parliament as well as the States of any power to depart from the fundamental provision that trade and commerce shall be free ***throughout India.***[45]

(Emphasis Supplied)

7.17 From the above legislative history and Constituent Assembly Debates, four propositions would emerge:-

"a. It is clear from a comparison of Clause 16, 243, 244 and 245 of the draft Constitution with Articles in Part XA (now Part XIII) that they were not merely arranged in seriatim but were substantially altered.

b. That freedom of trade, commerce and intercourse is not a fundamental right
.

c. That trade, commerce and intercourse in India is not absolutely free.

d. That the discriminatory tax (like erstwhile custom duties imposed by certain independent states) is harmful for the federation.

PLAINS OF GANGES CAN NEVER BE FERTILIZED BY WATER OF MURRAY ORPOTMAC RIVERS

7.18 The precedents as well support the view that tax laws are not contemplated in Article 301. Before considering the relevant precedents, a brief reference to the extent and scope of right to free trade as enforced in Australia, USA and Canada may be refereed to. It is to be kept in mind that the plains of Ganges can never be fertilized by waters of *Murray*[46] *or Potmac*[47]

[45] *Constituent Assembly Debate, Vol. IX, 8th September 1949*
[46] *Longest River of Australia*
[47] *River in United States of America*

But it is important to see the course which they have sailed and taken their countries to glory. It is imperative to mention that during the drafting process of Article 301, foot note for the same had reference to Australian Constitution. It is no gainsaying that our framers were learned men who drew our Constitution having hindsight of the wisdom of these great federations.

7.19 The main inspiration for Part XIII has been American and Australian models. These models present before the Constituent Assembly were re-designed and expanded by the framers of the Constitution in India according to the needs of Indians. It is important to note that the interpretation provided by other countries are just

indicative. They may have persuasive value because the context and history has been quite different as compared to India. At least in relation to Part XIII of the Constitution an indigenous interpretation should be provided without placing heavy reliance on the foreign cases as they may be subject to change which will inevitably stir the matter once again. Moreover, our constitutional structure is quite different from those provided under Australian and American Constitutions.

7.20 In Australia and the United States of America, giving textual meaning to the applicable Constitutional provisions, the Courts interpreted the 'commerce clause' or 'free trade clause' in such a manner that the (federal units) were completely barred to levy any taxes on inter-state trade and commerce, Fortunately off late, in these jurisdictions, the law has been diluted to enable the federal units to regulate inter-state trade and commerce even by imposing levies. This would be clear by brief reference to the case law governing inter-state trade in Australia, Canada and the United States of America.

COMMONWEALTH OF AUSTRALIA

7.21 Section 92 of the Australian Constitution declares that 'on the imposition of uniform duties of customs, trade, commerce and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free. *In Cole v Whitfield[Herein after 'Cole']* [48], and later in *CastlemaineTooheys Ltd v South Australia*[49] and, most recently, in *Betfair Pty Ltd v Western Australia*[50], the Court observed that Section 92 of the Australian
Constitution only meant that Australia was free from those measures which were discriminatory and protectionist burdens. Cole insisted that Section 92 proscribes both direct and indirect protectionist discrimination: -

> "'The concept of discrimination in its application to interstate trade and commerce necessarily embraces factual discrimination as well as legal operation. A law will discriminate against interstate trade or commerce if the law on its face subjects that trade or commerce to a disability or disadvantage or if the factual operation of the law produces such a result'. [51]

7.22 Earlier to this, Australian Courts have grappled to achieve uniformity until 1988 [Cole]. Earlier Judgments had taken a right based approach, wherein a single trader who was burdened, could claim violation of Section 92 of the *Australian Constitution*[52]. Such wide interpretation given in the earlier case laws led to development of narrower test by the High Court in Cole. Earlier Case laws were available and were cited in the Atiabari and Automobile also. It is interesting to note that our framers drawing experience of Bank *Nationalization Case* [53], were concerned about stifling the natural growth of the Country by broad law such as Section 92 of Australian Constitution.[54]

UNITED STATES OF AMERICA

7.23 Article 1 Section 8 Clause 3 of the U.S. Constitution states that "The Congress shall have the legislative power to regulate commerce, with foreign nations and among

several States, and with Indian Tribes." This Clause also known as the 'Commerce Clause' has been under judicial scrutiny for a long time. The plain reading of this Article means that the Federal Legislature is empowered to regulate the inter-state trade.

7.24 In *Brown v. Maryland*[55], a case involving the constitutionality of a Maryland law requiring all importers and wholesalers of foreign articles to obtain a license, Chief Justice Marshall reasoned that the rationale of ***McCulloch***[56] was "entirely applicable" to state taxation of private enterprises engaged in inter-state commerce. Thus, holding the Maryland statute unconstitutional, Justice Marshall stated:

> *"'We admit this power (of a State to tax its own citizens on their property within its territory) to be sacred We cannot admit that it may be used so as to obstruct or defeat (Congress') power to regulate commerce. It has been observed that the powers remaining with the States may be so exercised as to come in conflict with those vested in Congress. When this happens, that which is not supreme must yield to that which is supreme'."*

7.25 The Supreme Court in *Freeman v. Hewitt* [57], put a bar on the States to tax such activities which directly affected inter-state commerce as federal government was the sole authority to regulate these matters. Following extract may be relevant- 'The Commerce Clause was not. merely an authorization to Congress to enact laws for the protection and encouragement of commerce among the States, but by its own force created an area of trade free from interference by the States. In short, the Commerce Clause even without implementing legislation by Congress is a limitation upon the power of the States.... This limitation on State power ... does not merely forbid a State to single out interstate commerce for hostile action. A State is also precluded from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between States. It is immaterial that local commerce is subjected to a similar encumbrance'.

7.26 In 1977 in a landmark judgment in Complete *Auto Transit vs. Brady*[58] , the Supreme Court went back on the above approach and adopted practical effects approach, according to which, a State law which is "applied to an activity with a substantial nexus with the taxing state, fairly apportioned, non-discriminatory against inter-state commerce, and fairly related to the services provided by the State" shall not be invalidated on the ground that States lack legislative competence. Subsequently the Supreme Court has further empowered the States
to adopt legislations and it now only requires that there should be a fair relation or connection between the tax imposed and the general benefits provided to the taxpayers which include civic services as maintenance of public roads and running of mass transits (*refer D.H.| Holmes Company Ltd. vs. Shirley McNamara* [59]). In the *Commonwealth Edison Company vs. State of Montana*[60] the Supreme Court has observed that- 'when a general revenue tax does not discriminate against interstate commerce and is apportioned to activities occurring within the State, the State is free to pursue its own fiscal policies unembarrassed by the Constitution.' It is obvious from the line of cases that America has been moving towards empowering States to develop their own fiscal policy under the Commerce Clause. Our Constitution, on the other

hand, has achieved directly what the US Courts are trying to achieve by way of judicial interpretation.

CANADA

7.27 Canadian Constitution envisages freedom of trade under Section 121 as follows 'All Articles of the Growth, Produce, or Manufacture of any one of the Provinces shall, from and after the Union, be admitted free into each of the other Provinces'. It is important to note the federal scheme before referring to interpretation provided by the Courts in Canada. Under Section 92(2) provincial power to tax is restricted by three limitations i. The tax must be 'direct' ii. The tax must be 'within the province' iii. The tax must be for ***'provincial purposes'***[61]. Federal and Provincial powers overlap in the field of direct taxation, which includes the two most lucrative taxes, namely, income tax and the sales tax. Section 121 has been interpreted by the Supreme Court in ***Gold Seal Case (1921)***[62]***,*** In this Case the Supreme Court of Canada speaking through Duff J. observed that: '

> "The capacity of the Parliament of Canada to enact the amendment of 1919 is denied. With this I do not agree. And, first, I am unable to accept the contention founded upon Section 121 of the B.N.A. Act; the phraseology adopted, when the context is considered in which this section is found, shews, I think, that the real object of the clause is to prohibit the establishment of customs duties affecting interprovincial trade in the products of any province of the Union.' [63]

Similarly, Mignault J. stated:

> "'I think that, like the enactment I have just quoted, the object of section 121 was not to decree that all articles of the growth, produce or manufacture of any of the provinces should be admitted into the others, but merely to secure that they should be admitted "free," that is to say without any tax or duty imposed as a condition of their admission. The essential word here is "free" and what is prohibited is the levying of custom duties or other charges of a like nature in matters of interprovincial trade.' [64] "

7.28 The Conspectus of law in Australia and the United States of America which have federal Constitutions would show that initially the highest courts in those countries interpreted their respective constitutional provisions as totally prohibiting the States (federal Units) from levying any tax or regulating on inter-State trade and commerce, but subsequently there is a paradigm shift even in these jurisdictions and currently the existing provisions have been interpreted so as not to deny such powers to States.

INDIAN CASE LAW

7.29 Returning to the main controversy in the case, it may be noted that apart from the two leading judgments on the entry tax and compensatory tax in the context of transportation Cases, we have large number of cases decided by the various High courts and this Court. It is however not necessary to refer to all cases. It would be

suffice to refer to a few.

7.30 In Atiabari, the validity of Assam Taxation (on Goods Carried by Roads and Inland Waterways) Act, 1954, which squarely comes under Entry 56 of List II fell for consideration. It was assailed as violating Article 301, and as not saved by Article 304(b). The challenge was upheld. It is necessary to extract the following from the Atiabari.:

> "It is obvious that whatever may be the content of the said freedom it is not intended to be an absolute freedom; absolute freedom in matters of trade, commerce and intercourse would lead to economic confusion, if not chaos and anarchy; and so the freedom guaranteed by Article 301 is made subject to the exceptions provided by the other Articles in Part XIII. The freedom guaranteed is limited in the manner specified by the said Articles but it is not limited by any other provisions of the Constitution outside Part XIII. That is why it seems to us that Article 301, read in its proper context and subject to the limitations prescribed by the other relevant Articles in Part XIII, must be regarded as imposing a constitutional limitation on the legislative power of Parliament and the Legislatures of the States. What entries in the legislative lists will attract the provisions of Article 301 is another matter; that will depend upon the content of the freedom guaranteed; but wherever it is held that Article 301 applies the legislative competence of the Legislature in question will have to be judged in the light of the relevant Articles of Part XIII; this position appears to us to be inescapable. "
>
> 50. Let us now revert to Article 301 and ascertain the width and amplitude of its scope. On a careful examination of the relevant provisions of Part XIII as a whole as well as the principle of economic unity which it is intended to safeguard by making the said provisions, the conclusion appears to us to be inevitable that the content of freedom provided for by Article 301....
>
> 51. certainly includes movement of free trade which is of the very essence of all trade and is its integral part. If the transport or the movement of goods is taxed solely on the
> basis that the goods are thus carried or transported that, in our opinion, directly affects the freedom of trade as contemplated by Article 301. If the movement, transport or the carrying of goods is allowed to be impeded, obstructed or hampered by taxation without satisfying the requirements of Part XIII the freedom of trade on which so much emphasis is laid by Article 301 would turn to be illusory. When Article 301 provides that trade shall be free throughout the territory of India, primarily it is the movement part of the trade that it has in mind and the movement or the transport part of trade must be free subject of course to the limitations and exceptions provided by the other Articles of Part XIII....Besides, it is not irrelevant to remember in this connection that the Article we are construing imposes a constitutional limitation on the power of the Parliament and State Legislatures to levy taxes, and generally, but for such limitation, the power of taxation would be presumed to be for public good and would not be subject to judicial review or scrutiny. Thus considered we think it would be reasonable and

proper to hold that restrictions freedom from which is guaranteed by Article 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Article 301.'

(Emphasis Supplied)

7.31 In Atiabari, Chief Justice B. P. Sinha wrote a dissenting opinion holding that any inference that the taxation simpliciter is within the terms of Article 301 cannot be justified under the Constitution. Indeed, it is observed that, it is only such taxes which directly and immediately affect trade would fall within the purview of Article 301, though both the Learned Judges used different languages, the purports appears to be same. It is only such laws which operate in a restrictive manner, right to free trade that are prohibited. Be that as it is, rejecting the submission that Article 301 must be construed as freedom from all kinds of impediments, restraints and trade barriers including freedom from all taxation, the Learned Chief Justice said as follows;

> "'In my opinion, there is no warrant for such an extreme position. It has to be remembered that trade, commerce an intercourse include individual freedom of movement of every citizen of India from State to State, which is also guaranteed by Art.19(1)(d) of the Constitution. The three terms used in Art. 301 include not only free buying and selling, but also the freedom of bargain and contract and transmission of information relating to such bargains and contract as also transport of goods and commodities for the purposes of production, distribution and consumption in all their aspects, that is to say, transportation by land, air or water. They must also include commerce not only in goods and commodities, but also transportation of men and animals by all means of transportation. Commerce would thus include dealings over the telegraph, telephone or wireless and every kind of contract relating to sale, purchase, exchange etc. of goods and commodities.
>
> 15. Viewed in this, all comprehensive sense, taxation on trade, commerce and intercourse would have many ramifications and would cover almost the entire field of public taxation, both in the Union and in the State Lists. It is almost impossible to think that the makers of the Constitution intended to make trade, commerce and intercourse free from taxation in that comprehensive sense. If that were so, all laws of taxation relating to sale and purchase of goods on carriage of goods and commodities, men and animals, from one place to another, both inter-State and intra-State, would come within the purview of Art. 301 and the proviso to Art. 304(b) would make it necessary that all bills or Amendments or pre-existing laws shall have to go thereof the gamut prescribed by that proviso. That will be putting too great an impediment to the power of taxation vested in the States and reduce the States' limited sovereignty under the Constitution to a mere fiction. That extreme position has, therefore, to be rejected as unsound.'"

7.32 Dealing with the importance of taxing power of the State to raise money the

learned Chief Justice. opined thus :-

> "'In my opinion, another very cogent reason for holding that taxation simpliciter is not within the terms of Art. 301 of the Constitution is that the very connotation of taxation is the power of the State to raise money for public purposes by compelling the payment by persons, both natural and juristic, of monies earned or possessed by them, by virtue of the facilities and protection afforded by the State. Such burdens or imposts, either direct or indirect, are in the ultimate analysis meant as a contribution by the citizens or persons residing in the State or dealing with the citizens of the State, for the support of the Government, with particular reference to their respective abilities to make such contributions. Thus public purpose is implicit in every taxation, as such. Therefore, when Part XIII of the Constitution speaks of imposition of reasonable restrictions in public interest, it could not have intended to include taxation within the generic term "reasonable restrictions"'

7.33. In Automobile, the challenge was to the Rajasthan Motor Vehicles Taxation Act, 1951. The Appellants were unsuccessful before the Rajasthan High Court, which upheld the said Act. By majority of 4:3 this Court affirmed the judgment of the High Court. Justice S.K.Das who wrote the lead judgment observed that Part XIII is intended to achieve the federal economic and fiscal integration and addresses the questions of economic unity. He held that, "regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Article 301 and such measures need not comply with the requirements of the proviso to Article 304(b) of the Constitution, (and) that the relevant Articles in Part XIII apply only to legislation in respect of the entries relating to trade and commerce in any of the lists of the Seventh Schedule. But we must advert here to one exception which we have already indicated in an earlier part of this Judgment. Such regulatory measures do not impede the freedom of trade, commerce and intercourse and compensatory taxes for the use of trading facilities are not hit by the freedom declared by Article 301. They are excluded from the purview of the provisions of Part XIII of the Constitution for the simple reason that they do not hamper trade, commerce and intercourse but rather facilitate them".

7.34 Justice K. Subba Rao (as his lordship then was) in a separate opinion concurred with the majority and summarized the following principles that are to be applied while testing a law under challenge as violating Article 301 of the Constitution (1) Article 301 declares a right of free movement of trade without any obstructions by way of barriers, inter-State or intra-State, or other impediments operating as such barriers. (2) The said freedom is not impeded, but, on the other hand, promoted, by Regulations creating conditions for the free movement of trade, such as, police Regulations, provision for services, maintenance of roads, provision for aerodromes, wharfs etc., with or without compensation. (3) Parliament, may by law, impose restrictions on such freedom in the public interest; and the said law can be made by virtue of any entry with respect whereof Parliament has power to make a law.(4) The State also, in exercise of its legislative power, may impose similar restrictions, subject to the two conditions laid

down in Article 304(b) and subject to the proviso mentioned therein. (5) Neither Parliament nor the State Legislature can make a law giving preference to one State over another or making discrimination between one State and another, by virtue of any entry in the Lists, infringing the said freedom. (6) This ban is lifted in the case of Parliament for the purpose of dealing with situations arising out of scarcity of goods in any part of the territory of India and also in the case of a State under Article 304(b), subject to the conditions mentioned therein; and (7) The State can impose a non-discriminatory tax on goods imported from other States or the Union territory to which similar goods manufactured or produced in that State are subject.

7.35 As discussed above, a Constitution Bench of this Court in Atiabari had struck down the Assam Act levying the tax on goods carried by road or inland waterways. Making certain additional provisions, Assam Assembly enacted the Assam Act No. 10 of 1961, coming under Entry 56 of the State List, with the previous sanction of the President with the same nomenclature, which was impeached as unreasonable under Article 32 of the Constitution, in *Khyerbari Tea Company v. State of Assam*[65]. By the time, this Court took up the case, the scope and effect of provisions contained in Part XIII of the Constitution came to be considered in Automobile. Rejecting the challenge this Court observed that the freedom can be restricted by a law satisfying the two conditions in Article 304. In examining the constitutionality of the statute, it must be assumed that the legislature understands and appreciates the needs of the people and the laws it enacts are directed to problems which are made manifest by experience and that the legislature enacts the laws which the people's representatives consider to be reasonable for the purpose for which they are enacted. The presumption is in favor of the constitutionality of enactment. However, when it is shown that an Act invades the freedom of trade, it is necessary to enquire whether the State has proved that the restrictions imposed by way of taxation are reasonable and in public interest within the meaning of Article 304(b). It was also held that a law passed under Article 304(b) can be made to have retrospective effect.

7.36 In Jindal (2), the law was summarized by the Constitutional Bench as under:

> "'Article 301 is binding upon the Union Legislature and the State Legislatures, but Parliament can get rid of the limitation imposed by Article 301 by enacting a law under Article 302. Similarly, a law made by the State Legislature in compliance with the conditions imposed by Article 304 shall not be hit by Article 301. Article 301 thus provides for freedom of inter-State as well as intra-State trade and commerce subject to other provisions of Part XIII and correspondingly it imposes a general limitation on the legislative powers, which is relaxed under the following circumstances:
>
> (a) Limitation is relaxed in favour of Parliament under Article 302, in which case Parliament can impose restrictions in public interest. Although the fetter is limited enabling Parliament to impose by law restrictions on the freedom of trade in public interest under Article 302, nonetheless, it is clarified in Clause (1) of Article 303 that notwithstanding anything contained in Article 302, Parliament is not authorised even in public interest, in the making of any law, to give preference to

one State over another. However, the said clarification is subject to one exception and that too only in favour of Parliament, where discrimination or preference is admissible to Parliament in making of laws in case of scarcity. This is provided in Clause (2) of Article 303.

(b) As regards the State Legislatures, apart from the limitation imposed by Article 301, Clause (1) of Article 303 imposes additional limitation, namely, that it must not give preference or make discrimination between one State or another in exercise of its powers relating to trade and commerce under Entry 26 of List II or List III. However, this limitation on the State Legislatures is lifted in two cases, namely, it may impose on goods imported from sister State(s) or Union Territories any tax to which similar goods manufactured in its own State are subjected but not so as to discriminate between the imported goods and the goods manufactured in the State [see Clause (a) of Article 304]. In other words, Clause (a) of Article 304 authorises a State Legislature to impose a non-discriminatory tax on goods imported from sister State(s), even though it interferes with the freedom of trade and commerce guaranteed by Article 301. Secondly, the ban under Article 303(1) shall stand lifted even if discriminatory restrictions are imposed by the State Legislature provided they fulfil the following three conditions, namely, that such restrictions shall be in public interest; they shall be reasonable; and lastly, they shall be subject to the procurement of prior sanction of the President before introduction of the Bill.'"

7.37 One need to note that Atiabari dealt with the challenge to an enactment which squarely comes under Entry 56 whereas Automobile is a case concerned with the challenge to Rajasthan Motor Vehicle Taxation Act. Taxes on motor vehicles is a subject which falls under Entry 57. The cases which were subsequently decided by this court in relation to Part XIII, were decided by this Court were not concerned with Entries 56 and 57. Be that as it may, deviating a little, let me now examine the scope of Entry 52 and the nature of the tax contemplated there under. Entry 52 of the State list deals with ' taxes on the entry of the goods for consumption use or sale therein'. A law made under this entry like various Acts which are impugned in these appeals levy tax on entry of goods from one State to other. The taxable event is the entry into local area in another State. As defined in Concise Oxford Dictionary the verb 'enter' means 'to come or go into and entry as a noun is act of coming or **going'**[66]**.** There is a palpable difference between the entry of goods and sale of goods. Many enactments levying tax on sale define the sale as 'transfer of property from one person to another in course of business for cash or deferred payment.' When goods enter the State it may be for consumption, use or sale. The factum of entry and sale may not happen at the same time and, therefore, entry of goods is one thing and consumption, use or sale is another thing. Therefore, the mere fact that the goods are intended for sale is no significance to the taxable event in law on the entry of goods.

7.38 In *Hansa Corp*.[67] , the Constitutional validity of Karnataka Tax on Entry of Goods into Local Areas for Consumption, Use or Sale Therein Act, 1979 was challenged before this Court. This Court upheld the validity of the Act and pointed out that the formulation in Atiabari and Automobile was even applicable for Entry Tax under Entry

52 of the State List. This Court summed up the position of law as below- 'Entry 52 in State List read with Article 246 of the Constitution confers power on the State legislature to enact a law to levy tax on the entry of goods into a local area for consumption, use or sale therein. This tax in common parlance is known as 'octroi1. Octroi was leviable by the municipality under the power delegated to it under various laws providing for setting up of and administration of municipal corporations and municipalities. Octroi thus understood was being levied by various municipalities and municipal corporations in Karnataka State. Since some time a feeling had grown that octroi was obnoxious in character and impeded the development of trade and commerce and there was a clamour for its abolition. Taking note of the resentment of the business community, Karnataka State abolished octroi with effect from April 1, 1979. However, no one was in doubt that octroi was a major source of revenue to municipalities and its abolition would cause such a dent on municipal finances that compensation for the loss would be inevitable. Accordingly, the State Government undertook a policy of compensating the municipalities year by year. For generating funds for this compensation, rates of sales tax were raised and in some cases a surcharge was levied. The amount so collected was not sufficient to bridge the gap in municipal budget. To further augment the finances for compensating the municipalities, additional fund was sought to be generated by levy of tax under the impugned legislation. No doubt, the tax levied was one on entry of scheduled goods in local areas meaning thereby it had all the broad features of octroi, yet the manner of levy, the method of collection and the persons liable to pay the same were so devised by the impugned Act as to remove the obnoxious features of octroi. As the charging section shows, the tax was to be levied on entry of scheduled goods in a local area at a rate to be specified by the Government not exceeding 2% ad valorem. The taxing event would be the entry of scheduled goods in a local area. In fact, octroi was being levied on almost all conceivable goods entering into a local area for consumption, use or sale therein. There appears to be a discernible policy in selecting the goods set out in the schedule, the entry of which in a local area would provide the taxing event. The goods selected for levy are textiles, tobacco and sugar. Way back in 1957 there was a demand for abolition of sales tax on the scheduled goods and at the instance of the Union Government the State Governments agreed to forego their right to levy sales tax on the aforementioned scheduled goods on the condition that the Union Government would levy additional excise duty on them and distribute the net proceeds of such duty amongst the consenting States. Parliament accordingly has enacted the Additional Duties on Goods (Goods of Special Importance) Act, 1957. Therefore, while raising rates of sales tax and levying surcharge in respect of some other items the State Government could not have levied sales tax on the scheduled goods. They were, therefore, selected for the levy of the tax under the impugned Act on their entry into a local area'.

XXX

'On a conspectus of these decisions it appears well settled that if a tax is compensatory in character it would be immune from the challenge under Article 301. If on the other hand the tax is not shown to be compensatory in character it would be necessary for the party seeking to sustain the validity of the tax law to show that the requirements of

Article 304 have been satisfied
'.
7.39 In Atiabari, majority held that the legislative competence of the legislature will have to be judged in the light of relevant Articles of Part XIII and that what entries will attract Article 301 will depend on the content of freedom guaranteed. In Jaiprakash, this Court ruled that concept of compensatory tax evolved in Automobile does not apply to general notion of entry tax. As pointed out earlier Atiabari is a case dealing with tax under Entry 56, whereas Automobile is a case under Entry 57. In view of this it would not be safe to apply the majority opinion in Atiabari and Automobile while dealing with entry tax. I am therefore compelled to hold that tax law simpliciter is not contemplated in Article 301 of the Constitution.

7.40 There is no gainsaying that the law made by Parliament or State legislature is subject to Constitutional limitations. A law which abridges fundamental rights is rendered void by reason of Article 13. A law by the Union or the States relating to a subject matter outside the powers assigned under Articles 245 read with Article 246 and relevant legislative entries in the Seventh Schedule would be ultra vires as legislatively incompetent. Apart from these limitations, the law of the Union or the States is also subject to other Constitutional limitations. The provisions of Part XIII, especially, Article 304(a) and (b) also act as a limitation on the legislative jurisdiction of the Union and the States. The power endowed under Articles 245 and Article 246 to a competent legislature to make laws is 'subject to the provisions of the Constitution. Nonetheless, if a State makes law under Article 245(1) r/w. Article 246(3) in respect of the subjects enumerated in Entries 45 to 63 of List II in the Seventh Schedule, it is doubtful whether it can be invalidated only on the ground that it does not comply with Articles 301 and 304(a). Indeed various provisions of the Constitution dealing with fiscal measures in Part XII, for instance Articles 265, 269, 276 and 286, specifically deal with taxes, but in Part XIII, except Article 304(a), no other Article deals with taxes. Further Chapter I of Part XII of the Constitution specifically deals with provisions regarding 'Finance', whereas Part XIII deals with 'Trade, Commerce and Intercourse' within the territory of India. Thus, these two Parts are kept distinctly separate. Though every law is made subject to all provisions of the Constitution, it does not mean that every tax law made by the State must be made answerable to the general provisions relating to trade, commerce and intercourse. The provisions of the Constitution, the Constituent Assembly Debates and the precedents, lead us to such a conclusion. The reasons for this conclusion are summarized as below-

> First, Taxation is an incident of sovereignty, which cannot be curtailed by any implied limitations.[68]
>
> Secondly, It is part of any sovereign government to ensure a welfare State. To achieve the same, tax is the only course available to the government to generate revenue for purposes of welfare activities. Courts, therefore, cannot abridge the taxing power of the sovereign State.
>
> Thirdly, the very conception of Part XIII was only to prevent discriminatory taxes under Article 304(a).

Fourthly, argument of inconvenience cannot affect the interpretation of Article 301 to bring in new tests and expand the provision beyond what was imagined by the framers of our Constitution. Article 304 (a) is an isolated provision which only deals with the discriminatory taxes. Existence of such provision cannot furnish evidence to say that Article 301 is not subject to taxing power of the State.

Fifthly, the taxing entries are specifically provided for in the Seventh Schedule. It is settled principle under our Constitution that taxing power cannot be derived from a general entry. In light of this principle the Constituent Assembly passed the Articles and *Entries [69] in* the following time line: On 13 June, 1949 present Article 245 which was Article 217 (in the draft Constitution) was passed. On September 02, 1949 Entry 52 of State List (which was entry 61 in the draft Constitution) was passed. On September 08, 1949 PART XIII (which was PART XA in the draft Constitution) was passed. This shows that our Constitution framers are presumed to be aware of the inter-play of taxing provisions. Therefore, the only explicit limitation imposed on the taxing power of the State is Article 304(a) of the Constitution. Sixthly, we cannot ignore the legislative journey of Article 301 in Part XIII. At the stage of drafting, free trade, commerce and intercourse was in fact sought to be made a fundamental right but it was not accepted. Ultimately it was resolved to bring all the provisions relating to free trade, commerce and intercourse at one place. What started as a fundamental right came to be enacted as a constitutional right? Thus, there is abundant guidance from the legislative history in regard to incorporation of Article 301 only as a constitutional right.

Seventhly, That Article 306 cannot have an impact on the interpretation of Article 301, as it only saved certain discriminatory taxes. Since the framers wanted to preserve the imposition of such discriminatory taxes for a limited period, which otherwise would have been beyond the competence of State legislature to impose tax on import or on export of goods. Therefore taxes are not covered under the Article 301 only inter-state discriminatory taxes are barred under Article 304(a) of the Indian Constitution.
Eighthly, Tax management is a province of political sphere. Judiciary should provide certain latitude for the government as taxes are lifeline of the Governments.

Ninthly, Article 301 of the Indian Constitution uses the term 'free'. The word 'free' means 'which is not confined or restricted'. Either the trade is 'free or not free'. To state that trade, commerce and intercourse throughout the territory in India is free and then qualify this Article 301 with subsequent Articles under 302, 303 and 304 only portrays that Article 301 is merely clarificatory in nature. If trade was, indeed, free then majority of Articles in the Constitution would have been redundant. From the history, context and interpretation it is clear that Article 301 is just a form to be understood subject to other provisions of Part XIII. If no other motive for its insertion can be suggested, a sufficient one is found in the desire to remove all doubts i.e., the wordings of Article 301 is beyond any doubt a

clarificatory provision and the extent of freedom is limited to those discriminatory taxes, restrictions (other than taxation simpliciter) and prohibitions provided explicitly under Articles 302, 303 and 304."

7.41 In Atiabari and Automobile this Court relied on a non-obstante clause in Article 304 to hold that, by necessary implication, tax law come within the purview of Article 301. This view is not sound because one has to read the text and context while interpreting the constitutional provisions. In this regard, I respectfully agree with the reasoning and conclusions reached by Hon'ble the Chief Justice that non-obstante clause in Article 304 (a) is not determinative in the interpretation of Article 301.

PART-VIII : ARTICLE 304 OF THE CONSTITUTION

8.1 Whether a law levying tax on entry of goods needs to be tested with reference to Article 304(a) and (b) of the Constitution? In order to appreciate the implication of Article 304 of the Constitution, it is necessary to bear in mind that historical background of these provisions.
The Government of India Act, 1935 envisaged a federal Constitution for the whole of British India. The Government imposed restriction on the legislature of the States to legislate in relation to internal trade under Section 297 in the following terms:-

'"297 .(1)No Provincial Legislature or Government shall.

(a) by virtue of the entry in the Provincial Legislative List relation to trade and commerce within the Province, or the entry in that list relating to the production, supply, and distribution of commodities, have power to pass any law or take any executive action prohibiting or restricting the entry into or export from, the Province of goods of any class or description; or

(b) by virtue of anything in this Act have power to impose any tax, cess, toll, or due which, as between goods manufactured, or produced in the Province and similar goods not so manufactured or produced, discriminates in favour of the former or which, in the case of goods manufactured or produced outside that Province, discriminates between goods manufactured or produced in another locality. (2)Any law passed in contravention of this section shall, to the extent of the contravention, be invalid.'"

8.2 It may be noticed that prohibition contained in the section quoted above applied only to Provincial Governments and Provincial legislatures with reference to entries in the legislative list relating to trade and commerce and to production, supply and distribution of commodities. This section dealt with prohibitions or restrictions in respect of import into or export from a Province, of goods generally. It also dealt with the power to impose taxes etc. and prohibited discrimination against goods manufactured or produced outside a Province or goods produced in different localities.

8.3 The Sub Committee on Fundamental Rights comprising of Shri. K. M. Munshi, Sir Alladi Krishnaswami Iyer and Sir. B. N. Rau on March, 29 1947 introduced Clause 13 in

the following form:-

> "Subject to regulation by the law of the Union, trade, commerce and intercourse among the units, whether by means of internal carriage or by Ocean Navigation, shall be free: Provided that any unit may by law impose reasonable restrictions thereon in the interest of public order, ***morality or health.'*** [70]"

(Emphasis supplied)

8.4 The proviso herein above empowered the 'Unit' to impose by law, reasonable restrictions in the interest of the public order, morality or health. Sir B. N. Rau in his comments to the aforesaid draft discussed by the Sub Committee stated that 'the first paragraph of Clause 13 is
adopted from the Australian Constitution (Sec. 92) while the proviso was new'. Further, Sir Alladi Krishnaswami Iyer in his comments on Draft Report of 10th, 14th& 15th April, 1947, in relation to Clause 13 suggested that it must be made clear that :

> "'(1) Goods from other parts of India than in the units' concerned coming into the units cannot escape duties and taxes to which the goods produced in the units in themselves are subject.
>
> (2) It must also be open to the unit in an emergency to place restrictions on the rights declared by the clause" [71]

8.5 The suggestions of Sir. Alladi Krishnaswami Iyer were accepted and the Clause was accordingly modified and incorporated as Clause 14 as below :
14. (1) Subject to regulation by the law of the Union trade, commerce and intercourse among the units by and between the citizens shall be free:

> "Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in an emergency:'IVTTT'IYT H-1 Provided that nothing in this Section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject: Provided further that no preference shall be given by any regulation of commerce or revenue by unit to one unit over another. [72]

8.6 It may be relevant to note that while imposing reasonable restriction in the first Proviso, the imposition of non-discriminatory tax was in the second Proviso. The third Proviso was a pre-cursor of Article 303. On 21.04.1947, the aforesaid Clause 14 came up for consideration of the Advisory Committee. Explaining the purpose of enabling a State to impose reasonable restriction in the interest of public order, morality, health or in emergency, Sir Alladi Krishnaswamy Iyer said:

> "Suppose there is a general famine and people are starved that is what is meant here to be dealt with' The advisory Committee accepted the recommendation of the Sub-Committee in relation to Clause 14 with 'one change; the sub-clause

providing for central regulation of trade by or with non-citizens was dropped as being vague and unnecessary. [73] "

8.7 The Advisory Committee submitted its report on 23.04.1947 wherein Clause 10 provided as under:

"'10. Subject to regulation by the law of the Union, trade, commerce and intercourse among the units by and between the citizens shall be free: Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in any emergency:

Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject:

Provided further that no preference shall be given by any regulation of commerce or revenue by a unit to one unit over the another'. [74]

8.8 On 01.05.1947 certain amendments were suggested which were adopted by the Constituent Assembly. Clause 10, as amended, reads as follows:

"10. Subject to regulation by the law of the Union, trade, commerce, and intercourse among the units by and between the citizens shall be free:

Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in any emergency:

Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject:

Provided further that no preference shall be given by any regulation of commerce or revenue by a unit to one unit over another."

8.9 In the first Draft Constitution of October, 1947, Clause 17 reads as follows:

"'17. Subject to the provisions of any Federal Law, trade, commerce and intercourse among the units shall, if between the citizens of the federation, be free:

Provided that nothing in this section shall prevent ny unit from imposing goods imported from other unit from imposing goods imported from other units any tax to which similar goods manufactured or produced in that unit are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced:

Provided further that no preference shall be given by any regulation of trade,

commerce or revenue to one unit over another:

Provided also that nothing in this section shall preclude the Federal Parliament from imposing by Act restrictions on the freedom of trade, commerce and intercourse among the units in the interests of public order, morality or health or in cases of emergency'.[75]

8.10 On 01.11.1947, the Drafting Committee considered Clause 17 and was of the opinion that 'the first and second provisos to this clause should be transferred as independent clauses in the chapter dealing with relations between the different States and the third proviso was unnecessary.[76]

8.11 On 28.01.1948, the Drafting Committee decided to introduce three new clauses, namely Clause 192 E, 192 F & 192 G, relating to trade, commerce and intercourse. Clause 192 E, 192 F and 192 G as introduced by the Drafting Committee on 28.01.1948, reads as follows:

"192E. No Preference shall be given by any regulation of trade, commerce or revenue to one State or any part thereof over another State or any part thereof. 192-F. Notwithstanding anything contained in Article 17 or in the last preceding Article of this Constitution, it shall be lawful for any state- To impose on goods imported from other State any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced: and To impose by law any restrictions on the freedom of trade, commerce or intercourse with that State in the interests of public order, morality and health or in cases of emergency.

*The committee is of opinion that the provisions contained in Articles 192-E and 192-F should more appropriately be included in this Chapter than in Part III dealing with fundamental rights. 192-G (1) there shall be an Inter-State Commerce Commission consisting of such members as the president may think fit to appoint for the execution and maintenance within the territory of India of the provisions of this Constitution relating to Trade and Commerce.

(2) The term of the office of the members of the commission, and the remuneration to be paid to them shall be such as the President may by Order determine.

(3) The procedure of the commission shall be defined by the President by the Order and the Commission shall have such powers including the power of adjudication as the President may, from time to time, by Order, confer on it.

(4) It shall be the duty of the Commission to decide any dispute relating to Trade or Commerce between the States referred to it by the President for adjudication and the decision of the Commission shall be final and shall not be questioned in any Court'. On 29.01.1948, the said clause was further revised and the revised

clause reads as follows:

'*192-E. No preference shall be given to nor shall any discrimination be made between one state or any part thereof and another State or any part thereof by ay regulation of trade or commerce, whether by means of internal carriage through roads, railways or rivers or by means of navigation through seas.

*192-F Notwithstanding anything contained in Article 17 or in the last preceding Article of this Constitution, it shall be lawful for any State-flHTO

(a) to impose on goods imported from other State any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and r-p

(b) To impose by law such reasonable restrictions on the freedom of trade, commerce or intercourse with that State as may be required in the public interests.
*The committee is of opinion that the provisions contained in Articles 192-E and 192-F should more appropriately be included in this Chapter than in Part-lll dealing with the fundamental rights.

*192-G. Parliament shall by law appoint such authority as it considers appropriate for the carrying out of the provisions of Article 192-E and 192-F of this Constitution and confer on the authority so appointed such powers and such duties as it thinks necessary. in the Fundamental rights Chapter which reads as under:

'16. Subject to the provisions of Article 244 of this Constitution and of any law made by the Parliament, trade, commerce and intercourse throughout the territory of lndia shall be free. Inter-State trade and Commerce was dealt with in Article 243, Article 244 and Article 245 which reads as below:

'*243. No preference shall be given to one State over another nor shall any discrimination be made between one state and another by any law or regulation relating to trade or commerce, whether carried by land, water or air.

*244. Notwithstanding anything contained in Article 16 or in the last preceding Article of this Constitution, it shall be lawful for any State-

(a) to impose on goods imported from other States any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced: and

(b) To impose by land such reasonable restrictions on the freedom of trade, commerce or intercourse with that State as may be required in public interests:

Provided that during a period of five years from the commencement of this Constitution the provisions of Clause (b) of this Article shall not apply to trade or commerce in any of the Commodities mentioned in Clause (a) of Article 306 of this Constitution.

245. Parliament shall by law appoint such authority as it considers appropriate for the carrying out of the provisions of Articles 243 and 244 of this Constitution and confer on the authority so appointed such powers and such duties as it thinks necessary.[77]

8.12 In the comments and suggestions to the Draft Constitution of February, 1948, the note to the comment of the Ministry of Industry and Supply is relevant. The Ministry of Industry and Supply has expressed the view that Clause (b) of Article 244 is open to serious objection on principle and should be deleted altogether. The Ministry has pointed out that it is not possible to foresee the circumstances in which the freedom of trade, commerce or intercourse with a State will need to be interfered with by the State in the Public interest, unless it be on the basis of discrimination between the residents of one State and another, and this would be wholly contrary to the spirit of the Constitution. [78]

8.13 On 08.09.1949, Hon'ble Dr. Ambedkar moved for the deletion of these Articles and the motion was adopted by the Constituent Assembly without any opposition. The substance of these Articles was however, embodied in another amendment moved by Hon'ble Dr. Ambedkar immediately thereafter on the same day. All these Articles were added in Part XA. The events at the stage of drafting the Constitution, especially Part XIII would show the following which I may summarize at the cost of repetition:

First, initially the right to free trade was a Fundamental Right, but it was not accepted by the Advisory Committee and not even moved in the Constituent Assembly for adoption. Second, though the precursor clause to Article 304 underwent repeated changes before the Advisory Committee and the Drafting Committee, never it was suggested that freedom of trade was meant to be freedom from payment of taxes. Third, the power of federal unit to levy tax on the goods imported from other units was specifically adumbrated to dispel any doubt about taxing power of the State. The logical conclusion is that the power of the State to levy any tax on goods imported is specifically saved and declared in the final clause, therefore it would be impermissible to test a law imposing entry tax with reference to Article 304(b).

Fourth, taxes were never intended to be a restriction on freedom of trade.

8.14 Another important question which needs to be answered as a part of this reference is whether State enactments relating to levy of entry tax have to be tested with reference to both clauses (a) and (b) of Article 304 or only with reference to clause (a) of Article 304 of the Constitution? In other words is Clause (a) and (b) of Article 304 is conjunctive or disjunctive? The answer must be that the history, the context and the plain words indicate that Article 304 (a) and (b) are disjunctive in nature. A levy of tax need not be tested with reference to Article 304 (b) of the Constitution. Following are the reasons for reading Article 304 (a) and (b) of the Indian Constitution disjunctively. First, the legislative history and the intention of the framers as elucidated above clearly point out that taxes were never treated as restrictions in the first place. Secondly, Article

304(a) does not bar or limit State power to
levy non-discriminatory taxes on the goods imported from other States. What is restricted is levy of discriminatory tax only, so to say, similar goods manufactured or produced in that State are also subjected to tax, so as not to discriminate between the goods imported and goods manufactured or produced in the State.

> "Thirdly, the two clauses of Article 304 are connected by the word 'and'. Sub-clause (a) puts a restriction on the State to not impose a discriminatory tax, whereas sub-clause (b) deals with other restrictions relating to trade, commerce and intercourse. Fourthly, Article 304 (a) and (b), on a careful reading would show that Article 304 (a) and (b) are disjunctive. This is made clear by the proviso, which is to the effect that a Bill for the purpose of Article 304 (b) can be moved by the Legislature of the States, only by the previous sanction of the President. If Clauses (a) and (b) are not disjunctive, then the language of the proviso would have been certainly different and the Bill for the purpose for Clause (a) would have been mentioned. Conspicuous absence of reference to 304(a) in the proviso would certainly lend support to the view that Clause (a) and (b) of Article 304 are distinct and disjunctive. The proviso, it is well settled, is intended to explain the main operating part of the Article. It is never used or interpreted as expanding the operative part of the provision. Fifthly, if one reads Clauses (a) and (b) of Article 304 conjunctively, then it would not subserve the federal nature of the Constitution which is a basic structure."

8.15 I will now deal with the purport and scope of the word "discrimination" used in Article 304(a) by making some general observations. Article 304(a) should be interpreted keeping in mind the balanced development of the country, which is an important part of economic integration. To achieve the economic unity of the country, allowing trade and commerce without imposing taxes is not the only solution but it can also be achieved by bringing in overall prosperity. Part XIII of the Constitution permits some forms of differentiation, for example, to encourage a backward region or to create a level playing field for parts of the Country that may not have reached the desired level of economic development. Therefore, Part XIII envisions a twofold object: (i) facilitation of a common market through ease of trade, commerce and intercourse by erasing barriers; and (ii) regulations (or restrictions) which may be necessary for development of backward regions or in public interest. A brief reference to the Constituent Assembly debates would amply demonstrate the same. Hon'ble Member Shri P. S. Deshmukh said: 'How pompously did we decide that there shall be "free trade" everywhere! It is not such an easy thing as that and I hope advancement and progress of the various units of the Union varies considerably. Some of them are backward like Assam or Orissa where there are very few industries and very little trade is in the hands, at least of the indigenous population. We may have probably to give them some protection in order that they may rapidly come on par with other units. It may be necessary also from time to time to vary our provisions so far as aid and concessions to industries and other things are concerned. I therefore do not think that is right to bar all discrimination, as it is called (in fact it is not),barring all possibility of help to those who are backward and who are unable to compete with the more advanced. and who therefore stand in need of assistance. From that point of view, my amendment seeks to give Parliament a blank cheque and leave to it entirely the determination of the policy with regard to trade and

commerce not only of the whole Union or in regard to any particular State or States, but so far as all States and their trade and commerce inter se is concerned. Therefore, I have proposed a very simple provision as has been embodied in my amendment No. 340'.

(emphasis supplied)

> "Sir Alladi Krishnaswami Iyer stated: 'My friend Mr. Krishnamachari has pointed out that this freedom clause in the Australian Constitution has given rise to considerable trouble and to conflicting decisions of the highest Court. There has been a feeling in those parts of Australia which depend for their well-being on agricultural conditions that their interests are being sacrificed to manufacturing regions, and there has been rivalry between manufacturing and agricultural interests. Therefore, in a federation what you have to do is, first, you will have to take into account the larger interests of India and permit freedom of trade and intercourse as far as possible. Secondly, you cannot ignore altogether regional interests. Thirdly, there must be the power intervention of the Centre in any case of crisis to deal with peculiar problems that might arise in any part of India. All these three factors are taken into account in the scheme that has been placed before you'."

8.16 To what extent economic unity in India and regional interests has to be kept in mind while meaningfully implementing free trade clause in Article 301? In ***Video Electronics***[79] this Court had an occasion to delve into these aspects. This Court even suggested that there could be differentiation among regions and among the goods exchanged between the regions without attracting the tag of discrimination. The following passage from Video Electronics is apposite:

> "'Economic unity is a desired goal, economic equilibrium and prosperity is also the goal. Development on parity is one of the commitments of the Constitution. Directive principles enshrined in Articles 38 and 39 must be harmonized with economic unity as well as economic development of developed and under developed areas. In that light on Article 14 of the Constitution, it is necessary that the prohibitions in Article 301 and the scope of Article 304(a) and (b) should be understood and construed. Constitution is a living organism and the latent meaning of the expressions used can be given effect to only if a particular situation arises. It is not that with changing times the meaning changes but changing times illustrate and illuminate the meaning of the expressions used. The connotation of the expressions used takes its shape and color in evolving dynamic situations. A backward State or a disturbed State cannot with parity engage in competition with advanced or developed States. Even within a State, there are often backward areas which can be developed only if some special incentives are granted. If the incentives in the form of subsidies or grant are given to any part of units of a State so that it may come out of its limping or infancy to compete as equals with others, that, in our opinion, does not and cannot contravene the spirit and the letter of Part XIII of the Constitution. However, this is permissible only if there is a valid reason, that is to say, if there are justifiable and

rational reasons for differentiation. If there is none, it will amount to *hostile discrimination'.*[80]

8.17 There is a vital difference between mere 'differentiation' and 'discrimination. It is discrimination not differentiation that is sought to be prevented through Part XIII. Again reference to certain observations of this Court in Video Electronics would be pertinent:

> "'... very differentiation is not discrimination. The word 'discrimination1 is not used in art. 14 but is used in Articles 16, 303 & 304(a). When used in Article 304(a), it involves an element of intentional and purposeful differentiation thereby creating economic barrier and involves an element of an unfavorable bias. Discrimination implies an unfair classification. Reference may be made to the observations of this Court in Kathi Raning Rawat v. The State of Saurashtra, [1952] SCR 435 where Chief Justice Shastri at p. 442 of the report reiterated that all legislative differentiation is not necessarily discriminatory. At p. 448 of the report, Justice Fazal Ali noticed the distinction between 'discrimination without reason' and 'discrimination with reason'. The whole doctrine of classification is based on this and on the well-known fact that the circumstances covering one set of provisions or objects may not necessarily be the same as these covering another set of provisions and objects so that the question of unequal treatment does not arise as between the provisions covered by different sets of *circumstances'.*[81]

8.18 In the above case exemption and incentive granted by one State to its inhabitants was challenged as being violative of Article of 304 (a). Recognizing the concept of economic equality, this Court held :

> "'Concept of economic barrier must be adopted in a dynamic sense with changing conditions. What constitutes an economic barrier at one point of time often cease to be so at another point of time. It will be wrong to denude the people of the State of the right to grant exemptions which flow from the plenary powers of legislative heads in list II of the 7th Schedule of the Constitution. In a federal polity, all the States having powers to grant exemption to specified class for limited period, such granting of exemption cannot be held to be contrary to the concept of economic unity. The contents of economic unity by the people of India would necessarily include the power to grant exemption or to reduce the rate of tax in special cases for achieving the industrial development or to provide tax incentives to attain economic equality in growth and development. When all the States have such provisions to exempt or reduce rates the question of economic war between the States inter se or economic disintegration of the country as such does not arise. It is not open to any party to say that this should be done and this should not be done by either one way or the other. It cannot be disputed that it is open to the States to realize tax and thereafter remit the same or pay back to the local manufacturers in the shape of subsidies and that would neither discriminate nor be hit by art.304(a) of the Constitution. In this case and as in all constitutional adjudications the substance of the matter has to be looked into to find out whether there is any discrimination in violation of the constitutional mandate'

(emphasis supplied)

8.19 Thus stated, the principle laid down in Video Electronics is that, if a backward area in a State needs impetus for the development, and in such circumstances incentives are given for the industry to develop whether by way of subsidies or tax exemptions for a certain period of time as desired by the competent legislature, the same would be permissible and would fall outside the scope of Article 304 (a). Such State enactment is not inherently discriminatory, but rather aims to ensure economic equality which is a facet of economic unity.

8.20 A State law directed towards development of a particular region is permissible under Part XIII. In support, we may again refer to the discussion in the Constituent Assembly debates dealing with the concepts of "public interest" and "interest of general public". Clause 13 was introduced in Chapter dealing with Fundamental Rights making the right to free trade, commerce and intercourse as a Fundamental Right subject to reasonable restriction. Pandit Thakur Das Bhargava sought to move an ***amendment***[82] to substitute the words, 'public

[82] Constituent Assembly Debates, 1949, vol. IX, Page 1145'That is amendment No. 269 of List IV (Seventh Week), in clause (b) of the proposed new Article 274-D, for the words 'in the public interest', the words 'interests of the general public and are not inconsistent with the provision of Article 13 be substituted.' interest' for 'interests of the general public' he said :

'I maintain that there is great difference between the two expressions. 'Public interest' in regard to a State would only include the interests of the inhabitants of that State at the most though the word 'public' includes portions of the public. Therefore, the interests of a part of the inhabitants of a State would also mean 'public interest', whereas if you use the words "interests of the general public" they would have reference to the interests, of the. general public of India as a whole. It may be that on many occasions a conflict may arise. between the public interest as understood in the amendment of Dr. Ambedkar and 'the interests of the general public' as used in article 13. When that conflict arises it would be encouraging provincialism and the interests of a few as against the general interest if we accept the words 'public interest' in the place of the words "in the interests of the *general public*[83]*.*

8.21 This amendment was negatived. The fact that this amendment did not go through would indicate that 'public interest' could imply a regional interest that needs to be protected which may not be 'in the interests of the general public' but specific to a smaller region. Such an interpretation is supported by the manner in which the word 'discrimination' has been interpreted by a three Judge bench of this Court in Video Electronics. Thus it can be said that the common thread in Part XIII is the achievement of economic unity and parity which does not altogether preclude differentiation for justifiable and rational reasons wherever necessary. The heart and soul of Part XIII is to dissolve hostile discrimination within the territory of India.

Constituent Assembly debates, 1949, Vol. IX, p. 1125.

8.22 The second facet is that Article 304 (a) is a limitation to impose any tax on goods imported from other States. This power is subject to the condition that the goods

manufactured or produced within the State are also subjected to tax, so as not to discriminate between the goods imported from outside the State. Article 304(a) is not a limitation on the legislature of a State to impose such tax on goods imported. The only condition envisaged under Article 304 (a) is, same tax is imposable on the goods imported from other States as well as goods if manufactured in that State.

8.23 The contention that the taxing power lies in Article 304 (a) and not in Article 245 r/w 246 is not correct. The words "may by law" appearing in Article 304 is not source of legislative power. It is an option given to the States in case it decides to levy any tax on the goods imported from other States. The source of legislative power resides in Article 245 r/w. Article 246 which is indisputable. This power is not subject to any implied limitation. The plain reading would show that in a given situation, the State may by choice decide not to levy any tax imported from other States or opt to levy taxes on certain goods imported from other States. Indeed in all the entry tax laws, the charging section enables the levy of entry tax only on the scheduled goods. The scheduled goods are goods declared as attracting entry tax.

8.24 Discrimination is a relative concept; in order to discriminate a reference point is required. Article 304(a) rather than being an enabling provision to allow the State to impose tax, is a restricting provision, which prevents such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. The object is to prevent discrimination against imported goods by imposing tax on such goods at a rate higher than that borne by local goods since the difference between the two rates would constitute a tariff wall or fiscal barrier and thus impede the free flow of inter-State trade and commerce. It does not prohibit levy of tax as such in the situation wherein the goods are not produced or manufactured in the State itself and does not affect the authority of the State to tax the imported goods. It only bars discrimination on the basis of taxing the products manufactured within the State vis-a-vis imported goods which will only occur if the precondition of manufacturing in the taxing State is satisfied.

8.25 I agree with the conclusions and reasons given by the learned Chief Justice regarding the exemption/set off/credit with respect to Sales tax.

8.26 There was good amount of debate on the doctrine of compensatory tax evolved by this Court in Automobile. I am in respectful agreement with the consideration, reasoning and conclusion in the judgment of the learned Chief Justice, who held that concept of compensatory tax has neither any juristic basis nor a part of Indian Constitutional law. It is interesting and glaring to note that at the stage of drafting, at the stage of consideration by the Sub-Committee as well as Advisory Committee and when the Part XA (now Part XIII) was adopted by the Constituent Assembly, never even for a moment, the principle of compensatory tax was thought of.

PART-IX: CON CLU SION S

9.1 On an analysis and reasoning as herein above the following conclusions would emerge-

"a. Part XIII does not contemplate tax laws within its ambit except to the extent of Article 304(a) of the Constitution.

b. Article 304 (a) and (b) are disjunctive.

c. Restrictions mentioned under Article 304(b) of the Constitution do not include tax.

d. It is not correct to say that since goods being taxed are not that is to say, that Article 304 (a) does not bar levy of tax if the goods are not manufactured or produced within the State.

e. Article 304(a) of the Constitution protects from discrimination (for protectionism) and not mere differentiation."

9.2 Before parting with this case, I would like to express my appreciation for the way the hearing of the case took place before the Court. Attorney General needs to be specially mentioned and thanked, who had appeared and assisted the Court. Lastly, it was a wonderful sight to see young practitioners ably assisting their seniors which only goes on to reflect vibrancy of Indian Supreme Court Bar.

[3] Jindal Strips Ltd. v. State of Haryana (2003) 129 S.T.C 534	[4](2003) 8 SCC 0060	[5](2006) 7 SCC 0271
[6](2009) 21 V.S.T 10 (P&H)	[7](2009) 7) S.C.C 339.	[9](2010) 4 S.C.C 595
[10] AIR 1965 S.C 1636	[11](2005) 2 SCC 673	[14]AIR 1971 S.C 530
[15]AIR 1970 SC 0564	[16]RBI v. Pearless General Finance, A.I.R 1987 S.C 1023	[17](1939) F.C.R 18
[18](1986) 2 SCC 249	[20]Minerva Mills v. Union of India, A.I.R 1980 S.C 1789	[34](1973) 4 S.C.C 225
[35]AIR 2005 S.C 1646	[48](1988) 165 C.L.R 360	[49](1990) 169 CLR 436
[50](2008) 234 C.L.R 418	[51]Ibid, p. 399	[52]Common wealth v. Bank of new South Wales, (1949)
[79] C.L.R 497	[54]Constituent Assembly Debate, Vol. IX, 8th September 1949	[55] 25 U.S. (12 Wheat.) 419 (1827)
[79] C.L.R 497		
[56] 4 Wheat. 316 (1819)	[57]329 U.S. 249 (1946)	[58] 430 U.S. 274 (1977)
[59]486 U.S. 24 (1988)	[60]453 U.S. 609 (1981)	[61]Constitutional Law of Canada, Peter W. Hogg, Vol.1, pg. 857
[62]Gold Seal Ltd. V. Alberta AG, (1921) 62 S.C.R 424	[63]Ibid. at 456	[64]Ibid. at 470
[65](1964) 5 SCR 975 : AIR 1964 SC 925	[66]Concise Oxford Dictionary, p. 474 (10th Ed.)	[67](1980) 4 SCC 0463
[68]Maharaj Umeg Singh v. State of Bombay, A.I.R 1955 S.C 540.	[69]M.P.V. Sundararamier & Co. vs. The State of Andhra Pradesh and Anr.	[70]B. Shiva Rao, Framing of India's Constitution, A Study (2nd Ed.), p. 699 to707
[73]Ibid., p. 253	[74]Ibid., P. 297	[75]B. Shiva Rao, Framing of India's Constitution, Vol. III, p. 9 (2nd Ed.)

[76]Ibid, p. 330	[77]Ibid., p. 453 to 454	[78]B. Shiva Rao, The Framing of India's Constitution, Vol. IV, pg. 329
[79]Video Electronics v. State of Punjab, (1990) 3 SCC 87.	[80]Ibid. p. 113	[81]Ibid, p. 106-107.
[83]Constituent Assembly debates, 1949, Vol. IX, p. 1125.		

JUDGEMNT

R.Banumathi,J.,

1. I have perused the judgment of Hon'ble the Chief Justice. I agree with the views taken by Hon'ble the Chief Justice on Question Nos.1 and 4 with certain additions. On Question Nos. 2 and 3, while agreeing with the views of the Chief Justice over-ruling Jindal Stainless Ltd. (2), on the question of 'Compensatory tax', I have recorded my reasonings which in my view is necessary to be clarified. Since substantial questions of law arise for determination which is of considerable importance from the point of view of trade, commerce and intercourse and economic unity of the nation, I would like to give my own reasonings for my conclusions.

1(a). Question No. 1:- I agree with the conclusion of the Chief Justice holding that a non-discriminatory tax does not per se constitute a restriction on the right to free trade, commerce and intercourse guaranteed under Article 301 of the Constitution. I also agree with the view over-ruling the decisions in Atiabari and Automobile Transport to the extent they declare that taxes generally are restrictions on the freedom of trade, commerce and intercourse. I also agree with the view taken by the Chief Justice over-ruling *Jindal Stainless Ltd. (2) & Anr. v. State of Haryana & Ors*[1]. Insofar as the concept of compensatory taxes evolved in Automobile Transport. I am of the view, abandoning compensatory tax in the subsequent judicial pronouncement like the present one, might prejudice the interest of the concerned States.

1(b). Question No. 4:- I agree with the view taken by the Chief Justice on question No. 4 however, with the following additions:-

> " When the entry tax is levied by the Entry Tax Act enacted by the State Legislature, the term 'a local area' contemplated by Entry 52 may cover the 'Whole State' or 'a local area! as notified in the legislation. I agree with the view taken in Bihar Chamber of Commerce that from the point of view of entry tax that the State is a compendium of local areas and where the local areas contemplated by the Act cover the entire State, the difference between the State and 'a local area' practically disappears. (DD States have legislative competence to levy entry tax on the goods imported from other countries when those goods imported from other countries enter a local area for use, consumption or sale therein. (dddd Tax concessions/benefits/subsidies granted by the State for locally manufactured goods need not necessarily be limited for a specific period of time. 1(c). Questions Nos. 2 and 3:- Insofar as compensatory

taxes are concerned in the light of the conclusions on question No. 1, I hold that the nomenclature of 'compensatory' ascribed to the taxes levied by the State Government under Entry 52, List II pursuant to Automobile is unwarranted. The concept of compensatory tax was evolved fifty years back through judicial pronouncements. It has withstood the test of time and thus, any subsequent judicial pronouncement like the present one should not prejudice the interest of the parties involved. The State Governments should not suffer any loss of revenue solely because of judicial interpretations and innovations in Automobile and the case subsequent to it. Subject to passing the muster of Art. 304(a), entry tax levied by the States under entry 52, List II even though termed as compensatory tax does not fall foul of Art. 301. In my view, *Jindal Stainless Ltd. (2) & Anr. v. State of Haryana & Ors.(Supra)* is not a correct view in adopting quantifiable data approach; for a tax, there is no requirement of proximate quid pro quo and Jindal Stainless Ltd. (2) is overruled. I agree with the view taken in Bhagatram and Bihar Chamber of Commerce as the same is in harmony with the original design of compensatory tax laid down in Automobile.

1(d). For the above conclusions, I have put forth my views and reasonings under the following heads of discussions:-

Introduction	[Para Nos. 1 -1 (d)]
Background to the reference	[Para Nos. 2-7]
Scheme of the Constitution/distribution of legislative powers	[Para Nos. 8-14]
Freedom of trade commerce and intercourse	[Para Nos. 15-27]
Freedom under Article 301 is subject to Part XIII and other parts of the Constitution viz. Part III, IV, XII etc	[Para Nos. 28-35]
Question No. 1 with incidental questions	[Para Nos. 36-103]
Question No.4 with incidental questions	[Para Nos. 104-177]
Question Nos. 2 and 3	[Para Nos. 178-191]
Unjust Enrichment	[Para Nos. 192-198]
Conclusions	[Para Nos. 199]

BACKGROUND TO THE REFERENCE:

2. In Automobile the concept of compensatory tax has been judicially evolved as an exception to the provisions of Art. 301. Pre-1995 decisions have held that the entry tax

imposed on the entry of goods into a local area for consumption, use or sale therein is in the nature of a compensation, to which, the cost of an existing facility made available to the traders, or the cost of the specific facility planned to be provided to the traders, more or less, is to be commensurate with. Pre-1995 decisions further emphasized that the imposition of tax is must for the definite purpose of meeting the expenses on account of providing or adding to the trading facilities, either immediately or in future, provided the tax sought to be generated is based on a reasonable relation to the actual or the projected expenditure on the cost of the service or facility. But the decisions in *Bhagatram Rajeevkumar v. Commissioner of Sales Tax, M.P. & Ors*[2]*. and State of Bihar & Ors. v. Bihar Chamber of Commerce and Ors*[3]*.* held that even if the purpose of imposition of the tax is not to confer a special advantage on the traders, but to benefit the public in general including the traders, the levy can still be considered compensatory. In Bihar Chamber of Commerce, this Court reiterated the position that "some connection" between the tax and the trading facilities is sufficient to characterize it as compensatory tax. The Court went on further to hold that an indirect or incidental benefit to traders by reason of stepping up the developmental activities in various local areas of the State can be legitimately brought within the concept of compensatory tax and the nexus between the compensatory tax and the trading facility need not necessarily be either direct or specific. In J*indal Stripe Ltd. and Anr. v. State of Haryana and Ors*[4]*.* this Court referred the matter to the Constitution Bench to authoritatively lay down the principles vis-a-vis compensatory tax.

3. In *Jindal Stainless Ltd. (2) & Anr. v. State of Haryana & Ors*[5]*.* Constitution Bench considered the various decisions relating to compensatory tax and held that whenever a law levying compensatory tax is impugned as violative of Art. 301 of the Constitution, the Court has to see whether the impugned enactment facially indicates the proportionality to the quantifiable data on the basis of which the compensatory tax is sought to be levied. It was further held:

> "46. ...it must broadly indicate proportionality to the quantifiable benefit. If the provisions are ambiguous or even if the Act does not indicate facially the quantifiable benefit, the burden will be on the State as a service/facility provider to show by placing the material before the Court, that the payment of compensatory tax is a reimbursement/recompense for the quantifiable/ measurable benefit provided or to be provided to its payer(s). As soon as it is shown that the Act invades freedom of trade it is necessary to enquire whether the State has proved that the restrictions imposed by it by way of taxation are reasonable and in public interest within the meaning of Article 304 (b)."

4. The Constitution Bench further held that the test of "some connection" enunciated in Bhagatram was not only contrary to the working test propounded in Automobile but obliterated the very basis of compensatory tax. It was, therefore, held that the test of "some connection" as propounded in Bhagatram was not a correct view and the judgments in Bhagatram and Bihar Chamber of Commerce were overruled.

5. After the judgment of Constitution Bench in Jindal Stainless (2) dated 13.04.2006, the matter went to a Division Bench which in turn by their order dated 14.07.2006,

reported in *Jindal Stainless Ltd. (3) and Anr. v. State of Haryana & Ors.*[6], directed the High Courts to re-examine the challenge in the light of the principles laid down by the Constitution Bench. While doing so, this Court retained seisin of the appeals by directing the appeals to be listed in January, 2007 and in the meantime requested the High Courts to dispose of the challenge to the Act after granting opportunities to the respective parties to place materials on record. After the matter was so remanded, in pursuance of the parameters laid down by the Constitution Bench in Jindal Stainless Ltd. (2), the Punjab and Haryana High Court by judgment dated 14.03.2007, took the view that the levy under Haryana Local Area Development Act, 2000 was not compensatory. The State of Haryana challenged the aforesaid judgment dated 14.03.2007 in Civil Appeal No.4715 of 2008 and filed certain other appeals challenging orders in separate cases.

6. Considering the importance of the issues relating to Articles 301, 304 and other provisions of Part XIII of the Constitution, in *Jaiprakash Associates Ltd. vs. State of Madhya Pradesh and Ors*[7] [two Judges], the matter was referred to a larger Bench in terms of Art. 145(3) of the Constitution stating that the concept of compensatory tax is a judicially evolved concept and in a way provides a balancing factor between federal control and the State Taxing Board. It was observed that the concept had its matrix in transportation cases and did not apply to the general notion of entry tax. The Court considered it necessary to refer the batch of appeals to a larger Bench in terms of Art. 145(3) of the Constitution and framed ten questions for reference. Subsequently, in *Jindal Stainless Ltd. & Anr. v. State of Haryana & Ors.*[8] after referring to the reference made in Jaiprakash Associates, the matter was referred to a larger Bench. Accordingly, the matters are now before this larger Bench.

7. Even though ten questions were framed for reference, when the matters came up for consideration before this larger Bench, the issues for consideration were abridged to four questions as under:-

> "(1) Can the levy of a non-discriminatory tax per se constitute infraction of Article 301 of the Constitution of India?
>
> (2) If answer to Question No. 1 is in the affirmative, can a tax which is compensatory in nature also fall foul of Article 301 of the Constitution of India?
>
> (3) What are the tests for determining whether the tax or levy is compensatory in nature?
>
> (4) Is the entry tax levied by the States in the present batch of cases violative of Article 301 of the Constitution and in particular have the impugned State enactments relating to entry tax to be tested with reference to both Articles 304(a) and 304(b) of the Constitution for determining their validity?"

SCHEME OF THE CONSTITUTION/DISTRIBUTION OF LEGISLATIVE POWERS:

8. Art. 1 of the Constitution describes India as a Union of States, thereby implying the

indestructible nature of its unity. The country is divided into several units, known as States or Union Territories and the Constitution lays down not only structure of the Union Government but also the structure of the State Governments.

9. Art. 245 of the Constitution deals with “Extent of laws made by Parliament and by the Legislators of State". Art. 245(1) provides that the Parliament may make laws for the whole or any part of the territory of India, and the legislature of a State may make laws for the whole or any part of the State. As per subjects of legislation, all the conceivable subjects have been distributed between the Union and the States with reference to three Lists contained in the Seventh Schedule to the Constitution. The three Lists are exhaustive, yet as a matter of principle and also to meet unforeseen circumstances, Art. 248 and entry 97, List I stipulate that the residuary power vests in the Union i.e., Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent or State List.

10. Art. 246 stipulates that with respect to the matters enumerated in List I, Parliament has the exclusive jurisdiction; with respect to those in List II, State Legislatures have exclusive jurisdiction; and with respect to those in List III, both of them can legislate subject to the discipline enjoined in Art. 254. But the power of Parliament with respect to matters in List I is “notwithstanding anything in clauses (2) and (3)” of Art. 246. In other words, List I has priority over Lists III and II; and List III has priority over List II. The Scheme of legislative relations between the Union and the State is inviolable. [A.*K. Gopalan v. State of Madras*[9]*]*

11. As the opening words of Art. 245(1) state, the legislative powers of both Union and State Legislatures are subject to other provisions of the Constitution even though their powers are plenary within the spheres assigned to them respectively by the Constitution. Legislative competence of State Legislature can only be circumscribed by express prohibition contained in the Constitution itself. Unless and until there is any provision in the Constitution expressly prohibiting legislation on the subject either absolutely or conditionally, there is no fetter or limitation on the plenary powers which the State Legislatures enjoy to legislate on the topics enumerated in List II and List III of the Seventh Schedule to the Constitution. It is noteworthy that though Art. 245 is pre-fixed by the words ‘Subject to the provisions of this Constitution...’; Art. 246 is not. But because Art. 246 only provides for distribution of the legislative powers conferred under Art. 245, the words ‘subject to the provisions of the Constitution’ apply equally to Art. 246.

12. The power of the Parliament and State Legislature to enact laws flows from Articles 245 and 246. Considering the source of legislative powers of the Union and the State in Maharaj Umeg Singh and Others v. The State of Bombay and Others, 1955 (2) SCR 164, it was held as under:-

> “Under Article 246 the State Legislature was invested with the power to legislate on the topics enumerated in Lists II & III of the Seventh Schedule to the Constitution and this power was by virtue of Article 245(1) subject to the provisions of the Constitution."

13. A Constitution Bench of this Court in *K.T. Plantation Private Limited and Another v. State of Karnataka*[10] (Five Judges) observed as under:

> "186. A Constitution Bench of this Court in Hoechst Pharmaceuticals Ltd. case, held that the various entries in List III are not "powers" of legislation but "fields" of legislation. Later, a Constitution Bench of this Court in State of W.B. v. Kesoram Industries Ltd. (2004) 1 SCC 10 held that Article 245 of the Constitution is the fountain source of legislative power. It provides that subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the legislature of a State may make laws for the whole or any part of the State. ''

14. While interpreting Articles 245 and 246, in *State of Kerala and Ors. v. Mar Appraem Kuri Company Limited and Anr*[11]. this Court observed as under:-

> "35. Article 245 deals with extent of laws made by Parliament and by the legislatures of States. The verb "made", in past tense, finds place in the Head Note to Article 245. The verb "make", in the present tense, exists in Article 245 (1) whereas the verb "made", in the past tense, finds place in Article 245 (2). While the legislative power is derived from Article 245, the entries in the Seventh Schedule of the Constitution only demarcate the legislative fields of the respective legislatures and do not confer legislative power as such. While Parliament has power to make laws for the whole or any part of the territory of India, the legislature of a State can make laws only for the State or part thereof. Thus, Article 245 inter alia indicates the extent of laws made by Parliament and by the State Legislatures.
>
> 37. Article 246, thus, provides for distribution, as between Union and the States, of the legislative powers which are conferred by Article 245. Article 245 begins with the expression "subject to the provisions of this Constitution". Therefore, Article 246 must be read as "subject to other provisions of the Constitution".
>
> 38. For the purposes of this decision, the point which needs to be emphasized is that Article 245 deals with conferment of legislative powers whereas Article 246 provides for distribution of the legislative powers. Article 245 deals with extent of laws whereas Article 246 deals with distribution of legislative powers. In these articles, the Constitution Framers have used the word "make" and not "commencement" which has a specific legal connotation. [See Section 3(13) of the General Clauses Act, 1897.]
>
> [Emphasis Supplied]

FREEDOM OF TRADE, COMMERCE AND INTERCOURSE:

15. Art. 301 of the Constitution provides for freedom of trade, commerce and intercourse throughout the territory of India, subject to the other provisions of Part XIII, Articles 302-305 which permit the imposition of reasonable restrictions on this freedom

by Parliament and the State Legislatures. The underlining idea in making trade, commerce and intercourse throughout the territory of India free is to emphasize on the economic unity of India and to ensure that unity of the country may not be broken by internal barriers.

16. The Constitution-makers desired free flow of trade and commerce in India as they realized that economic unity and integration of the country provided the main sustaining force for the stability and progress of the political and economic unity of the nation, and that the country should function as one single economic unity without barriers on internal trade. In order to ensure that the State Legislatures subjected to local and regional pulls did not create trade barriers in future, Art. 301 was incorporated in the Constitution. Art. 301 in general enacts that "subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free". After having declared the general nature of the freedom of trade and commerce, Part XIII of the Constitution sets out the limitations to this freedom, in Articles 302 to 304 which re-state the powers of the Parliament and the State Legislatures in imposing restrictions on the freedom of trade, commerce and intercourse. Articles 302 to 304 are not exceptions to Art. 301. Articles 302 to 304 embody a statement of powers under Art. 246 and the Seventh Schedule with some limitations. Each re-stated power by itself overrides the freedom in Art. 301.

17. Art.302 empowers the Parliament to impose restrictions on the freedom of trade, commerce and intercourse provided they are required in public interest. The purpose of this provision is to allow the Government of India to restrict the movement of goods so as to safeguard a well-balanced economy and for proper organization or supply of goods and services. Famine may be raging in one part of the country while there is plenty in another part, as has been the past experience of the country in regard to food. If Parliament has no effective powers to impose restrictions in such situations on freedom of trade and commerce, then it will undermine the unity of nation. It is reasonable to presume that the Parliament, people's representative is a better judge of public interest and that its judgment must have primacy over any other judgment, including that of the courts.

18. Although Parliament is empowered to restrict the free movement of articles in trade and commerce, normally the laws passed by Parliament in this context ought to be non-discriminatory in character. Art. 303(1) of the Constitution prohibits Parliament and the State Legislature from making "any law giving or authorizing the giving of, any preference to one State over another, or making or authorizing the making or, any discrimination between State and another, by virtue of any entry relating to trade and commerce in any of the Lists in Seventh Schedule" Preference or discrimination amounts to a restriction on the freedom guaranteed under Art. 301 of the Constitution only if it is a law made by the virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule. Application of Art. 303(1) is to specific entries on trade and commerce and not to be confused with the general application of Art. 301 to all the legislative entries other than the entries relating to trade and commerce. But when any part of the country is suffering from scarcity of goods, Parliament may, to meet such a situation; pass even a discriminatory law [Art. 303(2)]. Art. 303(2) is an

exception to Art. 303(1) inasmuch that the limitations of Art. 303(1) lose operation when aforesaid preference and discrimination is made for the purpose of dealing with situation arising from scarcity of goods, and the Parliament may in these situations enact a law that gives or authorises giving preference or makes or authorises making of any discrimination.

19. As per Art. 304(a), a State Legislature may impose any tax on goods imported from other States or Union Territories to which similar goods produced in that State are also subject, so as not to discriminate between the goods so imported and goods so manufactured or produced within the State. A State Legislature is also authorised to impose reasonable restrictions on the freedom of trade and commerce with or within that State as may be required in public interest, subject to the condition that no Bill or Amendment shall be moved in the Legislature of a State without previous sanction of the President [Art. 304(b)]. Art. 304 begins with non-obstante clause and is intended to override both Art. 301 and Art. 303. Art. 304(a) does not prevent taxation of goods; it only prohibits taxes that discriminate between the goods imported from other States and similar goods that are manufactured or produced within the taxing State.

20. Under Art. 305, tax laws existing at the time of the commencement of the Constitution were safeguarded even if they violated the freedom of inter-State trade and commerce along with the power of Parliament to regulate them. At the same time, the President was empowered to make any changes to those laws as he thought fit. This Article in its present form was added by the Fourth Amendment of the Constitution, 1955, and it saves all the existing laws providing for State monopolies which were passed before coming into effect of the Fourth Amendment. Under Art. 307, Parliament is empowered to appoint such authority as it considers appropriate for carrying out the purposes of Articles 301 to 304 and to confer on that authority such powers and duties as it thinks necessary.

21. Part XII and Part XIII of the Constitution lay down the parameters within which State Governments can exercise their right to enact laws/impose tax, restricting the freedom of trade, commerce and intercourse. Purpose of including Part XIII (as it stands today) in the Constitution as emerges from Section 297 of the Government of India Act, 1935 was to confer a freedom of trade, commerce and intercourse, subject to restrictions and non-discriminatory tax laws. In this respect, Art. 301 does not confer any higher right. Even the Constitutional Assembly Debates show that the framers did not intend to confer any absolute freedom of trade, commerce and intercourse. Be it noted that they did not adopt the expression “absolutely free” as found in the Australian Constitution. Reference to “Constituent Assembly Debates 30.07.1949 to 18.09.1949” shows that Dr. B.R. Ambedkar while introducing Part XA: Trade, Commerce and Intercourse within the territory of India Articles 274A to 274D (which corresponds to Articles 301 to 304 and 307) before the Constituent Assembly specifically noted that it is not the intention to make trade, commerce and intercourse absolutely free in India. Relevant extracts from the debate are as under:-

“....I should also like, to say that according to the provisions contained in this part it is not the intention to make trade and commerce absolutely free, that is to say, deprive both Parliament as well as the States of any power to depart from the fundamental

provisions that trade and commerce shall be free throughout India. The freedom of trade and commerce has been made subject to certain limitations which may be imposed by Parliament or which may be imposed by the Legislatures of various states, subject to the fact that the limitation contained in the power of Parliament to invade the freedom of trade and commerce is confined to cases arising from scarcity of goods in any part of the territory of India and in the case of, the States it must be justified on the ground of public interest. The action of the States in invading the freedom of trade and commerce in the public interest is also made subject to a condition that any Bill affecting the freedom of trade and commerce shall have the previous sanction of the President; otherwise, the State would not be in a position to undertake such legislation " (Constituent Assembly Debates (CAD) 30.07.1949 to 18.09.1949 page 1126)

22. In fact, Shri T.T. Krishnamachari, while opposing to the idea of debarring States from imposing any kind of restriction on freedom of trade and commerce emphasized subjecting 'trade and commerce' to State's direct regulation, so that the economic progress of the country was not hindered. Relevant extract is as under:-

> "Shri T.T. Krishnamachari:.... Let me tell the House that so far as I am concerned I think this is about the maximum amount of liberty that we can give for trade and commerce, the maximum amount of concession that we can give to trade and commerce consistent with the future economic improvement of this country. Even as it was originally suggested, that we should make it a matter of fundamental right, and even without the restriction that have been put in article 16, I am afraid the economic progress of the country will become well-nigh impossible. There is absolutely no use in the honourable Member trying to confuse a matter of civil liberty with a mater of rights in respect of trade and commerce. The world has well-nigh come to a position when trade and commerce cannot be run without control and somekind of direction by the Government. If my honorable friends think that we are in the days of the nineteenth century when the laissez faire enthusiast had practically the ordering of everything in the world I am afraid they are mistaken."[CAD Page No.1140 dated 08.09.1949]

23. Reiterating the views of Shri T.T. Krishnamachari, Shri Alladi Krishnaswami Ayyar pointed out that the Scheme as evolved has taken into account larger interest of India along with the interests of particular State, wide geography of the country where the interest of one region differs from the interest of another region, and future prosperity of our country. Relevant extract is as under:-

> "Shri Alladi Krishnaswami Ayyar:.. It may be that manure and other things are required in one part of the country while profiteers from another part of the country may try to transport the goods from the part affected. At the same time, in the interests of the larger economy and the future prosperity of our country, a certain degree of freedom of trade must be guaranteed. My Friend, Mr. Krishnamachari has pointed out that this freedom clause in the Australian Constitution has given rise to considerable trouble and to conflicting decisions of the highest Court. There has been a feeling in those parts of Australia which depend for their well-being on agricultural conditions that their interests are being

sacrificed to manufacturing regions, and there has been rivalry between manufacturing and agricultural interests. Therefore, in a federation what you have to do is first, you will have to take into account the larger interests of India and permit freedom of trade and intercourse as far as possible. Secondly, you cannot ignore altogether regional interests. Thirdly, there must be the power intervention of the Centre in any case of crisis to deal with peculiar problems that might arise in any part of India. All these three factors are taken into account in the Scheme that has been placed before you."[CAD Page No.1143 dated 08.09.1949]

24. Referring to reasonable restrictions that may be imposed by the States and the necessity to obtain sanction from the President, Shri Alladi Krishnaswami Ayyar further observed as under:-

"Shri Alladi Krishnaswami Ayyar:...."Therefore, if on account of parochial patriotism or separatism, without consulting the larger interests of India as a whole if any Bill or amendment is introduced, it will be open to the President, namely, the Cabinet of India to withhold sanction. This is therefore a very restricted power that is conferred on the legislature of a State. After all what is the nature of the power given? The power is confined to imposing such reasonable, restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest therefore the President who has to grant sanction will have the opportunity to see that the legislation is in the public interest and that the restriction imposed is reasonable. It is not possible to devise a water tight formula for the purpose of defining these restrictions."

[CAD Page No.1144 dated 08.09.1949]

25.The purpose of including Part XIII in the Constitution as emerges from the Constituent Assembly Debates was to ensure the interest of the larger economy of the nation and to prevent unreasonable trade barriers in the free flow of trade, commerce and intercourse, impeding economic growth. Framers of the Constitution considered flow of trade, commerce and intercourse throughout the territory of India as important for economic unity, but they did not deify trade, commerce and intercourse nor they entertained any fetish for it. In fact, freedom of trade, commerce and intercourse was initially meant to be a fundamental right but was removed from the part pertaining to 'Fundamental Rights' as it was considered that it did not have any great content as a fundamental right.

26. It was considered that freedom of trade, commerce and intercourse need not be kept at such a high pedestal. It is apposite to refer to the following relevant Debates of the Constituent Assembly.

"Atul Chandra Gupta (Advocate, Calcutta High Court) has suggested that clause (b) of article 244 should be deleted as this clause negatives articles 16 and 243 by its vague generality. Note: Clause (b) of article 244 is based on the recommendation of the Advisory Committee as adopted by the Constituent Assembly. The Drafting Committee has considered it necessary to substitute for

the words “in the interest of public order, morality or health" which occur in the said recommendation, the words “in the public interests". [The Framing of India’s Constitution (Vol. 4) (Page 328)] Shri C. Subramanian (Madras : General): “..There are three Articles 243, 244 and 245 which deal with this subject ‘inter-state trade and commerce’ in the body of the Draft. Then in the list of legislative powers in the Union list, we find in entry 73 “inter-state trade and commerce subject to the provisions of entry 23 of List No. II". Then item 32 in List II is “trade and commerce within the state; markets and fairs"; and item 33 refers to the “regulation of trade, commerce and intercourse with other States for the purposes of the provisions of article 244 of this Constitution." Therefore, you will find inter-state trade and commerce, subject to article 244, is a Union subject. Parliament can deal with it. Trade and commerce within the state and inter-state commerce as provided in article 244 are given to the State Legislatures. You will find, Sir, that in article 244, even though it might be inter-state trade and commerce, the State Legislature is given certain powers to impose certain taxes and impose certain restrictions. Having this in mind, if we come to Article 16, we find the words, “subject to the provisions of article 244 of this Constitution", that is, even in respect of inter-state trade and commerce, the State Legislature has been given certain powers and that is not touched by this article. Therefore leaving that, the article would read “subject to the provisions of any law made by Parliament, trade and commerce and intercourse through the territory of India shall be free". I really fall to understand how this can be a fundamental right and whether there is any right at all reserved. The very conception of a fundamental right is that there is a certain right taken out of the province of the legislature either of the Union or of the State. To put it in other words, the sovereignty vests in the public, but that sovereignty is delegated to the legislatures or the sovereignty is expressed through the legislatures in respect of certain subjects. [CAD Page No. 798, 30.07.1949-18.09.1949] The Honourable Dr. B.R. Ambedkar: ...Now, I quite appreciate the argument that this article 16 is out of place in the list of fundamental rights, and to some extent, I agree with Mr. Subramaniam. But I shall explain to him why it was found necessary to include this matter in the fundamental rights. My Friend, Mr. SUbramaniam will remember that when the Constituent Assembly began, we began under certain limitations. One of the limitations was that the Indian States would join the Union only on three subjects- foreign affairs, defence and communications. On no other matter they would agree to permit the Union Parliament to extend its legislative and executive jurisdiction Or to put it briefly and in a different language, they were not prepared to allow trade and commerce to be included as an entry in List No.I. If it was possible for us to include trade and commerce in List I, which means that Parliament will have the executive authority to make laws with regard to trade and commerce throughout India, we would not have found it necessary to bring trade and commerce under article 16, in the fundamental rights. But as that door was blocked, on account of the basic considerations which operated at the beginning of the Constituent Assembly, we had to find some place, for the purpose of uniformity in the matter of trade and commerce throughout India, under some head. After exercising considerable amount of ingenuity, the only method we found of giving effect to the desire of a large majority of our people

that trade and commerce should be free throughout India, was to bring it under fundamental rights. That is the reason why, awkward as it may seem, we thought that there was no other way left to us, except to bring trade and commerce under fundamental rights. I think that will satisfy my friend Mr. Subramaniam why we gave this place to trade and commerce in the list of fundamental rights, although theoretically, I agree that the subject is not germane to the subject-matter of fundamental rights. With regard to the other argument, that since trade and commerce have been made subject to article 244, we have practically destroyed the fundamental right, I think I may fairly say that my friend Mr. Subramaniam has either not read article 244, or has misread that article. Article 244 has a very limited scope. All that it does is to give powers to the provincial legislatures in dealing with inter-state commerce and trade, to impose certain restrictions on the entry of goods manufactured or transported from another State, provided the legislation is such that it does not impose any disparity, discrimination between the goods manufactured within the State and the goods imported from outside the State. Now, I am sure he will agree that that is a very limited law. It certainly does not take away the right of trade and commerce and intercourse throughout India which is required to be free."

[CAD Page No. 1125, 30.07.1949 to 18.09.1949]

27. After this discussion in the Constituent Assembly, Part XA, (presently Part XIII of the Constitution) was moved and adopted in the present form. The fact that free trade and commerce in Part XIII was initially introduced as a Fundamental Right and then shifted from the Part pertaining to Fundamental Rights indicates that the framers of the Constitution considered that freedom of trade and commerce need not be exalted on par with Fundamental Rights.

FREEDOM UNDER ART. 301 IS SUBJECT TO PARTXIII AND OTHER PARTS OF THE CONSTITUTION PARTS III, IV AND XII ETC.:

28. An argument was advanced that Art. 301 is “subject only” to Part XIII and the same cannot be restricted by general and special powers of the Constitution. In this regard, reliance was placed upon Constituent Assembly Debates where an amendment to Art. 274A was moved by Pandit Thakur Das Bhargav:“I want the word ‘Part’ to be substituted by the word ‘Constitution’", which was not approved. Freedom under Art. 301 in the constitutional context does not mean freedom from all laws, it is subject to restrictions in Part XIII and also to other parts of the Constitution.

29. Art. 301 provides for freedom of trade, commerce and intercourse throughout the territory of India. It strikes an eco-political balance required for the working of a federal structure. Art. 301 cannot be interpreted as to mean a restriction on the plenary power of the State to impose tax in respect of the relevant “fields” in List II of the Seventh Schedule of the Constitution. What it means is that such plenary power of taxation shall not be used to create trade barriers or to discriminate between “goods manufactured within the State” and “goods imported”. The expression in Art. 301 “subject to” is a dominant expression. It indicates subservience of the freedom to Articles 302, 303 and

304.

30. Considering the scope of the expression “subject to” this Court in *K.T. Plantation (P) Ltd v. State of Karnataka*[12] observed:

> “Section 110 of the Land Reforms Act empowers the State Government to withdraw the exemption granted to any land referred to in Sections 107 and 108. Section 107 itself has been made “subject to" Section 110 of the Act. The words “subject to" conveys the idea of a provision yielding place to another provision or other provisions to which it is made subject.”

65. In Black’s Law Dictionary, 5th Edn. At p. 1278, the expression “subject to" has been defined as under:

> “Subject to - Liable, subordinate, subservient, inferior, obedient to; governed or effected by; provided that; provided; answerable for."
>
> 66. Since Section 107 is made subject to Section 110, the former section conveys the idea of yielding to the provision to which it is made subject that is Section 110 which is the will of the legislature...”

31. Interpretation of the Constitution should emerge from a reading of the whole of the Constitution to ensure that the overall objectives are achieved. Part XIII as a whole is based on a balanced scheme and it should be interpreted with reference to other parts of the Constitution including Part III, Part XII and Articles 38 and 39 of the Directive Principles of State Policy. Each of these Parts must be read not in isolation or as water tight compartments but harmoniously as a logical whole. The Constitution must be treated as a logical whole and provisions are not to be read in isolation. In *Kesavananda Bharti v. State of Kerala*[13], the Court stated:

> “56 It is not right to construe words in vacuum and then insert the meaning into an article. *Lord Green observed in Bidie v. General Accident, Fire and Life Assurance Corporation* [14]
>
> 61. I may also refer to the observation of Gwyer, C.J., and Lord Wright:
>
> “A grant of the power in general terms, standing by itself, would no doubt be construed in the wider sense; but it may be qualified by other express provisions in the same enactment, by the implications of the context, and even by considerations arising out of what appears to be the general scheme of the Act.”
>
> (Per Gwyer, C.J. — The Central Provinces and Berar Act, 1939, FCR 18 at 42 MR).
>
> “The question, then, is one of construction and in the ultimate resort must be determined upon the actual words used, read not in vacua but as occurring in a single complex instrument, in which one part may throw light on another. The

Constitution has been described as the federal compact, and the Construction must hold a balance between all its parts." (Per Lord Wright – James v. Commonwealth of Australia, 1936 AC 578 at 613.) See also Kihoto Hollohan v. Zachillhu and Ors. (1992) Supp 2 SCC 651"

[Paras 26 and 27].

32. In *T.M.A. Pai Foundation v. State of Karnataka*[15], the Supreme Court stated:-

"148 When constitutional provisions are interpreted, it has to be borne in mind that the interpretation should be such as to further the object of their incorporation. They cannot be read in isolation and have to be read harmoniously to provide meaning and purpose. They cannot be interpreted in a manner that renders another provision redundant. If necessary, a purposive and harmonious interpretation should be given."

It follows from the above decisions that while interpreting the Constitution the emphasis must be on reading it as a whole, and in a manner that the intent and object of no part of the Constitution is defeated. In this regard, there must be a holistic approach towards the provisions of the Constitution.

33. Object of Part XIII is not to make inter-State trade, commerce and intercourse absolutely free. Part XIII will have to be read along with other Parts of the Constitution namely, Parts III, IV and XII along with the basic features of sovereignty and federalism. Free trade, commerce and intercourse is subject to the other provisions of Part XIII as well as other constitutional provisions. Art. 301 does not use the word subject 'only' to Part XIII. The word "free" in Art. 301 is to be read not in isolation or in the limited context of Part XIII, but has to be read as part of the Constitution as a whole. The word "free" cannot be given a meaning which renders the legislative powers of the State ineffective. For instance, Art. 301 cannot be held to employ freedom from giving minimum wage, gratuity, provident fund etc. to the workers employed.

34. Articles 302 to 304 are neither exceptions nor provisos to Art. 301 and therefore, the principles of interpreting a proviso cannot be applied to them. But both Atiabari and Automobile proceeded on the footing that Art. 302 is in the nature of exception to Art. 301.
Gajendragdkar J. in Atiabari held:

"Thus, the effect of Art. 302 is to provide for an exception to the general rule prescribed by Article 301..." [Pages 853-854]
Similarly, Das J. in Automobile held:

"..The fact of the matter is that there is such a mix up of exception upon exception in the series of articles in Part XIII that a purely textual interpretation may not disclose the true intendment of Articles.. "

[Page 520]

".It seems to us that so far as Parliament is concerned, Art. 303(1) carves out an exception from the relaxation given in favour of Parliament by Art. 302; the relation given by Art. 302 is itself in the nature of exception of the general terms of Art. 301. It would be against the ordinary canons of construction to treat an exception or proviso as having such a repercussion on the interpretation of the main enactment so as to exclude from it by implication what clearly falls within its express term..." [Page 528]

The above view in Atiabari and Automobile is not correct. Articles 302 to 304 embody re-statement of powers under Art. 246 and the Seventh Schedule. Each re-stated power by itself overrides the freedom in Art. 301.

35. Further the majority in Atiabari held that:

".The doctrine of freedom of trade, commerce and intercourse enunciated in Art. 301 is not subject to the other provisions of the Constitution, but is made subject only to the other provision of Part XIII, that means, once the width and amplitude of freedom enshrined in Art. 301 are determined, they cannot be controlled by any provision outside PartXIII..." [Page 848]

The majority appears to have read Art. 301 as "subject only to Part XIII". In the opinion of learned author H.M. Seervai too, the majority view in Atiabari that Art. 301 is subject "only to Part III" was not correct. It is apposite to quote the relevant passage from H.M. Seervai's book on Constitutional Law of India, 4th Edition, Volume 3:

" The reasons are – (1) It read into Art. 301 after the words "subject" the word "only" which is not there and this is contrary to well-settled principles of interpretation. Further, the power to make rules, referred to in Arts. 302 to 305 is governed by Articles 245 and 246, and, therefore, subject to the provisions of our Constitution. (2) The proviso to Art. 304(b) which requires the previous consent of the President to a bill for the purpose of clause (b), necessarily takes us out of Part XIII to Part XI, since Art. 255 in that part provide that the failure to obtain the previous sanction of the President to the introduction of the bill can be made good by his subsequent assent. It follows therefore that the freedom guaranteed by Art. 301 is not limited to restriction permitted only by Art. 304(b) for the proviso to it is overridden by Art.255 (3). Trade is dealt with not only in Art. 301 but also in Art. 19(1)(g) and the relation of that Article is necessary for a proper interpretation of Part XIII. Article 19(1)(g) guarantees to every citizen the right to carry on any trade or business. But trade cannot be carried on without goods or property and the right to acquire, hold and dispose of property which is guaranteed under Art; 19(1) (f). Again, it is not only Art.303 which speaks of discrimination "Arts. 14 and 15 do likewise and the relation of this Article to 303 must be considered."

[Page 2591]

The States are right in submitting that the majority view, both in Atiabari and Automobile, is not correct. Part XIII and Freedom of Trade, Commerce and Intercourse will have to be read with other Parts of the Constitution, particularly, Part III, IV and XII and basic features of sovereignty and federalism.

QUESTION NO.1: CAN THE LEVY OF A NON-DISCRIMINATORY TAX PER SE CONSTITUTE INFRACTION OF ARTICLE 301 OF THE CONSTITUTION OF INDIA?

Power to Tax is an incident of State Sovereignty:-

36. Entries relating to taxation and levy of duty under the State List, Seventh Schedule are Entries 46-62 and under the Concurrent List, Seventh Schedule are Entries 35, 43 and 44. The power to tax is a sovereign right of the State and is essential to the very existence of a Government. Any fetters on the power of the State to generate revenue through taxes have a direct impact on the autonomy and governance of the State.

37. The term 'tax' is ordinarily used to express the exercise of the sovereign power to raise revenue for the expenses of the Government. Judge Cooley in his memorable work on the "Law of Taxation" stated that taxation is a mode of raising revenue for a public purpose; and the power of taxation is an essential and inherent attribute of sovereignty, belonging as a matter of right to every independent Government. He defined the power of taxation as the power inherent in the sovereign State to recover a contribution of money or other property in accordance with some reasonable rule of apportionment from the property or occupations within its jurisdiction for the purpose of defraying the public expenses: -

> ".It is obvious that it is an incident of sovereignty, and is co-extensive with that to which it is an incident. All subjects over which the sovereign power of a State extends are objects of taxation, but those over which it does not extend are, upon the soundest principles, exempt from taxation. This proposition may almost be pronounced self-evident. The power of taxation is an essential and inherent attribute of sovereignty, belonging as a matter of right to every independent Government. It is possessed by the Government without being expressly conferred by the people. The power is inherent in the people because the sustenance of the government requires contributions from them. In fact the power of taxation may be defined as "the power inherent in the sovereign state to recover a contribution of money or other property, in accordance with some reasonable rule or apportionment, from the property or occupation within its jurisdiction for the purpose of defraying the public expenses"."

(Cooley, Taxation (4th Edition) Pages. 72, 149, 150; Referred to in the Article Power to Tax by Herman M. Knoeller reported in Market Law Review Volume 22 Issue 3 April, 1938.)

38. This Hon'ble Court has held in a catena of cases that power to levy tax is a sovereign power of the State starting from *Raja Jagannath Baksh Singh v. The State of U.P. and Anr*[16]*.,* where this Hon'ble Court observed that:-

> " The power of taxation is, no doubt, the sovereign right of the State; as was observed by Chief Justice Marshall in M'Culloch v. Maryland [4 Law Edn. 579 p. 607] : "The power of taxing the people and their property is essential to the very existence of Government, and may be legitimately exercised on the objects to which it is applicable to the utmost extent to which the Government may choose to carry it. " In that sense, it is not the function of the Court to enquire whether the power of taxation has been reasonably exercised either in respect of the amount taxed or in respect of the property which is made the object of the tax. Article 265 of the Constitution provides that no tax shall be levied or collected, except by authority of law; and so, for deciding whether a tax has been validly levied or not, it would be necessary first to enquire whether the legislature which passes the Act was competent to pass it or not." [Emphasis Supplied] [Page 232-233]

39. Power to tax is a sovereign power and is legislative in character and it has to be exercised within the constitutional limitation. In *State of W.B. v. Kesoram Industries Ltd. and Others*[17] it was held as under:-

> "109. The primary purpose of taxation is to collect revenue. Power to tax may be exercised for the purpose of regulating an industry, commerce or any other activity; the purpose of levying such tax, an impost to be more correct, is the exercise of sovereign power for the purpose of effectuating regulation though incidentally the levy may contribute to the revenue..."
>
> Power of taxation has been regarded as an inherent attribute of sovereignty emanating from necessity. Same view was reiterated in *Yadlapati Venkateswarlu v. State of A.P*[18]*. [Para 9], State of U.P. & Anr. v. Synthetics and Chemicals Ltd. & Anr*[19]*. [Para 44], Amrit Banaspati Co. Ltd. and Anr. v. State of Punjab and Anr. [Para 10], Dena Bank v. Bhikhabhai Prabhudas Parekh & Co. and Ors*[21]*.* [Para 8]."

40. Subject to the Constitution and its inherent restrictions, the power of taxation is regarded as political and supreme. Power to levy tax is indispensable for the existence of any civilized Government as it is a necessity for its support and maintenance. Without taxes, for lack of source of revenue, the Government would become paralyzed. How much revenue is to be drawn and from which source is a matter of fiscal policy and wholly depends on the needs of a State. In order to support the existence of the State and its welfare activities, as mandated by the Directive Principles of the State Policy, the State is empowered to raise revenue through, (i) taxes and duties; (ii) loans raised by the issue of treasury bills, loans or ways and means of advances; (iii) fees for licenses; (iv) fees for services rendered; and (v) fines or other pecuniary penalties (Articles 199, 207 and 266). On behalf of the State, it was submitted that there are fiscal limitations against taking loans in view of debt servicing; even otherwise tax is preferable as it is a mode of re-distributing wealth in the form of public welfare.

41. In *Elel Hotels & Investments Ltd. and Others v. Union of India* [22]it was held:-

"20....Taxation is not now a mere source of raising money to defray expenses of Government. It is a recognized fiscal tool to achieve fiscal and social objectives..."

42. Parts XI and XII of the Constitution deal with "Relations between the Union and the States" and "Finance, Property, Contracts and Suits" respectively. Part XII dealing with finance etc. has been treated as Part dealing with the sovereign power of the States to impose taxes, which must always mean imposing burden on citizens and others in public interest. The power of taxation is vested in a sovereign State to carry on with the affairs of the Government. Our Constitution had laid the foundation of a Welfare State, very much extending the activities of the Government and the administration thus making it necessary for the State to impose taxes on a large scale and in much wider fields. The legislative competence of the Parliament or of the State Legislatures can only be circumscribed by express prohibition contained in the Constitution itself. The plenary powers of legislation vested in the Union and State Legislatures by the Constitution are not subject to any limitations other than those imposed by the Constitution itself.

43. In *Maharaj Umeg Singh and Ors. v. The State of Bombay and Ors*[23]. this Court held that since the power of the State to legislate within its legislative competence is plenary and the same cannot be curtailed in the absence of an express limitation placed on such power in the Constitution itself, there is no express prohibition on the legislative powers of the State to levy taxes on the goods entering into a local area for consumption, use or sale thereon. Taxes being the lifeblood of the State, they cannot be decimated by implication.

44. The power to tax is a sovereign power and is legislative in character. In a federal system, the legislative power is exercised by distribution of powers between the Union and the States; both are supreme in their respective spheres. State's power despite the limited width of its field is plenary in nature. Except where the constitutional intent is express and clear, the State's plenary power ought not to be whittled down by interpretation. In the present reference, we are concerned with entry 52, List II "Taxes on the entry of goods into a local area for consumption, use or sale therein". Entry tax is a tax levied on 'Entry of goods into a local area' for the purpose of consumption, use or sale therein. States within their spheres are autonomous entities and have the competence to enact legislation in the fields enumerated in List II of Seventh Schedule.

45. In the State List, there are eighteen entries on which the State Legislature has the power to levy taxes. States and only States have power to enact legislation in the above fields levying taxes and raise revenue. The above entries in List II relating to the imposition of taxes by the States, despite the limited width of its field are plenary in nature. States must have revenue to carry out their administration and the States are entitled to raise revenue by exercising its power to tax. Such an important power of taxation expressly granted under the Constitution cannot be allowed to be whittled down and made subservient to trade, commerce and intercourse.

46. Tax has always been treated as a distinct entity and is kept on a pedestal separate

from all the other legislative fields of the Seventh Schedule. It is worth repeating that the power of taxation is an inherent attribute of sovereignty emanating from necessity. As noted earlier, the exaction is not merely fundamental for existence of the State but also to support the welfare activities, therefore, it forms a pre-condition for exercise of other legislative power. The special status conferred on taxing statutes is evident from the following special provisions: Article 265 provides that no tax shall be levied or collected except by the authority of law; therefore there can be no levy or collection by exercise of executive power. Tax legislations are given the status of Money Bills under Articles 110 and 199 of the Constitution and, therefore, have a different laying procedure. They can originate only in the lower houses of the Parliament and the State Legislature as per Articles 109 and 198. Being a Money Bill, all the revenue is sent to the Consolidated Fund and can only be taken out through Appropriation Bills (Articles 114 and 204). Freedom in Art. 301 does not mean freedom from taxation –

47. Historically, Art. 301 was meant to do away with barriers between 'Native States' and the rest of India. Thus, Art. 301 should be interpreted in the light of the object i.e. "economic integration of the nation", as opposed to being aimed at any or every action which can possibly have an impact on trade, commerce and intercourse. "Free" in Art. 301 does not mean freedom from taxation; taxation simpliciter is not within the purview of Art. 301. In a sense, every tax imposed by a State Legislature may have an indirect effect on the flow of trade, commerce and intercourse. If the power of the State Legislature to enact any tax laws is held to be subject to the limitation under Art. 301, the legislative power of the State to levy taxes under various entries in List II would be rendered ineffective.

48. In various provisions in Part XII of the Constitution certain restrictions have specifically been incorporated on State's power to levy tax. Restrictions as to imposition of tax on the sale or purchase of goods [Art. 286]; Taxes on professions, trades, callings and employments, in terms of which power of the State Legislature is limited to levy tax on professions where the total amount payable is not exceeding rupees two thousand and five hundred per annum [Art. 276(2)]; the limitation on State's taxing power imposed by the Constitution itself or power is given to Parliament to provide the limitations by a law [Art.286 (2) and (3)]; Exemption from taxation by States in respect of water or electricity in certain cases and the power of the State Legislature to levy such tax after obtaining assent of the President [Articles 288, 288 (1) and (2)]; Identically, there are at least five entries in List II [entries 50, 51, 54, 55 and 57] which specifically provide that they are subject to the limitations/principles prescribed by Parliament by law made under List I and List III.

49. In the Constitution, wherever exemption from taxes were contemplated, they were expressly provided for–Exemption of property of the Union from State taxation [Art. 285]; Exemption from taxes on electricity [Art. 287]; Exemption from taxation by States in respect of water or electricity in certain cases [Art. 288]; Exemption of property and income of a State from Union taxation [Art. 289]. Exemption from tax power of Parliament/State Legislature must thus be provided expressly and unambiguously. Art. 289(2) shows that the trade or business carried on by, or on behalf of, the Government of the State, can also be subjected to tax and the tax could be "to such extent', if any, as

Parliament may by law provide. When even the trade or business carried on by or on behalf of the Government of the State can also be subjected to tax, it would be erroneous to hold trade, commerce and intercourse carried on by private individuals and companies in the country free from tax; and that too, by implication.

50. It is well-settled that even Fundamental Rights in Part III of the Constitution are not immune from taxation and taxation has been held to be "not a restriction". In *Indian Express Newspapers (Bombay) Pvt. Ltd. And Ors. etc. v. Union of India and Ors. Etc*[24]*.* levy of indirect tax on newspaper industry, through levies on imported newsprints was challenged as violative of Art. 19(1)(a). Holding that press is not immune from taxes it was held:-

> "49 Yet the American courts have recognized the power of the State to levy taxes on newspaper establishments, of course, subject to judicial review by courts by the application of the due process of law principle....Taxation is the legal capacity of sovereignty or one of its governmental agents to exact or impose a charge upon persons or their property for the support of the government and for the payment for any other public purposes which it may constitutionally carry out.
>
> 65. Newspaper industry enjoys two of the fundamental rights, namely the freedom of speech and expression guaranteed under Article 19(1) (a) and the freedom to engage in any profession, occupation, trade, industry or business guaranteed under Art. 19(1) (g) of the Constitution, the first because it is concerned with the field of expression and communication and the second because communication has become an occupation or profession and because there is an invasion of trade, business and industry into that field where freedom of expression is being exercised. While there can be no tax on the right to exercise freedom of expression, tax is leviable on profession, occupation, trade, business and industry. Hence tax is leviable on newspaper industry. But when such tax transgresses into the field of freedom of expression and stifles that freedom, it becomes unconstitutional. As long as it is within reasonable limits and does not i mpede freedom of expression it will not be contravening the limitation of Art. 19(2). The delicate task of determining when it crosses from the area of profession, occupation, trade, business or industry into the area of freedom of expression and interferes with that freedom is
>
> 69. In the case of ordinary taxing statutes, the laws may be questioned only if they are either openly confiscatory or a colourable device to confiscate. On the other hand, in the case of a tax on newsprint, it may be sufficient to show a distinct and noticeable burdensomeness, clearly and directly attributable to the tax."
>
> [Emphasis added]

51. In *All Bihar Schools Association and Anr. v. State of Bihar and Ors*[25]*.* it was held that religious minority institutions are not immune from general laws including tax measures and social welfare legislations. *Similarly, in Printers (Mysore) Ltd. and Anr. v.*

Asstt. Commercial Tax Officer and Ors[26]. after referring to Express Newspapers case, it was held that press is not immune from taxation or general law. Thus when even Fundamental Rights are not free from taxation, trade, commerce and intercourse cannot claim immunity from taxation.

52. Art. 304(a) allows levy of tax on goods imported from other States, any tax, to which similar goods manufactured or produced in that State are subject So as not to discrimin-ate between goods so imported and goods so manufactured or produced within the State. Art. 304(a) states non-discriminatory tax does not impede the flow of trade, commerce and intercourse. Art. 304(a) applies where the following conditions are cumulatively satisfied:-

> "(a) the State Legislature by law imposes a tax;
>
> (b) tax is imposed on goods imported into that State from other States or Union Territories;
>
> (c) a tax is also imposed on similar goods manufactured or produced in that State; and
>
> (d) there is no discrimination between goods imported and goods manufactured or produced in that State. When these four conditions are fulfilled, Art. 304(a) provides a constitutional route to levy non-discriminatory tax. Under Art. 304(b), the ban under Art.301 stands lifted even if discriminatory restrictions are imposed by the State Legislatures, provided they fulfill the following conditions-(a) such restrictions are in public interest; (b) they are reasonable; and (c) they are subject to obtaining of prior sanction of the President before introduction of the Bill or amendment.

53. While the States have legislative power to levy taxes on goods imported from other States, Art. 304(a) imposes restrictions on this power of the States to levy a tax on goods that would result in discrimination between goods imported from other States and similar goods manufactured or produced within the States. The non-obstante clause in Art. 304 with respect to Art. 301, actually indicates that since tax does not fall within the purview of Art. 301, therefore, Art. 304(a) was brought in to provide against discrimination based on source or destination of goods. Art. 304(a) is thus a restriction on the tax powers of the States, not to discriminate between the goods imported into the State with similar goods manufactured or produced within the taxing State.

54. Constituent Assembly Debates indicate that the framers of the Constitution while intending to guarantee free flow of trade, commerce and intercourse did not deify it. As discussed earlier, at the time of drafting Constitution, provision containing freedom of trade, commerce and intercourse which was initially shown as Fundamental Rights; but after debates, it was shifted to a separate Part [Part XIII]. The framers of the Constitution did not intend that trade, commerce and intercourse is free from taxation. Art. 304 provides for the power of the States to impose taxes, subject of course, the levy is not discriminatory. Hence, Art. 301 ought not to be read as freedom from tax laws.

55. In this regard, we may usefully refer to Constituent Assembly Debates/Framing of India's Constitution: Shri Alladi Krishnaswami Ayyar

> "And then, "Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which goods produced in the unit are subject". That is to say we ought not to differentiate; but at the same time, goods coming in should not go scot free: they should be subject to the same duty as goods produced in the area" (The framing of India's Constitution, Select Documents by Universal Law, Law Publishing Pvt. Co. Pvt. Ltd. Vol.2 Page.253) Gobind Ballabh Pant
> "There is unanimity about the body of this clause and it is clear that there should not be any discrimination against one unit by another unit. Otherwise we will be going against the very sense of a Union of Federal Constitution. If the units are to be discriminated against we will come to blows more often than otherwise. Therefore this should be avoided"(The framing of India's Constitution, Select Documents by Universal Law, Law Publishing Pvt. Co. Pvt. Ltd. Vol.2 Page.254) Shri Krishnaswami Ayyar
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> "So far as article 16 is concerned, the substance of the freedom of trade guarantee is preserved. We have prohibited the States and the Centre from passing discriminatory laws" [Constituent Assembly Debates dated 30.07.1949 to 18.09.1949 (Page 1144)]

56. A tax legislation could be challenged on the ground of legislative competence as well as violation of Fundamental Rights guaranteed under Part III of the Constitution. In Rai Ramkrishna and Ors. v. The State of Bihar (1964) 1 SCR 897, this Court while holding that tax Statutes were not beyond the constitutional limitation prescribed by Articles 14 and 19 held that the challenge must however be dealt with caution and circumspection:

> "13 that taxing statutes are not beyond the pale of the constitutional limitations prescribed by Articles 19 and 14, and he also concedes that the test of reasonableness prescribed by Art. 304(b) is justiciable. It is, of course, true that the power of taxing the people and their property is an essential attribute of the Government and Government may legitimately exercise the said power by reference to the objects to which it is applicable to the utmost extent to which Government thinks it expedient to do so. The objects to be taxed so long as they happen to be within the legislative competence of the legislature can be taxed by the legislature according to the exigencies of its needs, because there can be no doubt that the State is entitled to raise revenue by taxation. The quantum of tax levied by the taxing statute, the conditions subject to which it is levied, the manner in which it is sought to be recovered, are all matters within the competence of the legislature, and in dealing with the contention raised by a citizen that the taxing statute contravenes Art. 19, courts would naturally be circumspect and cautious. Where for instance, it appears that the taxing statute is plainly discriminatory, or provides no procedural machinery for assessment and

levy of the tax, or that it is confiscatory, Courts would be justified in striking down the impugned statute as unconstitutional. In such cases, the character of the material provisions of the impugned statute is such that the Court would feel justified in taking the view that, in substance, the taxing statute is a cloak adopted by the legislature for achieving its confiscatory purposes. This is illustrated by the decision of this Court in the case of Kunnathet Thathunni Moopil Nair v. State of Kerala [1961] 3 SCR 77, where a taxing statute was struck down because it suffered from several fatal infirmities. On the other hand, we may refer to the case of Raja Jagannath Baksh Singh v. State of Uttar Pradesh [1962] 46 ITR 169 (SC), where a challenge to the taxing statute on the ground that its provisions were unreasonable was rejected and it was observed that unless the infirmities in the impugned statute were of such a serious nature as to justify its description as a colourable exercise of legislative power; the Court would uphold a taxing statute."

[Emphasis supplied]

57. In *Hari Krishna Bhargav v. Union of India and Anr*[27]. the Bench noting the effect the series of decisions has had on Ramjilal, concluded that although the power to tax is not a power that transcends fundamental rights, a taxing Statute cannot merely be challenged on the ground that it is harsh and excessive. It was observed as under:-

"10. It was urged that even if the exercise of the powers to compel deposits be regarded as not unconstitutional, its exercise is harsh and the demands made by the State are excessive. Exercise of the taxing power by the State has undoubtedly to be tested in the light of the fundamental freedoms guaranteed by Ch. III of the Constitution. It is not a power which transcends the fundamental rights, as was assumed in certain earlier decisions : Ramjilal v. Income-tax Officer (1951) 19 ITR 174 (SC) ; Laxmanappa Hanumantappa v.Union of India (UOI) (1954) 26 ITR 754 (SC); and the view expressed by Venkatarama Ayyar J., in S. Anantha Krishnan v. State of Madras I.L.R. [1952] Mad. 933. But it is now settled by decisions of this Court (e.g.) Kunnathat Thathunni Moopil Nair v. The State of Kerala and Another (1961) 3 SCR 77 that a taxing statute is subject to the "conditions laid down in Art. 13 of the Constitution". A taxing statute may accordingly by open to challenge on the ground that it is expropriatory; or that the statute prescribes no procedure or machinery for assessing tax, but it is not open to challenge merely on the ground that the tax is harsh or excessive."

[Emphasis supplied]

Consistent view taken in the above series of decisions and other decisions is that tax legislations can be challenged on the ground that they infringe the Fundamental Rights under Part III but that does not however mean that there is freedom from taxation or that tax is per se a restriction on Fundamental Rights or freedom of trade, commerce and intercourse.

Tax is not a restriction per se:

58. The above Constituent Assembly Debates and the history of Art. 301 show that freedom envisaged in Art. 301 is not freedom from taxation but only freedom from trade barriers. So long as the tax remains non-discriminatory, its validity cannot be judged under Art. 301. Under Art. 246(3) of the Constitution, a 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 of the Seventh Schedule. Art. 246(3) is subject to clauses (1) and (2) of Art. 246 i.e. matters enumerated in Lists I and III of the Seventh Schedule. As per Art. 265, a tax can be imposed only under authority of law and there is no role of the Executive. Taxation includes the imposition of any tax as defined under Art. 366(28): "taxation" includes the imposition of any tax or impost, whether general or local or special, and "tax" shall be construed accordingly. It is a sovereign power of compulsory exaction as a part of any burden by public authority for public purposes enforceable by law. Imposing a tax is a compulsory exaction made for a public purpose without reference to any special benefit to the taxpayers.

59. The taxing power of the State stands independently fortified by Parts XI and XII of the Constitution of India and can only be challenged on the ground of reasonableness. It needs no reiteration that power of States to levy taxes for the purpose of governance and carrying out its welfare activities is a necessary attribute of State's sovereignty and in that sense it is a power of supreme attribute. It is well-settled that taxes are levied in public interest and hence, cannot be considered a restriction per se on the enjoyment of any freedom contemplated by the Constitution. It would be highly unjustified to view a taxing Statute as a restriction on individual freedoms.

60. The essential characteristics of a tax are that: (i) it is imposed under a statutory power without the taxpayer's consent and the payment is enforced by law; (ii) it is an imposition made for public purpose without reference to any special benefit to be conferred on the payer of the tax; and (iii) it is part of the common burden. In *Commissioner Hindu Religious Endowments. Madras v. Sri Lakshmindra Thirtha Swamiar of Sri Shirur Mutt*[28] the Constitution Bench has laid down the characteristics of a tax which has since been consistently followed and it is as under :-

> ".. A tax is a compulsory exaction of money by a public authority for public purposes enforceable by law and is not payment "for services rendered". This definition brings out, in all opinion, the essential characteristics of a tax as distinguished from other forms of imposition which, in a general sense, are included within it. It is said that the essence of taxation is compulsion, that is to say, it is imposed under statutory power without the taxpayer's consent and the payment is enforced by law. The second characteristic of tax is that it is an imposition made for public purpose without reference to any special benefit to be conferred on the payer of the tax. This is expressed by saying that the levy of tax is for the purposes of general revenue, which when collected revenues of the State. As the object of a tax is not to confer any special benefit upon any particular individual there is as it is said, no element of "quid pro quo" between the taxpayer and the public authority. Another feature of taxation is that as it is a part of the common burden, the quantum of imposition upon the taxpayer depends generally upon his capacity to pay."

The above decision was followed in *Indian Medical Association v. V.P. Santha and Ors*[29]*. and also in State of Gujarat and Ors. v. Akhil Gujarat Pravasi V.S. Mahamandal and Ors*[30]*.*

61. A five Judges Bench of this Court in *Federation of Hotel and Restaurant Association of India, Etc. v. Union of India and Ors*[31]*.* has held that mere excessiveness of a tax or even the circumstance that its imposition might tend towards diminution of the earnings or profits of the persons of incidence does not per se and without more, constitute violation of Art. 19(1)(g). The relevant extract from the judgment is as under:

> "62. A taxing statute is not, per se, a restriction of the freedom under Article 19(1)(g). The policy of a tax, in its effectuation, might, of course, bring in some hardship in some individual cases. But that is inevitable, so long as law represents a process of abstraction from the generality of cases and reflects the highest common factor. Every cause, it is said, has its martyrs. Then again, the mere excessiveness of a tax or even the circumstance that its imposition might tend towards the diminution of the earnings or profits of the persons of incidence does not, per se, and without more, constitute violation of the rights under Article 19(1)(g)."

62. Similar view was expressed in *Express Hotels Private Limited v. State of Gujarat and Anr*[32]*.* A taxing Statute is not per se restriction of the freedom under Art. 19(1)(g):

> "28. So far as the argument that Fundamental Rights under Article 19(1)(g) are violated by a levy on a mere provision for luxury, without its actual utilisation, is concerned it is settled law that the mere excessiveness of a tax or that it affects the earnings cannot, per se, be held to violate Article 19(1)(g)....''

63. Art. 304(a) authorizes a State Legislature to impose a non-discriminatory tax on goods imported from other States. Art. 304(a) does not prevent levy of tax on goods; what it prohibits is such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. The object is to prevent imported goods from being discriminated by imposition of a higher tax thereon than the local goods. Under Art. 304(b), States can impose reasonable restrictions on the freedom of trade, commerce and intercourse with or within that State as may be required in public interest; provided they obtain prior sanction of the President before introduction of the Bill. As taxes are levied for the purpose of raising revenue, they are not restrictions and are presumed to be in public interest. Thus, tax simpliciter is not a restriction on the freedom of trade and commerce and is outside the purview of Art. 301. Majority view in Atiabari and Automobile: Need of re-appreciation:-

64. In *Atiabari Tea Co. Ltd. v. The State of Assam and Ors.*[33]*,* Assam Legislature enacted the Assam Taxation (On Goods Carried by Roads or Inland Waterways) Act, 1954 acting on entry 56 of the State List and imposed tax at a rate of one anna per pound of tea in chest box, carried through the State of Assam by any means other than the railways and the air. The appellant who carried their tea to Calcutta in the State of

West Bengal through the State of Assam assailed the validity of the Act inter alia on the ground that it violated Art. 301 of the Constitution. Contention of the appellant was that words of Art. 301 are very wide and unambiguous and that it would be unreasonable to exclude from its ambit a taxing law which restricted trade, commerce or intercourse either directly or indirectly. The respondent-State of Assam urged that the provisions of sovereign power of the State to levy tax under Parts XI and XII of the Constitution stood by themselves and that the tax would not fall foul of Part XIII.

65. After discussing various provisions of Part XIII and after tracing the constitutional background, speaking for the majority, Justice Gajendragadkar held as under:-

> " Thus considered we think it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Art. 301 would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Art.301. The argument that all taxes should be governed by Article 301 whether or not their impact on trade is immediate or mediate, direct or remote, adopts, in our opinion, an extreme approach which cannot be upheld. If the said argument is accepted it would mean, for instance, that even a legislative enactment prescribing the minimum wages to industrial employees may fall under Part XIII because in an economic sense an additional wage bill may indirectly affect trade or commerce. We are, therefore, satisfied that in determining the limits of the width and amplitude of the freedom guaranteed by Art. 301 a rational and workable test to apply would be: Does the impugned restriction operate directly or immediately on trade or its movement?" [Page 860] [Emphasis Supplied] The majority based its opinion on the reasoning that any legislation whether taxing or otherwise which imposed any restrictions that had the effect of directly offending the movement or transport of goods would attract the provisions of Art. 301 and its validity could be sustained only if it satisfied Art. 302 or Art. 304(b) of the Constitution.

66. Sinha, C.J. in his dissenting judgment referred to the integration of "Native States" with the Government of India and how the "Native States" ultimately merged their individualities into India to emerge as one political unit with the result that what was called British India became under the Constitution 'Part-A States', and the "Native States" became 'Part-B States'. Sinha, C.J. pointed out that most of the "Native States", big or small had their own taxes, cesses, tolls and other imposts and duties meant not only for raising revenue but also as trade barriers and tariff walls. In the background of those circumstances, it was necessary to abolish all those trade barriers and custom posts as also in the interest of national solidarity, economic and cultural unity and freedom of trade and commerce guaranteed in the Constitution by Art. 301. Observing that the power to tax is inherent in sovereignty, public purpose is inherent in every taxation and tax simpliciter is not an impediment to the freedom of trade, commerce and intercourse, Sinha C.J. held as under:-

> ".. If that were so, all laws of taxation relating to sale and purchase of goods on

carriage of goods and commodities, men and animals, from one place to another, both inter-State and intra-State would come within the purview of Art.301 and the proviso to Art. 304(b) would make it necessary that all Bills or Amendments of pre-existing laws shall have to go through the gamut prescribed by that proviso. That will be putting too great an impediment to the power of taxation vested in the States and reduce the States' limited sovereignty under the Constitution to a mere fiction. That extreme position has, therefore, to be rejected as unsound." [Page 827] In my opinion, another very cogent reason for holding that taxation simpliciter is not within the terms of Art. 301 of the constitution is that the very connotation of taxation is the power of the State to raise money for public purposes by compelling the payment by persons, both natural and juristic, of monies earned or possessed by them, by virtue of the facilities and protection afforded by the State. Such burdens or imposts, either direct or indirect, are in the ultimate analysis meant as a contribution by the citizens or persons residing in the State or dealing with the citizens of the State, for the support of the Government, with particular reference to their respective abilities to make such contributions. Thus public purpose is implicit in every taxation, as such. Therefore, when Part XIII of the Constitution speaks of imposition of reasonable restrictions in public interest, it could not have intended to include taxation within the generic term "reasonable restrictions" [Page 828]

....The objections against the contention that taxation was included within the prohibition contained in Part XIII may thus be summarized:

(1) Taxation, as such, always implies that it is in public interest. Hence, it would be outside particular restrictions, which may be characterized by the Courts as reasonable and in public interest. (2) The power is vested in a sovereign State to carry on Government. Our Constitution has laid the foundations of a welfare State, which means very much expanding the scope of the activities of Government and administration, thus making it necessary for the State to impose taxes on a much larger scale and in much wider fields. The legislative entries in the three lists referred to above empowering the Union Government and the State Governments to impose certain taxations with reference to movements of goods and passengers would be rendered ineffective, if not otiose, if it were held that taxation simpliciter is within the terms of Art. 301. (3) If the argument on behalf of the appellants were accepted, many taxes, for example, sales tax by the Union and by the States, would have to go through the gamut prescribed in Articles 303 and 304, thus very much detracting from the limited sovereignty of the States, as envisaged by the Constitution. (4) Laws relating to taxation, which is essentially a legislative function of the State, will become justiciable and every time a taxation law is challenged as unconstitutional, the State will have to satisfy the courts - a course which will seriously affect the division of powers on which modern constitutions, including ours, are based. (5) Taxation on movement of goods and passengers is not necessarily an impediment.^Page 829] Article 301, with which Part XIII commences, contains the crucial words "shall be free" and provides the key to the solution of the problems posed by the whole Part. The freedom declared by this Article is not an absolute freedom from all legislation.

> As already indicated, the several entries in the three Lists would suggest that both Parliament and State Legislatures have been given the power to legislate in respect of trade, commerce and intercourse, but it is equally clear that legislation should not have the effect of putting impediments in the way of free flow of trade and commerce. In my opinion, it is equally clear that the freedom envisaged by the Article is not an absolute freedom from the incidence of taxation in respect of trade, commerce and intercourse, as shown by Entries 89 and 92 A in List I, Entries 52, 54 and 56 to 60 in List II and Entry 35 in List III. All these entries in terms speak of taxation in relation to different aspects of trade, commerce and intercourse. The Union and State Legislature, therefore, have the power to legislate by way of taxation in respect of trade, commerce and intercourse, so as not to erect trade barriers, tariff walls or imposts, which have a deleterious effect on the free flow of trade, commerce and intercourse. That freedom has further been circumscribed by the power vested in Parliament or in the Legislature of a State to impose restrictions in the public interest. Parliament has further been authorised to legislate in the way of giving preference or making discrimination in certain strictly limited circumstances indicated in cl. (2) of Art. 303. Thus, on a fair construction of the provisions of Part XIII, the following propositions emerge: (1) trade, commerce and intercourse throughout the territory of India are not absolutely free, but are subject to certain powers of legislation by Parliament or the Legislature of a State; (2) the freedom declared by Art.301 does not mean freedom from taxation simpliciter, but does mean freedom from taxation which has the effect of directly impeding the free flow of trade, commerce and intercourse; (3) the freedom envisaged in Art. 301 is subject to non-discriminatory restrictions imposed by Parliament in public interest (Art.302); (4) even discriminatory or preferential legislation may be made by Parliament for the purpose of dealing with an emergency like a scarcity of goods in any part of India [Art. 303(2)]; (5) reasonable restrictions may be imposed by the Legislature of a State in the public interest [Art. 304(b)]; (6) non-discriminatory taxes may be imposed by the Legislature of a State on goods imported from another State or other States, if similar taxes are imposed on goods produced or manufactured in that State [Art. 304(a)]; and lastly (7) restrictions imposed by existing laws have been continued, except insofar as the President may by order otherwise direct (Art. 305).
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> [Page 831-832] [Emphasis added]

67. A larger Bench of seven Judges was constituted in *Automobile Transport (Rajasthan) Ltd. v. The State of Rajasthan and Ors*[34]. in which the validity of Rajasthan Motor Vehicles Taxation Act, 1951 and the Rules made thereunder was under challenge. Section 4 of the
Rajasthan Act required every owner of motor vehicle “used in any public place or kept for use in Rajasthan” to pay tax at the appropriate rate specified in the Schedule to the Act. The appellants therein who were stage carriage operators challenged the validity of the Rajasthan Act on the ground that such levy contravened Art. 301 of the Constitution and was not saved by Art. 304(b) thereof. The validity of the Rajasthan Act was upheld by a majority of 4:3. Justice S.K. Das who spoke for the majority, agreed with the

majority view of Atiabari that only those restrictions which directly and immediately restrict or impede the free flow of trade, commerce and intercourse would be in violation of Art. 301. But the majority in Automobile added a clarification that a regulatory measure or measures imposing compensatory taxes for the use of trading facilities would not come within the purview of restrictions contemplated by Art. 301 and such measures need not comply with the requirements of Art. 304(b).

68. While concurring with the majority view that the provisions of the Rajasthan Motor Vehicles Taxation Act 1951, are regulatory in character, delivering a separate judgment. Justice Subba Rao widely referred to Section 92 of the Australian Constitution to hold that the Court will have to ascertain whether the impugned law in a given case affects the movement directly or indirectly. It was held that "only if a tax directly and immediately affects the movement of trade, it would be violating the freedom; on the other hand if the impact is indirect and remote it would be unobjectionable.

69. On behalf of the assessees, it has been argued before us that the majority judgments in Atiabari and Automobile held that State tax legislation must conform to Art. 304(b) in addition to Art. 304(a). The thrust of the submissions made is that entry tax falls within the expression 'restriction' under Art. 304(b). They submit that the State legislation levying tax on the goods imported into the State may have to be justified under Art. 304(b), if they are challenged as excessive in amount, to such an extent that they operate as a restriction on the movement of goods or persons and impose a burden on the freedom of trade and commerce.

70. Mr. P.P. Rao, Mr. Rakesh Dwivedi, Mr. V. Giri, Mr. Shyam Divan and Mr. Ajit Kumar Sinha learned Senior Counsel and other counsel appearing for the States advanced meticulous arguments that there is erroneous approach in the judgments of Atiabari and Automobile and they made the following submissions to fortify their contentions that the majority views in Atiabari and Automobile are to be re-visited:-

> "(i) Even though the majority referred to Section 297 of the Government of India Act, 1935 and referred to the economic unity of the nation, no detailed discussion was done on the history of Part XIII and Constituent Assembly Debates which threw considerable light on Part XIII and consequently erred in holding that Art. 301 read in its proper context imposes constitutional limitations on the legislative powers of the Parliament and the State. [Page 848] Majority in Atiabari held that :-
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> "..the freedom of the movement of trade cannot be subject to any restrictions in the form of taxes imposed on the carriage of goods or their movement, all that is meant is that the said restrictions can be imposed by the State Legislatures only after satisfying the requirement of Art. 304(b).." [Page 861]. If the said view of Atiabari is to be adopted then for each and every legislation, the State Legislatures will have to undergo the process of Art. 304(b). Tax is one important mode of raising revenue to enable the States to discharge its obligations as a Welfare State. Such plenary powers of the State legislature to impose taxes cannot be whittled down or made subservient to Art. 301.

(11) The majority read Art. 301 as subject only to the provisions of

Part XIII. [Page 848]

(iii) Majority drew support from the Constitutions of Australia and USA however one does not find any provision comparable to Part XIII in Australian and American Constitution. Even Australia and USA now reject the "direct and immediate test"
and have adopted "discrimination theory".

71. Learned Attorney General for India, Mr. Mukul Rohatgi has additionally submitted that bringing taxes within the purview of Art. 304(b) is completely foreign to the constitutional scheme of federalism as it would empower the President to, by virtue of proviso to Art. 304(b), super-adjudicate over the sovereign power of the State and that the sovereign power of the State cannot be subjected to an implied limitation as it would destroy sovereignty, federalism and economic unity of the country.

72. Art. 301 guarantees freedom of trade and commerce from "restrictions" and not freedom from all "laws". With due respect, in Atiabari, by application of "direct and immediate test', rather than examining the powers of the State Legislature to enact legislation with reference to the entries in List II, the majority has gone into the effects of the legislation. As per majority view of Atiabari, Art. 301 is a limitation upon the exercise of legislative powers of the State, which, in my view negates or limits the legislative power of the States expressly granted under various entries in List II of the Seventh Schedule. As rightly contended by the counsel for the States, in Atiabari and Automobile, there was no detailed reference to Constituent Assembly Debates which throw considerable light on the scope of Part XIII.

73. The view taken in Atiabari and Automobile that taxes may and do amount to restriction, is flawed. Taxing power of the State stands independently fortified by Part XII of the Constitution and can be challenged only on the ground of reasonableness. Through a series of judicial pronouncements, it is accepted that even a challenge to the taxing Statute under Articles 19(1)(g), 14 and under Part III of the Constitution has to be dealt with caution and only after great circumspection should the Statute be struck down. Freedom in Art. 301 is not freedom from taxation—non-discriminatory taxes are outside the purview of Art. 301:

74. In Atiabari, Sinha, C.J. took a different view of Art. 301 than the one taken by the majority and concluded as under:-

" (2) the freedom declared by Art. 301 does not mean freedom from taxation simpliciter, but does mean freedom from taxation which has the effect of directly impeding the free flow of trade, commerce and intercourse; " [Page 831]
"In my opinion, another very cogent reason for holding that taxation simpliciter is not within the terms of Article 301 of the Constitution is that the very connotation of taxation is the power of the State to raise money for public purposes by

compelling the payment by persons, both natural and juristic, of monies earned or possessed by them, by virtue of the facilities and protection afforded by the State. Such burdens or imposts, either direct or indirect, are in the ultimate analysis meant as a contribution by the citizens or persons residing in the State or dealing with the citizens of the State, for the support of the Government, with particular reference to their respective abilities to make such contributions. Thus public purpose is implicit in every taxation, as such. Therefore, when Part XIII of the Constitution speaks of imposition of reasonable restrictions in public interest, it could not have intended to include taxation within the generic term "reasonable restrictions..." [Page 828] According to Sinha C.J., every tax including a tax on 'movement of goods or passengers' was not necessarily an impediment or restraint in the matter of
trade, commerce and intercourse. As per Sinha C.J., taxation by its very nature could not be included within the term "reasonable restriction" used in Part XIII. The view of Sinha C.J. is a correct view and is in consonance with the consistent view taken by this Court that taxing statutes are not per se a 'restriction'. Atiabari and Automobile: Reference to Australian and American cases:

75. The Commonwealth of Australia Constitution Act came into being in 1900. Chapter I, Part V lays down the powers of the Parliament wherein, by virtue of Section 51 (i), Parliament is empowered to legislate with respect to 'trade and commerce with other countries, and among the States'. Chapter IV, Sections 81-105A deal with 'Finance and Trade'. The most relevant provision in this Chapter, for our purpose is Section 92 which has been consistently mooted upon and has evolved through several judicial pronouncements. Section 92 declares trade, commerce and intercourse to be absolutely free, subject only to imposition of custom duties. Further, Section 99 mandates that the Commonwealth shall not give preference to one State or any part thereof over another State or any part thereof while making any law or regulation with respect to trade, commerce or revenue. Under Section 102, the Parliament is authorised to make a law forbidding the States from making any preference or discrimination insofar as Railways are concerned, but with due regard to financial responsibilities incurred by States in connection with construction and maintenance of Railways.

76. The Constitution framers while ascertaining the scope of freedom of inter-State trade and commerce in India deliberated upon Section 92 of the Australian Constitution. Pandit Thakur Das Bhargav was in favour of making trade and commerce absolutely free in India. However, Shri T.T. Krishnamachari speaking for the Draft Committee brought out the difficulties which could have been faced by guaranteeing absolute freedom of trade and commerce in India on par with Section 92 of the Australian Constitution.

77. The following observations of Shri T.T. Krishnamachari are relevant to be noted:

"....I do not know if he realises that an ombnibus right such as the one that we recognise should not be given so far as freedom of trade and commerce is concerned, which perhaps has an echo in article 92 of the Australian

> Constitution, which has made the economic position of Australia a very difficult one today. They in Australia find that by reason of the fact that their provisions for amendment of the Constitution are so difficult that they are not able to amend the Constitution, and article 92 stands as a bar to any progressive legislation which they have undertaken. It may be right or it may be wrong - the people of Australia are behind the Government but when they wanted to nationalise banking, article 92 of the Australian Constitution has been held as a bar to the Government's power to nationalise the banks. There is no point in shutting the hands of the future Government in operating this Constitution.'' [Constitutional Assembly Debates, Volume IX, Page.1142, dated 30.07.1949-18.09.1949]

78. Shri T.T. Krishnamachari highlighted how Section 92 stood in between the nationalisation of private banks in Australia. This observation was probably made taking note of the view taken by Australian High Court, which was later affirmed by Privy Council in *Commonwealth of Australia v. Bank of New South Wales*[35] (famously known as Bank Nationalisation Case). In 1947, the Australian Government decided to nationalise private banks in Australia. In line of this process, the Banking Act, 1947, was enacted. However, the policy faced several controversies and was ultimately challenged before the courts. The Bank of New South Wales challenged the constitutional validity of Banking Act, 1947. The High Court of Australia found certain provisions of the Act to be invalid and thus, struck them down. The Commonwealth Government appealed against the decision in the Privy Council, however, the Privy Council affirmed the decision of the Australian High Court.

79. Our Constitution framers noticed the problems which had emerged in relation to the trade and commerce provisions of the Australian Constitution. After deliberations, the phrase "absolutely free" occurring in Section 92 of the Australian Constitution was not borrowed and incorporated in the Indian Constitution. While the framers of Indian Constitution took great caution to avoid the state of ambiguity faced in Australia with regard to freedom of trade and commerce, due to the judicial development in Atiabari and Automobile, confusions were sown in Indian scenario also.

80. Atiabari and Automobile adopted the 'Direct and Immediate test which had evolved in Australia through a series of pronouncements [*James v. State of South Australia*[36]*; James v. Cowan*[37]*; James v. Commonwealth of Australia*[38] and was dominantly relied upon in the Bank Nationalisation Case. In the Bank Nationalisation Case, it was held that Section 92 would be breached only where the law under challenge restricted trade and commerce directly and immediately. The Court observed that where the restriction is indirect or remote, the freedom
provided by Section 92 would not be impaired. The test on which every impugned legislation ought to be examined was formulated in the following terms: Does the law under challenge directly and immediately, as opposed to incidentally, restrict the trade and commerce in which the individual wa engaged? Atiabari and Automobile fundamentally concurred with the Australian cases to hold 'tax' as a restriction for the purposes of Part XIII of the Constitution of India. Gajendragadkar, J. in Atiabari observed:

> "It is commonplace to say that the political and historical background of the federal polity adopted by the Australian Commonwealth, the setting of the Constitution itself, the distribution of powers and the general scheme of the Constitution are different, and so it would to be safe to seek for guidance or assistance from the Australian decisions when we are called upon to construe the provisions of our Constitution.".

Gajendragadkar, J. further relied on the Bank Nationalisation Case to borrow the concept of 'direct and immediate impediment on the freedom of trade and commerce' from the Australian system. Relevant extract from Gajendragadkar J.'s judgment is as under:

> "In the case of Commonwealth of Australia v. Bank of New South Wales (1927) 40 C.L.R. 1 to which reference has already been made in connection with the test of pith and substance the Privy Council was examining the validity of s. 46 of Banking Act (Commonwealth) (No. 57 of 1947) in the light of the provisions of s. 92 of the Australian Constitution. In deciding the said question one of the tests which was applied by Lord Porter was : "Does the act not remotely or incidentally (as to which they will say something later) but directly restrict the inter-State business of Banking", and he concluded that "two general propositions may be accepted, (1) that regulation of trade, commerce and intercourse among the States is compatible with its absolute freedom, and (2) that s. 92 is violated only when a legislative or executive act operates to restrict such trade, commerce and intercourse directly and immediately as distinct from creating some indirect or consequential impediment which may fairly be regarded as remote""[Page 870 of SCR]

81. Again in Automobile, reliance was placed on Australian and American cases, in particular on Commonwealth of Australia v. Bank of New South Wales and James v. Commonwealth of Australia to finally hold that 'tax' is a restriction for the purpose of Part XIII of the Constitution. Subba Rao J. concurring with the majority view pointed out that Art. 301 was borrowed from Section 92 of the Australian Constitution, and after referring to the differences in the language of both the provisions and evolution of federation in both the
countries, Subba Rao J. chose to concur with "doctrine of direct and immediate effect". Following observations of Subba Rao J. clearly show that heavy reliance was placed by him on American and Australian decisions:-

> "In this context, the principles evolved by American and Australian decision in their attempt to reconcile the commerce power and the State police power or the freedom of commerce and the Commonwealth power to make laws affecting that freedom can usefully be invoked with suitable modifications and adjustments. Of all the doctrines evolved, in my view, the doctrine of "direct and immediate effect" on the freedom would be a reasonable solvent to the difficult situation that might arise under our Constitution. If a law, whatever may have been its source, directly and immediately affects the free movement of trade, it would be restriction on the said freedom. But a law which may have only indirect and remote repercussion

on the said freedom cannot be considered to be a restriction on it. ”

82. The above views taken in Atiabari and Automobile in the light of the Australian cases represent a mechanical implantation of a foreign concept into the Indian legal system, not keeping in view the distinct features of Indian Polity and the Constituent Assembly Debates. Majority view in Atiabari and Automobile do not appear to have taken note of the historical background of merger of ‘Native States’ with their individualities, with British India, and the federal nature of the Indian Constitution while discussing the fundamental question as to whether ‘Freedom’ in Art. 301 meant freedom from tax. The majority appears to have begun with the presumption of tax laws being subservient to Art. 301 and later concluded that if all the tax laws are brought in Art. 301, State’s legislative power to tax would be destroyed. Thereafter, in an attempt to save the taxing power of the State, they borrowed the concepts of ‘direct and immediate test’ and ‘compensatory tax’ from the Australian and American Cases.

83. In this regard, learned author H.M. Seervai in Constitutional Law of India, 4th Edition, Volume 3 has observed as under:

> “It is submitted that the principles of interpretation adopted by the majority judgment in the Atiabari case and by all the judgments in the Automobile case depart widely from well settled principles of construction. They first try to ascertain the intention of the framers of the Constitution, by reference to ‘history’ and then proceed to consider what construction would best effectuate that intention. But if an intention is to be first assumed, it is not difficult to read it into the words to be interpreted. It is submitted that words have to be interpreted according to their terms, or according to well known extrinsic aids to construction” [Page 2598] Mr. Seervai has also pointed out that the very observation that the Australian scenario is akin to the Indian scenario was flawed. It is obscure how the comparative study of the Australian and Indian Constitutions undertaken by this Court in Atiabari and Automobile lead to a conclusion that interpretation of Section 92 as done in Bank Nationalisation Case can be suitably adopted in Indian set-up. Mr. Seervai at Page 2599 observed as under:¬. provisions of part XIII of our Constitution are radically different. The judges who cite the Australian decisions repeat the warning that it is not safe to interpret the provisions of the Constitution by reference to decisions on other Constitutions, nevertheless those decisions are not only referred to but are found to support the interpretation that a tax may amount to a restriction under Article 301. But it is submitted that the decision in James v. Commonwealth of Australia, that a tax may amount to a ‘restriction’ cannot support the conclusion that a tax is included in Article 301...” [Page 2599]

84. Interestingly, the Australian cases relied upon in Atiabari and Automobile failed to withstand the test of time. As of today, by virtue of a seven Judges Bench, judgment of the High Court of Australia, the decisions in *James v. Common Wealth and Bank Nationalisation Case_stand overruled. In Cole v. Whitfield*[39] the High Court of Australia considered Section 92 and other ancillary provisions relating to freedom of trade and commerce and found the test of “direct and immediate effect” to be insignificant; the

Court held as under:-

> "48. Departing now from the doctrine which has failed to retain general acceptance, we adopt the interpretation which, as we have shown, is favoured by history and context. In doing so, we must say something about the resolution of cases in which no impermissible purpose appears on the face of the impugned law, but its effect is discriminatory in that it discriminates against inter-State trade and commerce and thereby protects intra-State trade and commerce of the same kind..."

85. In Cole v. Whitfield, the High Court while disapproving of the "individual rights" approach authoritatively adopted in Bank Nationalisation Case held that Section 92 guarantees freedom of inter-State trade and commerce only against the discriminatory protectionist burdens. This decision brought to an end the "quite unacceptable state of affairs" then attending Section 92 of the Constitution, as the preceding eighty years of judicial development concerning freedom of inter-State trade, commerce and intercourse in Australia "had yielded neither clarity of meaning nor certainty of operation". Cole v. Whitfield laid down that for a burden to be 'protectionist' it must 'discriminate' against inter-State trade or commerce in a 'protectionist sense'. The Court observed as under:

> "A law which has as its real object the prescription of a standard for a product or a service or a norm of commercial conduct will not ordinarily be grounded in protectionism and will not be prohibited by s 92. But if a law, which may be otherwise justified by reference to an object which is not protectionist, discriminates against interstate trade or commerce in pursuit of that object in a way or to an extent which warrants characterization of the law as protectionist, a court will be justified in concluding that it nonetheless offends s 92." [Page 66]

86. This requirement was based on an appraisal of the history of Section 92, which showed that its purpose was the achievement of inter-colonial free trade. As was observed in *Betfair Pty Ltd v Western Australia*[40]

> "S. 92 was not designed to create "a laissez-faire economy in Australia"; rather, it had a more limited operation, to prevent the use of State boundaries as trade borders or barriers for the protection of intrastate players in a market from competition from interstate players in that market." [Page 45] [Emphasis added]

While the reasoning in Cole v. Whitfield has been explained and developed in subsequent cases, fundamentally the judgment has withstood the test of time.

87. From the above it clearly emerges that the ramshackle cottage on which the decision in Atiabari and Automobile was based has itself fallen down. Even the idea of "freedom" in respect of trade and commerce in Australia has considerably changed to suit the dynamics of the present day trade and commerce. the Congress "To regulate commerce with foreign nations, and among several states, and with the Indian Tribes". The power of the Congress is not restricted to regulation of trade between the States

only, rather it can regulate international trade as well. So far as inter-State trade is concerned, Congress under the Commerce Clause is empowered to regulate broad areas of activities such as use of the channels of inter-State commerce, the protection of the instrumentalities of inter-State commerce, or persons or things in inter-State commerce, and activities that substantially affect inter-State commerce; whereas in the Indian Constitution, States have plenary power to legislate on the subjects enumerated in List II subject to the Constitutional limitations. Atiabari and Automobile erred in relying on *Freeman v. Hewit*[41] which has been discarded by the US Supreme Court itself in *Complete Auto Transit, Inc. v. Charles R. Brady*[42] In Complete Auto Transit, the US Supreme Court while dealing with an inter-State levy purported to be compensatory, formulated a four-part test to determine if a State tax violates the Commerce Clause: (i) Nexus: there must be a sufficient connection between the taxpayer and the State to warrant the imposition of State Tax Authority; (ii) Fair Apportionment: the State must not tax more than its fair share of the income of a taxpayer; (iii) No discrimination: the State must not treat out-of-State taxpayers differently than in-State taxpayers; and (iv) Related to services: the tax must be fairly related to services provided to the taxpayer by the State.

89. In view of the above, the position which stands good today is that the judgments of US Supreme Court, Privy Council and Australian High Court relied upon in Atiabari and Automobile have been overruled in Complete Auto Transit in USA and Cole v. Whitfield in Australia. The principle of 'direct and immediate effect on the trade and commerce' has been rejected and it has been held that the norms of commercial conduct shall not be 'protectionist' or 'discriminatory'. The principles of direct and immediate test' laid down in Atiabari and Compensatory Taxes' enunciated in Automobile are to be overruled and minority judgment of Sinha, C.J. that 'tax simpliciter is not violative of Art. 301 is to be affirmed. Art.304 (a) and (b) must be read disjunctively:

90. As the word "restrictions" in the marginal note of Art. 304 suggests plurality of powers and indicates that Clauses (a) and (b) of Art. 304 confer distinct powers. Art. 304(a) deals with tax; Art. 304(b) deals with restrictions that are reasonable and in public interest. Constitution framers could not have intended to include tax in Art. 304(b); since the elements of "reasonableness" and "public interest' are inherent in a tax. The use of the word "and" does not assist the interpretation that the provisions are conjunctive. It only means that:-

> (i) the State can impose taxes on goods coming from outside so as not to discriminate between the goods imported and goods manufactured or produced within the State [Art. 304 (a)] -and-
>
> (ii) It can also in addition impose other restrictions that are reasonable and in public interest [Art. 304 (b)] subject to the assent of the President. [Emphasis added] That Articles 304(a) and (b) are disjunctive, is also clear from the fact that the proviso to Art. 304(b) i.e. the presidential sanction is referable to Art. 304(b) only and not to a law imposing tax on goods imported from other States contemplated under Art. 304(a). This is because, Art. 304(a) has an inbuilt safeguard, inasmuch the taxes imposed on the goods coming from another State

cannot be discriminatory and, therefore, no presidential sanction is required.

91 . It is relevant to note that the word "and" is used after semi colon in Art. 304(a). While it is correct to say that the word "and" normally is conjunctive, it is also often construed as disjunctive on the basis of the legislative intent as gathered from the words of the proviso under context in which it was used. Considering whether the word "and" is conjunctive or disjunctive, in relation to Section 4(i) of Maharishi Mahesh Yogi Vedic Vishwavidyalaya Adhiniyam, 1995, in *Maharishi Mahesh Yogi Vedic Vishwavidyalaya v. State of Madhya Pradesh and Others*[43] and observing that the word "and" is used as disjunctive, this Court held as under:-

93 we also refer to the following decisions rendered by this Court in *Ishwar Singh Bindra v.State of U.P*[44]*,* wherein in para 11 it has been held as under: (AIR p. 1454)

> "11. ... It would be much more appropriate in the context to read it disconjunctively. In Stroud's Judicial Dictionary, 3rd Edn., it is stated at p. 135 that 'and' has generally a cumulative sense, requiring the fulfilment of all the conditions that it joins together, and herein it is the antithesis of or. Sometimes, however, even in such a connection, it is, by force of a context, read as 'or'. Similarly in Maxwell on Interpretation of Statutes, 11th Edn., it has been accepted that 'to carry out the intention of the legislature it is occasionally found necessary to read the conjunctions "or" and "and" one for the other'."[Emphasis supplied]

94. We may also refer to para 4 of the decision rendered by this Court in *Director of Mines Safety v. Tandur and Nayandgi Stone Quarries (P) Ltd*[45]*.* (SCC p. 211, para 4)

> "4. According to the plain meaning, the exclusionary clause in sub-section (1) of Section 3 of the Act read with the two provisos beneath clauses (a) and (b), the word 'and' at the end of para (b) of sub-clause (ii) of the proviso to clause (a) of Section 3(1) must in the context in which it appears, be construed as 'or'; and if so construed, the existence of any one of the three conditions stipulated in paras (a), (b) and (c) would at once attract the proviso to clauses (a) and
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> (b) of sub-section (1) of Section 3 and thereby make the mine subject to the provisions of the Act. The High Court overlooked the fact that the use of the negative language in each of the three clauses implied that the word 'and' used at the end of clause (b) had to be read disjunctively. That construction of ours is in keeping with the legislative intent manifested by the scheme of the Act which is primarily meant for ensuring the safety of workmen employed in the mines." [Emphasis supplied]"

95 we are not inclined to hold that the expression "and" used in the Preamble, as well as in Section 4 should be read conjunctively as contended by the learned counsel for the State. On the other hand, in the context in which the said expression is used, it will have to be read as "or" creating a disjunctive reading of the provision."

92. In *A.K. Gopalan v. State of Madras*[46] in the context of Art 22(7)(a) of the Constitution of India, Constitution Bench observed that since it is an enabling provision the

word ‘and’ should be read disjunctively and held as under:-

> “248 In fact clause (4) (b) contemplates the detention itself to be in accordance with the provisions of any law made by Parliament under sub-clause (a) and (b) of clause (7). Therefore, the detention can well be under the very law which the Parliament makes under sub-clause (a) and (b) of clause (7). As to the second point the argument is that Parliament has a discretion under clause (7) to make a law and it is not obliged to make any law but when our Parliament chooses to make a law it must prescribe both the circumstances under which, and the class or classes of cases in which, a person may be detained for a period longer than three months. I am unable to construe clause (7) (a) in the way suggested by learned counsel for the petitioner. It is an enabling provision empowering Parliament to prescribe two things. Parliament may prescribe either or both. If a father tells his delicate child that he may play table tennis and badminton but not the strenuous game of football, it obviously does not mean that the child, if he chooses to play at all, must play both table tennis and badminton. It is an option given to the child. Likewise, the Constitution gives to Parliament the power of prescribing two things. Parliament is not obliged to prescribe at all but if, it chooses to prescribe it may prescribe either or both
>
> ” [Emphasis added]
>
> Applying the ratio in the above decisions since the expression ‘and’ is used in Art. 304 after semi-colon, it will have to be read as ‘or’ creating a disjunctive reading of Art. 304(a) and Art. 304(b) indicating that the State Legislature can exercise its power either under Art.304 (a) or Art. 304 (b) or both. Whether Art. 304(b) coupled with the proviso is applicable to tax laws-Judicial Approach:

93. In Atiabari, majority held that “tax laws” fall within the comprehension of Art. 301 and, therefore, any legislation whether taxing or otherwise which imposes any direct restriction on the movement or transport of goods attracts the provisions of Art. 301, and its validity can be sustained only if it satisfies the requirements of Art. 302 or Art. 304. According to the above view in Atiabari, it is not possible for the State Legislature to pass any law at all with respect to some of the tax entries viz. sales tax (entry 54, List II); law relating to gambling (entry 34, List II) or tax on betting and gambling (entry 62, List II); and tax on the carriage of goods or passengers by road or inland waterways (entry 56, List II). If the legislations under the above entries are challenged on the ground that they operate as a direct restriction on the freedom of trade, commerce and intercourse, as per the view in Atiabari, these legislations may have to be justified under Art. 304(b). Atiabari approach would totally take away the sovereign powers of the State Legislature to enact laws in exercise of its powers under various taxing entries of List II, which could not have been the intention of the framers of the Constitution.

ART. 304(b) IS APPLICABLE ONLY TO NON-FISCAL LAWS AND NOT TO TAX LAWS-

94. Art. 304(a) and Art. 304(b) are two distinct powers and freedom of trade, commerce

and intercourse is subject to them. Art. 304(b) relates to reasonable restrictions imposed in public interest. Art. 304(b) deals with non-fiscal legislation imposing reasonable restrictions in public interest and tax laws are not included under Art. 304(b). In this regard, reliance has been placed on Interim Report of the Advisory Committee on the Subject of Fundamental Rights' dated 23.04.1947, as published in "The Framing of India's Constitution Select Documents-The Project Committee" by Universal Law Publishing Co. Pvt. Ltd. Learned Senior Counsel Mr. Rakesh Dwivedi has taken us through the chain of events leading to Art. 304(b) and the proviso's present form in Art. 304(b). Draft Article 10 of the " Justiciable Fundamental Rights"(page No.297 of the said book) presently Part XIII as originally proposed read as under:-

> "10. Subject to regulation by the law of the Union, trade, commerce, and intercourse among the units by and between the citizens shall be free: Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in an emergency: Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject: Provided further that no preference shall be given by any regulation of commerce or revenue by a unit to one unit over another."
>
> [Emphasis added]

95. The first proviso to Draft Art. 10 corresponds to Art. 304(b) and second proviso relates to Art. 304(a). That first proviso to Draft Art.10 [Art. 304(b)] relates only to "public order, morality or health or in an emergency" is also made clear from the Constituent Assembly Debates/Advisory Committee Proceedings. In this regard, we may refer to the speech of Shri Alladi Krishnaswami Ayyar in the Constituent Assembly Debates, which is as under:-

> "Alladi Krishnaswami Ayyar: "Subject to regulation by the law of the Union, trade, commerce, and intercourse among the units by and between the citizens shall be free." That is the general principle. Then come the exceptions, "Provided that any unit may by law impose reasonable restrictions in the interest of public order, morality or health or in an emergency." Suppose there is a general famine, and people are starved, that is what is meant here to be dealt with. And then "Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units the same duties and taxes to which the goods produced in the unit are subject." That is to say, we ought not to differentiate; but at the same time, goods coming in should not go scot-free; they should be subject to the same duty as goods produced in the area." [Emphasis Added] (Page. 253 of the said book of Select Documents-Project Committee)"

96. In October 1947, the Draft presented by the Drafting Committee shifted the then Art. 10 outside the Part on Fundamental Rights (Right of Freedom) to Articles 243 and 244 and the power under Art. 244(b) was kept within the States. Art. 244(b) as adopted reads as under:-

> "244. Notwithstanding anything contained in article 16 or in the last preceding

article of this Constitution, it shall be lawful for any State-

(a) to impose on goods imported from other States any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and

(b) to impose by law such reasonable restrictions on the freedom of trade, commerce or intercourse with that State as may be required in the public interest. "

97. In this regard "Note to Art. 244 (b)" as referred to in Page 328 of the said book Framing of India's Constitution Select Documents-Project Committee reads as under:-

"Note: Clause (b) of article 244 is based on the recommendation of the Advisory Committee as adopted by the Constituent Assembly. The Drafting Committee has considered it necessary to substitute for the words "in the interest of public order, morality or health" which occur in the said recommendation, the words "in the public interests".

The above note clearly shows that after Debate, based on the recommendations of Advisory Committee the phrase "public order, morality or health or in an emergency" was substituted with the word "public interest". This clearly shows that the framers of the Constitution never intended to bring tax laws within the fold of Art. 304(b).

98. After Debate, first proviso to Draft Art. 10 was adopted as Art. 274(D)(b) [present Art. 304(b)]. As seen from page 330 of the first Draft Constitution, the Committee was of the opinion that the first and second proviso should be transferred as independent clauses in the Chapter dealing with relation between the different States and the third proviso was found unnecessary in view of the opening words "subject to the regulation by the law of the Union and, accordingly, the same was adopted in Art. 274(D)(b) [Present Art. 304(b)] which reads as under:-

"(b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest. Provided that no Bill or amendment for the purposes of clause

(b) of this article shall be introduced or moved in the legislature of a State nor shall any Ordinance be promulgated for the purpose by the Governor or Ruler of the State without the previous sanction of the President."

99. If Art. 304(b) is also held to cover tax laws, it would amount to empowering the States to make laws imposing tax even on the freedom of trade, commerce and intercourse. As such there is no such entry in List II of Seventh Schedule of the Constitution so empowering the States. Commenting on this, learned author H.M.

Seervai in his Constitutional Law of India 4th Edition, Volume 3 observed as under:-

> "24.43. There are other reasons supporting the conclusion that a tax simpliciter is not a restriction on the freedom of trade. Article 304 itself makes a distinction between taxes and restrictions and the correct conclusion to draw from this fact is that restrictions in Art.304 (b) do not include a tax. Secondly, by virtue of the non obstante clause, Art.304 (b) enables even discriminatory restrictions to be imposed which are forbidden by Art. 303 (1). We have seen that Art. 303(1) cannot possibly refer to taxes. Thirdly, the whole scheme of taxation in our Constitution would be completely dislocated if Art.304 (b) included a tax. The taxing powers of the Union and the States have been made mutually exclusive so that Parliament cannot deprive the States of their taxing powers as has happened in countries where the powers of taxation are concurrent. It would be surprising if the Union legislature, i.e. Parliament could not take away the taxing powers of the State legislatures and yet it would be open to the Union executive under Art.304 (b) to deprive the State legislatures of their taxing powers. Again, if restrictions include a tax, two questions would arise. As a matter of language, Art.302 would then run: "Parliament may, by law, impose such restrictions, including a tax, on the freedom of trade and commerce or intercourse..." The Article would then become a source of power because there is no legislative entry relating to a tax "on the freedom of trade" unless the residuary entry is resorted to, Art. 304 (b) would raise the same question, and there would be no residuary entry to resort to, and it would raise the further question whether the reasonableness of taxes is made justiciable under our Constitution. "

Levy of taxes is the economic lifeline of the State. Framers of the Constitution never intended to include tax within the fold of Art. 304(b). To give the Centre a veto over the plenary power of the State to levy the tax would completely distort the Centre-State balance and cooperative federalism. Such an interpretation has no basis in the Constitutional Assembly Debates and is liable to be rejected.

100. The rationale for the sanction of President contemplated by proviso to Art. 304(b) is apparent from the fact that trade and commerce with foreign countries and inter-State trade and commerce are subject matters in List I of the Seventh Schedule (entries 41 and 42, List I). Further, trade and commerce in production, supply and distribution of industry controlled by the Union, food stuffs, including edible oils, seeds and oils; cattle fodder; raw cotton, cotton seed; and raw jute are subject matters in entry 33, List III. Entry 34, List III deals with price control. Only intra-State trade and commerce is in List II (entry 26, List II) subject to entry 33, List III, as stated therein. Parliament has thus occupied an overwhelming space with respect to trade and commerce within the State also. It is in this backdrop that the State has been given power to impose reasonable restrictions on the freedom of trade, commerce and intercourse with or within that State with the proviso requiring presidential assent before the Bill is introduced. The rationale, therefore, is that a non-fiscal law of the State with respect to freedom of trade, commerce and intercourse would be entrenching upon either the exclusive legislative field of the Parliament in List I or the occupied field of the Parliament in List III. It follows that Art. 304(b) relates to non-fiscal laws of the States. In the above context, the assent

of the President envisaged in proviso to Art.304(b) would be somewhat akin to the assent contemplated in Art. 254. Such assents are not judicially reviewable. [vide *Kaiser-i-Hind (P) Ltd. and Anr. v. National Textile Corpn. (Maharashtra North) Ltd. and Others*[47], (Paras 23 to 27)]

101. If the framers of the Constitution intended that State legislation required sanction of the President for tax laws pertaining to inter-State trade, commerce and intercourse, the Constitution would have made an express provision in the Constitution. Art.274 says that no Bill or Amendment which imposes or varies any tax or duty in which States are interested; or which alters meaning of "agricultural income" under Income Tax Act or principles of distribution; or, imposes surcharge for Union purpose shall be introduced or moved in either House of Parliament except on the recommendation of the President". This indicates the significance of revenue for States and also the limits on Union. If framers intended to have an identical framework in Art. 304 for State Tax Laws they would have expressly said so. Art. 288 also provides for the role of President in the context of imposition of tax by States in respect of water and electricity. Under Art. 288(1), the tax imposed by existing State laws would continue only subject to order passed by the President. Under Art. 288(2) the legislature of a State could impose a tax in respect of water or electricity stored, generated, consumed, distributed or sold by an authority established under any existing law or any law made by Parliament for regulating or developing any inter-State river or river valley unless the law has been reserved for the consideration of the President and has received his assent. This again shows that Presidential assent with respect to tax has to be specifically provided for.

102. In the light of the above discussion, the majority view in Atiabari, at Page 861 that the freedom of movement of trade cannot be subject to any restriction in the form of taxes and that such a legislation can be passed only after specifying the requirements of Art. 304(b), is not a correct view. I find merit in the submission made by Mr. Rakesh Dwivedi, Senior Advocate, that the Parliament has occupied an overwhelming space with respect to trade and commerce both within and outside the State and it is in this backdrop, that the State has been given power to impose such reasonable restrictions in "public interest" on the trade, commerce and intercourse with or within that State subject to the satisfaction of the proviso under Art. 304(b). It follows, therefore, that Art. 304(b) relates to non-fiscal laws of the States. To subject the State's sovereign legislative levying tax to Presidential assent would in effect erode the pillar of federalism which this country is built on. In the absence of an express provision in the Constitution, such presidential sanction for taxing laws cannot be read into the provision.

Conclusion on Question No.1:

103. Non-discriminatory taxes do not constitute infraction of Art. 301 of the Constitution. With due respect, the view taken in Atiabari and approved in Automobile Transport declaring that taxes do amount to restriction and that freedom of trade, commerce and intercourse cannot be subject to restriction in the form of taxes is not a correct view and are to be over-ruled. However, I am agreeing with the concept of compensatory tax evolved in the Automobile case for the reasons indicated while answering question Nos. 2 and 3.

QUESTION NO. 4: IS THE ENTRY TAX LEVIED BY THE STATES IN THE PRESENT BATCH OF CASES VIOLATIVE OF ART. 301 OF THE CONSTITUTION AND IN PARTICULAR HAVE THE IMPUGNED STATE ENACTMENTS RELATING TO ENTRY TAX TO BE TESTED WITH REFERENCE TO BOTH ARTICLES 304(a) AND 304(b) OF THE CONSTITUTION FOR DETERMINING THEIR VALIDITY?

104. The core question which needs to be addressed is whether the tax levied under entry 52, List II would impinge upon Article 301. Entry 52, List II reads as: "Tax on the entry of goods into a local area or consumption or sale therein". A bare reading of the entry would show that entry tax can be levied only on the satisfaction of the conditions in entry 52 of List II namely: (i) the tax to be levied on the entry of goods into local area; (ii) entry of goods into the local area is for consumption, use or sale therein.

105. There are two other entries in the Constitution which also authorize the levy of taxes which fall essentially on the movement of tradables within the country, viz., entry 56 of the State List and entry 89 of the Union List. Entry 56 of the State List empowers the State to levy "taxes on goods and passengers carried by road or inland waterways"; while entry 89 of the Union List contemplates the levy of "terminal taxes on goods or passengers carried by railway, sea or air, taxes on railway fares and freights". While there are variations in the operational form of taxes under entry 52, essentially these constitute a levy on entry of goods into a local area for sale, consumption or use therein. Under an entry tax regime, a company, trading firm or an individual would be liable to pay entry tax on goods brought into a local area for consumption, use or sale therein. The core question which needs to be addressed in respect of entry 52, List II of Seventh Schedule is whether the tax levied under the said entry would impinge upon Art. 301.

History and Purpose of Entry Tax:

106. The term "Entry Tax" traces its history back to a particular tax called "Octroi". The word "Octroi" comes from the French word 'octroyer' which means 'to grant' and in its original use meant 'an import' or 'a toll' or 'a town duty' on goods brought into a town. At first, octroi were collected at ports but being highly productive, towns began to collect them by creating octroi limits. They came to be known as "town duties". The term "octroi" appeared in the Scheduled Tax Rules framed under the Government of India Act, 1919. The expression signified a tax levied on entry into an area of a unit of local administration. The entry was re-fashioned and enacted as item 49 of the Provincial Legislative List under the Government of India Act, 1935. Item 49 reads as "Cesses on the entry of goods into a local area for consumption, use or sale therein". In *Burmah Shell Oil Storage and Disturbing Co. of India Ltd. Belgaum v. Belgaum Borough Municipality Belgaum Cell*[49], the Supreme Court of India while distinguishing terminal tax and Octroi held that the Octroi's leviable in respect of goods brought into a municipal area for consumption or use of sale.

107. When Government of India Act, 1935 was enacted, terminal taxes were separated from octroi and were included in the Union List while octroi was allocated to the provinces. The term "octroi" was avoided because terminal taxes are also 'octroi' in a sense. This scheme has been adopted in the Constitution with the difference that in the

entry relating to 'octroi' the word 'tax' replaces the word 'cess'. Levy of octroi was also criticized for being an obsolete method of the collection, involving stoppage of vehicles at the check posts outside the city limits, thereby obstructing flow of vehicular traffic, and causing wastage of business hours, loss of fuel etc.

108. Entry tax like 'octroi' is a tax on entry of goods into a local area for consumption, use or sale therein. However, entry tax is different from octroi, inter alia, in the following respects:- Firstly, it is not collected at the checkpost; but is payable by furnishing returns of the purchases from outside the local area or the details of the goods entered into the local area. Entry tax is easier to administer as returns are filed on self- assessment and it avoids the harassment associated with octroi. Secondly, it is imposed as an ad valorem tax as against octroi, which is generally a combination of specific and ad valorem levies. Thirdly, entry tax is a State-level levy while octroi is a local levy; entry tax revenue is treated as State revenue and is spent on local bodies for their development and the State in general.

109. On behalf of the assessees, it was contended that proper meaning attached to the words "local area" in Entry 52 is an area administered by a local body like a municipality, a district Board, a local Board, a Union Board, a Panchayat or the like. In this regard, reliance has been placed upon *Diamond Sugar Mills Limited v. State of U.P*[50]. wherein this Court held as under:-

> "Whether the entire area of the State, as an area administered by the State Government, was also intended to be included in the phrase "local area", we need not consider in the present case.
>
> "... We are of the opinion that the proper meaning to be attached to the words "local area" in Entry 52 of the Constitution, (when the area is a part of the State imposing the law) is an area administered by a local body like a municipality, a district board, a local board, a union board, a Panchayat or the like. The premises of a factory is therefore not a "local area"."
>
> This Court in *M.O. Shamsudhin v. State of Kerala*[51] has also held that:
>
> "the expression local area has been used in various Articles of the Constitution namely 3(b) 12, 245(1), 246, 277, 321, 323-A and 371-D. They indicate that the constitutional intention was to understand the 'local area' in the sense of any area which is administered by a local body, may be corporation, municipal board, district board etc. The High Court on this aspect held and in our opinion rightly that the definition does not comprehend entire State as local area as the use of word 'a' before 'local area'in the section is significant."

110. As discussed above, entry tax is not collected at the behest of municipality or a panchayat attached to a checkpost. It is payable by the assesses by filing their returns. Entry tax is a State level levy, levied by State Legislature upon entry of goods into a local area for consumption, use or sale therein. The local authorities themselves cannot levy the tax. The power is that of State Legislature and of no one. In Bihar Chamber of

Commerce, this Court was faced with the task of interpreting the term "local area" in the context of entry 52, List II. The Court observed that where State Legislature has levied a tax covering the entire State and proceeds of such tax are spent for common welfare activities of the State, the distinction between the State and the local areas practically disappears. In Bihar Chamber of Commerce, it was held as under:-

> "12 Where the local areas contemplated by the Act cover the entire States the distinction between the State and the local areas practically disappears. (The situation would, no doubts be different if the local areas are confined to a few cities or towns in the State and the levy is upon the entry of goods into those local areas alone. This is an important distinction which should be kept in mind while appreciating the aspect and also while examining the decisions of this Court rendered in fifties and sixties). The facilities provided in the State are the facilities provided in the local areas as well. Interests of the State and the interests of the local authorities are, in essence, no different....
>
> 36. Entry 52 empowers the State Legislature to levy this tax. The local authorities cannot themselves levy this tax. The power is that of the State Legislature and of none else. So long as the tax is levied upon the entry of goods into a local area for the purpose of consumption, use or sale therein, the requirement of Entry 52 is satisfied. The character of the tax so levied is that of entry tax – by whatever name it is called From the point of view of the entry tax, one may say that the State is a compendium of local areas. Spending for the purposes of the State is thus spending for the purposes of local areas. Situation may perhaps be different where the local areas are confined to a few cities or towns in the State. But where the local areas span the entire State, it cannot be argued that money spent for welfare schemes for improvement of roads, rivers and other means of transport and communication is not spent on or for the purposes of local areas. The purposes and needs of local areas are no different from the purposes and needs of the State - not at any rate to any appreciable degree "

The Entry tax is a State level levy and the entry tax revenue is treated as the State Revenue. As held in Bihar Chamber of Commerce, "the State is a compendium of local areas.... the purposes and needs of local areas are no different from the purposes and needs of the State." As entry tax levy being a State-level entry, it is spent on the development of local bodies and the State in general. When the entry tax is levied by the Entry Tax Act enacted by the State Legislature, the term 'a local area' contemplated by Entry 52 may cover the 'whole State' or 'a local area' as notified in the legislation. I agree with the views taken in Bihar Chamber of Commerce that from the view of Entry Tax, the State is a compendium of local areas and where the local areas cover the entire State, the difference between the 'State' and 'a local area' practically disappears.

111. Counsel appearing for the States contend that the burden of entry tax, if any, on the trader cannot by itself constitute a restriction on the inter-State movement of goods. To constitute a restriction per se on the freedom of trade, commerce and intercourse, levy of tax, in conjunction with other factors should actually create a substantial advantage in favour of the persons who indigenously manufacture or produce goods as

compared to the similar goods which are imported from outside the State. The sovereign power available to the State Legislature to levy tax cannot be decimated by every inconvenience that may be caused to a trader. If the tax is of such a character, that the burden, if any, borne by the dealer, can be absorbed by him as a part of his trade and business, then the trader will have to bear the same. It does not then make the tax discriminatory or create a restriction on the flow of goods from one State to another.

112. Imposition of entry tax is not merely "on movement or transport of goods"; consideration of entry 52, List II of Seventh Schedule shows that taxable event in the case of entry tax is entry of goods into the local area where it is to be used, consumed or sold therein. If the goods merely enter into a local area and then move to another destination beyond that local area, no tax can be levied under entry 52. To attract a levy under entry 52, List II, the goods must come to rest in the local area where they are taxed in the sense that their further movement and transport stands terminated and the goods are supposed to be used, consumed or sold in that local area. Since the taxable event under entry 52 is not the mere entry of the goods into the local area, but the fact that the goods are also to be used, consumed or sold, the necessary sequiter is that the movement of goods is terminated in that local area. Power to levy entry tax lies within the competence of a State Legislature. Since entry tax is leviable at the termination of the movement of trade and the goods have entered the local area for the purpose of use, consumption or sale, the levy of entry tax does not restrict flow of trade, commerce or intercourse and is not violative of Arti. 301 of the Constitution.

113. Taking us through various States' legislations, Senior Counsel Mr. Harish Salve on behalf of the assessees contended that the entry tax levied by State legislations are discriminatory and broadly classified the Entry Tax Statutes on discrimination into four different categories as under:-

> "States Alleged discrimination Tamil Nadu/Andhra Pradesh/ Kerala/Jharkhand Entry tax lev-ied only on goods imported from other States; no levy of entry tax on the goods manufactured inside the State which is discriminatory. Assam/Bihar /Haryana/Kerala(Post)Jharkhand/West Bengal/Tamil Nadu/Mizoram /Arunachal Pradesh/ Andhra Pradesh Facially, the legislations state that all goods are taxed; but grant exemption to the locally produced goods Orissa/Madhya Pradesh Local manufacturers are given the set¬off of entry tax paid on raw materials and thus preferential treatment given to locally produced goods. Chhattisgarh Excessive de-legation to the executive to levy entry taxes up to 50% who in turn levy higher rate of entry tax on certain goods and lesser rate for similar goods which is discriminatory. Entry Tax levied only on goods imported from other States: No levy of Entry Tax on the goods manufactured inside the State-Whether discriminatory.

114. Contention of the assessees is that entry tax is levied only on goods entering the local area from other States and there is no levy of entry tax on the locally produced goods when they move from one local area to another; as goods imported from other States are being discriminated against, such levy is not saved under Art. 304(a). It is

their contention that entry tax only on goods coming from outside the State and not intra-State entry of goods from one local area to another local area or on movement of goods is a clear case of discrimination, offending Art. 304(a).

115. The assessees seek to narrow down the wide purport of the term 'any tax' used in Art. 304(a) by contending that equivalence should be brought about in the imposition of entry tax itself. By contending so, the appellants have become oblivious of the fact that the State Legislature is always free to provide for equivalence in the Entry Tax Act, and alternately make provisions for adjustments and set-offs in other enactments of Sales Tax or Value Added Tax Acts.

116. The term 'any tax' means any exaction by any impost or levy. The effect of all the taxes levied on the goods imported from other States and the ones manufactured within the State must be such that no discrimination is caused either to the imported goods or locally manufactured goods. Unlike Section 92 of the Australian Constitution, Art. 304(a) does not talk of uniformity. Section 92 of the Australian Constitution reads as follows:- "On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free." No such restriction is imposed on the legislative power of the States in India to ensure uniformity in levy of a particular tax. The raison d! etre for use of the expression "so, however, as not to discriminate" is to prohibit protectionism. Moreover, Constitution of India does not contain a provision similar to Section 55 of the Australian Constitution which mandates one tax law on one subject. In India, the State Legislature is nowhere obligated by the Constitution to ensure that the law imposing tax deals with one subject of taxation only.

117. The chargeable event in the case of entry tax is entry of goods into a local area. By its very nature, entry tax does not contemplate impost on indigenous goods. Goods imported into a local area from another State are subjected to entry tax but goods entering into a local area from another local area of the same State do not attract entry tax. In this way, it may appear that goods imported from outside the State are put to a disadvantageous position but in terms of tax treatment there is no discrimination. The essence of Art. 304(a) lies in ensuring equality of fiscal burden and absence of discrimination. In terms of Art. 304(a), the only requirement is that the goods imported into the local area should not be discriminated against. As discussed infra, in tax treatment there is no discrimination between the goods.

118. The expression 'any tax' used in Art. 304(a) is generic in nature and covers all taxes on goods which a State is competent to impose by virtue of Articles 245 and 246 read with List II of Seventh Schedule. A Scheme adopted by a State Legislature whereby several taxes are levied on the goods (either locally produced or imported from other States) under different heads, cannot be faulted with if it conforms to the principle of equivalence and non-discrimination. For e.g., both sales tax levied under entry 54, List II and entry tax levied under entry 52, List II are taxes on goods. It is the burden of the tax which can discriminate and not the form. States are free to equalise the burden of entry tax on the goods imported from other States by giving them set-off against the sales tax paid by them in the exporting State. In such a manner, equivalence can be

brought about in the tax burden borne by the goods imported from other States and the locally manufactured/produced goods. The contention of the assessees that the term 'any tax' used in Art. 304(a) refers to every tax distinctly, thereby prohibiting imposition of entry tax on imported goods unless, entry tax is imposed on locally manufactured/produced goods, does not lead to just and reasonable interpretation of Art. 304(a). The wholesome effect of the taxes levied under distinct heads needs to be taken into account. The tax burden borne by the goods form a part of the price of the goods and if both, locally manufactured/produced goods and imported goods are subjected to similar tax burdens, irrespective of the heads under which the taxes are levied, say entry tax or sales tax etc., then no discrimination can be said to have been caused.

119. In case if entry tax not levied to equalize tax burden on the local goods and goods imported from outside, there will be huge trade diversion to low-rate tax State, causing loss of revenue to the high-rate tax States, where the goods are used or consumed. Let us take an example of entry tax in the case of motor vehicles. System of sales tax on motor vehicles varies from one State to another. Rates of tax also vary according to the category of the vehicles viz., car, jeep, scooter, motorcycle, truck, tractor etc. Inter-State sales tax differential is large enough to induce trade diversions from high-rate tax States to low-rate tax States. These trade diversions have their impact on the collection of sales tax and results in loss of tax revenue to the State and the local area where the vehicles are used; but there is tax gain to the exchequer of the low-rate tax State where the vehicles are shown to have been purchased. Thus levy of entry tax by the importing State where the vehicles are used is justified to accord equal treatment to vehicles purchased within the State and those purchased from outside.

120. Often the diversion occurs merely on paper; for instance, manufacturers of vehicles in Tamil Nadu may employ local dealers in low-rate tax State/Union territories to sell their products to consumers all over the country. Where the tax rates differ widely in adjoining States/Union Territories, dealers located in low-rate tax territories act as agents for purchasers from the State with high-rate tax areas/territories. The vehicles do not move physically but the sales are shown to have taken place outside the high-rate tax State. The
State where sale is said to have taken place stands to gain but the State where the vehicle is used loses the revenue of its sales tax. The extent of differentiation in tax rates is evidently large enough to induce trade diversion from high-rate tax States to low-rate tax territories. In such cases, levy of entry tax equalizes the revenue loss to the State where the vehicle is used, and at the same time prevents discrimination between the locally purchased vehicles and vehicles purchased in other States/Union Territories.

121. Entry of goods into a local area from another local area of the State can be effected either by a dealer who purchased the goods from the manufacturer or by an individual. A dealer who effects entry of goods into a local area from another local area in the same State would be taxed in the form of sales tax/VAT; so also the individual would have already paid the sales tax in another local area, where he bought the goods. In case of entry tax levied on goods imported from other State, set-off like in the cases of State enactments of Tamil Nadu and Andhra Pradesh is given to the extent of

the sales tax/VAT paid in the purchasing State; in few of the States like Kerala, after levy of entry tax, to the extent entry tax paid, input credit is given from the sales tax/VAT payable in the State where the goods are imported. Tax burden is more or less the same, for both indigenous goods and outside goods. This is because, where an entry tax is imposed on goods brought from outside, the benefit of credit of the amount already paid as entry tax is given as input credit for the purpose of payment of VAT. Moreover, if a State enactment provides for set-off and statutory exemptions to goods paying local sales tax, thereby equalising the net tax burden on the imported goods and
local goods, it does not fall foul under Art. 304(a), so long as it is balancing sales tax against the entry tax.

122. The question as to whether entry tax in a particular case constitutes an impediment will always have to be decided with reference to the comparison of burdens that are cast on persons who bring the goods into the taxing State and that which is suffered by the persons who manufacture or produce the goods within the State. Art. 304(a) does not prevent levy of tax on goods imported from other States. The expression used is 'any tax'; what is prohibited is such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. The object is to prevent imported goods from being discriminated against by imposing a higher tax thereon than on local goods. If the tax burden on both the categories are almost the same, then the entry tax obviously cannot constitute an impediment to the very flow of trade and commerce across the borders of the State. There is no merit in the contention of the assessees that the levy of entry tax only on goods imported from other States and not on indigenous goods is discriminatory and violative of Art. 304(a).

123. In a catena of decisions, this Court has struck down the levy of entry tax on the imported goods holding that the levy is discriminatory and not saved by Art. 304(a). In *Indian Cement and Ors. v. State of Andhra Pradesh and Ors.*[52], the Government of Andhra Pradesh issued a Notification reducing the rate of sales tax on sale of locally produced cement to bulk consumers to 4%, on the other hand, the sales tax imposed on sale of cement imported from the other States was levied at 13.75%. Thus, the indigenous cement producers had a benefit of 9.75%. Levy of sales tax imposed on sale of cement imported from other States was challenged as impeding free flow of trade and commerce. The Supreme Court held the Notification invalid as it was hit by Art. 304(a) affecting inter-State trade and commerce.

124. In *Western Electronic and Anr. vs. State of Gujarat and Ors*[53]. State of Gujarat imposed sales tax at 15% on all electronic goods whether locally manufactured or imported from outside. After sometime, the State reduced the tax to 10% on goods imported from outside and to 1% on locally manufactured goods with a view to give incentive to encourage local manufacturing units. The Supreme Court held that by applying different rates of tax between goods imported into the State of Gujarat and goods manufactured within that State is discriminatory and violative of Art. 304(a) and, accordingly, quashed the Notification.

125. In *State of U.P. and Anr. v. Laxmi Paper Mart and Ors*[54]. State Government had exempted the exercise-books made from paper purchases within Uttar Pradesh from the levy of sales tax. Whereas, exercise-books produced outside the State of Uttar Pradesh were subjected to sales tax at the rate of 5%. The said exemption granted to indigenously manufactured exercise-books was challenged. The challenge was upheld by this Court and the exemption granted to locally manufactured exercise-books was held to be discriminatory within the meaning of Art. 304(a) of the Constitution of India. Preferential treatment for locally produced goods by grant of exemption or set-off etc. and non-grant of such exemption or set-off to goods imported from other States - Not-discriminatory:

126. While States have the sovereign power to levy taxes to raise revenue, difference in rates of taxes by itself or granting tax incentive or concession to local manufacturer by itself, cannot amount to discrimination. The word "discrimination" involves an element of "intentional and purposeful differentiation". It creates economic and regional imbalances in India and is an area of concern.

127. Contention of States is that apart from legislative power to levy taxes, States also have the power to grant exemptions, tax concessions or incentives to the goods manufactured within the State so as to encourage the manufacturing units and traders within the State, and also to attain economic growth and development. Reiterating the same, the learned Attorney General has submitted that such fiscal measures are necessary for economic parity as also for further strengthening of the economic unity of the nation which the assessees themselves desire. *Placing reliance upon Video Electronics Pvt. Ltd. and Anr. v. State of Punjab and Anr*[55]. it was submitted that every differentiation in the tax rebate, exemption or tax concession granted to indigenous goods which may result in differentiation in the rate of tax on goods imported into the State, would not amount to discrimination falling foul under Art.304(a). The States submit that every differentiation is not discrimination, and only those restrictions which impede the flow of trade, commerce and intercourse would fall foul under Art.304 (a). The above contention of the States has been favourably considered by the Supreme Court over the years. The Supreme Court has taken note of the differentiation on consideration of natural or economic factors prevailing in different regions which need to be encouraged by providing tax incentives to attain economic equality in growth and development.

128. Part XIII envisages a two-fold object:- (i) facilitation of a common market through ease of trade, commerce and intercourse by removal of barriers; and (ii) development of economically backward regions through regulations or restrictions which may incidentally differentiate between States or regions. Part XIII is not about "freedom" alone but is a code of checks and balances on inter-State trade, commerce and intercourse intended to achieve economic integration of the country and parity. Balanced development of the country is an equally vital facet of economic integration. The "freedom" referred to in Art. 301 must take flavour from the expression "throughout the territory of India"; the Union was envisaged not only as a political union but also an economic union. The grand vision was to unify the country, not only politically but also by creation of an economic union of hitherto disparate Provinces and Princely States.

Freedom of movement of goods and services and the creation of a common market must be understood in this context. Thus, the spirit of Part XIII must be seen in the context of achieving a balance between a cohesive economic union having due regard for the federal character of the Constitution and not in the sense of a handicap for State's individual development.

129. We may usefully refer to the following passage authored by Prof. D.D. Basu in Comparative Federalism, Prentice Hall of India, 1987, which reads as under:

> "The great problem of any federal structure is to prevent the growth of sectional and local interests which are inimical to the interests of the nation as a whole. The strength of the Union may be achieved only by minimizing inter-State barriers as much as possible, so that the people may feel that they are the members of one nation, though they may, for the time being, be residents of particular geographical divisions of the country. One of the means to achieve this object is to guarantee to every citizen the freedom of movement throughout the territory of the Union, and also to reside and settle in any part thereof. While a federation is formed to preserve or secure regional autonomy, that is not done at the sacrifice of notional interests. Unless the national interests are safeguarded, the country would be divided into pieces, resulting in a weak government unable to maintain itself from foreign aggression, and would also create economic chaos in an age when apparently local disturbances have a wide repercussion. It is this last mentioned economic strength of the federation which is intended to be ensured by the safeguard for maintaining freedom of trade, commerce and intercourse throughout the federal territory, which safeguard the Union and the States are both enjoined not to violate." [Page 613] Part XIII and the provisions therein are to be interpreted in a manner that encourages a backward region or creates a level playing field for those parts of the country that may not have reached the desired level of development.

130. Historically, regional imbalances in India started from the British regime. During that time, industrialists started development in a few earmarked regions of the country like the metropolitan cities of Kolkata, Mumbai, Chennai that possessed rich potential for manufacturing, trading and transport facilities. This resulted in an uneven growth amongst the States, keeping few States less developed. The regional imbalances and general economy of the country were taken note of by the framers of the Constitution. The Constituent Assembly was conscious of the uneven development in different parts of the country and the need to create a level playing field by removal of trade barriers as well as by affording avenues for economic opportunity and economic equality for less developed parts of the country. Significant observations have been made in Constituent Assembly Debates justifying certain amount of flexibility to the States. In this regard, reference to Constituent Assembly Debates dated 30.07.1949 to 18.09.1949 whereby Dr. P.S. Deshmukh proposed a series of amendments in Part XIII granting powers to the States, is relevant to be noted:-
Dr. P.S. Deshmukh:

> "Trade and commerce are not things which are decided once, for all; they are

things that arise and grown from day to day. They may be varied; there may be circumstances and situations when the whole thing will have to be revised. This may arise so far as a particular State is concerned or in respect of more than one State.

How pompously did we decide that there shall be “free trade” everywhere. It is not such an easy thing as that and I hope that this is now broadly realized. For instance, we know that the stage, of advancement and progress of the various units of the Union varies considerably. Some of them are backward like Assam or Orissa where there are, very few industries and very little trade is in the hands, at least of the indigenous population. We may have probably to give them some protection in order that they may rapidly come on par with other units. It may be necessary also from time to time to vary our provisions so far as aid and concessions to industries and other things are concerned. I therefore do not think that is right to bar all discrimination, as it is called (in fact it is not), barring all possibility of help to those who are backward and who are unable to compete with the more advanced, and who therefore, stand in need of ‘assistance. ’ From that point of view, my amendment seeks to give Parliament a blank cheque and leave to it entirely the determination of the policy. With regard to the trade and commerce not only of the whole Union or in regard to any particular State or States, but so far as all States and their trade and commerce inter se is concerned. Therefore, I have proposed a very simple provision as has been embodied in my amendment No. 340.” [Page No. 1133] While the proposed amendments were not accepted, the debate acknowledged that flexibility to allow certain amount of leverage to the States was necessary and also desirable. It is apposite to refer to the following observation by Shri Alladi Krishnaswami Ayyar in Constituent Assembly Debates dated 30.07.1949 to 18.09.1949:- Shri Alladi Krishnaswami Ayyar: ‘‘.....My Friend Dr. Ambedkar, in the scheme he has evolved, has taken into account the larger interests of India as well as the interests of particular State and the wide geography of this country in which the interests of one region differ from the interests of another region My Friend Mr. Krishnamachari has pointed out that this freedom clause in the Australian Constitution has given rise to considerable trouble and to conflicting decisions of the highest Court. There has been a feeling in those parts of Australia which depend for their well-being on agricultural conditions that their interests are being sacrificed to manufacturing regions, and there has been rivalry between manufacturing and agricultural interests. Therefore, in a federation what you have to do is, first, you will have to take into account the larger interests of India and permit freedom of trade and intercourse as far as possible. Secondly, you cannot ignore altogether regional interests. Thirdly, there must be the power intervention of the Centre in any case of crises to deal with peculiar problems that might arise in any part of India. All these three factors are taken into account in the scheme that has been placed before you.” [Emphasis added] [Page No. 1143]

131. Similar was the concern expressed by Shri C. Rajagopalachari in his observations on the proposed draft Article 10:

“C. Rajagopalachari: I would request members who have given thought to this

subject to please inform me how the units will raise their revenue. As it is, the Union does not contemplate the distribution of subsidies to the provinces. The provinces or groups differ among themselves, some are rich and some are poor. Some are capable of managing with their existing resources; but others may have to increase their revenue for managing their affairs. If you impose so many limitations on them, how can they do that? It is all very well to say free trade is necessary; but how are the provinces to live?"

[Page No.254 of the Framing of India's Constitution Select Documents-The Project Committee, Volume 2 by the Indian Institute of Public Administration Universal Law Publishing Co. Pvt. Ltd.]

132. There are considerable regional disparities in India attributable to a variety of reasons. Economically speaking, of these reasons, the ones that are most apparent are geography and consequent economic inadequacy. States with access to seacoasts and natural resources including mineral wealth, water resources have a definite edge over the other States. Whereas States that have terrains that make access to a region difficult, including hills, rivers and dense forests, show lesser signs of economic development. Lack of perennial sources of water or water scarcity due to lower precipitation can also constrain the development of a region. Historically, more development opportunities have been made available to already forward States that had the initial geographic advantage. It is the natural tendency of the private sector to set up industries in already developed regions, which provide infrastructural support required to maintain those industries. This has accelerated the development in these forward States; and the backward regions, unable to attract significant investment have not seen much growth. To counter-balance this tendency, various incentive and disincentive schemes have been introduced to direct investments to backward regions. However, the success of these policies has been limited because often the States with these backward regions are unable to meet their expenses and provide economic overheads, such as transport, communication, power, banking & insurance etc. This has widened the gaps between the States where investments of the past have created adequate social and economic infrastructure to attract private investments and the States that were neglected in the past and are unable to attract investments due to lack of infrastructure. [Reference: N J Kurian, "Regional Disparities in India", Planning Commission of India, 2001 available at: http://planningcommission.nic.in/reports/sereport/ser/vision- 2025/regdsprty.

133. A recent news article published in 'The Hindu', titled "The gap between rich and poor States", delineates this economic disparity between the States. The authors propose that since contrary to global experiences, India continues to show trends of divergence among its large States, it is time to accept the country's economic diversity. Amid such economic disparity
among States with varying future needs and priorities, the way forward is greater devolution of fiscal and legislative powers on the States to create a level playing field. Relevant portion of this article reads as under:-

"...per capita net domestic product from 1960 to 2014 of India's 12 largest States,

that accounted for 85 per cent of the total population, shows that economic disparity within India's States is among the largest in the world... This gap of four times between the richest and the poorest large State in India is among the highest in the world. A similar ratio in other federal polities such as the U.S., European Union and China is between two and three times. Our convergence analysis shows that this economic disparity among States is only widening and not narrowing. India is the only large country in the world today that is experiencing an economic divergence among its States and not convergence, as economic theory would posit."

" Pre-1990 and post-1990 look like almost two different eras in India's history of economic diversity among States. Economic theory would suggest that the poorer regions grow faster to catch up with the richer States to cause an eventual convergence, as is happening globally. Contrary to global experiences of narrowing disparity, both across and within nations, India actually shows trends of an exacerbating divergence among its large States, implying the richer States will continue to grow faster."

"Whatever be the reasons, it is quite evident that the priorities of a more prosperous State will be quite different from those that are still very poor. India's cultural and political diversity is a well-entrenched fact. It is time to accept its economic diversity too. Amid such economic disparity among States with varying future needs and priorities, a Delhi-based one-size-fits-all policy regime for all of India is entirely anachronistics the struggles of the European Union in balancing common market policies for economically diverse nations should serve as a gentle reminder for an even more diverse India. "

[emphasis added]

[By Praveen Chakravarty and Vivek Dehejia [New Delhi Edition dated 5th September, 2016]

134. Since economic unity of the nation is the underlying object for freedom in Art. 301, it would be necessary to define the concept of economic unity adopted by the Constitution of India. Firstly, economic unity cannot but be federal in nature; it must involve the even development of all the States. All States, particularly, the underdeveloped and far-flung border-States have a right to develop themselves so as to secure the welfare of their residents. Secondly, the object of freedom of trade, commerce and intercourse is to foster economic unity by contribution to the development of all the States. Thirdly, as per the Directive Principles of State Policy, the States are to sub-serve common good; secure and protect a social order which stands for the welfare of the people; endeavour to provide an adequate means of livelihood; and also secure, within the limits of its economic capacity the right to work, education and public assistance.

135. Re-organisation of States is yet another factor which has to be borne in mind. Creation of State of Uttarakhand from the undeveloped hilly area of Uttar Pradesh;

State of Jharkhand from the predominantly tribal areas of the State of Bihar, State of Chhattisgarh from the State of Madhya Pradesh and the recent bifurcation of the State of Telangana from the State of Andhra Pradesh comes to mind. The newly bifurcated States have to develop their new capitals, create new State infrastructure including High Courts in due course. They have to develop their own industrial bases for manufacture and production and for creating job opportunities. To attract capital investment, they have to provide infrastructure like transport, communication, power and technology. Re-organisation of States apart, as a Welfare State, a State is under an obligation to create job opportunities and promote welfare of the people by securing standard of living and economic justice. Having regard to the multifarious activities of a Welfare State, it is necessary that the States must have leverage/flexibility in exercise of their power to levy taxes and, therefore, steps taken by the States that result in differentiation cannot amount to discrimination that impedes the free flow of trade, commerce and intercourse.

136. Manufacturing activities within the State involve several activities right from sourcing of raw-materials, manufacture of goods, marketing of the manufactured goods, and export of the manufactured goods. Manufacturing activities convert the State from a mere trade hub to a manufacturing hub, creating employment opportunities for the locals, thereby giving impetus to the growth of the State. Manufacturing is a giant step for boosting the economy of the State; it brings in opportunities and socio-economic benefits to the residents of the respective States. Per contra, goods coming in from outside the State only tap the market potential of the State without creating any employment opportunities or boosting the economy of the State. Thus granting exemptions/set-off/tax incentives to locally produced goods and not granting such exemption to goods coming from outside cannot be said to be discriminatory.

137. Furthermore, every differentiation is not necessarily discriminatory. The word ‘discrimination’ used in Art. 304(a) requires an element of intentional and purposeful differentiation that creates an economic barrier. It involves an element of an intentional difference between the treatment of locally produced goods and goods imported from other States. The distinction between “differentiation and discrimination” has been culled out in *Kathi Raning Rawat v. The State of Saurashtra*[56] wherein the Constitution Bench held as under:-

> “Patanjali Shastri J:....
>
> All legislative differentiation is not necessarily discriminatory. In fact, the word “discrimination” does not occur in Article 14. The expression “discriminate against” is used in Article 15(1) and Article 16(2), and it means, according to the Oxford Dictionary, “to make an adverse distinction with regard to; to distinguish unfavourably from others”. Discrimination thus involves an element of unfavourable bias and it is in that sense that the expression has to be understood in this context. If such bias is disclosed and is based on any of the grounds mentioned in Articles 15 and 16, it may well be that the statue will, without more, incur condemnation as violating a specific constitutional prohibition unless it is saved by one or other of the provisos to those articles. But the position under

Article 14 is different. Equal protection claims under that Article are examined with the presumption that the State action is reasonable and justified. This presumption of constitutionality stems from the wide power of classification which the legislature must, of necessity, possess in making laws operating differently as regards different groups of persons in order to give effect to its policies. The power of the State to regulate criminal trials by constituting different courts with different procedures according to the needs of different parts of its territory is an essential part of its police power - (cf. Missouri v. Lewis) (3). Though the differing (1) [1950] SCR 88 (3) 101 US 22 (92) AIR 1951 Hyderabad II."

"Fazl Ali, J.:

.I think that a distinction should be drawn between "discrimination without reason" and "discrimination with reason". The whole doctrine of classification is based on this distinction and on the well-known fact that the circumstances which govern one set of persons or objects may not necessarily be the same as those governing another set of persons or objects, so that the question of unequal treatment does not really arise as between persons governed by different conditions and different sets of circumstances..."

[Emphasis added]

138. The desired objective of economic integration through checks and balances to encourage less developed parts of the country, so that they may compete as equals with others, does not contravene Part XIII of the Constitution. In Video Electronics, the three Judges Bench held as under:

"20. The question as we see is, how to harmonise the construction of the several provisions of the Constitution, It is true that if a particular provision being taxing provision or otherwise impedes directly or immediately the free flow of trade within the Union of India then it will be violative of Article 301 of the Constitution. It has further to be borne in mind that Article 301 enjoins that trade, commerce and intercourse throughout the territory of India shall be free. The first question, therefore, which one has to examine in this case is, whether the sales tax provisions (exemption etc.) in these cases directly and immediately restrict the free flow of trade and commerce within the meaning of Article 301 of the Constitution, We have examined the scheme of Article 301 of the Constitution read with Article 304 and the observations of this Court in Atiabari's case [1961] 1 SCR 809 (supra), as also the observations made by this Court in Automobile Transport, Rajasthan's case [1963] 1 SCR 491 (supra). In our opinion Part XIII of the Constitution cannot be read in isolation. It is part and parcel of a single constitutional instrument envisaging a federal scheme and containing general scheme conferring legislative powers in respect of the matters relating to list II of the 7th Schedule on the States. It also confers plenary powers on States to raise revenue for its purposes and does not require that every legislation of the State must obtain assent of the President. Constitution of India is an organic document. It must be so construed that it lives and adapts itself to the exigencies of the

situation, in a growing and evolving society, economically, politically and socially. The meaning of the expressions used there must, therefore, be so interpreted that it attempts to solve the present problem of distribution of power and rights of the different States in the Union of India, and anticipate the future contingencies that might arise in a developing organism. Constitution must be able to comprehend the present at the relevant time and anticipate the future which is natural and necessary corollary for a growing and living organism. That must be part of the constitutional adjudication. Hence, the economic development of States to bring these into equality with all other States and thereby develop the economic unity of India is one of the major commitments or goals of the constitutional aspirations of this land. For working of an orderly society economic equality of all the States is as much vital as economic unity.

22. It has to be examined whether difference in rates per se discriminates so as to come within Articles 301 and 304(a) of the Constitution. It is manifest that free flow of trade between two States does not necessarily or generally depend upon the rate of tax alone. Many factors including the cost of goods play an important role in the movement of goods from one State to another. Hence the mere fact that there is a difference in the rate of tax on goods locally manufactured and those imported would not amount to hampering of trade between the two States within the meaning of Article 301 of the Constitution. As is manifest, Article 304 is an exception to Article 301 of the Constitution. The need of taking resort to exception will arise only if the tax impugned is hit by Articles 301 and 303 of the Constitution. If it is not then Article 304 of the Constitution will not come into picture at all. See the observations in Nataraja Mudaliar's case [1968] 3 SCR 829 of the report. It has to be borne in mind that there may be differentiations based on consideration of natural or business factors which are more or less in force in different localities. A State might be allowed to impose a higher rate of tax on a commodity either when it is not consumed at all within the State or if it is felt that the burden falling on consumers within the State, will be more than that and large benefit is derived by the revenue. The imposition of a rate of sales tax is influenced by various political, economic and social factors. Prevalence of differential rate of tax on sales of the same commodity cannot be regarded in isolation as determinative of the object to discriminate between one State and another. Under the Constitution originally framed revenue from sales tax was reserved for the States.

24. The object is to prevent discrimination against the imported goods by imposing tax on such goods at a rate higher than that borne by local goods. The question as to when the levy of tax would constitute discrimination would depend upon a variety of factors including the rate of tax and the item of goods in respect of the sale on which it is levied. Every differentiation is not discrimination. The word 'discrimination' is not used in Article 14 but is used in Articles 16, 303 & 304(a). When used in Article 304(a), it involves an element of intentional and purposeful differentiation thereby creating economic barrier and involves an element of an unfavourable bias. Discrimination implies an unfair classification. Reference may be made to the observations of this Court in Kathi Raning Rawat

v. State of Saurashtra, 1952 SCR 435 where Chief Justice Shastri at p. 442 of the report reiterated that all legislative differentiation is not necessarily discriminatory. At p. 448 of AIR) of the report, Justice Fazal Ali noticed the, distinction between 'discrimination without reason' and 'discrimination with reason'. The whole doctrine of classification is based on this and on the well-known fact that the circumstances covering one set of provisions or objects may not necessarily be the same as these covering another set of provisions and objects so that the question of unequal treatment does not arise as between the provisions covered by different sets of circumstances.

...28. Concept of economic barrier must be adopted in a dynamic sense with changing conditions. What constitutes an economic barrier at one point of time often cease to be so at another point of time. It will be wrong to denude the people of the State of the right to grant exemptions which flow from the plenary powers of legislative heads in List II of the 7th Schedule of the Constitution. In a federal polity, all the States having powers to grant exemption to specified class for limited period, such granting of exemption cannot be held to be contrary to the concept of economic unity. The contents of economic unity by the people of India would necessarily include the power to grant exemption or to reduce the rate of tax in special cases for achieving the industrial development or to provide tax incentives to attain economic equality in growth and development. When all the States have such provisions to exempt or reduce rates the question of economic war between the States inter se or economic disintegration of the country as such does not arise. It is not open to any party to say that this should be done and this should not be done by either one way or the other. It cannot be disputed that it is open to the States to realise tax and thereafter remit the same or pay back to the local manufacturers in the shape of subsidies and that would neither discriminate nor be hit by Article 304(a) of the Constitution. In this case and as in all constitutional adjudications the substance of the matter has to be looked into to find out whether there is any discrimination in violation of the constitutional mandate."

[Emphasis added]

Thus while considering the scope of "discrimination" under Art. 304(a) in Video Electronics, this Court has carved out an exception that States have powers to grant exemption to specific class for limited period and that such grant of exemption cannot be held to be discriminatory. To reduce the rate of tax in special cases or to provide tax incentives is for achieving the industrial development and attainment of economic equality in growth and development

139. In *Shri Mahavir Oil Mills and Anr. v. State of J&K and Others*[57] a Division Bench of this Court, however, struck a contrary note. The State of Jammu and Kashmir granted exemption to the edible oil produced by small scale industries within the State of Jammu and Kashmir from sales tax while subjecting the edible oil produced in other States to sales tax at 8 per cent. A subsequent Notification was issued on 20.12.1993 as a result of which the general rate of sales tax payable on edible oil became 8%. The

manufacturers of edible oil from the adjoining States claimed that the exemption granted from payment of tax to the local industries was discriminatory. The exemption given by the Government of Jammu and Kashmir to the manufacturers of the edible oil was absolute and the period of exemption was five years - which was later extended by another five years. The said legislation was struck down on the ground that the State has brought about discrimination prohibited by Art. 304(a) of the Constitution. The Court declined to apply the limited exception carved out in Video Electronics and observed that the said exception in Video Electronics cannot be widened or expanded to cover cases of a different kind. This Court held that the unconditional exemption granted to edible oil industries within the State of Jammu and Kashmir for a period of ten years and at the same time subjecting edible oil imported from other States to sales tax at 8% was discriminatory and violative of Art. 304(a) of the Constitution.

140. The decision in Video Electronics was, however, approvingly referred to by the Constitution Bench in *Sri Diavijav Cement Company Limited and Ors. v. State of Rajasthan and Others*[58] In Digvijay, Section 8 of the Central Sales Tax Act came up for consideration. Section 8 of the Central Sales Tax Act stipulates that the State Governments were empowered to either exempt any goods from Central Sales Tax or to prescribe a lower rate of tax. The State of Rajasthan had reduced the rate to seven percent though stipulated local sales tax was sixteen per cent. In consequence, cement in Rajasthan became cheaper in comparison to Gujarat and that increased the flow of cement from Rajasthan to other States. After referring to the cases Firm *ATB Mehtab Majid & Co v. State of Madras & Anr*[59]*. and State of Madras v. N.K. Nataraja Mudaliar*[30] this Court held as under:-

> "24. We are unable to agree with the contention of the learned counsel for the petitioners that the impugned notification had the effect of preventing or hindering the free movement of goods from one State to another. As far as the State of Rajasthan is concerned, it had the opposite effect. Merely because local rate of tax in the State of Gujarat on the sale of cement was higher than the inter-State sales tax on the cement sold from Rajasthan cannot lead to the conclusion that the impugned notification prevented or hindered the free movement of goods from one State to another. In fact the impugned notification had the opposite effect, namely, it increased the movement of cement from Rajasthan to other States. It is not as if the impugned notification created a barrier which may have had the effect of hindering free movement of goods but on the other hand, the sales tax barrier was lowered resulting in increased volume of inter-state trade."

141. It follows from the Constituent Assembly Debates and the decisions in Video Electronics and Digvijay that historical, cultural, geographical and other factors have an impact on trade and commerce. While insisting on economic integration of the nation, Courts are to keep in view the regional requirements so as to cater to the need of economic development of the nation as a whole. Government incentives to invest in backward areas granting subsidies or tax concessions for a certain period of time would be permissible and would fall outside the scope of Part XIII and Art. 304(a). Such action of the State Government is not discriminatory; rather it aims at ensuring economic equality.

142. In Video Electronics and Digvijay, this Court held that it is constitutionally permissible for a State Legislature to make laws that promote and encourage local trade; a form of affirmative action to move beyond the concept of discrimination towards true and a stronger union which is the underlining objective of the Constitution. Although balanced growth and economic integration of the nation as a whole has been accepted as one of the major objectives of economic planning, it is to make a headway in achieving the object. The growing regional disparities have become a reality and hence may pose a barrier to India's future economic growth.

143. India is a union of States with federalism as a basic feature of the Constitution. However, revenue-wise Union has an edge over the States. All major taxes like income tax, wealth tax, service tax, excise duty etc. are with the Union. Taxes raised by the States are insufficient to discharge their mandate as a Welfare State. India still exists in villages and countryside. Substantial number of population is still below poverty level. Subjects like public order (entry 1, List II); public health and sanitation, hospital and dispensaries (entry 6, List II); Education (entry 25, List III); providing employment opportunities; roads, bridges etc. and other infrastructure (entry 30, List II) inter alia are subject matters for the State; and States have limited resources to provide for education, healthcare, civic amenities, infrastructure, communications, village industries, rural employment and technology and to ensure dignified human living of the people of the State, without access to an adequate source of revenue.

144. As discussed earlier, development of the country is seemingly unbalanced and unequal. Despite the economic reforms initiated in the country about twenty five years ago, entrepreneurs are hesitant to invest in backward States because of varied reasons like inadequacy of power, lack of infrastructure and transportation, quality of human resources etc. Resultantly, few States continue to be backward States. In order to have a planned development for the benefit of the people and overall growth of the country as a nation, regional imbalances are to be removed. While trade, commerce and intercourse is important for the economic unity of the nation, the Courts cannot be oblivious of the responsibilities of a Welfare State in raising its resources by levy of taxes to meet the challenges. Incentives to invest in backward areas, subsidies and tax concessions are some of the measures used by the State to guide the location of the industries in backward areas and to generate employment opportunities for the people of the State. While power of taxation is indispensable, State also has the power to grant tax concessions or incentives to indigenous manufacturers/producers. Such incentives/tax concessions would certainly create differentiation between the locally produced goods and the goods that are imported into the State from the sister States; but the same cannot be said to be discriminatory and falling foul of Art.304(a).

145. I summarise my conclusion on this point as under:- While I agree with the views of the Constitution Bench in Digvijay and Video Electronics, I do not endorse the views of Mahavir Oil Mills. Accordingly, the law laid down in Laxmi Paper Mart which relies upon Mahavir Oils is also held bad in law. Moreover, Indian Cement needs no consideration as it has been specifically overruled in Digvijay. The conclusions in this regard could be summarized as under:-

"• Any difference in the rate of tax on goods locally manufactured and those imported, such difference not being discriminatory does not fall foul of Art. 304(a);

• Any incentive/benefits of concession in the rate of tax given to the indigenous manufacturers in order to encourage the manufacture/production in the State cannot be said to be discriminatory. Repercussions of Art. 304(a) when no local goods are produced:"

146. The State may by law impose any tax on imported goods to which submission of the assessees that when a State does not produce or manufacture goods within its territory then it cannot resort to the power conferred on it by Art.304(a) to impose a tax on similar imported goods. In support of their contentions, the assessees placed reliance upon *Kalyani Stores v. State of Orissa*[61] where no foreign liquor was produced or manufactured in the State of Orissa but tax was levied on foreign liquor imported into the State of Orissa. When the levy was challenged as violative of Art.301, it was held that:-

"7 The notification levying duty at the enhanced rate is purely a fiscal measure and cannot be said to be a reasonable restriction on the freedom of trade in the public interest. Article 301 has declared freedom of trade, commerce and intercourse throughout the territory of India, and restriction on that freedom may only be justified if it falls within Article 304. Reasonableness of the restriction would have to be adjudged in the light of the purpose for which the restriction is imposed, that is, "as may be required in the public interest". Without entering upon an exhaustive categorization of what may be deemed "required in the public interest", it may be said that restrictions which may validly be imposed under Article 304(b) are those which seek to protect public health, safety, morals and property within the territory. Exercise of the power under Article 304(a) can only be effective if the tax or duty imposed on goods imported from other States and the tax or duty imposed on similar goods manufactured or produced in that State are such that there is no discrimination against imported goods. As no foreign liquor is produced or manufactured in the State of Orissa the power to legislate given by Article 304 is not available and the restriction which is declared on the freedom of trade, commerce or intercourse by Article 301 of the Constitution remains unfettered."

[Emphasis supplied]

Learned Counsel for the assesses have relied on Kalyani Stores to contend that Art. 304(a) is the only avenue for the State to impose entry tax and the same can be availed of only when there are similar goods being manufactured within the State so as to prevent discrimination. However, the law laid down in Kalyani Stores cannot be applied in the case of entry tax
levied under entry 52, List II. The dictum of Kalyani Stores has a limited application to counterveiling duties imposed on sale of liquor levied under entry 51, List II and that too to the limited extent it is actually in force as of now. Power to impose counterveiling

duties of excise on alcoholic beverages etc. manufactured or produced in the State and counterveiling duties at the same or higher rates on similar goods manufactured or produced elsewhere in India, under entry 51, List II is materially distinct from a levy under entry 52, List II and thus, an interpretation of the law relating to the former cannot be applied to the latter.

147. Furthermore, Kalyani Stores does not appear to have noticed the non-obstante clause in Art. 304 "Notwithstanding anything in Article 301 or Article 303....". The non obstante clause should be understood in a manner appropriate to the substance of Articles 302 to 304. The true source of power of the State Legislature remains in Part XI, in Article 245 read with Article 246 and entries of List II. Art.304 is not a source of power; it embodies a re-statement of powers conferred under Articles 245 and 246 read with the entries of List II of Seventh Schedule with some limitations.

148. The rigorous view taken in Kalyani Stores was diluted in *State of Kerala v. Abdul Qadir and Others*[62] The State of Kerala levied a tax on tobacco which was imported into the State from outside. No tobacco was manufactured or produced within the State of Kerala. The Court, upon a challenge to the tax law, upheld the levy of tax on tobacco and observed that the correct approach was to see whether the impugned tax impeded the free flow of trade and commerce under Art.301. The Court stated that levy of tax on tobacco did not impede the free flow of trade and commerce.

149. The first part of Art. 304(a) re-states the power of the State to impose a tax on goods imported from the other States. Second part of Art. 304(a) places a limitation on the power of the State Legislature. It provides that a State may only tax imported goods so as not to discriminate them with the locally produced or manufactured similar goods i.e. the limitation of non-discrimination vis-a-vis similar internal goods. When a situation arises where no similar goods are manufactured or produced in that State, the tax merely does not fall within the scope of Art.304(a); the limitation is taken away but the power to tax remains. The sovereign and plenary power of the State to tax cannot be emasculated and made subject to a limitation that a State can only tax those goods which are produced within its territory also.

150. This is better explained by way of an example: Zinc is an important mineral resource used in galvanization of iron and steel. It is also used in automotive, electrical and machinery industries. Haryana does not have zinc ore, however, it does have the industries mentioned above. If zinc is imported from Odisha or Rajasthan, then State of Haryana can impose a tax on it, even though there is no local production of zinc. This does not mean that there is a discrimination against the imported zinc. Discrimination involves an element of intentional and purposeful differentiation; without a comparable good there cannot be a disparate treatment or discrimination of the imported zinc. Thus, a State law that imposes a tax on imported goods where similar goods are not manufactured or produced in that State, will meet the requirement of Art.304(a) and there would not arise any question of discrimination.

151. It is true that when similar goods are not manufactured inside the State, there are chances of a higher rate of tax on such goods brought into the taxing State from other States but that does not mean that there should be a blanket protection of such goods

from tax. Power of the State to tax the goods imported cannot be whittled down on the ground that there are no similar goods manufactured or produced within the taxing State. Exorbitant taxation of such goods will remain open to challenge under Part III in Art. 19(1)(g) read with Art. 19(6) and Art. 14. With these observations, I hold that the power to impose a tax on imported goods is not taken away when no similar local goods are manufactured within the State and thus, the law laid down in Kalyani Stores is not a good law.

Levy of Entry Tax on Imported Goods

152. Most of the States levy entry tax on the goods imported from outside the country when they enter into a local area for consumption, use or sale therein. The issue that arises is as to whether State Legislature is competent to levy entry tax on the goods imported from other countries when they enter into a local area for consumption, use or sale therein.

153. Contention of the assessees is that import and export across the customs frontiers are covered by entry 41, List I; duties of customs including export duties are covered by entry 83, List I of the Seventh Schedule and thus transactions relating to "import/export across customs frontiers including duties of customs including export duties" fall within the exclusive domain of the Parliament. It is further contended that the mandate of Clause 1(d) of Art. 286 of the Constitution prevents the State from levying sales tax so as not to interfere with the Union's legislative power with respect to import and export across frontiers (entry 41, List I) and "the duties of customs including export duty" (entry 83, List I). It is contended that if the State is permitted to levy entry tax under entry 52, List II on goods imported from outside the country, the same would amount to levy of 'tax on imported goods' which is a clear transgression of powers of the Parliament under entry 41 and entry 83 of List I.

154. Per contra, the States contend that once the imported goods are cleared on payment of customs duty, the goods are mixed with the mass of goods in India and when such imported goods enter into the local area, the States are well within their legislative competence to levy entry tax in exercise of their legislative power under entry 52, List II. Counsel for the States have submitted before us that the taxable event under entry 83, List I and that under entry 52, List II are distinct; taxable event with respect to entry 83, List I, is the act of import i.e. bringing of goods from a foreign country to India, whereas, the taxable event under entry 52, List II is the entry of goods into local area for consumption, use or sale therein. It was further argued that entry 41, List I which deals with trade and commerce with foreign countries, import and export across custom frontiers, and definition of custom frontiers has to be read along with entry 83, List I.

Meaning of the word "Import":

155. "Import" means bringing or taking by sea or air across any customs frontier. Import is defined in Section 2(23) and imported goods in Section 2(25) of the Customs Act as under:-

> "(23) "import", with its grammatical variations and cognate expressions, means bringing into India from a place outside India;
>
> (25) "imported goods" means any goods brought into India from a place outside India but does not include goods which have been cleared for home consumption;"

156. The meaning of the word "import" has been explained in P. Ramanatha Aiyar's "The Major Law Lexicon", 4th Edition 2010 as under:-

> "The term "import" means to bring into a country merchandise from abroad and is the direct converse of the term "export" which means to carry from a state or country, as wares in commerce. The term "export" signifies etymologically "to carry out" and "import" means to "bring in". Its commercial meaning is directly contrary to the term "export". Goods brought into the country from abroad. The importation of certain goods, as authorized reprints of copyright books, false coin and indecent or obscene prints, is expressly forbidden and with regard to certain other goods, such as wine, spirits and tobacco, restrictions are imposed as to the place and manner of their importation. Goods or services brought into a country for sale, from abroad, or to bring in such goods or services." (Trade Finance & Banking) [Page 3207]

157. Similarly, as per Section 2(e) of the Foreign Trade (Development and Regulation) Act (22 of 1992), "Import' and ''export' means respectively bringing into, or taking out of India, any goods by land, sea or air.

158. "Import' and "export' across customs frontiers and definition of 'customs frontiers' are covered by entry 41, List I and "duties of customs including export duties" are covered by entry 83, List I of the Seventh Schedule. Entry 41 and entry 83 of List I of the Seventh Schedule read as under:-

> "41. Trade and commerce with foreign countries; import and export across customs frontiers; definition of customs frontiers.
>
> 83. Duties of customs including export duties. "

159. As per Section 2(28) of the Customs Act, 1962 read with Section 5(1) of the Territorial Waters Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976, 'Indian Customs Waters' mean water extending in sea upto the limit of contiguous zone, i.e., a line, every point of which is at a distance of 24 Nautical Miles from the nearest point of the base line. These definitions define the customs frontier.

160. Goods imported in a vessel/aircraft require payment of customs duty before they are cleared into the country. Unless these are not meant for customs clearance at the port/airport of arrival by particular vessel/aircraft and are intended for transit by the same vessel/aircraft or trans-shipment to another customs station or to any place outside India, detailed customs clearance formalities of the landed goods have to be

followed by the importers. In respect of goods which are off-loaded, importers have the option to clear them for home consumption after payment of the duties leviable or to clear them for warehousing without immediate discharge of the duties leviable in terms of the warehousing provisions as provided in the Customs Act. Sections 45 to 48 deal with clearance of imported goods for home consumption. In terms of Section 46, every importer is required to file Bill of Entry for clearance of goods for home consumption or warehousing in the form as prescribed by regulations. In terms of Section 47 of the Customs Act, proper officer on being satisfied that the goods entered for home consumption are not prohibited goods and the importer has paid the import duty and on being satisfied that the prescribed formalities have been duly completed, passes an order for clearance of goods for home consumption. Evidently Chapter IX of the Customs Act is a facility for warehousing, deposit of imported goods and their clearance. Section 68 provides for clearance of warehoused goods for home consumption by the importer. Under Section 68, the warehoused goods can be cleared for home consumption by presenting Bill of Entry, paying import duty etc. and obtaining an order for clearance.

161. The moment imported goods are cleared for home consumption either under Section 47 of the Act or under Section 68 of the Customs Act, the imported goods mix up with the mass of goods in the country and enter into the local area. Import of goods into the territory of India and transit of goods within the country are not integral. Import of goods and customs clearance and the entry of goods into the local areas are two distinct events. In the case of customs duty, the taxable event is entry of goods into the territory of India. The taxable event under entry 52, List II is the entry of goods into local area for consumption, use or sale therein. Two taxable events are distinct in law and there is no overlap.

162. Under the Indian Constitution, the distribution of power with regard to tax has been done in a mutually exclusive manner and in great detail with reference to different aspects of property or goods. Considering an issue with regard to excise duty and sales tax payable by a manufacturer upon manufacture and sale in Province of *Madras v. M/s Boddu Paidanna and Sons*[63]*, the* Federal Court has held that:-

> "If the taxpayer who pays a sales tax is also a manufacturer or producer of commodities subject to a central duty of excise, there may no doubt be an overlapping in one sense; but there is no overlapping in law. The two taxes which he is called on to pay are economically two separate and distinct imposts. There is in theory nothing to prevent the Central Legislature from imposing a duty of excise on a commodity as soon as it comes into existence, no matter what happens to it afterwards, whether it be sold, consumed, destroyed, or given away... It is the fact of manufacture which attracts the duty, even though it may be collected later... In the case of a sales tax, the liability to tax arises on the occasion of a sale, and a sale has no necessary connection with manufacture or production. "

...there are two complementary powers, each expressed in precise and definite terms then there is no reason for extending the meaning of the expression 'duties of excise' at

the expense of the provincial power to levy taxes on sale of goods." [Page 101]

163. Boddu Paidanna has been affirmed in *Governor General of Council v. Province of Madras*[64] in following words:-

> "Here again their Lordships find themselves in complete accord with the reasoning and ocnslusions of the Federal Court in the Boddu Paidanna Case (1). The two taxes, the one levied upon a manufacturer in respect of his goods, the other upon a vendor in respect of his sales, may, as is there pointed out, in one sense overlap. But in law there is no overlapping. The taxes are separate and distinct imposts. If in fact they overlap, that may be because the taxing authority, imposing a duty of excise, finds it convenient to impose that duty at the moment when the exciseable article leaves the factory or workshop for the first time upon the occasion of its sale. But that method of collecting the tax is an accident of administration, it is not of the essence of the duty of excise which is attracted by the manufacturer itself. "

164. In Ram *Krishan Ram Nath Agarwal v. Secretary, Municipal Committee, Kamptee, Union of India*[65] a case relating to bidi manufacturer who was required to pay excise duty and octroi, the Supreme Court approved the Federal Court judgment and held that the 'excise duty' was tax on the 'manufacturer' while 'octroi duty' was a 'tax' on the 'entry of goods' within a particular area. Tobacco becomes subject to excise duty when it reaches the stage of manufacture and it does not conflict with a levy on the entry of goods within a certain area. It was observed that "it is wrong to think that two independent impost arising from two different sets of circumstances were not permitted in law".

165. In *Gujarat Ambuja Cement Ltd. v. Union of India*[66] the levy of service tax on carriage of goods by transport operators was challenged as being legislatively beyond the competence of Parliament. This Court held that there is a distinction between the object of tax, the incidence of tax as well as collection machinery. The legislative competence is to be determined with reference to object of the levy. It was held that the service tax and the tax under entry 56, List II are distinct.

166. As already noted, under our Constitution, there is no overlapping in the taxing power. The Constitution gives independent powers of taxation to the Union and the States. The taxing power of the Union and of the States are mutually exclusive. This avoids the difficulties which have arisen under other Federal Constitutions as rightly observed in *Hoechst Pharmaceuticals v. State of Bihar*[67] *and State of West Bengal v. Kesoram Industries*[68]

167. The other contention of the appellants is that the doctrine of 'Unbroken Package' should be applied in the context of entry 83, List I as was initially applied by US courts. Doctrine of 'Unbroken Package' postulates that import of goods continues even after crossing customs barrier until the package imported is broken up at the importer's destination and the goods are taken out. This argument was pressed upon mainly to save the foreign goods from suffering entry tax at the instance of State authorities. The

appellants contended that no entry tax can be levied under entry 52, List II by the State authorities before the package is broken.

168. Such a contention does not find force in the light of the fact that doctrine of 'Unbroken Package' has not only been discredited by Indian Courts, but also by the American Courts. In the American context, reference can be made to Prof. Tribe on American Constitutional Law States, in which the learned Professor has criticized the doctrine of 'Unbroken Package' in the following words:

> "in the dormant commerce clause context, the court long ago disparaged the 'unbroken-package doctrine as applied to interstate commerce as more artificial than sound' and the court has concluded that taxes imposed on goods while in transit through the taxing state are in effect potentially repeatable taxes on interstate commerce itself and are thus barred by the commerce clause. But non-discriminatory taxes imposed on goods prior to their movement into interstate transit, or subsequent to the completion of such transit, are taxes incapable of multiple application and are thus sufficiently local to survive jurisdiction scrutiny."
>
> [Page. 1162-1163]

169. Learned counsel on behalf of the States rightly contended that the 'original package doctrine' or 'unbroken package doctrine' as propounded in Brown v. State of Maryland by Chief Justice Marshall has been expressly disapproved by Indian courts as well. In this regard, reliance has been placed upon *Province of Madras v. Boddu Paidanna & Sons*[69] *State of Bombay v. F.N. Balsara (CB)*[70]*; State of Travancore-Cochin v. Shanmugha Vilas Cashew Nut Factory*[71]

170. In *Gramophone Company of India Ltd. v. Birendra Bahadur Pandey*[72]*,* this Court while interpreting the word "import' in Section 53 of the Copyright Act, 1957, discredited the 'Doctrine of Unbroken/original Package' in the following terms:

> "37. The Calcutta High Court thought that goods may be said to be imported into the country only if there is an incorporation or mixing up of the goods imported with the mass of the property in the local area. In other words the High Court relied on the 'original package doctrine' as enunciated by the American Court. Reliance was placed by the High Court upon the decision of this Court in the Central India Spinning and Weaving and Manufacturing Co. Ltd. The Empress Mills, Nagpur v. Municipal Committee, Wardha [1958]1SCR1102 . That was a case which arose under the C.P. and Berar Municipalities Act and the question was whether the power to impose 'a terminal tax on goods or animals imported into or exported from the limits of a municipality' included the right to levy tax on goods which 'were neither loaded or unloaded at Wardha but were merely carried across through the municipal area'. This Court said that it did not. The word 'import', it was thought meant not merely the bringing into but comprised something more, that is 'incorporating and mixing up of the goods with the mass of the property in local area', thus accepting the enunciation of the 'Original Package Doctrine' by Chief Justice Marshall in Brown v. State of Maryland 6 L.

> Ed. 78. Another reason given by the learned Judges to arrive at the conclusion that they did, was that the very levy was a 'terminal tax' and, therefore the words 'import and export', in the given context, had something to do with the idea of a terminus and not an intermediate stage of a journey. We are afraid the case is really not of any guidance to us since in the context of a 'terminal tax' the words 'imported and exported' could be construed in no other manner than was done by the Court. We must however say that the 'original package doctrine' as enunciated by Chief Justice Marshall on which reliance was placed was expressly disapproved first by the Federal Court in the Province of Madras v. Boddu Paidanna:1942 FCR 90 and again by the Supreme Court in State of Bombay v. F.N. Balsara,. Apparently these decisions were not brought to the notice of the Court which decided the case of Central India Spinning and Weaving and Manufacturing Co. Ltd., The Empress Mills, Nagpur v. Municipal Committee, Wardha. So we derive no help from this case. As we said, we prefer to interpret the word 'import' as it is found in the Copyright Act rather than search for its meaning by referring to other statutes where it has been used. ”

171. Chapter VIII of Customs Act deals with goods in Transit. Section 54 deals with trans-shipment of goods without payment of duty upon presentation of bill of trans-shipment. The inland container depot and land custom station are creatures of Statute. They are not determinative of the taxable event for imposition of custom duty on imports. Many of the provisions are facilitative and/or intended for purposes of valuation and fixation of rates. The crucial aspect is that according to entry 83, List I as well as the Customs Act, 1962 the taxable event is ‘import or ‘bringing of the goods into India’ and it is distinct from the taxable event of entry 52, List II.

172. The assessees contended that a factory unit may have a warehouse where goods are deposited and are kept under a bond which may even permit sale or manufacture. It was even contended that the warehouse itself may be in the same local area, illustratively in Delhi/Mumbai.

173. Sections 2(43), 2(44) and 2(45) deal with warehouse, warehoused goods and warehousing station. Section 9 requires the Board to issue a Notification in the Official Gazette declaring places to be warehousing stations at which alone public warehouses may be appointed and private warehouses may be licensed. The public warehouses are appointed under Section 57 and private warehouses are licensed under Section 58.

174. On behalf of the States, it was submitted that there is no submission by any of the assessees that there is a warehousing station in their factory units or in the local area where they are located or that there is any public warehouse or private warehouse so located. Our attention was drawn to SLPs pertaining to Indian Oil Corporation, Vedanta and NALCO to contend that the assessees have not produced any evidence nor is there any pleading that the Bill of Entry is filed in the factory units or in a land custom station which is located in the same local area as the assessees’ unit. Hence, it is submitted that the warehouse and warehouse bond based contentions have been advanced without any basis in pleadings and facts.

175. A comparison of Sections 58 and 57 shows that a licensed private warehouse is different from a public warehouse. Section 58 deploys the expression "dutiable goods imported by or on behalf of the licensee, or any other imported goods". Similar expression is not used in Section 57 with respect to public warehouses wherein dutiable goods may be deposited. It is clear that the goods deposited in private warehouses are considered to be goods which have already been imported. Further, 'warehousing bond' is dealt with in Section 59 which is issued where the goods have been entered for warehousing and after assessment of the duty, the bond is executed for a sum twice the amount of the duty assessed. When the requirements in Section 59 are complied with then permission to deposit the goods in warehouse is granted. This indicates that both in public warehouses and private warehouses the deposits are permitted only for goods which are already imported. Stringent provision is made in Section 59(2) to pay all duties or interest on or before the date of demand. Under Section 62, the proper custom officer exercises control over all the warehoused goods and he may cause any warehouse to be locked. The owner of the goods can with the sanction of the proper officer deal with the goods, show the goods for sale and even carry on any manufacturing process or other operations in the warehouse in relation to such goods.

176. Such warehousing or warehousing bond cannot prevent the levy of entry tax, especially where warehouse is established in a factory unit. On the basis of the law laid down above, I hold that the taxable events under entry 83, List I and entry 52, List II are distinct; any movement of the imported goods to the warehouse in the factory unit would not prevent the State from levying and collecting entry tax when such goods enter a local area of the State for consumption, use or sale therein._

177. Summarily, the conclusion on question No.4 is as under:-

> "• Entry tax with reference to entry 52, List II of Seventh Schedule is not violative of Art. 301 subject to the levy being non-discriminatory i.e. passing the muster of Art. 304(a). A levy sustainable under Art. 304(a), being non-discriminatory would ipso facto be out of the purview of Art. 301.
>
> • When the entry tax is levied by the Entry Tax Act enacted by the State Legislature, the term 'a local area' contemplated by Entry 52 may cover the 'Whole State' or 'a local area' as notified in the legislation. I agree with the view taken in Bihar Chamber of Commerce that from the point of view of entry tax that the State is a compendium of local areas and where the local areas contemplated by the Act cover the entire State, the difference between the State and 'a local area' practically disappears.
>
> • Articles 304(a) and 304(b) are to be read disjunctively; both apply to different subject matters; while Art. 304(a) deals with tax, Art. 304(b) deals only with non-fiscal matters.
> Conclusions on the incidental questions arising under Question No.4:-
>
> • Where there is equivalence in terms of tax treatment between the locally

produced goods and the ones imported from other States, levy of entry tax on the goods imported from other States when there is no such levy on the locally produced goods is not discriminatory.

• Every differentiation is not discrimination. Any difference in the rate of tax on goods locally manufactured and those imported, such difference not being discriminatory does not fall foul under Art.304(a). Any incentive/benefits of concession in the rate of tax given to the local manufacturers/producers in order to encourage the local manufacturers/production in the State cannot be said to be discriminatory. Digvijay and Video Electronics have laid down the correct law. Mahavir Oil Mills is not a correct view.

• Levy of entry tax on the goods imported from the other States is not discriminatory merely on the ground that there are no similar goods manufactured or produced within the taxing State. The law laid down in Kalyani Stores is not a good law.

• Levy of entry tax on the goods imported from outside India which enter into local area for consumption, use or sale therein is within the legislative competence of the State.

QUESTION NO. 2: IF ANSWER TO QUESTION NO.1 IS IN THE AFFIRMATIVE, CAN A TAX WHICH IS COMPENSATORY IN NATURE ALSO FALL FOUL OF ARTICLE 301 OF THE CONSTITUTION OF INDIA?

QUESTION NO. 3: WHAT ARE THE TESTS FOR DETERMINING WHETHER THE TAX OR LEVY IS COMPENSATORY IN NATURE?

178. The concept of 'compensatory tax' is a judicially evolved concept. Majority in Atiabari held that taxes may and do amount to restrictions and hence tax legislation is subject to scrutiny under Art. 301. In Atiabari, the test of "direct and immediate effect on trade, commerce and intercourse" was evolved. The majority in Atiabari had thus completely read down State's taxing power under entry 52, List II thereby holding that State's legislative power is subject to the freedom clause in Art. 301. This had an adverse effect on the legislative power of the State to levy tax and its financial autonomy.

179. In Automobile, while the Supreme Court affirmed the views of Atiabari, compensatory taxes were carved out as an exception to Art. 301. In Automobile, this Court evolved the concept of compensatory taxes and held that "regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Article 301". Compensatory taxes were held to be ones which did not hinder the freedom of trade, commerce and intercourse, instead facilitated the same. Further, the Court laid down a "working test" to ascertain whether a tax is compensatory or not in the following terms:-

"27.... It seems to us that a working test for deciding whether a tax is

compensatory or not is to enquire whether the trades 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. It would be impossible to judge the compensatory nature of a tax by a meticulous test, and in the nature of things that cannot be done."

180. In Automobile, the Bench negating the requirement of setting up a separate fund for the taxes collected in the name of compensatory tax, held that the State need not maintain a separate fund for the compensatory taxes so collected from the traders enjoying the benefit of the services provided by the State; rather it is sufficient if the State provides certain facilities for better conduct of traders' business. This Court held as under:-

> "28. Nor do we think that it will make any difference that the money collected from the tax is not put into a separate fund so long as facilities for the trades people who pay the tax are provided and the expenses incurred in providing them are borne by the State out of
> whatever source it may be..."

Having observed so, in Automobile itself, this Court had ruled out the element of quid pro quo from the ambit of compensatory tax. While stressing on the need for ensuring that the assessees are not 'paying much more than what is required for providing the facilities', the Court merely intended to prohibit levy of an exorbitant tax. It was nowhere intended by the Court to authorise levy of 'fee' in the name of 'compensatory tax'.

181. In various cases, this Court has repeatedly held that regulatory measures like licensing or price control or compensatory measures cannot be treated as violative of freedom of trade, commerce and intercourse within the territory of India. While upholding the enhancement of the motor vehicles tax, in G.K. Krishnan v. State of Tamil Nadu (1975) 1 SCC 375, this Court held that a compensatory tax is not a restriction upon the movement part of trade and commerce. Neither should the tax go beyond a proper recompense to the State for the actual use made of the physical facilities provided in the shape of a road nor it is necessary that there should be a separate fund or express allocation of money for the maintenance of roads to prove the compensatory purpose, when such purpose is proved by alternative evidence.

182. The decision in Krishnan's case was reiterated in *International Tourists Corporation and Ors. v. State of Haryana and Ors*[73]. in which levy of tax on passengers and goods under The Punjab Passengers and Goods Taxation Act, 1952 and similar other enactments of other States were under challenge. State of Haryana levied a tax on transporters plying motor vehicles between Delhi and Jammu and Kashmir. The transporters would use national highway, pass through Haryana, without picking up or setting down passengers in the State. Since, the responsibility to construct and maintain the highways is with the National Highways Authority of India, it was contended by the transporters that the tax could hardly be regarded as compensatory. But the Court rejected this contention and held that if the taxes were to be proportionate to the expenditure on regulation and service, it would not be a tax but a fee. It was pointed out that in the case of a fee, it may be possible to precisely identify and measure the

benefits received from the Government and in the case of regulatory and compensatory tax, it would be well-nigh impossible to identify and measure the benefits received and the expenditure incurred and to levy the tax in accordance with such benefits. It was held as under:-

> "9. While in the case of a fee it may be possible to precisely identify and measure the benefits received from the Government and levy the fee according to the benefits received and the expenditure incurred, in the case of a regulatory and compensatory tax it would ordinarily be wellnigh impossible to identify and measure, with any exactitude, the benefits received and the expenditure incurred and levy the tax according to the benefits received and the expenditure incurred. What is necessary to uphold a regulatory and compensatory tax is the existence of a specific, identifiable object behind the levy and a nexus between the subject and the object of the levy. If the object behind the levy is identifiable and if there is sufficient nexus between the subject and the object of the levy, it is not necessary that the money realised by the levy should be put into a separate fund or that the levy should be proportionate to the expenditure. There can be no bar to an intermingling of the revenue realised from regulatory and compensatory taxes and from other taxes of a general nature nor can there be any objection to more or less expenditure being incurred on the object behind the compensatory and regulatory levy than the realisation from the levy."
>
> [Emphasis added]

183. In *M/s. Bhagatram Rajeevkumar v. Commissioner of Sales Tax, M.P. and Ors*[74]. it was held that even if there is some link or some connection between the tax and the facilities extended to the trade directly or indirectly the levy cannot be challenged as invalid.

184. The same dictum was followed in *State of Bihar and Ors. v. Bihar Chamber of Commerce and Ors*[75]., wherein this Court considered the challenge to a legislation in which the State of Bihar levied entry tax on the goods entering into a local area for consumption, use or sale therein. The Act was challenged as violative of Art.301 of the Constitution. After referring to Bhagatram, it was held as under:-

> "18. In this connection, it is necessary to notice a few decisions brought to our notice. In Bhagatram Rajeevkumar (1995) Suppl. 1 SCC 673, a three-judge Bench of this Court has rejected the argument that to be compensatory, the tax must facilitate the trade. The reason is obvious: if a measure facilitates the trade, it would not be a restriction on trade but an encouragement to it. It was observed: [SCC Page 678, Para 8]
>
> ".The submission of Shri Ashok Sen, learned Senior Counsel that compensation is that which facilitates the trade only does not appear to be sound. The concept of compensatory nature of tax has been widened and if there is substantial or even some link between the tax and the facilities extended to such dealers directly or indirectly the levy cannot be impugned as invalid. The stand of the

State that the revenue earned is being made over to the local bodies to compensate them for the loss caused, makes the impost compensatory in nature, as augmentation of their finance would enable them to provide municipal services more efficiently, which would help or ease free flow of trade and commerce, because of which the impost has to be regarded as compensatory in nature, in view of what has been stated in the aforesaid decisions, more particularly in Hansa Corpn. Case (1980) 4 SCC 697".

[Emphasis supplied]

185. The Constitution Bench in Jindal Stainless Ltd. (2) after placing reliance on Automobile concluded that there is difference between a taxing Statute whose purpose is collection of revenue, and a taxing Statute whose purpose is regulation. The Court formulated a working test to determine whether the impugned law is a product of the exercise of regulatory power or taxing power: "If the impugned law seeks to control the conditions under which an activity like trade is to take place then such law is regulatory". The Bench concluded that the only way to reconcile a compensatory tax Statute that chooses movement of trade and commerce as a criterion and in effect impedes it, is by holding it as regulatory and, therefore, outside the scope of Articles 301, 302 & 304.

"38.... If the impugned law seeks to control the conditions under which an activity like trade is to take place then such law is regulatory. Payment for regulation is different from payment for revenue. If the impugned taxing or non-taxing law chooses an activity, say, movement of trade and commerce as the criterion of its operation and if the effect of the operation of such a law is to impede the activity, then the law is a restriction under Article 301. However, if the law enacted is to enforce discipline or conduct under which the trade has to perform or if the payment is for regulation of conditions or incidents of trade or manufacture then the levy is regulatory. This is the way of reconciling the concept of compensatory tax with the scheme of Articles 301, 302 and 304. ..."

The Bench further held:

"45. To sum up, the basis of every levy is the controlling factor. In the case of "a tax", the levy is a part of common burden based on the principle of ability or capacity to pay. In the case of "a fee", the basis is the special benefit to the payer (individual as such) based on the principle of equivalence. When the tax is imposed as a part of regulation or as a part of regulatory measure, its basis shifts from the concept of "burden" to the concept of measurable/ quantifiable benefit and then it becomes "a compensatory tax" and its payment is then not for revenue but as reimbursement/ recompense to the service/facility provider. It is then a tax on recompense. Compensatory tax is by nature hybrid but it is more closer to fees than to tax as both fees and compensatory taxes are based on the principle of equivalence and on the basis of reimbursement/recompense. If the impugned law chooses an activity like trade and commerce as the criterion of its operation and if the effect of the operation of the enactment is to impede trade

and commerce then Article 301 is violated.

46. Burden on the State: Applying the above tests/parameters, whenever a law is impugned as violative of Article 301 of the Constitution, the Court has to see whether the impugned enactment facially or patently indicates quantifiable data on the basis of which the compensatory tax is sought to be levied. The Act must facially indicate the benefit which is quantifiable or measurable. It must broadly indicate proportionality to the quantifiable benefit. If the provisions are ambiguous or even if the Act does not indicate facially the quantifiable benefit, the burden will be on the State as a service/facility provider to show by placing the material before the Court, that the payment of compensatory tax is a reimbursement/recompense for the quantifiable/measurable benefit provided or to be provided to its payer(s). As soon as it is shown that the Act invades freedom of trade it is necessary to enquire whether the State has proved that the restrictions imposed by it by way of taxation are reasonable and in public interest within the meaning of Article 304(b) [see para 35 (of AIR) of the decision in Khyerbari Tea Co. Ltd. and Anr. v. State of Assam].'' For compensatory tax, Jindal Stainless Ltd. (2) thus ingrained the tests of (i) facial declaration; and (ii) proportionality to the quantifiable benefits provided to its payers, as an essential element. It was held that compensatory taxes like fees always have to be proportionate to the benefits and the decisions rendered in Bhagatram and Bihar Chamber of Commerce were declared bad in law.

186. Until Jindal Stainless Ltd. (2) compensatory taxes were dealt as taxes and only Jindal Stainless Ltd. (2) equated compensatory tax to 'a fee' and held that compensatory tax is based on the principle of "pay for the value" and that it is a sub-class of 'fee'. It was further held that compensatory tax is a recompense/reimbursement. The distinction between a 'tax' and a 'fee' lies primarily in the fact that a 'tax' is levied as a part of common burden, while a 'fee' is for payment of a specific benefit or privilege rendered by some governmental agency. The distinction between 'tax' and 'fee' has been elucidated in Gujarat Ambuja Exports Limited and Another v. State of Uttarakhand and Others (2016) 3 SCC 601 as under:

"..it is necessary to consider the difference between the concept of tax and that of a fee. The neat and terse definition of tax which has been given by Latham, C.J., in Matthews v. Chicory Marketing Board (1938) 60 C.L.R. 263 is often cited as a classic on this subject. "A tax", said Latham, C.J., "is a compulsory exaction of money by public authority for public purposes enforceable by law, and is not payment for serviced rendered". In bringing out the essential features of a tax this definition also assists in distinguishing a tax from a fee. It is true that between a tax and a fee there is no generic difference. Both are compulsory exactions of money by public authorities; but whereas a tax is imposed for public purposes and is not, and need not, be supported by any consideration of service rendered in return, a fee is levied essentially for services rendered and as such there is an element of quid pro quo between the person who pays the fee and the public authority which imposes it....In regard to fees there is, and must always be, co-relation between the fee collected and the service intended to be rendered..The distinction between a tax and a fee is, however, important, and it is recognized by

the Constitution. Several Etnries in the Three Lists empower the appropriate Legislatures to levy taxes; but apart from the power to levy taxes thus conferred each List specifically refers to the power to levy fees in respect of any of the matters covered in the said List excluding of course the fees taken in any Court."

The same view was reiterated in *State of Tamil Nadu v. TVL South Indian Sugar Mills Association*[76] *Krishi Upaj Mandi Samiti and Others v. Orient Paper & Industries Ltd*[77]*. and Krishna Das v. Town Area Committee, Chirgaon*[78]

187. It must be reiterated that all the taxes are intended for public purpose and are levied in public interest. Levy of tax is not to fill the State coffers but to perform various functions including public welfare for which said funds are required. Taxation is not a profit-making exercise for the States; as stated earlier, the States perform several functions for which they require funds and have the power to levy tax to raise revenues and thus virtually all taxes are monies paid for services or facilities provided by the State. Art. 266(1) provides that all revenue including that from taxes received by a State Government shall form one consolidated fund—the Consolidated Fund of the State. This fund is a reservoir and resources placed in it are a part of the whole. All revenue is subsumed in it and cannot be delineated. The Consolidated Fund of a State is a single unified account for the State and withdrawal of money from the same is protected by the requirement of passing an Appropriation Act. Further, Art. 266(3) by stating that 'no money out of any Consolidated Fund shall be appropriated except in accordance with law - for the purposes and in the manner provided in the Constitution' provides another safeguard in lieu of ensuring legitimate use of public money. The manner of appropriation of money collected in the Consolidated Fund of the State falls under Part VI, Chapter III, ranging from Articles 202 to 206 of the Constitution. There are sufficient constitutional safeguards for the appropriation of money collected in Consolidated Fund. The revenue generated by the States in the form of entry tax has to necessarily form part of this Fund, and once it so subsumed, States cannot be asked to show a 'proximate quid pro quo' by furnishing 'quantifiable data1 as to their expenditure. It may not be possible for the States to show with mathematical precision a direct link between the expenditure incurred in individual cases and the corresponding levy imposed.

188. I hold that the entry tax levied by various States, falling within the domain of entry 52, List II, is a tax simpliciter, even though by nomenclature it is termed as a 'compensatory tax'. Subject to passing the muster of Art. 304(a), entry tax levied by the States under entry 52, List II even though termed as compensatory tax does not fall foul of Art. 301. The ratio laid down in Jindal Stainless Ltd. (2) equating compensatory taxes to fee had wide ramifications. Some High Courts viz., Orissa, Chhattisgarh and Madhya Pradesh upheld the levy of entry tax as compensatory. Many other High Courts struck down the levy applying the test laid down in Jindal Stainless Ltd. (2). In those cases where the levy was struck down, High Courts held that the State could not show what were the benefits provided to the traders who imported goods from outside the States to recompense the tax payer.

189. I disagree with the narrow approach in Jindal Stainless Ltd. (2) equating compensatory taxes to 'fee' and mandating the States to prove 'proximate quid pro quo'

by ‘quantifiable data approach’. Since now we have held that taxes are outside the purview of Art. 301, taxes in the name of ‘compensatory taxes’ are also outside the purview of Art. 301. To uphold a regulatory or compensatory tax, comprehensive parameters cannot be laid down as they may vary depending upon the nature of the levy. Automobile case itself has laid down parameters of compensatory taxes (Das J. at Pages 536-537). It is not necessary that the money so collected should be put into a separate fund or that the levy should be proportionate to the expenditure.

190. Insofar as levy of entry tax is concerned, enactments of some States facially declare that they are compensatory. The compensatory tax so levied is subsumed in the Consolidated Fund of the State. Once there is intermingling in the Fund and money is spent for public purposes of development of various local areas like construction, maintenance of roads and bridges, and for other amenities which facilitate trade, there will always be a link between the liability of the tax borne by the traders and benefits enjoyed by them either directly or indirectly.

191. To summarise the conclusions on question Nos. 2 and 3:-

• In so far as compensatory taxes are concerned in the light of the conclusion on question No.1, I hold that the nomenclature of ‘compensatory’ ascribed to the taxes levied by the State Government under Entry 52, List II pursuant to Automobile is
unwarranted. The concept of compensatory tax was evolved fifty years back through judicial pronouncements. It has withstood the test of time and thus, any subsequent judicial pronouncement like the present one should not prejudice the interest of the parties involved. The State Governments should not suffer any loss of revenue solely because of judicial interpretations and innovations in Automobile and the cases
subsequent to it.

• Subject to passing the muster of Art. 304(a), entry tax levied by the States under entry 52, List II even though termed as compensatory tax does not fall foul of Art. 301. It is not necessary that the money realized by the levy should be put into a separate Fund or that the levy should be proportionate to the expenditure. There is no bar to subsumption of the revenue realized from regulatory/compensatory taxes into the Consolidated Fund of the State as they are no different from other taxes of a general nature. Moreover, the quantum of expenditure incurred in achieving the object behind a compensatory levy cannot be inquired into.

• Jindal Stainless Ltd. (2) & Anr. v. State of Haryana & Ors. (2006) 7 SCC 241 is not a correct view in adopting quantifiable data approach; for a tax, there is no requirement of proximate quid pro quo and Jindal Stainless Ltd. (2) is overruled. The view taken in Bhagatram and Bihar Chamber of Commerce is correct as the same is in harmony with the original design of compensatory tax laid down in Automobile.

REFUND AND UNJUST ENRICHMENT:-

192. Lastly, it is necessary to consider an important issue raised by the assessees on the payment of tax/refund of tax in case the validity of the legislations is upheld or otherwise as the case may be. It has come on record that many Entry Tax legislations of the State are enacted pursuant to Bhagatram and Bihar Chamber of Commerce. But Jindal Stainless Ltd. (2) which we have now over-ruled, has led to a scenario of discordant judicial pronouncements, whereby some High Courts have struck down the impugned legislation as being non-compensatory, while the others have upheld the laws declaring them compensatory. In some States, the High Courts have passed interim orders directing petitioners to pay 33% of the demand and in some cases 50% of the demand. When the matters were admitted by the Court, interim orders were passed directing the assessees to pay 50% of the demand. But, this Court cannot lose sight of the fact that assessees have not pleaded and produced evidence to establish that they have not passed on the tax burdens to the consumers. In absence of such a submission, the normal presumption is that they have passed on the tax burden. Had they contended otherwise, burden would have been on them to allege and establish the same. In the absence of any such allegation and proof, the claim of refund is not called for.

193. Learned Senior Counsel Mr. Giri has argued that the payment effected under the Entry Tax Act can be legitimately taken into account for the purpose of fixing the price of goods that can be collected by the same person as a dealer under the Sales Tax Act, just as in the case of Sales Tax. It is thus submitted that the burden suffered by the goods in question have actually been passed on to the consumer and that at any rate the assesses would not be entitled to any refund.

194. Learned Senior Counsel Mr. Rakesh Dwivedi has submitted that the doctrine of unjust enrichment is invoked in cases where the States have acted on the basis of earlier Supreme Court judgments or where the laws have been operating for a very long time and the rights and liabilities of the people have crystallised on the basis of such laws, and where the laws are subsequently declared ultra vires and previous judgments are over-ruled. It is further submitted that in such cases, particularly in tax matters, law is declared prospectively and the reason behind such prospective application is to save the taxes which has been already collected. In order to support his contentions, he relied on the decisions of this Court in *Synthetics & Chemicals v. State of U.P*[79]*. Belsund Sugar Co. Ltd. v. State of Bihar*[80]; *Mafatlal Industries Ltd vs Union of India*[81] etc.

195. By catena of judicial pronouncements, this Court has fairly laid down the concept of 'unjust enrichment' in respect of tax laws. The doctrine of ‘unjust enrichment’ is that no person can be allowed to enrich inequitably at the expense of another. A right of recovery/payment under the doctrine of ‘unjust enrichment’ arises where retention of a benefit is considered contrary to justice or against equity. The concept of ‘unjust enrichment’ is applicable for the purpose of grant of refund. The concept provides that if a person pays tax/duty to the Government in terms of the prevailing tax Statutes and passes it on to the consumers and, subsequently, the tax/duty is found not payable, refund cannot be claimed from the Government authorities, as whatever liability he had

incurred has already been recovered. And, if he gets the refund, he would be unjustly enriched.

196. In *Mafatlal Industries Ltd v. Union of India (Supra),* a nine-judge Bench of this Court considered the scope and ambit of the said doctrine in detail. The Court held that Central Excise and Salt Act is a self-contained Code which also provides for determination of claim of refund. The Act was found to have expressly declared that no refund shall be made except in accordance therewith. The Court further held that even in regard to exercise of jurisdiction under Articles 32 and 226, Court would certainly take note of the legislative intent manifested in the provision in the Act. The Court further dealt extensively with the scope of refund in a case where the burden of tax has been passed on to the consumers. An excerpt from the majority view reads as under:

> " 108. A claim for refund, whether made under the provisions of the Act as contemplated in proposition... (i) above or in a suit or writ petition in the situations contemplated by proposition (ii) above, can succeed only if the petitioner/plaintiff alleges an d establishes that he has not passed on the burden of duty to another person/other persons. His refund claim shall be allowed/decreed only when he establishes that he has not passed on the burden of the duty or the extent he has not so passed on, as the case may be. Whether the claim for restitution is treated as a constitutional imperative or as a statutory requirement, it is neither an absolute right nor an unconditional obligation but is subject to the above requirement, as explained in the body of t he judgment. Where the burden of the duty has been passed on, the claimant cannot say that he has suffered any real loss or prejudice. The real loss or prejudice is suffered in such a case by the person who has ultimately borne the burden and it is only that person who can legitimately claim its refund. But where such person does not come forward or where it is not possible to refund the amount to him for one or the other reason, it is just and appropriate that amount is retained by the State, that is, by the people. There is no immorality or impropriety involved in such a proposition. The doctrine of unjust enrichment is a just and salutary doctrine. No person can seek to collect the duty from both ends. In other words, he cannot collect the duty from the purchaser at one end and also collect the same duty from the State on the ground that it has been collected from him contrary to law. The power of the court is not meant to be exercised for unjustly enriching a person. The doctrine of unjust enrichment is, however, inapplicable to the State. State represents the people of the country. No one can speak of the people being unjustly enriched. "

197. In *Godfrey Philips India Ltd. v. State of U.P.*[82] the constitutional validity of the Uttar Pradesh Tax on Luxuries Act, 1995 as also other State Acts was challenged inter alia on the ground of legislative competence of the State Legislatures. The Court allowed the petition and held that the State Legislatures were not competent to impose luxury tax on tobacco and tobacco products and the Acts were declared ultra vires and unconstitutional. In the intervening period, however, tax was collected by the appellants from consumers and also paid to the State Governments. The Court held as under:

> "94. It was stated on behalf of the State Governments that after obtaining interim

orders from this Court against recovery of luxury tax, the appellants continued to charge such tax from consumers/customers. It is alleged that they did not pay such tax to respective State Governments. It was, therefore, submitted that if the appellants are allowed to retain the amounts collected by them towards luxury tax from consumers, it would amount to "unjust enrichment" by them.

95. In our opinion, the submission is well founded and deserves to be upheld. If the appellants have collected any amount towards luxury tax from consumers/customers after obtaining interim orders from this Court, they will pay the said amounts to the respective State Governments."

From the above decision in Godfrey Philips India Ltd., it is clear that even when the legality of a tax has been challenged successfully, there can be no question of the State tax being retained by the dealer/manufacturer notwithstanding its illegality.

198. It is well-settled that a claim of refund can be allowed only when the claimant establishes that he has not passed on the tax burden to the consumers. No refund can be granted so as to cause windfall gain to any person when he has not suffered the burden of tax. The possibility of the tax burden having been passed on to the consumers by the assessees cannot be ruled out in the present case. Applying the law laid down above to the present case, it emerges that the assessees cannot claim refund irrespective of whether the impugned legislations are declared valid or unconstitutional. Unless the assessees establish that they have not passed on the tax burden to the consumers, they cannot make a claim for refund and unjustly enrich themselves.

199. Summary of the conclusions on Question Nos. 1 to 4 are as under:-

Question No. 1:

Non-discriminatory taxes do not constitute infraction of Art. 301 of the Constitution. With due respect, the view taken in Atiabari and approved in Automobile Transport that taxes do amount to restriction and that freedom of trade, commerce and intercourse cannot be subject to restriction in the form of taxes is not a correct view and are to be over ruled. However, I am agreeing with the theory of compensatory tax evolved in the Automobile case for the reasons indicated hereunder while answering Question Nos. 2 and 3.

Question No.4:-

• Entry tax with reference to entry 52, List II of Seventh Schedule is not violative of Art. 301 subject to the levy being non-discriminatory i.e. passing the muster of Art. 304(a). A levy sustainable under Art. 304(a), being non-discriminatory would ipso facto be out of the purview of Art.

• When the entry tax is levied by the Entry Tax Act enacted by the State Legislature, the term 'a local area' contemplated by Entry 52 may cover the 'Whole State' or 'a local area! as notified in the legislation. I agree with the view taken in Bihar Chamber of Commerce that from the point of view of entry tax that

the State is a compendium of local areas and where the local areas contemplated by the Act cover the entire State, the difference between the State and 'a local area' practically disappears.

• Articles 304(a) and 304(b) are to be read disjunctively; both apply to different subject matters; while Art. 304(a) deals with tax, Art. 304(b) deals only with non-fiscal matters.

• Where there is equivalence in terms of tax treatment between the locally produced goods and the ones imported from other States, levy of entry tax on the goods imported from other States when there is no such levy on the locally produced goods is not discriminatory.

• Every differentiation is not discrimination. Any difference in the rate of tax on goods locally manufactured and those imported, such difference not being discriminatory does not fall foul under Art.304(a). Any incentive/benefits of concession in the rate of tax given to the local manufacturers/producers in order to encourage the local manufacturers/production in the State cannot be said to be discriminatory. Digvijay and Video Electronics have laid down the correct law. Mahavir Oil Mills is not a correct view.

• Levy of entry tax on the goods imported from the other States is not discriminatory merely on the ground that there are no similar goods manufactured or produced within the taxing State. The law laid down in Kalyani Stores is not a good law.

• Levy of entry tax on the goods imported from outside India which enter into local area for consumption, use or sale therein is within the legislative competence of the State.

Question Nos. 2 and 3:-

• In so far as compensatory taxes are concerned in the light of the conclusion on question No.1, I hold that the nomenclature of 'compensatory' ascribed to the taxes levied by the State Government under Entry 52, List II pursuant to Automobile is unwarranted. The concept of compensatory tax was evolved fifty years back through judicial pronouncements. It has withstood the test of time and thus, any subsequent judicial pronouncement like the present one should not prejudice the interest of the parties involved. The States should not suffer any loss of revenue solely because of judicial interpretations and innovations in Automobile and the decisions subsequent to it.

• Subject to passing the muster of Art. 304(a), entry tax levied by the States under entry 52, List II even though termed as compensatory tax does not fall foul of Art. 301. It is not necessary that the money realized by the levy should be put into a separate Fund or that the levy should be proportionate to the expenditure. There is no bar to subsumption of the revenue realized from

regulatory/compensatory taxes into the Consolidated Fund of the State as they are no different from other taxes of a general nature. Moreover, the quantum of expenditure incurred in achieving the object behind a compensatory levy cannot be inquired into.

• *Jindal Stainless Ltd. (2) & Anr. v. State of Haryana & Ors. (Supra)* is not a correct view in adopting quantifiable data approach; for a tax, there is no requirement of proximate quid pro quo and Jindal Stainless Ltd. (2) is overruled. The view taken in Bhagatram and Bihar Chamber of Commerce is correct as the same is in harmony with the original design of compensatory tax laid down in Automobile.

Unjust Enrichment:

The concept of unjust enrichment is applicable for considering the question of refund. Unless the assessees establish that they have not passed on the tax burden to the consumers, they cannot make a claim for refund and unjustly enrich themselves.

[1](2006) 7 SCC 0241
[2](1995) Suppl. (1) SCC 0673
[3](1996) 9 SCC 0136
[4](2003) 8 SCC 0060
[5](2006) 7 SCC 0241
[6](2006) 7 SCC 0271
[7](2009) 7 SCC 0339
[8](2010) 4 SCC 0595
[9]AIR 1950 SC 0027
[10](2011) 9 SCC 0001
[11] (2012) 7 SCC 0106
[12](2011) 9 SCC 0001
[13](1973) 4 SCC 0225
[14](1948) [All E.R. 0995, 998
[15](2002) 8 SCC 0481
[16](1963) 1 SCR 0220
[17](2004) 10 SCC 0201
[18](1992) Suppl. (1) SCC 0074
[19](1991) 4 SCC 0139
[20](1992) 2 SCC 0411
[21](2000) 5 SCC 0694
[22](1989) 3 SCC 0698
[23]AIR 1955 SC 0540
[24](1985) 1 SCC 0641
[25](1988) 1 SCC 0206
[26](1994) 2 SCC 0434
[27]AIR 1966 SC 0619
[28](1954) SCR 1005
[29](1995) 6 SCC 0651
[30](2004) 5 SCC 0155
[31](1989) 3 SCC 0634
[32](1989) 3 SCC 0677
[33]1961 SCR 0809
[34](1963) 1 SCR 0491
[35](1949) 79 CLR 497:[1950] AC 0235
[36](1927) 40 CLR 0001
[37](1932) A C. 0542
[38](1936) A.C. 578
[39](1988) 78 ALR 0042
[40](2008) 244 ALR 0032
[41]329 U.S. 249 (1946)
[42](1977) USSC 0054: (1977) 430 US 274
[43](2013) 15 SCC 0677
[44]AIR 1968 SC 1450
[45](1987) 3 SCC 0208
[46]AIR 1950 SC 0027
[48](2002) 8 SCC 0182
[49](1963) SCR Suppl. (2) 216
[50](1961) 3 SCR 0242
[51](1995) 3 SCC 0351
[52] (1988) 1 SCC 0743
[53](1988) 2 SCC 0568
[54] (1997) 2 SCC 0697
[55](1990) 3 SCC 087
[56](1952) SCR 0435
[57](1996) 11 SCC 0039
[58](2000) 1 SCC 0688
[59]AIR 1963 SC 0928
[60](1968) 3 SCR 0829
[61](1966) 1 SCR 0865
[62](1969) 2 SCC 0363
[63]AIR 1942 FC 0033 = 1942 FCR 90
[64]AIR 1945 PC 0098 = 58 LW 228
[65]AIR 1950 SC 0011
[66](2005) 4 SCC 0214
[67](1983) 4 SCC 045
[68](2004) 10 SCC 0201
[69]AIR 1942 FC 0033 = 1942 FCR 90
[70]AIR 1951 SC 0318
[71](1954) SCR 0053
[72](1984) 2 SCC 0534
[74] (1995) Supp (1) SCC
[76](2015) 13 SCC 0748
[77](1995) 1 SCC 0655
[78](1990) 3 SCC 0645
[79](1990) 1 SCC 0109
[80](1999) 9 SCC 0620
[81](1997) 5 SCC 0536
[82](2005) 2 SCC 0515
[73](1981) 2 SCC 318
[75](1996) 9 SCC 136

JUDGMENT

Dr.D.Y.Chandrachud,J.,

This judgment is structured to consist of the following parts :
A Introduction;

B Part XIII of the Constitution : text and context;

C Constitutional history as a guide;

D The trend-setting decisions : Atiabari and Automobile Transport;

D1 Atiabari : Article 301 and taxation
D.2 Automobile Transport

E Compensatory taxes;

E.1 Original understanding

E.2 Khyerbari

E.3 Subsequent applications

E.4 The breaking point

E.5 Doctrinal concerns and inconsistencies

F The content of freedom : goods, services, persons and capital;

G Taxation and Federalism;

H Taxing powers;

H.1 Article 245 and constitutional limitations

H.2 Sovereignty and constitutional limitations

H.3 Part XIII and taxation

H.3.1 All taxes are not impediments

H.3.2 Articles 302, 303 and 304

H.3.3 Construing Article 304

H.3.4 Conjunctive or disjunctive: 'may'; 'and'

H. 3.5 Article 304(a) not the universe of taxation

I Tax legislation : Judicial review and Part XIII;

I.1 Taxation and Part XII

I.2 The standard of judicial review

I.3 Limitations of Sinha CJ's view in Atiabari

I.4 Presidential Sanction : the proviso to Article 304(b)

J Article 304(a) : the principle of non-discrimination;

J.1 Precedent - 1963 to 1980

J.2 Exemptions and incentives : Video Electronics and Mahavir

J.3 Article 304(a) and reasonable classification

J.3.1 Formal and substantive equality

J.4 Production and manufacture within the home state

K Entry tax;

K.1 Octrois and terminal taxes

K.2 Entry taxes and Article 304(a)

K.3 Meaning of 'Local area'

K.4 Severability

K.5 Equalising tax burdens

K.6 Entry tax and imported goods

M Direct and inevitable effect test;

N Conclusion.

A Introduction

1. References to Benches of nine Judges, or at any rate decisions by nine, are a comparative rarity. Despite a prolific tradition of precedent in our judicial institutions, there have been only eight reported decisions by a Bench of nine Judges since the adoption of the *Constitution*[84]**.** The present reference traverses an area of constitutional law which is fraught with unresolved complexity. The draft-persons of the Constitution perceived the freedom of trade, commerce and intercourse to lie at the heart of the economic unity of the nation. They were keenly aware that parochial pressures emanating from within the states could pose real challenges to the creation of a pan-India common market. The dangers of protectionist policies within the states had nonetheless to be balanced with the need to meet the aspirations for development of all areas within the country. Levels of economic attainment in the provinces and erstwhile princely states were far from uniform at the eve of Independence. Many of the erstwhile princely states had concerns about ceding their control over trade and commerce to a national entity. Part XIII was formulated in this background. It represents the balancing vision of the framers and seeks to create an equilibrium between free trade and regulation, state and federal control and between provincial autonomy and national interests in an area closely related to economic growth and development.

2. Yet, the semantics of the provisions adopted in framing all of six constitutional articles which comprised Part XIII- Articles 301 to 306 - attracted criticism within the Constituent Assembly. One member complained of several provisions threatening to become a "paradise for lawyers where there will be so many innumerable loopholes that we will be wasting years and years before we could come to the final and correct interpretation of many years later, a distinguished Judge of this court spoke of the "mix up of exception upon exception in the series of articles in Part XIII that a purely textual interpretation may not disclose the true intendment of the *articles* [86]**".** Those remarks continue to be relevant even now. The law in the area of free trade and commerce has remained in a state of flux despite successive decisions by Constitution benches of this court. A similar judicial cri de coeur has found expression in *Australia* [87]*.* That this is so should not seem surprising : this is an area of the Constitution which cuts across major concerns about the federal structure, the states' power to tax and, the relationship between growth, development and free trade.

Each of those concerns has a pointed contemporary relevance with the adoption of the constitutional amendment providing for a Goods and Services Tax. When the hearings began, many of the counsel had reservations on the continued relevance of the reference. With the passage of the one hundred and first constitutional amendment, the distribution of the legislative power to tax goods and services has undergone a significant change. The

[89] Judges decisions : Ahmedabad St. Xaviers College Society v. State of Gujarat (1974) 1 SCC 717; Indra Sawhney v. Union of India 1992 Supp (3) SCC 217; Supreme Court Advocates-on-Record Association v. Union of India (1993) 4 SCC 441; S.R.Bommai v. Union of India (1994) 3 SCC 1; Attorney General of India v. Amratlal Prajivandas (1994) 5 SCC 54; Mafatlal Industries Ltd v. Union of India (1997) 5 SCC 536; Special Reference No. 1 of 1998 (1998) 7 SCC 739; I. R. Coelho versus State of Tamil Nadu (2007) 2 SCC 1.

[85] P.S. Deshmukh : Constituent Assembly Debates, Vol. IX, pp. 1131; see also: B. Shiva Rao, The Framing of India's Constitution – A study, p. 704 (1978)

[86] Justice S K Das : (1963) 1 SCR 491, Para 10, pg. 520

[87] Cri De Coeur : (i) According to Merriam-Webster: passionate outcry (as of appeal or protest)

(ii) According to Oxford Dictionary: A passionate appeal, complaint or protest

taxing entry for the levy of Entry tax (Entry 52 of List II of the Seventh Schedule), which lies at the core of the dispute in the present reference, stands deleted as part of a constitutional process by which several taxes are being subsumed under the GST. Yet, the reference has to be answered, not the least of the reasons for which is the determination of past liabilities and entitlements. But more fundamentally, the reference raises important issues of constitutional principle about the relationship of the freedom of trade and commerce with the fiscal and regulatory concerns of the states over the need to bring growth and development within. The issues raised have a vital bearing on the intersection of the Constitution with free trade one hand and growth and development on the other.

4. This judgment will explore the socio-economic and political compulsions which led the founding fathers of the Constitution to adopt the guarantee under Article 301. The political backdrop of partition with its attendant social suffering provided a powerful rationale for a constitutional structure which would knit the nation together as a cohesive unit. The instrumentalities of trade and commerce were conceived, in the vision of the draftsmen of the Constitution, as a means for bringing about economic integration. The economic integration of India into a common market was to be achieved by guaranting the freedom of trade throughout the territory of India. Yet, at its birth the new nation comprised of different regions, with disparate social attainments and economic development. They had their own concerns, be they the erstwhile princely states or the states which formed part of British India. Part XIII reflected an attempt by the framers to draw a balance between freedom on one hand and the need to regulate to protect diverse aspects of public interest both of a national and regional character, on the other. The regulatory power under Article 302 would enable the national legislative body to perceive and regulate aspects of public interest of a national character. Within the area of regulation a distribution was envisaged between the Centre and the States to preserve the balance within the newly created federation. The attention that was bestowed to the regulatory requirements of the states in relation to trade and commerce reflected the need for bringing the states on board for producing a viable and acceptable social compact that the constitutional document embodies.

5. Part XIII of the Constitution reflects a consciously crafted constitutional superstructure which looks upon the freedom to trade and to engage in commerce not merely from the perspective of trade and commerce itself, but from a wider national perspective that incorporates both the needs of the nation as reflected in regulatory powers of the centre and the concerns of the federating states to preserve their interests and obligations as well as their commitments to their people.

6. The debates of the Constituent Assembly provide a valuable insight, grounded in history, which helps us in illuminating the meaning and content of the text of Part XIII. History constitutes a seminal value in interpreting the words of the Constitution since the events which were a forerunner to the adoption of the Constitution shed light on the concerns which led to the adoption of the text. Yet, as our contemporary jurisprudence recognises, the text of the Constitution cannot be frozen by the context of history which

produced the language of the text. The concerns that motivated the framers provide a historical context which is an aid to constitutional interpretation. But, it is important to realise that the Constitution as an organic document has to evolve with societal change. The challenges to governance which India has faced over the last seven decades cannot be ignored in giving present meaning to the constitutional text. The words of the Constitution cannot be frozen in their content with reference to the intent of its framers. To succeeding generations lies the task of imparting a meaning that would, while ensuring a sense of continuity, infuse the constitutional document with the ability to meet the challenges of the present and foreseeable future.

7. I have had the privilege of reading the draft of the judgment of the learned and distinguished Chief Justice. My judgment has been necessitated by my inability to agree with some of the crucial issues raised there, especially on its conclusion that taxes (except for discriminatory taxes) can never be restrictions within the meaning of Part XIII. On the aspects on which we agree, I have adduced my own reasons.

B Part XIII of the Constitution : Text and Context

8. Part XIII of the Constitution has more than an abundant share of constitutional intricacies. Despite a judicial discourse of more than five decades, the debate on the true meaning of its provisions continues to bedevil academics, lawyers and judges who have had occasion to visit its provisions.

9. The ambit of Part XIII is trade, commerce and intercourse within the territory of India. *Article 301*[88] mandates that trade, commerce and intercourse throughout the territory of India shall be free, "subject to the other provisions" of Part XIII. The freedom thus conferred is subject to the restrictions that are contemplated in the provisions of Part XIII that follow. The sources of the restrictions, the extent of the restrictions and the limitations or qualifications upon the power to restrict are defined in Part XIII.

10. In framing Article 301, the framers of the Constitution made a deliberate departure from the text of the Australian and US Constitutions. Article 1 Section 8 of the US Constitution confers upon Congress the power "to regulate commerce with foreign nations and among the several states" (besides the Indian tribes). Section 92 of the Australian Constitution stipulates that "on the imposition of uniform duties of customs, trade, commerce and intercourse among the states whether by means of internal carriage or ocean navigation shall be absolutely free". The expression 'absolutely free' occurring in the Australian Constitution was consciously not adopted in the framing of India's Constitution. A simpler expression, "free", was preferred to "absolutely free".

Dr B R Ambedkar while moving the introduction of draft Part XA of the Constitution (corresponding to Part XIII) emphasised the impact of the deletion of the qualification "absolutely" in defining the extent of the freedom. Dr Ambedkar observed that :

[88] *Article 301: Freedom of trade, commerce and intercourse : Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.*

> "I should also like to say that according to the provisions contained in this part, it is not the intention to make trade and commerce absolutely free, that is to say,

deprive both Parliament as well as the States of any power to depart from the fundamental provision that trade and commerce shall be free throughout India."

At a certain level, the expression "absolutely free" adds little by way of substantive content to 'free'. However, in the context of comparative constitutional history, the deletion of the word 'absolute' carried significance. Absolute freedom may carry the meaning that the freedom is not subject to restrictions. The use of the word 'absolute' was liable to give rise to an inference that the freedom was unqualified. The observations of Dr Ambedkar indicate that while trade, commerce and intercourse are to be free, that freedom is not unqualified but that it is subject to the provisions of Part XIII. While conferring the freedom, the Constitution recognises expressly that the freedom which it confers would be subject to the provisions of Part XIII.

12 . The second aspect of Article 301 in which a conscious departure was made from the US and Australian Constitutions is that the freedom of trade, commerce and intercourse extends, in our Constitution, throughout the territory of India and not merely among the states. The expression 'among the states' would cover a movement inter-State or across State boundaries. In discarding the expression "among the states" (which is used in Section 92 of the Australian Constitution) and "among several states" (which is used in Article 1 Section 8 of the US Constitution), Article 301 guarantees a more comprehensive coverage to the freedom to include both inter-State and intra-State trade, commerce and intercourse. 'Throughout the territory of India', means in every part of India. In other words, the freedom that is conferred by Article 301 extends over but is not confined to inter-State movement across State boundaries.

13.

The Constitution, while recognising the freedom of trade, commerce and intercourse throughout the territory of India makes that freedom subject to the provisions of Part XIII. ***Article 302***[89] empowers Parliament to impose restrictions on the freedom of trade, commerce and intercourse between one state and another or within any part of the territory of India. This is subject to qualifications. First, restrictions have to be imposed by law. Second, they must be such as may be required in the public interest. However, the empowerment of Parliament under Article 302 to impose restrictions on the freedom guaranteed by Article 301 is subject to constitutional limitations prescribed in clause 1 of Article 303. Under clause 1 of ***Article 303*** [90], there is an absolute prohibition upon Parliament making any law giving or authorising the giving of preferences to one state over another or making a discrimination between one state and another, by virtue of any entry relating to trade and commerce in any of the lists of the Seventh Schedule. A similar limitation is imposed on the state legislatures. The non-obstante provision in clause 1 of Article 303 is somewhat inapposite in its application to the legislature of a state. In its application to Parliament, the non-obstante provision which operates over Article 302 was intended to impose a constitutional limitation

[89] *Article 302 : Power of Parliament to impose restrictions on trade, commerce and intercourse : Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part or the territory of India as may be required in the public interest.*

upon Parliament while legislating to impose a restriction in the public interest. Since Article 302 applies only to Parliament and not to the state legislatures, the non-obstante

provision contained in Article 303 is to that extent inartistic. Be that it is may, clause 1 of Article 303 imposes a constitutional limitation upon the law making power of Parliament and the state legislatures while enacting a law by virtue of any entry relating to trade and commerce in the lists of the Seventh Schedule. The constitutional limitation prevents the grant of preferences or the making of discrimination between one state and another while enacting a law by virtue of any of the entries relating to trade and commerce in the lists of the Seventh Schedule. However, the constitutional limitation upon the power of Parliament under clause 1 of Article 303 is lifted in clause 2 where Parliament enacts a law for dealing with a situation arising from the scarcity of the goods in any part of the territory of India. The freedom under Article 301 is thus subject to Parliamentary restrictions under Article 302. The power to impose restrictions is subject to the limitations in clause 1 of Article 303. However, those limitations can be relaxed in the situation contemplated by clause 2 of Article 303. The prohibition on the enactment of law which has the effect of granting preferences or making discrimination between states is, in relation to Parliament, lifted by clause 2 when it is necessary to deal with a situation of the scarcity of goods in any part of India.

14. ***Article 304***[91] commences with a non-obstante provision, "notwithstanding anything in Article 301 or Article 303". Under clause (a), a state legislature may by law impose on goods imported from other states, a tax to which similar goods manufactured or produced in that state are subject. This has to be done in a manner that does not discriminate between the goods so imported and goods so manufactured or produced in the state which imposes the tax. Clause (a) of Article 304 subjects the taxing power of a state with reference to goods imported from other states to a constitutional limitation of non-discrimination. The prohibition of non-discrimination is in regard to the tax which is imposed on goods imported from another state. The equality of treatment is with reference to the tax imposed on goods manufactured or produced in the state. The non-obstante provision which refers to Article 301 carries the clear intendment that a tax of the nature within the contemplation of clause (a) of Article 304 would, but for that provision have fallen within the ambit of Article 301. The effect of the non-obstante provision is that notwithstanding Article 301 (which would otherwise bring within its purview a tax of this nature), clause (a) of Article 304 enables the imposition by a state of a tax on imported goods subject to the constitutional limitation of non-discrimination between the goods that are imported into the state with goods that are manufactured or produced within the state. Both clause (1) of Article 303 and clause (a) of Article 304 embody principles of non-discrimination, though with different facets.

15. Clause (1) of Article 303 deals with preferences or discrimination between one state and another. Article 304 (a) deals with a non-discriminatory tax imposed on goods imported into

[91] *Article 304 : Restrictions on trade commerce and intercourse among states : Notwithstanding anything in article 301 or article 303, the Legislature of a State may by law – (a) impose on goods imported from other States [or the Union territories] any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and (b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest: provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature or a State without the previous sanction of the President.*

a state when a similar tax is imposed on goods produced or manufactured in the state.

Article 302 refers to restrictions in general without any qualification as regards the fiscal or non-
fiscal nature of the restrictions. The constitutional limitation imposed by Article 303 on the power to impose a restriction under Article 302 is also not defined with reference to a fiscal or non-fiscal provision. Article 304(a) is a species of restriction namely, a non-discriminatory levy of tax. Clause (b) of Article 304 enables the legislature of a state to impose by law reasonable restrictions as may be required in the public interest on the freedom of trade, commerce or intercourse with or within that state. The expression "with or within that state" indicates that the state legislature in exercise of its power can impose restrictions both in regard to inter-State as well as intra-State trade, commerce and intercourse. The power of the state to do so is, however, conditioned by three limitations : the first is that the restriction must be reasonable; the second is that the restriction should be required in the public interest; and the third which is spelt out in the proviso, is that the Bill or an amendment for the purpose of clause (b) shall not be introduced or moved in the legislature of a state without the previous sanction of the President.

16. A plain construction of the provisions of clause (a) and clause (b) of Article 304 would indicate that clause (a) is not exhaustive of the universe of taxing legislation insofar as the state legislatures are concerned. Clause (a) of Article 304 embodies the principle of non-discrimination and prescribes it as a limitation subject to which a state may by law impose a tax on goods which are imported into the state. Clause (a) lifts the embargo arising from Article 301 on the power of a state to impose a tax on goods imported from other states subject to a condition: the State may impose any tax to which similar goods manufactured or produced in that state are subject. Clause (a), in other words deals only with the taxation of goods which are imported from other states or union territories.

17. Clause (b) of Article 304 refers to reasonable restrictions on the freedom of trade, commerce or intercourse with or within the state. An intra-State restriction is within the purview of clause (b) but not within clause (a). Clauses (a) and (b) are separated by the conjunctive 'and'. The use of the expression 'and' must however be read together with the prefatory part of Article 304. Article 304 provides that the legislature of a state 'may' by law impose a tax on goods imported from other states, subject to the principle of non-discrimination [embodied in clause (a)]. The state legislature may also impose such reasonable restrictions as are required in the public interest [under clause (b)]. Clause (b) is, however, subject to the proviso.

18. The provisions of Part XIII of the Constitution contain an elaboration of the freedom of trade, commerce and intercourse and the restrictions which the Constitution contemplates as being within the legislative powers of Parliament and the state legislatures. The legislative power conferred upon Parliament can restrict the ambit of the freedom to the extent that is specified in Articles 302 and 303. Similarly, the state legislatures are subject to the limitations contained in Article 303 (1) and Article 304. Parliament as well as the state legislatures are subject to constitutional limitations on the exercise of their law making power in restricting the freedom of trade, commerce and intercourse.

19. The extent of the freedom under Article 301 has in this manner been made subject to the provisions of Part XIII. Those provisions of Part XIII define the extent to which a restriction can be imposed by law as well as the limitations on the power of Parliament and the state legislatures while prescribing a restriction.

C Constitutional history as a guide

20. The Constitution was enacted in a historical and comparative framework. Historically, there was the presence in India prior to independence of the British Indian territories on the one hand and the princely states on the other. The founding fathers intended while enacting Part XIII to wield India into an economically integrated entity. In adopting Part XIII, the founding fathers did not intend to elaborate as much on the notion of lassiez-faire as on the integration of India into an economic entity.

21. The Constitution was framed in the context of a social, economic and political upheaval. The Constituent Assembly debates provide an enriching insight into the problems and concerns that were present to the minds of the draftsmen of the Constitution, as they adopted what became Part XIII. Dr B Shiva Rao in his seminal work titled 'The Framing of India's Constitution' [92] explains the historical perspective which led to the attention of the Constituent Assembly being engaged towards the freedom of trade and commerce within the territories of the Union :

> "Under the British Rule, freedom of trade was the established practice in British India, with no inter-provincial duties or other trade barriers. With the advent of provincial autonomy in April, 1937, it was considered necessary to place this mater on a statutory basis. Accordingly, section 297 of the Government of India Act, 1935, prohibited Provincial Governments from imposing barriers on trade within the country; nor could they levy any tax, cess, toll or other due which discriminated between goods manufactured in one locality and similar goods manufactured elsewhere. But this was far from ensuring freedom of internal trade throughout the sub-continent. Indian States could, and very often did, levy export and import duties at their frontiers and some of them derived considerable revenue from this source."

22. On 29 March 1947, the Sub-committee on Fundamental Rights discussed and adopted the draft provisions submitted by B N Rau on the freedom of trade and commerce, which read thus :

> "Subject to regulation by the law of the Union, trade, commerce and intercourse among the units, whether by means of internal carriage or by ocean navigation, shall be free: Provided that any unit may by law impose reasonable restrictions thereon in the interest of public order, morality or health." (Id. at p.699)

23. While discussing the report of the Sub-committee Alladi Krishnaswami Ayyar opined that: (i) goods which enter a particular unit from other units of the of the union should

[92] *Chapter 22 Pat. 699*

not escape duties and taxes to which goods produced in the concerned unit itself were subject; (ii) in an emergency a unit should be able to place restrictions on inter-State trade and commerce; (iii) the right should extend to non-citizens; and (iv) the freedom of trade should cover coastal trade specifically. After these suggestions were accepted, the Advisory Committee took up the issue for discussion. Commenting on these developments, B Shiva Rao (supra) specifically adverts to the view of C Rajagopalachari which was that the units of the Union must have the power to impose customs duties and other taxes for raising revenue. A contrary view was, however, expressed inter-alia by Alladi Krishnaswami Ayyar. Shiva Rao's statement of what transpired is extracted below :

> "During the discussions, Rajagopalachari expressed the view that units should be given power to impose customs duties and other taxes for genuine revenue purposes; if this was not conceded, the clause would wrest from them a substantial means of increasing their revenues and hamper the progress of the comparatively poorer ones amongst them. Alladi Krishnaswami Ayyar and K M Panikkar feared, on the other hand, that the grant of such taxing power to the Provinces or States might encourage competition between them and thus weaken the federal idea and should, therefore, be prevented. The committee accepted the provisions as recommended by the sub-committee with one change; the sub-clause providing for central regulation of trade by or with non-citizens was dropped as being vague and unnecessary." (Id. at p.700)

24. The clause was debated in the Constituent Assembly. B N Rau incorporated the following clauses in the draft constitution of October 1947 :

> "Subject to the provisions of any Federal law, trade, commerce and intercourse among the units shall, if between the citizens of the Federation, be free : Provided that nothing in this section shall prevent any unit from imposing on goods imported from other units any tax to which similar goods manufactured or produced in that unit are subject, so, however, as not to discriminate between goods so manufactured or produced : Provided further that no preference shall be given by any regulation of trade, commerce or revenue to one unit over another: Provided also that nothing in this section shall preclude the Federal Parliament from imposing by Act restrictions on the freedom of trade, commerce and intercourse among the units in the interests of public order, morality or health or in cases of emergency." (Id. at p. 701)

25. The Drafting Committee thereafter redrafted the above provisos which came to be included as independent articles under the heading of "Inter-State Trade and Commerce" in Part IX of the draft constitution. Article 16 (which formed a part of the Chapter on Fundamental Rights) provided that subject to the provisions of Article 244 and of any law made by Parliament, trade, commerce and intercourse throughout the territory of India would be free. Article 243 prohibited preferences and discrimination between one state and another. Articles 244 permitted the imposition of a non-discriminatory tax by a state on goods imported from another state similar to a tax which goods manufactured in the state are subject.

26. Alladi Krishnaswami Ayyar had strong reservations to allowing the imposition of reasonable restrictions on inter-State trade, on the ground that this would practically nullify the freedom of trade secured under draft Article 16, the expression "in the public interest" being vague. When draft Article 16 was taken up in the Constituent Assembly, objections were raised to it being adopted as an Article under the Fundamental Rights. Subjecting the freedom of trade under Article 16 to a law made by Parliament and to the power of the state to impose taxes and restrictions was in this view destroying the fundamental character of the freedom conferred and no residue would be left which could not be curtailed by Parliament or the states.

27. Dr B R Ambedkar while responding to the inclusion of Article 16 drew attention to the history surrounding the article. The Indian states had initially agreed to join the Union only in respect of foreign affairs, defence and communications. They were unwilling to allow the Union Parliament to have legislative authority over trade and commerce by its inclusion in the Union List of the Seventh Schedule. ***Shiva Rao***[93] states that on the other hand it was believed that the formation of an All-India Union would be without meaning if trade and commerce throughout the Union was not free. After the speech by Dr Ambedkar, draft Article 16 was adopted to be added to the Constitution.

28. Subsequently, the Constituent Assembly accepted the view of Dr Ambedkar that a separate part, Part XA, exclusively devoted to trade, commerce and intercourse within the territory of India be adopted. Part XA was to consist of Articles 274A to 274E. Eventually, Article 16 was deleted from the Chapter on Fundamental Rights on the ground that with the inclusion of the right in Article 274A (corresponding to present Article 301), the retention of Article 16 was rendered superfluous. Dr Ambedkar explained that different articles which were scattered in various parts were brought together in one part dealing with the freedom of trade, commerce and intercourse. Shiva Rao adverts to the observations of Alladi Krishnaswami Ayyar, which are significant :

> "Alladi Krishnaswami Ayyar replied that the transfer of a provision in regard to freedom of inter-State trade from one part of the Constitution to another did not alter or affect the nature of the right embodied in it; the mere placing of a provision in the chapter on fundamental rights did not carry with it any particular sanctity, nor did its justiciability depend on such placement."
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> (Id. at p.706)

Moreover, with the integration of the Indian states and with the strong federation having materialised there was no need felt to retain the provision for freedom of inter-State trade in the chapter on Fundamental Rights.

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29. Partition and the immense human suffering inflicted upon large segments of the population provided a strident political backdrop for the need to preserve the unity of the

[93] *(supra at page 703)*

nation. In assigning the role of a strong centre in the federal polity, the founding fathers had a constitutional vision for preserving the political unity of free and democratic India.

The economic history of both the British and Indian states was marred by famines and scarcity. Present to the minds of the founding fathers were the inequalities of resources and disparities in development between various provinces, including those that constituted British India on one hand and Indian states on the other. The framers of the Constitution contemplated that the provisions of draft Part XA (present Part XIII) should be an instrument for achieving economic progress under the rubric of one nation. Part XIII was the corner stone for fostering the economic development of the nation. In the vision of the founding fathers, India had to be knit together in terms of an economic and fiscal union.

30. In the social and political milieu that preceded the adoption of the Constitution, the emphasis in Part XIII was not as much upon creating a market economy: laissezfaire was not an attractive political doctrine. In fact, responding to an amendment that was proposed by Pandit Thakur Das Bhargava that the freedom of trade should be absolute, T T Krishnamachari, responded by stating that the extent of freedom which was allowed "is about the maximum amount of liberty that we can give for trade and commerce, the maximum amount of concession that we can give to trade and commerce consistent with the future economic improvement of this country". He observed :

> "Even as it was originally suggested, that we should make it a matter of fundamental right, and even without the restrictions that have been put in Article 16, I am afraid the economic progress of the country will become well-nigh impossible. There is absolutely no use in the honourable Member trying to confuse a matter of civil liberty with a matter or rights in respect of trade and commerce. The world has well-nigh come to a position when trade and commerce cannot be run without control and some kind of direction by the Government. If my honourable friends think that we are in the days of the nineteenth century when the laissez faire enthusiast had practically the ordering of everything in the world, I am afraid they are mistaken."

In his address to the Constituent Assembly, T T Krishnamachari emphasised the need to restrain the exercise of state powers which, it was apprehended, may be deployed to pursue narrow provincial interests :

> "A certain amount of freedom of trade and commerce has to be permitted. No doubt, restrictions by the State have to be prevented so that the particular idiosyncrasy of some people in power or narrow provincial policies of certain States should not be allowed to come into play and affect the general economy of the country."

31. Yet regional concerns could not be ignored. Addressing the Constituent Assembly, Alladi Krishnaswami Ayyar spoke about the diversity of interests, geographical position and economic attainments of various regions of the country. They required attention as well:

> "My friend, Dr Ambedkar in the scheme has evolved and has taken into account the larger interests of India as well as the interest of particular states and the

> wide geography of this country in which the interests of one region differ from the interests of another region. There is no need to mention that famine may be raging in one part of the country while there is plenty in another part. It may be that manure and other things are required in one part of the country while profiteers from another part of the country may try to transport the goods from the part affected. At the same time, in the interests of the larger economy and the future prosperity of our country, a certain degree of freedom of trade must be guaranteed."

Consistent with the concern about enabling the country to achieve economic prosperity, he spelt out the following priorities underlying Part XIII :

> "Therefore in a federation what you have to do is, first you will have to take into account the larger interests of India and permit freedom of trade and intercourse as far as possible. Secondly, you cannot ignore altogether regional interests. Thirdly, there must be the power of intervention of the Centre in any case of crisis to deal with peculiar problems that might arise in any part of India. All these three factors are taken into account in the scheme that has been placed before you."

32. The introduction of the proviso to draft Article 274 (D) [corresponding to the proviso to the present Article 304 (b)] was justified as being necessary "if on account of parochial patriotism or separatism without consulting the larger interest of India as a whole," a bill or amendment was introduced by a state legislature. This was regarded by Alladi Krishnaswami Ayyar as "a very restricted power that is conferred on the legislation of a state" to impose reasonable restrictions on the freedom of trade, commerce and intercourse with or within that state as may be required in the public interest. Therefore, it was envisaged that the President who had to grant sanction will have the opportunity to see that the legislation is in the public interest and that the restriction imposed is reasonable. Moreover, he observed "it is not possible to devise a watertight formula for defining these restrictions."

33. The deliberations in the Constituent Assembly surrounding the introduction of Part XIII leave little ambiguity about the constitutional philosophy underlying the introduction of the guarantee of free trade, commerce and intercourse. The guarantee of that freedom was guided by the object of fostering economic development. Towards achieving that goal, the founding fathers recognised the need to weave the nation into one economic entity. At the same time, regional interests representing the diversity prevalent within the states had to be recognised by allowing a regulatory role for the states. While recognising the importance of the state legislatures in relation to trade, commerce and intercourse, the founding fathers had evident concerns about what they described as parochial interests or narrow provincial policies posing a danger to the economic development of the nation. Hence, the Union Government was conferred with a power of intervention which was qualitatively different from the regulatory power conferred upon the states. To the Union Government was assigned the role of ensuring that the goal of pursuing economic development of the nation as one economic entity was not destroyed by the pursuit of parochial interests. It was in that background that the proviso to Article 304 (b) mandated the prior sanction of the President to a bill or

amendment introduced in the state legislature for imposing reasonable restrictions in the public interest on the freedom that was guaranteed by Part XIII.

34. The founding fathers were careful when they noted that it was not possible to elucidate by a watertight formula, the form in which such restrictions may take. The nature of the Indian economy on the eve of the adoption of the Indian Constitution was radically different from the economy which has emerged in the era of trade liberalism and beyond. I shall deal with the impact of those changes in a subsequent part of this judgment. At this stage, it would suffice to note that the guarantee of freedom for trade, commerce and intercourse which the Constitution adopted in Part XIII was an instrument of fostering economic progress as an important facet of national policy.

D. The trend-setting decisions : Atiabari and Automobile Transport

35 Two decisions rendered over five decades ago have shaped constitutional jurisprudence under Part XIII. They form the fulcrum of the reference in these proceedings. The first is the decision of a Constitution Bench in *Atiabari Tea Company Ltd. v. The State of Assam* [94] The second is a decision of seven Judges in the *The Automobile Transport (Rajasthan) Ltd. v. The State of Rajasthan*[95]*.*

36. In Atiabari, the Assam Taxation (on goods carried by roads and inland waters ways) Act, 1954 was enacted by the state legislature under entry 56 of the State List to the Seventh Schedule. The law provided for the levy of a tax on manufactured tea in chests carried by motor vehicles (except by railways and airways) at a specified rate per pound.

37. A Special Bench of the High Court dismissed the petitions challenging the validity of the Act. By a judgment of the Supreme Court rendered by a majority, the appeals and petitions filed under Article 32 by producers of tea were allowed. The majority held the Act to be ultra-vires.

38. Justice P B Gajendragadkar delivered the leading majority judgment on behalf of Justices K N Wanchoo and K C Dasgupta, while Justice J C Shah delivered a separate judgment. Justice Gajendragadkar held that the Act imposed a direct restriction on the freedom of trade and in the absence of compliance with the provisions of Article 304(b), it was unconstitutional. Justice Shah held that Part XIII imposes restrictions on the legislative powers of Parliament and state legislatures under Articles 245, 246 and 248 read with the lists of the Seventh Schedule. According to this view, restrictions on freedom of trade and commerce include burdens in the nature of taxation. The Act was held as having infringed
Article 301 and failing compliance with the proviso to Article 304 (b), it was found to be unconstitutional. Chief Justice B P Sinha differed with the majority on the ground that Part XIII of the Constitution did not justify the inference that taxation simpliciter is within Article 301 of the Constitution.

39. The correctness of the view in Atiabari was reconsidered by a larger bench of seven Judges in Automobile Transport (supra). The Rajasthan Motor Vehicles Taxation Act,

1951 provided for the levy of a tax on motor vehicles used in any public places or kept for use in Rajasthan. The Rajasthan High Court, in view of a judgment rendered by its Full Bench negatived a challenge to the provisions of the Act. The decision of the Rajasthan High Court had been rendered before the judgment in Atiabari was pronounced. When a Bench of seven Judges considered the matter in this Court, Justice S K Das, delivered the leading majority judgment on behalf of himself and Justices Kapoor and Sarkar.

40. The view of the three judges was that the Act did not violate the provisions of Article 301 because the taxes imposed were compensatory in nature which did not hinder the freedom of trade, commerce and intercourse. The interpretation placed by the majority in Atiabari was held to be "correct, but subject to this clarification" that regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not fall within the purview of the restrictions contemplated by Article 301 and need not comply with the requirements of the proviso to Article 304(b) of the Constitution. Justice B Subba Rao agreed with the view of Justice S K Das, in a concurring judgment.

41. Justice M Hidayatullah delivered a dissenting judgment for and on behalf of himself and Justices Rajagopala Ayyangar and Mudholkar. In the view of the minority a tax which is made a condition precedent to the right to enter upon and carry on business is a restriction on the right to carry on trade and commerce. The tax, it was held, was not a fee for administrative purposes, its object being to raise revenue. The judgment of the minority held that the tax was directly upon trade and on its movement.

42. In order to facilitate an analysis of the varying and divergent lines of thought in the three judgments in Atiabari and the three judgments in Automobile Transport (supra), it would be necessary to consider the views expressed under the following heads :

D. 1 Atiabari : Article 301 and taxation

43. Chief Justice Sinha in his judgment in Atiabari held that freedom under Article 301 could not be construed in such a comprehensive manner as to include freedom from all impediments, restraints and barriers, including freedom from all taxes :

> "13. Learned counsel for the appellants vehemently argued that the freedom contemplated by Article 301 must be construed in its most comprehensive sense of freedom from all kinds of impediments, restraints and trade barriers, including freedom from all taxation. In my opinion, there is no warrant for such an extreme position."
> (Id. at p.826)
>
> Defining the expressions trade, commerce and intercourse, Chief Justice Sinha held
> that :
>
> "13 The three terms used in Article 301 include not only free buying and selling, but also the freedom of bargain and contract and transmission of information

relating to such bargains and contracts as also transport of goods and commodities for the purposes of production, distribution and consumption in all their aspects, that is to say, transportation by land, air or water. They must also include commerce not only in goods and commodities, but also transportation of men and animals by all means of transportation. Commerce would thus include dealings over the telegraph, telephone or wireless and every kind of contract relating to sale, purchase, exchange etc. of goods and commodities."

(Id. At p. 826-827)

44. In the view of Chief Justice Sinha, in this comprehensive sense, taxation of trade, commerce and intercourse would cover almost the entire field of public taxation both in the Union and in the State lists. Hence, "it is almost impossible to think that the makers of the Constitution intended to make trade, commerce and intercourse free from taxation in that comprehensive sense".

(emphasis supplied)

45. The first reason adduced in Chief Justice Sinha's judgment for not adopting such a comprehensive definition of the freedom under Article 301 is that the power to tax in order to raise revenue is a manifestation of sovereignty. Being a sovereign power, it is not ordinarily justiciable. Second, the power of the states to raise finances for the purpose of government is elucidated in Part XII of the Constitution. Article 265 imposes a prohibition on the levy or collection of a tax except by authority of law. Part XII of the Constitution which deals with finances and Part XIII are self-contained provisions, one not being subject to the other :

"Hence, both Parts XII and XIII are meant to be self-contained in their respective fields. It cannot, therefore, be said that the one is subject to the other."

The third reason adduced in the judgment of Chief Justice Sinha for not adopting such a comprehensive definition of the freedom conferred by Article 301 is the dilution of the power of the states to impose taxes, which would result from adopting such a construction :

"14...It is almost impossible to think that the makers of the Constitution intended to make trade, commerce and intercourse free from taxation in that comprehensive sense. If that were so, all laws of taxation relating to sale and purchase of goods on carriage of goods and commodities, men and animals, from one place to another, both inter-State and intra-State, would come within the purview of Article 301 and the proviso to Article 304(b) would make it necessary that all Bills or Amendments of pre-existing laws shall have to go through the gamut prescribed by that proviso. That will be putting too great an impediment to the power of taxation vested in the States and reduce the States' limited sovereignty under the Constitution to a mere fiction. That extreme position has, therefore, to be rejected as unsound." (Id. at p. 827)

Fourthly, Chief Justice Sinha held that Article 304 is divided into two parts : (i) clause(a) which deals with the imposition of discriminatory taxes by a state legislature; and (ii) clause(b) which relates to the imposition of reasonable restrictions. This, in the view of the Chief Justice, indicates that the imposition of taxes is not within the fold of reasonable restrictions on the freedom of trade, commerce and intercourse :

> "12 But a close examination of the provisions of Article 304 would show that it is divided into two parts viz. (1) dealing with imposition of discriminatory taxes by a State Legislature; and (2) relating to imposition of reasonable restrictions, thus showing that imposition of taxes, discriminatory or otherwise, is a class apart from imposition of reasonable restrictions on freedom of trade, commerce and intercourse." (Id. at p. 824) Fifthly, Chief Justice Sinha opined that "not all taxes constitute necessarily an impediment or restraint in the matter of trade, commerce and intercourse" :
>
> "15 all taxation is not necessarily an impediment or a restraint in the matter of trade, commerce and intercourse. Instead of being such impediments or restraints, they may, on the other hand, provide the wherewithals to improve different kinds of means of transport, for example, in cane growing areas, unless there are good roads, facility for transport of sugarcane from sugarcane fields to sugar mills may be wholly lacking or insufficient. In order to make new roads as also to improve old ones, cess on the grower of cane or others interested in the transport of this commodity has to be imposed, and has been known in some parts of India to have been imposed at a certain rate per maund or ton of sugarcane transported to sugar factories. Such an imposition is a tax on transport of sugarcane from one place to another, either intra-State or inter-State. It is the tax thus realised that makes it feasible for opening new means of communication or for improving old ones. It cannot, therefore, be said that taxation in every case must mean an impediment or restraint against free flow of trade and commerce. Similarly, for the facility of passengers and goods by motor transport or by railway, a surcharge on usual fares or freights is levied, or may be levied in future. But for such a surcharge, improvement in the means of communication may not be available at all. Hence, in my opinion, it is not correct to characterise a tax on movement of goods or passengers as necessarily connoting an impediment, or a restraint, in the matter of trade and commerce. That is another good reason in support of the conclusion that taxation is not ordinarily included within the terms of
> Article 301 of the Constitution."
>
> (Id. at p. 827-828)
>
> Sixthly, in the view of the Chief Justice Sinha "taxation simpliciter" is not within the terms of Article 301 since the very purpose underlying the taxing power is the ability of the state to raise money for public purposes by compelling the payment by those who are taxed of moneys earned or possessed by them, by virtue of the facilities and protection offered by the state. A public purpose is implicit in every taxation. Part XIII when it refers to 'reasonable restrictions in the public interest'

could not have intended to include taxation within the ambit of the expression.

46. At the same time, Chief Justice Sinha rejected the 'extreme proposition' that taxation would be wholly outside the purview of Article 301. That position was rejected on the ground that firstly, Article 304 contains a specific reference to taxation and secondly, Article 305 prior to its repeal made a specific reference to taxation for certain purposes. Chief Justice Sinha made a distinction in the following observations :

"17 The Article thus brings out the clear distinction between taxation as such for the purpose of revenue and taxation for the purpose of making discrimination or giving preference, both of which are treated by the Constitution as impediments to free trade and commerce. In other words, so long as the impost was not in the nature of an impediment to the free flow of goods and commodities between one State and another, including in this expression Union territories also, its legality was not subject to an attack based on the provisions of Part XIII." (Id.atp. 830)

47. In this view, a law which imposes an impediment to the free flow of trade, commerce and intercourse such as by a high tariff wall is not a measure of taxation but assumes a character of a trade barrier :

> "16 If a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution - makers to abolish by Part XIII." (Id. at p. 829)
>
> The conclusions of the Chief Justice are restated in the following propositions :
>
> "16....The objections against the contention that taxation was included within the prohibition contained in Part XIII may thus be summarised: (1) Taxation, as such, always implies that it is in public interest. Hence, it would be the outside particular restrictions, which may be characterised by the courts as reasonable and in public interest. (2) The power is vested in a sovereign State to carry on Government. Our Constitution has laid the foundations of a welfare State, which means very much expanding the scope of the activities of Government and administration, thus making it necessary for the State to impose taxes on a much larger scale and in much wider fields. The legislative entries in the three Lists referred to above empowering the Union Government and the State Governments to impose certain taxations with reference to the movement of goods and passengers would be rendered ineffective, if not otiose, if it were held that taxation simpliciter is within the terms of Article 301. (3) If the argument on behalf of the appellants were accepted, many taxes, for example, sales tax by the Union and by the States, would have to go through the gamut prescribed in Articles 303 and 304, thus very much detracting from the limited sovereignty of the States, as envisaged by the Constitution. (4) Laws relating to taxation, which is essentially a legislative function of the State, will become justiciable and every

time a taxation law is challenged as unconstitutional, the State will have to satisfy the courts – a course which will seriously affect the division of powers on which modern constitutions, including ours, are based. (5) Taxation on movement of goods and passengers is not necessarily an impediment." (Id. at p. 829-830) The basic principle which is enunciated in the judgment of the Chief Justice Sinha is that :

"18 (2) the freedom declared by Article 301 does not mean freedom from taxation simpliciter, but does mean freedom from taxation which has the effect of directly impeding the free flow of trade, commerce and intercourse." (Id. At p. 831)

48. The test, in the view of Chief Justice Sinha, is whether a tax has the effect of directly impeding the free flow of trade, commerce and intercourse. If it does, it falls within the ambit of Article 301. The test is of the true nature and effect of the tax. Does it impose an impediment to the free flow of trade, commerce & intercourse? An illustration of such an impediment is a high tariff wall which then assumes the character of a trade barrier. A high tariff wall is an example of an impediment under taxing laws to the freedom of trade, not an exhaustive elaboration. Those taxes which impede the free flow of trade and commerce are within Article 301.

49. The judgment of Justice Gajendragadkar, for the majority holds that the power of taxation is subject to constitutional provisions :

"35...Basing himself on this character of the taxing power of the State, the learned Attorney General has asked us to hold that Part XIII that can have no application to any statute imposing a tax. In our opinion, this contention is 'not' well-founded "therefore, the true position appears to be that, though the power of levying tax is essential for the very existence of the government, its exercise must inevitably be controlled by the constitutional provisions made in that behalf. It cannot be said that the power of taxation per se is outside the purview of any constitutional limitations." (Id. at p. 846)

50. Justice Gajendragadkar noted first, that the power under Article 265 of the Constitution to levy a tax under the authority of law is referable to Article 245 read with the corresponding legislative entries in the Seventh Schedule. Since Article 245 is subject to the provisions of the Constitution, the power of Parliament and of the state legislatures to impose taxes is subject to the application of constitutional provisions, which must include Part XIII :

"37....Now, if we look at Article 245 which deals with the extent of laws made by Parliament and by the Legislatures of States, it begins with the words "subject to the provisions of this Constitution"; in other words, the power of Parliament and the Legislatures of the States to make laws including laws imposing taxes is subject to the provisions of this Constitution and that must bring in the application of the provisions of Part XIII." (Id. at p. 847-848) Second, in this view, the freedom of trade, commerce and intercourse under Article 301 is subject only to the provisions of Part XIII which means that the amplitude of the freedom cannot be

controlled outside Part XIII. Thirdly, in the view of Justice Gajendragadkar, the freedom guaranteed by Article 301 is a freedom from all restrictions except those which are contemplated under Part XIII :

"42....Stated briefly trade even in a narrow sense would include all activities in relation to buying and selling, or the interchange or exchange of commodities and that movement from place to place is the very soul of such trading activities. When Article 301 refers to the freedom of trade, it is necessary to enquire what freedom means. Freedom from what? is the obvious question which falls to be determined in the context. At this stage, we would content ourselves with the statement that the freedom of trade guaranteed by Article 301 is freedom from all restrictions except those which are provided by the other Articles in Part XIII." (Id. at p. 853) Fourthly, Justice Gajendragadkar adverts to the effect of the non-obstante clause in Article 304 which enables the imposition of a tax notwithstanding the provisions of Article 301 :

"46 How a tax can be levied on internal goods is, however, provided by Article 304(b). The non-obstante clause referring to Article 301 would go with Article 304(a), and that indicates that tax on goods would not have been permissible but for Article 304(a) with the non-obstante clause. This incidentally helps to determine the scope and width of the freedom guaranteed under Article 301; in other words, Article 304(a) is another exception to Article 301."

(Id. at p. 856)

In this view, Article 304 (a) and Article 304(b) have to be read together. That tax legislation is included in Article 301 is an inference from the use of the non-obstante clause in Article 304. Finally, Justice Gajendragadkar held that movement of trade is the essence of the freedom guaranteed by Article 301. If transport or movement of goods is taxed solely on the basis that goods are carried or transported, that would affect directly the freedom of trade under Article 301 :

"49 it certainly includes movement of trade which is of the very essence of all trade and its integral part. If the transport or the movement of goods is taxed solely on the basis that the goods are thus carried or transported that, in our opinion, directly affects the freedom of trade as contemplated by Article 301. If the movement, transport or the carrying of goods is allowed to be impeded, obstructed or hampered by taxation without satisfying the requirements of Part XIII, the freedom of trade on which so much emphasis is laid by Article 301 would turn to be illusory. When Article 301 provides that trade shall be free throughout the territory of India, primarily it is the movement part of the trade that it has in mind and the movement or the transport part of trade must be free subject of course to the limitations and exceptions provided by the other Articles of Part XIII."(Id. At p. 859)

51. Justice Gajendragadkar did notice the need to draw a balance for preserving the powers of the states in a federal constitution. The test which he formulated is that the restrictions which fall within Article 301 are those which directly and immediately restrict or impede the free flow or movement of trade :

"50 Thus considered we think it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Article 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Article 301. The argument that all taxes should be governed by Article 301 whether or not their impact on trade is immediate or mediate, direct or remote, adopts, in our opinion, an extreme approach which cannot be upheld." (Id. At p 860)

52 . Justice Gajendragadkar, in the ultimate analysis also shuns an interpretation under which all taxes would be brought within the ambit of Article 301. The principle which the learned judge adopts is that taxing laws are not excluded from the operation of Article 301 and that they can and do amount to restrictions on freedom. Yet, tax laws which directly and immediately restrict trade or its movement are alone within the ambit of Article 301.

53. Justice Shah joined the conclusion of the majority in holding that the Assam enactment violated the guarantee of freedom under Article 301 and had not passed muster under the proviso to Article 304(b). But Justice Shah agreed with the conclusion of the majority on a much wider premise that all laws of taxation fall within the purview of Article 301. In his view, trade and commerce comprehends traffic in goods and much more. In this view, while movement of goods may be an important ingredient of effective commerce, movement itself is not an essential ingredient of commerce. In his view :

> "66 What is guaranteed is freedom in its widest amplitude — freedom from prohibition, control, burden or impediment in commercial intercourse. Not merely discriminative tariffs restricting movement of goods which are included in the restrictions and are hit by Article 301, but all taxation on commercial intercourse, even imposed as a measure for collection of revenue is so hit. Between discriminatory tariffs and trade barriers on the one hand and taxation for raising revenue on commercial intercourse, the difference is one of purpose and not of quality. Both these forms of burden on commercial intercourse trench upon the freedom guaranteed by Article 301."
>
> (Id. at p. 874-875)

The freedom under Article 301, in the judgment of Justice Shah, connotes freedom from tax burdens as well as other impediments but is subject to Part XIII of the Constitution.

54. The distinction between the judgment of the majority and the view of Justice Shah is precisely in the extent to which tax laws are held to fall within the ambit of Article 301. For the majority, movement constitutes the soul of trade whereas for Justice Shah, it is

not an essential ingredient in all situations. For the majority, it is the movement or the transport part of trade that must be free subject to the limitations in Part XIII. However, it was only such taxes as directly and immediately impede trade that fall within the purview of Article 301. Justice Gajendragadkar rejected the contention that all taxes should be governed by Article 301 whether or not their impact on trade is immediate and direct on the one hand or whether it is remote and "mediate "on the other. For Justice Shah every law of taxation of commercial intercourse, even when it is a measure for the collection of revenue is hit by Article 301.

55. Having said this, it is necessary also to note that there was at the same time an agreement on principle on certain crucial aspects of Part XIII between the views expressed in the judgment of the majority and the views of Justice Shah. Firstly, the majority (as noted earlier) spoke of constitutional restrictions and limitations on the legislative powers of Parliament and the state legislatures, and emphasized that Part XIII is a source of such a limitation. Justice Shah agreed with this premise in the following observations:

> "64....On the exercise of the legislative power to tax trade, commerce and intercourse, restrictions are prescribed by certain provisions contained in Part XII, e.g., Articles 276, 286, 287, 288 and 289: but these restrictions do not exhaustively delimit the periphery of that power. The legislative power to tax is restricted also by the fundamental freedoms contained in Part III, e.g., Articles 14,15(1), 19(1)(g) and 31(1) and is further restricted by Part XIII. Article 245, clause (1), of the Constitution expressly provides that the legislative powers of the Parliament and the State Legislatures to make laws are subject to the provisions of the Constitution; and Article 301 is undoubtedly one of the provisions to which the legislative powers are subject."
>
> (Id. at p. 873)
>
> Secondly, Justice Shah like the majority emphasized the non-obstante provision of Article 304 which operates with reference to Article 301. In his view, if Article 301 did not deal with the burdens of taxation, there was no reason to incorporate a non-obstante provision in Article 304 :
>
> "74.. If Article 301 and Article 303 did not deal with the restrictions or burdens in the nature of tax, the reason for incorporating the non-obstante clause to which Article 304, clause (1), is subject, cannot be appreciated. Undoubtedly, the provisions of Part XIII of the Constitution do not impose additional or independent powers of taxation; the powers of taxation are to be found conferred by Articles 245, 246 and 248 read with the Lists in the Seventh Schedule, and the provisions of Part XIII are limitative of the exercise of legislative power. The circumstance that the Constitution has chosen to deal with a specific field of taxation as an exception to Articles 301 and 303 (which should really be Article 303(1)) strongly supports the inference that taxation was one of the restrictions from the imposition of which by the guarantee of Article 301, trade, commerce and intercourse are declared free." (Id at p. 881) Thirdly, Justice Shah adopts

the same position as the majority did in holding that the expression 'restrictions' in clause (b) of Article 304 includes a restriction in the nature of a tax :

"75 Clause (b) deals with a general restriction which includes a restriction by the imposition of a burden in the nature of tax. Clause (a) deals with a specific burden of taxation in a limited field." (Id. at p. 881)

56. The basic difference between the judgment of the majority and the decision of Justice Shah lies in the extent to which the taxing power is regarded as being within or outside the purview of Article 301. For the majority every taxing legislation is not within the ambit of Article 301. The guarantee under Article 301 is against such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Only those taxes which directly and immediately restrict trade would fall within Article 301. For Justice Shah all taxation on commercial intercourse would attract the provisions of Article 301.

57. A comparison of the view that was adopted by the majority with the judgment of Chief Justice Sinha would indicate differences of substance on some issues and essentially of degree on other aspects. Chief Justice Sinha prefaced his discussion with the premise that taxation is governed by Part XII and that Part XII and Part XIII are self-contained and independent provisions. Moreover, Chief Justice Sinha held that taxation being an essential attribute of sovereignty, it would not be appropriate in a federal structure to make the state power of taxation subservient by the application of Article 304 (b) to all taxing legislation. However, Chief Justice Sinha ultimately accepts the position that not all but some tax legislation is subject to the mandate of Article 301. In his view, so long as a tax imposition is not an impediment to the free flow of trade, commerce and intercourse, it must pass muster and would not fall within Article 301. Justice Gajendragadkar also held (speaking for the majority) that a tax law which directly and immediately restricts trade will fall within the ambit of Article 301. The test in the judgment of Chief Justice Sinha is whether a tax law "has the effect of directly imposing the free flow of trade". The test adopted by the majority of "such taxes as directly and immediately restrict trade" find a broad co-relation to the test adopted by Chief Justice Sinha. The difference in the view of the majority from that of the learned Chief Justice on this aspect was essentially a difference of degree. Chief Justice Sinha noted that he differed with the majority on the ground that the Constitution does not justify the inference that taxation simpliciter is within the terms of Article 301. In his view, the Assam legislation in that case was a taxing statute simpliciter without any discrimination against dealers or producers outside the state. The majority held the tax to be unconstitutional since its object was to collect taxes on goods solely on the ground that they are carried by road or by inland waterways within the area of the state. This, for the majority, was a restriction within the ambit of Article 301 which could have been achieved lawfully only by satisfying the requirements of Article 304 (b). On the other hand, Chief Justice Sinha would regard only a discriminatory tax as a restriction on trade.

D. 2 Automobile Transport

58. The seven Judge bench in Automobile Transport dealt, in the three judgments which were delivered, with: (i) the nature and extent of the freedom guaranteed by Article 301; (ii) the power to impose taxes; (iii) constitutional limitations or restrictions on the power to tax; (iv) the necessity of interpreting the provisions of Part XIII so as not to eviscerate the sovereignty of the states; and (v) whether, and if so, the extent to which Part XIII controls fiscal legislation.

D.2.1 Freedom and regulation

59. Justice S K Das, in the leading judgment of the majority held that though Article 301 "runs unqualified", the freedom must necessarily be delimited by considerations of social orderliness :

> "10.. As the language employed in Article 301 runs unqualified the Court, bearing in mind the fact that that provision has to be applied in the working of an orderly society, has necessarily to add certain qualifications subject to which alone that freedom may be exercised."
>
> (Id. at p. 521)

60. Justice Subba Rao in a concurring judgment held that the freedom conferred by Article 301 is a freedom of trade across borders. The freedom is to trade unrestricted by barriers :

> "35 the said composite expression means trade across the borders: what is free is that trade. It is implicit in the concept of freedom that there will be obstructions to it. Such obstructions or barriers may be, in the present context, to the freedom to trade across the borders.
>
> Article 301 provides for freedom from the said barriers or impediments in effect operating as barriers. This freedom from barriers cannot operate in vacuum and must be limited by space. A barrier may be put up between two States at the boundary of the States or between two districts, two taluks, two towns or between two parts of a town. The barrier may be at a particular point, at a boundary or might take the form of a continuous impediment till the boundary is crossed. It may take different forms. The restrictions may be before or after movement. It may be a prior restraint or a subsequent burden. But the essential idea is that a barrier is an obstacle put across trade in motion at a particular point or different points. The expression "shall be free" declares in a mandatory form a freedom of such transport or movement from such barriers." (Id. at p. 547-548)

61. Freedom under Article 301, being throughout the territory of India, Justice Subba Rao held that Article 301 removes both inter-State and intra-State barriers, making the country as a whole into one unit :

> "36 The freedom declared under Article 301 may be defined as a right to free movement of persons or things, tangible or intangible, commercial or non-commercial, unobstructed by barriers, inter-State or intra-State or any other

impediment operating as such barriers."
(Id. at p. 548)

62 . Yet, the judgment of the majority posits that freedom under Article 301 is not impaired by facilitative regulations. Such regulations are facilitative because they promote trade and are not restrictive of it. The concept of facilitative regulations is in tandem with the view that the right under Article 301 is capable of regulation so as to preserve an orderly society. Regulations such as those defining limits of speed for transport vehicles, permissible loads or requiring the registration of vehicles do not impede trade. Adverting to these examples Justice S K Das held :

> "10 that the application of rules like the above does not really affect the freedom of trade and commerce; on the contrary they facilitate the free flow of trade and commerce. The reason is that these rules cannot fairly be said to impose a burden on a trader or deter him from trading: it would be absurd, for example, to suggest that freedom of trade is impaired or hindered by laws which require a motor vehicle to keep to the left of the road and not drive in a manner dangerous to the public. If the word "free" in Article 301 means "freedom to do whatever one wants to do", then chaos may be the result."
>
> (Id. At p. 522)

Justice Subba Rao adopted the same position. Facilitative regulations, in his view, do not restrict trade :

> "37...Before a particular law can be said to infringe the said freedom, it must be ascertained whether the impugned provision operates as a restriction impeding the free movement of trade or only as a regulation facilitating the same. Restrictions obstruct the freedom, whereas regulations promote it. Police regulations, though they may superficially appear to restrict the freedom of movement, in fact provide the necessary conditions for the free movement. Regulations such as provision for lighting, speed, good condition of vehicles, timings, rule of the road and similar others, really facilitate the freedom of movement rather than retard it. So too, licensing system with compensatory fees would not be restrictions but regulatory provisions; for without it, the necessary lines of communication, such as roads, water-ways and air-ways, cannot effectively be maintained and the freedom declared may in practice turn out to be an empty one. So too, regulations providing for necessary services to enable the free movement of traffic, whether charged or not, cannot also be described as restrictions impeding the freedom."
>
> (Id. at p. 549)

Significantly, these observations of Justice Subba Rao indicate that fees for the use of facilities or as charges for regulations which facilitate trade do not hinder or obstruct the free flow of trade. For, without those facilities, trade would be rendered difficult.

D. 2.2 Taxation and constitutional limitations

63. Justice S K Das held that the power to impose taxes is essential for the existence of government. Yet, in his view, it can be controlled by constitutional provisions. Part XII of the Constitution controls the power to levy taxes. But, Part XII does not exhaust the limitations on the power to tax:

> "13.. though the power of levying tax is essential for the very existence of government, its exercise may be controlled by constitutional provisions made in that behalf. It cannot be laid down as a general proposition that the power to tax is outside the purview of any constitutional limitations. We have carefully examined the provisions in Part XII of the Constitution and are unable to agree that those provisions exhaust all the limitations on the power to impose a tax." (Id. at p. 527)

64. Justice Subba Rao dealt with the issue from the perspective of whether the power of taxation is subject to limitation. Justice Subba Rao analysed the legal presumption that taxation is in the public interest and that it is not possible for a court to determine whether a particular rate of tax is reasonable. Considering the matter, Justice Subba Rao observed thus :

> "39 A law of taxation is made by Parliament or the Legislature of a State, as the case may be, in exercise of the power conferred under the Constitution by virtue of the entries found therein. It is a law just like any other law made under the Constitution. This Court, in K. Thathunni Moopil Nair v. State of Kerala [AIR (1962) SC 552] and in Balaji v. I T. Officer [AIR (1962) SC 123] , held that a law of taxation would be void if it infringed the fundamental right guaranteed under Article 19 of the Constitution. "Therefore, the law of taxation also should satisfy the two tests laid down in Article 19(6) of the Constitution. It is said that a law of taxation is always in public interest. Ordinarily, it may be so, but it cannot be posited that there cannot be any exceptions to it. A taxing law may be in public interest in the sense that the income realised may be used for public good, but there may be occasions, when the rate or the mode of taxation may be so abhorrent to the principles of natural justice or even to the well settled principles of taxation that it may cause irremediable harm to the public rather than promote public good, that the court may have to hold that it is not in public interest. Nor can I agree with the contention that it is impossible for a court to hold in any case that a rate of taxation is reasonable or not". (Id. at p. 553) In this view, no restriction, if it is unreasonable, can be more deleterious to freedom than the imposition of a fiscal burden on it, which may in certain circumstances destroy the very freedom. Consequently, Justice Subba Rao rejected the notion that laws of taxation are outside the scope of the freedom guaranteed by Article 301. The presumption of the fiscal law being in the public interest does not exclude judicial review where the law has transgressed those boundaries.

65. Justice Hidayatullah was explicit in holding that "taxation is within the prohibition contained *in Part XIII*[96]*."*

Id. at p-637

66. The basic premise of the majority is that tax legislation is subject to constitutional limitations or restrictions. Under Article 265, a tax can be levied only with the authority of law. Article 245 which empowers Parliament to enact legislation for the territory of India and the state legislatures, for the territories of the respective states, is "subject to the provisions of this Constitution." This expression would include Parts XII and XIII. Justice S K Das held thus :

> "13.. Article 245 which deals with the extent of laws made by Parliament and by the Legislatures of States expressly states that the power of Parliament and of the State Legislatures to make laws is "subject to the provisions of this Constitution". The expression "subject to the provisions of this Constitution" is surely wide enough to take in the provisions of both Part XII and Part XIII. In view of the provisions of Article 245, we find it difficult to accept the argument that the restrictions in Part XIII of the Constitution do not apply to the taxation laws."
> (Id. At p. 527-528)

67. Having held that the power of taxation is subject to constitutional limitations which include Part XIII, Justice S K Das rejected what he described as a "narrow interpretation" which postulates that save and except for Article 304(a), none of the other provisions of Part XIII extend to taxing statutes. That submission was also not accepted by Justice Subba Rao.

D. 2.3 State sovereignty

68. The majority was conscious of the need to preserve the sovereignty of the states. State autonomy would be impaired by an extensive construction of Article 301 and if all measures of taxation were brought within its ambit. Adopting such a view would lead to a situation where every law passed by the state legislature would be subject to the proviso to Article 304(b). Justice S K Das observed that a construction which would bring about such a result must be avoided :

> "11 Such an interpretation would, in our opinion, seriously affect the legislative power of the State Legislatures which power has been held to be plenary with regard to subjects in List II. The States must also have revenue to carry out their administration and there are several items relating to the imposition of taxes in List II. The Constitution-makers must have intended that under those items, the States will be entitled to raise revenue for their own purposes. If the widest view is accepted, then there would be for all practical purposes, an end of State autonomy even within the fields allotted to them under the distribution of powers envisaged by our Constitution.

[96] *Id. at p-637*

> An examination of the entries in the Lists of the Seventh Schedule to the Constitution would show that there are a large number of entries in the State List (List II) and the Concurrent List (List III) under which a State Legislature has power to make laws. Under some of these entries, the State Legislature may

impose different kinds of taxes and duties, such as property tax, profession tax, sales tax, excise duty etc., and legislation in respect of any one of these items may have an indirect effect on trade and commerce. Even laws other than taxation laws, made under different entries in the Lists referred to above, may indirectly or remotely affect trade and commerce. If it be held that every law made by the Legislature of a State which has a repercussion on tariffs, licencing, marketing regulations, price-control etc. must have the previous sanction of the President, then the Constitution insofar as it gives plenary power to the States and State Legislatures in the fields allocated to them would be meaningless". (Id. at p. 524-525)

69. Justice Subba Rao in the concurring judgment also noted that conceivably, every law enacted by a state legislature in pursuance of its legislative power may remotely affect trade. If every Bill introducing such a legislation were to be subjected to the prior sanction of the President under the proviso to Article 304 (b) that would result in a serious dilution of the autonomy of the states :

"38. The Constitution confers on the Parliament and the State Legislatures extensive powers to make laws in respect of various matters. A glance at the entries in the Lists of the Seventh Schedule to the Constitution would show that every law so made may have some repercussion on the declared freedom. Property tax, profession tax, sales tax, excise duty and other taxes may all have an indirect effect on the free flow of trade. So too, laws, other than those of taxation, made by virtue of different entries in the Lists, may remotely affect trade. Should it be held that any law which may have such repercussion must either be passed by the Parliament or by the State Legislature with the previous consent of the President, there would be an end of provincial autonomy, for in that event, with some exceptions, all the said laws should either be made by the Parliament or by the State Legislature with the consent of the Central Executive Government. By so construing, we would be making the Legislature of a State elected on adult franchise the handmaid of the Central executive." (Id. At p. 550)

70. Justice Hidayatullah was also concerned about the consequence on state autonomy of the adoption of a view which subjugated all state legislations having a conceivable, if even remote, impact upon trade to Presidential sanction :

"124... the financial independence of the States was secured by an elaborate division of heads of taxation, which were well thought out to provide the States with the means of independent existence and the wherewithal of nation-building activities. There is hardly any tax which the States are authorised to collect which could not be said to fall on traders. Property tax, sales tax, municipal taxes, electricity taxes (to mention only a few) are paid by traders as well as by non-traders. To say that all these taxes are so many, restrictions upon the freedom of trade, commerce and intercourse is to make the entire Constitutional document subordinate to trade and commerce. Since it is axiomatic that all taxes which a tradesman pays must burden him, any tax which touches him must fall within

> Article 304, if the word "restriction" is given such a wide meaning, every such legislation will then be within the pleasure of the President, and this could not have been intended. "Restriction" must, therefore, mean something more than a mere tax burden." (Id. at p. 633-634)

Every burden of tax, in this view would not be a restriction of trade and commerce. Justice Hidayatullah too shared this concern when he observed :

> "125. To bring all taxes within the reach of Article 301 and thus to bring them also within the reach of Article 304 is to overlook the concept of a Federation, which allows freedom of action to the States, subject, however, to the needs of the unity of India. Just as unity cannot be allowed to be frittered away by insular action. The existence of separate States is not to be sacrificed by a fusion beyond what the Constitution envisages." (Id. at p. 634-635)

E. Compensatory Taxes

E. 1 Original understanding

71. The judgment of the majority evolved the concept of compensatory taxes in response to its felt concern to preserve state autonomy. Compensatory taxes which are in the nature of a charge for the use of trading facilities would not be regarded as being a hindrance to the freedom of trade, so long as they are reasonable. By first devising the concept and then placing it beyond the pale of Article 301, the Court in Automobile Transport ensured that compensatory taxes would not be subject to the constitutional grind of Article 304(a). A class of tax legislation bearing a compensatory character was carved out of Part XIII.

72 . What are compensatory taxes? Explaining the concept, Justice S K Das in "10. Another class of examples relates to making a charge for the use of trading facilities, such as, roads, bridges, aerodromes etc. The collection of a toll or a tax for the use of a road or for the use of a bridge or for the use of an aerodrome is no barrier or burden or deterrent to traders who, in their absence, may have to take a longer or less convenient or more expensive route. Such compensatory taxes are no hindrance to anybody's freedom so long as they remain reasonable; but they could of course be converted into a hindrance to the freedom of trade." (Id. at p. 522)

In this view, for a tax to become prohibited, it has to be a tax, the effect of which is to directly hinder "the movement part of trade"[97] . So long as a tax remains compensatory or regulatory, it does not operate as a hindrance. Again, this was elaborated in the following observations :

[97] Id. at p-523

> "14..But we must advert here to one exception which we have already indicated in an earlier part of this judgment. Such regulatory measures as do not impede the freedom of trade, commerce and intercourse and compensatory taxes for the use of trading facilities are not hit by the freedom declared by Article 301."

(Id. at p. 528)

In the view of the majority :

"17..Regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Article 301 and such measures need not comply with the requirements of the proviso to Article 304 (b) of the Constitution." (Id. at p. 533)

Compensatory taxes were held to lie outside Article 301. Not being 'restrictions' which hamper the freedom of trade, compensatory taxes would not fall within the ambit of Article 301 and were not subject to the rigours of the proviso to Article 304(b).

73. The tax imposed by the State of Rajasthan was held to be compensatory since it facilitated trade and commerce :

"19....The taxes are compensatory taxes which instead of hindering trade, commerce and intercourse facilitate them by providing roads and maintaining the roads in a good state of repairs." (Id. At p. 536)

A tax would not cease to be compensatory merely because the precise or specific amount which is calculated is not actually used to provide facilities. The test on whether a tax is compensatory is formulated thus :

> "19.It seems to us that a working test for deciding whether a tax is compensatory or not is to enquire whether the trades 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." (Id.at p.536)
>
> Even if the proceeds from the tax are not credited to a separate fund that would make no difference so long as facilities are provided for trades' people who pay the tax. In his concurring judgment, Justice Subba Rao also adopted the 'direct and immediate effect' test. Justice Subba Rao held that :
>
> "38...If a law directly and immediately imposes a tax for general revenue purposes on the movement of trade, it would be violating the freedom. On the other hand, if the impact is indirect and remote, it would be unobjectionable. The Court will have to ascertain whether the impugned law in a given case affects directly the said movement or indirectly and remotely affects it." (Id. at p. 550-551)

A law which directly and immediately affects the free movement of trade in this view is a restriction on freedom. However, a measure which is compensatory or regulatory does not hinder trade :

> "40.. Of all the doctrines evolved, in my view, the doctrine of "direct and immediate effect" on the freedom would be a reasonable solvent to the difficult

situation that might arise under our Constitution. If a law, whatever may have been its source, directly and immediately affects the free movement of trade, it would be restriction on the said freedom. But a law which may have only indirect and remote repercussions on the said freedom cannot be considered to be a restriction on it. Taking the illustration from taxation law, a law may impose a tax on the movement of goods or persons by a motor-vehicle; it directly operates as a restriction on the free movement of trade, except when it is compensatory or regulatory. On the other hand, a law may tax a vehicle as property, or the garage wherein the vehicle used for conveyance is kept. The said law may have indirect repercussions on the movement, but the said law is not one directly imposing restrictions on the free movement."

74. Justice Hidayatullah adopted the position that a tax would amount to a restriction when it is placed upon trade directly and immediately. But, in his view, a distinction would have to be drawn between a tax which is paid by tradesmen in common with non-tradesmen and a tax upon trade. A tax which is imposed upon trade, as such, must be distinguished from general taxes imposed for the purposes

> "125.That a tax is a restriction when it is placed upon a trade directly and immediately may be admitted. But there is difference between a tax which burdens a trader in this manner and a tax, which being general, is paid by tradesmen in common with others. The first is a levy from the trade by reason of its being trade, the other is levied from all, and tradesmen pay it because everyone has to pay it. There is a vital difference between the two, viewed from the angle of freedom of trade and commerce. The first is an impost on trade as such, and may be said to restrict it; the second may burden the trader, but it is not a restriction' of the trade. To refuse to draw such a distinction would mean that there is no taxing entry in Lists I and II which is not subject to Articles 301 and 304, however general the tax and however non-discriminatory its imposition."

75. Justice Hidayatullah accepted the notion of facilitative regulations such as traffic rules and rules of the road. Such regulatory provisions, in his view, are not restrictions at all since they do not hamper trade or impair its freedom. Consequently, a fee for rendering services to the trade would not hamper or restrict it. Similarly, an administrative fee may also be viewed as a part of regulation and would not fall to be classified as a restriction. A tax however, which is a condition precedent to the right to enter upon and carry on business stands on a different footing :

> "131. Let us now see whether the validity of taxation laws directly impinging on trade and commerce can be upheld on the ground that they are regulatory. Here, a distinction must be made between fees and taxes. Fees charged as quid pro quo for services rendered or as representing administrative charges are quite different from taxes, pure and simple. Fees may partake of regulation when they are demanded to enable Government to meet the cost of administration. But the tax, with which we are concerned, is hardly a fee in that narrow sense. It is a tax for raising revenue."

Justice Hidayatullah dissented from the judgment of the majority on the ground that the tax in question was evidently not a fee for administrative purposes nor could it be justified as representing a payment for services. The object of the tax was to raise revenue, which distinguished it from a fee.

76. The correctness of the decision in Automobile Transport - as indeed of the earlier decision in Atiabari - lies at the heart of this reference. At this stage, it would be necessary to recapitulate the basic principles which emerged from Automobile Transport. The decision and the principles which it proceeds to formulate have their own logic. First, Automobile Transport enunciates that the freedom under Article 301 is consistent with facilitative regulations which enhance, rather than hinder trade. Second, though the power to tax is an essential attribute of government, it is subject to constitutional limitations including amongst them Part XIII of the Constitution. As a consequence, tax laws are not as a matter of principle outside the ambit of Article 301. Third, the test to be applied in determining whether a law infringes the freedom guaranteed by Article 301 is whether the direct and immediate effect is to hinder the movement of trade. A law which has that effect, including a tax law must, where it has been enacted by the state legislature be subject to the provisions of Article 304. Fourth, compensatory taxes which are imposed in consideration of the facilities which are provided by the state to trade and commerce are outside the ambit of Article 301. Fifth, a compensatory tax does not hinder the freedom of trade and commerce and need not comply with the requirements of the proviso to Article 304(b) of the Constitution.

E.2 Khyerbari

77. In Atiabari, an enactment of 1954 legislated by the State of Assam was found to be invalid. The state legislature then obtained the previous sanction of the President under Article 304(b) and proceeded to enact the Assam Taxation (on goods carried by road or on inland waterways) Act - 1961. A Constitution Bench dealt with the challenge to the new law *in Khyerbari Tea Co. Ltd. v. State of Assam*[98].

78. Justice Gajendragadkar who delivered the judgment of the majority held that the judgment in Automobile Transport introduced a "clarificatory rider" to the majority view in *Atiabari*[99] and that it had "substantially accepted" the ***earlier decision***[100]***.***

79. The opinion of Justice Gajendragadkar in Khyerbari seems to indicate an element of reservation in regard to the concept of compensatory taxes. Compensatory taxes, the judge noted, were evolved in conceptual terms in Australia in the context of Section 92 which is

[98] *(1964) 5 SCR 975*
[99] *Id. at p-985*
[100] *Id. at p. 986*

"absolute in terms" and on its "literal construction, admits of no exceptions". Justice Gajendragadkar indicated that the constitutional compulsions which led to the notion of compensatory taxes not being a hindrance to freedom being adopted in Australia were absent in India. Articles 302 to 304 specifically provide for the imposition of restrictions on the

freedom guaranteed by Article 301. Justice Gajendragadkar adverted to the minority view of Justice Hidayatullah in Automobile Transport on this aspect. His observations on the concept of compensatory taxes are as follows :

> "13. Section 92 is absolute in terms and on its literal construction, admits of no exceptions. The Australian decisions, therefore, had to introduce distinctions, such as compensatory or regulatory tax laws in order to take laws answering the said description out of the purview of Section 92. In our Constitution, however, though Article 301 is worded substantially in the same way as Section 92, Articles 302 and 304 provide for reasonable restrictions being imposed on the freedom of trade subject to the requirements of the said two articles, and so, the problem facing judicial decisions in Australia and in this country in regard to the freedom of trade and the restrictions which it may be permissible to impose on it, is not exactly the same. The minority view expressed by Hidayatullah, J. has pointedly referred to this aspect of the matter."

80. In Khyerbari, the judgment of the Supreme Court noted in more than one place that the tax in question had not been supported by the State of Assam on the ground that it was compensatory. Justice Gajendragadkar held that if the enactment had been claimed by the state to be compensatory, it would have been necessary to constitute a larger Bench to reconsider the position. This was because the state law of 1954 was enacted as a consequence of the earlier law having been invalidated in Atiabari. In Atiabari, the view of the majority was that such a tax (even if compensatory) could be sustained only after complying with Article 304(b). The earlier law had been struck down 'though it was compensatory'. Justice Gajendragadkar found that it would be unfair to preclude the petitioners from contending that the compensatory character of the levy was not material to its validity under Part XIII. Justice Gajendragadkar accordingly held as follows :

> "14.. If in the present case, it had been urged before us that the tax levied by the Act is compensatory in character, it would have been necessary to consider the question once again by constituting a larger Bench. It will be recalled that the Act with which we are concerned has been passed by the Assam Legislature directly as a result of the decision of this Court in Atiabari Tea Co. case [(1961) 1 SCR 809] ; that decision was that if the tax imposed by the Act was compensatory in character, then the Act could be sustained only if it was passed after complying with the provisions of Article 304(b). The Assam Legislature has accordingly adopted the said procedure and passed the Act. If the Act had been compensatory in character, it would have become necessary for us to consider the whole position once again, because it would obviously be unfair and unjust that the earlier Act should have been struck down though it was compensatory in character and in testing the validity of the present Act, it should be open to the petitioners to contend that its compensatory character is irrelevant to the enquiry under Article 304(b)."

81. A reference to the larger bench was however obviated since the High Court had held that Act not to be compensatory and no submission to the contrary was urged by

the state. The new enactment of the Assam Legislature was upheld against the challenge that it violated Articles 14, 19 and 301 :

> "45. It is, of course, true that the validity of tax laws can be questioned the light of the provisions of Articles 14, 19 and 301 if the said tax direct and immediately imposes a restriction on the freedom of trade; but the power conferred on this Court to strike down a taxing statute if it contravenes the provisions of Articles 14, 19 or 301 has to be exercised with circumspection bearing in mind that the power of the State to levy taxes for the purpose, governance and for carrying out its welfare activities is a necessary attribute sovereignty and in that sense it is a power of paramount character. In what case a taxing statute can be struck down as being unconstitutional is illustrated in the decision of this Court in K.T. Moopil Nair v. State of Kerala. [(1961) 3 SCR 77] It is in regard to such a taxing statute which can properly be regarded a purely confiscatory that the power of the court can be legitimately invoked and exercised".
>
> The law enacted by the state legislature was upheld in Khyerbari not on the ground that it was compensatory- such a justification having not been pressed by the state - but on the ground that its provisions were not violative of Articles 14, 19 and 301. The Act was not confiscatory and was held to pass muster under Articles 14, 19 and 301.

E.3 Subsequent applications_

82 Between 1962 and 1995, the working test adopted in Automobile Transport for determining whether a tax is compensatory was adopted largely in the context of motor vehicle taxes. See in this context the decisions in *S K Madar Saheb v. State of AP*[101]; *Bolani Ores Ltd v. State of Orissa*[102]; *G. K. Krishnan v. State of TN*[103]; *International Tourist Corpn. v. State of Haryana*[104]*; Malwa Bus Service (P) Ltd. v. State of Punjab*[105]; *Meenakshi v. State of Karnataka*[106]*; B.A. Jayaram v. Union of India*[107] *and State of Maharashtra v. Madhukar Balkrishna Badiya*[108]*.*

83. In *International Tourist Corporation v. State of Haryana* [109]*,* Justice O. Chinnappa Reddy speaking for a Bench of two Judges of this Court refined the test of a regulatory and compensatory tax by stipulating that there must exist a specific or identifiable object behind the levy and a nexus between the subject and the object. This Court held:

> "9.While in the case of a fee it may be possible to precisely identify and measure the benefits received from the Government and levy the fee according to the benefits received and the expenditure incurred, in the case of a regulatory and compensatory tax it would ordinarily be well nigh impossible to identify and measure, with any exactitude, the benefits received and the expenditure incurred and levy the tax according to the benefits received and the expenditure incurred. What is necessary to uphold a regulatory and compensatory tax is the existence of a specific, identifiable object behind the levy and a nexus between the subject and the object of the levy. If the object behind the levy is identifiable and if there is sufficient nexus between the subject and the object of the levy, it is not

necessary that the money realised by the levy should be put into a separate fund or that the levy should be proportionate to the expenditure." (Id. at p. 328)

Reading the nexus requirement into a compensatory tax represented the effort of this Court to bring clarity to the otherwise vague and uncertain core of a judicially evolved doctrine.

84 In *G K Krishnan v. State of Tamil Nadu*[110], a tax on motor vehicles under the Motor Vehicle Taxation Act, 1931 was under challenge on the ground of a violation of Article 301. By a notification, the rate of tax which was imposed on a quarterly basis was enhanced. Justice K K Mathew who delivered the judgment of a Bench of three Judges of this Court observed that the judgment in Automobile Transport "practically overruled" the decision in Atiabari :

> "13 insofar as it held that if a State Legislature wanted to impose tax to raise moneys necessary in order to maintain roads, that could only be done after obtaining the sanction of the President as provided in Article 304(b)".
>
> (Id. At p. 380)
>
> Justice Mathew held that there is a clear distinction between a law which interferes with the freedom to trade and a law which merely regulates :
>
> "14....The word "free" in Article 301 does not mean freedom from regulation. There is a clear distinction between laws interfering with freedom to carry out the activities constituting trade and laws imposing on those engaged therein rules of proper conduct or other restraints directed to the due and orderly manner of carrying out the activities. This distinction is described as regulation. The word "regulation" has no fixed connotation. Its meaning differs according to the nature of the thing to which it is applied. The true solution, perhaps, in any given case, could be found by distinguishing between features of the transaction or activity in virtue of which it fell within the category of trade, commerce and intercourse and those features which, though invariably found to occur in some form or another in the transaction or action are not essential to the conception. What is relevant is the contrast between the essential attribute of trade and commerce and the incidents of the transaction which do not give it necessarily the character of trade and commerce. Such matters relating to hours, equipment, weight/size of load, lights, which form the incidents of transportation, even if inseparable, do not give the transaction its essential character of trade or commerce. Laws for Government of such incidents "regulate". (Id. at p. 381)

85. The Bench of three Judges, following the line of precedent in Automobile Transport held that for a law to become a prohibited tax, it has to be a direct tax, the effect of which is to hinder the movement part of trade. A tax which is compensatory or regulatory does not however operate as a restriction on the freedom under Article 301. The nature of a compensatory tax was considered in the following observations :

> "17. Strictly speaking, a compensatory tax is based on the nature and the extent of the use made of the roads, as for example, a mileage or ton-mileage charge or the like, and if the proceeds are devoted to the repair, upkeep, maintenance and depreciation of relevant roads and the collection of the exaction involves no substantial interference with the movement. The expression "reasonable compensation" is convenient but vague. The standard of reasonableness can only lie in the severity with which it bears on traffic and such evidence of extravagance in its assessment as comes from general considerations. What is essential for the purpose of securing freedom of movement by road is that no pecuniary burden should be placed upon it which goes beyond a proper recompense to the State for the actual use made of the physical facilities provided in the shape of a road. The difficulties are very great in defining this conception. But the conception appears to be based on a real distinction between remuneration for the provision of a specific physical service of which particular use is made and a burden placed upon transportation in aid of the general expenditure of the State. It is clear that the motor vehicles require, for their safe, efficient and economical use, roads of considerable width, hardness and durability; the maintenance of such roads will cost the government money. But, because the users of vehicles generally, and of public motor vehicles in particular, stand in a special and direct relation to such roads, and may be said to derive a special and direct benefit from them, it seems not unreasonable that they should be called upon to make a special contribution to their maintenance over and above their general contribution as taxpayers of the State. If, however, a charge is imposed, not for the purpose of obtaining a proper contribution to the maintenance and upkeep of the road, but for the purpose of adversely affecting trade or commerce, then it would be a restriction on the freedom of trade, commerce or intercourse." (Id. at p. 382)

86. The Bench of three Judges in G K Krishnan (supra) was bound by the view which was taken by a larger Bench of seven Judges in Automobile Transport. The above extract however, indicates the difficulties which the Court noticed in applying concepts such as "reasonable compensation", an expression, which however convenient, is but vague. The Court noticed the rationale for the doctrine of compensatory taxes: providing recompense to the state for the provision of services which facilitate trade. A compensatory tax is distinguished from a general measure of taxation. The state may impose the tax as a part of raising revenues in aid of the general expenditure of the state. Though, all revenues of the state in the ultimate analysis are expended for public purposes, a burden imposed as a part of raising resources for meeting general expenditure is not compensatory. A compensatory tax in terms of the concept evolved by the Supreme Court in Automobile Transport is to provide a proper recompense to the state for the provision or use of all facilities made available to trade and commerce.

87. Justice Mathew, observed that in such matters, a rough approximation rather than a mathematically accuracy is what is required. The law imposed by the state legislature was held to pass muster of judicial review.

88. The judgment in G K Krishnan (supra) is also noteworthy because it raises the issue

as to whether the restrictions contemplated by Article 304(b) would include the levy of a non-discriminatory tax. Justice Mathew held that it was strange that the power to impose a tax conferred upon the states should yet depend upon the sanction of the President under the proviso to Article 304(b) :

> "27. Whether the restrictions visualized by Article 304(b) would include the levy of a non-discriminatory tax is a matter on which there is scope for difference of opinion. Article 304(a) prohibits only imposition of a discriminatory tax. It is not clear from the article that a tax simpliciter can be treated as a restriction on the freedom of internal trade. Article 304(a) is intended to prevent discrimination against imported goods by imposing on them tax at a higher rate than that borne by goods produced in the State. A discriminatory tax against outside goods is not a tax simpliciter but is a barrier to trade and commerce. Article 304 itself makes a distinction between tax and restriction. That apart, taxing powers of the Union and States are separate and mutually exclusive. It is rather strange that power to tax given to States, say, for instance, under Entry 54 of List II to pass a law imposing tax on sale of goods should depend upon the goodwill of the Union Executive. It is said that a tax on sale does not impede the movement of goods. But Shah, J. said in State v. Nataraja [AIR 1969 SC 147 : (1968) 3 SCR 829 : (1968) 22 STC 376] : "that tax under Central sales tax on inter-State sale, it must be noticed, is in its essence a tax which encumbers movement of trade and commerce." (Id. at p. 385) Justice Mathew also observed that the Court was not called upon to make any pronouncement on whether there was any warrant to restrict Article 301 to the movement part of trade and commerce. However, as the court held, it was unnecessary to pursue the matter any further as the tax imposed under the notification of the state in that case was held to be compensatory in character and hence not restrictive of the freedom.

E.4 The breaking point

89. The judgment in Automobile Transport held that compensatory taxes lie outside the purview of Article 301. Justice Mathew while upholding that the Madras Motor Vehicles Taxation Act, 1931 had cautioned in G K Krishnan (supra) that the concept of reasonable compensation is "convenient but vague" and emphasized "very great" difficulties in defining it. The issue came to the fore in M/s *Bhagatram Rajeev Kumar v. Commissioner of Sales Tax, M.P*[111]. An entry tax was imposed on goods such as sugar on which no sales tax is leviable, under the Madhya Pradesh Sthaniya Kshetra Me Mal Ke Pravesh Par Kar Adhiniyam, 1976. No sales tax could be levied on sugar since it is one of the goods on which additional excise duty is leviable under the Additional Duties of Excise Act, 1957. This Court held that though sugar was a commodity on which no sales tax is leviable because additional excise duty is payable, it was within the taxing provisions of the entry tax legislation. There was a challenge to the entry tax law on the ground that it violated Article 301 and that it was not regulatory or compensatory. A Bench of three Judges of this Court held that the figures which had been disclosed by the state as justification for the levy as a compensatory tax were not disputed. However, the Bench reformulated the test of what constitutes a compensatory tax in the following observations :

> "8 The concept of compensatory nature of tax has been widened and if there is substantial or even some link between the tax and the facilities extended to such dealers directly or indirectly, the levy cannot be impugned as invalid. The stand of the State that the revenue earned is being made over to the local bodies to compensate them for the loss caused, makes the impost compensatory in nature, as augmentation of their finance would enable them to provide municipal services more efficiently, which would help or ease free flow of trade and commerce, because of which the impost has to be regarded as compensatory in nature, in view of what has been stated in the aforesaid decisions, more particularly in Hansa Corpn. Case." (Id. at p. 678)

90. These observations made a marked departure from the test which was adopted in the judgment of seven Judges in Automobile Transport. The test of a compensatory tax as formulated in Automobile Transport is whether the trade has the use of facilities for the conduct of its business and is required to pay not patently much more than what is required for providing the facilities. In a substantially watered down redefinition of the test, Bhagatram required a "substantial or even some link" between the tax and the facilities extended "directly or indirectly". The underlying basis or foundation for regarding a tax as compensatory was almost obliterated. The reference in Bhagatram to the earlier decision in *State of Karnataka v. Hansa Corporation* [112], clearly overlooks that in that case the state had made no effort to sustain the validity of the tax on the ground that it was compensatory in character. Hence, the Bench in Hansa Corporation expressly clarified that it was not necessary for the Court to examine whether the tax was compensatory. Yet, the decision in Hansa Corporation was construed in Bhagatram to be an authority for the proposition that even some link between the facilities provided and the payment demanded, whether direct or indirect, would suffice.

91. The decision in Bhagatram was followed by another Bench of two judges in *State of Bihar v. Bihar Chamber of Commerce*[113]. At issue was an entry tax imposed by the Bihar (Tax on Entry of Goods into Local Areas for Consumption, Use or Sale therein), 1993. The High Court had held the Act to be invalid on the ground that the state had not disclosed material to justify that it was compensatory or regulatory nor had the state fulfilled the requirements of Article 304(b). The submission of the state in appeal was that the enactment was intended by the state legislature to offset atleast in part the loss of revenue caused to it, as a result of a decision of this Court *in India Cement Ltd. v. State of Tamil Nadu*[114]. The state submitted that due to a loss of revenue from the cess on minerals, it was necessary for the state to find alternative sources of revenue to support its welfare schemes. The money raised would, it was asserted, be spent for the welfare of the state, which was divided into local areas. Moreover, it was urged that even if the levy was not compensatory, the assent of the President had been obtained under Article 304(b) read with Article 255. The enactment was held to be compensatory. The following tests were laid down:

> "12....It is not and it cannot be stipulated that for the purpose of establishing the compensatory character of the tax, it is necessary to establish that every rupee collected on account of the entry tax should be shown to be spent on providing

the trading facilities. It is enough if some connection is established between the tax and the trading facilities provided. The connection can be a direct one or indirect one, as held by this Court in Bhagatram Rajeevkumar v. CST [1995 Supp (1) SCC 673 : (1995) 96 STC 654] : (SCC p. 678, para 8)

..“The concept of compensatory nature of tax has been widened and if there is substantial or even some link between the tax and the facilities extended to such dealers directly or indirectly the levy cannot be impugned as invalid” Though not stated in the counter-affidavit, we can take notice of the fact that the State does provide several facilities to the trade including laying and maintenance of roads, waterways and markets, etc. As a matter of fact, since the levy is by the State, we must also look to the facilities provided by the State for ascertaining whether the State has established the compensatory character of the tax.”

(Id. at p. 147) The Court in Bihar Chamber of Commerce held that so long as “some connection is established between the tax and the trading facilities provided” the levy would be held to be compensatory in character.

92. These decisions were doubted by a Bench of two-Judges in *Jindal Stripe Ltd. v. State of Haryana*[115].

93. Jindal Stripe involved a batch of appeals raising a challenge to the Haryana Local Area Development Tax Act, 2000 on the ground that it was “violative” of Article 301 and was not saved by Article 304. A Bench of two judges held that the decisions in Bhagatram and Bihar Chamber of Commerce seem to have deviated from the principles underlying the imposition of a compensatory tax which had held the field from 1962 to 1995. In the view of the referring Bench, if the test enunciated in the above two cases was to be accepted as the position in law, any tax could pass the test of a compensatory tax without infringing upon the freedom ordained by Article 301. The reference was heard by a Constitution Bench in *Jindal Stainless Ltd.(2) v. State of Haryana* [116], The Constitution Bench in Jindal Stainless elucidated the difference between regulatory and taxing powers. Taxing legislation, the Court ruled, is based on the concept of burden and on the principle of ability to pay. On the other hand, regulatory charges are a recompense for the costs or expenses incurred by the state for the provision of services or facilities:

“31.. .Suffice it to state at this stage that the basis of special assessments, betterment charges, fees, regulatory charges is “recompense/reimbursement” of the cost or expenses incurred or incurrable for providing services/facilities based on the principle of equivalence unlike taxes whose basis is the concept of “burden” based on the principle of ability to pay. At this stage, we may clarify that in the above case of Automobile Transport [(1963) 1 SCR 491 : AIR 1962 SC 1406], this Court has equated regulatory charges with compensatory taxes and since it is the view expressed by a Bench of seven Judges, we have to proceed on that basis. The fallout is that compensatory tax becomes a sub-class of fees”. (Id.at p. 264) Based on this distinction, the Constitution Bench held that if a law, fiscal or otherwise, operates upon the movement

of trade or commerce and its effect is to impede that activity, the law would constitute a restriction under Article 301. However, if the law seeks to enforce a payment for regulation of conditions or incidents of trade, it is regulatory in character:

"38 If the impugned law seeks to control the conditions under which an activity like trade is to take place then such law is regulatory. Payment for regulation is different from payment for revenue. If the impugned taxing or non-taxing law chooses an activity, say, movement of trade and commerce as the criterion of its operation and if the effect of the operation of such a law is to impede the activity, then the law is a restriction under Article 301. However, if the law enacted is to enforce discipline or conduct under which the trade has to perform or if the payment is for regulation of conditions or incidents of trade or manufacture then the levy is regulatory." (Id. at p. 266)

94. The Constitution Bench held that taxes are levied as a part of the common burden. While the foundation of a fee is "the principle of equivalence", the basis of a tax is ability to pay. The main basis of a fee or a compensatory tax is an equivalence and a "quantifiable measurable benefit". A compensatory tax has to be broadly proportional :

"42...Compensatory tax is based on the principle of "pay for the value". It is a sub-class of "a fee". From the point of view of the Government, a compensatory tax is a charge for offering trading facilities. It adds to the value of trade and commerce which does not happen in the case of a tax as such. A tax may be progressive or proportional to income, property, expenditure or any other test of ability or capacity (principle of ability). Taxes may be progressive rather than proportional. Compensatory taxes, like fees, are always proportional to benefits. They are based on the principle of equivalence. However, a compensatory tax is levied on an individual as a member of a class, whereas a fee is levied on an individual as such. If one keeps in mind the "principle of ability" vis-a-vis the "principle of equivalence", then the difference between a tax on one hand and a fee or a compensatory tax on the other hand can be easily spelt out." (Id. At p. 267)

95. The Constitution Bench held that a compensatory tax is a compulsory contribution levied broadly in proportion to the special benefits derived to meet the costs of regulation or an outlay which is incurred to provide a special advantage to trade, commerce and intercourse. Whenever a law is impugned as being violative of Article 301, the Court must determine whether the enactment facially or patently indicates quantifiable data on the basis of which the compensatory tax is sought to be levied. The statute must broadly indicate a proportionality to a quantifiable benefit. Even if the statute were not to indicate this, the state may discharge the burden cast upon it by producing material to indicate that the payment of the compensatory tax is a reimbursement or recompense for a quantifiable/measurable benefit provided or to be provided to the payer of the tax. The reference was answered by the Constitution Bench by holding that the test of what constitutes a compensatory tax had been substantially altered by the decisions in Bhagatram and Bihar Chamber of Commerce in a manner which was inconsistent with the judgment of seven Judges in Automobile Transport. In

holding that ‘some connection’ or ‘some link’ between the tax and the facilities extended would suffice, ‘whether direct or indirect’, the judgments in the Bhagatram and Bihar Chamber of Commerce were held to have deviated from the settled concept of compensatory taxes and were hence overruled.

E.5Doctrinal concerns and inconsistencies

96. The theory of compensatory taxes was evolved in Automobile Transport to assimilate doctrinal concerns at several levels. Freedom of trade and commerce under Article 301 of the Constitution is expressly made subject to the provisions of Part XIII. The deliberate use of the expression ‘free’ instead of “absolutely free” (the latter expression being adopted in the Australian Constitution) coupled with the language of Article 301 which subjects its provisions to Part XIII is indicative of the fact that the freedom which is guaranteed is subject to legislative control. Articles 302, 303 and 304 are a part of the constitutional scheme which, while defining the ambit of the freedom in Article 301 subjects it to restrictions under Articles 302 and 304. The nature of the restrictions and the limitations on the power of Parliament and of the state legislatures while legislating to impose restrictions is conditioned by constitutional parameters. The conditions are based on the fulfilment of substantive and procedural norms: substantive such as the principle of non-discrimination, the element of public interest and reasonableness; and procedural (if it can be regarded as a matter of procedure) by requiring the sanction of the President prior to the introduction of a Bill in the state legislature.

97. At a doctrinal level, the Court in Automobile Transport was cognizant of the fact that regulation of trade and commerce may, in fact, facilitate trade rather than impede its freedom. As the Court postulated, the freedom to trade does not mean a freedom to trade in chaos. Conditions of chaos are destructive of an orderly society. Conditions which ensure a disciplined and orderly conduct of trade and commerce facilitate trade. Trade also pre-supposes the existence of infrastructure and the provision of facilities for pursuing the avenues of commerce and trade. The state which provides those facilities has a legitimate interest in recovering the costs which it incurs. In the absence of resources generated by charges levied for the use of facilities, the state may not have the wherewithal to provide the facilities in the first place. Hence, when the concept of compensatory taxes was devised, Justice S K Das, in Automobile Transport adverted to collections made for the use of trading facilities, such as roads, bridges and airports. “Such compensatory taxes” as the judgment held, were not a hindrance to anyone’s freedom so long as they remain reasonable. So long as the tax was compensatory or regulatory, it did not operate as a hindrance. In another part of the judgment, Justice Das held that a regulatory measure or measures imposing compensatory taxes for the use of trading facilities did not fall within the purview of restrictions contemplated by Article 301 and did not have to comply with the requirements of the proviso to Article 304(b).

98. The judgment in Automobile Transport indicates that a second doctrinal concern which weighed with the Court was a dilution of the sovereign power to tax conferred upon the states if all fiscal legislation was required to pass muster of a Presidential

sanction under the proviso to Article 304(b). This concern was present to the mind of the Court in Automobile Transport, when Justice Das observed that if all legislation of the state legislatures which has a repercussion on tariffs, licensing, marketing regulation and price control was required to proceed through a prior Presidential sanction, the plenary power of the states in the fields of legislation allocated to them would be meaningless. The theory of compensatory taxes was an answer to this conundrum. So long as the tax retained a compensatory character, it did not fall within the fold of Article 301. If a compensatory tax does not offend Article 301, the provisions of Article 304(b) are not attracted. In the same vein, Justice Subba Rao cautioned against a construction of Part XIII that would render the states as "the handmade of the central executive". Besides the 'direct and immediate' test which the learned judge considered to be a "reasonable solvent", Justice Subba Rao also adverted to a tax which is compensatory or regulatory not operating as a restriction on the free movement of trade.

99. Compensatory taxes were envisaged as a doctrinal concept to preserve an area where the sovereignty of the state legislatures in fiscal matters could operate without the constraining influence of a prior Presidential sanction. Such taxes would not fall within the ambit of Article 301. Their position was reconciled with freedom on the ground that a compensatory tax for the use of facilities is not a hindrance to trade but facilitates it.

100. The difficulties that the concept of compensatory taxes would encounter had their seeds in the formulation in Automobile Transport itself. The judgment of Justice Das used the concept in varying contexts as a tax for the use of facilities and, in other places, as a tax to provide facilities. Use relates to the availment of a facility. Providing for facilities emphasises the role of the state in terms of the investment which it incurs and the expenditure required for upkeep and maintenance. Use and provision may be two shades of the same coin but they have their own distinctions. The concept of compensatory taxes was by its very nature formulated in terms which were vague and not capable of precise definition. The judgment of the majority in Automobile Transport speaks of compensatory taxes not being a hindrance, so long as they are reasonable. Moreover, the working test that was adopted in the judgment made it clear that it was not the precise or specific amount that is collected that is required to be expended for providing facilities. The working test is that the trade which has the use of facilities for the better conduct of business does not pay 'patently much more' than what is required for providing the facilities. 'Paying not patently much more' is a concept which suffers from vagueness. How much more is within the ambit of the phrase 'not patently much more' introduces an element of subjectivity. A standard which is subjective becomes uncertain and indefinite in its practical application. The lack of precision about what constitutes a compensatory tax undoubtedly did furnish to the Court and to the process of judicial review a measure of flexibility to preserve the sovereignty of the state legislatures. The difficulties which would be encountered however became evident, when the three judge Bench in Bhagatram and the two judge Bench in Bihar Chamber of Commerce rested the decision on a "some connection" or "some link" requirement. If some connection or some link were to suffice, the whole notion of compensatory taxes being a means of recouping the states for the cost of providing facilities to the trade

would tend to disappear. In fact, as the decision in Bhagatram indicated, the compensatory aspect of the tax which was upheld in that case was a loss which was sustained by the state as a result of sugar not being amenable to sales tax (being a commodity on which an additional duty of excise was leviable). Similarly, in Bihar Chamber of Commerce, the state had sought to sustain the tax as compensatory on the ground that the loss of revenue sustained from the cess upon minerals, as a result of a judgment of the Supreme Court, had to be made up by tapping an alternative source of revenue. These two decisions showed that the concept of compensatory taxes was understood by the states not as a method of compensating a state for the provision of infrastructure and facilities to the trade but as a measure to recover a loss of revenue under another head. If compensatory taxes were to mean compensation for the loss of state revenue under some other head, the theory which found acceptance in the two decisions of this Court had travelled far beyond the domain that was contemplated in Automobile Transport. Correctly, therefore, both the decisions in Bhagatram and in Bihar Chamber of Commerce were overruled in Jindal Stainless. However, both the decisions led to subjectivity, uncertainty and vagueness.

101. A close reading of the decision in Jindal Stainless indicates that while the earlier decisions in Bhagatram and in Bihar Chamber of Commerce were overruled, the pendulum had swung to the other extreme. The Constitution Bench in Jindal Stainless proceeded to explain the basis of the "judicially evolved concept" of compensatory taxes by distinguishing a tax which is based on the principle of ability to pay from a fee which is based on the principle of equivalence. Compensatory taxes, the Constitution Bench held, constitute a sub-class of a fee and are based on the principle of "pay for value". In holding that the collection on account of a compensatory tax must be "broadly in proportion" to the special benefits derived to defray the costs of regulation or to meet the outlay incurred, the Constitution Bench was restating the working test of Automobile Transport. But the subsequent observations in Jindal Stainless make it evident that the Constitution Bench introduced a near mathematical formulation which would not be consistent with the test which was propounded in Automobile Transport. The judgment of the Constitution Bench requires that the enactment which imposes a compensatory tax must facially or patently, indicate quantifiable data and a benefit which is quantifiable or measurable. The Court held that however, where a statute did not to do so, the burden would lie on the state as a service provider to produce material indicating that the payment of the tax is a reimbursement or recompense for a quantifiable/measurable benefit. These observations bring the concept of a compensatory tax in line with a fairly strict application of a quid pro quo principle which had not been accepted in Automobile Transport. In fact, the Bench of seven Judges in Automobile Transport had specifically clarified that the precise amount that is realized need not be spent on the provision of facilities and the only requirement is that the trade should not be made to pay patently much more than what is incurred for the provision of the facilities. The observations in Jindal Stainless requiring the establishment of a nexus or relationship between a quantifiable or measurable benefit and a reimbursement/recompense to the state are contrary to and inconsistent with the law which was laid down in Automobile Transport.

102. Evidently, both Justice Gajendragadkar in Khyerbari and Justice Mathew in G. K.

Krishnan had reservations about the concept of compensatory taxes. Justice Gajendragadkar recorded his reservations because the predecessor of the enactment of the state legislature of Assam in issue in Khyerbari had been struck down in the decision in Atiabari. The majority in Atiabari had held the tax to be invalid for want of compliance with the proviso to Article 304(b) despite its compensatory character. Justice Gajendragadkar held that if the new enactment, which had been brought into force after complying with the proviso to Article 304(b) was to be supported by the state as being compensatory in character, a reference to a larger Bench would have been necessitated. That, however, did not become necessary because the State of Assam did not support the enactment as being compensatory before the Supreme Court. These observations of Justice Gajendragadkar were in the decision rendered in 1964 in Khyerbari. Eleven years later, Justice Mathew in an eloquent judgment in G.K. Krishnan spoke about the expression 'reasonable' being convenient but vague. The judge stressed that that were very difficulties in defining this conception. The Constitution Bench in Jindal Stainless was bound by the doctrine of compensatory taxes which had been formulated by a larger Bench of seven Judges in Automobile Transport. The validity of the compensatory tax theory was not under challenge.

103. The judicially evolved concept of compensatory taxes has created in its wake new problems in its search for solutions. If a strict reading of the doctrine of compensatory taxes in terms of the 'quantifiable/measurable benefits' approach is adopted (as did the Constitution Bench in Jindal Stainless) the formulation assumes the character of a strict application of a quid pro quo test. A compensatory tax is then a fee properly so called. The Constitution, in the legislative entries contained in the Lists in the Seventh Schedule classifies taxes and fees under distinct heads. If a compensatory tax were to assume the character of a fee, that raises the question as to whether the concept has any utility in the first place. If, on the other hand, the concept of compensatory taxes were to have a loose and undefined ambit, by the application of the 'some link' or 'some connection' test (as was adopted in Bhagatram and Bihar Chamber of Commerce), then any connection would suffice for a tax to be called compensatory. Both these approaches which are extreme in their own way are contrary to the law laid down by seven Judges in Automobile Transport. Bhagatram and Bihar Chamber of Commerce render the concept so loose and undefined as to denude it of its rationale. Jindal Stainless while overruling these decisions adopted a strict standard which was not contemplated by Automobile Transport. Bhagatram and Bihar Chamber of Commerce were overruled in Jindal Stainless as being contrary to the test laid down in Automobile Transport. But as we have seen, the quantifiable/measurable benefit test laid down in Jindal Stainless by the Constitution Bench is itself replete with doctrinal problems, besides its patent inconsistency with Automobile Transport. If both these extremes are to be avoided, we are left with the middle ground which the decision in Automobile Transport sought to adopt. However, the basic conception of compensatory taxes as propounded in Automobile Transport is vague and indefinite and has produced a maze of doctrinal uncertainty, if not chaos in constitutional litigation. As this batch of appeals indicates, the state legislatures have amended their entry tax legislation to incorporate specific statutory provisions indicating the manner in which the proceeds of the tax would be utilized so as to enable the tax to approximate a compensatory tax. Once the state legislature has done so, by adopting statutory provisions, would the Court have

either the expertise or the competence to second guess the basis which has been made by the state legislature? The answer to that would necessarily have to be in the negative. The Court cannot assume the character of an accountant overseeing the balance sheets of income and expenditure and enquiring into capital account investments made by the states. Such matters do not lie within the competence or ken of judicial review. More fundamentally, all tax revenues are utilised by the state for public purposes. All taxation being in aid of the creation of conditions of social order, a compensatory element can never be disassociated from taxation. Equally insofar as fees are concerned, the payment which is required to be made is not always voluntary. The contribution exacted from trade and commerce may not always be for the actual use of a facility but may be for the provision of the facility which trade and commerce is entitled to use. The state expends large budgets on providing expenditure to maintain law and order and security. The distinction between a tax and a fee has become blurred in our jurisprudence and Courts have found it difficult to find a clear dividing line.

104. A doctrinal irrationality which the theory of compensatory taxes fails to meet is a discriminatory compensatory tax. Discriminatory taxes which single out goods originating in other states to hostile discrimination violate Article 304(a). If compensatory taxes as a class fall outside Part XIII, this would include even those compensatory taxes which are discriminatory. While holding that compensatory taxes fall outside Part XIII, the theory propounded by this Court did not account for the position that discriminatory compensatory taxes constitute an impediment to trade and commerce, thereby violating Article 301.

105. Hence, the notion of compensatory taxes is beset with doctrinal problems. The concept has led to uncertainty and vagueness and has produced inconsistencies in constitutional adjudication. Constitutional adjudication must avoid these uncertainties which result in a multiplication of litigation and uncertainty both to the revenue and to the tax payer. Uncertainty in the application of fiscal legislation leads to a situation where tax compliance is beset with interpretational and practical difficulties. A concept which is replete with such evident problems is best eschewed.

F The content of freedom : goods, services, persons and capital

106. Article 301 has guaranteed the freedom of trade, commerce and intercourse (subject to the provisions of Part XIII). Article 19(1)(g) guarantees to every citizen the right to carry on any occupation trade or business. At a certain level, a distinction can be drawn between the two sets of freedoms. Article 19(1)(g) guarantees individual freedom. Article 301, on the other hand, looks at trade, commerce and intercourse as a whole. Such a distinction however may have its own limitations. Individual rights of all citizens protected by Article 19 lead to the establishment of a constitutional democratic order governed by the rule of law and based on human freedom. The dichotomy that Article 301 in its perspective looks at trade and commerce as a whole (as distinguished from an individual right) may also have its own limitations. The freedom recognised by Article 301 is enforceable. Enforceability is at the behest of an individual. In the constitutional recognition of freedom dwells the constitutional right of the individual to enforce it and to secure remedies for enforcing wrongs. The real content of freedom lies

in the right which inheres in it and in the protection of the individual to enforce the right. The freedoms guaranteed by Article 301 are enforceable at the instance of individuals who are aggrieved by state action. Thus, a distinction between Article 19(1)(g) and Article 301on the basis of the former reflecting an individual right as opposed to a collective entitlement under the latter may not be completely accurate. Though, one is an enforceable fundamental right of a citizen while the other is a recognition of the free flow of trade, commerce and intercourse, both in essence are enforceable, and enforceable at the behest of aggrieved individuals. A more nuanced perspective with regard to both sets of rights recognises that both reflect shades of the same universe of freedom.

107. Indian society and the economy have evolved between the advent of the Constitution and the present in a manner that would appear unrecognisable between 1950 and now. The entrepreneurial spirit of the nation has resulted in a diversification of the economy. A predominantly agricultural economy at the birth of the Constitution has increasingly found change in the last seven decades with the enhancement of the manufacturing base, and in more recent times to the diversification into services, especially financial services. The age of the internet was yet to dawn when the Constitution was adopted. The internet with its powerful tools for the dissemination of knowledge and information has provided new avenues for business, trade and commerce. The ambit of Article 301 must in a contemporary context incorporate all avenues of trade, commerce and intercourse and the instrumentalities by which they flourish.

108. Trade and commerce do not exist in a vacuum. The channels of trade and commerce require a stable social order for business transactions to be concluded, for contracts to be fulfilled and for commercial dealings to be enforced in law. The sanctity of contracts, secure conditions for trade and commerce and conditions which ensure an ease of doing business are supported by the state which has a vital role in the preservation of the rule of law. The meaning of the guarantee under Article 301 must in a modern context accommodate the needs and aspirations of business that would allow for economic development and growth to take place in the nation. Fundamentally the creation of a common market for goods and services requires the removal of obstacles to the free movement of goods, persons, services and capital between the states which constitute the Union of India. These four fundamental freedoms are the foundation of Article 301. The free movement of goods constitutes the traditional domain of trade and commerce. Our Constitution in its recognition of the freedom of intercourse protects the movement of persons engaging in commercial intercourse. Trade and commerce has diversified into services which constitute a vital element in the economic life of the nation. The movement of capital is the foundation for trade and commerce. Capital provides the foundation for business. These four freedoms guaranteeing the free movement of goods, services, persons and capital between the states, form the basis of the guarantee under Article 301. Commercial transactions by which the free movement of each constituent element takes place fall within the ambit of the freedom.

G Taxation and Federalism

109. In determining an interpretation that would bring a balance between the diverse strands of Part XIII, it is necessary for the Court equally to bear in mind the needs of the federal structure. The doctrine of the basic structure of the Indian Constitution has evolved to incorporate federalism as one of its integral features.

110. The guarantee that trade, commerce and intercourse shall be free throughout the territory of India is subject to the provisions of Part XIII. The meaning of the expression "throughout the territory of India" is elucidated by Article 1 of the Constitution which stipulates that "India, that is Bharat, shall be a Union of States". The Union which the Constitution postulates is defined in terms of a political union and an economic union which brought together the erstwhile provinces of British India and the princely states. The freedom under Article 301 comprehends, as we have seen, the free movement of goods, services, persons and capital. These are essential ingredients in the creation of a common market as an incident of an economic union. The freedom under Article 301 is not absolute for, the constitutional guarantee is subject to the provisions of Part XIII. The provisions of Article 302 to Article 304 bring about a balance between the guarantee of freedom on one hand and legislative control over trade and commerce on the other hand. While doing so, those articles define the powers of Parliament and the state legislatures, while subjecting them to restraints that are intended to preserve the power of regulating trade and commerce.

111. While the Constitution does in that sense subordinate the freedom under Article 301 to the provisions of Part XIII, it would not be correct to read the provisions of Part XIII in isolation. Part XIII is an integral element of the Constitution, but so are the other Parts under which executive and legislative powers are constitutionally conferred upon the structures of governance in the Union and the States. While construing the provisions of the Constitution it is necessary to construe the text in the context of the organic nature of the constitutional document. The linkages between various Parts of the Constitution contribute to the creation of a composite whole. No segment of the Constitution can be read in isolation. The scheme of the Constitution must hence be understood having regard to its history, text and context.

112. A Constitution Bench of this Court in *Kihoto Hollohan v. Zachillhu , emphasised*[117] the essential oneness of the Constitution when it held that:

> "26. In expounding the processes of the fundamental law, the Constitution must be treated as a logical whole. Westel Woodbury Willoughby in The Constitutional Law of the United States (2nd Edn. Vol. 1, p.65) states :
>
> "The Constitution is a logical whole, each provision of which is an integral part thereof, and it is, therefore, logically proper, and indeed imperative, to construe one part in the light of the provisions of the other parts"
>
> 27. A constitutional document outlines only broad and general principles meant to endure and be capable of flexible application to changing circumstances – a distinction which differentiates a statute from a Charter under which all statutes are made " (Id. at p.676) Words of the Constitution "cannot be read in isolation

and have to be read harmoniously to provide meaning and purpose" (*T.M.A Pai Foundation v. State of Karnataka*[118]*).*

113. The judgment of Justice Gajendragadkar, speaking for the majority in Atiabari, however construed the language of Article 301 to mean that the guarantee of freedom was subject only to the provisions of Part XIII. With respect, this does not constitute an appropriate approach to constitutional interpretation since it leads to a construction of Part XIII in isolation from other provisions which have a significant bearing on the nature of the freedom and its relationship with the structures of governance. To consider the guarantee under Article 301 as being subject only to Article 302 to 304 overlooks the relationship of Part XIII with other provisions of the Constitution. Freedom is integral to that relationship.

114 . The issue as to whether the Constitution creates a federal structure was debated upon in the Constituent Assembly. When the Draft Constitution was being discussed, T T Krishnamachari while supporting the view that the Constitution was to establish a federal structure observed thus :

> "the first criterion is that the State must exercise compulsive power in the enforcement of a given political order, the second is that these powers must be regularly exercised over all the inhabitants of a given territory, and the third is the most important and that is that the activity of the State must not be completely circumscribed by orders handed down for execution by the superior unit. The important words are 'must not be completely circumscribed', which envisage some powers of the State are bound to be circumscribed by the exercise of federal authority. Having all these factors in view, I will urge that our Constitution is a federal Dr. Ambedkar gave expression to the same thought in the following observations:
>
> "The basic principle of federalism is that the legislative and executive authority is partitioned between the Centre and the States not by any law to be made by the Centre but by the Constitution itself. This is what the Constitution does. The States under our Constitution are in no way dependent upon the Centre for their legislative or executive authority. The Centre and the States are coequal in this matter. It is difficult to see how such a Constitution can be called centralism. It may be that the Constitution assigns to the Centre too large a field for the operation of its legislative and executive authority than is to be found in any other federal Constitution. It may be that the residuary powers are given to the Centre and not to the States. But these features do not form the essence of federalism. The chief mark of federalism as I said lies in the partition of the legislative and executive authority between the Centre and the units by the Constitution. This is the principle embodied in our Constitution." (Id. at p.22)

115. A Bench of six Judges of this Court in *State of West Bengal v. Union of India* [119] dealt with whether the property of a state in coal bearing areas is immune from acquisition by the Union. This Court held that in the structures of constitutional governance that are created by the Constitution full sovereignty does not reside in the

states. Moreover, the Constitution contains a marked tilt in favour of the powers of the Union. Chief Justice B P Sinha adverted to the provisions of Part XIII "which seek to make India a single economic unit for purposes of trade and commerce under the overall control of the Union Parliament and the Union Executive[120] " Our Constitution, the Court held "was not true to any traditional pattern of federalism[121]." Legal sovereignty is vested in the people of India while political sovereignty is distributed between the Union and the States, with greater weight age in favour of the Union. In that context, this Court held that :

> "35. The normal corporate existence of States entitles them to enter into contracts and invests them with power to carry on trade or business and the States have the right to hold property. But having regard to certain basic features of the Constitution, the restrictions on the exercise of their powers executive and legislative and on the powers of taxation, and dependence for finances upon the Union Government, it would not be correct to maintain that absolute sovereignty remains vested in the States
>
> 36. The Parliamentary power of legislation to acquire property is, subject to the express provisions of the Constitution, unrestricted. To imply limitations on that power on the assumption of that degree of political sovereignty which makes the States coordinate with and independent of the union, is to envisage a Constitutional scheme which does not exist in law or in practice. On a review of the diverse provisions of the Constitution, the inference is inevitable that the distribution of powers– both legislative and executive does not support the theory of full sovereignty in the States so as to render it immune from the exercise of legislative power of the Union Parliament particularly in relation to acquisition of property of the States."
>
> (Id at p.396)

116. The evolution of constitutional doctrine in the five decades that have elapsed since the judgment in State of West Bengal (supra) indicates a recognition that the Constitution does indeed create a federal structure. Though the federal structure is asymmetric in the powers assigned to the states as compared to those assigned to the Centre this does not render the Constitution unitary. The Constitution is federal and in the working of a democratic Constitution, judicial review has stepped in to restore the balance despite the asymmetries of distribution and powers. The provisions of the Constitution which indicate a tilt in favour of the Union do not detract from the principle that in the fields which are assigned to them, the states are intended to be integral elements of a federal structure. They are sovereign within their competence, subject to constitutional limitations.

117. This principle was set forth in the following terms in Special Reference 1 of 1964[122] under Article 143 of the Constitution:

> "The supremacy of the Constitution is fundamental to the existence of a federal State in order to prevent either the legislature of the federal unit or those of the

member States from destroying or impairing that delicate balance of power which satisfies the particular requirements of States which are desirous of union, but not prepared to merge their individuality in a unity. This supremacy of the Constitution is protected by the authority of an independent judicial body to act as the interpreter of a scheme of distribution of powers. Nor is any change possible in the Constitution by the ordinary process of federal or State legislation." (para 38)

118. The constitutional position is authoritatively set forth in the judgment in *S.R. Bommai v. Union of India*[123] . Justice K. Ramaswami construed federalism to be a basic feature, in the following observations :

> "247. Federalism envisaged in the Constitution of India is a basic feature in which the Union of India is permanent within the territorial limits set in Article 1 of the Constitution and is indestructible Neither the relative importance of the legislative entries in Schedule VII, Lists I and II of the Constitution, nor the fiscal control by the Union per se are decisive to conclude that the Constitution is unitary. The respective legislative powers are traceable to Articles 245 to 254 of the Constitution. The State qua the Constitution is federal in structure and independent in its exercise of legislative and executive power. However, being the creature of the Constitution the State has no right to secede or claim sovereignty. Qua the Union, State is quasi-federal. Both are coordinating institutions and ought to exercise their respective powers with adjustment, understanding and accommodation to render socio-economic and political justice to the people, to preserve and elongate the constitutional goals including secularism."(Id. at p. 205) Justice B.P. Jeevan Reddy accepted the same doctrinal position in the following terms :
>
> "276. The fact that under the scheme of our Constitution, greater power is conferred upon the Centre vis-a-vis the States does not mean that States are mere appendages of the Centre. Within the sphere allotted to them, States are supreme. The Centre cannot tamper with their powers. More particularly, the courts should not adopt an approach, an interpretation, which has the effect of or tends to have the effect of whittling down the powers reserved to the States must put the Court on guard against any conscious whittling down of the powers of the States."(Id. At p. 216-217)

Justice P.B. Sawant, similarly held that though there are provisions under which the Centre has overriding powers over the states, our Constitution does create a federal structure. The states are sovereign in the fields which are left to them.

119. In ITC v. Agricultural Produce Market Committee , this Court emphasised that in interpreting the text of the Constitution the Court should ensure, where the language permits that the powers of the state legislatures are not diluted and that the principles of federalism are preserved (See also in this context Kuldip Nayar v. Union of India)

120. The federal constitutional doctrine has consequences for interpretation. In interpreting the text of the Constitution, the Court must construe the text in a manner

that would preserve the carefully crafted balance between the Union and the states. Where the language of the text permits, the effort of constitutional interpretation should be to ensure that the states are not subordinated to the Union in areas reserved to them. Yet it is equally a matter of constitutional doctrine that here a particular provision (such as the proviso to Article 304(b) imposes a specific requirement (assent of the President before a Bill is introduced in the state legislature) which subjects the legislative power of the states to constitutional limitations, it would not be open to the Court to ignore the plain meaning and effect of such a provision. The text of the Constitution cannot be subverted on the basis of an abstract notion or hypothesis. While creating a federal structure, the draftsmen of the Constitution were conscious of the need for preserving a political and economic Union. If, as a part of that constitutional scheme, the text of the document has incorporated specific provisions, they must be given their plain meaning and effect. It would not be open to the Court to dilute the meaning of the text on the basis of a priori considerations.

H Taxing powers H.1 Article 245 and constitutional limitations

121. Article 245 of the Constitution provides for the extent of laws made by Parliament and the legislatures of the states. Clause 1 of Article 245 enables Parliament "subject to the provisions of this Constitution" to make laws for the whole or any part of the territory of India and for the legislature of a state to make laws for the whole or any part of the state. Implicit in Article 245, which defines the territorial extent of laws enacted by Parliament and the state legislatures, is the power to enact laws. Defining the extent of the law making power with reference to territorial coverage presupposes the existence of a power to frame legislation in the first place. Hence Article 245 is the fountainhead of legislative power. It makes legislative powers subject to constitutional limitations. The distribution of legislative powers is embodied in Article 246 which deals with the subject matter of laws made by the Parliament and by the state legislatures. Parliament has exclusive powers to make laws with respect to matters enumerated in List I of the Seventh Schedule. Subject to the law making powers of Parliament in List I, the legislature of a state has exclusive power to enact law for the state with respect to any of the matters enumerated in List II. Parliament and the state legislatures have concurrent powers to enact legislation in respect of matters enumerated in List III. Article 245 is the source of legislative power. Article 246 distributes legislative powers between Parliament and the state legislatures on the basis of the Lists in the Seventh Schedule. Article 245, in the conferment of legislative powers upon Parliament and the state legislatures makes them subject to the provisions of the Constitution.

122.The power to enact laws is a manifestation of sovereignty. The Constitution while conferring legislative powers upon the Union and the states makes them subject to constitutional limitations. The sovereignty of the legislature is subject to the norms of the written constitution. The power to tax is subsumed in legislative power. Like all legislative power, fiscal legislation is subject to the mandate of the written constitution. This is the plain consequence of the opening words of Article 245(1) under which the conferment of legislative powers is made subject to the provisions of the Constitution.

123. The entries in the legislative lists of the Seventh Schedule are not sources of

legislative power but only define the subjects or heads of legislation entrusted to the law making competence of Parliament and the state legislatures. Read together, Articles 245 and 246 confer legislative power upon the Union and the states in the first place and distribute that power between them to enact legislation on the fields of legislation entrusted to their competence. Though Article 245 is made expressly subject to the provisions of the Constitution while there are no such similar words in Article 246, both Articles are subject to the other provisions of the Constitution. The language of Article 245 which subjects the conferment of legislative power to constitutional provisions is a recognition of the doctrinal principle that all constitutional power vesting in the organs of the state is subject to constitutional limitations. The Constitution which entrusts power conditions the entrustment to the observance of constitutional safeguards and limitations. All legislative power is subject to constitutional limitations.

124. In *State of Kerala v. Mar Appraem Kuri Co. Ltd* [126], this Court construed the relationship between Articles 245 and 246 in the following observations :

> "35...While the legislative power is derived from Article 245, the entries in the Seventh Schedule of the Constitution only demarcate the legislative fields of the respective legislatures and do not confer legislative power as such
>
> 36. Article 246 deals with the subject-matter of laws made by Parliament and by the legislatures of States. The verb "made" once again finds place in the Head Note to Article 246. This article deals with distribution of legislative powers as between the Union and the State Legislatures, with reference to the different Lists in the Seventh Schedule."
>
> 37. Article 246, thus, provides for distribution, as between Union and the States, of the legislative powers which are conferred by Article 245. Article 245 begins with the expression "subject to the provisions of this Constitution". Therefore, Article 246 must be read as "subject to other provisions of the Constitution".
>
> (Id. at p. 128)

125 The limitations on the exercise of legislative power emanate from

> "(i) guarantees of freedom under Part III of the Constitution containing fundamental rights; (ii) the requirement that the law making authority must possess legislative competence to enact a law on the subject on which it legislates; and (iii) other constitutional limitations. Part XIII of the Constitution is one of those constitutional limitations. The constitutional limitation emanating from Part XIII arises from the recognition which it contains of the guarantee of free trade, commerce and intercourse. Hence the first premise upon which legislative powers are conferred upon and distributed between the Centre and the states is that though the enactment of law is a manifestation of sovereignty, law making authority under the Indian Constitution is subject to constitutional restraints. Absolute power does not dwell in any constitutional authority which is subject to a written constitution.

126. The legislative entries in the Lists of the Seventh Schedule to the Constitution delineate general fields of legislation separately from taxing heads. In the Union List taxing entries are contained from Entries 82 to 92C. The residual entry, Entry 97 deals with matters not enumerated in the state or concurrent lists, including any tax not mentioned in either of those lists. In the state list taxes are comprised in Entries 46 to 62. Fees are dealt with under separate heads: in Entry 96 of List I, Entry 66 of List II and Entry 47 of List III.

H.2 Sovereignty and constitutional limitations

127. The power to tax has been considered to be an essential attribute of government and a sovereign power vesting in the state. Thomas Cooley in his "Treatise on the Constitutional Limitations which rest upon the Legislative power of the States of the *American Union*[127]" provides a jurisprudential foundation to the taxing power in the following observations :
(Indian Reprint 2005)

> "Taxes are defined to be burdens or charges imposed by the legislative power upon persons or property, to raise money for public purposes. The power to tax rests upon necessity, and is inherent in every sovereignty. The legislature of every free State will possess it under the general grant of legislative power, whether particularly specified in the constitution among the powers to be exercised by it or not. No constitutional government can exist without it, and no arbitrary government without regular and steady taxation could be anything but an oppressive and vexatious despotism, since the only alternative to taxation would be a forced extortion for the needs of government from such persons or objects as the men in power might select as victims. In the language of Chief Justice Marshall : "The power of taxing the people and their property is essential to the very existence of government, and may be legitimately exercised on the objects to which it is applicable to the utmost extent to which the government may choose to carry it. The only security against the abuse of this power is found in the structure of the government itself. In imposing a tax, the legislature acts upon its constituents. This is, in general, a sufficient security against erroneous and oppressive taxation. The people of a State, therefore, give to their government a right of taxing themselves and their property; and as the exigencies of the government cannot be limited, they prescribe no limits to the exercise of this right, resting confidently on the interest of the legislator, and on the influence of the constituents over their representative, to guard them against its abuse." (Id. at p.2-3)

Under the Indian Constitution the conferment of legislative power to impose, collect and enforce the realization of taxes is specifically spelt out from and enumerated under constitutional provisions. Taxing entries in Lists I and II are specifically enumerated and their ambit defined. Article 366(28) of the Constitution defines the expression taxation to include "the imposition of any tax or impost, whether general or local or special" and provides that the expression tax "shall be construed accordingly".
128 Several decisions of this Court have regarded the taxing power as an essential

attribute of government and sovereignty. In *Rai Ramkrishna v. State of Bihar*[128], it was held that :

> "It is, of course, true that the power of taxing the people and their property is an essential attribute of the Government and Government may legitimately exercise the said power by reference to the objects to which it is applicable to the utmost extent to which Government thinks it expedient to do so. The objects to be taxed so long as they happen to be within the legislative competence of the legislature can be taxed by the legislature according to the exigencies of its needs, because there can be no doubt that the State is entitled to raise revenue by taxation."

In *Raja Jagannath Baksh Singh v. State of U.P*[129]. , this principle was stated as follows:

> "15...The power of taxation is, no doubt, the sovereign right of the State; as was observed by Chief Justice Marshall in M"Culloch v. Maryland [4 Law Edn. 579 p. 607] : "The power of taxing the people and their property is essential to the very existence of Government, and may be legitimately exercised on the objects to which it is applicable to the utmost extent to which the Government may choose to carry it."
>
> In *Amrit Banaspati Co. Ltd. v. State of Punjab* [130], this Court held that :
>
> "10....taxation is a sovereign power exercised by the State to realise revenue to enable it to discharge its obligations." (Id. At page 424).
>
> In *Dena Bank v. Bhikhabhai Prabhudas Parekh & Co*[131]. , this Court held thus: "8 the State is entitled to raise money by taxation because unless adequate revenue is received by the State, it would not be able to function as a sovereign Government at all. It is essential that as a sovereign, the State should be able to discharge its primary governmental functions and in order to be able to discharge such functions efficiently, it must be in possession of necessary funds and this consideration emphasises the necessity and the wisdom of conceding to the State, the right to claim priority in respect of its tax dues." (Id.atp. 702)

129. The limitation on the states' power to tax must as a consequence be found in constitutional limitations. This follows the constitutional principle that all legislative powers conferred upon the Union Parliament and the state legislatures are an attribute of sovereignty. Hence the limitations on the exercise of those powers are such as have been crafted by the Constitution. These limitations which impose a fetter on the exercise of legislative powers may arise as a result of the guarantees of freedom in Part III; restraints arising from legislative competence and constitutional limitations imposed by other provisions of the Constitution. Hence in *Maharaj Umeg Singh v. State of Bombay* [132], this Court held that the power of legislation that is vested in the state is plenary and the fetters or limitations on the exercise of legislative powers could only be imposed by the Constitution itself. The Court recognized that the Constitution may itself lay down fetters or limitations on the exercise of the power such as in Article 303 or Article 286(2). The fetter or limitation must however be traceable to the Constitution. In

Firm Bansidhar Premsukhdas v. State of Rajasthan[133], this Court adverted to the decision in *Thakur Jagannath Baksh Singh v. United Provinces* [134], and held that the limitation on the plenary powers of the legislature to enact law must be traced to an express provision in the Constitution :

> ".It is well-established that Parliament or the State Legislatures are competent to enact a law altering the terms and conditions of a previous contract or of a grant under which the liability of the Government of India or of the State Governments arises. The legislative competence of Parliament or of the State Legislatures can only be circumscribed by express prohibition contained in the Constitution itself and unless and until there is any provision in the Constitution expressly prohibiting legislation on the subject either absolutely or conditionally, there is no fetter or limitation on the plenary powers which the legislature is endowed with for legislating on the topics enumerated in the relevant lists. This view is borne out by the decision of the Judicial Committee in Thakur Jagannath Baksh Singh v. United Provinces." (Id. at p. 19)

130. The legislative power of the states to impose taxes is subject, in general, to the same constitutional parameters which govern the exercise of all legislative power. The containment of legislative power follows from three constitutional precepts. First, legislation is valid if it is enacted by a legislature which has competence to enact law on the subject. This is the consequence of the distribution of legislative power between the Union and the States under Articles 245 and 246 read with the lists contained in the Seventh Schedule. The legislatures, whether at the national or the state level, are entrusted with the power of legislation in exercise of which they must confine themselves to the boundaries allocated by the Constitution. These boundaries are defined with reference to the competence to enact law governing a particular subject matter. Parliamentary legislative power has a residuary or catch all area: subjects not enunciated elsewhere fall in its ambit. Second, the enumeration off undamental rights by Part III of the Constitution operates as a restraint on the sovereign power vesting in the legislatures to enact law. Article 13 of the Constitution stipulates that the state shall not enact law which violates the freedoms guaranteed by the Chapter on fundamental rights. A law whether made before or after the advent of the Constitution is void to the extent of its inconsistency with Part XIII. Third, other constitutional limitations or restrictions may condition or contain the law making power including in the field of taxation. These constitutional provisions are a manifestation of the doctrine of constitutional limitations under which every organ of the state which is a creation of the Constitution operates in the field assigned to it.

131. In the field of taxation, the containment of legislative powers vesting in the states may take place through provisions which are in the nature of : (i) abstraction; (ii) eclipse; and (iii) limitations or restrictions. These categories, it must be noted are convenient reference points for understanding the source of constitutional restrictions. An illustration of an abstraction of legislative power is contained in Entry 54 of the State List which provides for taxes on the sale or purchase of goods other than newspapers, subject to the provisions of Entry 92(A) of the Union List. Entry 92(A) of the Union List

was introduced by the Sixth amendment to the Constitution in 1956 to provide for 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. Under Entry 54 of the State List as it originally stood, the states possessed an unfettered area for imposing taxes on the sale or purchase of goods other than newspapers. Arguably, this could extend to the exercise of taxing powers on inter-state trade on the strength of the explanation to Article 286. For the purposes of this judgment, it is not necessary to burden the record by referring to the judgment in The *Bengal Immunity Company v The State of Bihar*[135]. As a result of the sixth amendment, the ambit of Entry 54 is now expressly subject to the power of the Union under Entry 92(A) of List I.

132. Article 286 stipulates that a state law shall not impose or authorize the imposition of a tax on the sale or purchase of goods, where the sale or purchase takes place outside the state or in the course of import or export from or outside the territory of India. Article 286(1) provides an express bar. Article 269(3) empowers Parliament by law to formulate principles for determining when a sale or purchase or consignment of goods takes place in the course of inter-state trade or commerce. Parliament, in exercise of its powers under Article 269(3) enacted the Central Sales Tax Act 1956. Sections 14 and 15 of that Act provide a list of goods of special importance, the manner of imposing taxes and the restrictions on the power of imposing taxes.

133. The second source of containment on the legislative powers of the states in the area of taxation is Article 253 of the Constitution under which Parliament, notwithstanding anything contained in the earlier provisions of Chapter 1 of Part XI is entrusted with the power to enact legislation for the entire territory of India for implementing a treaty, agreement or convention with one or more countries or to implement a decision at an international conference association or other body. The non-obstante provision of Article 253 operates in relation to Articles 245 to 252. Hence, the legislative powers of the states including in the area of taxation may be eclipsed where Parliament has enacted a law to effectuate India's international obligations in pursuance of Article 253.

134. The third source of constitutional containment on the legislative power of a state is in the form of limitations of which Clause 3 of Article 286 provides an illustration. Under Clause 3, Parliament provides the restrictions and conditions in regard to "the system of levy, rates and other incidents of tax" upon which a law enacted by a state providing for a tax of the nature specified in sub-clause (a) and (b) is subject. Sub-clause (a) deals with a tax on the sale or purchase of goods declared to be of special importance in inter-state trade or commerce by a law enacted by Parliament. Sub-clause (b) deals with a tax on the sale or purchase of goods falling under sub-clauses (b), (c) and (d) of Article 366(29A). Among other things, a tax on contracts for hire purchase and involving transfer of the right to use goods is subject to the restrictions and conditions which are provided by a law enacted by Parliament in regard to the system of levy rates and other incidents of tax.

135. The constitutional containment of the legislative powers of the states also originates in the provisions of Part XIII which enable Parliament and the state

legislatures to impose restrictions on inter-state trade or commerce subject to defining parameters. Whether, and if so, the extent to which taxes are within the purview of Part XIII is being dealt with separately below.

H.3 Part XIII and taxation

136. The basic submission on the part of the states is that freedom under Article 301 is not freedom from taxation. This submission has been adduced primarily on the foundation that the Indian Constitution contemplates the position of the states as constitutional units of a federal structure, each of whom is sovereign within the fields allotted. Taxation, it has been urged is a manifestation of sovereign power which is foundational to the existence of government. Tax revenues are required for welfare and developmental activities. Hence, it has been submitted that these are strong reasons for not construing the freedom under Article 301 as freedom from taxation.

137. The next limb of the submission is that under Article 265, taxes can only be imposed under a law enacted by the competent legislature and the executive has no role to play in the levy and collection of tax, except under delegated legislative power. Under various Articles of Part XII [for instance Articles 276(2), 286(1) and 288(2)] the Constitution provides for limitations on the taxing powers of the states or powers are conferred upon Parliament to provide for limitations by law (Clauses 2 and 3 of Article 286). There are at least five entries in the State List of the Seventh Schedule (Entries 50,51,54,55, and 57) which are specifically subject to limitations or principles prescribed by Parliament by a law made under List I and List III. In other words, it has been urged that wherever an exemption from taxes or a limitation on states' taxing powers is contemplated by the Constitution, this has been expressly provided under Articles 285, 287, 288 and 289. Consequently, it has been urged that exemption from the taxing power cannot be a matter of inference or implication and must be provided expressly and unambiguously. Moreover, under Article 289(2), a trade or business carried on by or on behalf of the government of a state can be subjected to tax "to such extent" as Parliament may by law provide. Based on this and the judgment of a nine Judge Bench of this Court in *NDMC v. State of Punjab* [136], it has been urged that in a situation where the Constitution subjects even the trade or business of a state to tax, an exemption in favour of trade, commerce and intercourse carried on by private individuals cannot be contemplated particularly by implication.

138. While evaluating this submission, it would at the outset be necessary to notice that there are two extreme positions which lie at opposing ends of the spectrum. The first is the position adopted by Justice J C Shah in Atiabari that all taxation falls within the ambit and purview of Part XIII. This submission postulates that every tax constitutes a restraint on the freedom of trade, commerce and intercourse. The opposing end of the spectrum is that taxes per se can never be a restraint on free trade since it is through the raising of revenues that a state provides ordered conditions for the safe, secure and efficient means for transacting trade and commerce. In this view, only a discriminatory tax would run afoul of Part XIII [being violative of Article 304(a)] and, so long as a tax is non-discriminatory, it cannot be contrary to the provisions of Part XIII. This position would broadly correspond to the view espoused by Chief Justice Sinha. The middle

ground which was sought to be advanced in the decision in Automobile Transport was that compensatory taxes would lie outside Part XIII since they facilitate rather than restrict trade. Taxes which are not compensatory and which in their direct and immediate effect restrict trade would be subject to the rigours of Article 304(b) of the Constitution.

H.3.1 All taxes are not impediments

139 While evaluating the merits of the rival viewpoints, it cannot be gainsaid that an orderly society is a condition precedent for an environment in which trade, commerce and intercourse can flourish. Trade and commerce survive and flourish on the foundation of the rule of law. The sanctity of contracts must be recognized, protected and enforced through a legal system which creates rights and provides remedies for redressal. Again, the free movement of goods, services, persons and capital requires the existence of public order and conditions which allow for trade and commerce to take place unhindered. Neither trade nor commerce can flourish amidst violence, unrest and social disorder. Taxes provide revenue for the state to sustain manifold activities which are geared to providing conditions of social order. The state provides infrastructure both tangible and intangible. Tax revenues form an essential part of the requirements necessary for states to govern. Taxes are required by Article 265 to be imposed by a law enacted by Parliament or the state legislatures. Without the power to raise revenues, the ability of the state to create conditions requisite for trade and commerce to exist would be denuded. Hence, as a matter of first principle it cannot be postulated that taxation in whatever form is a burden on trade, commerce and intercourse and that every tax necessarily hinders trade. Such a wide construction cannot be accepted simply because by raising revenues through the means of taxation, the state provides a political and legal order based on the rule of law where contractual transactions can be executed effectively. The extreme position that every law which imposes a tax is to be regarded as a hindrance to trade, commerce and intercourse is unsustainable.

140. In the context of the relationship between the freedom guaranteed by Part III of the Constitution and the taxing power, it has been the consistent position of this Court that fundamental rights [particularly, the freedom of trade and business under Article 19(1)(g)] do not confer an immunity from taxation. In *Indian Express Newspapers v. Union of India*[137], this Court held that the rights guaranteed by Article 19(1)(a) and Article 19(1)(g) are subject to clauses (2) and (6) and the newspaper industry has not been granted an exemption from taxation in express terms. On the other hand, Entry 92 of the Union List of the Seventh Schedule empowers Parliament to make laws for levying taxes on sale or purchase of newspapers and on advertisements published therein. The police power, taxation and eminent domain were held to be a form of social control essential for peace and good governance. Newspapers were held not to be free from the requirement of bearing a common fiscal burden, like others:

> “43....Their newspapers have to be transported by roads, railways and air services. Arrangements for security of their property have to be made. The Government has to provide many other services to them. All these result in a big drain on the financial resources of the State as many of these services are

heavily subsidized. Naturally such big newspaper organizations have to contribute their due share to the public exchequer. They have to bear the common fiscal burden like all others." (Id. at p. 671)

This Court held that in the case of an ordinary taxing statute, a law may be questioned if it is openly confiscatory or a colourable device to confiscate. On the other hand, in the case of a tax on newsprint, it would be sufficient to show a "distinct and noticeable burdensomeness, clearly and directly attributable to the tax". While therefore holding that it was rejecting the submission that no tax could be levied on the newspaper industry, this Court held that any such levy was subject to judicial review under the provisions of the Constitution.

141. In *Government of Tamil Nadu v. Ahobila Matam*[38], this Court held that the imposition of an assessment on lands held by a religious denominational institution would not attract the right guaranteed by Article 26 of the Constitution. In *All Bihar Christian Schools' Association v. State of Bihar*[139] , this Court held that an unaided minority institution is not immune from the operation of the general laws of the land and cannot claim an immunity, inter alia, from measures of taxation. Apart from these decisions, there are judgments of this Court holding that a taxing statute is not per se a restriction on the freedom under Article 19(1)(g). In *Federation of Hotel & Restaurant Association of India v. Union of India*[140] , this
Court while laying down the above principle held that the mere excessiveness of a tax or a diminution of profit earnings does not per se without more constitute a violation of rights under Article 19(1)(g). (See also in this context : *Express Hotels (P) Ltd. v. State of Gujarat*[141] *, and Pankaj Jain Agencies v. Union of India*[142]*).*

142. In *Vrajlal Manilal & Co. v. State of M.*P[143], this Court held that an increase in the rate of tax on a particular commodity cannot per se be said to impede free trade and commerce in that commodity. The Court reaffirmed the principle that in order to be a restriction or impediment a legislative measure must directly or immediately impede the free flow of trade, commerce and intercourse so as to fall within the prohibition of Article 301. A tax may in certain cases directly and immediately restrict or hamper the flow of trade. Whether the imposition of a tax does so in each case has to be judged on its own facts and in its own setting of time and circumstance.

H.3.2 Articles 302, 303 and 304

143. Articles 302, 303 and 304 provide for restrictions on trade and commerce. The marginal note to each of the three articles specifically contemplates restrictions on or with regard to trade and commerce. The marginal note to Article 302 refers to the power of Parliament to impose restrictions on trade, commerce and intercourse. Under Article 302 Parliament is empowered by law to impose restrictions in the public interest on the freedom of trade, commerce and intercourse between one state and another or within any part of the territory of the India. Consequently, Parliamentary power under Article 302 to impose restrictions is not only confined to inter-state trade but extends to restrictions within any part of the territory of India. However, Article 303 imposes a limitation both on Parliament and the state legislatures. Under Article 303, neither

Parliament nor the legislature of a state can enact a law giving or authoring the giving of a preference to one state over another or making or authorising the making of discrimination between one state and another, by virtue of any entry relating to trade and commerce in any of the lists in the Seventh Schedule. Article 303 has a non-obstante provision which overrides Article 302. The non-obstante clause in Article 303 is evidently inapposite in relation to the legislature of a state because Article 302 does not apply to a state legislature in the first instance. Evidently the non-obstante provision can have meaning only in relation to Parliament because it has the effect of stipulating that the power of Parliament to impose restrictions in the public interest under Article 302 is subject to the principle of non-discrimination and non-grant of preferences to one state over another under Article 303.

144. Be that it is may, the effect of the norm which Article 303 enunciates is that neither Parliament nor the legislature of a state can grant preferences while enacting law to one state over another or make any discrimination. Article 303 concludes with the words "by virtue of any entry relating to trade and commerce in any of the lists in the Seventh Schedule." These words were held by Justice Subba Rao in Automobile Transport to have the widest import. The entries which specifically refer to trade and commerce in the Seventh Schedule are entries 41 and 42 of the Union List, entries 26 and 27 of the State List and Entry 33 of the Concurrent list. Entries 41 and 42 of the Union List are as follows :

> 41. Trade and Commerce with foreign countries; import and export across customs frontiers; definition of customs frontiers
>
> 42. Inter-State trade and Commerce. Entry 26 of the State List is as follows :
>
> 26. Trade and commerce within the State subject to the provisions of Entry 33 of List III.
>
> 27. Production, supply and distribution of goods subject to the provisions of Entry 33 of List III.Entry 33 of the Concurrent list is as follows :
>
> 33. Trade and commerce in and the production, supply and distribution of -
> (a) the products of any industry where the control of such industry by the Union is declared by Parliament by law to be expedient in the public interest, and imported goods of the same kind as such products;
>
> (b) foodstuffs, including edible oilseeds and oils;
>
> (c) cattle fodder, including oilcakes and other concentrates;
>
> (d) raw cotton, whether ginned or unginned, and cotton seed; and
>
> (e) raw jute.

145. In Automobile Transport it was urged that the expression "by virtue of the entries

relating to trade and commerce in any of the lists in the Seventh Schedule" are of wider import than the words "by virtue of the said entries". Therefore, any law under Article 303 made by virtue of any entry in any of the lists in the Seventh Schedule, if it relates to trade and commerce, would be covered by the exception. Accepting the submission, Justice Subba Rao held as follows :

> "42....The words "any entry relating to trade and commerce in any of the Lists" are of the widest import and they yield to a very liberal interpretation. The phraseology used supports this interpretation. The reason of the exception also sustains it. There cannot be any distinction on principles, from the standpoint of the mischief sought to be averted, between a law made by virtue of an entry ex-facie referring to trade and commerce and that made by virtue of any entry affecting trade and commerce. For instance, a law may be made by Parliament under entries relating to railways, highways, shipping etc. These entries do not expressly refer to trade and commerce, though they may directly affect trade and commerce. If a law made under entry 26 of List II giving preference or making discrimination among the states is objectionable, it should also be objectionable, if made by virtue of any other entry. I would, therefore, hold that any law made by Parliament by virtue of any entry imposing the said discrimination restrictions would be under the said article." (Id. at p. 559- 560)

146. Justice Hidayatullah who delivered a dissenting judgment for and on behal of himself and Justices Rajagopala Ayyangar and Mudholkar adopted a similar interpretation of the language of Article 303. The learned Judge held that in the Seventh Schedule there are many other entries apart from entries 41 and 42 of List 1, entries 26 and 27 of List II and Entry 33 of list III regulating inter-state trade. In that context, he observed that :

> "103....By the words of Article 303 'by virtue of any entry relating to trade and commerce' is meant not the five Entries last named by us but others also, e.g., Entry 8 of List II, Entries 29, 30, 81 of List I, Entry 29, 15 of List III (to mention only a few from each List). Thus, is achieved one purpose which is paramount viz., that the exercise of the commerce powers, however derived is not to be exercised to create preferences and discrimination between one state and other State Legislature or both acting in union. No question of the content of the power or its source can arise in this
> context, because the prohibition is absolute. The article makes a great advance upon Section 297 of the Government of India Act 1935. In the section, the inhibition was only against a Provincial Legislature or Government. Here the inhibition embraces not only these but is also against Parliament and the Central executive. The executive limb has been made powerless, because the source of restrictions must be 'law' and if a law cannot be made, executive action per se would be ineffective without more. Further, Section 297 was concerned only with goods and their taxation differentially. The Article takes in its stride not only the passage of goods or their taxation but all other matters inherent in free trade, commerce and intercourse."

147. However, it has been urged that this interpretation would be contrary to the position which has been adopted since the judgment in *MPV Sundararamier v. State of Andhra Pradesh*[144]: In support, it has been submitted that the taxing entries in the lists of the Seventh Schedule are indicated separately from non-taxing entries. Hence, it is urged, the words of Article 303 cannot be interpreted to include taxing entries. This submission cannot be accepted as a matter of first principle. What the judgment in MPV Sundararamier lays down is that in the lists of the Seventh Schedule, the subjects of taxation are dealt with under distinct heads. Hence, the subject of a tax cannot be traced to a non-taxing entry. It was held that :

> "51. In List I, Entries 1 to 81 mention the several matters over which Parliament has authority to legislate. Entries 82 to 92 enumerate the taxes which could be imposed by a law of Parliament. An examination of these two groups of Entries shows that while the main subject of legislation figures in the first group, a tax in relation thereto is separately mentioned in the second Construing Entry 42 in the light of the above scheme, it is difficult to resist the conclusion that the power of Parliament to legislate on inter-State trade and commerce under Entry 42 does not include a power to impose a tax on sales in the course of such trade and commerce."

148. This principle would have no bearing on the interpretation of the words in Article 303 which restrain Parliament and the state legislatures from granting preferences to one state over another and from discriminating between one state and another "by virtue of any entry relating to trade and commerce" in any of the lists in the Seventh Schedule. These words namely "entry relating to trade and commerce" are of the widest import. The expression "relating to" has a well-known connotation in law extending its ambit to all matters which are reasonably proximate or connected to the subject. While the constitution mandates the principle of non-discrimination between one state over another and the non-grant of preferences under Article 303, there is no basis to confine those words merely to the entries noted earlier (entries 41 and 42 of List I, entries 26 and 27 of List II and entry 33 of List III).

149. To recapitulate, the submission that the scope of Article 303 is restricted only to the four entries noted above cannot commend itself for acceptance of the following reasons :

> "(i) the key expressions in Article 303 are "shall have the power to make any law" making any discrimination between one state and another and "by virtue of any entry relating to trade and commerce";
>
> (ii) the expression "power to make any law" would on its plain and literal meaning include tax laws. There is no justification to read this as "any law other than a tax legislation;
>
> (iii) the expression "any entry relating to trade and commerce has a comprehensive significance, meaning something that is associated with or having a nexus to. The words 'any entry relating to trade and commerce' are

words of amplitude and cannot be construed in a restrictive sense."

150. In *State of Madras v. NK Nataraja Mudaliar*[145], a Constitution Bench of this Court, while construing the provisions of the Central Sales Tax Act, 1956 dealt with the submission that entries relating to trade and commerce in the legislative lists, within the meaning of Article 303 would not include entries with respect to the levy of a tax on trade and commerce. It was also urged that the words in Article 303 must be confined to entries 41 and 42 of List I, entries 26 and 27 of List II and entry 33 of List III. This issue was however kept open by the Constitution Bench, as is evident from the following extracts :

> "12. It was contended on behalf of the State that the power under Article 303 could only be exercised so as to restrict the authority of the Parliament which arises by virtue of an entry relating to trade and commerce in the legislative lists and it was urged that an entry with respect to the levy of tax on trade and commerce and is not an entry relating to trade and commerce and therefore there is no prohibition against the Parliament exercising power or authorising the giving of any preference to one State over another or making or authorising the making of any discrimination between on State and another by exercise of taxing power. Reliance in support of that contention was placed upon the judgment in Sundararamier and Company v. State of Andhra Pradesh MANU/SC/0151/1958: [1958] 1 SCR 1422 in which Venkatarama Aiyar, J., pointed out that under the scheme of entries in List I & II of the Seventh Schedule, the power of taxation exercisable in respect of any matter is a power distinct from the power to legislate in respect of that matter. It was also urged that the expression "an entry relating to trade and commerce in any of the Lists in the Seventh Schedule i.e. entries 41 & 42 of List I, entries 26 & 27 of List III and entry 33 of List III in the Seventh Schedule, and extended to no others. On the other hand, it was contended that all legislative entries which directly affect trade and commerce are also within the expression "entry relating to trade and commerce
>
> 13. We need to express no opinion on the two questions argued before us. The question whether entries relating to trade and commerce in the Lists in the Seventh Schedule are restricted to entries 41 & 42 of List I, entries 26 & 27 of List II and entry 33 of List III, or relate to all general entries which affect trade and commerce, is academic in the present case. Nor do we think it necessary to decide whether for the purpose of Article 303 entries relating to tax on sale or purchase of goods i.e. entry 92A of List I, and entry 54 of List II are entries relating to trade and commerce, for, in our opinion, an Act which is merely enacted for the purpose of imposing tax which is to be collected and to be retained by the State does not amount to law giving, or authorising the giving of any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, merely because of varying rates of tax prevail in different States."

151. In a subsequent judgment of a Constitution Bench in *State of Tamil Nadu v. Sitolakshmi Mills*[146], the assesse had claimed before the Madras High Court that it was

not liable to be taxed at the higher rate under Section 8(2)(b) of the Central Sales Tax Act, 1956 on the turnover of sales in the course of inter-state trade to government or to unregistered dealers even though they had not obtained the C and D forms because Section 2(B) violates Articles 301 and 303(1) of the Constitution. The High Court accepted those claims. In appeal, the Constitution Bench observed:

> "8....Normally, a tax on sale of goods does not directly interfere with the free flow or movement of trade. But a tax can be such that because of its rate or other features, it might operate to impede the free movement of goods. The majority judgment delivered by Shah, J., in State of Madras v. N.K. Nataraja Mudaliar proceeds on the basis that tax under the Central Sales Tax Act is in its essence a tax which encumbers movement of trade and commerce, but the tax imposed in the case in question was saved by the other provisions of Part XIII. The Court then said that the exercise of the power to tax would normally be presumed to be in the public interest and as Parliament is competent under Article 302 to impose restrictions on the freedom of trade, commerce and intercourse between one State and another or within any part of the territory of India as may be required in the public interest, the tax was saved. .
>
> 9. Bachawat, J., in his judgment in the case said that if a tax on intra-State sales does not offend Article 301, logically, a tax on inter-State sales also cannot do so, that a tax does not operate directly or immediately on the free flow of trade or the free movement or transport of goods from one part of the country to the other, that the tax is on the sale, and that the movement is incidental and a consequence of the sale. He observed further that even assuming that the Central Sales Tax is within the mischief of Article 301, it is certainly a law made by Parliament in the public interest and is saved by Article 302
>
> 10. As already stated, Section 8(2)(b) deals with sale of goods other than declared goods and it is confined to inter-State sale of goods to persons other than registered dealers or governments. The rate of tax prescribed is 10 per cent or the rate of tax imposed on sale or purchase of goods inside the appropriate State, whichever is higher. The report of the Taxation Inquiry Committee would indicate that the main reason for enacting the provision was to canalize inter-State trade through registered dealers, over whom the appropriate government has a great deal of control and thus to prevent evasion of tax :
>
> "Where transactions take place between registered dealers in one State and unregistered dealers or consumers in another, this low rate of levy will not be suitable, as it is likely to encourage avoidance of tax on more or less the same scale as the present provisions of Article 286 have done. If this is to be prevented, it is necessary that transactions of this type should be taxable at the same rates which exporting States impose on similar transactions within their own territories. The unregistered dealers and consumers in the importing State will then find themselves be unable to secure any advantage over the consumers of locally purchased articles, nor of course will they, under this system, be able to escape the taxation altogether, as many of them do at present."[See Report of

the Taxation Enquiry Commission, 1953-54, Vol. 3, p. 57]...

In other words, it was to discourage inter-State sale to un-registered dealers that Parliament provided a high rate of tax, namely 10 per cent. But even that might not serve the purpose if the rate applicable to intra-State sales of such goods was more than 10 per cent. The rate of 10 per cent would then be favourable and they would be at an advantage compared to local consumers. It is because of this that Parliament provided, as a matter of legislative policy that the rate of tax shall be 10 per cent or the rate applicable to intra-State sales whichever is higher

11. If prevention of evasion of tax is a measure in the public interest, there can be no doubt that Parliament is competent to make a provision for that purpose under Article 302, even if the provision would impose restrictions on the inter-State trade or commerce."
(Id. at 413-414)

The statutory provision was consequently upheld on the ground that as a measure for preventing the evasion of tax in the public interest, Parliament was competent to enact it under Article 302 even if it restricted inter-state trade and commerce. H.3.3 Construing Article 304

152. The area which assumes a great deal of importance in the present case is whether it would be correct to postulate that taxes, save and except for discriminatory taxes under Article 304(a) would lie outside the pale and purview of Part XIII. If this submission was to be accepted, the necessary consequence would be that only a discriminatory tax of the nature contemplated by Article 304(a) would offend the guarantee of freedom under Article 301. A non-discriminatory tax would lie outside the purview of Part XIII. Once a tax meets the parameters of Article 304(a), it would not breach the freedom of trade and commerce. Clauses a and b of Article 304 would - in the line of argument have to be treated in a disjunctive manner and a tax which is consistent with Clause (a) would not need to meet the requirements of Clause (b).

153. Justice G P Singh in his seminal treatise, 'Principles of Statutory ***Interpretation***'[147] states that marginal notes to constitutional provisions are, as a matter of interpretation,

[147] *14th Edition, page 190- in foot note 91. Bengal Immunity Co.Ltd. v. State of Bihar, AIR 1955 SC 661, p.676 : (1955) 2 SCR 603. See also Golaknath v. State of Punjab, AIR 1967 SC 1643, p. 1658:1967 (2) SCR 762,*

where marginal note to Article 368 was referred. treated as being a part of the Constitution and as providing some guidance as to the meaning of a provision :

"Marginal notes appended to Articles of the Constitution have been held to constitute part of the Constitution as passed by the Constituent Assembly and therefore they have been made use of in construing the Articles, e.g. Article 286, as furnishing 'prima facie', 'some clue as to the meaning and purpose of the Article'." While Article 301 stipulates that trade, commerce and intercourse

throughout the territory of India shall be free, this guarantee is made subject to the other provisions of Part XIII. Part XIII has employed both the expressions "subject to" on the one hand and "notwithstanding anything" on the other. The expression "subject to" has a well-known legal connotation which conveys the idea of a provision yielding place to another provision or to other provisions to which it is made subject. This principle has been enunciated in the judgment of this Court in *South Indian Corporation (P) Ltd. v Board of Revenue* [148].

154. In State *of Bombay v. The United Motors (India) Ltd*[149] *,* Chief Justice Patanjali Sastri, speaking for a Constitution Bench spoke of the subordination of the freedom under Article 301 to the powers of the states to levy non-discriminatory taxes. The learned Judge held :

> "11 It will be seen that the principle of freedom of inter-State trade and commerce declared in Article 301 is expressly subordinated to the State power of taxing goods imported from sister States, provided only no discrimination is made in favour of similar goods of local origin. Thus the states in India have full power of imposing what in American State Legislation is called the use tax, gross receipts tax, etc. not to speak of the familiar property tax, subject only to the condition that such tax is imposed on all goods of the same kind produced or manufactured in the taxing State, although such taxation is undoubtedly calculated to fetter inter-State trade and commerce. In other words, the commercial unity of India is made to give way before the State-power of imposing "any" non-discriminatory tax on goods imported from sister Sates." (Id. at p. 1081)

155. Article 304 begins with a non-obstante provision which takes effect notwithstanding what is contained in Articles 301 or 303. A non-obstante provision of this nature has a distinctive meaning. In *Chandavarkar Sita Ratna Rao v. Ashalata S. Guram* [150], this Court held that :

> "68.It is well settled that the expression 'notwithstanding' is in contradistinction to the phrase 'subject to', the latter conveying the idea of a provision yielding place to another provision or other provisions to which it is made subject." (Id. at p. 478)
>
> In *South India Corporation v. Board of Revenue* [151], while interpreting Articles 372 and 278 of the Constitution, this Court emphasised that the phrase "notwithstanding anything in the Constitution" is equivalent to stating 'inspite of the other articles of the Constitution' or that the other articles shall not to be an impediment to the operation of that particular article."

156. The use of the non-obstante clause in Article 304 in its application to Article 301 has been debated. That is because while Article 301 makes the guarantee of freedom of trade and commerce subject to the other provisions of Part XIII, Article 304 commences with a non-obstante provision which operates notwithstanding what is contained in Article 301. A reasonable construction or meaning would have to be attributed to these two provisions. So construed, Article 304, in its non-obstante

provision, must mean that it would permit what is contemplated by Clauses (a) and (b) even though it would otherwise be within the ambit of the freedom guaranteed by Article 301. Similarly, in its application to Article 303, the non-obstante clause in Article 304 indicates that despite the prohibition that is contained in Article 303, the state legislature is empowered to do something of the nature that falls within the ambit of the provision. The non-obstante provision of Article 304 governs both Clauses (a) and (b) that follow. By virtue of Clause (a), the legislature of a State can, despite the provisions of Article 301, impose a non-discriminatory tax. The power to impose a tax, it must be noted, is not conferred by Clause (a) of Article 304 but is a power which is traceable to the legislative power of the states under Articles 245 and 246 of the Constitution read with the legislative entries in the State List. Article 304(a) is a clear indication that though a tax may constitute a restriction within the meaning of Article 301, the imposition of a non-discriminatory tax is permissible to the state legislature. Article 304(a) lifts an embargo that would otherwise have existed but for the non-obstante provision. Article 304(a), however, mandates that a tax which is being imposed on goods imported from other States or Union territories must be a tax to which similar goods manufactured or produced in that state are subject. Moreover, the tax shall not discriminate between goods that are imported and goods so manufactured and produced.

H.3.4 Conjunctive or disjunctive : 'may'; 'and'

157. Clauses (a) and (b) of Article 304 are separated by the use of the expression "and". The issue is whether the expression "and" is to be construed as conjunctive or disjunctive. Clause (b) contemplates reasonable restrictions being imposed under a law enacted by the state legislature on the freedom of trade, commerce and intercourse with or within that state as are required in the public interest. The proviso operates only in relation to clause (b) and not clause (a). It stipulates that no bill or amendment for the purposes of clause (b) shall be introduced or moved in the legislature of a state without the previous sanction of the President. The mandate of the proviso can however be cured under Article 255 which provides as follows :

> "Article 255 : No Act of Parliament or of the Legislature of a State and no provision in any such Act, shall be invalid by reason only that some recommendation or previous sanction required by this Constitution was not given, if assent to that Act was given –
>
> (a) where the recommendation required was that of the Governor, either by the Governor or by the President;
>
> (b) where the recommendation or previous sanction required was that of the President, by the President."
>
> Hence even though the previous sanction which is required under the proviso to Article 304(b) before the introduction of a bill has not been obtained, this deficiency can be cured if assent to the Act passed by a legislature is given by the President. 158 Article 304 provides that the legislature of a state may by law (a) impose a non-discriminatory tax as provided in clause (a); and (b) impose

reasonable restrictions on the freedom of trade, commerce or intercourse. The expression 'may' in the prefatory part of Article 304 has to be read together with the expression 'and' which separates clauses (a) and (b). The use of the expression 'may' is indicative of the intent that the legislature of a state is not bound to levy an impost on goods imported from other states (though if it does so, the tax has to be non-discriminatory). Similarly, the state legislature has an enabling power to impose restrictions under clause (b). The legislature 'may' do so. It has the discretion whether to impose a tax or to impose a restriction and is not bound to do so.

159. The word 'and' is normally used in the conjunctive ***sense (G P Singh on Interpretation of Statutes[152]).*** However, this is not always the case. Coupled with the use of the expression 'may, the expression 'and' in Article 304 should be construed to mean and/or. In other words, the legislature of a state may take recourse to both clauses (a) and (b) of Article 304 or either of them.

160 The nuances of statutory interpretation when the expressions 'may' and 'and' are used together, have been succinctly summarised in "Statutory Interpretation" by Ruth Sullivan. The statement of legal position is thus :

> "2) "And" and "Or" a) Joint or Joint and Several "and" Both "and" and "or" are inherently ambiguous. "And" is always conjunctive in the sense that it always signals the cumulation of the possibilities listed before and after the "and". However, Id. at p. 530 "and" is ambiguous in that it may be joint or joint and several. In the case of a joint "and", every listed possibility must be included: both (a) and (b); all of (a), (b), and (c). In the case of a joint and several "and", all the possibilities may be, but need not be, included: (a) or (b) or both; (a) or (b) or (c), or any two, or all three. In other words, the joint and several "and" is equivalent to "and/or" Which meaning is appropriate depends on the context. When "and" is used before the final item in a list of powers, for example, it is joint and several :
>
> To carry out the purposes of this Act, the Governor in Council may make regulations respecting

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[152]Id. at p. 530

> (a) the conditions on which licences may be issued;
>
> (b) the information and fees that firearm vendors may be required to furnish; and
>
> (c) the annual fees that firearm owners may be charged... In this provision the Governor in Council is empowered to make regulations on any one or more of the listed subjects. However, notice what happens if "may" is replaced by "shall". If the Governor in Council is obliged to make regulations respecting (a) conditions (b) information and (c) fees, the joint and several "and" becomes joint". In the context of Article 304(a) the use of the expression 'may' in the prefatory part together with 'and' which separates clauses (a) and (b) indicates that the true meaning and intent is conveyed by the joint and several and/or. The state legislature may impose a tax falling under clause (a) as well as a reasonable

restriction falling under clause (b). Alternately it may impose one of them. These being enabling provisions, the legislature may not take recourse to either. However, when it imposes a tax and/or a restriction, the state legislature has to abide by the conditions of clauses (a) and (b) respectively."

H.3.5 Article 304(a) not the universe of taxation

161. The submission of the states is that Article 304(a) is the only provision which deals expressly with a tax measure and that clause (b) can never be construed to cover the imposition of a tax. This submission has been founded on more than one rationale. First, it has been submitted that when Article 304 uses separate expressions, taxes and restrictions, there is no reason or justification to bring taxes within the ambit of restrictions. Second, it has been submitted that clause (b) of Article 304(a) contemplates the imposition of a reasonable restriction in the public interest. Taxation, it has been urged is presumed to be in the public interest. Third, it has been submitted that in the context of Article 19, judgments of this Court which have held that the guarantee under Article 19(1)(g) does not confer an immunity from taxation.

162. A discriminatory tax is prohibited by Article 304(a). There is intrinsic material in the constitutional text to indicate that Article 304(a) does not exhaust the universe of taxation for the purposes of Part XIII. First, Article 304(a) provides that the legislature of a state may by law impose on goods imported from other states or union territories any tax to which similar goods manufactured or produced in that state are subject. The ambit of clause (a) is a tax on goods, the origin of the goods being a state other than the state which is imposing the tax. Article 301 (over which the non-obstante clause contained in Article 304 operates) has a geographical coverage which extends throughout the territory of India. Article 301 guarantees the freedom of trade and commerce not only across state boundaries but equally freedom within any part of the territory of India. If the freedom of trade and commerce is restricted by a discriminatory tax - as Article 304(a) postulates is the case - the imposition of a discriminatory tax on internal movement within a state must by the same logic breach the freedom guaranteed by Article 301. Since Article 304(a) covers only a tax on goods imported from other states, a discriminatory tax on goods which do not traverse state boundaries would not fall within the ambit of Article 304(a). Yet it would offend Article 301. A state may conceivably have a justification in the public interest in doing so or for imposing such a tax and if it were to do so, it must meet the requirements of Article 304(b). If Article 304 (b) were to be construed to not include taxes, such a course of action would be barred, however legitimate be the state interest.

163. There is a second reason why the language and scheme of Part XIII must lead to the conclusion that it is not only discriminatory taxes of the nature contemplated by Article 304(a) which fall within the ambit of the Part. Article 304(a) only covers a tax on goods (goods imported from other states as seen above). A tax imposed by the state legislature otherwise than on goods, does not fall within the ambit of Article 304(a). The taxing entries of List II of the Seventh Schedule include various taxes that fall within the legislative competence of the state legislatures other than a tax on goods. Among the taxing entries of List II (entries 46 to 62) are several which deal with aspects of taxation

of goods. They include Entry 51 (providing for duties of excise on (i) alcoholic liquors for human consumption; and (ii) opium, hemp and other narcotics drugs and narcotic manufactured and produced in the state and countervailing duties on similar goods manufactured or produced elsewhere in India); Entry 52 (taxes on the entry of goods into a local area for consumption, use or sale); Entry 53 (taxes on the consumption and sale of electricity); Entry 54 (taxes on the sale or purchase of goods other than newspapers subject to Entry 92A of List I); Entry 56 (taxes on goods carried by road or on inland waterways); Entry 57 (taxes on vehicles, whether mechanically propelled or not, suitable for use on roads subject to Entry 35 of List III) and Entry 58 (taxes on boats). Entries which deal with taxes other than on goods are Entry 56 (taxes inter alia on passengers carried by road or on inland waterways); Entry 59 (tolls); Entry 60 (tax on professions, trades, callings and employments); Entry 61 (capitation taxes) and Entry 62 (taxes on luxuries, including taxes on entertainments, amusements, betting and gambling). Article 304(a) applies only to taxes on goods. A tax which is not on goods or on aspects bearing on goods is not governed by Article 304(a). A discriminatory tax which is not on goods is not within the prohibition of that article. For instance, a discriminatory tax on luxuries, entertainments, amusements, betting and gambling will not be governed by Article 304(a). Similarly, Article 304(a) will not apply to a tax on passengers carried on roads or inland waterways under Entry 56. Since the ambit of Article 304(a) is a non-discriminatory tax on goods imported from other states, it is evident that this provision is not exhaustive even of those discriminatory taxes which will offend Article 301. There are taxes which fall within the legislative competence of the states, other than on goods, which are outside the purview of Article 304(a). If those taxes impede the freedom of trade, commerce and intercourse they would infringe Article 301 though they do not fall within Article 304(a).

164. Third, Article 302 has been held to enable Parliament to impose Central Sales Tax (Sitolakshmi Mills) (supra). The expression “restrictions” in Article 302 has been construed not to exclude a restriction by way of a taxing measure. If the expression ‘restriction’ for the purposes of Article 302 does not exclude a legislative measure by way of a fiscal imposition, it cannot evidently be excluded from the ambit of the phrase ‘restrictions’ in Article 304.

165. Fourth, this conclusion is buttressed by the non-obstante provision contained in Article 304. The plain meaning of the non-obstante provision is that state legislatures may enact legislation in exercise of their law making authority under Articles 245 and 246, of the nature contemplated by clauses (a) and (b) of Article 304, despite the fact that such a legislative measure would otherwise fall within the ambit and purview of Article 301. The non-obstante provision in Article 304(a) refers to Article 301. Obviously, unless something falls within the ambit of Article 301, there is no reason to incorporate the non-obstante clause in Article 304(a). In other words, what Article 304(a) does is to indicate that despite the fact that a legislative measure falls under Article 301, it is permissible if it adheres to Article 304. Despite Article 301, it is permissible in view of Article 304(a). Article 304(a) lifts the embargo.

166. The use of the clause of subjection in Article 301 and the non-obstante provision in Article 304 have been criticised as a case of inartistic draftsmanship. A clause which

makes a constitutional provision or, for that matter, a statutory provision subject to another makes the provision in which that clause is contained subordinate to the provision to which it is subjected. On the other hand, a non-obstante provision commencing with the word 'notwithstanding' is intended to indicate that the text in which the provision is contained overrides another. The criticism is that the expressions "subject to the other provisions of this Part" in Article 301 and "notwithstanding anything in Article 301" in Article 304(a) are incongruous. For, the former expression subjects Article 301 to the other provisions of Part XIII [including Article 304(a)]. Hence, it was unnecessary to use a non-obstante clause in Article 304(a).

167. Having noticed this criticism, it is necessary to harmonise the text of Article 301 with Article 304. The guarantee of freedom under Article 301 is subject to Part XIII. Article 304 enables a state legislature in the exercise of its legislative power (under Articles 245 and 246) to enact a law despite the fact that it may otherwise fall within the ambit of Articles 301 or 303. Article 303 contains the mandate that neither Parliament nor the legislature of the state can grant preferences to one state over another or discriminate between one state and another by virtue of the entries relating to trade and commerce in the lists of the Seventh Schedule. Article 303 postulates (in relation to Parliament) that the power conferred upon Parliament under Article 302 to impose restrictions on the freedom of trade, commerce or intercourse, in the public interest between one state and another or over any part of the territory of India cannot be exercised so as to grant preferences or to discriminate between one state and another. However, this embargo is lifted by clause (2) of Article 303 when Parliament is dealing with a situation of scarcity of goods in any part of the territory of India. In relation to the legislature of the state, Article 303(1) imposes the same mandate against the grant of preferences between states or the making of any discrimination. However, clause (2) of Article 303 does not apply to the state legislatures. Clause (1) of Article 303 is a restraint on discriminating between one state over another or from granting preferences between them. In other words, the treatment which is extended to one state has to be extended to every other state. The grant of preferences or the making of discrimination is proscribed. Article 303(1) is akin to a provision in international trade parlance conferring a 'most favoured nation' treatment. Under such an 'mfn' clause, treatment extended to one nation state has to be extended to the other. Article 303(1) embodies a similar principle inter se between the states so as to ensure a uniformity of treatment between states when Parliament or the state legislatures enact a law in exercise of their law making power. A state legislature which enacts a law is required to confer a parity of treatment to other states and is prevented from granting preferences to one state over another or from making discrimination between one state and another, by the operation of Article 303(1). Article 304(a), however, allows the legislature of a state to impose a tax on goods imported from other states or union territories so long as the tax is one which is imposed on similar goods manufactured or produced in that state. Article 304 (a) in other words has the effect of lifting an embargo which would arise under Article 301. The clause of subjection in Article 301 and the non-obstante clause of Article 304 can hence be harmonised.

168. Article 306 of the Constitution (prior to its repeal by the Constitution (Seventh Amendment) Act, 1956) dealt with the power of certain states in Part B of the First

Schedule to impose restrictions on trade and commerce. Article 306 before its deletion provided as follows :

> "306. Notwithstanding anything in the foregoing provisions of this Part or in any other provisions of this Constitution, any State specified in Part B of the First Schedule which before the commencement of this Constitution was levying any tax or duty on the import of goods into the State from other States or on the export of goods from the State to other States may, if an agreement in that behalf has been entered into between the Government of India and the Government of that State, continue to levy and collect such tax or duty subject to the terms of such agreement and for such period not exceeding ten years as may be specified in the agreement : Provided that the President may at any time after the expiration of five years from such commencement terminate or modify any such agreement if, after consideration of the report of the Finance Commission constituted under Article 280, he thinks it necessary to do so."

The above provision clearly envisages that taxes and duties which were being levied on imports into and exports from Part B states were restrictions. Hence, a specific provision was incorporated, to provide for their continuance for a stipulated period. That such taxes and duties would otherwise have infringed Article 301 is evident from the non-obstante provision permitting their continuance.

169. Article 306 as it was originally incorporated into the Constitution provided a clear indicator that the founding fathers did not intend to use the expression 'restrictions' in contradistinction to taxes or duties on the import or export of goods between states.

170. Article 304(a) elaborates that a particular form of taxation - a non-discriminatory tax on goods - shall not be construed to violate Article 301. But Article 304(a) is not exhaustive of the universe of taxation. Article 304(a) has three defining characteristics. The first is that the tax is a tax on goods. The second is that it is a tax on goods imported from other states. The third is the non-discrimination norm in relation to similar goods produced or manufactured in the state. A tax which fails to meet the yardstick embodied in Article 304(a) will violate Article 301. But Article 304(a) cannot be a basis for holding that every fiscal measure (apart from a discriminatory tax) lies outside the purview of Part XIII. For one thing, the rate of tax is but one element of taxation. There are other elements in a fiscal exaction including assessment, the machinery for collection and set offs and exemptions which can have an important bearing on whether the tax operates in a manner that impedes the freedom of interstate trade and commerce. Moreover, as we have noticed earlier, a discriminatory tax otherwise than on goods, does not attract the provisions of Article 304(a). Finally, a non-discriminatory tax may also become an impediment on the freedom of trade and commerce where the tax is so high as to render it confiscatory. Hence, a discriminatory fiscal imposition of the nature which offends Article 304(a) is illustrative of but not exhaustive of fiscal

171. The Constituent Assembly, while adopting Article 304 incorporated a marginal note which describes the ambit of the provision as : "restrictions on trade, commerce and intercourse amongst states". The marginal note is a broad indicator of constitutional

intent. It is a constitutional indicator of the position that a restriction on the freedom of trade and commerce can be fiscal or non-fiscal in origin. The marginal note evidently utilizes the expression "restrictions" in relation to the entirety of the article. Though a marginal note cannot override constitutional text nor can it control the specific meaning of the words used in the text, it is a broad indicator or pointer to the meaning intended.

172. For these reasons, it would be untenable to postulate as a general principle that it is only a discriminatory tax falling within the ambit of Article 304(a) that is subject to Part XIII of the Constitution.

I Tax legislation - Judicial review and Part XIII

I.1Taxation and Part XII

173. In early decisions of this Court, the issue as to whether the legislative power to tax was subject to constitutional control independent of Article 265 was analysed. The initial view was that the power of taxation was subject to exclusively to Article 265 under which a tax can be imposed only with the authority of law. Consequently, a Constitution Bench of this Court in *Ramjilal v. Income Tax Officer, Mohindargarh* [153], held that the protection against imposition and collection of taxes save by authority of law directly comes from Article 265 and is not secured by clause (1) of Article 31:

> "11... If collection of taxes amounts to deprivation of property within the meaning of Article 31(1), then there was no point in making a separate provision again as has been made in Article 265. It, therefore, follows that clause (1) of Article 31 must be regarded as concerned with deprivation of property otherwise than by the imposition or collection of tax, for otherwise Article 265 becomes wholly redundant. In the United States of America, the power of taxation is regarded as distinct from the exercise of police power or eminent domain. Our Constitution evidently has also treated taxation as distinct from compulsory acquisition of property and has made independent provision giving protection against taxation save by authority of law."

174. However, in *Kunnathat Thathunni Moopil Nair v. The State of Kerala*[154] , Chief Justice Sinha speaking for a Constitution Bench rejected the submission that Article 265 of the Constitution was "a complete answer" to the validity of a state taxing law (The Travancore- Cochin Land Tax, 1955). The Constitution Bench held that Article 265 imposes a limitation by which a tax cannot be levied or collected by a mere executive fiat. Under Article 265, a tax can be imposed only with the authority of law which, it was held, must mean a valid law. For a law to be valid, it must be enacted by a legislature which possesses legislative competence and the tax must accord with Article 13. Hence, the Constitution Bench ruled that if the enactment imposing a tax violates Article 14, it would have to be struck down since the guarantee of equal protection of law must extend even to taxing statutes. Another Constitution Bench in *Balaji v. Income Tax Officer, Special Investigation Officer* [155], rejected the submission that taxing legislation was immune to a challenge on the ground of a violation of Article 19. In *Chhotabhai Jethabhai Patel & Co. v. Union of India*[156], a Constitution Bench ruled that the judgment

in Ramjilal could not have meant that if a law imposing a tax is outside the legislative competence of the legislature enacting it, it could be a law under which a person could be deprived of property under Article 31 or regarding which the Supreme Court could not be approached for relief under Article 32. The Constitution Bench held that it was also not possible to accept a more limited proposition that once a tax law is covered by an entry in the legislative lists and does not contravene a direct prohibition such as Article 276 (2) or Article 286, such a law is immune from a challenge under Part III of the Constitution. A taxing legislation could be impugned on the ground of : (i) lack of legislative competence; (ii) violation of a prohibition under a specific article of the Constitution; or (iii) repugnancy to the fundamental rights guaranteed by Part III.

175. In *Raja Jagannath Baksh Singh v. State of U.P.* [157], the Constitution Bench held that though in Ramjilal (supra) there were general observations which indicated that the fundamental rights guaranteed in Part III could not be invoked in respect of a taxing statute, a consensus had emerged in subsequent decisions of this Court that a law imposing a tax could be challenged not only for want of legislative competence but also on the ground of its violating the freedoms contained in Part III.

176. A law which imposes a tax is not immune from constitutional challenge merely because taxation is a manifestation of the sovereign power of the state or because there is a presumption that a tax is imposed by the legislature in public interest. Taxing legislation is subject to constitutional restraints originating in the legislative competence of the legislature to enact the law, the guarantees of fundamental freedoms contained in Part III and constitutional limitations originating in the provisions of the Constitution.

I.2The standard of judicial review

177. The standard of judicial review in relation to taxing legislation however recognizes that there inheres in the legislature the power to determine the objects on which a tax should be levied and to classify persons or properties for the purposes of the levy. If the classification is rational, a taxing statute cannot be challenged merely because different rates of taxation are prescribed for different categories of persons or objects. The validity of a taxing statute cannot be challenged merely on the ground that the rate of taxation is excessive. However, if the statute is a colourable piece of legislation or a fraud on legislative power, it would be open to challenge on the ground that while enacting the law, the legislature has adopted a cloak or devise to confiscate the property of a citizen who is taxed. But such a conclusion cannot be reached merely on a finding that the tax which is imposed is unreasonably high or excessive.

178. Conceptually, the availability of judicial review in regard to taxing legislation is distinct from the standard of judicial review. Taxing legislation is not immune from constitutional challenges based on a lack of legislative competence, a breach of fundamental rights or a violation of a constitutional limitation or provision. But the standard of judicial review in relation to fiscal statutes recognizes that the legislature must possess a wide latitude to classify persons or objects for the purposes of the levy.

179. In Federation of Hotel *and Restaurant Association of India v. Union of India*[158], the

Constitution Bench applied the test of palpable arbitrariness when a fiscal statute is challenged on the ground of Article 14. The Court held :

> "46. It is now well settled though taxing laws are not outside Article 14, however, having regard to the wide variety of diverse economic criteria that go into the formulation of a fiscal policy, the legislature enjoys a wide latitude in the matter of selection of persons, subject matter, events, etc., for taxation. The tests of the vice of discrimination in a taxing law are, accordingly, less rigorous. In examining the allegations of a hostile, discriminatory treatment what is looked into is not its phraseology, but the real effect of its provisions. A legislature does not, as an old saying goes, have to tax everything in order to be able to tax something. If there is equality and uniformity within each group, the law would not be discriminatory. Decisions of this Court on the matter have permitted the legislatures to exercise an extremely wide discretion in classifying items for tax purposes, so long as it refrains from clear and hostile discrimination against particular persons or classes."
> ((Id. at p. 658-659)

I.3 Limitations of Sinha CJ's view in Atiabari

180. Part XIII of the Constitution uses the expression "law" in Articles 302, 303 and 304, among others. There is no reasonable basis for holding that Part XIII includes all laws enacted by Parliament or the State legislatures except laws falling under Entries 82 to 96C of the Union List and Entries 46 to 62 of the State List. The judgment of Chief Justice Sinha in Atiabari broadly enunciated four reasons for excluding taxes from Part XIII of the Constitution :

> "i) imposition of taxes is a manifestation of the sovereign power of the state which possess the inherent power to impose taxes to raise %evenues;
>
> ii)taxation is specifically governed by Part XII which is a self-contained code and the validity of a taxing statute cannot be assessed with reference to a provision outside Part XII;
>
> iii) taxes provide for resources to improve facilities for trade and do not constitute a restriction on the movement of trade; and
>
> iv) the concept of public purpose being implicit in every tax law, it cannot form a part of Article 301. With the greatest of deference to the view of the learned Chief Justice, it is difficult to subscribe to the general proposition that tax laws per se lie outside the ambit of Part XIII. Taxation is indeed a manifestation of the sovereign power of the state to raise revenues for public purposes. But the exercise of sovereignty is subject to the constitutional limitations of a written constitution. Enactment of law by a law making body which possess a legislative competence over the subject matter upon which it legislates is one of the constitutional limitations. The Constitution distributes legislative powers between the Union and States. While doing so it carves out fields of legislation which are reserved to the

Union and the States respectively. Legislative powers in relation to taxation are also distributed between the Union and the States. Hence, all legislative power (of which the legislative power to impose a tax is a part) is subject to the distribution provided in the Constitution. Exercise of sovereign power is governed by the norms of a written Constitution. Taxing statutes, like other legislation, are subject to constitutional limitations including those contained in Part XIII. Hence, the general notion that taxation is a manifestation of sovereign powers must also comprehend within that conceptualisation, the limitations which the Constitution imposes upon all legislative power of which the taxing power is a part.

181. The second ground which weighed in the decision of Chief Justice Sinha in Atiabari has been considered earlier. Article 245 mandates that all laws are subject to the provisions of the Constitution. From that basic premise, it must follow that the limitations on the taxing power are not only those which are referable to Part XII. A subject such as taxation may be referable to a specific part of the Constitution, such as Part XII. This does not mean that its validity must be assessed only with reference to the provisions of that Part. The provisions of the Constitution are not isolated or watertight compartments. Constitutional provisions do not rest in silos.

182. As regards the third rationale undoubtedly, the revenues which the state raises from fiscal exactions generate resources which are also utilized to augment trade and commerce. This, however, does not confer an immunity from a challenge that a law which is enacted in pursuance of the taxing power breaches specific provisions of the Constitution.

183. While the concept of public purpose is implicit in tax law, it is also implicit in all legislation which is presumed to be in the public interest. Yet the presumption of constitutionality or of legislation being in the public interest does not confer a protection or immunity against a specific challenge on the ground that it violates a constitutional limitation such as that originating in legislative competence, the fundamental rights or constitutional provisions.

I.4 Presidential sanction : the proviso to Article 304(b)

184. There is an aspect of the submission of the states bearing on the impact of the requirement of Presidential sanction under the proviso to Article 304(b), which requires close scrutiny. The submission is that if “reasonable restrictions” on the freedom of trade, commerce or intercourse with or within a state are construed to include a legislative measure imposing a tax, this would constitute a substantial encroachment on the power of the states to impose taxes. The requirement of obtaining prior Presidential sanction to a bill which is to be introduced or moved in the legislature of a state it is urged will, it is urged dilute the sovereign power of the states to impose taxes in the fields reserved for them and make them subservient to the Union.

185. While evaluating this submission, it must be emphasised that the proviso attaches to clause b of Article 304. Article 303 prohibits both Parliament and the legislature of a state from enacting laws granting preferences to one state over another or making discrimination between one state over another.

186. Article 303(2) makes an exception in respect of Union legislation enacted to deal with a situation of scarcity of goods in any part of the territory of India. The prohibition contained in clause 1 of Article 303 is, hence, lifted in the case of Parliament by clause 2. In the case of a state legislature, Article 303(1) is attracted where it grants preferences or makes a discrimination between one state and another. Article 304 in its non-obstante clause refers inter alia to Article 303. Consequently, where a state legislature seeks to enact legislation granting a preference to one state over another or to make a discrimination of the nature referred to in Article 303(1), it must comply with the requirements of a Presidential sanction under the proviso to Article 304(b). Where the law enacted by the state legislature would result in a preference or discrimination prohibited under Article 303(1), the embargo can be lifted upon obtaining the previous sanction of the President under the proviso to Article 304(b). J Article 304(a) : The principle of non-discrimination 187Article 304(a) has been analysed and applied in judicial precedent over the last six decades. The context in which each of the decided cases arose for decision has undoubtedly shaped and refined the jurisprudence on the subject. Successive Benches have fleshed out the content of its language. While understanding Article 304 (a), this Court has to analyse the meaning of the expressions (i) 'goods imported from other states'; (ii) 'any tax to which similar goods manufactured or produced in that state are subject'; and (iii) 'so, however, as not to discriminate between goods so imported and goods so manufactured'. While defining the meaning of these expressions, judicial review is confronted with the basic question of when Article 304(a) would apply and the situations in which the requirement of a non-discriminatory tax is fulfilled. An important aspect of Article 304(a) is whether it permits a classification by the state legislature based on the need to achieve the economic development of the state. If development is a legitimate priority, to what extent does Article 304(a) condition the power of the state legislature to encourage the growth of its own industries by the grant of incentives, rebates and exemptions through fiscal legislation?

J.1 Precedent : 1963 to 1980

188. An early decision arose in *State of Madhya Pradesh v. Abdeali* [159]. The state government issued a notification under the Madhya Bharat Sales Tax Act, 1950, exempting the sale of footwear from the payment of sales tax subject to three conditions :

> "(i) The foot-wear had to be hand-made and not manufactured on a power machine;
>
> (ii) The sale price should not exceed a stipulated amount; and
>
> (iii)The sale must be by a manufacturer or a member of his family."

189. A Constitution Bench of this Court held that the notification did not discriminate between foot-wear manufactured or produced in the state and that which was imported from other states since the three conditions of the notification equally applied to all foot-

wear irrespective of its origin. A notification granting an exemption for the benefit of small manufacturers making hand-made shoes of a small value who may be unable to compete with large manufacturers was valid. Significantly, in relation to Article 304(a) it was held that the exemption notification made no discrimination between out-of state manufacturers and in-state manufacturers since its conditions applied equally to both. A manufacturer situated outside the state could also claim the benefit of the exemption upon fulfilling the conditions of the exemption. Hence Article 304(a) was held not to have been breached.

190. In *Firm A.T.B. Mehtab Majid v. State of Madras*[160], the validity of Rule 16 of the rules framed under the Madras General Sales Tax Act, 1939 was challenged by the petitioner who was a dealer in hides and skins. The petitioner sold material which was tanned outside the state as well as what was tanned inside. The contention was that tanned hides and skins imported from outside the state and sold within were subject to a higher rate of tax than the tax imposed on hides and skins tanned and sold within the state. Moreover, hides or skins imported from outside the state after purchase in a raw condition and then tanned inside the state were subject to higher taxes than those purchased in a raw condition within the state and tanned there. The Constitution Bench rejected the submission that Article 304(a) is attracted only when the goods enter the state while crossing its border. In other words, the imposition provided under clause (a) must not be only at the point of entry. The plea of discrimination was upheld by this Court since the sale of hides or skins which had been purchased in the state and then tanned within the state was not subject to any further tax. This Court found that there was a breach of Article 304(a) for the following reasons :

> "17 If the dealer has purchased the raw hide or skin in the State; he does not pay on the sale price of the tanned hides or skins; he pays on the purchase price only. If the dealer purchases raw hides or skins from outside the State and tans them within the State, he will be liable to pay sales tax on the sale price of the tanned hides or skins. He too will have to pay more for tax even though the hides and skins are tanned within the State, merely on account of his having imported the hides and skins from outside and having not therefore paid any tax under sub-rule (1)."
>
> Significantly, the Constitution Bench also dealt with the submission of the state that
> the circumstance of hides or skins tanned within the state and on which tax had been paid earlier at the time of their purchase in a raw condition was sufficient to consider them to be different from hides or skins tanned outside the state. This Court held that :
>
> "18...The similarity contemplated by Article 304(a) is in the nature of the quality and kind of the goods and not with respect to whether they were subject of a tax already or not."

191 In a subsequent decision in A *Hajee Abdul Shakoor v. State of Madras*[161], this Court held that Section 2(1) of the Madras General Sales Tax (Special Provisions) Act, 1953

discriminated against imported hides and skins sold upto 1 August 1957. The rate of tax on the sale of tanned hides and skins was:

> "10 2 per cent on the purchase price of those hides and skins in the untanned condition, while the rate of tax on the sale of raw hides and skins in the State during 1955 to 1957 is 3 pies per rupee." Referring to the judgment in Mehtab Majid, this Court held that:
>
> "10. In the earlier case, discrimination was brought about on account of sale price of tanned hides and skins to be higher than the sale price of untanned hides arid skins, though the rate of tax was the same, while in the present case, the discrimination does not arise on account of difference of the price on which the tax is levied as the tax on the tanned hides and skins is levied on the amount for which those hides and skins were last purchased in the untanned condition, but on account of the fact that the rate of tax on the sale of tanned hides and skins is higher than that on the sale of untanned hides and skins. The rate of tax on the sale of tanned hides and skins is 2% on the purchase price of those hides and skins in the untanned condition while the rate of tax on the sale of raw hides and skins in the State during 1955 is 3 pies per rupee. The difference in tax works out to 7/1600th of a rupee, i.e. a little less than, U naya paise per rupee. Such a discrimination would affect the taxation upto the 1st of August 1957 when the rate of tax on the sale of raw hides and skins was raised to 2% of the sale price."

192. Another judgment of a Constitution Bench in S*tate of Madras v. N.K. Nataraja Mudaliar*[162,] involved a case where the provisions of the Central Sales Tax Act, 1956 were challenged on the ground that the Act permitted the levy of tax at varying rates in different states. This challenge was accepted by the High Court on the ground that the imposition of varying rates of tax in different states on similar inter-state transactions constituted an impediment, thereby offending Article 301. While tracing the history of the legislation Justice J.C. Shah speaking on behalf of three judges held that the enactment encumbered the movement of trade and commerce for the following reasons :

> "10. Tax under the Central Sales Tax Act on inter-State sales, it must be noticed, is in its essence a tax which encumbers movement of trade or commerce, since by the definition in Section 3 of the Act, a sale or purchase of goods is deemed to take place in the course of inter-State trade or commerce, if it– (a) occasions the movement of goods from one State to another; (b) is effected by a transfer of documents of title to the goods during their movement from one State to another."
>
> However, the judgment held that the Central Sales Tax Act which was enacted for
> imposing a tax to be collected and retained by the state did not either grant a preference to one state or another or make any discrimination merely because varying rates of tax prevailed in different states. This Court rejected the view which had prevailed in the High Court that different rates of tax on the sale of the same or similar commodities by different states placed an unequal burden on

inter-state trade:

> "14. The flow of trade does not necessarily depend upon the rates of sales tax: it depends upon a variety of factors, such as the source of supply, place of consumption, existence of trade channels, the rates of freight, trading facilities, availability of efficient transport and other facilities for carrying on trade. Instances can easily be imagined of cases in which notwithstanding the lower rate of tax in a particular part of the country and goods may be purchased from another part, where a higher rate of tax prevails. Supposing in a particular State in respect of a commodity, the rate of tax is 2 per cent but if the benefit of that low rate is offset by the freight which a merchant in another State may have to pay for carrying that commodity over a long distance, the merchant would be willing to purchase the goods from a nearer State, even though the rate of tax in that State may be higher. Existence of long-standing business relations, availability of communications, credit facilities and a host of other factors – natural and business – enter into the maintenance of trade relations and the free flow of trade cannot necessarily be deemed to have been obstructed merely because in a particular State the rate of tax on sales is higher than the rates prevailing in other States."
>
> (emphasis supplied)

The object of enacting a central legislation on the subject was explained thus:-

> "17 But since the power of taxation could be exercised in a manner prejudicial to the larger public interests by the States, it was found necessary to restrict the power of taxation in respect of transactions which had an inter-State content. Amendment of Article 286 and the enactment of the Sales Tax Validation Act 1956, and the Central Sales Tax Act, 1956, were all intended to serve a dual purpose: to maintain the source of revenue from sales tax to the States and at the same time to prevent the States from subjecting transactions in the course of inter-State trade so as to obstruct the free flow of trade by making commodities unduly expensive."

193. The leading judgment held that Article 304 prohibits the imposition of differential rates of tax by the same state on goods manufactured or produced in the state and similar goods imported into the state. But where the rates of tax imposed on imported goods by a taxing state are not different from the rates of tax on goods manufactured or produced within, Article 304(a) has no application. Consequently, the prevalence of different rates of sales tax in the states under the Central Sales Tax Act, was held not to be determinative of the giving of a preference or making of a discrimination. Justice R.S. Bachawat while agreeing with the order passed by the leading majority judgment, however, held that just as a sales tax on intra-state sales would not normally offend Article 301, similarly a tax on inter-state sale would not do so. In his view, a tax on sale did not directly or immediately operate on the free flow of trade or the free movement of the transport of goods from one part of the country to another. Justice K.S. Hegde concurred with the majority the ground that the provisions of the Central Sales Tax Act had no direct or immediate impact on inter-state trade or commerce since sufficient

safeguards were provided - firstly, by providing for the levy of sales tax in the state in which the goods are produced and secondly, by placing restrictions on the power of the states in fixing the rates.

194. The judgment of the Constitution Bench in *Kalyani Stores v. The State of Orissa* [163], involved a challenge to a levy imposed by the state of Orissa under the Bihar and Orissa Excise Act, 1915 at a rate of Rs.40/- per L.P. Gallon on foreign liquor of Indian manufacture imported into the state from other parts of the country. Subsequently, acting under the Bihar and Orissa Excise Act, 1915, the duty was enhanced to Rs.70/- per L.P. Gallon. Under Section 27 of the Bihar and Orissa Excise Act, 1915, a countervailing duty was provided on an excisable article imported into the state. Countervailing duties are provided for in Entry 51 of List II to the Seventh Schedule to the Constitution. This Court noted that countervailing
duties can only be levied if similar goods are actually produced or manufactured in the state on which excise duties are being levied :

> "4 The fact that countervailing duties may be imposed at the same or lower rates suggests that they are meant to counterbalance the duties of excise imposed on goods manufactured in the State. They may be imposed at the same rate as excise duties or at a lower rate, presumably to equalise the burden after taking into account the cost of transport from the place of manufacture to the taxing State. It seems therefore that countervailing duties are meant to equalise the burden on alcoholic liquors imported from outside the State and the burden placed by excise duties on alcoholic liquors manufactured or produced in the State.
> If no alcoholic liquors similar to those produced or manufactured imported into the State are produced or manufactured, the right to impose counterbalancing duties of excise levied on the goods manufactured in the State will not arise. It may therefore be accepted that countervailing duties can only be levied if similar goods are actually produced or manufactured in the State on which excise duties are being levied."
> During the course of discussions, the Constitution Bench held that the restriction on the freedom guaranteed by Article 301 could only be justified if it fell within Article 304. The reasonableness of the restriction had to be adjudged having regard to the purpose for imposing the restriction in the public interest. In that case, it was held that since no foreign liquor was produced or manufactured in the State of

> "7...Without entering upon an exhaustive categorization of what may be deemed "required in the public interest", it may be said that restrictions which may validly be imposed under Article 304(b) are those which seek to protect public health, safety, morals and property within the territory. Exercise of the power under Article 304(a) can only be effective if the tax or duty imposed on goods imported from other States and the Tax or duty imposed on similar goods manufactured or produced in that State are such that there is no discrimination against imported goods. As no foreign liquor is produced or manufactured in the State of Orissa. The power to legislate given by Article 304 is not available and the restriction

which is declared on the freedom of trade, commerce or intercourse by Article 301 of the Constitution remains unfettered."

195. The notification enhancing the duty was held to violate Article 301 and was found not to have complied with Articles 304(a) and (b). The judgment in Kalyani Stores was explained and confined to the facts of the case in a subsequent decision in *State of Kerala v. A.B. Abdul Khadir* [164]. In Abdul Khadir this Court held that the earlier decision did not intend to lay down a proposition of universal applicability that the imposition of a duty or tax in every case would per se be an infringement of Article 301 and only such restrictions which directly or immediately impede the free flow of trade fall within the prohibition of Article 301.

196. A Constitution Bench of this Court in *Rattan Lal & Co. v. The Assessing Authority , applied the test formulated in N.K. Nataraja Mudaliar (supra) in the context of a challenge*[165] *to* the Punjab General Sales Tax (Amendment and Validation) Act, 1967 and the Punjab Sales Tax (Haryana Amendment and Validation) Act, 1967. The Constitution Bench held that so long as the rate of tax is the same between goods imported from other states and similar goods, produced or manufactured within the state, Article 304 is satisfied.

197. In *V. Guruviah Naidu and Sons v. State of Tamil Nadu*[166], a Bench of two Judges of this Court repelled a challenge to the validity of a tax imposed under the Madras General Sales Tax Act, 1959 on raw hides and skins and on dressed hides and skins. In that case the rate of sales tax for raw hides and skins was three per cent, whereas for dressed hides and skins it was one and a half per cent. The Court held that a lower rate of tax in the case of dressed hides and skins was prescribed to offset the difference between the higher price of dressed hides and skins and the lower price of raw hides and skins. No material was shown to indicate that despite this lower rate of tax, imported hides and skins were subjected to discrimination. Upholding the levy, the Division Bench held as follows :-

"9.. The question as to when the levy of tax would constitute discrimination would depend upon a variety of factors including the rate of tax and the item of goods in respect of the sale of which it is levied. The scheme of Items 7(a) and 7(b) of the Second Schedule to the State Act is that in case of raw hides and skins which are purchased locally in the State, the levy of tax would be at the rate of 3 per cent at the point of last purchase in the State. When those locally purchased raw hides and skins are tanned and are sold locally as dressed hides and skins, no levy would be made on such sales as those hides and skins have already been subjected to local tax at the rate of 3 per cent when they were purchased in raw form. As against that, in the case of hides and skins which have been imported from other States in raw form and thereafter tanned and then sold inside the State as dressed hides and skins, the levy of the tax is at the rate of 11/2 per cent at the point of first sale in the State of the dressed hides and skins. This levy cannot be considered to be discriminatory as it takes into account the higher price of dressed hides and skins compared to the price of raw hides and skins. It also further takes note of the fact that no tax under the State Act has been paid in

respect of those hides and skins. The legislature, it seems, calculated the price of hides and skins in dressed condition to be doubled the price of such hides and skins in raw state. To obviate and prevent any discrimination or differential treatment in the matter of levy of tax, the legislature therefore prescribed a rate of tax for sale of dressed hides and skins which was half of that levied under Item 7(a) in respect of raw hides and skins." (Id. at p. 239-240)

198. A subsequent judgment of a Bench of two Judges in *State of Karnataka v. Hansa Corporation*[167], involved a challenge to the constitutional validity of an entry tax legislation, namely, the Karnataka Tax on Entry of Goods Into Local Areas for Consumption, Use or Sale Therein Act, 1979. The law was enacted under Articles 245 and 246 read with Entry 52 of the State List. Explaining the ambit of Article 304(a), this Court held that :

"30. Article 304 lifts the embargo placed on the legislative power of State to enact law which may infringe the freedom of inter-State trade and commerce if its requirements are fulfilled. Article 304(a) imposes a restriction on the power of legislature of a State to levy tax which may be discriminatory in character by according discriminatory treatment to goods manufactured in the State and identical goods imported from outside the State. The effect of Article 304(a) is to treat imported goods on the same basis as goods manufactured or produced in a State. This Article further enables the State to levy tax on such imported goods in the same manner and to the same extent as may be levied on the goods manufactured or produced inside the State. If a State tax law accords identical treatment in the matter of levy and collection of tax on the goods manufactured within the State and identical goods imported from outside the State, Article 304(a) would be complied with. There is an underlying assumption in Article 304(a) that such a tax when levied within the constraints of Article 304(a) would not be violative of Article 301 and State legislature has the power to levy such tax." (Id. at p. 712) The Court considered whether the Act being leviable on the entry of goods into a local area, it had a direct and immediate impact on the movement of goods thereby infringing the freedom of inter-state trade guaranteed in Article 301. In that context, the Court observed thus :

"32....To the extent, the impugned tax is levied on the entry of goods in a local area it cannot be gainsaid that its immediate impact would be on movement of goods and the measure would fall within the inhibition of Article 301. Can it, however, be said that this tax imposes restrictions which in the facts and circumstances of the case could not be said to be reasonable?" (Id. At p. 713) The Court held that the petitioners were unable to establish before the High Court that the burden of the tax was so heavy as to constitute an unreasonable restriction on the freedom of trade and commerce. The Court held that a levy which was reasonable in its impact on the movement of goods and was imposed for augmenting municipal finances which had been adversely affected due to the abolition of octroi could not be held to be an impediment to inter-state trade and commerce. Even if the tax imposed an economic impediment to the activity taxed, it was held not to be unreasonable or against public interest. The Court

observed that though the Bill had not received the sanction of the President under clause (b) of Article 304, this was cured under Article 255 by the grant of Presidential assent and hence the legislation fell within the purview of Article 304(b). Being not discriminatory, it was held that Article 304(a) was not breached. The constitutional validity of the legislation was thus analysed on both the anvil of clauses (a) and (b) of Article 304 by the Bench of two Judges.

J.2 Exemptions and incentives : Video Electronics and Mahavir

199. A Bench of two Judges of this Court in *Weston Electroniks v. State of Gujarat*[168], dealt with the validity of an exemption granted under the Gujarat Sales Tax Act, 1969. A notification was issued under Section 49(2) of the Act by which sales tax on television sets imported from outside the state was fixed at 10 per cent, whereas it was one per cent for goods manufactured within the state. Adverting to the judgment of the Constitution Bench in Mehtab Majid, a Bench of two learned Judges noted the defence of the state that the rate of tax was reduced for locally manufactured goods by way of an incentive, placing reliance on clauses (b) and (c) of Article 39 of the Constitution. This in the view of the Court did not provide a justification for a discrimination between imported goods and goods which were locally manufactured or produced. The prescription of a lower rate of tax for the latter was held to be invalid. This Court held :

> ". An exception to the mandate declared in Article 301 and the prohibition contained in clause (1) of Article 303 can be sustained on the basis of clause (a) of Article 304 only if the conditions contained in the latter provision are satisfied. In the result, the discrimination effected by applying different rates of tax between goods imported into the State of Gujarat and goods manufactured within the State must be struck down."

200. The judgment in Weston Electroniks was considered but distinguished by a larger Bench of three Judges of this Court in Video *Electronics Pvt. Ltd. v. State of Punjab* [169]. The judgment of this Court, inter alia, dealt with a challenge to the constitutional validity of notifications issued under the Uttar Pradesh Sales Tax Act, 1948, as well as under the Punjab General Sales Tax Act. Under the notification issued under the Uttar Pradesh legislation, an exemption from the payment of sales tax was granted for goods manufactured in new industrial units, where the date of commencement of production fell between two stipulated dates. The exemption was for a stipulated period reckoned from the date of first sale if such sale took place not later than six months from the commencement of production. The period of exemption was confined for a specified period of three to seven years. Insofar as the State of Punjab was concerned, sales tax at the rate of 12 per cent was provided on electronic goods sold within the state irrespective of their manufacture. In pursuance of a notification issued under the sales tax law, the rate of sales tax payable by electronic manufacturing units producing goods specified there under was brought down from 12 per cent to 1 per cent. The reduction in sales tax was defended on the ground that it was an incentive to a backward industrial state. While affirming the legality of the exemption notifications, a Bench of three learned Judges observed that this was not a case involving "a naked blanket preference in favour of locally manufactured goods, as against goods coming from outside ***the***

state[170]". The Court held that the both under the notifications issued in Uttar Pradesh and in Punjab there was no discrimination against goods manufactured outside the state for the following reasons:

> "35....In case of Punjab, an overwhelmingly large number of local manufacturers of similar goods are subject to sales tax and, therefore, the general statement that the manufacturers within the State are favoured against the manufacturers outside the State, is incorrect. Under the notifications in case of U.P., only newly set up units are eligible to claim the benefits thereunder for a limited period of 5 years and that also only if they strictly comply with the terms and conditions set out in the notification." (Id. at p. 113)

201. A close reading of the judgment in Video Electronics would thus indicate that both sets of notifications involving the States of Uttar Pradesh and Punjab were carefully structured to cover one or more of the following circumstances:

> "(i)Availability of a reduced rate of sales tax to new industrial units;
>
> (ii) Applicability of a reduced rate of sales tax to producers of certain specified goods, such as electronic goods;
>
> (iii) Limitation of the period during which the reduced rate of tax could operate; and
>
> (iv)Applicability of the general rate of sales tax to an overwhelmingly large number of local manufacturers, at par with imported goods.

202. While sustaining the grant of a reduced rat of sales tax, this Court distinguished, inter

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[170](Id. at p. 112, Para 35)

alia, the judgment in Weston Electroniks (supra) and similar cases in the following observations :

> "30 These cases were not at all concerned with granting of exemption to a special class for a limited period on specific conditions of maintaining the general rate of tax on the goods manufactured by all those producers in the State who do not fall within the exempted category at par with the rate applicable to imported goods as we have read these cases. Hence, it was not necessary in those decisions to consider the problem in its present aspect. If, however, the said power is exercised in a colourable manner intentionally or purposely to create unfavourable bias by prescribing a general lower rate on locally manufactured goods either in the shape of general exemption to locally manufactured goods or in the shape of lower rate of tax, such an exercise of power can always be struck down by the courts. That is not the situation in the instant cases." (Id. at p. 110)
>
> (emphasis supplied)

However, in the same judgment, the following observations have been made :

> "20 In our opinion, Part XIII of the Constitution cannot be read in isolation. It is part and parcel of a single constitutional instrument envisaging a federal scheme and containing general scheme conferring legislative powers in respect of the matters relating to List II of the Seventh Schedule on the States. It also confers plenary powers on States to raise revenue for its purposes and does not require that every legislation of the State must obtain assent of the President. Constitution of India is an organic document Hence, the economic development of States to bring these into equality with all other States and thereby develop the economic unity of India is one of the major commitments or goals of the constitutional aspirations of this land. For working of an orderly society, economic equality of all the State is as much vital as economic unity."
>
> (Id at p. 104)

203. The substratum of the judgment in Video Electronics, clearly is that Article 304(a) would not be breached by a classification brought about by a carefully structured notification which grants incentives to local industry of a specified class of units, with reference to a specific category of manufactured goods and for a stipulated period. If the observations in paragraph 20 (quoted above) are however, construed to set a broad principle, that would defeat the primary objective underlying Article 304(a) of the Constitution. This was noticed in a subsequent decision in Shree Mahavir Oil Mills v. State of J&K171. In that case, under the J&K General Sales Tax Act, 1962, sales tax on edible oil was prescribed at 4 per cent. However, in order to protect the local edible oil industry, the state government issued a notification directing that the goods manufactured by a dealer operating as a small-scale industrial unit in the state would be exempted from the payment of tax to the extent and for the period specified. Subsequently, edible oils in general were shifted from Schedule D to Schedule C attracting tax at 8 per cent. There were in fact no large industries in Jammu and Kashmir producing edible oil. Out-of state manufacturers unsuccessfully impugned the notification before the High Court. Explaining the ambit of Article 304, the Bench of two learned Judges observed thus :

> "8....The idea was not really to empower the State Legislatures to levy tax on goods imported from other States and Union Territories — that they are already empowered by other provisions in the Constitution — but to declare that that power shall not be so exercised as to discriminate against the imported goods vis-a-vis locally manufactured goods. The clause, though worded in positive language has a negative aspect. It is, in truth, a provision prohibiting discrimination against the imported goods. In the matter of levy of tax — and this is important to bear in mind — the clause tells the State Legislatures — "tax you may the goods imported from other States/Union Territories but do not, in that process, discriminate against them vis-a-vis goods manufactured locally". In short, the clause says: levy of tax on both ought to be at the same rate. This was and is a ringing declaration against the States creating what may be called "tax barriers" — or "fiscal barriers", as they may be called — at or along their

boundaries in the interest of freedom of trade, commerce and intercourse throughout the territory of India, guaranteed by Article 301. As we shall presently point out, this clause does not prevent in any manner the States from encouraging or promoting the local industries in such manner as they think fit so long as they do not use the weapon of taxation to discriminate against the imported goods vis-a-vis the locally manufactured goods. To repeat, the clause bars the States from creating tax barriers — or fiscal barriers, as they can be called — around themselves and/or insulate themselves from the remaining territories of India by erecting such "tariff walls." (Id. at p. 45)

204. The judgment in Video Electronics was distinguished on the ground that in that case the notifications of the States of Uttar Pradesh and Punjab were carefully circumscribed :

"22 So far as the Uttar Pradesh notification was concerned, it was held that inasmuch as it was a case of grant of exemption "to a special class for a limited period on specific conditions" and was not extended to all the producers of those goods, it does not offend the freedom guaranteed by Article 301. Similarly, in the case of Punjab notification, it was held that since the exemption is for certain specified goods and also because "an overwhelmingly large number of local manufacturers of similar goods are subject to sales tax", it cannot be said that local manufacturers were favoured as against the outside manufacturers." (Id. at p. 51) Again, it was held that :

> "23. All the above observations were made to justify (1) grant of incentives and subsidies and (2) exemption granted to new industries, of a specified type (small-scale industries commencing production within the two specified dates) and for a short period. They were not meant to nor can they be read as justifying a blanket exemption to all small-scale industries in the State irrespective of their date of establishment. The case before us clearly falls within the ratio of the Constitution Bench decision in A.T.B. Mehtab Majid and the decisions in Indian Cement, W.B. Hosiery Assn. and Weston Electroniks. The limited exception created in Video Electronics does not help the State herein for the reason that exemption concerned herein is neither confined to "new industries", nor is circumscribed by other conditions of the nature stipulated in the Uttar Pradesh notification. It is not possible to go on extending the limited exception created in the said judgment, by stages, which would have the effect of robbing the salutary principle underlying Part XIII of its substance. Indeed, it has been the contention of Shri Salve that, on principle, the exception carved out in Video Electronics is unsustainable. For the purpose of this case, it is not necessary for us to say anything about the correctness of Video Electronics. Suffice it to say that the limited exception carved out therein cannot be widened or expanded to cover cases of a different kind. It must be held that the total exemption granted in favour of small-scale industries in Jammu and Kashmir producing edible oil (there are no large-scale industries in that State producing edible oil) is not sustainable in law." (Id. at p. 52)

205. The Court cautioned that a limited exception which had been carved out in Video

Electronics should not be enlarged “lest it eat up the main provision.” An unconditional exemption in the case of edible oil produced within the state from sales tax while subjecting similar goods produced in other states to sales tax at 8 per cent was held to violate Article 304(a) of the Constitution.

206. The judgment in Shree Mahavir Oil Mills expressly left open the correctness of the view in Video Electronics. In Shree Mahavir Oil Mills an exemption from the payment of sales tax altogether granted to local industry was set aside as violating Article 304(a). The earlier decision in Video Electronics was distinguished on the ground that it related to a case not involving a blanket preference.

J.3 Article 304(a) and reasonable classification,

207. Does Article 304(a) prohibit a state from making a reasonable classification? Article 303 contains a prohibition on the legislature of a state granting a preference to one state over another and for making a discrimination. Article 304 operates, inter alia, as an exception to the norm contained in Article 303 as a result of its non-obstante provision. Under clause (a) of Article 304 a state may impose on goods which are imported from other states “any tax” to which similar goods manufactured or produced in that state are subject. This is followed by the further requirement that the imposition of such a tax shall “so however” not discriminate between goods so imported and goods so manufactured or produced. The principle which underlies clause (a) of Article 304 is non-discrimination between goods imported from another state and goods produced or manufactured within. Clause (a) enables the state legislature to impose a tax on goods imported, in the exercise of its legislative power, so long as that tax is imposed also on similar goods manufactured or produced within. The latter part of clause (a) which contains a mandate against discrimination must have some meaning. In drafting the provision, the founding fathers evidently did not confine it merely to a norm providing a parity of taxes between imported goods and similar goods produced or manufactured within. While stipulating that “any tax” to which similar goods produced or manufactured in the state are subject can be imposed on goods imported into the state from other states, clause (a) contains the mandate that there should be no discrimination between goods, that are imported and goods that are manufactured within. The judgment in Video Electronics construed Article 304(a) as not precluding a state from taking steps to promote the growth of its own nascent industry. In the case of the State of Punjab, the defence of the State was that a reduced rate of sales tax was imposed to boost the electronics manufacturing industry and to stop existing industrial units shifting to neighbouring states, particularly having regard to “the prevailing peculiar circumstances of Punjab”. Moreover, while states, such as Gujarat and Maharashtra were fully developed industrial states, Punjab at that stage was backward in terms of industrial growth. These factors undoubtedly weighed with this Court in sustaining the notification. 208 A state does have a legitimate concern and interest in ensuring the growth and development of its own industry. Levels of industrial growth and economic development are not uniform across the country. A state legislature can have a legitimate interest, in the exercise of its law making power, to ensure balanced development and growth of its industry, particularly, in the nascent stage of industrial development. Yet, while doing so and granting incentives the legislature or as its delegate, the state government must ensure that the grant of incentives is carefully structured so as not to defeat the

underlying spirit and object of Article 304(a). Moreover, when the grant of such an incentive is challenged, it is for the state to justify it with reference to circumstances which have a bearing on legitimate state interest.

J.3.1 Formal and substantive equality

209. Equality and non-discrimination are elements of the same universe. Equality has both a formal and substantive content. In a formal sense, equality perceives of governance under the same legal regime and the application of the same legal principles. Uniform application of law fulfils the norm of formal equality. Substantive equality looks beyond formal equality. That which may satisfy the requirements of formal equality may be inadequate and insufficient to meet the vision of substantive equality. Substantive equality recognises that there are histories of discrimination based on social background, gender and access to resources. They determine the pursuit of opportunity. Hence, formal equality may not necessarily result in just outcomes. Treating all individuals alike may perpetuate deprivation and denial of economic opportunity to those for whom the social order has not provided equal access to education or to the resources necessary for economic advancement. Hence, substantive equality is premised on the foundation that in order to produce just outcomes and a real equality between individuals who are unequally situated, the legal regime must comprehend an understanding of their past histories of discrimination, disability and injustice.

210. Regions within a nation are not equal in a real sense in terms of economic advancement and social development. Typically, economic development has spread along areas which developed around the availability of infrastructure and resources. As ports and railways developed over the last century and a half, the benefits of development permeated to regions where economic opportunity was available. Yet, other areas of the country have remained in a state of comparative under-development as a result of circumstances such as geographical isolation and the absence of developed means of communication. Many regions have suffered from the absence of education and unavailability of access to health and sanitation. Social deprivation and discrimination have been the defining characteristic of large swathes of the nation. In this background, substantive equality like its mirror image-non-discrimination-construes the need for development in terms of mitigating regional histories of suffering and strife, and of denial, deprivation and discrimination.

211. Article 304(a) is an amalgam of formal as well as substantive norms of equality. At a formal level, the provision requires that when a state imposes a tax on imported goods, the tax must likewise be imposed on similar goods which are manufactured or produced in the state. Parity of tax between domestic goods produced and manufactured in a state with those which are imported from other states is the first and formal requirement. But beyond this, Article 304(a) brings into focus substantive principles by embodying a norm of non-discrimination in its latter stipulation. Non-discrimination in a substantive sense requires a level playing-field. Two states in the nation may not be comparable in terms of social development and economic advancement. One state may be industrialised with a growth of capital investment in

urban infrastructure while another state may be predominantly agricultural. Article 304(a) does not prohibit a state from taking steps that are necessary for development and growth within its territories. But the submission is that while a state is at liberty to adopt policies which lead to its own economic advancement, it cannot utilise tax treatment as a measure to do so in a manner that would be forbidden by Article 304(a). This submission undoubtedly carries a degree of weight. But equally, parity of tax treatment between goods produced and manufactured in a state and those which are imported from other states must be balanced with the need to produce a state of non-discrimination in a
substantive as opposed to formal sense. Hence, the judgment of this Court in *Shree Mahavir Oil Mills v. State of J&K*[171] , while construing the earlier decisions in Video Electronics, held that the limited exception carved out in the latter decision should not consume the rule. Video Electronics was a situation where a rebate of sales tax was carefully structured to cover industrial units of a well-defined class over a measurable period of time and for rational reasons. This was not an unrestricted or blanket preference to domestic goods. Article 304(a) was intended to protect freedom of trade and commerce from protectionism and parochial demands in the interest of the economic unity of the nation. Hence, while Article 304(a) cannot be read to prohibit a classification, it cannot be read to allow states to pursue policies of protectionism that destroy the essential freedom of trade and commerce.

J.4 Production and manufacture within the home state

212. Another aspect which needs close analysis is whether under Article 304(a), it is necessary that a state must actually produce or manufacture goods similar to goods imported from other states which are sought to be taxed. The crucial words are “any tax to which similar goods manufactured or produced in that state are subject”. Article 304(a) is not in the nature of a countervailing duty. Entry 51 of List II of the Seventh Schedule on the other hand, provides for countervailing duties and is as follows :

> “51. Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India-
>
> (a) Alcoholic liquors for human consumption;
>
> (b) Opium, Indian hemp and other narcotic drugs and narcotics; But not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.”

213. The words “similar goods manufactured or produced” are common to both Article 304(a) and Entry 51. However, the notion of a countervailing duty under Entry 51 (as the judgment in Kalyani Stores explains) is intended to counterbalance the duty of excise levied on articles which are produced or manufactured in the state. The countervailing duty is imposed on articles which are produced or manufactured elsewhere in India. In the context of a countervailing duty, this Court in Kalyani Stores held that it postulates the actual production or manufacture of goods. This principle

cannot be extrapolated to Article 304(a) where the tax which is imposed is not in the nature of a countervailing duty. Article 304(a), when it refers to a tax on goods, covers taxes on any aspect of goods which fall within the legislative competence of the state legislature. The latter part of Article 304(a) which contains the words "so however as not to discriminate between goods so imported and goods so manufactured and produced" is not a surplusage. The object of the latter part is to ensure that there is no discrimination between goods which are produced or manufactured in the state and goods which are imported from other states. If a particular rate of duty is levied on goods which are produced or manufactured in a state, a higher rate of duty cannot be levied on goods imported from other states. This, however, does not preclude a state from imposing a duty on imported goods where it does not actually produce or manufacture goods of that description. The observations of this Court in Kalyani Stores were made in the context of a countervailing duty under Entry 51 of List II which is distinguishable. A state, in other words, is not confined by Article 304(a) to impose a tax on imported goods, confined only to the basket of goods actually produced or manufactured within that state. To take an example, if motor vehicles are manufactured in six states, Article 304(a) does not restrict the power of the state legislatures of the other states to impose a tax (in the exercise of the legislative power) with respect to motor vehicles. Any other construction would lead to the unintended, if not absurd, consequence that a tax on goods which are imported from other states can be levied only by those states which actually manufacture similar goods within the state. If a state does not manufacture or produce goods similar to the imported goods on which a tax is imposed, no question of discrimination will arise. The object of Article 304(a) is to prevent disparity of treatment between goods that are produced or manufactured in a state and goods which a state imports from other states. Where a state does not actually produce or manufacture goods of that description. no issue of discrimination qua Article 304(a) would arise.

K Entry Tax

214. Entry 52 of List II to the Seventh Schedule of the Constitution provides for :

"52. Taxes on the entry of goods into a local area for consumption, use or sale therein." Entry 89 of List I provides for terminal taxes on goods or passengers, carried by railway, sea or air; taxes on railway fares and freights.

K.1 Octrois and Terminal taxes

215 .The legislative history surrounding the incorporation of Entry 52 is a significant guide to interpreting its provisions. Section 80A of the Government of India Act, 1915 defined the powers of the provincial legislatures. Under the Devolution Rules, the following provisions were contained in Item Nos. 7 and 8 of the Second Schedule :

> "Item No. 7. An octroi Item No. 8. A Terminal tax on goods imported into or exported from a local area save where such tax is first Imposed in a local area in which an octroi was not levied on or before 6 July, 1917."

In the Government of India Act, 1935, Entry 49 of the legislative lists (list II) provided as follows :

> "49.Cesses on entry of goods into a local area for consumption, use or sale therein. Terminal taxes were

216. In the Government of India Act, 1935, Entry 49 used the expression "entry of goods into a local area for consumption, use or sale therein", instead and in place of "octroi" (as contained in the Devolution Rules under the Act of 1915). The Constitution incorporated Entry 52 in List II in language which corresponds to Entry 49 of List II under the Government of India Act, 1935 but with the difference that the expression 'taxes' is used instead of 'cesses'.

217. The imposition of octroi has a historical significance both in India and elsewhere. Tracing its history, a Constitution Bench of this Court in *Diamond Sugar Mills Ltd. v. The State of Uttar Pradesh* [173]., explained the meaning of octroi thus :

> "Octroi is an old and well known term describing a tax on the entry of goods into a town or a city or a similar area for consumption, sale or use therein. According to the Encyclopaedia Britannica octroi is an indirect or consumption tax levied by a local political unit, normally the commune or municipal authority, on certain categories of goods on their entry into its area."
>
> (Id. at p. 252)

218. Octroi was a tax levied on the entry of goods into areas which were administered by local bodies. When the draftsmen of the Constitution incorporated Entry 52 in List II, it was with the knowledge that the expression 'local area' had been used in the Government of India Act, 1935. Moreover, it could not but have been present to the minds of the framers that the expression 'octroi' which was used in the Devolution Rules had been replaced subsequently in Entry 49 of List II in the Government of India Act of 1935 with a description rather than label : the label being descriptive of the entry of goods into a local area; the purpose being consumption, use or sale therein. The expression 'therein' also indicates that the goods enter for the purpose of being used, consumed or sold within the local area.

219. The situation that fell for consideration before the Constitution Bench in Diamond Sugar Mills arose under Section 3 of the UP Sugar Cane Cess Act, 1956 under which the State Government was empowered to impose a cess not exceeding a stipulated amount on the entry of sugarcane into the premises of a factory for use, consumption or sale therein. The legislative competence of the state legislature was questioned on the ground that the premises of a factory did not constitute a local area within the meaning of Entry 52. The Constitution Bench held thus :

> "The etymological meaning of the word "local" is "relating to" or "pertaining to" a place. It may be first observed that whether or not the whole of the State can be a "local area", for the purpose of Entry 52, it is clear that to be a "local area" for this

> purpose it must be an area within the State. On behalf of the respondents, it is argued that "local area" in Entry 52 should therefore be taken to mean "any part of the State in any place therein". So, the argument runs, a single factory being a part of the State in a place in the State is a "local area".
>
> In other words, "local area" means "any specified area inside the State". The obvious fallacy of this argument is that it draws no distinction between the word "area" standing by itself and the phrase "local area". If the Entry had been "entry of goods into any area of the State " some area would be specified for the purpose of the law levying the cess on entry. If the Constitution makers were empowering the State Legislatures to levy a cess on entry of goods into any specified area inside the state, the proper words to use would have been "entry of goods into any area " It would be meaningess and indeed incorrect to use the words they did use "entry of goods into a local area".

The use of the words "local area" instead of the word "area" cannot but be due to the intention of the Constitution-makers to make sure that the power to make laws relating to levy on entry of goods would not extend to cases of entry of goods into any and every part of the state from outside that part but only to entry from outside into such portions of the state as satisfied the description of "local area". (Id. at p. 250)

> In holding that a factory could not be a local area, the Constitution Bench observed that :
> "It was with the knowledge of the previous history of the legislation that the Constitution-makers set about their task in preparing the lists in the seventh Schedule.
> There can be little doubt therefore that in using the words "tax on the entry of goods into a local area for consumption, use or sale therein", they wanted to

express by the words "local area" primarily area in respect of which an octroi was leviable under item 7 of the Schedule tax rules, 1920-that is, the area administered by a local authority such as a municipality, a district Board, a local Board or a Union Board, a Panchayat or some body constituted under the law for the governance of the local affairs of any part of the State. Whether the entire area of the State, as an area administered by the State Government, was also intended to be included in the phrase "local area", we need not consider in the present case." (Id. at p. 253)

220. These observations indicate that Entry 52 having used the expression "local area" rather than "area", the Constitution did not intend that the entry of goods into just any area in the state would attract the entry. The entry had to be into a local area. A local area is an area administered by a local authority such as a municipality, a district or a local board or a panchayat or some other body constituted by law for administering the governance of local affairs in any part of the state. Whether the entire state could be declared as a local area was, however, kept open in Diamond Sugar Mills.

221. In another judgment of a Constitution Bench in Bangalore *Woollen Cotton and Silk*

Mills Co. Ltd. v. Corporation of the City of Bangalore[175], there was a challenge to the constitutional validity of the imposition of octroi duty on cotton and wool by the Bangalore Municipal Corporation Act, 1949 inter alia under the provisions of Article 301. The octroi duty was, in the submission of the state, saved by Article 305 which stipulated that nothing in Articles 301 and 303 shall affect the provisions of any existing law except in so far as the President may by order otherwise direct. The Constitution Bench accepted the submission and held that there was no contravention of Article 301.

222. In Burmah Shell Oil Storage and Distribution Co. India Ltd. v. The Belgium Borough Municipality , the appellant had unsuccessfully moved the High Court for a writ seeking to prohibit the municipality from charging octroi on its products which were brought inside octroi limits for sale. The goods brought into octroi limits by the appellant comprise of four categories :

> "(i) Goods consumed by the appellant;
>
> (ii) Goods sold by the appellant itself or through dealers and consumed within octroi limits by others;
>
> (iii) Goods sold by the appellant itself or through dealers within octroi limits but consumed outside; and
>
> (iv) Goods sent by the appellant from its depot within octroi limits to points outside the municipality where they were produced and consumed by others.

223. Under Section 73 of the Bombay Municipal Boroughs Act, 1925, the municipality was empowered to impose an octroi on animals or goods brought within the octroi limits for consumption, use or sale therein. The Constitution Bench took note of the legislative history relating to terminal taxes and octroi. Terminal Taxes were concerned only with the entry of goods into a local area irrespective of whether or not they were used there. Octrois were taxes on goods brought into the local area for consumption, use or sale. When the Constitution was adopted, the expression octroi was avoided and instead a description was used. Expounding the ambit of Entry 52, the Constitution Bench observed as follows:

> "21. It is not the immediate person who brings the goods into a local area who must consume them himself, the act of consumption may be postponed or may be performed by someone else but so long as the goods have been brought into the local area for consumption in that sense, no matter by whom, they satisfy the requirements of the Boroughs Act and octroi is payable. Added to the word "consumption" is the word "use" also. There may be certain commodities which though put to use are not 'used up' in the process. A motor-car brought into an area for use is not used up in the same sense as food-stuffs. The two expressions use and consumption together therefore, connote the bringing in of goods and animals not with a view to taking them out again but with a view to their retention either for use without using them up or for consumption in a manner which destroys, wastes or uses them up."

(Id. at p. 230-231)

224. The Constitution Bench ruled that so long as goods are brought inside the area for sale within the area to an ultimate consumer, it makes no difference that the consumer does not consume them in the area but takes them out for consumption elsewhere :

> "22 The word "therein" does not mean that all the act of consumption must take place in the area of the municipality. It is sufficient if the goods are brought inside the area to be delivered to the ultimate consumer in that area because the taxable event is the entry of goods which are meant to reach an ultimate user or consumer in the area." (Id. at. P. 233)
>
> Hence, the appellant was held to be liable to pay octroi duty on goods brought into a local area :
>
> (i) To be consumed by itself or sold directly by it to consumers;
>
> (ii)For sale to dealers who in their turn sold the goods to consumers within the municipal area irrespective of whether such consumers bought them for use inside or outside the area. However, the appellant was not liable to octroi in respect of goods which it brought into a local area for re-export."

225. For many years after the adoption of the Constitution, local bodies across the country continued to levy octroi, which was an important source of revenue. Octroi was levied under state legislation, enacted with reference to Entry 52 of List II (read with Articles 244, 245 and 246). Octroi, however, assumed an obnoxious character and was a subject of comment by this Court in Hansa Corporation (supra). Octroi duty became associated with check posts installed by local bodies. The octroi barriers became notorious for long queues of fully laden vehicles awaiting entry into local limits. Worse still, octroi became a vexed symbol of the misdeeds of local officials or contractors tasked with the collection of octroi duty. Over a period of time, accepting the clamour of the trade, octroi was gradually phased out and replaced by entry tax legislation in the states. Noteworthy, among the changes made, was that the tax would be leviable upon a dealer. Moreover, the tax would be collected not at the octroi or municipal limit but subsequently after the submission of returns.

K.2 Entry taxes and Article 304(a)

226. For the purposes of this reference, it is necessary to clarify at the outset that the detailed provisions of each state legislation pertaining to entry tax do not fall for consideration. It is sufficient for the purposes of the present reference to consider some of the important aspects of entry tax legislation vis-a-vis Part XIII which are of common concern.

227. The first significant aspect of the matter is the inter-play between entry tax legislation and Article 304 (a). The interface between the two arises because entry tax is levied on the entry of goods into a local area for consumption, use or sale therein. If

the goods originate in any other state, the imported goods would upon entry into a local area be liable to entry tax since the charging event is the entry of the goods into the local area for consumption, use or sale. Issues of discrimination arise on whether similar goods produced or manufactured within the state are subject to entry tax.

228. Article 304 permits the state legislature to impose on goods imported from another state any tax to which similar goods produced or manufactured in the state are subject. The object is to ensure that there is no discrimination between the goods "so imported" and the goods "so produced or manufactured". The critical requirement of Article 304 (a) is that the tax must be origin neutral. Hence, where the state legislature levies an entry tax on goods entering a local area (without making any discrimination based on whether or not the goods originate in the state or are imported from outside) the mandate of Article 304(a) would be met.

229. The issue is whether Article 304 (a) would be breached by imposing an entry tax only upon goods that are imported from other states. Plainly, if a tax is imposed on goods which are imported from other states without subjecting similar goods produced or manufactured within the state to the tax, there would be a violation of Article 304(a). This would constitute an unconstitutional discrimination between goods imported from other states which are subject to tax and goods produced or manufactured within the state which are not subject to the levy. Such an act of discrimination may take place, for instance, in a situation where state law defines the entire area of the state as a local area or by incorporating a specific definition of the expression dealer or importer to mean an importer of goods from outside the state. For instance, goods may be subject to entry tax only when they cross the state boundary. Movement of goods exclusively within the state, is not subject to entry tax. Alternatively, the expression local area may be defined with reference to the entire state. If the legislation imposes a tax only upon the entry of goods originating outside the state into the state, while goods produced and manufactured within the state are not subject to the levy, this would constitute a hostile discrimination prohibited by Article 304 (a).

K.3 Meaning of 'Local area'

230. The issue as to whether the entire area of a state can be treated as a local area for the purposes of Entry 52 of List II, was specifically kept open for consideration in the judgment of the Constitution Bench in Diamond Sugar Mills.The issue was, however, dealt with in a judgment of three learned Judges of this Court in *Shaktikumar M. Sancheti v. State of Maharashtra*[176]. In that case an entry tax was levied under Section 3 of the Maharashtra Tax on Entry of Motor Vehicles into Local Areas Act, 1987. The Act was challenged by contractors or dealers of motor vehicles who had purchased them outside the state and had brought them within the state of Maharashtra as being a colorable exercise of legislative power under Entry 52 of List II as well as violating Article 301. Taking note of the fact that the issue of what constitutes a local area had not been decided in Diamond Sugar Mills, the Bench of three Judges held as follows :

> "4....The expression 'local area' has been used in various Articles of the Constitution, namely, 3, 12, 245(1). 246, 277, 321, 323A. and 371(D). They

indicate that the constitutional intention was to understand the 'local area' in the sense of any area which is administered by a local body, may be corporation, municipal board, district board etc. The High Court on this aspect held, and in our opinion rightly that the definition does not comprehend entire State as local area as the use of the word 'a' before 'local area' in the Section is significant. The taxable event according to the High Court, is not the entry of vehicle in any area of the State but in a local area. The High Court explained it by giving an illustration that if a motor vehicle was brought from Jabalpur (Madhya Pradesh) for being used or sold at Amravati (in Nagpur District of Maharashtra), which was the border area, taxable event was not the entry in Nagpur District but entry in area of Amravati Municipal Corporation. The levy, therefore, is not, as urged by the learned Counsel for appellant, on entry of vehicle in any part of the State but in any local area in the State. It cannot, therefore, be struck down on this ground."

(Id. at p. 355)

231. The Seventy-third amendment to the Constitution has incorporated Part IX which deals with Panchayats while the Seventy fourth amendment has incorporated Part IXA which deals with Municipalities. Article 243(d) defines Panchayats as institutions of self-government constituted under Article 243(b) for the rural areas. Article 243(b) requires the constitution in every state of Panchayats at the village, intermediate and district levels. Article 243H (a) empowers the legislature of a state by law to authorize a Panchayat to levy, collect and appropriate such taxes, duties, tolls and fees in accordance with such procedure and subject to such limits. Article 243Q provides for the constitution of a Nagar Panchayat, a Municipal Council and a Municipal Corporation. Article 243X empowers the legislature of a state by law to authorize a Municipality to levy, collect and appropriate such taxes duties, tolls and fees in accordance with such procedure and subject to such limits. With these amendments, local areas now have assumed a constitutional context and significance.

232. In the judgment in Diamond Sugar Mills, the Constitution Bench emphasized that in using the expression local area, the framers of the Constitution were aware of the previous legislative history and meant an area administered by a body (such as Municipalities, Panchayats or local board) constituted under the law for the governance of local affairs in any part of the state. This statement of principle in the decision in Diamond Sugar Mills now stands fortified in view of the constitutional amendments brought by the insertion of Parts IX and IXA into the Constitution. A local area cannot be defined with reference to the entire state but will comprehend within the state, an area that is administered by a local body constituted under the law.

K.4 Severability

233. On behalf of the states, it has been urged that where a state legislature provides for the levy of an entry tax only upon goods brought from outside the state, the offending words may be treated as severable and struck down so as to allow for the imposition on goods entering a local area both from within or outside the state. Such an exercise would clearly be impermissible. Where the state legislature has evinced a clear intent to

levy a tax only upon the entry of goods originating from outside the state, it would be impermissible, by a process of interpretation as suggested to excise the offending words. Such an excise would not fall within the permissible scope of reading down the statute. The effect of such a judicial exercise would be to impose a levy upon goods moving into a local area from within the state, though, this has not been done by the state legislature. Whether such a levy should be imposed is a matter for the state legislature to determine in its law making authority. This Court in the exercise of its power of judicial review can hold that a discrimination between goods imported from outside the state and goods produced or manufactured within the state for the levy of a tax would be violative of Article 304(a). Where the state legislature has committed an act of hostile discrimination by imposing a tax only upon goods originating outside the state upon their entry within it, the court must strike down such a provision which violates Article 304(a). The provision cannot be re-written by judicial interpretation to mean that the tax will be levied both on goods originating outside the state and goods originating within the state and entering a local area. Re-writing a legislative provision is impermissible in the exercise of judicial review.

K.5 Equality of tax burdens

234. At first impression Article 304(a) presents a fairly simple application. If a tax at the rate of five per cent is imposed by a taxing state on goods imported from other states, similar goods which are produced or manufactured within the taxing state must be subjected to a five per cent tax. If a higher rate of tax is imposed on goods originating in other states which are imported into the taxing state, this would result in a discrimination against imported goods. Such a discrimination is sought to be obviated by the requirement that the rate of tax should be the same as between similar goods produced or manufactured within the taxing state and goods imported from other states. This furnishes the rationale for several decisions of this Court, which hold that Article 304(a) mandates the same rate of tax and once that requirement is fulfilled, the application of the provision is at an end.

235. The submission of the petitioners, however, which falls for close examination is that Article 304(a) requires that the very tax which is imposed by a taxing state on imported goods must be imposed on domestic goods. In the context of entry tax, the submission is that unless the taxing state imposes it on similar local goods, an entry tax cannot be imposed on goods imported from other states. If goods manufactured or produced in the taxing state are not subject to entry tax, that will result in a discrimination if imported goods of other states are so subject.

236. The example which has been set out above of the application of differential rates of tax, for the same tax imposed on domestic as opposed to imported goods presents a simple application of Article 304(a). The example is simple in the sense that a discrimination is then effected in the imposition of the same tax by subjecting domestic and imported goods to differing treatment. The picture may, however, become more nuanced. Different states have adopted varying models while framing legislation in a manner which, according to them, fulfils the mandate of Article 304(a). Whether it in fact, does so is for the court to determine.

237. A state may have a single legislative enactment providing for both entry tax and sales tax at equal rates. Some other states provide for set offs and statutory exemptions to goods paying local sales tax. Certain states provide a similar set off for goods imported from another state, if they are sold in the taxing state. The legislation of some states provides for a reduction of tax liability under the sales tax law by the amount of entry tax paid while in other cases, state legislation provides for a reduction of entry tax by the amount of tax paid under the General Sales Tax Act. Similarly, state enactments provide for the reduction of liability under entry tax legislation by the amount of tax which is paid under the sales tax law of that state. Contrariwise, such a reduction has not been made available to imported goods in certain state legislation. The state legislation may have excluded from entry tax those local goods which are liable to pay sales tax under the State Act. However, an importer of scheduled goods who incurs liability under value added tax legislation, by virtue of the sale of imported goods or the sale of goods manufactured by consuming such imported scheduled goods, is entitled to a set off. State legislation in certain cases exempts goods from entry tax if after entry in a local area, the goods are sold there and become liable to pay value added tax. In other cases, manufacturers in a local area are exempt from paying entry tax on raw material imported from another local area or another state. In some cases, manufacturers in a local area are required to pay the same entry tax on raw material imported from another local area or another state.

238. These examples furnish illustrations of different patterns and approaches adopted by state legislation. It is necessary to clarify that in this reference the nuances of each state law are not being considered since the cases would have to be placed for disposal before the appropriate Bench after the reference is answered. For the purposes of this reference, it is sufficient for the court to lay down broad principles governing the area without going into individual facts or detailed provisions covering each case in relation to the period at issue in the respective states.

239. Article 304(a), in so far as is material, authorises the legislature of a state to impose on "goods imported" from other states "any tax to which similar goods manufactured or produced in that state are subject". Several aspects of Article 304(a) merit emphasis :

240. The first is that Article 304(a) refers to the imposition of any tax on goods. The provision is not either a source of legislative power nor does it prescribe fields of legislation. The expression "any tax on goods" is of a generic nature and covers all taxes which a state is competent to impose on any aspect of goods under Articles 245 and 246 read with List II of the Seventh Schedule. The expression 'any tax' would mean any exaction in the nature of an impost or levy which the state legislature is competent to enact by virtue of its legislative powers. The expression 'any tax' must mean what it says: it means any levy which the state is constitutionally competent to legislate. The second aspect of Article 304(a) is the latter part which provides that the state shall act :

> "so, however, as not to discriminate between goods so imported or goods so manufactured or produced."

241. The fundamental reason for the incorporation of this provision is to prohibit discrimination being practiced by the state against imported goods by embarking upon protectionist policies. The discrimination which the constitutional provision is intended to rule out is discrimination which is protectionist in nature. A state cannot impose taxes in a manner that would make the goods of another state non-competitive so as to effectively bar the inflow of trade by utilizing fiscal exactions. Thirdly, the latter part of Article 304(a) is prefaced by the expression "so however". In *Words and Phrases*[177], the expression however has been explained as indicating "an alternative intention, a contrast with a previous clause and a modification of it under ***circumstances***[178]". The Oxford dictionary defines the expression 'however' to mean "in any case, at all events, at any rate." Another meaning attributed to the phrase is "used by itself, or followed by points of suspension, as an interjection or as a formula concluding, introducing or modifying an utterance in some contextual way". *P Ramanatha Aiyar's Law Lexicon*[179] states that the word 'however' in a deed or will indicates an alternative intention, a contrast with a previous clause and a modification of it under certain circumstances. The latter part of Article 304(a) follows upon the first which enables the state to impose on goods which are imported from other states any tax to which the goods produced or manufactured within the state are subject. The latter part constitutes a positive re-affirmation that in any case, at all events and at any rate there shall be no discrimination between goods manufactured or produced within the taxing state and "between". That

[177] *(Permanent Ed. Vol. 19A)*
[178] *(IInd Ed. Vol. II, p. 59)*
[179] *(4th Ed. Vol. III, Id. at p. 3134)*

goods imported from other states. This narrative is the dominant theme of Article 304 (a). Fourthly, an expression of some significance that is used in the latter part of Article 304(a) is

expression has been employed so as to mandate that there shall be no discrimination between goods imported into the taxing state from other states and goods that are manufactured and produced within. The use of the expression "so" in the latter part is an obvious reference to the imported goods and the goods manufactured or produced within, referred to in the first part. The expression 'between' postulates that imported goods and local goods must be allowed a level playing field in the taxing state. Imported goods from another state cannot be placed at a comparative disadvantage. The expression 'between' also signifies that goods produced or manufactured within the taxing state should also not be discriminated against. In seeking parity of treatment, it is as much the obligation of the taxing state to ensure that there is no discrimination against goods originating in other states, as much as it is its concern to ensure that domestic goods are not discriminated against. The former is a matter of constitutional obligation. However, it does not exclude a similar obligation and concern of the taxing state in respect of goods produced and manufactured within its territorial limits. Both must go hand in hand. Discrimination both in a positive manner against imported goods and a reverse discrimination against domestic goods are within the ambit of Article 304(a). The fifth important principle which requires emphasis is that our Constitution does not embody a requirement that the state legislature while enacting a legislation must legislate separately in respect of each subject of legislation contained in List II. A law enacted by the state legislature imposing a fiscal levy may cover more than one

subject of legislation falling within its legislative competence in List II. In contrast, Section 55 of the Australian Constitution mandates that there shall be one tax law on one subject. Article 55 of the Australian Constitution reads as follows:

> "Article 55 : Laws imposing taxation shall deal only with the imposition of taxation and any provision therein dealing with any other matter shall be of no effect. Laws imposing taxation except laws imposing duties of customs or of excise shall deal with one subject of taxation only; but laws imposing duties of customs shall deal with duties of customs only, and laws imposing duties of excise shall deal with duties of excise only."

242. The Indian Constitution does not impose such a restriction on the states. Considered from a different perspective, "rag-bag" legislation is constitutionally permissible under the Indian Constitution and it is open to a single enactment to draw sustenance from more than one entry which falls within the legislative competence of the enacting legislature. [See in this context*: Ujagar Prints (II) v. Union of India* [180], *All India Federation of Tax Practitioners v. Union of India*[181] , and *State of A.P. v. NTPC*[182] *].*

243. As a matter of constitutional doctrine, there is no restraint on the plenary powers of Parliament as well as the state legislatures which requires the legislative body enacting a statute to legislate only upon one head of legislation falling within its competence. The legislature can distribute or allocate its regulatory or law making requirements (both fiscal and non-fiscal) in a manner which best sub-serves its needs and concerns. Once this be the position, its impact upon the interpretation of Article 304(a) is that it is open to the state legislature to have due regard to the equality of tax burdens, when it legislates to impose "any tax" so long as it does not breach the notion of non-discrimination as between goods that are imported from other states and goods which are produced or manufactured within. It is legitimately entitled to ensure that the tax burden should not discriminate between locally produced or manufactured goods of that state and goods originating in other states. The substance must prevail over form. Once there is no constitutional necessity that the form in which legislation is enacted in India must cover only one legislative entry, the legislature is entitled to devise a law in a suitable manner which while being consistent with the norm of non-discrimination also preserves a parity of tax burden between goods imported and domestic goods. This is the foundation of the theory of equivalence.

244. The burden of establishing that there is a discrimination against goods which are imported from other states lies on the person who sets up such a plea. In answering a plea of discrimination, it would be open to the state to establish that the legislative provision which it has enacted maintains the principle of non-discrimination between goods produced and manufactured within the state and goods imported from other states while at the same time bringing about parity in terms of tax burden between domestic and imported goods. Sales tax is referable to Entry 54 of List II ("taxes on the sale or purchase of goods other than newspapers, subject to the provisions of Entry 92A of List I"). Entry tax is referable to Entry 52 of List II ("taxes on the entry of goods into a local area for consumption, use or sale therein"). Both sets of taxes fall within the competence of the state legislature. Taxable events under entries both entries are

distinct : in the case of one the sale of goods and in the case of the other, entry of goods into a local area for consumption, use or sale therein. Both deal with separate aspects of the taxation of goods; the taxable events being proximate though distinct. The expression "any tax" recognises the full panoply of taxes on goods falling within List II. If a law can cover Entry 52 and Entry 54 of List II, there is no reason to prohibit the state law making authority from having due regard to the tax burdens imposed on domestic goods and goods imported from other states under entry tax and sales tax legislation, taken as a composite whole. "Any tax" does not mean a tax under one entry of List II as a discrete and isolated legislation independent of any another entry. Any adjustment, exemption or set off based on the payment of sales tax may be intended to avoid double taxation and discrimination. Whether this object has been legitimately achieved by the enacting law is a matter to be determined on its interpretation and application.

245. It is trite law that every discrimination involves a differentiation but every differentiation does not implicate discrimination. (*Digvijay Cement v. State of Rajasthan*[183]). The enquiry into whether a state has practiced discrimination against goods imported from other states will commence with an investigation into whether the state legislation has made any differentiation between the two sets of goods. This is not merely in terms of the rate of tax but there are other important aspects including :

> "(i)procedures and machinery including aspects such as licencing, recognition and compliance:
>
> (iii)Measure of the tax; and
>
> (iv)Exemptions or set offs; Beyond this enquiry, the court would need to analyse the reasons for the differentiation and then to determine as to whether there has been a discrimination violative of Article 304(a)."

K.6 Entry tax and imported goods

246. Entry 83 of List I provides for "duties of customs including export duties". The submission of the petitioners is that there being no over-lapping of legislative entries, the field of Entry 52 of List II would begin where that of Entry 83 of List I ends. Hence, while considering whether entry tax can be imposed in relation to goods imported into India, it is urged that until the goods become a part of the land mass, they can be subjected to a law under Entry 83 of List I and to a duty of import. It is only where a Bill of entry for home consumption is filed that the goods cease to be imported goods. Until then, it is urged, no entry tax would be leviable.

247. The taxable event referable to a law enacted under Entry 83 of List I (in relation to an import customs duty) is the act of import by which goods originating in a foreign country are brought into India. Section 2 (23) of the Customs Act, 1962 defines the expression import to mean "bringing into India from a place outside India". The expression imported goods is defined to mean "any goods brought into India from a place outside India" but so as not to include goods which have been cleared for home consumption. Section 2 (26) defines the expression importer in relation to any goods at

any time between their importation and the time when they are cleared for home consumption, to include any owner or any person holding himself out to be an importer.

248. Section 46 provides that the importer of any goods (other than goods for transit or transhipment) shall present to the proper officer a bill of entry for home consumption or warehousing in the prescribed format. The bill of entry can be presented at any time after the delivery of the import manifest or import report. Section 47 provides for clearance of goods for home consumption upon the satisfaction of the officer that the goods entered for home consumption are not prohibited goods and the importer has paid the import duty assessed thereon together with the charges payable under the Act. Section 48 provides for the sale of goods by the person having custody if they are not cleared for home consumption or warehousing or transhipped within 30 days from the date of unloading. Chapter IX provides for warehousing. Section 57 provides for public warehouses where dutiable goods may be deposited. Section 58 provides for the licencing of private warehouses where dutiable goods may be deposited. Section 59 provides for the execution of a warehousing bond. Section 60 deals with the grant of permission to deposit goods in a warehouse. Section 61 provides for the period during which goods can remain in a warehouse. Under Section 64, the owner's right to deal with warehoused goods has been statutorily recognized to the extent mentioned therein. Section 65 enables the owner of any warehoused goods with due permission to carry on any manufacturing process or operations in the warehouse, relating to the goods. Section 68 provides for the clearance of warehoused goods for home consumption subject to the presentation of a bill of entry, payment of import duty and all penalties and charges and upon the passing of an order of clearance for home consumption. Section 73 provides for the cancelation and the return of a warehousing bond.

249. The Constitution distributes subjects of legislation including, amongst them, those covering fiscal matters between the Union and the States. The fields or subjects of legislation are elaborately defined so as to exclude the possibility of overlapping between entries in List I and those in List II. Even where the fields may appear to overlap, they must be construed to be mutually exclusive. The submission of the petitioners proceeds on the basis that if entry into any part of India from outside India is an entry into a local area, it would nonetheless be necessary to earmark the ambit of Entry 83, List I and Entry 52 List II respectively. Both, according to the petitioners cover taxes on the movement of goods. According to the petitioners, Entry 52 should cover an entry into a local area after the importation of the goods is complete since the field of Entry 83 continues to subsist until the goods have been imported by filing of a Bill of entry for home consumption.

250. Entry 83 of List I and Entry 52 of List II have separate and distinct fields of operation. Entry 41 of List I deals with trade and commerce with foreign countries; import and export across customs frontiers; and definition of customs frontiers. The distribution of powers with reference to the taxing entries in List I and II is mutually exclusive.

251. In a decision rendered in 1942 by the Federal Court in *Province of Madras v.*

Messrs. Boddu Paidanna & Sons[184] , it was held that if a tax payer who pays sales tax is also a manufacturer subject to excise duty "there may no doubt be overlapping in one sense, but there is no overlapping in law". The two taxes which he is called upon to pay - excise duty and sales tax were held to be "economically two separate and distinct imposts". There was, in the view of the Federal Court no reason to expand the meaning of the expression 'duties of excise' at the expense of the provincial power to levy taxes on the sale of goods. The judgment of the Federal Court was affirmed by the *Privy Council in Governor General in Council v. Province of Madras* [185]. The Privy Council held that :

> "The two taxes, the one levied upon a manufacturer in respect of his goods, the other upon a vendor in respect of his sales, may, as is there pointed out, in one sense overlap. But in law there is no overlapping. The taxes are separate and distinct imposts. If in fact they overlap, that may be because the taxing authority, imposing a duty of excise, finds it convenient to impose that duty at the moment when the exciseable article leaves the factory or workshop for the first time upon the occasion of its sale. But that method of collecting the tax is an accident of administration, it is not of the essence of the duty of excise which is attracted by the manufacture itself."

252 Applying the same principle, this Court held in *Ram Krishan Ram Nath Agarwal v. Secretary, Municipal Committee, Kamptee* [186]that a Bidi manufacturer was liable to pay excise duty and octroi on two distinct taxing events : whereas excise duty is a tax on manufacture, octroi duty is a tax on the entry of goods into a local area. In The *Jiyajeerao Cotton Mills Ltd. v. State of Madhya Pradesh*[187] , a textile mill which was generating electricity for running the mill (and not for sale) questioned the levy of electricity duty on the ground that this would amount to a levy of excise duty which fell exclusively within the competence of Parliament under Entry 84 of List I. Rejecting the submission, this Court held that :

> "6. It is difficult to see how the levy of duty upon consumption of electrical energy can be regarded as duty of excise falling within Entry 84 of List I. Under that Entry, what is permitted to Parliament is levy of duty of excise on manufacture or production of goods (other than those excepted expressly by that entry). The taxable event with respect to a duty of excise is "manufacture" or "production". Here the taxable event is not production generation of electrical energy but its consumption. If a producer generates electrical energy and stores it up, he would not be required to pay any duty under the Act. It is only when he sells it or consumes it that he would be rendered liable to pay the duty prescribed by the Act. The Central Provinces and Berar Electricity Act was enacted under Entry 48-B of List II of the Government of India Act, 1935. The relevant portion of that Entry read thus: "Taxes on the consumption or sale of electricity"
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> Entry 53 of List II of the Constitution is to the same effect."
> (Id. At p. 286-287)

253. In *D G Gose v. State of Kerala* [188], this Court held that a tax on buildings imposed

under the Kerala Building Tax Act, 1961 was referable to Entry 49 of List

> II and was not a tax on the capital value of assets under Entry 86 of List I. In that context, it was held that :
>
> "7....So if a tax is levied on all that one owns, or his total assets, it would fall within the purview of Entry 86 of List I, and would be outside the legislative competence of a State legislature, e.g. a tax on one's entire wealth. That entry would not authorise a tax imposed on any of the components of the assets of the assessee. A tax directly on one's lands and buildings will not therefore be a tax under Entry 86
>
> 8.. If, therefore, a tax is directly imposed on 'buildings', it will bear a direct relation to the buildings owned by the assessee. It may be that the building owned by an assessee may be a component of his total assets, but a tax under Entry 86 will not bear any direct or definable relation to his building. A tax on 'buildings' is therefore a direct tax on the assessee's buildings as such, and is not a personal tax without reference to any particular property." (Id. at. p. 421)

254 This decision has been affirmed in *Union of India v. H S Dhillon*[189] While reiterating this position in *Lt. Col. Sawai Bhawani Singh v. State of Rajasthan*[190], this Court held that
:

> "7 These two taxes are separate and distinct in nature and it cannot be said that there was any overlapping, or that the State Legislature was not competent to levy such tax on lands and buildings merely on the ground that they have been subjected to another tax as a component of the total assets of the person concerned."
>
> (Id. at p. 111)

255. In M/s *R R Engineering Co. v. Zila Parishad Bareilly* [191], a tax was imposed on "circumstances and property" under the UP Kshettra Samitis & Zila Parishad Adhiniyam, 1961. This composite tax was questioned on the ground that this was essentially a tax on income under Entry 82 of List I and therefore outside the legislative competence of the state legislature. Rejecting this submission, this Court held that :

> "17. The Full Bench decision under appeal in the instant case, R.R. Engineering Co. [R.R. Engineering Co. v. Zila Parishad, Bareilly, AIR 1970 All 316], has taken the same view of the nature of the tax on circumstances and property by holding that it is not a tax on income but is a tax on a man's financial position, his status as a whole, depending upon his income from trade or business. Earlier, another Full Bench of the Allahabad High Court had held in Zila Parishad, Muzaffar Nagar v. Jugal Kishore that the tax on circumstances and property is fundamentally distinct from and cannot be equated with income tax, that it is not covered by item 82, List I, Schedule VII, of the Constitution and that it is essentially a tax on status or financial position combined with a tax on property.

These decisions correctly describe the nature of the tax on circumstances and property. We affirm the view taken therein, especially that the aforesaid tax is not a tax on income."
(Id at p. 337)

The constitutional principle has been enunciated by a Constitution Bench in *Godfrey Phillips India Ltd. v. State of U P* [192] thus :

"The logical corollary of holding that taxes are imposed only on taxable events is that even when an entry speaks of a levy of a tax on goods, it does not include the right to impose taxes on taxable events which have been separately provided for under other taxation entries. The tax in respect of goods has sometimes been referred to as a tax on an aspect of the goods and sometimes as the taxable income. (See *Federation of Hotel Restaurant v. Union of India*[193] (Pr. 13, 14, 16)."
(Id. at p. 544)

256 The principle of law is hence well-settled : the taxing powers of the Union and the states are mutually exclusive. (See in this context the decisions in *Hoechst Pharmaceuticals v. State of Bihar* [194]; and State *of West Bengal v. Kesoram Industries* [195]).

257 A Bench of nine Judges of this Court in Re Sea Customs , distinguished the taxable event in the case of a duty of excise, which is the manufacture of goods, with a sales tax where the taxable event is the act of sale. Dealing with customs duties, the Bench of nine Judges speaking through Sinha, CJ held as follows :

"Similarly in the case of duties of customs including export duties though they are levied with reference to goods; the taxable event is either the import of goods within the customs barriers or their export outside the customs barriers. They are also indirect taxes like excise and cannot in our opinion be equated with direct taxes on goods themselves. Now, what is the true nature of an import of an import duty? Truly speaking, the imposition of an import duty, by and large, results in a condition which must be fulfilled before the goods can be brought inside the customs barriers, i.e. before they form part of the mass of goods within the country."

(Id. at. p. 543)

Entry of goods into a local area for consumption, use or sale therein attracts the charging provision of entry tax legislation. The levy which is referable to Entry 52 of List II is attracted the moment the goods enter a local area for consumption, use or sale. The Customs Act, 1962 has made a beneficial provision for allowing goods to be deposited in public or private warehouses and for the clearance of goods for home consumption. These provisions cannot and do not detract from the power of the state legislatures under Entry 52 nor do they denude the states from levying an entry tax once the taxable event under state law has occurred.

258. In the present case, the grievance of the states is that the petitioners have not stated in the pleading that there is any warehousing station in their factory units or in the local area where they are located. Hence, the contentions are stated to have been advanced without any basis in the pleadings or facts. Moreover, it has been submitted that the petitioners have not produced any evidence that the bill of entry is filed in the factory units or in a land customs station located in the same local area as the petitioner's units.

259. For the purposes of this reference, it is not appropriate for the court to conclusively adjudicate upon the issues raised relating to the facts of the above cases. Hence, it is only appropriate and proper that all the facts are fully established before the regular bench adjudicating upon the cases relating to goods imported from abroad. However, the constitutional position in respect of Entry 83 of List I and Entry 52 of List II has been clarified above. The taxable event for the imposition of a duty of customs is distinct from the taxable event in respect of an entry tax, which is the entry of goods into a local area for consumption, use and sale therein. M Direct and inevitable effect test

260. Whether taxes per se constitute an impediment upon the freedom of trade, commerce and intercourse is an issue which has resulted in two contrary positions, neither of which has been subscribed to in this judgment. At one end of the spectrum is the theory that all taxes impede the freedom of trade, commerce and intercourse. If this theory were to be accepted, the entire tax regime and the state taxing power would be controlled by Part XIII of the Constitution. The states which are sovereign within their own sphere would in the exercise of their constitutional power to raise revenues by way of taxation be subject to the rigours of Part XIII. Such an extreme view is not acceptable either from the stand point of textual construction or from its consequence for the federal structure of the Constitution. All taxes do not impede the freedom of trade, commerce and intercourse. In fact, as discussed earlier, taxes provide the means by which revenues can be raised under a regime of law made by law making bodies at the federal and state level. Absent a taxing power, the states would be bereft of revenues needed for maintaining order and governance. Trade, commerce and intercourse cannot survive in the abstract and without conditions of stability and order created by the state. Moreover, the revenues which are made available to the state provide the basis for creating infrastructure and amenities, both direct and incidental, through which trade and commerce can effectively be transacted and can flourish. Hence, the extreme proposition that all taxes constitute a restriction or impediment upon trade has been eschewed.

261. At the other end of the spectrum lies the view that taxes do not constitute a restriction upon the freedom of trade, commerce and intercourse. If this view were to be accepted, Part XIII would have no role as a constitutional limitation on taxing legislation save and except for discriminatory taxes of the kind that are prohibited by Article 304(a). The position that Article 304(a) constitutes the entire universe of taxation for the purpose of Part XIII has been rejected by this judgment on the ground that it suffers from fundamental fallacies and is contrary to the text of Part XIII. To recapitulate, the grounds for so holding are :

"(i) Laws for the purposes of Part XIII must mean all laws and not to the exclusion of taxing legislation;

(ii) The constitutional validity of Parliamentary legislation imposing sales tax has been upheld on the basis of the provisions of Article 302 which enables Parliament to impose restrictions on the freedom of trade and commerce in the public interest. If taxing legislation is regarded as a restriction for the purposes of Article 302, there is no reason to exclude the same interpretation for the purposes of Article 304;

(iii) Article 304(a) deals with a specific area of taxation - taxation of goods. The legislative powers of the state legislatures in List II of the Seventh Schedule enables them to tax persons, activities or things (*Godfrey Phillips India Ltd. v. State of UP* [196]). Article 304(a) covers only the last category namely a tax on goods. It does not cover taxes on persons (profession taxes or luxury tax) or taxes on activities (betting and gambling);

(iv) Article 301 guarantees free trade, commerce and intercourse throughout the territory of India. Inter-state trade as well as trade and commerce within a state is guaranteed. Article 304(a) covers only taxes imposed on goods imported from other states. Article 304(a)
in other words does not coverim posts on goods traversing within a state;

(v) Article 306 of the Constitution, as it stood prior to its repeal contemplated that restrictions could take the form of duties and imposts; and

(vi) The expression 'restrictions' has been utilized in Part XIII of the Constitution, as the provisions of Articles 302, 303, 304 and 306 would indicate in a manner that would not exclude taxing legislation. The consistent view of Constitution Benches of this Court has been that taxes may under certain circumstances amount to a restriction on the freedom of trade and commerce. The position has been lucidly summarized in the erudite judgment of Justice M N Venkatachaliah (as the learned Chief Justice then was) in *Express Hotels Pvt. Ltd. v. State of Gujarat*[197]. After reviewing the position of law, the learned judge held thus :

"Taxes can and do sometimes, having regard to their effect and impact on the free flow of trade constitute restrictions on the freedom under Article 301. But the restriction must stamp from the provisions of the law imposing the tax which could be said to have a direct and immediate effect of restricting the free flow of "trade, commerce and intercourse". It is not all taxes that have this effect."
(Id. at p. 697)

262. Nearly, five decades of jurisprudence having developed in support of the above principle, there is neither any rationale of constitutional principle or law that should leave this Court to make a departure from the position and to hold that taxes can in no circumstances constitute a restriction on the freedom of trade and commerce.

Moreover, it has been accepted even as a matter of judicial precedent that taxation serves not only the purpose of raising revenues but is also a powerful instrument of social control. The states and the Union in the exercise of their legislative powers, utilise taxation not only as a means of raising revenues to support their developmental activities but also as a measure of achieving social objects. Whether the pursuit of those social objects or the pursuit of social regulation infringes upon the area of free trade and commerce cannot be decided a priori. The power of taxation is capable of being used in a manner which can constitute, in a given case, a restraint or impediment on the freedom of trade and commerce.

263. In determining as to when taxes can constitute a restriction on the freedom of trade and commerce, the direct and immediate effect test (as refined subsequently) provides a judicially manageable framework. The test of direct and immediate effect was enunciated in the judgments in Atiabari and Automobile Transport. The test is firmly entrenched as a part of our jurisprudence. In *R C Cooper v. Union of India*[198], a Bench of eleven Judges of this Court while adjudicating upon the validity of a law providing for bank nationalization overruled the judgment in *A K Gopalan v. The State of Madras*[199] which had taken the view that it was the object of the action of the state in relation to the fundamental right of the individual and not the effect of the action that was relevant. This Court held that :

> "49 But it is not the object of the authority making the law impairing the right of a citizen, nor the form of action that determines the protection he can claim: it is the effect of the law and of the action upon the right which attracts the jurisdiction of the Court to grant relief. If this be the true view, and we think it is, in determining the impact of State action upon constitutional guarantees which are fundamental, it follows that the extent of protection against impairment of a fundamental right is determined not by the object of the Legislature nor by the form of the action, but by its direct operation upon the individual's rights."
>
> (Id at p. 288)
> In *Bennett Coleman & Co. v. Union of India* [200], the same principle was formulated in the following statement of law :
>
> "..First, it is not the object of the authority making the law impairing the right of the citizen nor the form of action that determines the invasion of the right. Secondly, it is the effect of the law and the action upon the right which attracts the jurisdiction of the court to grant relief. The direct operation of the Act upon the rights forms the real test." (Id at p. 799)

264 In *Maneka Gandhi v. Union of India*[201], this Court refined this test to mean the "direct and inevitable effect" of the action impugned. The direct and inevitable effect is that which necessarily must be intended by the state legislature, or, in other words, what may be described as the doctrine of intended and real effect. This Court held that :

"20. It may be recalled that the test formulated in R.C. Cooper case merely refers to "direct operation" or 'direct consequence and effect' of the State action on the

fundamental right of the petitioner and does not use the word "inevitable" in this connection. But there can be no doubt, on a reading of the relevant observations of Shah, J., that such was the test really intended to be laid down by the Court in that case. If the test was merely of direct or indirect effect, it would be an open-ended concept and in the absence of operational criteria for judging "directness", it would give the Court an unquantifiable discretion to decide whether in a given case a consequence or effect is direct or not. Some other concept-vehicle would be needed to quantify the extent of directness or indirectness in order to apply the test. And that is supplied by the criterion of "inevitable" consequence or effect adumbrated in the Express Newspapers case. This criterion helps to quantify the extent of directness necessary to constitute infringement of a fundamental right. Now, if the effect of State action on fundamental rights is direct and inevitable, then a fortiori it must be presumed to have been intended by the authority taking the action and hence this doctrine of intended and real effect." (Id. atp.299)

265. In order to determine whether a law providing for the imposition of a tax constitutes a restriction on the freedom of trade, commerce and intercourse, the principle that must be applied is whether the direct and inevitable effect or consequence of the law is to impede trade and commerce. The burden must lie on the person who alleges that such is the effect of the tax to plead and establish to the satisfaction of the court that the consequence which is alleged does in fact exist. The direct and inevitable consequence for the purposes of Part XIII of the Constitution is not the same as an infringement of the fundamental right to carry on an occupation trade or business under Article 19(1)(g). Under Article 19 (1)(g), it is the individual's right to carry on trade or business which is guaranteed as a fundamental freedom. When a legislative measure seeks to curtail that freedom, the test is whether the right of the individual has been infringed or eviscerated. In the context of Part XIII, the matter is looked at from the perspective of trade and commerce as a whole. Hence, in a case which falls under Part XIII of the Constitution it is for the petitioner to demonstrate and establish that the direct and inevitable effect of the law imposing a tax is to impede or restrict the flow of trade and commerce.

266. The mere fact that the activity which is taxed is related to the flow or movement of trade and commerce is not sufficient in itself to lead to the inference that a tax on that activity impedes or restricts it. Businessmen and traders must and do necessarily factor in the requirement of tax compliance as a part of an overall business plan. Hence, the mere fact that the tax is imposed with reference to an activity or thing which constitutes an aspect of trade or commerce is not sufficient in itself lead to the consequence that it is a restriction or impediment of trade and commerce. The petitioner with such a grievance must cross the threshold of establishing in cogent terms before the Court that the direct and inevitable effect of the tax law is to constitute an impediment of trade and commerce.

267. In the context of entry tax, it is said on behalf of the petitioners that, there cannot be an entry into a local area of goods for consumption, use or sale unless the tax is paid. If the tax is not paid there can be no entry of goods. This is the basis for urging that entry tax constitutes a direct impediment or restriction on the freedom of trade and commerce. This approach to the issue cannot be accepted. In the regulatory sphere,

adherence to a regulatory statute may be made a condition precedent to engaging in a particular line of activity involving business, trade or commerce. However, the requirement of compliance does not by itself render the statute an impediment of trade and commerce. Similarly, in the fiscal arena, the fact that a tax liability has to be discharged as an incident of or a pre-condition for engaging in a line of activity does not by itself - and without actual proof of impediment or restraint - constitute a restriction. A conclusion that the inevitable consequence and effect of the legislation is to impede or restrict trade and commerce can be drawn only on the basis of demonstrable material that establishes that the impact of the tax is to result in that consequence. The burden to establish this is on the person who seeks to do so as a ground for relief.

268 In a regulatory area as well as in a fiscal context, the legislature may prescribe the fulfilment of certain requirements subject to which a line of business, trade or commerce may be pursued. The fulfilment of those requirements may be set down as a condition precedent. A statutory regulator may for instance stipulate requirements of licencing or registration before a commercial activity which it regulates can be undertaken. Licencing or registration norms may stipulate financial and other requirements which need to be fulfilled as a pre-condition for carrying on an activity or business. The fact that a statute allows for or prescribes such norms which constitute a condition precedent is not reason enough to hold that they constitute restrictions in themselves or an impediment of trade and commerce. The right to carry on trade and commerce is not a right to be free from regulation that ensures orderly conditions for the pursuit of the activity. Nor can a right be exercised in such a manner as would create chaos through unregulated actions of numerous participants. In other words, the fact that a requirement operates as a pre-condition is not sufficient in itself to hold that it impedes or restricts trade. In order to constitute an impediment, the condition must be demonstrated to cause, as a direct and inevitable consequence of its operation a restr-iction of trade or commerce. Every regulatory requirement does not restrict or impede trade and commerce even if at the threshold, its fulfilment is a condition enabling a person or entity to engage in a regulated activity.

269. In a fiscal context, the payment of an impost or levy is attracted when the taxing event occurs. The tax may be on persons, activities or things. It is the taxing event which incurs the charge or liability to tax. The charge may be associated with an aspect of an activity or thing. The mere fact that this aspect is connected with the flow or movement of trade or commerce does not in itself lead to the conclusion that the tax constitutes an impediment or restriction. The impediment does not lie in the aspect of the activity or thing which is the subject of the tax but in its consequence. Every tax or movement on entry does not impede trade or commerce. The volume of trade in a commodity is determined by numerous variables including the nature of the product, availability of raw material, transportation and infrastructure, the nature and extent of competition, market cycles as well as the elasticity of demand and supply. The tax structure is one ingredient which has a bearing on the allocation of resources. For a tax to constitute a restriction, there must be demonstrable material to indicate that its direct and inevitable effect or consequence is to obstruct or impede trade or commerce. Before the tax is held to be a restriction, the threshold must be crossed by demonstrating that the immediate and necessary consequence is to restrict impede or

obstruct trade as a whole. Unless the impact of the financial levy is demonstrated, in terms of its direct and inevitable consequence, to restrict trade or commerce the provisions of Article 304 (b) would not be attracted. For, there has to a restriction in the first place before the issue of its reasonableness arises. Consequently, it is not possible to hold that the mere fact that the charge of the tax is associated with an aspect of the movement of trade and commerce indicates that it is a restriction in every case. The burden lies upon the individual or entity asserting the existence of a restriction to demonstrate its impact in terms of the direct and inevitable effect test as adopted above. Hence, there can be no a priori assumption that an entry tax constitutes a restriction or impediment to trade and commerce.

N Conclusion

The conclusions of this judgment are, in summation, formulated below :

270. The freedom guaranteed by Article 301 enables goods, services, persons and capital to engage in trade, commerce and commercial intercourse throughout the territory of India. The expression 'throughout' extends the ambit of the freedom across and within state boundaries. Article 301 subserves the constitutional goal of integrating the nation into an economic entity comprising of a common market for goods and services.

271. The freedom guaranteed by Article 301 is not absolute but is subject to legislative control by Parliament and the state legislatures. Articles 302, 303 and 304 define the ambit of the restrictions which Parliament and the state legislatures may impose by laws enacted in pursuance of their legislative powers under Articles 245 and 246. Besides providing for permissible restrictions, those articles lay down the limits which govern the law making authority.

272. Articles 245 and 246 together constitute the source of the legislative power of Parliament and the state legislatures. Article 245 is subject to the provisions of the Constitution. Every constitutional authority is subject to its provisions. No arm of the Constitution is vested with absolute power. Every institution created by the constitution operates subject to the governing principles of the written constitution and is subject to the limitations which it prescribes. Constitutional limitations on legislative power originate in the necessity that the enacting body must possess legislative competence on the subject on which it enacts law, that the law which it enacts must not infringe fundamental rights and that it must abide by other norms prescribed by the Constitution.

273. Part XIII of the Constitution enunciates a set of constitutional limitations on the legislative power to regulate trade, commerce and commerce.

274. The federal structure is one of the basic features of the Constitution. Judicial interpretation of Part XIII must factor in the necessity of ensuring that the carefully crafted balance between the Union and the States is preserved.

275. Taxation is a sovereign power entrusted by the Constitution to the Union and the States. The Seventh Schedule distributes legislative power, including the power to tax,

between Parliament and the state legislatures. The interpretation of Part XIII must ensure that the autonomy of the states in the fields assigned to them is not eroded.

276. While recognising sovereignty in the fields assigned to the centre and the states, the Constitution subjects its sovereign arms to constitutional limitations which are designed to preserve the balance which it has created. Hence all legislative power, including of a fiscal nature has to abide by the norms of the written constitution. Judicial review of fiscal legislation however recognises the wide latitude which inheres in the legislatures both at the national and state level to classify persons, objects and things for the purpose of raising revenues.

277. The concept of compensatory taxes was judicially evolved in the decision in Automobile Transport to exclude certain regulatory measures and fiscal exactions from the operation of Part XIII. The concept has created doctrinal inconsistencies and uncertainty in the application of legal standards. The decision in Automobile Transport is to that extent overruled.

278. The proposition that taxes do not constitute a restriction on the freedom of trade and commerce (save and except for a discriminatory tax which violates Article 304(a)) does not reflect a valid constitutional principle. Article 304(a) does not constitute the entire universe of taxation for the purpose of Part XIII. Article 304(a) deals with a species of non- discriminatory taxes : non-discriminatory taxes on goods imported from other states.

279. As a statement of constitutional principle, neither of the two positions which lie at the extreme ends of the spectrum is valid : at one end is the position that all taxes are restrictions and at the other end, is the position that no tax (except a discriminatory tax on goods) is a restriction. All taxes do not constitute restrictions. Some taxes may impede trade and commerce.

280. A tax may amount to a restriction where its direct and inevitable effect is to restrict the freedom of trade, commerce and intercourse. The burden to establish this is on the person who seeks to assail the validity of a particular tax on the ground that it amounts to a restriction on the freedom guaranteed by Article 301. Unless this threshold is crossed, the proviso to Article 304(b) will have no application for, it is only when there is a restriction that the question of its reasonableness can arise.

281. The expression 'may' in Article 304 has to be read in conjunction with the expression 'and' which separates clauses (a) and (b). The true construction of the expressions is in the sense of a joint and several "and/or".

282. Article 304(a) does not require that in order to impose a tax on goods imported from other states, similar goods must be actually produced or manufactured within the taxing state. The object of the provision is to prevent states from following protectionist policies by discriminating against goods produced or manufactured by other states. Article 304(a) does not import the concept of a countervailing duty.

283. Article 304(a) does not prevent a reasonable classification. The provision comprehends both formal and substantive notions of equality. Formal equality would be met when the same rate of tax is prescribed for goods imported from other states as is levied on goods produced and manufactured within. Apart from the rate of tax, other significant aspects include procedural provisions such as licensing and registration, the machinery for assessment and set-offs and exemptions. Substantive equality recognises the need for the development of underdeveloped areas of the country. A balance has to be struck between the concerns of both formal and substantive equality. The decisions in Video Electronics and Mahavir must be understood in that context.

284. The expression "any tax" in Article 304(a) does not mean a tax which is referable to only one subject of legislation falling under a taxing entry in List II of the Seventh Schedule. When a legislature legislates, the full range of its plenary powers is available to it. In India, the legislatures are not confined to imposing a tax under one entry while formulating a fiscal law. Hence, Article 304(a) does not fetter the state legislatures from ensuring an equality of tax burden between goods that are imported from other states and goods manufactured or produced within.

285. While enacting entry tax legislation referable to Entry 52 of List II, it is permissible for the state legislature to have regard to the equalisation of tax burdens between goods imported from other states and goods manufactured or produced within. The legislature may have regard to the tax burden under value added tax/sales tax law as well as entry tax, considered as a composite whole. Whether the scheme of exemptions and set offs has achieved an equalisation of tax burdens as between goods domestic to a state and those imported from other states is an issue to be considered in each case having due regard to the provisions of state legislation.

286. A "local area" for the purposes of Entry 52 of List II is not the entire state. Local area postulates an area within a state administered by a local body under relevant state legislation.

[94](1961) 1 SCR 809
[95](1963) 1 SCR 0491
[101](1972) 4 SCC 0635
[102](1974) 2 SCC 777
[103](1975) 1 SCC 0375
[104](1981) 2 SCC 0318, 1981 SCC (Tax) 103
105[1983] 3 SCC 237, 1983 SCC (Tax) 162
[106]AIR (1983) SC 1283
[107](1984) 1 SCC 0168
[108](l988) 4 SCC 0290, (1988) SCC (Tax) 506
[109](1981) 2 SCC 0318
[110](1975) 1 SCC 0375
[111](1995) Supp.(1) SCC 0673
[112](1980) 4 SCC 0697
[113](1996) 9 SCC 0136
[114](1990) 1 SCC 0012
[115](2003) 8 SCC 0060
[116](2006) 7 SCC 0241
[117](1992) Supp 2 SCC 0651
[118](2002) 8 SCC 0481
[119](1964) 1 SCR 0371
[120](Id at p. 396)
[121](Id at p.396)
[122](1961) 1 SCR 0413
[123](1994) 3 SCC 0001
[124](2002) 9 SCC 0232
[125](2006) 7 SCC 0001
[126](2012) 7 SCC 0106
[128]AIR (1963) SC 1667
[129](1963) 1 SCR 0220
[130](1992) 2 SCC 0411
[131](2000) 5 SCC0 694
[132]AIR (1955) SC 0540
[133](1966) Supp SCR00 81
[134](1946) FCR 0111
[135](1953) 1 BLJR 0048
[136](1997) 7 SCC 0339
[137](1985) 1 SCC 0641
[138](1987) 1 SCC 0038
[139](1988) 1 SCC 0266
[140](1989) 3 SCC 0634
[141](1989) 3 SCC 0677
[142](1994) 5 SCC 0198
[143](1986) Supp. 1 SCC 0201
[144]AIR (1950) SC 0468

[145](1968) 3 SCR 0829
[146](1974) 4 SCC 0408
[148](1964) 4 SCR 0280
[149](1953) 4 SCR 1069
[150](1986) 4 SCC 0447
[151](1964) 4 SCR 0280
[153](1951) 2 SCR 0127
[154](1961)3 SCR 0077
[155](1962) 2 SCR 0983
[156](1962) Supp. (2) SCR 0001
[157](1963) 1 SCR 0220
[158](1989) 3 SCC 0634
[159]AIR (1963) SC 1237
[160](1963) Suppl.(2) SCR 435
[161]AIR (1964) SC 1729
[162](1968) 3 SCR 0829
[163](1966) 1 SCR 0865
[164](1970) 1 SCR 0700
[165](1969) 2 SCR 0544
[166](1977) 1 SCC 0234
[167](1980) 4 SCC 0697
[168](1988) 2 SCC 0568
1[69](1990) 3 SCC 0087
[170](Id. at p. 112, Para 35)
[171](1996) 11 SCC 0039
[172](1996) 11 SCC 0039
[173](1961) 3 SCR 0242
[174](1961) 3 SCR 0707
[175](1963) Supp. 2 SCR 0216
[176](1995) 1 SCC 0351
[180](1989) 3 SCC 0488
[181](2007) 7 SCC 0527
[182](2002) 5 SCC 0203
[183](2000) 1 SCC 0688 (Pr. 24)
[184](1942) F.C.R.0090
[185]AIR (1945) PC 0098
[186]AIR (1950) SC 0011
[187](1962) Supp. 1 SCR 0282
[188](1980) 2 SCC 0410
[189](1971) 2 SCC 0779
[190](1996) 3 SCC 0105
[191](1980) 3 SCC 0330
[192](2005) 2 SCC 0515
[193](1983) 4 SCC 0045
[194](2004) 10 SCC 2011
[195](1963) 3 SCR 0787
[197](1989) 3 SCC 0677
[198](1970) 1 SCC 0248
[199](1950) 1 SCR 0088
[200](1972) 2 SCC 0788
[201](1978) 1 SCC 0248

JUDGMENT

Ashok Bhushan,J.,

1. Before this Constitution Bench of Nine Judges of the Apex Court of this country which have time and again, when there arose serious debates and doubts on the Constitutional provisions of our country, authoritatively concluded the debates and quenched the doubts, a galaxy of lawyers by their illuminating arguments engaged the Court for long twenty one days hearing. Now, it is our turn to respond.

2. In preparing my judgment I had advantage of going through thoughtful & well reasoned judgment of My Lord the Chief Justice. I deeply regret my inability to share the views of learned Chief Justice on Question No. 1 & 4 as framed by us, although I agree with the conclusion of His Lordship on Question No. 2 & 3. The views of Dr. Justice D. Y. Chandrachud in his scholarly judgment are fairly near my own except on few subjects on which I have expressed different opinion. Looking to the vital Constitutional issues having a far reaching impact on economic unity of the country, I consider it my duty to express my views in my own way on all issues raised before us. I begin my task in following manner.

3. This larger Bench has been constituted on a reference made by a Constitution Bench of this Court in *Jindal Stainless Ltd & another Vs. State of Haryana & Othe*[1], expressing doubts on correctness of Constitution Bench Judgment in Atiabari Tea Co. Ltd, 1961 (1) SCR 809 and 7 Judges Bench Judgment in Automobile Transport case, (Supra)on interpretation of Part XIII of the Constitution of India. Part XIII of the Constitution was engrafted by framers of the Constitution to attain the goal of economic unity of the country. Large number of issues ranging from principles of constitutional interpretation, federalism, sovereignty of states, limitation on legislative powers of the States, freedom of trade, commerce and intercourse as envisaged by Constituent Assembly, to the interpretation of various articles of Constitution including Article 301 – 306 contained in Part XIII, have arisen before us in this bunch of cases.

4. For answering the questions which have arisen before us, various aspects related to the issues noticed above are to be deliberated with reference to relevant precedents. We have thus identified certain broad steps for our discussion before attempting to answer the specific questions.

5. On the above subjects, learned eminent counsel appearing before us have thrown different shades of light to illuminate the topics, which we are sure, shall make our task easy to discharge our constitutional responsibility of interpreting the Constitution. The Constitution, not only, contains the goals and aspirations set by Constituent Assembly for our country, but it is also a guiding star for the future generations to attain the highest standards of social, political, economic and individual life. We have divided our discussion into parts which are; firstly, the facts leading to this reference. Secondly, two Constitution Bench judgments in Atiabari Tea Company and Automobile Transport. Thirdly, submissions made before us by learned counsel appearing for various parties. Fourthly, the discussion on the subjects relevant on questions falling for our considerations. Fifthly, our conclusions, and sixthly, our answers. Fourth part contains following subjects:-

A. LEGISLATIVE HISTORY AND DEBATES IN CONSTITUENT ASSEMBLY ON FREEDOM OF TRADE, COMMERCE AND INTERCOURSE.

B. NATURE OF FEDERALISM IN CONSTITUTION OF INDIA.

C. LIMITATIONS ON THE LEGISLATIVE POWER OF THE STATE UNDER THE CONSTITUTION.

D. WHETHER PART XIII OF THE CONSTITUTION INCLUDES "TAX LEGISLATION" AND WORD "RESTRICTION" USED THEREIN INCLUDES TAX LEGISLATION.

E. LEGISLATIVE HISTORY AND CONSTITUENT ASSEMBLY DEBATES RELATING TO ARTICLE 304(a) AND ARTICLE 304(b).

F. INTERPRETATION, SCOPE AND AMBIT OF ARTICLE 304(a) AND ARTICLE 304(b).

G. ENTRY 52, LIST II OF VIITH SCHEDULE.

H. MEANING OF RESTRICTION AS USED IN PART XIII.

I. WHETHER DIRECT AND IMMEDIATE EFFECT TEST AS LAID DOWNIN ATIABA-RI & APPROVED IN AUTOMOBILE TRANSPORT IS NO LONGER A CORRECT TEST.

J. COMPENSATORY TAX THEORY.

PART I
FACTS AND EVENTS LEADING TO REFERENCE TO THIS NINE JUDGES BENCH

6. For fully appreciating the issues and questions raised in this batch of cases, certain facts and events preceding the Reference to this larger Bench need to be noted. The challenges to various State Legislations were laid before different High Courts on various grounds including the ground that levy of Entry Tax violates the freedom of trade, commerce and intercourse as guaranteed by Article 301 of the Constitution of India and Legislations are not saved under Article 304.

7. One of the State Legislations, namely, Haryana Local Area Development Tax Act, 2000 came to be challenged before Punjab and Haryana High Court. The High Court by its judgment dated 21.12.2001 upheld the validity of the Act which judgment came to be challenged in Civil Appeal No.3453 of 2002 with connected matters; Jindal Stainless Ltd. & Anr. vs. State of Haryana & Ors. In the above appeals, appellants were Industries or Association of Industries manufacturing their products within the State of Haryana. The raw materials for their respective products were brought from outside the State. The above 2000 Act was enacted to provide for levy and collection of tax on the entry of goods into the local area of the State of Haryana for consumption and use therein and matters incidental thereto and connected thereto. One of the grounds of challenge was that 2000 Act is violative of Article 301 and not saved under Article 304. The Pubjab and Haryana High Court repelled the challenge holding that Entry Tax being compensatory in nature is outside the purview of Article 301 as has been held by the Constitution Bench judgment in *Atiabari Tea Co. Ltd. vs.The State of Assam& Ors*[2], and larger Bench judgment of Seven Judges in *Automobile Transport (Rajasthan) Ltd. vs. The State of Rajasthan and Ors*[3],

8. In Atiabari Tea Co.Ltd.(supra) the Assam Taxation(on goods carried by Roads and Inland Waterways) Act, 1954 was challenged. The Assam High Court upheld the validity of that Act against which the matter was taken to this Court, the appellant contended that Act violated the freedom of trade and it was without previous President's Sanction as required by Article 304(b). The majority rejected the argument raised on behalf of the State that Tax Laws are outside Part XIII. It was held that the Tax Laws can and do amount to restriction freedom from which is guaranteed to trade under Part XIII. It was held that a rational and workable test to be applied for finding out is; whether the impugned restrictions operate directly and immediately on trade or its movement.

9. The above decision of the Constitution Bench came for consideration before larger Bench in Automobile Transport (supra). In which case Rajasthan Motor Vehicles Taxation Act, 1951 came to be challenged on the ground that it violates Article 301. The Rajasthan High Court has upheld the validity of that Act. The larger Bench in the Automobile Transport case by majority approved the ratio of Atiabari Tea Co.Ltd. Subject to an exception which was judicially crafted that compensatory taxes are not hindrance to any body's freedom. It was held that regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contained in Article 301 and such measures need not comply

with the requirement of the proviso to Article 304(b).

10. It was further held that a working test for deciding whether a tax is compensatory or not is to enquire whether the traders people are having the use of certain facilities for the better conduct of their business and paying not much more than what is required for providing the facilities.

11. The above two judgments, around which discussion before us has centered shall be noted hereinafter in some detail including the views expressed by the majority and minority.

12. What is compensatory tax came for consideration by this Court in the context of M.P. Sthaniya Kshetra Me Mal Ke Pravesh Par Kar Adhiniyam, 1976 in *M/s. Bhagatram Rajeevkumar vs. Commissioner of Sales Tax, M.P. and others*[4] . The Three Judge Bench in the above case held that the concept of compensatory nature of tax has been widened and if there is substantial or even some link between the tax and the facilities extended to such dealers directly or indirectly the levy cannot be impugned as invalid. The above Three Judge Bench judgment was followed by a Two Judge Bench in *State of Bihar and others vs. Bihar Chamber of Commerce and others*[5], which was in the context of Bihar (Tax on Entry of Goods into Local Areas for Consumption, Use or Sale Therein) Act, 1993. Two Judge Bench reiterated the position that "some connection" between the tax and the trading facilities is sufficient to mention it as compensatory tax.

13. Now reverting back to *Jindal Stripe Ltd.and another vs. State of Hayana and others*[6] , before the Two Judge Bench of this Court, submissions on behalf of State of Haryana that tax is compensatory in nature and submissions by the appellant that the Act violates Article 301 was noted. The Two Judge Bench also referred to Aitabari Tea Co. Ltd. And Automobile Transport (Rajasthan) Ltd. and noted the working test for finding out a compensatory tax as laid down in Automobile Transport. Two Judge Bench expressed its doubt regarding the correctness of tests laid down by Bhagatram Rajeevkumar and Bihar Chamber of Commerce to find out whether the tax is compensatory or not. Two Judge Bench expressed its doubt and observed that interpretation of Article 301 vis-a-vis compensatory tax need to be laid down by a Constitution Bench. Following was laid down in paragraph 26 and 27:

> "26. The decisions in Bhagat Ram and Bihar Chamber of Commerce now say that even if the purpose of imposition of the tax is not merely to confer a special advantage on the traders but to benefit the public in general including the traders, that levy can still be considered to be compensatory. According to this view, an indirect or incidental benefit to traders by reason of stepping up the developmental activities in various local areas of the State can be legitimately brought within the concept of compensatory tax, the nexus between the tax known as compensatory tax and the trading facilities not being necessarily either direct or specific.
>
> 27.Since the concept of compensatory tax has been judicially evolved as an exception to the provisions of Article 301 and as the parameters of this judicial

concept are blurred particularly by reason of the decisions in Bhagat Ram (supra) and Bihar Chamber of Commerce(supra), we are of the view that the interpretation of Article 301 vis-a-vis compensatory tax should be authoritatively laid down with certitude by the Constitution Bench under Article145(3)."

14. Consequent to Reference made to the Constitution Bench in Jindal Stripe Ltd.(supra), a Five Judges Bench answered the Reference by its judgment dated 13th April, 2006 reported in *Jindal Stainless Ltd.(2) and another vs. State of Haryana and others*[7], the Constitution Bench overruled judgments of Bhagatram Rajeevkumar and Bihar Chamber of Commerce and recorded their views in paragraph 52-53 to the following effect:

"52. In our opinion, the doubt expressed by the referring Bench about the correctness of the decision in Bhagatram's case followed by the judgment in the case of Bihar Chamber of Commerce was well-founded.

53.We reiterate that the doctrine of "direct and immediate effect" of the impugned law on trade and commerce under Article 301 as propounded in Atiabari Tea Co. Ltd. v. State of Assam and the working test enunciated in Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan for deciding whether a tax is compensatory or not vide para 19 of the report, will continue to apply and the test of "some connection" indicated in para 8 of the judgment in Bhagatram Rajeevkumar v. Commissioner of Sales Tax, M.P. and followed in the case of State of Bihar v. Bihar Chamber of Commerce, is, in our opinion, not good law. Accordingly, the constitutional validity of various local enactments which are the subject matters of pending appeals, special leave petitions and writ petitions will now be listed for being disposed of in the light of this judgment."

15. After judgment of the Constitution Bench all the matters including the matters of Jindal were again listed before a Two Judge Bench. Two Judge Bench noticed that basic issues revolve around the concept of compensatory tax and the High Courts concerned had not examined the issues in the proper perspective as they were bound by the judgments of Bhagatram Rajeevkumar and Bihar Chamber of Commerce. Referring to the Constitution Bench judgment in Jindal Stainless Ltd.(2) (supra) this Court in *Jindal Stainless Ltd.(3) and another vs. State of Haryana and others*[8], permitted the parties to place the data in the writ petitions before the High Court and the High Courts were requested to decide the aforesaid issues within five months. Following was stated in paragraphs 5 & 6:

“5.Since relevant data do not appear to have been placed before the High Courts, we permit the parties to place them in the concerned Writ Petitions within two months. The concerned High Courts shall deal with the basic issue as to whether the impugned levy was compensatory in nature. The High Courts are requested to decide the aforesaid issue within five months from the date of receipt of our order. The judgment in the respective cases shall be placed on record by the concerned parties within a month from the date of the decision in each case pursuant to our direction. "6.Place these matters for further hearing in

third week of January, 2007."

16. Different High Courts in consequence to directions by this Court in Jindal Stainless Ltd.(3) (supra) decided the matter one or other way. Some of the High Courts held the Act, which were under challenge, compensatory in nature whereas other High Courts relying on the Constitution Bench judgment in Jindal Stainless Ltd.(2), held the respective Acts as not compensatory. The judgments of the different High Courts consequent to directions in Jindal Stainless Ltd.(3) came to be challenged by different assessees and the State before this Court. A batch of SLPs came for consideration before Two Judge Bench. Two Judge Bench observed that though some of the factors have been addressed to by the Constitution Bench in Jindal Stainless (2)(supra) whereas certain other constitutional issues are involved. Two Judge Bench opined that considering the importance of the issues relating to Articles 301 and 304 and Part XIII of the Constitution, it is necessary to refer the matter to a larger Bench in terms of Article 145(3) of the Constitution. In Reference order following was stated in paragraphs 8 and 9:

"8.The concept of compensatory tax is judicially evolved and in a way provides a balancing factor between federal control and State Taxing Board. The concept really had its matrix in transportation cases and does not apply to general notion of Entry Tax. Therefore, considering the importance of the issues relating to Articles 301 and 304 and Part XIII of the Constitution, we consider it necessary to refer the matter to a larger Bench in terms of Article 145(3) of the Constitution.

9.The following questions are referred for the aforesaid purpose:

(1) Whether the State enactments relating to levy of Entry Tax have to be tested with reference to both Clauses (a) and (b) of Article 304 of the Constitution for determining their validity and whether Clause (a) of Article 304 is conjunctive with or separate from Clause (b) of Article 304?

(2) Whether imposition of Entry Tax levied in terms of Entry 52 List II of 7th Schedule is violative of Article 301 of the Constitution? If the answer is in the affirmative whether such levy can be protected if Entry Tax is compensatory in character and if the answer to the aforesaid question is in the affirmative what are the yardsticks to be applied to determine the compensatory character of the Entry Tax.

(3) Whether Entry 52, List II, 7th Schedule of the Constitution like other taxing entries in the Schedule, merely provides a taxing field for exercising the power to levy and whether collection of Entry tax which ordinarily would be credited to the Consolidated Fund of the State being a revenue received by the Government of the State and would have to be appropriated in accordance with law and for the purposes and in the manner provided in the Constitution as per Article 266 and there is nothing express or explicit in Entry 52, List II, 7th Schedule which would compel the State to spend the tax collected within the local area in which it was collected?

(4) Will the principles of quid pro quo relevant to a fee apply in the matter of taxes imposed under Part XIII?

(5) Whether the Entry Tax may be levied at all where the goods meant for being sold, used or consumed come to rest (standstill) after the movement of the goods ceases in the 'local area'?

(6) Whether the Entry Tax can be termed a tax on the movement of goods when there is no bar to the entry of goods at the State border or when it passes through a local area within which they are not sold, used or consumed?

(7) Whether interpretation of Articles 301 to 304 in the context of Tax on vehicles (commonly known as 'transport') cases in Atiabari's case (supra) and Automobile Transport's case (supra) apply to Entry Tax cases and if so, to what extent.
(8) Whether the non discriminatory indirect State Tax which is capable of being passed on and has been passed on by traders to the consumers infringes Article 301 of the Constitution?

(9) Whether a tax on goods within the State which directly impedes the trade and thus violates Article 301 of the Constitution can be saved by reference to Article 304 of the Constitution alone or can be saved by any other Article?

(10) Whether a levy under Entry 52, 18th List II, even if held to be in the nature of a compensatory levy, it must, on the principle of equivalence demonstrate that the value of the quantifiable benefit is represented by the costs incurred in procuring the facility/services (which costs in turn become the basis of re-imbursement/recompense for the provider of the services/ facilities) to be provided in the concerned 'local area' and whether the entire State or a part thereof can be comprehended as local area for the purpose of Entry Tax?"

17.Consequent to the above Reference order dated December, 2008 in *Jaiprakash Associates Limited vs. State of Madhya Pradesh and others*[9], the matter again came to be listed before a Constitution Bench of Five Judges. The Constitution Bench again heard the entire batch of cases including the appeals against the judgment dated 21.12.2001 of the Punjab and Haryana High Court where the validity of 2000 Act was upheld. The Constitution Bench by its order dated April 16, 2010, reported in *Jindal Stainless Ltd. and another vs. State of Haryana and others*[10], decided to make a Reference for constituting a suitable larger Bench for reconsideration of the judgments of this Court in Atiabari Tea Co. Ltd. and Automobile Tranposrt (Rajasthan) Ltd. The Constitution Bench in its order noted the following in paragraphs 1,2 and 3:

"1.On 18th December, 2008, when some of the cases in the present batch camfor
hearing before a Division Bench of this Court to which one of us, Kapadia, J., was a party, the Division Bench of this Court found that some of the High Courts before which the State Entry Tax stood challenged had taken the view that Clause (a) and Clause (b) of Article 304 of the Constitution of

India are independent of each other and that if the impugned law stood saved under Article 304(a) then it need not be tested with reference to Clause (b) for determining its validity.

2. Accordingly, on 18th December, 2008, the Division Bench of this Court referred to the Constitution Bench 10 questions, the most important of which being - whether the State enactments relating to levy of entry tax have to be tested with reference to both Article 304(a) and Article 304(b) of the Constitution and whether Article 304 (a) is conjunctive with or separate from Article 304(b)? Consequently, the matter stood referred to the Constitution Bench of this Court.

3. Accordingly, on 16th March, 2010, the entire batch of cases came for hearing before the Constitution Bench in which the lead matter is Jindal Stainless Ltd. and Anr. v. State of Haryana and Ors. When the hearing commenced before the Constitution Bench, we found that the assessees (original petitioners in the High Courts) are heavily relying upon the tests propounded by a 5-Judge Bench of this Court in Atiabari Tea Co. Ltd. v. The State of Assam and Ors., which tests subject to the clarification, stood reiterated in the subsequent judgment delivered by a larger Bench of this Court in the case of The Automobile Transport (Rajasthan) Ltd. v.
The State of Rajasthan and Ors."

18. The Constitution Bench was of the view that on a number of aspects a larger Bench of this Court needs to revisit the interpretation of Part XIII of the Constitution including the various tests propounded in the judgments of the Constitution Bench of this Court in Atiabari Tea Co. and Automobile Transport(Rajasthan) Ltd. Some of these aspects which need consideration by a larger Bench of this Court were enumerated in Paragraphs 11, 12 and 13 & 14 which are relevant, are to the following effects:

"11.Some of these aspects which need consideration by larger Bench of this Court may be briefly enumerated. Interplay/interrelationship between Article 304(a) and Article 304(b). The significance of the word "and" between Article 304(a) and 304(b). The significance of the non obstante clause in Article 304. The balancing of freedom of trade and commerce in Article 301 vis-a-vis the States' authority to levy taxes under Article 245 and Article 246 of the Constitution read with the appropriate legislative Entries in the Seventh Schedule, particularly in the context of movement of trade and commerce.

12. Whether Article 304(a) and Article 304(b) deal with different subjects? Whether the impugned taxation law to be valid under Article 304(a) must also fulfil the conditions mentioned in Article 304(b), including Presidential assent? Whether the word "restrictions" in Article 302 and in Article 304(b) includes tax laws? Whether validity of a law impugned as violative of Article 301 should be judged only in the light of the test of non-discrimination? Does Article 303 circumscribe Article 301? Whether "internal goods" would come under Article 304(b) and "external goods" under Article 304(a)? Whether "per se test"

propounded in Atiabari's case (supra) should or should not be rejected? Whether tax simpliciter constitutes a restriction under Part XIII of the Constitution? Whether the word "restriction" in Article 304(b) includes tax laws? Is taxation justiciable? Whether the "working test" laid down in Atiabari makes a tax law per se violative of Article 301? Inter-relationship between Article 19(1) (g) and Article 301 of the Constitution? These are some of the questions which warrant reconsideration of the judgments in Atiabari Tea Co. Ltd and Automobile Transport (Rajasthan) Ltd. (supra) by a larger Bench of this Court.

13. In conclusion, we may also mention that though the judgments in Atiabari Tea Co. Ltd. and Automobile Transport (Rajasthan) Ltd. (supra) came to be delivered 49 years ago, a doubt was expressed about the tests laid down in those two judgments even in the year 1975 in the case of G.K. Krishnan and Ors. v. State of Tamil Nadu and Ors. by Mathew, J., vide para 27, which reads as under:

"27.Whether the restrictions visualized by Article 304(b) would include the levy of a non-discriminatory tax is a matter on which there is scope for difference of opinion. Article 304(a) prohibits only imposition of a discriminatory tax. It is not clear from the article that a tax simpliciter can be treated as a restriction on the freedom of internal trade. Article 304(a) is intended to prevent discrimination against imported goods by imposing on them tax at a higher rate than that borne by goods produced in the State. A discriminatory tax against outside goods is not a tax simpliciter but is a barrier to trade and commerce. Article 304 itself makes a distinction between tax and restriction. That apart, taxing powers of the Union and States are separate and mutually exclusive. It is rather strange that power to tax given to States, say, for instance, under Entry 54 of List II to pass a law imposing tax on sale of goods should depend upon the goodwill of the Union Executive."

(emphasis supplied)

14. For the aforestated reasons, let this batch of cases be put before Hon'ble Chief Justice of India for constituting a suitable larger Bench for reconsideration of the judgments of this Court in Atiabari Tea Co. and Automobile Transport (Rajasthan) Ltd. (supra)."

19. In pursuance of Reference made by the Constitution Bench by its order dated 16th April, 2010 Hon'ble the Chief Justice has constituted this Nine Judges Bench to hear the matter.

20. Although in paragraphs 11 and 12, as extracted above, certain questions were noted by the Constitution Bench, when the hearing began in the present batch of cases this Bench with the assistance of learned counsel appearing for the parties have re-framed the questions to be considered. Four main issues which have been framed by this Bench are as follows:

"1. Can the levy of a non-discriminatory tax per se constitute infraction of Article

301 of the Constitution of India?

2. If answer to Question No.1 is in the affirmative, can a tax which is compensatory in nature also fall foul of Article 301 of the Constitution of India.

3. What are the tests for determining whether the tax or levy is compensatory in nature?

4. Is the Entry Tax levied by the States in the present batch of cases violative of Article 301 of the Constitution and in particular have the impugned State enactments relating to Entry Tax to be tested with reference to both Articles 304(a) and 304(b) of the Constitution for determining their validity?

21. With regard to Question No.1 nine incidental questions have also been framed which are as follows:

"1. Is levy of taxes an attribute of a sovereign State?

2. If the answer to Question No.1 is in the affirmative, does Article 246 of the Constitution of India recognise the sovereign power of States to make laws including laws levying taxes on subject matters enumerated in Entry II of 7th Schedule?

3. Is the power to make laws and levy taxes reserved In favour of the States under Article 246 read with List-II subject to Part-XIII of the Constitution?

4. In case answer to Question No.3 is in the negative, would any interpretation of provisions of Article 301 of the Constitution that makes the power to make laws and levy taxes subservient to Article 301 have the effect of denuding the States of their sovereign power and affecting the federal structure envisaged by the Constitution?

5. Is levy of taxes presumed to be in public interest?

6. If answer to Question No.5 is in the affirmative, can levy of taxes be justified as reasonable restrictions imposed in public interest?

7. If levy of taxes under Article 304(b) were permissible only with the previous sanction of the President, would such levies not come under judicial scrutiny for determining whether the levy is reasonable and in public interest?

8. If answer to the Question No.7 is in the affirmative, would it not affect the separation of powers between the legislature on the one hand and the judiciary on the other?

9. In the absence of anything to show that Article 301 excludes only such taxes as are compensatory in nature, would the compensatory tax theory not bring

about a dichotomy that is inconsistent with the language employed in Article 301?

22. Learned counsel for the parties have made their respective submissions in reference to the above questions framed by this Bench.

PART II
ATIABARI TEA CO. LTD.

23. The Constitution Bench of this Court, by majority opinion, delivered by P.B. Gajendragadkar J. had considered various aspects of Part XIII of the Constitution of India, especially Article 301. The challenge before this Court was to the provisions of Assam Taxation (on goods carried by Roads and Inland Waterways) Act, 1954 (hereinafter referred to as "the Assam Act, 1954"). Under the Assam Act, 1954, appellants who were growers of tea in the West Bengal or in Assam and carried out their tea to the market in Calcutta were asked to pay tax on goods in their journey in part of territory of Assam.

24. The appellant had challenged the vires of the Assam Act, 1954 before the Assam High Court on various grounds including the ground that provisions of the Assam Act, 1954 are violative of rights given under Article 301 of Constitution of India. The Assam High Court repelled the challenge by Dismissing the writ petition. Three appeals were filed on Certificate granted by the High Court; two writ petitions were directly filed under Article 32, challenging the vires of the Assam Act, 1954. Both the appeals and the writ petitions were heard by the Constitution Bench. The majority opinion was expressed by P.B. Gajendragadkar J.: B.P. Sinha, C.J. and J.C. Shah, J. delivered separate opinions. Before the Constitution Bench, the principal submission which was made by the appellants/petitioners was that Article 301 of the Constitution of India grants the freedom of trade, commerce and intercourse throughout the territory of India and the Assam Act, 1954 levies tax on carrying out the tea throughout the State of Assam, and it had the effect of interfering with the above freedom. The respondent contended that the Act in pith and substance, a legislature to levy tax on certain classes of types of goods carried by road or inland, waterways strictly within entry of the State List, the Assam Act, 1954 was not within the prohibition contained under Article 301 of the Constitution of India. One of the submissions pressed before the Constitution Bench was that taxing power having been conferred on the State by Article 245 to 24 8 read with relevant Entries in List II, Part XIII cannot be held to be attracted on the taxing statue.

25. P.B. Gajendragadkar J. rejected the arguments that the tax laws are outside Part XIII. Following was observed as under:-

> " Thus the intrinsic evidence furnished by some of the Articles of Part XIII shows that taxing laws are not excluded from the operation of Art.301; which means that tax laws can and do amount to restrictions freedom from which is guaranteed to trade under the said part "

26. Further, question posed by P.B. Gajendragadkar J. was that whether all tax laws attract the provisions of Part XIII? Whether their impact on trade or its movement is direct and immediate or indirect and remote? Answering the said questions, it was observed as under:¬

> " Thus considered we think it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Article 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Article 301. The argument that all taxes should be governed by Article 301 whether or not their impact on trade is immediate or mediate, direct or remote, adopts, in our opinion, an extreme approach which cannot be upheld "
>
> Further, it was observed that:¬" We are, therefore, satisfied that in determining the limits of the width and amplitude of the freedom guaranteed by Article 301 a rational and workable test to apply would be: Does the impugned restriction operate directly or immediately on trade or its movement? "

27. After laying down the relevant proposition on interpretation of Part XIII and after applying the said propositions to the Assam Act, 1954, following was observed in the majority opinion:-

> " It purports to put a restraint in the form of taxation on the movement of trade, and if the movement of trade is regarded as an integral part of trade itself, the Act in substance puts a restriction on trade itself. The effect of the Act on the movement of trade is direct and immediate; it is not indirect or remote; and so legislation under the said Entry must be held to fall directly under Article 301 as legislation in respect of trade and commerce "

28. B.P. Sinha, C.J. in his minority opinion held that freedom declared by Article 301 does not mean freedom of taxation simpliciter but it does mean freedom from taxation which has the effect of directly impeding the free flow of trade, commerce and intercourse.

29. Sinha J. also held that if legislature imposes a tax, which is an impediment to the free flow of trade, commerce and intercourse, such law assumes character of trade barrier which is contrary to freedom granted under Article 301. Following was observed by Sinha J.

> " If a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution- makers to abolish by Part XIII "

30. Sinha J. upheld the Assam Act, 1954. The third opinion of The Constitution Bench was expressed by Shah J. Shah J. held that taxation was one of the restrictions from the imposition of which by the guarantee of Article 301 trade, commerce and intercourse was declared free. Shah J. expressed his conclusion in following words:¬" On a careful review of the various Articles, in my judgment, by Part XIII, restrictions have been imposed upon the legislative power granted by Articles 245, 246 and 248 and the lists in the seventh schedule to the Parliament and the State Legislatures and those restrictions include burdens of the nature of taxation. Therefore, the power to tax commercial intercourse vested by the legislative lists in the Parliament or the State Legislatures, is circumscribed by Part XIII of the Constitution and if the exercise of that power does not conform to the requirements of Part XIII, it would be regarded as invalid "

31. As noted above, by the majority opinion expressed by Gajendragadkar, J. with whom Shah J. concurred, the provisions of Assam Act, 1954 were held to be infringing the Article 301 and since the Bill had not received the assent of President as required under Article 304(b) proviso, the Act was declared void. The Automobile Transport (Rajasthan) Ltd.

32. The writ petitions were filed before the Rajasthan High Court challenging the demand of payment of tax due on their registered motor vehicles under the Rajasthan Motor Vehicles Taxation Act, 1951 (hereinafter referred to as 'the Act').

33. In the writ petitions, principal contention raised before the High Court was that the provision of the Act imposing tax on their motor vehicles was unconstitutional and void as they contravened the freedom of trade, commerce and intercourse throughout the territory of India as guaranteed by Article 301 of the Constitution of India.

34. The Division Bench of the High Court referred the matter to the Full Bench. The Full Bench took the view that taxation under the aforesaid Act cannot be said to offend Article 301 for its effect on trade, commerce is only indirect and consequential and it may be regarded only as remote.

35. The matter was taken to this Court and heard by a Constitution Bench of five Judges which felt that having regard to the importance of the Constitutional issues involved and the views expressed by this Court in case "*Atiabari Tea Co. Ltd. Vs. The State of Assam and Others" reported in*[11], the appeals should be heard by a larger Bench. The appeals were consequently placed for hearing before the Bench of seven Judges. Three opinions came to be delivered in the larger Bench. S.K. Das, J. delivered the judgment for himself, J.L. Kapur, J., A.K. Sarkar J. and K. Subba Rao, J. delivered separate opinion concurring with the opinion expressed by Das J.

36. Justice M. Hidayatullah delivered minority judgment on behalf of himself and N. Ra-jagopala Ayyangar, J., J.R. Mudholkar, J., Dass J. and SubbaRao J. Das, J. upheld the provisions of the Act, upholding the provisions of the Act as regulatory and compensatory. However, while upholding the provisions of the Act, the majority judgment approved the earlier Constitution Bench Judgment in Atiabari

Tea Co. Ltd (supra) with one clarification, in following words:

> "The interpretation which was accepted by the majority in the Atiabari Tea Co. case is correct, but subject to this clarification. Regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Art.301 and such measures need not comply with the requirements of the provisoto Art.304(b) of the Constitution."

37. Das, J. held that tax for use of a road or for the use of bridge is not barrier or burden or deterrent to traders. It was held that such taxes are compensatory taxes which do not hinder anybody's freedom. Following was observed by Das, J.:-

> " The collection of a toll or a tax for the use of a road or for the use of a bridge or for the use of an aerodrome is no barrier or burden or deterrent to traders who, in their absence, may have to take a longer or less convenient or more expensive route. Such compensatory taxes are no hindrance to anybody's freedom so long as they remain reasonable; but they could of course be converted into a hindrance to the freedom of trade. If the authorities concerned really wanted to hamper anybody's trade, they could easily raise the amount of tax or toll to an amount which would be prohibitive or deterrent or create other impediments which instead of facilitating trade and commerce would hamper them. It is here that the contrast, between "freedom" (Article 301) and "restrictions" (Articles 302 and 304) clearly appears: that which in reality facilitates trade and commerce is not a restriction, and that which in reality hampers or burdens trade and commerce is a restriction. It is the reality or substance of the matter that has to be determined. It is not possible a priori to draw a dividing line between that which would really be a charge for a facility provided and that which would really be a deterrent to a trade; but the distinction: if it has to be drawn, is real and clear. For the tax to become a prohibited tax it has to be a direct tax the effect of which is to hinder the movement part of trade. So long as a tax remains compensatory or regulatory it cannot operate as a hindrance "

38. Das, J. did not accept the arguments that restrictions in Part XIII of the Constitution do not apply to taxation laws.

39. After laying down the relevant test for examining the validity of taxing statue, Das J. noted various provision of the Act. It was held that Section 4 of the Act makes it clear that tax is imposed on a motor vehicle which is to be used in any public place or kept to be used for in the State of Rajasthan. What should be the test to enquire as to whether a tax is a compensatory or not, following was stated as under:¬" It seems to us that a working test for deciding whether a tax is compensatory or not is to enquire whether the trades 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. It would be impossible to judge the compensatory nature of a tax by a meticulous test, and in the nature of things that cannot be done "

40. Ultimately, Das, J. held that the Act does not violate the provision of Article 301 and the tax imposed under the Act are compensatory taxes which did not hinder the freedom of trade, commerce and intercourse assured by Article 301. Taxes imposed were legal and High Court had rightly dismissed the writ petitions. Subba Rao J., agreed with the conclusion arrived by Das, J.

41. It was held, that the arguments cannot be accepted that law of taxation is outside the scope of freedom enshrined under Article 301 of the Constitution. Subba Rao, J. also laid down that the doctrine of "direct and immediate effect" is the most important doctrine to find out whether there is restriction on the free movement of trade. It was further held that compensatory or regulatory tax cannot be treated as restriction.

42. Hidyatullah, J. also expressed a view that all taxes or taxing laws are not outside the reach of Part XIII. It was further held that tax is a restriction when it is placed upon a trade directly and immediately. But the tax being generally paid by tradesman in common with others, cannot be held to be infringing freedom of trade under Article 301.Following obse-rvations were made as under:

> ¬" That a tax is a restriction when it is placed upon a trade directly and immediately may be admitted. But there is a difference between a tax which burdens a trader in this manner and a tax, which being general, is paid by tradesmen in common with others. The first is a levy from the trade by reason of its being trade, the other is levied from all, and tradesmen pay it because every one has to pay it. There is a vital difference between the two, viewed from the angle of freedom of trade and commerce. The first is an impost on trade as such, and may be said to restrict it; the second may burden the trader, but it is not a "restriction" of the trade. To refuse to draw such a distinction would mean that there is no taxing entry in Lists I and II which is not subject to Articles 301 and 304, however general the tax and however non-discriminatory its imposition. To bring all the taxes within the reach of Article 301 and thus to bring them also within the reach of Article 304 is to overlook the concept of a Federation, which allows freedom of action to the States, subject, however, to the needs of the unity of India. Just as unity cannot be allowed to be frittered away by insular action, the existence of separate States is not to be sacrificed by a fusion beyond what the Constitution envisages. No doubt, Part XIII ensures economic unity to India and combines the federating States into the larger State called India. The Constitution also permits independent powers of taxation. What the Constitution does not permit is that trade, commerce and intercourse should be rendered "unfree". Trade and commerce remain free even when general taxes are paid by tradesmen in common with non-tradesmen "

43. Hidyatullah, J. held that taxes which are imposed by the Act by Schedules II, III and IV operates restriction on trade and commerce directly. Hence, the provisions have to be held offending Article 301 and resort to the procedure prescribed by Article 304 (b) having not been taken, the Act is ultra vires to the Constitution of India.

PART III
SUBMISSIONS

44. The arguments on behalf of the petitioners, who have challenged various Entry Tax Legislations, have been led by Shri Harish Salve, learned senior counsel. For the petitioners, we have also heard several other eminent Senior Advocates and other counsel who have additionally made substantial submissions, however, to avoid repetition of submissions while referring to the submissions of other counsel we have not noted the submissions which have already been covered by Shri Harish Salve.

45. The arguments on behalf of different States have been led by Shri P.P. Rao and Shri Rakesh Dwivedi, Senior Advocates. Several other counsel have also made submissions, however, to avoid repetition, we have noted only those submissions which were not covered by Shri P.P. Rao and Shri Rakesh Dwivedi. Shri Mukul Rohatagi, learned Attorney General has also made his submissions.

46. Shri Harish Salve, learned senior counsel leading the arguments on behalf of the petitioner made elaborate submissions on various aspects of Part XIII of the Constitution of India. Shri Salve traced the legislative history of Part XIII of Constitution by referring to the
Government of India Act 1919 and Government of India Act, 1935. It is submitted by Shri Salve that a Tax commonly known as "Octroi" was enforced in 1901 even before the Government of India Act, 1935.

47. It is contended that Article 301 of the Constitution of India was originally framed as Draft Article 16 which was included in the Chapter of Fundamental Rights which clearly indicates that framers of the Constitution intended to guarantee freedom of trade, commerce and intercourse as a fundamental right. He has taken us to the discussion in the Constituent Assembly. He submitted that provisions of Article 304 Sub-clause (b) was thread-ware discussed and the constituent assembly consciously decided not to make any change in the scheme as delineated by Article 304 Sub-clause (b) proviso. In our Constitution we avoided American pattern which only declared rights, rather our constitution has a strict balance between powers granted to Parliament and State to frame law. It is contended that there is a clear federal slant in favour of Union which is clear from the scheme of the Constitution.

48. Shri Salve contended that tax legislations were also He submitted that textual reading of various articles in Part XIII indicate that framers of the Constitution clearly intended that Part XIII shall also operate on tax legislation. He contended that had tax legislation was not included in Part XIII there was no occasion for specific mention of tax in Article 304(a) and Article 306 [as it was before the Constitution (7th Amendment) Act 1956] of the Constitution of India. He, however, contended that the freedom from the tax law or any other law was guaranteed under the Article 301 only to the extent when the tax legislation or any other law
impeded trade, commerce and intercourse throughout the territory. He submitted that historically there were various tax barriers in different independent states prior to

enforcement of the Constitution and to remove the barriers, the freedom of trade, commerce and intercourse was included in Part XIII.

49. Referring to majority view in Atiabari case (supra) he contended that the tax laws are covered by Part XIII of the Constitution. He submitted that above majority view in Atiabari was not doubted by subsequent 7 Judges Bench in Automobile Transport (supra) . Shri Salve however submitted that various statutes regulating trade and commerce may not impede trade and commerce like laws pertaining to traffic rules. Taxes, regulatory in nature may not be hit by Article 301. However, it is contended that taxes which have effect directly and immediately on the trade, commerce and intercourse violates Article 301. He contended that Entry Tax under Entry 52 of List II of VIIth Schedule of the Constitution is one subject which directly impede Freedom of trade and commerce.

50. Answering Question No. 1, Shri Salve contends that in a set of circumstances non-discriminatory tax may violate Article 301. Shri Salve coming to incidental questions contended that taxation is an attribute of the sovereignty however differences lie in a case where legislative power is limited by Constitution. He contends that source of legislative power is Article 245 (1) which is "subject to the provisions of the Constitution". It is contended that express constitutional limitation is clearly laid down in Article 245 (1) , and the legislative powers have to be exercised by Parliament or State subject to the provisions of this Constitution. Article 246 is division of legislative powers between the Parliament and the State which shall always be subject to general limitation as contained in Article 245 Sub-article (1).

51. Answering to subsidiary Question No. 2, Shri Salve submits that Article 246 of the Constitution recognizes the sovereign powers of the State to make laws including laws levying taxes on such matters elaborated in List II of VIIth Schedule.

52. Answering to subsidiary Question No. 3, he contends that powers to make laws and levying of taxes reserved in favour of the State under Article 246 read with List II of VIIth Schedule are subject to Part XIII of the Constitution.

53. Replying to the incidental Question 4, he contends that freedom guaranteed under Article 301 is a limitation envisaged in the Constitutional Scheme and the States are free to legislate as contemplated by Article 301 and the limitation contained in 304(b) is with larger object to achieve the economic unity of the country. There is no question of surrender of sovereign power by the State but legislative power can always be limited by the express provision of the Constitution. Referring to provision of Article 285 and 286 of the Constitution, Shri Salve contended that those are provisions of the Constitution which work as limitation on the legislative power of the State. There are various provisions in the Constitution which work as limitation on the legislative power of the state and limitation envisaged by different provisions of the Constitution being part of the Constitutional scheme it cannot be said that States are denuded with their sovereign power.

54. Answering to incidental Question No. 5 and 6 Shri Salve contends that taxes are

always presumed to be in public interest, but however, the levy of taxes are restrictions imposed in public interest is a question which has be decided by considering the individual legislation. Levy of taxes may or may not be reasonable restrictions.

55. Answering to incidental Question No. 7, Shri Salve contends that under Article 304(b) a State is empowered to legislate imposing reasonable restriction on the freedom of trade and commerce and intercourse in the public interest subject to obtaining previous sanction of the President. The State thus is free to legislate with one limitation that the Bill is to be moved with the previous sanction of the President. State autonomy is in no manner affected. The judicial review being a basic structure of the Constitution, the Court is fully empowered to examine whether a law framed by State complies with Part XIII of the Constitution. He submits that there is no question of affecting separation of powers merely on the ground that State Legislation can be judicially scrutinized regarding compliance of Part XIII of the Constitution.

56. Answering to the subsidiary Question No. 9, Shri Salve contends that Compensatory Tax Theory is not consistent with the language implied in Article 301. He submits that Compensatory Tax Theory is a theory which has been judicially evolved in Automobile Transport case (supra). However, Compensatory Tax Theory is not consistent with the Scheme of Part XIII of the Constitution nor it can be said that if a tax is compensatory, it goes beyond the purview of Article 301.

57. Shri Salve answering Question Nos.2 and 3 contends that tax which is said to be compensatory may also fall foul of Article 301. It is contended that compensatory theory has not worked well and it has created more problem than solved. All States have picked up compensatory theory and have made statements in the statute that Entry Tax collected shall be spent for the benefit of the trader. The statutes have only made facial compliance. The test as approved by Automobile Transport that is "direct and immediate effect" has to be applied to find out as to whether a particular statute impedes the trade. Compensatory tax is mixing of two constitutional concepts namely tax and fee.

58. Coming to Question No.4, Shri Salve contends that Article 304(a) is not a source of power of the statute, rather it is one of the exceptions carved out to Article 301 where the State can legislate. He further submits that Article 304 sub-clause (a) only covers inter-State trade and does not cover intra-State trade. The provision of Article 304 sub-clause (b) proviso was limitation which was consciously put in the larger interest by the economic unity of India. The President normally does not veto any tax proposed by the State under Article 304(b) nor any such instances before the Court has come, to come the conclusion that a State's autonomy in legislation has in any manner affected. Power given under Article 304(b) proviso is the power to oversee the restrictions put by the State viz larger object and purpose. Although Article 304(b) uses the words restrictions on the freedom of trade, commerce or intercourse, the said restrictions may also include restriction by way of taxing statute. He submits that movement of goods from one local area of a State to local area of another State does not fall under Article 304(a) but it falls under Article 304(b).

59. Justice Hidyatullah's views in Automobile Transport case be accepted that tax to be compensatory is not the way out from Article 301. He further submitted that any tax viz. by its legal structure and practical effect may impede the trade and have a immediate and direct effect. Shri Salve also posed a question as to whether goods imported from other countries entering into a local area are liable to pay Entry Tax under legislation covered by Entry 52 List II ? He submits that in the above case the Entry Tax, if any, has to be justified under Article 304(b). Goods not covered by Article 304(a) should satisfy Article 304(b). The pre-condition permitting Entry Tax under Article 304(a) is that similar goods of that very State have to be taxed first.

60. Shri Salve in support of his submissions has also placed reliance on various judgments of this Court as well as judgments of the Australian High Court, Privy Council and US Supreme Court which shall be referred to while considering the submissions in detail.

61. Shri A.K.Ganguly, learned senior counsel, submitted at very outset that reference to this larger bench to reconsider the decisions in Atiabari and Automobile is not warranted.

62. Relying on Constitution Bench judgment in *Keshav Mills case(Keshav Mills Vs. Commissioner of Income Tax*[12] he submits that when this court decides questions of law which are binding under Article 141 on all courts, it must be constant endeavor and concern of this court to introduce and maintain an element of certainty and continuity. In the interpretation of law in the continuity, he submits that review excise is to be undertaken only when earlier decision was clearly erroneous. The Constitution Bench in Jindal Stainless Ltd(supra) without any appropriate reason has made a reference for constituting a larger bench for reconsideration of the judgment of this Court in Atiabari Tea Co. and Automobile Transport, Rajasthan ltd.(supra).

63. He further submitted that reliance on observation of Mathew J *in G.K.Krishnan Vs. State of Tamil Nadu*[13] which was only an Obiter could not have been basis for making a reference to larger bench.

64. The compensatory theory as evolved by Automobile Transport has worked well and need not be touched. However, he submits that there should be broad co-relation between the compensatory tax and facilities extended to traders.

65. Referring to Article 304(a) and 304(b), Shri Ganguly submits that both the above sub-clauses of Article 304 are gateway to go out from the clutches of Article 301. Article 304 (b) is a federal check and has come due to the historical reasons. Sh. Ganguly has also ref-erred to Sarkaria Commission's Report' which rejected the demand of certain State for omission of Article 304(b) from the Constitution. He further submitted that the procedure on referring to State bills to the President as contemplated by Article 304(b) ensures that the obligation of India that it owes international community are met.

66. Shri T.R. Andhyarujina, learned senior counsel submits that sub-clauses (a) and

(b) of Article 304 are not disjunctive. Hence, even if a State law is not discriminatory under Article 304(a), it is still required to comply with the requirement of Article 304(b).

67. Shri Andhyarujina submitted that one of the tests to be applied for finding out as to whether the tax poses any tariff barrier is that when the tax is more than the value of the goods, it is a tariff barrier which is hit by Article 301.

68. Shri S.K. Bagaria, learned senior counsel submits that under Article 304(a) tax can be imposed on inter-State trade, whereas when goods move from one local area to other local area within a State, tax can be covered only under Article 304(b). He submits that the question whether a tax is a tariff barrier or not cannot be decided quantitatively but can be decided qualitatively.

69. Shri Bagaria submits that he appears for Steel Authority of India in some cases. He stated that Bhilai is maintained by Steel Authority of India and all expenditures for maintaining it and all civic amenities in township are being provided by Steel Authority of India. In township in Bhilai, there are no facilities being provided by the State. He referred to the details of expenditures spent by Steel Authority of India during the years 1995-96 to 2008-2009. He submits that the State Government do not provide any facility and expenditure currently is more than 200 crores every year. He submits that the State not providing municipal/civil facilities is not entitled to levy Entry Tax as a tax compensatory in nature.

70. Shri Arvind P. Datar, learned senior counsel contends that the concept of compensatory tax as judicially evolved in Automobile Transport has to go. He submits that concept of compensatory tax is anomalous, tax being compulsory extraction and all taxes are to be utilized for public good. He suggests that proper test is whether there is 'Appreciable Adverse Effect' on trade and commerce, which can be determined by the manner in which trade and commerce was carried out before the impugned law and the manner in which it is carried on after the impugned enactment. He submits that the restrictions as referred to in Part XIII can be of multiple applications. They can be fiscal, environmental, commercial and in the form of labour law. Entry Tax cannot be levied on entry of the goods in the State. Referring to the word 'and' used in Article 304(a) and 304(b), he submits that 'and' be interpreted as joint and several. He submits that a non-discriminatory tax which does not violate Article 304(a) may still violate Article 304(b) if it has discriminatory procedural provisions.

71. The ultimate effect on trade and commerce has to be seen even if it is not direct and immediate. No State is an Island, law in one State has its effect on other States also. The State is not the final Judge of restriction which is contained in the statute framed by it. Hence, Presidential assent is required. There are various provisions in the Constitution like Article 31A, 200, 201, 213, 254, 361 and Sixth Schedule where Presidential assent is required. In Article 204, 255, 304 and 349 the Presidential sanction is required.

72. Mr. V. Laxmikumaran, learned senior counsel, contends that free trade, commerce

and intercourse means free movement of goods, services, persons and capital(investment). Article 304(a) relates to tax on goods and Article 304(b) relates to other taxes and measures. Article 304(a) mandates that a state can impose tax on goods imported from other states less than or equal to taxes imposed on like-goods manufactured or produced in that state. The tax referred to in Article 304(a) should be read with general exceptions, set-off, credit etc available to goods as manufactured or produced in that state. Learned counsel has also referred to General Agreement of Tariff and Trade, 1947 (GATT, 1947) of which India is a founding member. The whole purpose of GATT, 1947 was to encourage free trade among the GATT members by eliminating tariff and non-tariff barriers. Learned counsel further submitted that even if a tax levied by the state is non-discriminatory, it may impede right guaranteed under Article 301. Learned counsel supports his submission by giving an illustration. In a state laptops and I-pads are manufactured. A State which wants to encourage the manufacturing of laptop has put only 0.5 % tax on laptop but has imposed 50 % tax on I-pad with an intent to discourage the import of I-pad. The said state's above action may not be violating Article 304(a), however, procedure prescribed in Article304(b) has to be applied with. Another example where state, although, complies with Article 304(a) but violates Article 304(b) given by learned counsel is; the State of Maharashtra imposed Entry Tax exactly equal to the local taxes but puts conditions: (i) All goods to Maharashtra should enter only through Balharshah; (ii)Finished goods manufactured in Maharashtra should have at least 75 % local content. Learned counsel thus contends that while imposing tax by the state both the Articles 304(a) and 304(b) have to be complied with.

73. Shri Jagdeep Dhankar, learned senior counsel, contends that Part XIII of the Constitution is a basic structure of the Constitution. He contends that nothing can be more basic than economic unity of the country. Learned senior counsel submitted that compensatory theory cannot be supported which shall only lead to right to litigate. Words "tax" and "restrictions" are employed in Part XIII separately. These are not interchangeable and there can be no component of tax in the restrictions adverted in Part XIII. He submitted that the Preamble of the Constitution is to be relied and looked into while interpreting the constitutional question.

74. Shri Ravindra Srivastava, learned senior counsel, submitted that as a concept compensatory tax cannot be supported. Compensatory tax is a misnomer and it was unnecessary. He submitted that taxes which have direct and immediate effect are hit by Article 301. Relying on opinion of Justice Hidayatullah in Automobile case, he contended that if a tax is imposed solely on the basis of movement of goods, it is violative of Article 301, however, if it is a common burden it does not violate Article 301. Elaborating the concept of tax he submitted that there are two concepts for imposition of tax that are (i) "Ability-to-Pay Principle" and (ii) "Benefit Principle". He submitted that examination of each legislation / tax legislation is necessary having regard to the provisions of a particular Act to arrive at conclusion whether the tax amounts to restriction and if so, whether it is saved under Article 304. Learned counsel for the petitioner referring to SLP(C) No. 23990 of 2009 Steel Authority of India Ltd. contends that the quantum of Entry Tax varies from 0.5% to 5 0% which clearly demonstrate that it is an impediment in the trade and hit by Article 301.

75. Shri N. Venkataraman, learned senior counsel, submits that Constitution of India is designed in such a way that State's power to legislate is restricted in many ways. Legislative power in different entries of List II are subject to legislative power of the Union under List I. He has referred to power under Entry 54 List II, which is made subject to the power of the Union under Entry 92A, List I.

76. He further submits that Article 254 clarifies State's power of taxation. Further, Article 286 sub-clause (3)(a) and (3)(b) restricts the State's power of taxation. Similarly, Part XIII is restriction on the State legislative power. Articles 302 to 304 also contain various restrictions on the powers of Parliament and the States in making laws.

77. Referring to the Constitution (One Hundred and Twenty Second Amendment)Bill, 2014 he submits that Union and State have reached to a conversion where both are entitled to legislate. He has referred to Article 246A of the Bill. There is consensus between Union and the States to abolish all the taxes including Entry Tax and is now to be subsumed in two taxes that is services and goods. The above Bill indicates that we have now moved to real economic unity.

78. Shri Dhruv Agrawal, learned senior counsel, submits that freedom of trade, commerce and intercourse is a basic structure of the Constitution. Referring to the Preamble of the Constitution learned senior counsel submits that the unity and integrity of the Nation is a basic feature of the constitutional structure. Part XIII has been inserted in the Constitution to achieve the economic unity of the country. Shri Agrawal has also referred to the Constituent Assembly Debates.

79. Shri Gopal Jain, learned senior counsel appearing for the appellants in C.A.No.3453 of 2002 submits that the Constitutional Scheme is a well crafted architecture which must be read holistically. A Constitutional provision has to be interpreted from the reading of the whole of the Constitution to ensure that overall objectives are achieved.

80. Shri Dilip Tandon, learned counsel referring to judgment of this Court in Automobile Transport contended that the opinion expressed by Justice Hidayatullah be accepted. Shri Tandon submitted that he adopts the arguments of Shri Harish Salve and Shri Ravindra Srivastava, learned senior counsel.

81. Smt. Suruchi Aggarwal, learned counsel submitted that Article 301 is a restriction on the legislative power of the State. Referring to Article 304(a) she contends that Article 304(a) is resorted since it is presumed that the law would be a restriction under Article 301. She referring to provisions of the Haryana Local Area Development Tax Act, 2000 contends that manner of collecting Entry Tax violates Article 286. She submits that liability and pay-ability of Entry Tax is different which is nothing but a discrimination.

82. Shri Tushar Mehta, learned Additional Solicitor General appearing on behalf of the Indian Oil Corporation submits that judgment in Automobile Transport case has held the

field since 1964 and need not be disturbed. He submits that Entry Tax would invariably impede inter-State trade. Hence,they must, therefore, pass the test of clause (a) and clause (b) cumulatively. Article 304(a) does not apply to goods imported into India and not manufactured or produced in any other State.

83. Coming to the Entry Tax levied to Indian Oil Corporation, Shri Mehta submits that Indian Oil Corporation transports crude oil from its own underground pipelines from A to B State. The States are not manufacturing crude oil but they are still demanding Entry Tax. The States where Indian Oil Corporation has its own refinery have levied the Entry Tax. Referring to Mathura refinery situated in the State of U.P., he contends that the State of U.P. does not produce any crude oil hence, Entry Tax cannot be demanded under Article 304(a). Demand of Entry Tax is clearly discriminatory. Learned ASG, however, fairly conceded that there is no pleading to the above effect taken before the High Court by the Indian Oil Corporation. He further submits that during the course of the submission he will bring on record necessary pleading on behalf of the Indian Oil Corporation in the appeal before this Court.

84. Shri Mukul Rohatgi, learned Attorney General has made his submissions. Shri Rohatgi submitted that power to tax in List II is Sovereign and Plenary Power which can be curtailed only by express provisions of the Constitution of India. Part XIII of the Constitution does not deal generally with tax except, in so far as, it makes reference under Article 304(a). Entire ethos of Part XIII of the Constitution is a discrimination and that too a deliberate discrimination. Article 304(a) and Article 304(b) are disjunctive. Article 304(a) applies to taxes whereas Article 304(b) applies to non-fiscal measures. Taxes are assumed to be in public interest and are reasonable. Under sub-clause(b) of Article 304, President cannot be made super adjudicator. India is a Federation and the sovereign power of the State cannot be subjected to an implied control.

85. Shri Rohatgi submitted that federal structure is a basic feature of our Constitution. Though India is described as a Quasi-Federal or a Federation with strong central bias, this does not militate from the fact that states are sovereign in the field which is left to them under the Constitution. Shri Rohatgi submitted that Constitution is to be read as a whole. Part XIII of the Constitution must be interpreted with reference to other parts of the Constitution, including Part III of the Constitution, Part XII and Article 38 and Article 39 of the Directive Principles of State Policy.

86. Referring to Article 245 and Article 246 learned Attorney General submitted that Article 245 is the source of legislative power, whereas, Article 246 provides for distribution of legislative functions between the Union and the states. He submitted that Article 245 begins with the express provision 'subjects to the provisions of this Constitution' which phrase has also to be read under Article 246. Learned Attorney General submitted that GST Bill having been passed on 3rd August, 2016 in the Rajya Sabha, after ratification by the states, the only issue relevant in the present batch of cases shall be with regard to Entry Tax as was enforced in past. Entry 52 List II providing for Entry Tax shall stand deleted after Bill becomes a Law. He submitted that passing of the GST Bill indicates that we have proceeded to economic unity.

87. What is prohibited by Part XIII is pernicious or hostile discrimination by or between States. Freedom of trade, commerce and intercourse is not absolute as is evident from various provisions of Part XIII of the Constitution. Restrictions on the power of Parliament and the State Legislature as referred to in Article 303, is confined to the powers under the entries relating to trade and commerce only. The restrictions thus do not include tax. Entries relating to tax in List II that is Entries 46 to 63 were never contemplated under Article 303.

88. Part XIII deals with "Restrictions" and "Taxes" differently. A clear dichotomy was intended between taxes on the one hand and restrictions on the other hand. Article 302 does not refer to tax, whereas, concept of tax is well known to the Constitution and has been used in Part XII in several articles. Article 304(b) does not refer to taxes, word "Tax" is found in Article 304(a) which cannot be imported in Article 304(b). It is obvious that reference under Article 304(b) is to "restrictions" other than tax. Coming to the Compensatory Tax learned Attorney General submits that since we are at the fag end of Entry Tax Regime, it shall be appropriate to stick with Compensatory Tax Theory.

89. Shri P.P.Rao, learned senior counsel, has made his submissions on behalf of States of Madhya Pradesh and Andhra Pradesh. Shri Rao submits that it is well settled that a Constitution must not be construed in any narrow and pedantic sense and the construction which is most beneficial to the widest possible amplitude of its power must be adopted. He further submits that no entry in the VIIth Schedule of the Constitution should be so read as to rob the entry of its content. He submits that in a federal system of governance, the power to levy tax is an inherent attribute of a sovereign function of a State.

90. Clause(a) and Clause(b) of Article 304 are mutually exclusive. Taxes are covered in Clause(a) whereas restrictions other than taxes are covered in Clause(b). It is only discriminatory taxes vis-a-vis goods of other States and Union Territories which restrict the freedom of trade in Article 301 and all other taxes do not obstruct the said freedom. The federal character of the Constitution is a part of the basic structure. The power to levy Entry tax under Entry 52 of the State is not subject to any restriction.

91. The framers of the Constitution never intended that the exclusive power of State to levy tax on the entry of goods be subject to requirement of obtaining the previous sanction of the President mention in proviso of Article 304(b). For imposing a tax on goods coming from other State, it is not essential that similar goods produced and manufactured in the State should be taxed. The only restriction is that the tax shall not be discriminatory. Taxes per se are not restrictions. Only taxes which suffer from the vice of protectionist discrimination vis-a-vis goods imported from other States and Union Territories interfere with the freedom of trade, commerce and intercourse mentioned in Article 301. The whole scheme of Part XIII is that the discriminatory tax interferes with the trade, commerce and intercourse. A Non-discriminatory tax does not interfere with the freedom of trade, commerce and intercourse.

92. The framers of the Constitution intended minimum inroads in power of taxation in

the State. Learned Counsel has referred to various passages from Atiabari and Automobile Transport case. Referring to observations made by Gajendragadkar J. that "how a tax can be levied on internal goods is, however, provided by Article 304(b)....", he submits that the above observations cannot be said to laying down a law since the issue never arose in the above case. He submits that the above observations are not the ratio decidendi and do not constitute a precedent. Shri Rao further submits that the concept of compensatory taxes as laid down in Automobile Transport case is alien to the Constitution and is unsustainable. The discrimination which is referred to in Article 304(a) is hostile discrimination.

93. Shri Shyam Divan, learned senior counsel has appeared on behalf of the State of Haryana. Shri Divan submitted that the core constitutional value of Part XIII of the Constitution is creating an economic unity across India.
94. Article 302 - 305 are in the nature of exceptions to Article 301. Article 304 being an exception to Article 301 ought to be read, narrowly. He gives an example of protectionist barrier i. e. a State wants to protect the agriculture of its own State for which, a restriction is imposed that all agriculture-based industries shall take raw-materials only from within the State. He submitted that this is an example of 'trade barrier' by a protectionist measure. Article 304(a) has a limited scope and ambit.

95. Power both in (a) and (b) can be exercised or either (a) or (b) can be exercised or none can be exercised. There is no necessity that power under 304(a) and 304(b) are to be exercised necessarily together. Shri Divan further submitted that there is difference between differentiation and discrimination. Lastly, he contended that in terms of 2 0 00 Act and 2 00 8 Act, the entire tax collected by the State under the respective statute would be utilized for the development of trade, commerce and industry in the state.

96. Shri Rakesh Dwivedi, learned senior counsel has advanced his submissions on behalf of the States of Orissa, Bihar, Madhya Pradesh, Tamil Nadu and West Bengal. Shri Dwivedi submits that petitioners' arguments are that the judgments of this Court in Atiabari and Automobile Transport be not revisited. Shri Dwivedi submits that there were fundamental errors in both the above decisions. He submits that following fundamental errors are, in the above two cases :

> "I. (i) Both the cases confined on economic unity as sole factor for trade, commerce and intercourse;
>
> (ii) whereas, a perusal of various provisions of the Constitution indicates that economic unity depends on the continuity of political unit; and
>
> (iii)Territory of Union is nothing but States and Union Territories.
>
> II. This Court completely ignored the concept of 'Federalism' which has now been accepted as basic feature of the Constitution after judgment of this Court in Kesavanand Bharati's case (supra).

III. Each of their Lordships in aforesaid cases draw support from various Australian and US cases, whereas, there is no comparison of Part XIII with Australian and US Constitution. In US, States have no power to legislate except law and order, good governance and peace. These differences in our Constitution and the Constitutions of Australia and US have been completely overlooked. Law as developed in Australia and US i.e. "direct and immediate effect" for finding out impediment in the trade has now been given a go by both by Australian and US Courts. Both the Courts have moved to a "discriminatory" test.

IV. In both the above cases one does not find any detailed consideration of history of Part XIII as emerging from Constituent Assembly Debates specifically regarding economic unity.

V. All the judgments considered history from the point view of Section 297 of the Government of India Act, 1935 and they conclude that it was all about trade barriers.
VI. In Part XIII "subject to the provision of this Part" was read as "subject to only the provisions of this Part".

VII. This Court in both the above cases did not examine fully the nature of taxation.

(i) Tax is an incident of sovereignty.

(ii) Tax is necessary for carrying out the welfare activities by the State.

(iii)Tax can neither be imposed by implication nor taxing power can be limited by implication.

(iv) The tax can only be for a public purpose which has its roots in Article 265 of the Constitution.

(v) Taxing powers of the State and the Union are mutually exclusive except to the extent as mentioned in the respective Entries in List II and any other provision of Constitution. Even Parliament cannot restrict the taxing power of a State flowing from Entries of List II.

(vi) Article 289(2) – Even, a State doing business is not exempted from tax. Trade and business never were treated as exempted from tax."

97. Shri Dwivedi further submits that tax per se is not covered by Part XIII. Tax is not a trade barrier and unless it is discriminatory it shall not be treated as a barrier. The right of trade, commerce and intercourse cannot be exalted as

98. Shri Dwivedi submits that "Free" in Article 301 does not mean free from tax. State's power, despite the limited width of its field is plenary in nature. Wherever,exemption

from taxes were contemplated they were expressly provided as under Articles 285, 287,288 and 289. Referring to Part III of the Constitution, he submits that Part III does not confer freedom from taxation. A fortiori, Article 301, which is not a fundamental right cannot result in conferring a freedom of trade, commerce and intercourse from tax. He submits that there are inherent limitations on taxation by a State. The imposition of tax is always for public purpose and various inherent limitations in taxation operate as limitation in taking any discriminatory or any other unreasonable measures. Article 302 to 304 are not exceptions or provisos to Article 301. Coming to Article 304, it is submitted that both clauses (a)and (b) of Article 304 are disjunctive and freedom of trade, commerce and intercourse is subject to them. The word 'and' normally is conjunctive but it is often construed as disjunctive where the legislative intent as gathered from the words of the provision and the context indicate that it was used in the disjunctive sense. Learned counsel elaborating his submissions contends that Article 304 relates to inter-State trade which is apparent from marginal heading.

99. He submits that by use of the words "within that State" alongwith "with", it is clearly meant that the words "within that State" was used in relation to inter-State trade. He submits that inter-State does not come to an end after the entering into the State. It may have some effect and operation within the State also.

100. Shri Dwivedi further submits that the Presidential Sanction as contemplated in Article 304(b) proviso was due to the reason that Article 304 is related to inter-State trade and it falls in Entry 42 List I. He submits that justification for requirement of obtaining Presidential sanction in proviso to Article 304(b) is the restriction which may touch the inter-State trade, which is not within the legislative power of the State.

101. Learned counsel further submits that mere excessiveness of rate of taxes does not v-iolate Article 14 and 19 as has been held by this Court in a large number of cases which principle has also to be applied for examining the challenge that high quantum of tax impedes the trade.

102. Shri Dwivedi further submits that in the event submission is not accepted that tax is out of Article 301, alternatively tax simpliciter is outside the Article 301. He submits that this Court held in large number of cases that in the context of Part III of the Constitution tax per se does not violate the fundamental rights. Tax simplicitor being out of reach of Article 301 only those taxes which substantially destroy\impede the Trade can fall foul to Article 301. He contends that framers of the Constitution were conscious that freedom of Trade and Commerce, and Intercourse does not include freedom from tax. The tax can become a barrier if imposed preferentially and discriminately. That is why, they separately provided for restricting the taxing power under Article 304(a). He, however, submits that there shall be an onerous burden on the petitioner to prove that the tax is an impediment.

103. Coming to the Australian cases relied by this Court in Atiabari Tea Company Ltd and Automobiles, he submits that 'direct and immediate effect test' which was propounded in above two cases based on earlier cases of Australian High Court, including James Vs. Commonwealth (1936) 55 CLR (1), a 7Judges Bench of High

Court of Australia in Cole Vs. Whitfield and Another reiterated in (1988)78 ALR (41) have rejected the 'direct immediate effect test' and has preferred to discriminatory test. The 7Judges Bench held that the various interpretations of Section 92 which have attracted any support over the years only the Fiscal Charges Theory and the Anti-Discrimination Interpretation have been favoured.

104. Coming to cases of U.S. Supreme Court, learned counsel submits that trend of cases indicates that effort is on shifting the test of discrimination. He submits that in the Complete Auto Transit Vs. Charles R Brady 430 U.S. 274, it was held that it was not the purpose of commerce clause to relieve those engaged in interstate commerce from their just share of State tax burden, even though, it increases the cost of doing business.

105. Coming to Entry 52 List II, learned counsel contends that, even if, we apply the Test laid down in the Automobile, the goods coming from other states come to repose in a local area and the Entry Tax is not tax on border or a tax on movement of goods. The legislative scheme of different states for which he appears indicates that no tax is collected at border and only a transit pass is given and the Entry Tax is to be paid based on self-assessment. Article 304(a) protects this type of Entry Tax.

106. Shri Dinesh Dwivedi, learned senior counsel has made his submissions on behalf of the State of U. P. Shri Dwivedi, answering the Question No. 1 submits that levy of Non-Discriminatory Tax per se does not constitute infraction of Article 301. He further submits that the question regarding the Compensatory Tax need not be answered since compensatory nature of tax is outside the Constitutional Scheme and has to be struck down. Learned counsel submits that the Constitution is a living organism and each part of it throws light on other part of the Constitution. Every part of the Constitution has to be looked into and no part has to be interpreted de horse the other provisions of the Constitution.

107. Shri V.Giri, learned senior counsel has appeared on behalf of the State of Kerala. He submits that 383 Appeals have been filed by the State of Kerala against the Judgment of Kerala High Court striking down the Kerala Tax On Entry Of Goods Into Local Areas Act, 1994 . He submits that the High Court has struck down the Act on the ground that tax imposed is not Compensatory and it violates Article 301 of the Constitution.

108. Shri Giri submits that at the time of payment of Sales Tax, the credit of Entry Tax is to be given. He submits that with regard to goods produced and manufactured within the State and manufactured from outside the State the tax burden is almost similar and tax being non-discriminatory does not fall foul to Article 301.

109. Shri Ajit Kumar Sinha, learned senior counsel has made his submissions on behalf of State of Jharkhand. Shri Sinha submits that the Bihar Entry Tax Act, 1993, as enacted by State of Bihar was adopted by State of Jharkhand after reorganization of the State in the year 2000.

110. He submits that although Patna High Court upheld the Act 1993 but Jharkhand

High Court has struck down the enactment. One of the grounds taken by Jharkhand is that for amendments made by the State of Jharkhand in the 1993 Act, no Presidential Sanction was obtained. He submits that for carrying out the amendments, no Presidential sanction was required.

111. Shri Jugal Kishore Gilda, learned Advocate General of the State of Chhattisgarh has addressed his submissions on behalf of State of Chhattisgarh. Learned Advocate General has at the very outset stated that he adopts the submission made by Sh. P.P.Rao and Shri Rakesh Dwiwedi.

112. Shri Dev Dutt Kamath, learned Additional Advocate General has raised submissions on behalf of State of Karnataka. He submits that Constitution validity of Karnataka(Tax on entry of goods) Act 1979 has already been upheld by this Court in *'State of Karnataka Vs. Hansa Corporation[14]'.*

113. He submits that in fact in three Civil Appeals being Civil Appeal No. 4476 of 2000, SLP(Civil) No. 16786-16788 of 2009 and SLP(Civil) No. 12789 of 2009, the questions referred to this larger Bench do not arise and he adopts the submissions made by Sh. P.P.Rao and Sh. Rakesh Dwiwedi.

114. Shri Saurabh Shyam Shamshery, learned Additional Advocate General has appeared for the State of Rajasthan. He submits that Rajasthan Tax on Entry Of Goods Into Local Areas Act, 1999 had been upheld against which Special Leave Petition had been filed by Assesses in the year 2001. Subsequently, after the judgment of this Court in Jindal Stainless Steel (2) division Bench dated 21st August, 2007, declared Act 1999 as 'ultra vires' to Article 301 against which judgment the appeal has been filed by the State which is pending.

115 . Shri Harish Salve, learned senior counsel in rejoinder to the submissions made by learned Attorney General, learned counsel appearing for different States and other parties, contends that submission that taxing power is some sort of sovereignty, is not a correct preposition.

116. The earlier view that tax is out of Part III has been reversed. When it is said that Part XIII includes tax no one is asking to emasculate State's sovereignty. What is prohibited by Part XIII is the impediment to trade and commerce, 'direct and immediate'. The sanction of President, as contemplated in Article 304 (b) does not mean that such sanction affects the sovereignty of the State. The proviso to 304(b) operates in a very narrow field.

117. Shri Salve further contends that Sinha, J developed Tariff Wall Theory, as impediment of trade since he was of the opinion that taxing legislation can not be challenged under Part III. Shri Salve referring to judgment of this Court in K*. K. Kochuni and Others Vs. State of Madras and Others, and K. T. Moopil Nair Vs. State of Kerala and Others[16]*, and few subsequent cases contends that taxing statute can very well be challenged on the ground of violating provisions of Part III of the Constitution. He submits that when taxing statute can be challenged under Part III, there is no inhibition from entertaining the challenge to a taxing statute for violation of Part XIII.

118. Shri Salve to point out difference between challenge under Article 19 and Article 301, gives an example. An oil company carrying out trade in entire country is faced with an exorbitant rate of Entry Tax in one State, the company cannot contend that freedom to carry out its profession as guaranteed under Article 19(1)(g) have been affected. Whereas a trader carrying on business in that State may be affected by an exorbitant tax and can contend that the exorbitant tax impedes the trade under Article 301.

119. Shri Salve submits that entry tax legislations of different States in the country can be characterized in different groups. He submits that one group of the legislations which consists of States of Tamil Nadu, Andhra Pradesh, Kerala is the legislation in which Entry Tax is imposed only on the goods which are imported from different State and no tax is imposed on locally produced/manufactured goods which is clearly discriminatory and violative of Article 304(a). He submits that second category of legislation consists of cases where in the enactment facially Entry Tax is imposed on the goods i.e. goods coming from out of State and local goods, but legislation contains a devise by which there is set-off\exemptions to the local goods which result in non-imposition of Entry Tax on the local goods, leading to another kind of discrimination which also violates Article 304(a). In the second category, State of Assam, Bihar, Jharkhand and few other States are included. There is third category of legislation where discrimination is practiced in several manners, for example, manufacturers are given set-off of Entry Tax on raw-materials like State of Orissa and Madhya Pradesh. There is fourth category of legislation where Entry Tax is imposed by creating a special area like State of Chhattisgarh.

120. Shri Salve contends that the submission raised on behalf of the States that question of discrimination under Article 304(a) is to be decided based upon the totality of burden of taxes and not the impact of a particular tax, is contrary to the plain language of Article 304(a) and would defeat the underlying object of Part XIII of the Constitution. Shri Salve further submits that Article 304(a) has two parts. Under first part of the Act 'State by law may impose on goods imported from other States, any tax to which similar goods manufactured or produced in that State are subject.' He submits that the second part provides for non-discrimination, which is indicated by words 'as not to discriminate'.

121. Lastly, Shri Salve replying to the submission of unjust enrichment contends that presumption that tax has been passed on is a rebutable presumption and whether tax has been passed or not is a question of fact and has to be considered by assessing authorities. He has also referred to judgment of this Court reported in *Godfrey Phillips India Ltd Vs. State of U.P*[18]*.* With regard to capital goods he contends that there cannot be passing on of any tax.

122. Shri A. K. Ganguly, learned senior counsel, making his submission in rejoinder contends that Constitutional history and Debates of the Constituent Assembly clearly indicates that Part XIII of the Constitution contemplated taxation to be a 'restriction' on the freedom of trade, commerce and intercourse and restrictions were permitted only to a limited exemption in the form of Article 302 – 306. Coming to Entry 52 list II, Shri A. K.

Ganguly submits that contemplated entry of goods into a local area, the framers of the Constitution were well aware of the State boundaries and did not deliberately choose entry into a State boundary. Entry 52 does not contemplate State as a unit. Incidence of levy is different from provisions relating to machinery to collect Entry Tax. Coming to Article 304(a), Shri Ganguly submits that provisions contemplate fulfillment of two conditions i.e. similar goods manufactured and produced in the State are subject to tax and further non-discriminatory taxes between the imported goods and the local goods. He further contends that other varieties of taxes not covered under 304(a) shall fall in 304(b).

123. Shri S. K. Bagaria, Shri Arvind P. Datar, Sri Ravindra Srivastava, Sri B. Laxmikumaran and Shri N. Venkataraman have also made their submissions in rejoinder.

124. Shri S. K. Bagaria, learned senior counsel, in his rejoinder submits that Article 304(a) has two conditions. He further submits that Entry 92(a) and 92(b) of List II cover the entire interstate trade and all facets of interstate movement.

125. Shri Arvind P. Datar, learned senior counsel, in his submissions reiterated that tax laws per se are not outside the purview of Part XIII. He further contends that Article 304(b) includes taxation. He submits that Article 304(a) refers to goods alone whereas taxes can be levied on persons, activities and things also. Article 304(a) shall not cover other parts of the taxes which necessarily has to go under Article 304(b). Entry Tax only on the goods imported from outside States and not levying them on entry into local areas from within the State is not permissible. Such taxes are violative of Entry 52 List II which permits Entry Tax only on entry into "local areas". Article 304(b) could also include taxes when rate of tax is same but there were other features which are restrictions. High rate of tax may not militate Article 19(1)(g) but it may violate Article 304(b). He submits that the question of tax barrier, as propounded in Atiabari has to be left to case to case. Restrictions contemplated under Part XIII can both be fiscal and non-fiscal. As on date 42 per cent of taxes of Union go to the State.

126. Coming to Video Electronics, learned counsel submits that if the object of a State is economic development, the State cannot levy different taxes with regard to imported goods and local goods, the State is free to give subsidies, and other assistance to any kind of industry but providing for discriminatory taxes in the name of economic development is in the teeth of Article 304(a). Any discrimination between local goods and imported goods is per se hostile. Coming to question of unjust enrichment, learned counsel submits that the issue has to be left to be considered by the assessing authorities. He submits that the States have different laws and facts which in each case are different and have to be examined for applying the theory of unjust enrichment. Learned counsel submits that in the event of this Court overruling Atiabari and Automobile today, overruling of the judgments has to be prospective so that position regarding tax settled already be not disturbed. Learned counsel has also referred to certain interim orders passed by this Court wherein it was specifically mentioned that State shall not be entitled to press unjust enrichment. He submits that any amount deposited under the Court's order is not an unjust enrichment.

127. Shri B. Laxmikumaran, learned senior counsel in his rejoinder reiterates that tax per se is covered under Article 301. Referring to Article 304(a),learned counsel submits that same tax is to be levied when the goods enter into the local areas from the other States and the local goods within the States. Equalising the total quantum of the Entry Tax levied on imported goods and some other local taxes within the States which is not in the nature of Entry Tax, is not permissible. Various parameters are to be looked into for the purposes of understanding discrimination. He further contends that Article 304(b) can cover tax law in addition to other law.

128. Shri N. Venkataraman,learned senior counsel in his rejoinder contends that legislative powers of both the Union and the States are subject to the provisions of the Constitution including limits thereupon and enacted therein.

12 9. In the end, we have again heard Shri P. P. Rao and Shri Rakesh Dwivedi in reply to some additional submissions made in rejoinder.

PART IV
A. LEGISLATIVE HISTORY AND DEBATES IN CONSTITUENT ASSEMBLY ON FREEDOM OF TRADE, COMMERCE AND INTRECOURSE

130. The discussion on the above subject needs to be focused on following three aspects, namely:

> "a. Legislative history of freedom of trade,
>
> b. Freedom of trade as it emerges from the debates in the Constituent Assembly,
>
> c. Tax, whether was treated as 'restriction' on the freedom of trade by Constituent Assembly."

131. During the British Rule, by the end of 19th Century efforts for drafting a Constitution for India had begun. Under the inspiration of Shri Bal Gangadhar Tilak, the Swaraj Bill,
1885 was the first non-official attempt of drafting the Constitution. The dominion status as achieved by Australia and passing of Australian Constitution Act 1900 was noticed by those associated with National Movement. Indian leaders including Members and Ex-Members of Central and Provincial Legislature had framed a Bill, namely, 'Commonwealth of India Bill, 1925' which was read in House of Commons in December, 1925, contained a clause on freedom of trade to the following effect:

> "25. Trade, commerce and intercourse among the provinces shall be free, and there shall be no preference given to any province or provinces."

132. In the British India, freedom of trade was in practice with no internal provincial duties or other trade barriers whereas in the Indian States internal custom and other trade barriers were there. The above practice took statutory form in Section 297 of

Government of India Act, 1935 which prohibited provincial Government from imposing barriers on trade within country. Section 297 reads as under:

> "297. "(1) No Provincial Legislature or Government shall– (a) by virtue of the entry in the Provincial Legislative List relating to trade and commerce within the Province, or the entry in that list relating to the production, supply, and distribution of commodities, have power to pass any law or take any executive action prohibiting or restricting the entry into, or export from, the Province of goods of any class or description; or
>
> (b) by virtue of anything in this Act have power to impose any tax, cess, toll, or due which, as between goods manufactured or produced in the Province and similar goods not so manufactured or produced, discriminates in favour of the former, or which, in the case of goods manufactured or produced outside the Province, discriminates between goods manufactured or produced in one locality and similar goods manufactured or produced in another locality.
>
> (2) Any law passed in contravention of this section shall, to the extent of the contrav-ention, be invalid."

133. Declaration of Cabinet Mission Plan on May 16, 1946 by British Prime Minister was to ensure that India attains freedom and decide as to what form of Government is to replace the existing regime. The Cabinet Mission Plan laid foundation for Constitution, functioning and procedure of Constituent Assembly.

134. The Constituent Assembly was well aware of the Constitution of Australia, USA and other Constitutions of world. On the freedom of trade the Constituent Assembly preferred the Australian model from Sections 92 and 99 of the Australian Constitution, which were to the following effect: free On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free...."

> “99. Commonwealth not to give preference The Commonwealth shall not, by any law or regulation of trade, commerce, or revenue, give preference to one State or any part thereof over another State or any part thereof."

135. The *Privy Council in James vs. Commonwealth of Australia*[19], had occasion to consider the freedom of trade as granted under Section 92 of the Constitution of the Australia. Following was stated by the Privy Council:

> “Thus reference may be made to the sections dealing in the midst of which s.92 is placed. It is well known that one of the objects which the federation sought to achieve was the abolition of restrictions on trade between the Colonies, and of the diversity in the different States of tariffs and border regulations; this was described as “the old inter-colonial trade war."

136. Section 92 was interpreted as to mean "free trade means,in ordinary parlance

freedom from tariffs". Professor David P. Derham, of Melbourne University dealing on the subject; "Some Constitutional problems arising under Part XIII of the Indian Constitution" has expressed his views on Section 92 of the Australian Constitution in following manner:

> "In its Australian origins there is no doubt whatever that freedom of trade, commerce and intercourse means at least freedom from taxation. One of the main motives of the federal movement in Australia was the desire to do away with what had become known as "border barbarism"-the operation of customs barriers on the State borders. Section 92 of the Australian Constitution was one of the provisions drawn to achieve this purpose, to ensure the economic unity of Australia, to prevent the continuance of competing State fiscal systems."

137. The framers of the Indian Constitution although took inspiration from Section 92 above, but even at initial stages the freedom of trade was contemplated with restriction and with permission to levy only certain taxes. The Sub-Committee on fundamental rights submitted a report dated 16.04.1947 to the Advisory Committee in Para 6 of which following was stated:

> "6. We are of the opinion that every citizen is entitled to free trade, commerce and intercourse within the territories of the Union unburdened by any internal duties or taxes of customs. At the same time, we realise that many Indian States depend upon such duties and taxes for a considerable part of their revenue and cannot do without it all at once. Similar difficulties have arisen in the framing of the constitutions of other countries and unless there is a scheme for a smooth transition to free trade in the Union friction will inevitably arise. Some agreement will therefore have to be made with those States in the light of their existing rights with a view to their ultimate elimination within a period to be prescribed by the Constitution. Thereafter, there will be untrammeled free trade within the Union."

138. The Advisory Committee considered the report of the sub-committee on fundamental rights. Shri Sardar Vallabhbhai Patel, Chairman Advisory Committee sent report dated 23rd April, 194 7 to the Constituent Assembly, in paragraph 5 of which following was stated:

> "5. Clause 10 deals with the freedom, throughout the Union, of trade, commerce and intercourse between the citizens. In dealing with this clause we have taken into account the fact that several Indian States depend upon internal customs for a considerable part of their revenue and it may not be easy for them to abolish such duties immediately on the coming into force of the Constitution Act. We, therefore, consider that it would be reasonable for the Union to enter into agreements with such States, in the light of their existing rights, with a view to giving them time, up to a maximum period to be prescribed by the Constitution, by which internal customs could be eliminated and complete free trade established within the Union."

139. Constituent Assembly on 1st May 194 7 considered the report on

fundamental rights.

140. Shri K. M. Munshi made following statement with regard to Custom Duties and Taxes:

> “The proviso contemplates that a Unit can impose certain customs duty with a view to bring up the level of the price of goods imported to the level of the price of the goods manufactured in the Unit itself. Otherwise, the goods produced in other Units will flood that particular Unit. With that view only has this proviso been added. Provinces, therefore, can impose certain duties and taxes on goods imported from other units with a view to bring up the value to the level of good manufactured in the Unit itself. But it was felt, Sir, that this was incomplete. Such regulations and conditions may be made as to favour the goods produced in the Unit and therefore, the words 'and under regulations and conditions which are non-discriminatory' have to be added, so that conditions must not be such as to force up the price of the goods imported. Therefore, the whole point is that there should not be any regulation or any conditions of such a nature which would favour the goods produced in the Unit as against those produced and imported from outside."

Certain amendments on 01st May 1947 were adopted.

141. In the Draft Constitution finalized by Drafting Committee, freedom of trade, commerce and intercourse throughout the territory of India was incorporated as one of the fundamental rights in Clause 16 in following words:

> “16. Subject to provisions of Article 244 of this Constitution and any law made by Parliament, trade, commerce and intercourse throughout the territory of India shall be free.”

142. trade and commerce' where articles 243, 244 and 245 which were to the following effect:

243. Prohibition of preference Or discriminat ion to one State over another by any law or regulation relating to trade or commerce	No preference shall be given to one State over another nor shall any discrimination be made between one State and another by any law or regulation relating to trade or commerce, whether carried by land, water or air. The committee is of opinion that the provisions contained in articles 243 and 244 should more appropriately be included in this Chapter than I Part III dealing with Fundamental Rights
.. 244. Restriction on trade, commerce and intercourse between States.	Notwithstanding anything contained in article 16 or in the last preceding article of this Constitution, it shall be lawful for

	any State– "(a) to impose on goods imported from other States any tax to which similar goods manu factured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and (b) to impose by land such reasonable restrictions on the freedom of trade, commerce or intercourse with that State as may be required in the public interests: Provided that during a period of five years from the commencement of this Constitution the provisions of clause (b) of this article shall not apply to trade or commerce in any of the commodities mentioned in clause (a) of article 306 of this Constitution.
245. Appointment of authority to carry out the provisions of articles 243 and 244.	Parliament shall by law appoint such authority as it considers appropriate for the carrying out of the provisions of articles 243 and 244 of this Constitution and confer on the authority so appointed such powers and such duties as it thanks necessary."

Draft Article 16 came for discussion before the Constituent Assembly on 03rd December 1948.

143. Shri C. Subramaniam raised the objection to the effect that powers given to the State Legislature have been in respect of interstate trade and commerce to impose certain taxes and Article 16 being subject to the law of the Parliament, how it can be fundamental right and whether there is any right at all reserved.

144. Dr. B. R. Ambedkar replied the objections of Shri Subramaniam and explained as to why Article 16 was placed in fundamental rights. Dr. Ambedkar stated that Constituent Assembly when began its task, there were limitations since the States were to join the Union only on three subjects, namely, foreign affairs, defence and communication, said Dr. Ambedkar that it was realized that there would be no use and purpose in forming an All India Union if trade and commerce throughout India was not free. Hence it was decided to put article in fundamental rights. Following was stated by Dr. Ambedkar:

> “But I shall explain to him why it was found necessary to include this matter in the fundamental rights. My friend, Mr. Subramaniam will remember that when the Constituent Assembly began, we began under certain limitations. One of the limitations was that the Indian States would join the Union only on three subjects- foreign affairs, defence and communications. On no other matter they would agree to permit the Union Parliament to extend its legislative and executive jurisdiction. So he will realise that the Constituent Assembly, as well as the Drafting Committee, was placed under a very serious limitation. On the one hand it was realized that there would be no use and no purpose served in forming an All-India Union if trade and commerce throughout India was not free. That was the general view. On the other hand, it was found that so far as the position of the States was concerned, to which I have already made a reference, they were not prepared to allow trade and commerce throughout India to be made subject to the legislative authority of the Union Parliament. Or to put it briefly and in a different language, they were not prepared to allow trade and commerce to be included as an entry in List No. 1. If it was possible for us to include trade and commerce in List I, which means that Parliament will have the executive authority to make laws with regard to trade and commerce throughout India, we would not have found it necessary to bring trade and commerce under article 16, in the fundamental rights. But as that door was blocked, on account of the basic considerations which operated at the beginning of the Constituent Assembly, we had to find some place for the purpose of uniformity in the matter of trade and commerce throughout India, under some head. After exercising considerable amount of ingenuity, the only method we found of giving effect to the desire of a large majority of our people that trade and commerce should be free throughout India, was to bring it under fundamental rights."

145. One more important statement made by Dr. Ambedkar was to the following effect:

> "Yes, but reasonable restrictions do not mean that the restrictions can be such as to altogether destroy the freedom and equality of trade. It does not mean that at all."

146. The Constituent Assembly resolved to adopt the motion making Article 16 as a part of the Constitution. On 08th September 1949, Dr. Ambedkar moved a motion for inserting a Part XA consisting of Article 274A, 274B, 274C, 274D and 274E. Part XA included provisions as contained in Article 16 as Article 2 74A as was passed in the fundamental rights and Article 274B to 274E as was earlier contained in provisions of Article 244, 245 in the Draft Constitution. Dr. Ambedkar, while moving a motion stated that articles dealing with the freedom of trade and commerce were scattered in different parts of the Draft Constitution, as article 16 was under fundamental rights and article 24 3, 244 and 245 were in Part IX. Various amendments were proposed by Pandit Thakur Das Bhargava and other members. After a great discussion Part XA was passed to be included in the Constitution with certain minor amendments.

147. Subsequently, Dr. Ambedkar on 16th October 1949 moved a motion for insertion

of Article 274DD, which was to the following effect: the foregoing provisions of this Part or in any other provisions of this Constitution, any State which before the commencement of this
Constitution was levying any tax or duty on the import of goods into the State from other States or on the export of goods from the State to other States may, if an agreement in that behalf has been entered into between the Government of India and the Government of that
"274DD. Notwithstanding anything contained in Power of certain States in Part III of the First schedule in impose restrictions on trade and commerce by the levy of certain taxes and duties on the import of goods into or the export of goods from such States. State, continue to levy and collect such tax or duty subject to the terms of such agreement and for such period not exceeding ten years from the commencement of this Constitution as may be specified in the agreement: Provided that the President may at any time after the expiration of five years from such Commencement terminate or modify any such agreement if, after consideration of the report of the Finance Commission constituted under article 260 of this Constitution, he thinks it necessary to do so."

148. While discussing Article 274DD, one of the Members of the Constituent Assembly Shri Raj Bahadur has expressed his concern about continuance of custom duties and taxation which according to him were great restrictions to the trade and commerce. Following views were expressed by Shri Raj Bahadur:

> "Shri Raj Bahadur (United State of Matsya): I have sought this opportunity, to take a few minutes of this House while this article is under consideration to give vent to the feeling of the common people in the States' Unions about these customs, duties and taxation. As a matter of fact, ever since political awakening dawned upon the people of the Indian States customs taxes have been a particular target of political opposition. It was not without reason that the people of the Indian States and their movements were set against the imposition of customs duties on both imports and exports. It was because of a particular feeling amongst the people that this opposition was there. We have felt all through that all our trade, our industries have been crippled because of these Customs Duties. Even today we are not going to be benefited by it. Somehow or other , because these States were not viable units and they had to balance their budget the customs taxation was resorted to. Apart from that it was also supposed to be a part of the sovereign rights of the States. But so far as the interests of the people were concerned, they were not served by the imposition of these customs duties. Constituent Assembly adopted Article 274DD."

149. The debates on draft article 264(A) (Now Article 286 in the Constitution) with regard to imposition of sales tax came for consideration on 16.10.1949 which are also relevant in the context of freedom of trade and commerce. Dr. B.R. Ambedkar stated that imposition of sales tax has created lot of difficulties in the matter of freedom of trade and commerce. Dr. B.R. Ambedkar further stated that imposition of sales tax shall not be in conflict with provisions of Part XA (Now Part XIII) . Following was stated by Dr. Ambedkar:

"Sir, as everyone knows, the sales tax has created a great deal of difficulty throughout India in the matter of freedom of trade and commerce. It has been found that the very many sales taxes which are levied by the various Provincial Governments either cut into goods which are the subject matter of imports or exports, or cut into what is called inter-State trade or commerce. It is agreed that this kind of chaos ought not to be allowed and that while the provinces may be free to levy the sales tax there ought to be some regulations whereby the sales tax levied by the provinces would be confined within the legitimate limits which are intended to be covered by the sales tax. It is, therefore, felt that there ought to be some specific provisions laying down certain limitations on the power of the provinces to levy sales tax. The first thing that I would like to point out to the House is that there are certain provisions in this article 264A which are merely reproductions of the different parts of the Constitution. For instance, in sub-clause(I) of article 264A as proposed by me, sub-clause (b) is merely a reproduction of the article contained in the Constitution, the entry in the Legislative List that taxation of imports and exports shall be the exclusive province of the Central Government. Consequently so far as sub-clause (1) (b) is concerned there cannot be any dispute that this is in any sense an invasion of the right of provinces to levy as sales-tax. Similarly, sub-clause (2) is merely a reproduction of Part XA which we recently passed dealing with provisions regarding inter-State trade and commerce. Therefore so far as sub-clause(2) is concerned there is really nothing new in it. It merely says that if any sales tax is imposed it shall not be in conflict with the provisions of Part XA."

150. The moving idea and inspiration for framing relevant articles pertaining to freedom of trade and commerce was and is the realization that a federal union needs the creation and the preservation of national economic fabric and the removal of or prevention of local barriers to economic unity so that competing economic units within unions shall not threaten the stability of the nation as a whole. The Unity of India was seen to some extent on above realization.

151. From what we have noted above, it is clear that the Constitution framers gave great importance to the freedom of trade and commerce. In the beginning, when States had conceded to union, only foreign affairs, defence and communication, right of freedom of trade and commerce was placed in the Chapter of Fundamental Rights since it was thought that making of All India Union will be useless if trade and commerce is not free. Dr. Ambedkar on 08.09.1949, during the debates had stated that even though, there may be reasonable restriction on the right, however, the restriction can be such which altogether may not destroy the freedom and equality of trade.

152. The Constitution framers were conscious of the fact that goal set-up for freedom of trade and commerce is to eliminate internal custom duties and States were conceded to impose limited taxes with restrictions as envisaged in the proposed articles.

153. Article 274DD as adopted by the Constituent Assembly, which became Article 306 of the Constitution allowed the existing taxes and duties by the States on the import

into or export of goods for a period not exceeding 10 years clearly indicates that taxes are restrictions on trade and commerce, hence period of 10 years was allowed to abolish the same and the State to ensure free flow of trade and commerce.

154. One more important fact is to be noticed from the Constituent Assembly Debates dated 8th September, 1949 in reference to Article 244 (now Article 304), which permitted the State to impose any tax on goods imported from other States. Dr. B.R. Ambedkar referred the above Article 244 as a provision giving limited power to impose certain restrictions on the entry of goods. Dr. Ambedkar in his statement in the proceeding instead of repeating the word 'tax' as specifically mentioned in Article 244 used the word 'restriction'. The above also indicates that the use of word 'restriction' included the tax also.

155. From the legislative history as noted above and the extent of freedom of trade and commerce as emerged from Constituent Assembly Debates, it is abundantly clear that the taxes were treated as restriction on freedom of trade and commerce and it was further comprehended that restriction on freedom of trade and commerce can be put by taxation also.

156. 'In the people of India', vests the legal sovereignty while the political sovereignty is distributed between Union and the States. We having adopted for ourselves a well thought, well deliberated written Constitution, it is pertinent to know the structure of our Constitution. Learned counsel for the parties during their respective submissions have referred to the federal structure of the Constitution and one of the submissions raised before us is that while interpreting the Constitution the federal structure of the Constitution has to be kept in mind, since, the framers of the Constitution must have never intended to dilute the federal structure of the Constitution.

157. The Constituent Assembly of India consisting of illustrious members drawn from all parts of the country deliberated all aspects of the new Constitution and took considerable pain and caution in drafting the Constitution which may fulfill the aspirations of independent India. Initially, it was perceived that the federal Government i.e. Union Government shall be responsible for Foreign Affairs, Defence and Communication. After declaration of Partition on 3rd June, 1947, there was considerable change in the views of the Constituent Assembly. Union Constitution Committee on 6th June, 1947 took a decision that Constitution would be federal with a strong Centre. Granville Austin in the Indian Constitution:Cornerstone of a Nation has described the shift in the following words:

> “Mountbatten announced Partition on 3 June 1947. Within four days the Assembly had embarked on a centralized federal union. On 5 June the Union and Provincial Constitution Committees,having spent much of the first month of their lives marking time, met in joint session and concluded that in the light of the June Third Statement the Cabinet Mission Plan no longer applied to the Assembly. The following day the Union Constitution Committee met alone. Present were Nehru, the Chairman, Prasad,Azad,Pant,Jagjivan Ram, Ambedkar, Ayyar, Munishi, Shah, S.P. Mookerjee, V.T.Krishnamachari, Panikkar, N.G.

Ayyangar,and P. Govinda Menon. These men took the following tentative decisions: That the Constitution would be federal with a strong centre; That there should be three 'exhaustive' legislative lists, and that residuary powers should vest in the Union Government; That the Princely States should be on a par with the provinces regarding the Federal List,subject to special matters; and That generally speaking the Executive authority of the Union should be co-extensive with its legislative authority."

158. The Drafting Committee which was charged with the duty of preparing a Constitution in accordance with the decision of the Constituent Assembly on the reports made by discussion on 4th November, 1948. Dr. B.R. Ambedkar while placing the Draft Constitution/while moving the motion had deliberated over the nature of the Constitution. Dr. Ambedkar stated that the Draft Constitution is Federal Constitution in the following words:

"Two principal forms of the Constitution are known to history-one is called Unitary and other Federal. The two essential characteristics of a Unitary Constitution are:

(1) the supremacy of the Central Polity,and

(2) the absence of subsidiary Sovereign politics. Contrariwise.a Federal Constitution is marked: (1) by the existence of a Central polity and subsidiary polities side by side, and (2)by each being sovereign in the field assigned to it. In other words, Federation means the establishment of a Dual Polity. The Draft Constitution is, Federal Constitution inasmuch as it establishes what may be called a Dual Polity. This Dual Polity under the proposed Constitution will consist of the Union at the Centre and the States at the periphery each endowed with sovereign powers to be exercised in the field assigned to them respectively by the Constitution."

159. Dr. Ambedkar also referred to the Constitution of USA and highlighted the difference between Indian Federation and American Federation. While speaking on the difference of
Indian Federation to that of American Federation Dr. Ambedkar stated:

"But there are some other special features of the proposed Indian Federation which mark it off not only from the American Federation but from all other Federations. All federal systems including the American are placed in a tight mould of federalism. No matter what the circumstances, it cannot change its form and shape. It can never be unitary. On the other hand the Draft Constitution can be both unitary as well as federal according to the requirements of time and circumstances. In normal times,it is framed to work as a federal system. But in times of was it is so designed as to make it work as though it was a unitary system."

160. Dr. Ambedkar further stated that a Federal Constitution cannot but be a written Constitution. The following was stated:

"A Federal Constitution cannot but be a written Constitution and a written Constitution must necessarily be a rigid Constitution. A Federal Constitution means division of Sovereignty by no less a sanction than that of the law of the Constitution between the Federal Government and the States, with two necessary consequences

(I) that any invasion by the Federal Government in the field assigned to the States and vice versa is a breach of the Constitution (2)such breach is a justiciable mater to be determined by the Judiciary only."

161. A.V. Dicey in his celebrated work "The Law of the Constitution" while dealing with the aim of Federation stated the following:

"A federal state is a political contrivance intended to reconcile national unity and power with the maintenance of 'state rights'. The end aimed at fixes the essential character of federalism. For the method by which federalism attempts to reconcile the apparently inconsistent claims of national sovereignty and of state sovereignty consists of the formation of a constitution under which the ordinary powers of sovereignty are elaborately divided between the common or national government and the separate States. The details of this division vary under every different federal constitution,but the general principle on which it should rest is obvious. Whatever concerns the nation is a whole should be placed under the control of the national government. All matters which are not primarily of common interest should remain in the hands of the several States."

162. A.V. Dicey further stated about three leading characteristics of federalism;

"the supremacy of the constitution- the distribution among bodies with limited and co-ordinate authority of the different powers of government- the authority of the Courts to act as interpreters of the constitution."

163. Shri Alladi Krishnaswami Ayyar while referring to Part XA i.e. trade, commerce and intercourse (within the territory of India) referring to factors of federation in the context of trade, commerce and intercourse stated as follows:

“Therefore, in a federation what you have to do is, first, you will have to take into account the larger interests of India and permit freedom of trade and intercourse as far as possible. Secondly, you cannot ignore altogether regional interests. Thirdly, there must be the power intervention of the Centre in any case of crisis to deal with peculiar problems that might arise in any part of India. All these three factors are taken into account in the scheme that has been placed before you."

164. The nature of federalism as contained in the Constitution of India came for consideration before this Court in large number of cases. Several larger Benches of this Court dealt with the issue and had deliberated and explained the principles of federalism as incorporated in the Constitution. A Seven Judge Bench in the Special

Reference No.1 of 1964: In the matter of: Under Article 143 of the Constitution of India, (1965) 1 SCR 413 referring to fundamental feature of a Federal Constitution laid down that supremacy of the Constitution is fundamental to the existence of the Federal Constitution, following was stated:

> "In dealing with this question, it is necessary to bear in mind one fundamental feature of a federal constitution. In England, Parliament is sovereign; and in the words of Dicey, the three distinguishing features of the principle of Parliamentary Sovereignty are that Parliament has the right to make or unmake any law whatever; that no person or body is recognised by the law of England is having a right to override or set aside the legislation of Parliament; and that the right or power of Parliament extends to every part of the Queen's dominions (Dicey, The Law of the Constitution 10th ed. pp. xxxiv, xxxv). On the other hand, the essential characteristic of federalism is "the distribution of limited executive, legislative and judicial authority among bodies which are co-ordinate with an independent of each others." The supremacy of the constitution is fundamental to the existence of a federal State in order to prevent either the legislature of the federal unit or those of the member States from destroying or impairing that delicate balance of power which satisfies the particular requirements of States which are desirous of union, but not prepared to merge their individuality in a unity. This supremacy of the constitution is protected by the authority of an independent judicial body to act as the interpreter of a scheme of distribution of powers."

165. In the landmark judgment of this Court in His *Holiness Kesavanand Bharati Sripadagalvaru vs. State of Kerala and another*[20] a new dimension was given to the Constitutional principles. This Court by majority judgment declared that the basic feature of the Constitution could not be amended by a constitutional amendment. Chief Justice, Sikri while delivering the majority judgment had held that federal character of the Constitution is one of the basic structures of the Constitution.

166. Shelat and Grover, JJ. while delivering concurring Opinion had also stated that our Constitution has all essential elements of federal structure. In paragraph 486 following was stated:

> "The Constitution has all the essential elements of a federal structure as was the case in the Government of India Act, 1935, the essence of federalism being the distribution of powers between the federation or the Union and the States or, the provinces. All the legislatures have plenary powers but these are controlled by the basic conce-pts of the Constitution itself and they function within the limits laid down in it Per Gajendragadkar
>
> C. J. in Special Reference No. 1 of 1964, [1965] 1 S.C.R. 413. All the functionaries, be they legislators, members of the executive or the judiciary take oath of allegiance to the Constitution and derive their authority and jurisdiction from its provisions. The Constitution has entrusted to the judicature in this country the task of construing the provisions of the Constitution and of safeguarding the fundamental rights Ibid p. 446. It is a written and controlled

Constitution."

167. Again a Seven Judge Bench in *State of Rajasthan and others vs. Union of India and other*[21]*s,* had an occasion to consider the nature of Indian Constitution. M.H. Beg, CJ,while delivering majority decision in paragraph 57 following was stated:

> "57. The two conditions Dicey postulated for the existence of federalism were: firstly,
> ”a body of countries such as the Cantons of Switzerland, the Colonies of America, or the Provinces of Canada, so closely connected by locality, by history, by race, or the like, as be capable of bearing, in the eyes of their inhabitants an impress of common nationality”; and, secondly, absolutely essential to the founding of a federal system is the "existence of a very peculiar state of sentiment among the inhabitants of the countries”. He pointed out that, without the desire to unite there could be no basis for federalism. But, if the desire to unite goes to the extent of forming an integrated whole in all substantial matters of Government, it produces a unitary rather than a federal constitution. Hence, he said, a federal State "Is a political contrivance intended to reconcile national unity with the maintenance of State rights." The degree to which the State rights are separately preserved and safeguarded gives the extent to which expression is given to one of the two contradictory urges so that there is a union without a unity in matters of government. In a sense, therefore, the Indian union is federal. But, the extent of federalism in it is largely watered down by the needs of progress and development of a country which has to be nationally integrated, politically and economically coordinated, and socially, intellectually and spiritually up-lifted. In such a system, the States cannot stand in the way of legitimate and comprehensively planned development of the country in the manner directed by the Central Government "

168. Further in paragraph 60 referring to Dr. Ambedkar following was stated:

> "60. Although Dr. Ambedkar thought that our Constitution is federal "inasmuch as it
> establishes what may be called a Dual Polity," he also said, in the Constituent Assembly, that our Constitution makers had avoided the 'tight mould o federalism' in which the American Constitution was forged. Dr. Ambedkar, one of the principal architects of our Constitution, considered our Constitution to be both unitary as well as federal according to the requirements of time and circumstances'."

169. A *Nine Judge Bench had occasion to elaborately and others vs. Union of India and others,*[22]*,* Ahmadi, J. referring to federal character of the Constitution in paragraph 14 following was stated:

> "14.In order to understand whether our Constitution is truly federal, it is essential to know the true concept of federalism. Dicey calls it a political contrivance for a body of States which desire Union but not unity. Federalism is, therefore, a

concept which unites separate States into a Union without sacrificing their own fundamental political integrity. Separate States, therefore, desire to unite so that all the member-States may share in formulation of the basic policies applicable to all and participate in the execution of decisions made in pursuance of such basic policies. Thus the essence of a federation is the existence of the Union and the States and the distribution of powers between them. Federalism, therefore, essentially implies demarcation of powers in a federal compact."

170. Ahmadi, J. further stated that the Constitution of India is differently described, more appropriately as 'quasi-federal' because it is a mixture of the federal and unitary elements, leaning more towards the latter.

171. B.P. Jeevan Reddy, J., held that the founding fathers wished to establish a strong a Center. In the light of the past history of this sub-continent, this was probably a natural and necessary decision. In paragraphs 275 and 276 following was stated:

"275. A review of the provisions of the Constitution shows unmistakably that while creating a federation, the Founding Fathers wished to establish a strong Centre. In the light of the past history of this sub-continent, this was probably a natural and necessary decision. In a land as varied as India is, a strong Centre is perhaps a necessity. This bias towards Centre is reflected in the distribution of legislative heads between the Centre and States. All the more important heads of legislation are placed in List I. Even among the legislative heads mentioned in List II, several of them, e.g., Entries 2, 13, 17, 23, 24, 26, 27, 32, 33, 50, 57 and 63 are either limited by or made subject to certain entries in List I to some or the other extent. Even in the Concurrent List (List III), the parliamentary enactment is given the primacy, irrespective of the fact whether such enactment is earlier or later in point of time to a State enactment on the same subject-matter. Residuary powers are with the Centre. By the 42nd Amendment, quite a few of the entries in List II were omitted and/or transferred to other lists. Above all, Article 3 empowers Parliament to form new States out of existing States either by merger or division as also to increase, diminish or alter the boundaries of the States

276. The fact that under the scheme of our Constitution, greater power is conferred upon the Centre vis-a-vis the States does not mean that States are mere appendages of the Centre. Within the sphere allotted to them, States are supreme. The Centre cannot tamper with their powers. More particularly, the courts should not adopt an approach, an interpretation, which has the effect of or tends to have the effect of whittling down the powers reserved to the States. It is a matter of common knowledge that over the last several decades, the trend the world over is towards strengthening of Central Governments be it the result of advances in technological/scientific fields or otherwise, and that even in USA the Centre has become far more powerful notwithstanding the obvious bias in that Constitution in favour of the States. All this must put the court on guard against any conscious whittling down of the powers of the States. Let it be said that the

federalism in the Indian Constitution is not a matter of administrative convenience, but one of principle the outcome of our own historical process and a recognition of the ground realities. This aspect has been dealt with elaborately by Shri M.C. Setalvad in his Tagore Law Lectures "Union and State relations under the Indian Constitution" (Eastern Law House, Calcutta, 1974). The nature of the Indian federation with reference to its historical background, the distribution of legislative powers, financial and administrative relations, powers of taxation, provisions relating to trade, commerce an industry, have all been dealt with analytically. It is not possible nor is it necessary for the present purposes to refer to them. It is enough to note that our Constitution has certainly a bias towards Centre vis-a-vis the States Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan, (1963) 1 SCR 491, 540: AIR 1962 SC 1406. It is equally necessary to emphasise that courts should be careful not to upset the delicately-crafted constitutional scheme by a process of interpretation."

172. A Constitution Bench in *4*, held that India is not a federal State in the traditional sense of the term and it is not a true federation formed by agreement between various States and it has been described as quasi-federation and similar other concepts. Dr. Justice Durga Das Basu in his Treatise "Comparative Federalism" by tracing the history of framing of our Constitution stated following in Chapter IV "Indian Federation in particular"-

"The strong centralising tendency of the Indian federation which has attracted the notice of foreign observers, can be properly appreciated only if its genesis is understood. Federation, under our Constitution, is the resultant of conflicting forces. The political tradition of the country was unitary, but it was not possible to adopt a unitary Constitution, since it was necessary to fit in the Indian States (about 600 in number) which had practically become independent since the lapse of paramountcy, as a result of the Indian Independence Act, 1947. On the other hand, it was not possible to make the Union the 'exceptional' government as in the United States, because all the units of the federation were not equally developed,and central control was necessary to secure uniform development of the country as well as of the backward classes of the population. Above all, a strong Central Government had been necessitated by the situation created by the partition of the country. It may be recalled that the Objectives Resolution adopted by the Constituent Assembly at the outset envisaged that the units of the Union of India should be 'autonomous' and vested with residuary power. But the framers of the Draft Constitution had to depart from the federal concept embodied in the Objectives Resolution owing to a change in the political situation which had taken place in the meantime. The object of the framers of our Constitution,thus,was to build a strong central authority whichmight resist external aggression and also to check internal disruptive forces that might tend to undermine the nascent State. This object has been sought to be attained,not only by endowing larger enumerated powers upon the Union than Elsewhere and by giving it the residue [Art.248] (as in Canada), but also by enabling the Centre itself to assume control of the units whenever there is any threat of

disruption either from outside or from within."

173. The law declared by this Court as noted above clearly indicate that the Indian Constitution is basically federal in form and is marked traditional characteristics of a federal system, namely, supremacy of the Constitution, division of power between the Union and States and existence of an independent judiciary. Federalism is one of the basic features of Indian Constitution. However, the history of Constitution including the Debates in the Constituent Assembly indicate that the distribution of powers was given shape with creating a strong Centre with the object of unity and integrity of India. The States are sovereign in the allotted fields. The Indian Constitution cannot be put in traditional mould of federalism. The traditional concept of federalism has been adopted with necessary modification in the framework of the Constitution to suit the country's necessity and requirement. The sum total of above discussion is that federalism in the Constitution is limited and controlled by the Constitution and the exercise of powers of both the States and the Centre are controlled by express provisions of the Constitution.

174. The submission that while interpreting Part XIII of the Constitution federal nature of the Constitution has not to be tinkered with shall be adverted hereinafter while dealing with interpretation of different Articles of Part XIII of the Constitution specially Article 304.

C. LIMITATION ON THE LEGISLATIVE POWER OF THE STATE UNDER THE CONSTITUTION

175. Thomas M. Cooley in "A Treatise on the Constitutional Limitations" defines a Constitution in the following words:

> "A constitution is sometimes defined as the fundamental law of a state, containing the principles upon which the government is founded, regulating the division of the sovereign powers, and directing to what persons each of these powers is to be confided, and the manner in which it is to be exercised. Perhaps an equally complete definition would be, that body of rules and maxims in accordance with which the powers of sovereignty are habitually exercised."

176. The Indian Constitution has adopted federal structure as noted above. Three characteristics of federal system are : (1) supremacy of the Constitution; (2) division of powers between the Union and State Governments; and (3) existence of an independent judiciary. The Constitution operates as a fundamental law. Organs of the States, i.e., executive Legislature and judiciary derive their authority and discharge their responsibilities within the framework of the Constitution. Neither the Union Parliament nor State Legislature are sovereign. The legislative power given to Parliament and State Legislature is provided for and dealt in the Constitution. The State is sovereign to legislate on any subject in conformity with the Constitutional limitations. What are the limitations envisaged by the Constitution in exercise of the legislative power of the State, is one of the issues for consideration before us. Learned counsel appearing for the States contend that the power to legislate as on the subjects as enumerated in List II is a sovereign power which also includes power of State to impose taxes in which no

limitation can be read from Part XIII of the Constitution. It is contended that it is only by a specific prohibition or limitation in the Constitution which has to be read as limiting the sovereign power of the State. On the other side, the petitioners contend that State Legislature while exercising its power of taxation exercise the same legislative power as it does while enacting any other law which it is competent to enact and there is no qualitative distinction between the exercise of legislative power enacting a law levying tax or enacting a non-fiscal law. In making of any law, all limitations envisaged by the Constitution shall apply. Learned counsel appearing for the States have submitted that limitations on taxing power of the State Legislature are all contained only in Part XII of the Constitution and no other limitation in exercise of State legislative power can be read.

177. Article 13 sub-clause (2) in Part III of the Constitution provides express prohibition in making of law by the State. Article 13 sub-clause (2) is as follows:

> "13(2). The State shall not make any law which takes away or abridges the rights conferred by this Part and any law made in contravention of this clause shall, to the extent of the contravention, be void."

178. Part XI of the Constitution deals with "Relations between the Union and the States". Chapter I of which contains heading "Legislative Relations". Chapter I contains Article 245 to Article 255. Article 245 begins with the words : subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the Legislature of a State may make laws for the whole or any or any part of the State. Article 24 6 deals with the subject-matter of the laws made by Parliament and by the Legislatures of States. Articles 245 and 246 are as follows:

> "245. Extent of laws made by Parliament and by the Legislatures of States.-(1) Subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the Legislature of a State may make laws for the whole or any part of the State.
>
> (2) No law made by Parliament shall be deemed to be invalid on the ground that it would have extra-territorial operation."
>
> 246. Subject-matter of laws made by Parliament and by the Legislatures of States.-(1) Notwithstanding anything 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 anything in clause (3), Parliament, and, subject to clause (1), 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 this 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."

179. During submissions before us, one of the issues raised is as to whether Article 245 is source of legislative power or it is Article 246. Some of the counsel appearing on behalf of
the States contend that the word "subject to the provisions of this Constitution" is there only in Article 245 which does not govern, Article 246 under which Legislature of any State has
exclusive power to make law. Articles 245 and 246 both cover the same subject i.e. law making by the Parliament and the Legislature. Article 245 deals with the extent of laws whereas Article 246 deals with the subject-matter of laws. Both the Articles together define and demarcate the legislative powers to be exercised by the Parliament and the States. The issue is no longer res integra. The Constitution Bench of this Court in *Maharaj Umeg Singh and others vs. The State of Bombay and other*[23] had occasion to consider the extent and limitations on the legislative powers as provided under Articles 245 and 246. Following was laid by this Court in the above case:

"The fetter or limitation upon the legislative power of the State Legislature which had plenary powers of legislation within the ambit of the legislative heads specified in the Lists II & III of the Seventh Schedule to the Constitution could only be imposed by the Constitution itself and not by any obligation which had been undertaken by either the Dominion Government or the Province of Bombay or even the State of Bombay. Under Article 246 the State Legislature was invested with the power to legislate on the topics enumerated in Lists II & III of the Seventh Schedule to the Constitution and this power was by virtue of article 245(1)subject to the provisions of the Constitution. The Constitution itself laid down the fetters or limitations on this power, e.g., in article 303 or article 286 (2) ."

It is relevant to note that Constitution Bench has noticed Article 303 as one of the Articles by which limitations were put on the legislative powers of the State.

180. The above view has been reiterated in a large number of judgments of this Court. It will be sufficient to refer only one more Constitution Bench judgment of this Court in *State of Kerala and others vs. Mar Appraem KuriCompany Limited and another*[24], This Court again had occasion to consider Articles 245 and 246. The Constitution Bench held in the said case that while the legislative power is derived from Article 245, entries in the Seventh Schedule of the Constitution only demarcate the legislative fields of the respective legislatures and do not confer legislative power as such. Following observations were made in paragraph 35:

"35 While the legislative power is derived from Article 245,the entries in the Seventh Schedule of the Constitution only demarcate the legislative fields of the respective legislatures and do not confer legislative power as such. While Parliament has power to make laws for the whole or any part of the territory of India, the legislature of a State can make laws only for the State or part thereof. Thus Article 245 inter alia indicates the extent of laws made by Parliament and by the State Legislatures."

181. In paragraph 37 it was laid down that the expression "subject to other provisions of the Constitution" has also to be read in Article 24 6, following was laid down in paragraph 37:

"Article 246, thus, provides for distribution, as between Union and the States, of the legislative powers which are conferred by Article 245. Article 245 begins with the expression "subject to the provisions of this Constitution". Therefore, Article 246 must be read as "subject to other provisions of the Constitution".

182. Thus, it is well settled that legislative power of the State is subject to the provisions of the Constitution. The words 'subject to the provisions of this Constitution' had to give its full meaning and content. Thus, limitation of the legislative powers wherever found in the Constitution has to be given effect to. There can be no doubt that Part XII of the Suits" and there are various express limitations provided in Part XII, namely, Articles 276, 286 and certain other Articles but can Part XII be treated as the only limitations on the legislative powers of the States, the answer has to be in negative. We have already extracted Article 13 sub-clause (2) and there are more than one Constitution Bench judgments which held that taxing legislation has also to conform Article 13 sub-clause(2). In Kunnathat Thathunni Moopil Nair vs. The State of Kerala and another, (1961) 3 SCR 77, Constitutional validity of Travancore-Cochin Land Tax Act, 1955 was challenged. Following contention was raised by the petitioners:

"On the legal aspect of the controversy raised on behalf of the petitioners, it was argued that the Act has its justification in Art.265 of the Constitution, which was not subject to the provisions of Part III of the Constitution and that, therefore, Arts. 14, 19, 31 could not be pressed in aid of the petitioners. It was also contended that even if the Act is, in effect,confiscatory, it cannot be questioned, being a taxing statute."

183. Repelling the contention the Constitution Bench held that tax legislation is also subject to Article 13. Following was held:

"It has to be done by authority of law, which must mean valid law. In order that the law may be valid, the tax proposed to be levied must be within the legislative competence of the Legislature imposing a tax and authorizing the collection thereof and, secondly, the tax must be subject to the conditions laid down in Art.13 of the Constitution. One of such conditions envisaged by Art.13(2) is that

the Legislature shall not make any law which takes away or abridges the equality clause in Art.14 which enjoins the State not to deny to any person equality before the law or the equal protection of the laws of the country."

184. Another Constitution Bench judgment in *Hari Krishna Bhargav vs. Union of India and another*[25], held that exercise of taxing power is also to be tested in the light of the fundamental freedoms guaranteed under Chapter III of the Constitution. Following was observed in paragraph 7:

"7....Exercise of the taxing power to the State has undoubtedly to be tested in the light of the fundamental freedoms guaranteed by Ch.III of the Constitution. It is not a power which transcends the fundamental rights, as was assumed in certain earlier decisions. Ramjilal v. Income-tax Officer Mohinder Garh, 1951 SCR 127: (AIR 1951 SC 97): Laxmanappa Hanumantappa v. Union of India,1955-1 SCR 769: (AIR 1955 SC 3): and the view expressed by Venkataramma Ayyar, J., in Anantha Krishnan v. State of Madras, ILR (1952) Mad 933: (AIR 1952 Mad 395). But it
is now settled by decisions of the Court (e.g.), Kunnathat Thathunni Moopil Nair v.State of Kerala, 1961-3 SCR 77: (AIR 1961 SC 552), that a taxing statute is subject to the "conditions laid down in Art.13 of the Constitution". A taxing statute may
accordingly be open to challenge on the ground that it is expropriatary, or that the statute prescribes no procedure or machinery for assessing tax, but it is not open to challenge merely on the ground that the tax is harsh or excessive."

185. All legislative powers is subject to limitations in the Constitution, be it fiscal statutes or non-fiscal statutes.

186. Now, we come to the question as to whether Part XIII also contains limitations on the legislative power of the State. Part XIII of the Constitution has been included in the Constitution after great deliberation and debates in the Constituent Assembly as noted above. Part XIII contains one of the most important right and principle on which country was to march to attain economic freedom. Justice Gajendragadkar,

J. has beautifully explained the nature and contents of right guaranteed under Part XIII in following words: -

"The provision contained in Article 301 guaranteeing the freedom of trade, commerce and intercourse is not a declaration of a mere platitude, or the expression of a pious hope of a declaratory character; it is not also a mere statement of a directive principle of State policy; it embodies and enshrines a principle of paramount important that the economic unity of the country will provide the main sustaining force for the stability and progress of the political and cultural unity of the country."

187. Justice Gajendragadkar speaking for majority in the above case has also held that Article 301 is a Constitutional limitation on the legislative power of the Parliament and

the States in following words:-

> "That is why it seems to us that Article 301, read in its proper context and subject to the limitations prescribed by the other relevant Articles in Part XIII, must by regarded as imposing a constitutional limitation on the legislative power of Parliament and the Legislatures of the States."

188. While discussing the "limitation on the legislative power of the State under the Constitution" we have already concluded that Article 245 which is a source of all legislative power puts a general limitation on all legislative power which has been expressly made 'subject to the provisions of this Constitution'. When all legislative powers are subject to the provision of Constitution, Part XIII being also a part of the Constitution, all legislative power has also to be subject to Part XIII.

189. A textual interpretation of Part XIII also lead to the same conclusion. Article 303 is an express provision which provides for 'restriction on the legislative power of the Union and the States with regard to trade and commerce'. Article 304 is another provision which although empowers the legislature of the State to put restriction on trade, commerce and intercourse among the States by law, but law to be made by the State is hedged by various restrictions as contained in Article 304(a) and 304(b). Thus Article 304 is also a limitation on legislative power of the State.

190. This Court in *State of Karnataka and Another Vs. Hansa Corporation*[26], has held in Para 30:

> "Article 304(a) imposes a restriction on the power of the legislature of a State to levy tax ".

191. Article 301 contains a general limitation on all legislative power. A Constitutional Bench of this Court *in State of Tamil Nadu and Others Vs. Sitolaxmi Mills and Others*[27] in para 7 as Stated:

> "....In other words Article 301 imposes a general limitation on all legislative power in order to secure that trade, commerce and intercourse in the territory of India shall be free".

192. *Justice K. Mathew in G. K. Krishnan and Others Vs. State of Tamil Nadu and Others*[28] had again reiterated that Article 304 imposes a general limitation on all legislative power, he states that 'Article 301 imposes a general limitation on all legislative power in order to secure that trade, commerce and intercourse throughout the territory of India shall be free'. In view of the aforesaid discussion, we conclude that Part XIII of the Constitution contains limitation on the legislative power of the State and all legislative power of the State whether fiscal or non-fiscal has to conform Part XII of the Constitution. D. Whether Part XIII of the Constitution covers "tax legislation" and word "restriction" used therein includes tax legislation.

193. The above subject is being considered in two parts. Firstly, whether Part XIII of the

Constitution covers tax legislation and secondly, whether word restriction used in Part XIII includes tax legislation.

Whether Part XIII covers tax legislation

194. Learned counsel for both the parties have to make different submissions on the above subject. Learned counsel for the petitioners on the one hand contends that all tax legislation which restrict freedom of trade, commerce and intercourse are covered by Part XIII whereas learned counsel appearing for the States contend that Part XIII only covers non-discriminatory taxes as referred to under Article 304(a) and no other tax legislation is covered under Part XIII.

195. Gajendragadkar J., speaking for majority in Atiabari Tea Co. Ltd. has rejected the argument that tax laws are outside Part XIII. Even Sinha C.J., having expressed the following

> "...Therefore, when Part XIII of the Constitution speaks of imposition of reasonable restrictions in public interest, it could not have intended to include taxation within the generic term 'reasonable restrictions'...."

In the same Paragraph further observed:

> "... if a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution makers to abolish by Part XIII... "

196. Shah J., in Atiabari Tea Company has held that all taxations which imposed restriction are hit by Article 301. The Automobile Transport (supra) where correctness of Atiabari Tea Co. was questioned reiterated that taxation is included in Part XIII. Following was observed by Das J.

> " ...in view of the provisions of Article 245, we find it difficult to accept the argument that the restrictions in Part XIII of the Constitution do not apply to taxation laws... "

197. Both K. Subba Rao, J. and M. Hidayatullah, J. in their separate opinions have held that restriction by law of taxation is also hit by Article 301.

198. Learned Counsel for the States in support of their submission further contends that both the words i.e. 'tax' and 'restriction' have been used in Article 304(a) and Article 304(b) separately. Both the words are not interchangeable nor the scheme of Article 3 04 indicates that the word 'restriction' includes taxation. Learned counsel further submits that reading taxation into word 'restriction' as used in Part XIII is accepting an interpretation which fetters the plenary powers of legislation granted to the States under the Constitution.

199. All subsequent judgments of this Court have also proceeded on the premise that a tax legislation which impedes the freedom of trade, commerce and intercourse and is not saved by Article 302 to 304 is invalid. Apart from the reason which found favour in Atiabari Tea Company and Automobile Transport the following reasons reinforces our view that Part XIII covers all tax legislations which impede the freedom of trade, commerce and intercourse:

(a) The express use of word tax in Article 304(a) and 306 (as it existed before its repeal by Constitution's 7th Amendment Act, 1956) indicates that taxes were expressly included in Part XIII. Had the taxes, apart from as mentioned in 304(a) were not to be covered under Part XIII, Article 306 ought not to have been engrafted which permitted continuance of tax or duty on the import and export of the goods, in Part B States for a period not exceeding ten years from the commencement of the constitution. The framers of the Constitution were conscious that unless an overriding effect is given to taxes which are continuing in the State the same shall fall foul to Article 301.

(b) Article 302 uses the phrase, "Parliament may by law". Whereas Article 303 uses the phrase "neither Parliament nor the legislature of the State shall have power to make any law " Article 304 uses the phrase the legislature of a State "may by law". All laws framed by Parliament or State in exercise of legislative entries under VIIth Schedule are law. Article 302 – 304 contain exception according to which, freedom of trade, commerce and intercourse as guaranteed under Article 301 can be overridden. The word law is wide enough to include both fiscal and non-fiscal legislations.

(c) Article 303 imposes restriction on the legislative power of the Union as well as of the State with regard to trade and commerce. Article 303(1) provides that a State shall have no powers to make any law giving or authorising the giving of, any preference to one State over another, or making or authorising the making of, any discrimination between one State or another, by virtue of any entry relating to trade and commerce in any Lists of the VIIth Schedule. The legislative power of the State, which is restricted under 303(1) cannot be held to be confined only to law as referred to in 304(a) rather it can extend to a legislation by virtue of any entry relating to the trade and commerce in List II. From this, it is clear that tax legislation which are covered under Part XIII are not confined to only Article 304(a).

(d) In the event, the submission is accepted that all taxes are outside Part XIII except non-discriminatory taxes as permitted under Article 304(a), the same will lead to giving right to the Parliament and State Legislature to pass facially non-discriminatory laws but creating restrictions on trade and commerce by other means by providing arbitrary procedure and various other kind of restraints. The taxation which can impede the trade, commerce and intercourse thus cannot be confined only to non-discriminatory taxation. Even, non-discriminatory taxes which create restraint on trade have to be held to fall foul to Article 301. In the

event of accepting the above submission, the restraint in trade by other means of taxation shall be out of reach of Part XIII, which is never the intention of the framers of the Constitution.

(e) Article 304(a) covers imposition of taxes on goods imported from other States. Article 304(a) does not apply to imposition of taxes on intra-State trade. Can it be presumed that intra-State taxation, if it contains restraint on trade between one local area to another local area or is discriminatory, the same is outside the reach of Article 301? The answer is obviously no. Trade and commerce throughout the territory of India is to be free. Thus reach of Article 301 is not confined to taxation as contemplated by 304(a) rather Part XIII embraces in itself all kind of tax legislation, which contains restraint on trade, commerce and intercourse.

(f) Article 304(a) only covers taxes on goods imported from other State and Union Territories. List II of VIIth Schedule contains various other entries which empower the State to levy taxes. Entry 49 to Entry 62 enumerate various fields of taxing legislation. In the event, the submission is accepted that it is only taxes referred to under Article 304(a), are covered by Part XIII, all taxing legislations as enumerated in List II shall go out of reach of Part XIII. Whether Constitution framers contemplated that restriction in freedom of trade, commerce and intercourse can be imposed by the State by taxing legislation other than those referred to in 304(a), answer has to be negative. Other taxing legislation apart from those, mentioned in Article 304(a) are not immuned from restriction contained in Part XIII. For example, Entry 49 provides 'taxes on lands and buildings'. A State Legislation is passed imposing taxes on buildings where trade and commerce is carried, the effect of which is to impede the trade and commerce, can it be said that such tax legislation cannot be questioned as violating Article 301. The answer is that such legislation has also to comply with Article 301. Thus, Article 304(a) is not the only taxation which is covered by Part XIII. But it is only species of taxation which has been expressly indicated for carving out gateway for the State Legislature to impose tax which may not impede Article 301.

(g) Lastly, there are no provision in Part XIII which negate the applicability of Part XIII on taxes which operates as restriction to trade, commerce and intercourse. Something which is not expressly excluded in Part XIII cannot be excluded by way of interpretation. Whether restriction used under Part XIII includes tax legislation"

200. While discussing the subject 'Legislative History and Debates in Constituent Assembly' on freedom of trade, commerce and intercourse, we have already found that taxes were treated as restrictions on freedom of trade and commerce and it was further comprehended that restrictions on freedom of trade and commerce can be put by taxation also. Apart from above, there are following reasons which support our conclusion that word 'restriction' used in Part XIII includes tax legislation:

"(i) The textual interpretation of Part XIII itself indicates that taxes were contemplated to be included in word 'restriction'. The heading of Article 304 reads 'restrictions on trade, commerce and intercourse among States'. Although the heading refers to 'restrictions' but Article 304(a) uses the word 'any tax'.

(ii) The same conclusion is drawn from the Article 306 as it was enacted. Article 306 also contained a heading 'power of certain States in Part B of the Ist Schedule to impose restriction on 'trade and commerce'.' Article 306 contained a non obstante clause empowering Part B, States to continue to levy and collect such tax, subject to an agreement with the Government of India which was being levied at the time of commencement of the Constitution. The heading only referred to restrictions on trade and commerce whereas section referred to imposition of taxes. Thus textual interpretation of Article 304 and 306 clearly indicates that word 'restriction' was used as inclusive of taxes. Article 19(2) to Article 19(6). The word 'restriction' has also been used in Part XIII. The word 'restriction' appearing in Part III and Part XIII have the same meaning and should be construed as such. It is well known principle of statutory interpretation of Constitution that when the same words or phrases are used in different parts of the Constitution, the same meaning should be ascribed to such word unless the context demands otherwise. It is sufficient to refer to judgment of this Court in Kesavananda Bharati Versus State of Kerala, (1973) 4 SCC 225. Justice "Hegde and Mukherjea" in Para 640 had reiterated the above principle as:

"...it is one of the accepted rules of construction that the courts should presume that ordinarily the Legislature uses the same words in a statute to convey the same meaning. If different words are used in the same statute, it is reasonable to assume that, unless the context otherwise indicates, the Legislature intended to convey different meanings of those words.

This rule of interpretation is applicable in construing a Constitution as well... "

(iv) This Court had occasion to consider the word 'restriction' as used in Part III in context of taxing legislation, namely, Travancore-Cochin Land Tax Act, 1955 in K.T. Moopil Nair Versus State of Kerala and Anr., 1961 (3) SCR 77. When word 'restriction' as used in Part III has been held to include restriction by tax legislation also, we see no reasons for not reading tax legislation in word 'restriction' in Part XIII also. The word restriction has to be given same meaning as contained in Part XIII.

(v) Article 302 contains a heading 'power of Parliament to impose restrictions on trade, commerce and intercourse'. Article further provides that the Parliament by laws impose such restrictions on the freedom of trade, commerce and intercourse. Under Article 302 tax laws enacted by the Parliament, namely, Central Sales Tax Act, 1956 has been saved by this Court in State of Madras Vs. N. K. Nataraja Mudaliar 1968 (3) SCR 829. Bachawat, J., agreeing with the majority opinion stated as following:

"I may add that even assuming that the Central Sales Tax Act, 1956 is within the mischief of Art. 301, it is certainly a law made by Parliament in the public interest and is saved by Art. 302. find nothing in the Act which offends Art. 303(1) ."

(vi) The word 'restriction' used in Article 304(b) has also to be interpreted in the same manner. As noted above, Article 304(a) covers limited field to taxes on goods imported from other States. Article 304(a) does not cover intra-State taxation. An Intra-State Tax Legislation, impeding the freedom of trade, commerce and intercourse between one local area to another local area, has also to fall foul to Article 301. There may be valid reasons for State legislature to impose restriction with regard to intra-State taxation and there may be reasons for fixing different rate of taxes with regard to different local areas, which may be a restriction on the trade, commerce and intercourse. Article 304(b) is a
window by which a State can impose reasonable restriction in public interest. In the event, it is held that Article 304(b) does not cover taxes, the State will have no mechanism to impose restriction on intra-State trade and with regard to imposition of taxes other than goods imported from other States, which can not be the intention of framers of the Constitution. From the foregoing discussion, we arrive at following conclusions:

i. Part XIII of the Constitution covers tax legislation which restrict freedom of trade, commerce and intercourse.

ii. The word 'restriction' used in Part XIII includes tax legislations also.

E. LEGISLATIVE HISTORY AND CONSTITUENT ASSEMBLY DEBATES RELATING TO ARTICLE 304(a)AND 304(b)

201. By Section 297 of Government of India Act, 1935, the certain restrictions on the Provincial Legislature and the Government were imposed to ensure freedom of trade, as has already been noted above. When the Constituent Assembly proceeded to finalise the provisions of the Constitution on freedom of trade and commerce, the Legislative Scheme as such under Section 297 was already enforced. By Section 297(1)(a) the State Legislature and Government were prohibited from restricting the entry into, or export from, the Province of goods of any class or description; and further by Section 297(1)(b) imposition of any tax, cess, toll, or due which was discriminatory in nature was prohibited. As noted above the Sub-Committee on the fundamental rights in its report dated 3rd April, 1947 has proposed the following clause with regard to trade, commerce and intercourse:

"13.Subject to regulation by thelaw of the Union, trade,commerce, and intercourse among the units, whether by means of internal carriage or by ocean navigation, shall be free Provided that any unit may by law impose reasonable restrictions thereon in the interest of public order, morality or health. "

202 . Shri Alladi Krishnaswami Ayyar put a note on the above Clause 13 which was to the following effect:

> "Clause 13. Though I have been in some measure responsible for the inclusion of this clause I feel it must be made clear That : (1) goods from other parts of India than in the units concerned coming into the units cannot escape duties and taxes to which the goods produced in the units themselves are subject."

203. While submitting the report of the Sub-Committee date 16th April, 1947, Chairman of Fundamental Rights Sub-Committee stated that although every citizen is entitled to free trade Commerce and intercourse within the territories of the Union unburdened by any internal duties or taxes of customs but many Indian States depend upon such duties and taxes for a
considerable part of their revenue and cannot do without it all at once. It was stated that some agreement had to be made with those States in the light of their existing rights with a
view to their ultimate elimination within a period to be prescribed by the Constitution.

204 . Thus, with regard to the taxes the above view was reiterated by Shri Vallabhbhai Patel in the report of Advisory Committee submitted on 23rd April, 1947. Shri C. Rajagopalachari in Advisory Committee proceeding had stated :

> "I think we should add to 14(1) that this shall not be a bar to the imposition of taxes for genuine purposes of revenue." Before the Constituent Assembly the Advisory Committee had recommended Clause 10 regarding trade, commerce and

> "10. Subject to regulation by the law of the Union trade, commerce, and intercourse among the Units by and between the citizens shall be free: Provided that any Unit may by law impose reasonable restrictions in the interest of public order, morality or health in or in an emergency: Provided that nothing in this section shall prevent any Unit from imposing on goods imported from other Units the same duties and taxes to which the goods produced in the Unit are subject:
>
> Provided further that no preference shall be given by any regulation of commerce revenue by a Unit to one Unit over another."

205. The above Clause 10 came for discussion before the Constitution Assembly on Ist May, 1947. Shri K.M. Munshi before the Constituent Assembly placed amendment for adding The words 'and under regulations and conditions which are non-discriminatory'. The Constituent Assembly approved Clause 10 by accepting amendment proposed by Shri K.M. Munshi. Third proviso thus was approved as follows:

> "Provided that nothing in this section shall prevent any Unit from imposing on

goods imported from either Units the same duties and taxes to which the goods produced in the Unit are subject and under regulations and conditions which are non-discriminatory."

206 . The above proviso was included in the Draft Constitution published in October, 1947 and thereafter draft as finalized by Drafting Committee provided for restriction on trade, commerce and intercourse by Article 244 which was of the following effect:

"244. Notwithstanding anything contained in Article 16 or in the last preceding Article of this Constitution, it shall be lawful for any State-

(a) to impose on goods imported from other States any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and

(b) to impose by law such reasonable restrictions on the freedom of trade, commerce or intercourse with that State as may be required in the public interests: Provided that during a period of five years from the commencement of this Constitution the provisions of clause (b) of this article shall not apply to trade or commerce in any of the commodities mentioned in clause (a) of Article 306 of this Constitution."

207. Article 244 which was subsequently approved as Article 274D in Part XA and was adopted as Article 304 of the Constitution. The above indicates that initially the provisions empowered the State "to impose on goods imported from other States any tax to which similar goods manufactured or produced in that State are subject", and by an amendment another restriction i.e. "so, however, as not to discriminate between goods so imported and goods so manufactured or produced" was added. Article 304(a) contains both the above restrictions on the legislative power of the State. The proceedings of the Constituent Assembly, thus, clearly indicate that both the above conditions have been added in the provision as separate conditions and the second condition was added by way of amendment in addition to the first condition which already existed. Now coming to Article 304(b) which was similar to draft Article 244(b), Constituent Assembly debated the above Article threadbare.

208. Dr. Ambedkar had moved motion for inclusion of a separate Part XA wherein Article 244 was deleted and substituted by a draft Article 274D which was to the similar effect. In the Constituent Assembly Debates dated 3rd December,1948 the draft Article 16 which was included in the fundamental rights came for consideration. In the context of the above discussion objections were raised to Article 244 by Shri C. Subramanian. Shri C. Subramanian raised objection that a State Legislature has been given power to impose certain taxes and impose certain restrictions which clearly means that no fundamental right is reserved for free trade and commerce. The objection of Shri C. Subramanian was taken in the
following words:

"You will find, Sir, that in article 244, even though it might be inter-state trade and commerce, the State Legislature is given certain powers to impose certain taxes and impose certain restrictions. Having this in mind, if we come to Article 16, we find the words "subject to the provisions of article 244 of this Constitution", that is, even in respect of inter-state trade and commerce, the State Legislature has been given certain powers and that is not touched by this article. Therefore leaving that, the article would read "subject to the provisions of any law made by Parliament, trade and commerce and intercourse through the territory of India shall be free". I really fail to understand how this can be a fundamental right and whether there is any right at all reserved.

The very conception of a fundamental right is that there is a certain right taken out of the province of the legislature either of the Union or of the State."

209 Dr. Ambedkar replying to the above objection with regard to Article 244 stated as follows:

"With regard to the other argument, that since trade and commerce have been made subject to article 244, we have practically destroyed the fundamental right, I think I may fairly say that my friend Mr. Subramaniam has either not read article 244, or has misread that article. Article 244 has a very limited scope. All that it does is to give powers to the provincial legislatures in dealing with inter-state commerce and trade, to impose certain restrictions on the entry of goods manufactured or transported from another State, provided the legislation is such that it does not impose any disparity, discrimination between the goods manufactured within the State and the goods imported from outside the State. Now, I am sure he will agree that that is a very limited law. It certainly does not take away the right of trade and commerce and intercourse throughout India which is required to be free."

210. As stated above Article 244 was akin to Article 274D which was sought to be added in new Chapter and came for discussion on 8th September, 1949 before the Constituent Assembly. Dr. B.R. Ambedkar by moving a motion in support of Chapter XA giving a complete picture of the Articles now put at one place stated as follows:

"I should also like, to say that according to the provisions contained in this part it is not the intention to make trade and commerce absolutely free, that is to say, deprive both Parliament as well as the States of any power to depart from the fundamental provision that trade and commerce shall be free throughout India. The freedom of trade and commerce has been made subject to certain limitations which may be imposed by Parliament or which may be imposed by the Legislatures of various States, subject to the fact that the limitation contained in the power of Parliament to invade the freedom of trade and commerce is confined to cases arising from scarcity of goods in any part of the territory of India and in the case of the States it must be justified on the ground of public interest.

The action of the States in invading the freedom of trade and commerce in the public interest is also made subject to a condition that any Bill affecting the freedom of trade and commerce shall have the previous sanction of the President; otherwise, the State would not be in a position to undertake such legislation."

211. Pandit Thakur Das Bhargava raised various amendments. Pandit Bhargava moving his amendments stated:

"Now, in regard to these amendments my submission is that the way in which I look at the subject is different from the way in which Dr. Ambedkar look at it. According to me, these rights of trade and commerce and intercourse should be absolute and only circumscribed by provisions relating to emergencies while in his view, the power of the Central Government as well as of the provincial Governments should be there, and these rights should be qualified We have already passed article 16 which runs thus:

"Subject to the provisions of article 244 of this Constitution and of any law made by Parliament, trade, commerce and intercourse throughout the territory of India shall be free."

This article yet stands as it is. There has so far been no amendment that it stands abrogated. The existence of this article in the Chapter on Guaranteed Rights assures us that this is a fundamental right. The nature of this fundamental right has been,
I know, curtailed to a great extent by the use of the words "and of any law made by Parliament". Subject to this, this fundamental right has been guaranteed to the citizens of India by the Constitution we have already passed.

212. With regard to Article 274D, Pandit Thakur Das Bhargava raised serious objections to sub-cluase (b), following was stated by Pandit Bhargava"

"Similarly Sir, in regard to article

2 74D, I have no objection to clause (a); but so far as (b) is concerned, this is the clause to which I object most seriously. I think this is unnecessary because when the powers are given to the Parliament as originally they were given to the Parliament, I have no objection. The Parliament shall have to consider it from the general standpoint, from the standpoint of the whole of India, whereas a State is bound to consider it from a parochial point of view, from the point of view of the State and therefore, this mutual jealousy is bound to arise if we allow these powers to the State. Therefore, the policy of the Government should be that so far as the State is concerned, they should not be allowed to exercise that power unless it be through Parliament. If a State is empowered to use its powers under clause (a) I have no quarrel as it will be a salutary power; but if you allow clause (b) to remain as it is, I do not understand what it may lead to. "

213. Prof.Shibban Lal Saksena also supported the amendments moved by Pandit Bhargava.

214. Shri T.T. Krishnamachari replying the objections of Pandit Bhargava stated following with regard to Article 274D:

> "So far as 2 74D is concerned, my honourable Friend Pandit Thakur Das Bhargava will either wholly amend it in such a way as to completely change its shape or completely eliminate it. I feel that it arises—I have no doubt—from a particular bitter experience of his in which a Provincial Government has not executed its duty towards its people in the proper way. But hard cases do not always mean bad law. There is not reason for us to completely shut out discretion or the States in so far as the Central Government will have enough power not merely to have a uniform fiscal policy but also as far as possible to have a uniform economic policy. And that is provided by the fact that the President's previous sanction is necessary in regard to any legislation undertaking by the State under clause (b) of 274D. Pandit Thakur Das Bhargava: Is it not exactly the reason why the Provinces and the State Legislatures should not be given the power? Shri T. T. Krishnamachari: That is exactly the reason why they should be given the power. The State should be given a certain amount of right in this matter and the only reason why the Centre should interfere is to see that the economic and fiscal policy of the Centre is not unduly interfered with, and to the extent that it cannot be interfered with the State must be given a reasonable amount of power to order its own affairs."

215. Shri Alladi Krishnaswami Ayyar replying the objections of Pandit Bhargava with regard to Article 274D stated as follows:

> "Then I am surprised at exception being taken to the terms of article 274D. It does not give any unfettered power to the States.The proviso clearly lays down—
>
> "No Bill or amendment for the purposes of clause (b) of this article shall be introduced or moved in the legislature of the State nor shall any Ordinance be promulgated for the purpose by the Governor or Ruler of the State without the previous sanction of the President".
>
> Therefore, if on account of parochial patriotism or separatism, without consulting the larger interests of India as a whole if any Bill or amendment is introduced, it will be open to the President, namely, the Cabinet of India to withhold sanction. This is therefore a very restricted power that is conferred on the legislature of a State. After all what is the nature of the power given ? The power is confined to imposing such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest therefore the President who has to grant sanction will have the opportunity to see that the legislation is in the public interest and that the restriction imposed is reasonable. It is not possible to devise a water-tight formula for the purpose of defining these restrictions."

216. Replying the Debate, Dr. B.R. Ambedkar stated that he cannot usefully add anything to what Shri T.T. Krishnamachari And Shri Alladi Krishnaswami Ayyar had said. Article 274D was added to the Constitution by negating the amendments. From the above, it is clear that objections with regard to Article 274D sub-clause (b) which is now Article 304(b) were raised before the Constituent Assembly but the objections were overruled by retaining Article 274D sub-clause (b) which is now Article 304(b), thus, inclusion of Article 304(b) in the Constitution was consequent to well deliberated Constitutional Scheme and was accepted as restriction on the power of State to have uniform fiscal policy and uniform an economic policy.

F. INTERPRETATION, SCOPE AND AMBIT OF ARTICLE 304(a) AND ARTICLE 304(b)

217. Article 304 of the Constitution reads as follows:

> "304. Restrictions on trade, commerce and intercourse among States.— Not with standing anything in article 301 or article 303, the Legislature of a State may by law—
>
> (a) impose on goods imported from other States or the Union territories any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and
>
> (b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest: Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President. "

218. 'Article begins with a non obstante clause i.e. 'notwithstanding anything in Article 301 or 303'. Article 301 declares that trade, commerce and intercourse throughout the territory of India shall be free. Article 304 has overriding effect over Article 301, Article 304 provides for 'restrictions on trade, commerce and intercourse' amongst States, as is clear by its heading, which otherwise would not have been permissible under 301. Article 304 also overrides restrictions on the legislative power of the State as provided for in Article 303.

219. Article 304 empowers legislature of a State by law to impose on goods imported from other States or Union Territories any tax. A plain reading of Article 304(a) indicates that it contains certain conditions for imposition of taxes on goods imported from other States. Article 304(a) can be divided in following parts:-

i . Impose on goods imported from other States or Union Territories;

ii. Any tax to which similar goods manufactured or produced in that State are

subject;

iii. So, however, as not to discriminate between goods so imported and so manufactured or produced;

220. We have already noted, while noticing the proceeding before the Constituent Assembly that in the initial draft corresponding to 3 04 (a) the condition iii, i.e., "as not to discriminate between goods so imported and goods so manufactured or produced" was not there which was added by an amendment brought by Shri K. M. Munshi. Thus (ii) and (iii) Part of Article 304, as noted above contains two separate and independent conditions for invoking 304(a). Learned counsel for the States have submitted that the main content of Article 304(a) is imposition of non-discriminatory taxes. It is contended that in event, there are no similar goods manufactured or produced in the State to the goods which are imported there is no question of discrimination and State is free to tax imported goods, which are not produced or manufactured in the State. On first blush, the submission appears to be attractive but on a deeper scrutiny it merits rejection. Article 304 is, in nature of enabling provisions to the State, to impose taxes on goods imported from other States. Framers of the Constitution had stated that the goods coming from other parts of the India in the units concerned cannot escape duties and taxes to which the goods produced in the units are subject. There is specific purpose and object in enabling the State to impose tax on goods imported from other States only when similar goods manufactured or produced in that State are subject. The object is that trade and commerce throughout the territory of India has to be free, as required by Article 301 and limited power to State was given to tax the outside goods when local goods are subject to taxes. In event, locally manufactured or produced goods are not subject to any tax, State has no jurisdiction to impose tax on similar goods coming from other States. Tax on the locally manufactured or produced goods is condition precedent for imposing tax on similar goods coming from other States. Idea is that when State does not tax its locally manufactured or produced goods, similar goods coming from out of the State be permitted a free flow which is a part of freedom guaranteed under Article 301.

221. The last condition that 'so, however, as not to discriminate between goods so imported and goods so manufactured or produced... " is another limb of restriction which prohibits the State from discriminating in imposing taxes on imported goods as compared to goods manufactured or produced locally. The question of discrimination shall arise only when first condition that is locally manufactured or produced goods are taxed by a State. In event, a particular good is not produced or manufactured in a State, State cannot be allowed to impose tax on goods coming from other States. First condition that is, taxing of the local goods being not fulfilled, the question of discrimination, does not arise. We are thus of the considered opinion that power under Article 304(a) for imposing taxes on the imported goods can be exercised by a State only when similar goods manufactured or produced locally are subject to tax. When the similar goods are not subject to tax or similar goods are not available in the State, the State is obliged to permit free flow of goods from other States which is cardinal principle enshrined in Article 301 and the relaxation to the States has been given only on a condition that State imposes taxes both on local goods and outside goods. Article

304(a) came for consideration before this Court in several cases including the Constitution Bench of this Court in *State of Madhya Pradesh Vs. Bhailal Bhai and Others*[29] in the above case the State has filed an appeal against judgment of the High Court of M.P. filed by the assessee permitting the refund of the tax assessed and collected from them holding assessment and collection as violative of Article 301 and not being saved by 304(a). The writ petitioners were carrying business of sale of tobacco in accordance with the notifications issued by the State Government, in the notification in question the tax was imposed only on imported tobacco and not on home grown tobacco which was noticed by the High Court in the judgment in following words:

> "The High Court was of opinion on a consideration of the notification under which the tax was assessed that it imposed a tax only on imported tobacco and not on home grown tobacco and so it did not come within the special provisions of Art. 304(a) of the Constitution and consequently the infringement of Art. 301 of the Constitution which resulted from the imposition of a tax on import of goods made the provisions void in law. The prayer for refund was allowed in the applications out of which C.A. Nos. 362-377, C.A. Nos. 861-867 of 1962 and C.A. No. 25 of 1963 have arisen. The prayer was rejected in the remaining applications. In the present appeals the State of Madhya Pradesh challenges the correctness of the High Court's decision that the taxing provision was unconstitutional and void and also the orders for refund made in some of the petitions mentioned above. "

222 . This Court came to conclusion that similar goods manufactured or produced in the State of the Madhya Bharat have not been subject to the tax which tobacco imported from other States have to pay hence tax was not saved under 304(a), affirming the judgment of the High Court this Court held as follows:

> "There can, therefore, be no escape from the conclusion that similar goods manufactured or produced in the Sate of Madhya Bharat have not been subjected to the tax which tobacco leaves, manufactured tobacco and tobacco used for Bidi manufacturing, imported from other States have to pay on sale by the importer. This tax is, therefore, not within the saving provisions of Art. 304(a). As already pointed out it contravenes the provisions of Art. 301 of the Constitution. The tax has therefore been rightly held by the High Court to be invalid. It is clear that the assessment of tax under these notifications was thus invalid in law. "

223. In another Constitution Bench judgment, Kalyani Stores Vs. State of Orissa and Others 1966 1 SCR 865 Article 304(a) again came for consideration. In the above case, the petitioners have challenged the notification dated 31 March 1961 issued under Bihar & Orissa Excise Act, 1915 by which

224 . The petitioners were asked to pay duty at the rate of Rs. 30, in respect of stocks of liquor found in the shop after April 1, 1961. The petitioners challenged the legality of the levy by filing a writ petition, the following contention was raised before this Court:

> "The appellants contended, inter alia that the State could levy under s.27 of the Bihar and Orissa Act duty on excisable articles produced or manufactured in the

State and a countervailing duty on excisable articles imported into the State, imposed with a view to equalize the burden on the imported articles with the burden on manufactured articles in the State, but no countervailing duty on liquor imported could be levied if there was in the year of licence no liquor, similar to the imported liquor, manufactured within the State, and as there was no distillery in the State manufacturing "foreign liquor" the levy of countervailing duty was without authority of law. "

225. The writ petition was dismissed by the High Court justifying the levy of duties of excise as countervailing duties under Entry 51 List II in VIIth Schedule. The judgment came to be challenged before this Court. This Court negativated the view of the High Court, justifying the levy as countervailing duty in following words:

"The fact that countervailing duties may be imposed at the same or lower rates suggests that they are meant to counterbalance the duties of excise imposed on goods manufactured in the State. They may be imposed at the same rate as excise duties or at a lower rate, presumably to equalise the burden after taking into account the cost of transport from the place of manufacture to the taxing State. It seems, therefore, that countervailing duties are meant to equalise the burden on alcoholic liquors imported from outside the State and the burden placed by excise duties on alcoholic liquors manufactured or produced in the State. If no alcoholic liquors similar to those imported into the State are produced or manufactured, the right to impose counterbalancing duties of excise levied on the goods manufactured in the State will not arise. It may, therefore, be accepted that countervailing duties can only be levied if similar goods are actually produced or manufactured in the State on which excise duties are being levied. "

226. This Court held that exercise of power under Article 304(a) can only be effective if the tax duty is imposed on goods imported from other States and the tax or duty imposed
on similar goods manufactured or produced in that State are such. This Court held as no foreign liquor is manufactured or produced in the State of Orissa, power to legislate given under Article 304(a) is not valid and following was laid down:

"Exercise of the power under Art. 304(a) can only be effective if the tax or duty is imposed on goods imported from other Sates and the tax or duty imposed on similar goods manufactured or produced in that State are such that there is no discrimination against imported goods. As no foreign liquor is produced or manufactured in the State of Orissa the power to legislate given by 'Art. 304 is not available and the restriction which is declared on the freedom of trade, commerce or intercourse by Art. 301 of the Constitution remains unfettered."

227. In the above two Constitution Bench judgments, this Court have clearly struck down levy of taxes on import of goods, when there was no taxes levied by State on the goods locally manufactured or produced or those goods were not locally available.

228. The question of discrimination between tax imposed on the imported goods and

that of locally manufactured or produced goods is another factor, on which the levy can fall foul. In Firm A.T.B. Mehtabmajid and Company Vs. State of Madras and Anothers 1963 SCR Supl.(2) 435 a question of discriminatory levy under Article 304(a) was considered.

229. In a writ petition under Article 32 of the Constitution filed in this Court, rule 16 of Madras General Sales Tax (Turnover and Assessment Rules, 1939) was under challenge.
Petitioner was a dealer in hides and skins who used to sell the hides and skins taken from outside the State of Madras as well as those taken from inside the State. Case of the petitioner was to the following effect:

> "It is contended for the petitioner that the effect of this rule is that tanned hides or skins imported from outside the State and sold within the State are subject to a higher rate of tax than the tax imposed on hides or skins tanned and sold within the State, in as much as sales tax on the imported hides or skins tanned outside the State is on their sale price while the tax on hides or skins tanned within the State, though ostensibly on their sale price, is, in view of the proviso to cl. (ii) of sub-r. (2) of r. 16. really on the sale price of these hides or skins when they are purchased in the raw condition and which is substantially less than the sale price of tanned hides or skins. Further, for similar reasons, hides or skins imported from outside the State after purchase in their raw condition and then tanned inside the State are also subject to higher taxation than hides or skins purchased in the raw condition in the State and tanned within the State, as the tax on the former is on the sale price of the tanned hides or skins and on the latter is on the sale price of the raw hides or skins. Such a discriminatory taxation is said to offend the provisions of the Art. 304(a) of the Constitution. Similar are the contentions for the intervenes in the case."

230. This Court held that taxing laws can be restrictions on the trade, commerce and intercourse and the tax which is affecting and discriminating goods of one State and goods of another may affect the free flow of trade and offend Article 301 and will be followed only if it comes within the term of Article 304(a). This Court held as follows:

> "It is therefore now well settled that taxing laws can be restrictions on trade, commerce, and intercourse, if they hamper the flow of trade and if they are not what can be termed to be compensatory taxes or regulatory measures. Sales tax, of the kind under consideration here, cannot be said to be a measure regulating any trade or a compensatory tax levied for the use of trading facilities. Sales tax, which has the effect of discriminating between goods of one State and goods of another, may affect the free flow of trade and it will then offend against Art. 301 and will be valid only if it comes within the terms of Art. 304(a). Article 304(a) enables the Legislature of a State to make laws affecting trade, commerce and intercourse. It enables the Imposition of taxes on goods from other States if similar goods in the State are subjected to similar taxes, so as not to discriminate between the goods manufactured or produced in that State and the goods which are imported from other States. This means that if the effect of

the sales-tax on tanned hides or skins imported from outside is that the latter becomes subject to a higher tax by the application of the proviso to sub-rule of r. 16 of the Rules, then the tax is discriminatory and unconstitutional and must be struck down."

231. This Court allowed the petition by recording the following conclusion:

"We are therefore of opinion that the provisions of r. 16(2) discriminate against the imported hides or skins which had been purchased or tanned outside the State and that therefore they contravene the provisions of Art. 304(a) of the Constitution.

2 32 . The law laid down by the above Constitution Bench judgment of this Court reaffirms our view that for enabling a State to make a law under Article 304 (a), following two preconditions, which are independent of each other have to be satisfied:

a. Imposes on goods imported from other States or the Union Territories any tax to which similar goods manufactured or produced in that State are subject.

b. So, however, as not to discriminate between goods so imported and goods so manufactured and produced;"

233. During the course of his submission Shri Salve has referred to enactments of State of Tamil Nadu, States of Kerala, State of Assam and State of Andhra Pradesh. Referring to Tamil Nadu Entry Tax on Entry of Goods into Local Areas Tax Act, 2001, Shri Salve has contended that under Section 3 sub-section 2, tax is payable by an importer. Entry of goods into local area was defined as entry of scheduled goods into a local area from any place outside the State for consumption, use or sale therein. His contention was that enactment clearly imposes Entry Tax only on goods imported and there was no Entry Tax on the local goods which clearly violates Article 304(a) of the Constitution of India.

234. We find force in the submission of Shri Salve, which is supported by the Constitution Bench judgments in State of Madras Vs. Bhailal Bahi and Kalyani Stores Vs. State of Orissa and Others. Imposition of tax only on imported goods when no such tax is levied on local goods violates Article 304(a). The Division Bench of the *Madras High court in ITC Ltd. Vs. State of Tamil Nadu and Others*[29] Madras has struck down the enactment. To the same effect, submissions have been made by Shri Salve with regard to Entry Tax enactments of State of Kerala, State of Andhra Pradesh and

235. Articles 304(a) and 304(b) are joined with conjunction 'and'. Learned counsel for the petitioners who have challenged the various enactments of various States contend that clauses (a) and (b) of Article 304 have to be read conjunctively as they are not mutually exclusive. It is contended that tax Legislation by State has to comply both clauses (a) and (b) whereas learned counsel for the States contends that word 'and' has to be read disjunctively. Legislation which is in accordance with Article 304(a) need not be in compliance of Article 304(b). Learned counsel for the States has further

contended that in fact Article 304 (b) does not include tax legislation, hence, it is another reason to contend that tax legislation complying Article 304(a) need not to comply Article 304(b).

236. We need to first advert to true meaning and purpose of word 'and' which joins both clauses (a) and (b) of Article 304. According to the principles of statutory interpretation the word 'and' is normally used conjunctively and word 'or' is normally used disjunctively but at times they are used as vice versa to give effect to the manifest intention of the Legislation as disclosed in the context of the Legislation. This Court in large number of cases have read word 'and' as 'or'. In 1969(1) SCR 219, this Court had occasion to consider the word 'and' as used in Section 3(b) of the Drugs Act, 1940. Section 3(b)(1) which defines the Drug provided as:

> "The definition of "drug" contained in S.3(b) is in the following terms :-
>
> (i) all medicines for internal or external use of human beings or animals and all substances intended to be used for or (in the diagnosis, treatment), mitigation or prevention of disease in human beings or animals other than medicines and substances exclusively used or prepared for use in accordance with Ayurvedic or Unani systems of medicine "

237. The issue before this Court as to whether word 'and' used in the Section 3(b)(1) between words "medicines and substances" be read as 'or', this Court laid down the following:

> "Now if the, expression "substances" is to be taken to mean something other than "medicine" as has been held in our previous decision it becomes difficult to understand how the word "and" as used in the definition of drug in s. 3 (b) (i) between "medicines" and "substances" could have been intended to have been used conjunctively. It would be much more appropriate in the context to read it disjunctively. In Stroud's Judicial Dictionary, 3rd Ed. it is stated at page 135 that "and" has Generally a cumulative, sense, requiring, the fulfillment of all the conditions that it joins together, and herein it is the antithesis of "or". Sometimes, however, even in such a connection, it is, by force of a contents, read as "or". Similarly in Maxwell on Interpretation of Statutes, 11th Ed., it has been accepted that "to carry out the intention of the legislature it is occasionally found necessary to read the conjunctions 'or' and 'and' one for the other".

238. We may revert to the Constitutional Scheme to find out the true purpose and object of the provision. Article 304 is an exemption granted to the State when State can impose taxes and impose restrictions on the freedom of trade and commerce which freedom is guaranteed under Article 301 of the Constitution of India. Article 304 begins with the words "Notwithstanding anything in Article 301 or Article 303, the Legislature of a State may by law—". Two sub-clauses (a) and (b) are enabling powers given to the State by which taxes can be imposed on imported goods and restrictions can be imposed on the freedom of trade, commerce or intercourse. In the event, we tend to

read conjunction 'and' as 'or' it may mean that the State may exercise only one of the enabling powers as given in the clauses (a) and (b). It is not the intention of Article 304 to empower the State to only exercise either of the powers, the clear intendment of the State is that the State may by law impose on goods imported from other States any tax-clause (a);and impose reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State – clause (b). The use of word 'may' in the beginning of Article 304 indicates that the power is enabling and States are entitled to exercise either or both the powers as may be required in the facts of the case.

239. Further, there is no compulsion on the State to exercise powers given in clauses (a) and (b) both. The State may choose to exercise only power given in clause (a) or power given in clause (b). We, thus, are not persuaded to accept the contention that whenever State makes a law under clause (a) it has necessarily to comply clause (b) also. Shri Arvind P. Datar, learned senior counsel, has submitted that use of word 'and' between clauses (a) and (b) of Article 304 is joint and several and has to be read as and/or. In support of his submission he has placed reliance on the Statutory Interpretation, Second Edition by RUTH SULLIVAN. Learned Author has expressed following views on 'And' or 'Or':

> "2) "And" and "Or"
> a) Joint or Joint and Several "and" Both "and" and "or" are inherently ambiguous. "And" is always conjunctive in the sense that it always signals the cumulation of the possibilities listed before and after the "and". However, "and" is ambiguous in that it may be joint or joint and several. In the case of a joint "and", every listed possibility must be included: both (a) and (b); all of (a), (b), and (c). In the case of a joint and several "and", all the possibilities may be, but need not be, included:
> (a) or (b)
> or both; (a) or (b) or (c), or any of two, or all three. In other words, the joint and several "and" is equivalent to "and/or".
>
> Which meaning is appropriate depends on the context. When "and" is used before the final item in a list of powers, for example, it is joint and several:
>
> To carry out the purposes of this Act, the Governor in Council may make regulations respecting
>
> (a) the conditions on which licences may be issued;
>
> (b) the information and fees that firearm vendors may be required to furnish; and
>
> (c) the annual fees that firearm owners may be charged. In this provision the Governor in Council is empowered to make regulations on any one or more of the listed subjects. However, notice what happens if "may" is replaced by "shall". If the Governor in Council is obliged to make regulations respecting (a) conditions (b) information and (c) fees, the joint and several "and" becomes joint."

240. We find force in the submission and we are of the view that word 'and' between

clauses (a) and (b) has to be read as joint and several, both meaning can be assigned as per
requirement of a State Legislature. One of the submissions raised by the learned counsel of the petitioners as note above is that whenever State Legislature imposes a tax by law under clause (a), it has necessarily to go through the procedure provided under clause 304(b), since both the clauses are conjunctive and require compliance. We are not inclined to accept the extreme submission that in each and every case whenever law is framed under clause (a) procedure under clause (b) has to be complied with. The proviso to clause (b) that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President, is confined to clause (b) which indicates that Constitutional Scheme does not provide that it is necessary to comply for framing law under clause (a)the requirement of clause (b) also. We, however, hasten to add that there may be cases where a law which may conform the requirement under sub-clause (a) but still contains restrictions on the freedom of trade, commerce and intercourse, in that event, compliance of clause (b) may also be necessary, but a law framed in accordance with clause (a) imposing a tax which does not contain any restriction on the freedom of trade, commerce and intercourse as envisaged in clause (b) need not go through the procedure as contemplated by clause (b). We thus come to the conclusion that with regard to law made by State Legislature exercising the power under clause (a) of Article 304 which does not impose any restriction on the freedom of trade, commerce and intercourse need not comply with Article 304 (b). However, a law even though may comply with Article 304(a) but contains restrictions on the freedom of trade, commerce and intercourse has to obtain sanction of the President as contemplated by proviso to clause (b). The requirement of obtaining previous sanction of the President has to be decided in accordance with the nature and content of the State Legislation.

241. One of the submissions which has been emphatically pressed by Shri P.P. Rao and Shri Rakesh Dwivedi, learned senior counsel appearing for the States is that requirement of obtaining previous sanction of the President by the State Legislature erodes the sovereignty of the State Legislature of making law in the field allocated to them included in the VIIth Schedule read with Article 246 . It is contended that a State's taxing power is a sovereign power granted to the State and insisting for previous sanction of the President for framing a taxing legislation by the State erodes their sovereignty and is also against the federal structure of the Constitution. We in the foregoing paragraphs have elaborately considered the nature of federal structure of the Constitution of India, which is not a federal Constitution, as it is traditionally understood. This Court termed the Constitution of India as quasi-federal, mixture of federal and unitary elements, leaning more towards the latter, as noted above. The division of powers between Union and the State Legislatures is clearly defined and demarcated in the Constitutional Scheme. The Constitutional Scheme delineates the scheme of check and balances between the Union and States. Apart from Article 304(b) following are the other Constitutional provisions where Presidential sanction has been contemplated:

> “(1) 31-A. Saving of laws providing for acquisition of estates, etc.—
>
> (1) Notwithstanding anything contained in Article 13, no law providing for—

Xxxxxxxxxxxxxxxxxxx

Provided that where such law is a law made by the Legislature of a State, the provisions of this article shall not apply thereto unless such law, having been reserved for the consideration of the President, has received his assent.

(2) 31-C. Saving of laws giving effect to certain directive principles.—

Xxxxxxxxxxxxxxxxxx

Provided that where such law is made by the Legislature of a State, the provisions of this Article shall not apply thereto unless such law, having been reserved for the consideration of the President, has received his assent.

(3) 213. Power of Governor to promulgate Ordinances during recess of Legislature.—

Xxxxxxxxxxxxxxxxxx

Provided that the Governor shall not, without instructions from the President, promulgate any such Ordinance if —

(a) a Bill containing the same provisions would under this Constitution have required the previous sanction of the President for the introduction thereof into the
| Legislature; or

(b) he would have deemed it necessary to reserve a Bill containing the same provisions for the consideration of the President; or

(c) an Act of the Legislature of the State containing the same provisions would under this Constitution have been invalid unless, having been reserved for the consideration of the President, it had received the assent of the President; or

Xxxxxxxxxxxxxxxxx

(4) 254. Inconsistency between laws made by Parliament and laws made by the Legislature of States.—

Xxxxxxxxxxxxxxxxxx

(2) Where a law made by the Legislature of a State with respect to one of the matters enumerated in the Concurrent List contains any provision repugnant to the provisions of an earlier law made by Parliament or an existing law with respect to that matter, then the law so made by the Legislature of such State

shall, if it has been reserved for the consideration of the President and has received his assent, prevail in that State:

Xxxxxxxxxxxxxxxxxx

(5) 274. Prior recommendation of President required to Bills affecting taxation in |which States are interested.—

(1) No Bill or amendment which imposes or varies any tax or duty in which States are interested, or which varies the meaning of the expression "agricultural income" as defined for the purposes of the enactments relating to Indian income-tax, or which affects the principles on which under any of the foregoing provisions of this Chapter moneys are or may distributable to States, or which imposes any such surcharge for the purposes of the Union as is mentioned in the foregoing provisions of this Chapter, shall be introduced or moved in either House of Parliament except on the recomm-endation of the President.

(6) 288. Exemption from taxation by States in respect of water or electricity in certain cases.—

Xxxxxxxxxxxxxxxxxx

(3) The Legislature of a State may by law impose, or authorize the imposition of, any such tax as is mentioned in clause (1), but no such law shall have any effect unless it has, after having been reserved for the consideration of the President, received his assent; and if any such law provides for the fixation of the rates and other incidents of law by any authority, the law shall provide for the previous consent of the President being obtained to the making of any such rule or order.

242 . The above provisions are part of our Constitutional Scheme and could not be wished away by saying that such provisions impinge upon the sovereign power of the State. Power of a State Legislature to the above extent is expressly limited by Constitutional Scheme. Article 304(b) proviso is one of such Constitutional Schemes where the State power is restricted and limited to the above extent. The Constituent Assembly Debates, as noticed above, clearly bring about the rationale of introduction of the requirement of Presidential assent in respect of certain laws by which State Legislature put restriction on the freedom of trade, commerce and intercourse. We have noted above that in the Constituent Assembly there was serious objection raised against clause (b) of Article 304 and amendment was moved for deletion of clause (b) from the Constitution. The above amendment after great discussion was negatived by approving the limited restraint put on the State Legislature as engrafted in Article 304(b) proviso.

243. A Constitution Bench of this Court in *Kaiser-I-Hind Pvt. Ltd. and another vs. National Textile Corpn. (Maharashtra North) Ltd. and others*[30], has held that the power exercised by the President under Article 304(b) is in consonance with the federal structure of the Constitution. Doraiswamy Raju, J. agreeing with majority judgment

stated following in paragraph 77:

> "....The powers actually exercised by the President, at any rate under Articles 31-A, 31-C, 254(2) and 304(b) are a special constituent power vested with the Head of the Union, as the protector and defender of the Constitution and safety valve to safeguard the fundamental rights of citizens and federal structure of the country's polity as adopted in the Constitution "

244. The Sarkaria Commission was constituted to have re-look over the Centre-State relations under the Constitution of India. Sarkaria Commission dealt with "Legislative Relations" in Chapter II. The objections of State Governments were noted in para 2.40.01 to the following effect:

> "2.40.01 Some State Governments and a political party have asked for omission of Article 304, and, in the alternative, for deletion of the Proviso to Article 304(b). The arguments advanced are: "Whether the restrictions imposed by an Act of a State Legislature on the freedom of trade and commerce are reasonable and whether they are in the public interest for purposes of Article 304(b) are questions to be decided ultimately by the High Court or Supreme Court. If the High Court finds that the restrictions are unreasonable or opposed to the public interest, previous sanction of the President or his subsequent assent cannot cure the infirmity. If the legislation is otherwise valid and the restrictions are reasonable and in the public interest, his previous sanction will be a superfluity. In any case the requirement relating to the previous sanction of the President directly encroaches on the field assigned to the State Legislature...".

245. The objects of Article 304 (b) and its contents were noted in para 2.40.06 to the following effect:

> "2.40.06 The broad object of the provisions of Articles 301 and 304 is to ensure that the commercial unity of India is not broken up by physical and fiscal barriers erected by the State Legislatures through parochial or discriminatory exercise of their powers. The proviso to Article 304(b) enables the President to ensure, at the initial stage, that the State Legislation does not, by imposing unreasonable restrictions on trade, commerce or intercourse, endanger the commercial unity of the nation. It is true that clause (b) is not confined to inter-State trading activities, it extends to trade within the State, also. But intra-State trading activities often have a close and substantial relation to inter-State trade and commerce. State laws, though purporting to regulate trade within a State, may have inter-State implications. They may impose discriminatory taxes or unreasonable restrictions which impede the freedom of inter-State trade and commerce. That is why, both inter-State and intra-State trade have been made the subject of limitations on State legislative power under Article 304(b)."

246. The Sarkaria Commission in para 2 .40 . 07 has also recorded : "However, no instance of a Bill reserved under the Proviso to clause (b) of Article 304, which might have been vetoed by the President, has been cited." In para 2 .40 . 08 it was concluded:

"2.40.08. For these reasons, we cannot support the demand for amendment of Article 304, or omission of the Proviso to its clause (b)."

247. The Sarkaria Commission after hearing the States' point of view had specifically adverted to on Constitutional provisions contained in Part XIII of the Constitution. After elaborate consideration on the subject in Part XIII "trade, commerce and intercourse within the Territory of India" in paragraph 18.3.14 and 18.3.15 following was stated:

"18.3.14. We have observed in the Chapter on "Legislative Relations" that intra-State trading activities often have a close and substantial relation to inter-State trade and commerce. State laws though purporting to regulate intra-State trade, may have implications for inter-State trade and commerce. These may impose discriminatory taxes or unreasonable restrictions, impeding the freedom of intra-State trade and commerce. If clause

(b) of Article 304 is deleted, the commercial and economic unity of the country may be broken up by State laws setting up barriers to free flow of trade an inter-course through parochial or discriminatory use of their powers. The suggestion of the State Government is not workable even from a functional standpoint. 18.3.15. From a broad conceptual angle, the suggestion for excluding intra-State trade and commerce from the
purview of Article 302 and for deletion of the Proviso to Article 304(b) does not stand close scrutiny. It is not in consonance with the prevailing concept of federalism. It presumably draws, inspiration from the antiquated and obsolete theory of federalism, according to which two levels of government were supposed to function in water-tight compartments in isolation from each other. Such a "dual" federalism is nowhere a functional reality in the modern world. Even in the so-called classical federation of the United States of America federalism is now a dynamic process of government, a system of shared responsibilities and cooperative action between the three tiers of government. The Constitution-framers were conscious of this reality. Indeed, the very scheme of Articles 301 to 304 which imposes limitations on the legislative powers of the Union and of the States, both with respect of inter-State and intra-State commerce and intercourse, is expected to be worked in cooperation by the Union and the States. The mere fact that Article 303(2) gives an exclusive power to Parliament to m ake a discriminatory law for dealing with a situation of scarcity of goods, or that the Proviso to Article 304(b) gives a supervisory power to the President (i.e. Union Council of Ministers) over a State legislation seeking to impose restrictions on inter-State or intra-State trade, is not a good enough argument to hold that these are anti-federal features making unjustifiable encroachment on the autonomy of the States. No doubt, these features give due weight age to the Union. But the scheme of the Articles in Part XIII considered as a whole, is well-balanced. It reconciles the imperative of economic unity of the Nation with interests of State autonomy by carving out in clauses (a) and

(b)of Article 304, two exceptions in favour of State legislature to the freedom

guaranteed under Article 301."

248. Now one more limb of submissions with regard to Article 304(b) needs to be considered. The submission on behalf of the States is that Article 304 sub-clause (b) does not contemplate taxing legislation. It is contended that Article 304 (a) has specifically used word 'tax' and absence of word 'tax' in Article 304(b) clearly indicates that the Constitution framers have intended to cover restrictions other than tax. Learned counsel for the petitioners have refuted the submission and their contention is that word 'restrictions' used in Article 304(b) is vide enough to include tax legislation. Gajendragadkar, J. speaking for majority in Atiabari Tea Co.Ltd. (supra) has expressly held at page 856 "how tax can be levied on internal goods, is, however, provided by Article 304(b)". Shri P.P. Rao, learned senior counsel appearing for the States, in the context of the above observation submits that the above observations made in majority judgment are only obiter, neither the issue was before the Court nor it can be said that after due consideration the law was laid down. In G.K. Krishnan & ors. Vs. State of Tamil Nadu (supra) a doubt was expressed by Justice Mathew that as to whether Article 304(b) would include levy by a non-discriminatory tax was a matter on which there was scope for difference of opinion. Justice Mathew did not express his opinion that tax legislation is not included in Article 304(b).

249. Article 304(a) as noted above is only with regard to the imposition of tax on goods imported from other States. Article 304(a) does not refer to taxes imposed on the local goods. In the event, the State Legislature imposes restrictions on the freedom of trade and commerce by taxing legislation covering local goods, whether the validity of it cannot be tested on anvil of Article 301. Further, State in public interest requires imposition of reasonable restriction by imposing tax on the local goods, what procedure it has to follow so as to not impede Article 301. There cannot be any dispute that power to legislate including tax legislation is the power allocated to State Legislature under the Constitutional Scheme under Article 245 and 246. Article 304 is not a source of power of legislation by State rather as the heading of the section indicates that it is a "Restriction on trade, commerce and intercourse among States." As we have noted above, Article 304(a) only deals with goods imported from other States hence for imposing reasonable restrictions in the public interest on trade, commerce and intercourse with regard to local goods, only way out for a State to save its legislation is to go through the route as provided under Article 304(b). We cannot imagine that merely because State Legislature has competence to frame tax law with regard to local goods, it can impose taxes which amount to impeding the freedom of trade and commerce, whe-reas the Constitution does not provide any exemption to State Legislature in that regard.

250. There are few more reasons due to which we are of the opinion that word 'restriction' uses in Article 304(b) also includes taxation law.

251. A State Legislature in exercise of its legislative power referable to any of the Entries of List II can frame law both fiscal or non-fiscal. When Article 304 uses words "by law" and the law is a wider term which embraces both fiscal and non-fiscal legislation with regard to clause (b), it cannot be limited as only non-fiscal law. If we

have to hold that Article 304 (b) does not refer to tax law, we have to give different meaning to words "by law" used in the beginning of Article 304 which governs both clauses (a) and (b). The mere fact that clause (a) uses the words 'any tax' and clause (b) does not use the word 'tax' is not of much significance since the word restrictions used in clause (b) is wide enough to cover any kind of restriction by fiscal law. Neither Article 302 nor Article 303 uses the word 'tax'. Both Articles are dealing with freedom of trade and commerce, non-use of word 'tax' in Article 304 (b) is also inconsequential. We thus are of the opinion that the word 'restrictions' under Article 304(b) is vide enough to include restrictions placed both by fiscal or non-fiscal law.

252 . At this stage, we will like to clarify one aspect of the matter, the submission has been advanced by learned counsel for the State that in the event, it is accepted that word 'restriction' in Article 304(b) includes taxation, it will be a serious restraint on the legislative power of the State, which is plenary and sovereign power. It is to be clarified that Article 304 (b) does not cover each and every legislative exercise of a State. The legislation which contains restriction on freedom of trade, commerce and intercourse only need to be routed through Article 304(b). In the event, a State legislation does not contain any restriction to freedom of trade, commerce and intercourse, there is no necessity of routing through Article 304(b) in which, case Article 304 (b) is not at all required to be resorted to. The State legislation, when it impedes the freedom of trade, commerce and intercourse and imposes reasonable restrictions by fiscal or non-fiscal legislation it needs to go through the routes of Article 304(b) to insulate it from the wrath of Article 301.

253. Article 304(b) thus operates in a very limited field, as explained above and plenary legislative power of the State, in no manner, is restricted by Article 304(b). We are thus of the view that apprehension of the learned counsel for the State that Article 304(b) operates serious restraint on the legislative power is misplaced. We thus conclude that word 'restriction' as used in Part XIII as well as in Article 304(b) at the Constitution includes tax legislation also.

254. With reference to Article 304(a), one of the aspects on which learned counsel for the parties have taken different stand is as to whether exemptions granted in tax by a State Legislature to the local goods does or does not violate Article 304(a). Shri Salve while elaborating his challenge to Entry Tax legislation of different States has referred to the second group of enactments in which an entry tax is imposed on the goods coming from outside and local goods but legislation contains device by which there is set off/ exemptions to the local goods which result in non-imposition of Entry Tax to the local goods leading to discrimination violating Article 304(a). On the other hand, counsel appearing for the States submit that a State is not, in any manner, precluded from granting exemption to specified class of goods to give a helping hand for development of a particular industry specially in a State which is not so developed and State patronage for development is necessary. It is contended that all States are not equal in its economic and industrial development and backward State needs a special treatment by way of exemption in tax in deserving cases for coming up at level playing field with other States. It is contended that State's protection by way of exemption/set off in such cases cannot be termed as discrimination. It is contended that discrimination is one

when it is a hostile discrimination.

255. Learned counsel for the parties have placed reliance on various pronouncements of this Court in support of their respective submissions which we shall notice hereinafter.

256. A Constitution Bench of this Court in Firm *A.T.B. Mehtab Majid and Co. vs. State of Madras and another*[31], had occasion to consider Article 301 and Article 304 in the context of Madras General Sales Tax Act, 1939 and Madras General Sales Tax Rules, 1939. The writ petition was filed under Article 32 by a dealer who was dealing in hides And skins tanned outside the State of Madras, as well as those tanned inside the State. The dealer was assessed to sales tax for the year 1955-56 representing the sales of tanned hides and skins which were obtained from the outside of the State of Madras. Rule 16 was challenged by the petitioner raising following contention:

> "6. It is contended for the petitioner that the effect of this Rule is that tanned hides or skins imported from outside the State and sold within the State are subject to a higher rate of tax than the tax imposed on hides or skins tanned and sold within the state, inasmuch as sales tax on the imported hides or skins tanned outside the State is on their sale price while the tax on hides or skins tanned within the State, though ostensibly on their sale price, is, in view of the proviso to clause (ii) of sub-rule (2) of Rule l6, really on the sale price of these hides or skins when they are purchased in the raw condition and which is substantially less than the sale price of tanned hides or skins, Further, for similar reasons, hides or skins imported from outside the State after
> purchase in their raw condition and then tanned inside the State are also subject to higher taxation than hides or skins purchased in the raw condition in the State and tanned within the State, as the tax on the former is on the sale price of the tanned hides or skins and on the latter is on the sale price of the raw hides or skins. Such a discriminatory taxation is said to offend the provisions of Article 304(a) of the
> Constitution. Similar are the contentions for the interveners in the case."

257. This Court after considering the respective submissions held that tax on hides and skins imported from outside being higher, it is discriminatory and unconstitutional. Following was held:

> "10. It is therefore now well settled that taxing laws can be restrictions on trade, commerce and intercourse, if they hamper the flow of trade and if they are not what can be termed to be compensatory taxes or regulatory measures. Sales tax, of the kind under consideration here, cannot be said to be a measure regulating any trade or a compensatory tax levied for the use of trading facilities. Sales tax, which has the effect of discriminating between goods of one State and goods of another, may affect the free flow of trade and it will then offend against Article 301 and will be valid only if it comes within the terms of Article 304(a).

11. Article 304(a) enables the legislature of a State to make laws affecting trade, commerce and intercourse. It enables the imposition of taxes on goods from other States if similar goods in the State are subjected to similar taxes, so as not to discriminate between the goods manufactured or produced in that State and the goods which are imported from other States. This means that if the effect of the sales tax on tanned hides or skins imported from outside is that the latter becomes subject to a higher tax by the application of the proviso to sub-rule of Rule 16 of the Rules, then the tax is discriminatory and unconstitutional and must be struck down."

258. Petitioners rely on *Weston Electronics and another vs. State of Gujarat and others,* Under Section 49 sub-Section (2) of Gujarat Sales Act, 1969 the State was empowered to exempt, in the public interest, any specified class of sales from sales tax. In 1981, while the rate for electronic goods entering the Gujarat State for sale therein was maintained at 15%, the rate in respect of locally manufactured goods was reduced to 6% by notification. By further notification in the year 1986, the rate of tax on imported television was reduced from 15% to 10% whereas rate of tax on manufactured television within the State was reduced from 6% to 1%.The petitioners, manufacturers of electronic goods including televisions whose factories are located at Delhi, and goods are sold in all over India including Gujarat, challenged the exemption granted to the goods manufactured in the State of Gujarat as violative of

259. The State submitted before this Court that the rate of tax was reduced in the case of goods manufactured locally in order to provide an incentive for encouraging local manufacturing units. This Court referring to earlier judgments of this Court held that discrimination by applying different rates of tax is not sustainable, following was stated:

"6. In answer to the writ petition, the respondents point out that the rate of tax was reduced in the case of goods manufactured locally in order to provide an incentive for encouraging local manufacturing units. Reference is made to clauses (b) and

(c) of Article 39 of the Constitution. We do not think that any support can be derived from the two clauses of Article 39. Clause (a) of Article 304 is clear in meaning. An exception to the mandate declared in Article 301 and the prohibition contained in clause (1) of Article 303 can be sustained on the basis of clause (a) of Article 304 only if the conditions contained in the latter provision are satisfied.

7. In the result, the discrimination effected by applying different rates of tax between goods imported into the State of Gujarat and goods manufactured within that State must be struck down."

260. Another two Judge Bench judgment in *Indian Cement and others vs. State of Andhra Pradesh and others*[33], had a occasion to consider notification issued under Section 9(1) of Andhra Pradesh General Sales Tax Act, 1957 whereby rate of tax in respect of sales made by indigenous cement manufacturers to manufacturers of cement products in the State of Andhra Pradesh was reduced. Notification under Section 8(5) of Central Sales Tax Act, 1956 was also issued reducing rate of tax on the sale of cement

made in the course of inter-State trade or commerce. Two Judge Bench of this Court referring to Atiabari Tea Co. Ltd. and Automobile Transport Ltd. Stated following in paragraph 12:

> "12. There can be no dispute that taxation is a deterrent against free flow. As a result of favourable or unfavourable treatment by way of taxation, the course of flow of trade gets regulated either adversely or favourably. If the scheme which Part XIII guarantees has to be preserved in national interest, it is necessary that the provisions in the article must be strictly complied with. One has to recall the farsighted observations of Gajendragadkar, J. in Atiabari Tea Co. case [AIR 1961 SC 232 (1961) 1 SCR 809] and the observations then made obviously apply to cases of the type which is now before us.
> "

261. This Court held both the notifications issued by Andhra Pradesh Government unsustainable in law. Following was stated in paragrph 14:

> "14 Variation of the rate of interstate sales tax does affect free trade and commerce and creates a local preference which is contrary to the scheme of Part XIII of the Constitution. The notification extends the benefit even to unregistered dealers and the observations of Hegde,
>
> J. on this aspect of the matter are relevant. Both the notifications of the Andhra Pradesh Government are, therefore, bad and are hit by the provisions of Part XIII of the Constitution. They cannot be sustained in law."

262 . Now, we come to a three Judge Bench judgment on which much reliance has been placed by the counsel for the State, i.e. *Video Electronics Pvt. Ltd. And another vs. State of Pubjab and another,*[34] In the above case this Court had occasion to consider notifications issued by Uttar Pradesh Government under Section 4-A of Uttar Pradesh Sales Act, 1948. Constitutional validity of Section 4-A of the Act and Section 8(5) of Central Sales Tax, 1956 was also challenged. The petitioner carry on the business of selling cinematographic films and other equipments like projectors, sound films, photo films etc. manufactured outside the State of Uttar Pradesh. New units of manufacturer as defined in 1948 Act in the State of U.P. were exempted for different periods ranging from 3 to 7 years on conditions set out in the notification. Petitioner challenged the notification as violative of rights guaranteed under Part XIII as well as Article 14 and 19(1)(g) of the Constitution.

263. This Court held that the power to grant exemption is always inherent in all taxing statutes. The reasons for notification as submitted on behalf of the State i.e. economic encouragement and growth found favour and it was held that exemption do not violate Article 304 . This Court laid down following in paragraph 26 at page 108:

> "26 Economic unity of India is one of the constitutional aspirations of India and safeguarding the attainment and maintenance of that unity are objectives of the Indian Constitution. It would be wrong, however, to assume that India as a whole is already an economic unit. Economic unity can only be achieved if all

parts of whole of Union of India develop equally, economically. Indeed, in the affidavits of opposition various grounds have been indicated on behalf of the respondents suggesting the need for incentives and exemptions, and these were suggested to be absolutely necessary for economic viability and survival for these industries in these States. These were based on cogent and intelligible reasons of economic encouragement and growth. There was a rationale in these which is discernible. The power to grant exemption is always inherent in all taxing statutes. If the suggestions/submissions as advanced by the petitioners are accepted, it was averred, and in our opinion rightly, that it will destroy completely or make nugatory the plenary powers of the States. If the exemption is based on natural and business factors and does not involve any intentional bias, the impugned notifications to grant exemption of limited period on certain specific conditions cannot be held to be bad. Judged by that yardstick, the present notifications cannot be held to be violative of the constitutional provisions. An examination of Article 304(a) would reveal that what is being prohibited by this article which is really an exception to Article 301 will not apply if Article 301 does not apply."

264 . This Court further held that grant of exemption to specified class for limited period, such granting of exemption cannot be held to be contrary to the concept of economic unit.
Following was stated:

"28. Concept of economic barrier must be adopted in a dynamic sense with changing conditions. What constitutes an economic barrier at one point of time often ceases to be so at another point of time. It will be wrong to denude the people of the State of the right to grant exemptions which flow from the plenary powers of legislative heads in List II of the Seventh Schedule of the Constitution. In a federal polity, all the States having powers to grant exemption to specified class for limited period, such granting of exemption cannot be held to be contrary to the concept of economic unity. The contents (sic concept) of economic unity by the people of India would necessarily include the power to grant exemption or to reduce the rate of tax in special cases for achieving the industrial development or to provide tax incentives to attain economic eq-uality in growth and development. When all the States have such provisions to exempt or reduce rates the question of economic war between the States inter se or economic disintegration of the country as such does not arise. It is not open to any party to say that this should be done and this should not be done by either one way or the other. It cannot be disputed that it is open to the States to realise tax and thereafter remit the same or pay back to the local manufacturers in the shape of subsidies and that would neither discriminate nor be hit by Article 304(a) of the Constitution. In this case and as in all constitutional adjudications the substance of the matter has to be looked into to find out whether there is any discrimination in violation of the constitutional mandate."

265. This Court also referred to Article 38 and 39. Earlier two judgments in Indian Cement Ltd. (supra) and Weston Electronics (supra) were noticed by this Court and it

was held that these cases were not at all concerned to a special class, had a specific condition of maintaining the general rate of tax, hence they were not applicable. This Court further held that if the power of exemption is in exercise of colourable manner to create unfavourable bias by prescribing general lower rate on locally manufactured goods either in the shape of general exemption to locally manufactured goods or in the shape of lower rate of tax, such an exercise of power can always be struck down by the Courts.

266. The Court also considered the notification issued by the Punjab Government whereby two different rates of tax were provided differentiating between the manufacturers of electronic goods outside the State and within the State. In paragraph 36 following was stated:

> "36. It has to be reiterated that sales tax laws in all the States provide for exemption. It is well settled that the different entries in Lists I, II and III of the Seventh Schedule deal with the fields of legislation, and these should be construed widely, liberally and harmoniously. And these entries have been construed to include ancillary or incidental power. Power to grant exemption is inherent in all taxing legislations. Economic unity is a desired goal, economic equilibrium and prosperity is also the goal. Development on parity is one of the commitments of the Constitution.
> Directive principles enshrined in Articles 38 and 39 must be harmonised with economic unity as well as economic development of developed and under developed areas. In that light on Article 14 of the Constitution, it is necessary that the prohibitions in Article 301 and the scope of Article
> 304(a) and (b) should be understood and construed. Constitution is a living organism and the latent meaning of the expressions used can be given effect to only if a particular situation arises. It is not that with changing times the meaning changes but changing times illustrate and illuminate the meaning of the
> expressions used. The connotation of the expressions used takes its shape and colour in evolving dynamic situations. A backward State or a disturbed State cannot with parity engage in competition with advanced or developed States. Even within a State, there are often backward areas which can be developed only if some special incentives are granted. If the incentives in the form of subsidies or grant are given to any part of (sic or) units of a State so that it may come out of its limping or infancy to compete as equals with others, that, in our opinion, does not and cannot contravene the spirit and the letter of Part XIII of the Constitution. However, this is permissible only if there is a valid reason, that is to say, if there are justifiable and rational reasons for differentiation. If there is none, it will amount to hostile discrimination.
> Judged in this light, despite the submissions of Mr Sanjay Parikh and Mr Vaidyanathan, we are unable to accept the contentions that the petitioners sought to urge in this application The three Judge Bench, thus, upheld the exemption in both the
> notifications as noted above.

267. In the judgment of Video Electronics the opinion was expressed by Sabyasachi Mukherji, CJ. Soon after the judgment of Video Electronics (supra) a three Judge Bench of this Court also consisting of Sabyasachi Mukherji, CJ in *Andhra Steel Corporation vs. Commissioner of Commercial Taxes in Karnataka,*[35] had occasion to consider exemption granted under Karnataka Sales Tax Act. In the above case the assessee purchases iron scrap from inside and outside the State of Karnataka for the purpose of manufacturing iron ingots, iron steel rounds and tor-steel. The main point urged before this Court challenging the exemption as violative Article 304(a) was noted in paragraph 4 to the following effect:

> "4. The main point was urged in this appeal was that Section 5(4) of the Act insofar as it pertains to Item 2 in Schedule IV read with the Explanation II is violative of Article 304(a) of the Constitution as under that provision the sale of finished goods manufactured out of imported raw material is taxed but the sale of finished goods manufactured out of locally purchased raw material is not taxed and that amounts to hostile discrimination in the rate of tax or quantum of tax." This Court took the view that the case in hand was fully covered by the decision of A.T.B. Mehtab Majid (supra). Following was stated in paragraph 22 and 23:
>
> "22 The tax was levied under the State Act in respect of steel semis. The State Act exempted steel semis which have been manufactured out of iron scrap which have suffered tax but not the other categories where the scrap had not suffered tax at that
> stage. This is directly covered by the decision in A.T.B. Mehtab case [1963 Supp 2 SCR 435 : AIR 1963 SC 928 : (1963) 14 STC 355] and that decision has not been dissented in Nataraja Mudaliar case[(1968) 3 SCR 829 : AIR 1969 SC 147 : (1968) 22 STC 376] or Rattan Lal & Co. case [(1969) 2 SCR 544 : AIR 1970 SC 1742 : (1970) 25 STC 136] . The decision in A.T.B. Mehtab case [1963 Supp 2 SCR 435 : AIR 1963 SC 928 : (1963) 14 STC 355] is by a Constitution Bench and had not been dissented so far in any case. The ratio of the judgment being fully applicable, the judgment of the High Court under appeal is not acceptable.
> 23. We accordingly hold that the provision which is impugned in this case is ultra vires and accordingly set aside the judgment of the High Court and allow the writ petition filed by the assessee in the High Court. There will be no order as to costs.

268. Now we come to two Judge Bench judgment of this Court in Shree Mahavir Oil Mills and another vs.State of J & K and others, (1996) 11 SCC 39. In the above case notification under Section 5 of the J & K General Sales Tax Act, 1962 dated 7.3.1991 was issued exempting small scale industrial units in the State for a period of five years. The rate of sales tax was 4% which was raised to 8%. The manufacturers brining edible oil from outside the State found tax discriminatory in so far as exemption was granted to all small scale industrial units in the State. The writ petitions and letters patent appeals filed before the High Court were dismissed and the matter was carried to this Court.

269. After noticing the scheme under Part XIII and specifically Article 304, this Court

while interpreting Article 304(a) stated following:

> "8 The wording of this clause is of crucial significance. The first half of the clause would make it appear at the first blush that it merely states the obvious: one may ind-eed say that the power to levy tax on goods imported from other States or Union Territories flows from Article 246 read with Lists II and III in the Seventh Schedule and not from this clause. That is of course so, but then there is a meaning and a very significant principle underlying the clause, if one reads it in its entirety. The idea was not really to empower the State Legislatures to levy tax on goods imported from other States and Union Territories — that they are already empowered by other provisions in the Constitution — but to declare that that power shall not be so exercised as to discriminate against the imported goods vis-à-vis locally manufactured goods. The clause, though worded in positive language has a negative aspect. It is, in truth, a provision prohibiting discrimination against the imported goods. In the matter of levy of tax — and this is important to bear in mind — the clause tells the State Legislatures — "tax you may the goods imported from other States/Union Territories but do not, in that process, discriminate against them vis-à-vis goods manufactured locally".
>
> In short, the clause says: levy of tax on both ought to be at the same rate. This was and is a ringing declaration against the States creating what may be called "tax barriers" — or "fiscal barriers", as they may be called — at or along their boundaries in the interest of freedom of trade, commerce and intercourse throughout the territory of India, guaranteed by Article 301. As we shall presently point out, this clause does not prevent in any manner the States from encouraging or promoting the local industries in such manner as they think fit so long as they do not use the weapon of taxation to discriminate against the imported goods vis-a-vis the locally manufactured goods. To repeat, the clause bars the States from creating tax barriers — or fiscal barriers, as they can be called — around themselves and/or insulate themselves from the remaining territories of India by erecting such "tariff walls". Part XIII is premised upon the assumption that so long as a State taxes its residents and the residents of other States uniformly, there is no infringement of the freedom guaranteed by Article 301; no State would tax its people at a higher level merely with a view to tax the people of other States at that level. And it is this clause which has a crucial bearing on this case "

270. Two Judge Bench noticed earlier cases as well as three Judge Bench judgment in Video Electronics (supra). In paragraph 23 this Court came to the conclusion that the total exemption granted in favour of small-scale industries in Jammu & Kashmir producing edible oil is not sustainable in law. The Court held that States are free to encourage and promote the establishment and growth of industries within their States by all such means as they think proper but they cannot, in that process, subject the goods imported from other States to a discriminatory rate of taxation, i.e., a higher rate of sales tax vis-a-vis similar goods manufactured/produced within that State. This Court noticed that although a limited exception has no doubt been carved out in Video

Electronics but that exception cannot be enlarged lest it eat up the main provision. The Court while declaring the exemption as violative of Article 304(a) directed in paragraph 27 as follows:

> "2 7. We declare that the exemption granted by Notification No.SRO 93 of 1991 to local manufacturers/producers of edible oil is violative of the provisions contained in Articles 301 and 304(a). At the same time, we direct that: (a) the appellants shall
> not be entitled to claim any amounts by way of refund or otherwise by virtue of or, as a consequence of, the declaration contained herein and (b) that the declaration of invalidity of the impugned notification shall take effect on and from 1-4-1997. Till that date,i.e.,up to and inclusive of 31.3.1997, the impugned notification shall continue to be effective and operative. Appeal allowed in the above terms."

271. The State exercises legislative power under Article 246 read with List II which is plenary in nature, when it has power to levy tax it is also entitled to grant of exemption/remission of tax. There cannot be any dispute to the power of a State Legisla-ture in providing for exemption/remission in tax to a specified class based on an intelligible differentia. A Constitution Bench in S*tate of Madhaya Pradesh vs. Abdeali*[36], need also to be noted.

272. In the above case, in exercise of power under Section 4(3) of Madhya Bharat Sales Tax Act, 1950 exemption was granted from payment of Sales Tax in the following manner:

> "2 In exercise of the powers conferred by Section 4, sub-section (3) of the Madhya Bharat Sales Tax Act, Samvat 2 0 07 the Rajpramukh in supersession of the Notification 59(c) (t) P.R. 412-54, dated 27-5-1955 of this department has exempted from the payment of sales tax, in case of sale by the manufacturer or any member of his family, the sale of all such shoes, chappals, country shoes and footwears which are hand-made and which are not manufactured on power machine and whose sale price does not exceed Rs 12-8-0."

273. The respondent was carrying on business of importing and selling different style of footwear in the State of Madhaya Pradesh. The respondent contended before the Sales Tax Officer that he was not liable to pay any sales tax on sale of hand-made shoes, chappals and other types of footwear whose sale price did not exceed Rs 12-8-0 per pair. The claim of the respondent was rejected that the respondent does not fulfill the conditions of the notification. In the writ petition filed by the respondent in the High Court one of the contentions was raised to the following effect:

> "3 The respondent further averred that if the exemption were held to be in favour of sales by a manufacturer or a member of his family and not on sales by an importer, then the notification would be discriminatory in nature and would contravene the provisions of Article 304(a) of the Constitution. On these grounds the respondent prayed that the assessment order dated March 25, 1958 be

quashed and the Sales Tax Officer be directed to exempt from tax such sales by the respondent as were cove-red by the exemption granted by the notification dated January 28, 1956. In their reply to the writ petition the appellants pointed out that the notification dated January 28, 1956 did not in any way discriminate between footwear manufactured or produced in the State of Madhya Pradesh and footwear imported from outside, because the conditions laid down in the notification were equally applicable to both types of goods and one of^ these conditions was that the sale which was to be exempted from tax must be by the manufacturer or a member of his family. "

274 . The High Court allowed the writ petition. The State carried the matter to this Court. This Court noted that notification dated January 28, 1956 makes no discrimination between footwear manufactured or produced in the State of Madhya Pradesh and footwear imported from other States and the exemption granted by the notification depends on the fulfillment of three conditions mentioned therein. Following was held by this Court in paragraph 8:

"8. We now proceed to consider these alternative submissions of learned counsel for the appellants. We do not think that the notification dated January 28, 1956 makes any such Discrimination between footwear manufactured or produced in the State of Madhya Pradesh and footwear imported from other States as is prohibited by Article 304(a) of the Constitution. We have already pointed out that the exemption granted by the notification in question depends on the fulfillment of three conditions and all the three conditions are equally applicable to footwear manufactured or produced in the State and footwear imported from other States. It is obvious that the exemption is for the protection and benefit of small manufacturers who make hand-made shoes of small value and who may be unable to compete with large-scale manufacturers of footwear made on machines. Such a classification in the interests of small manufacturers has often been made and upheld by this Court.

(See Orient Weaving Mills (P) Ltd. v. Union of India [Petition No. 110 of 1961 decided on February 28, 1962.]; and British India Corporation Ltd. v. Collector of Central Excise, Allahabad [Petition No. 94 of 1955 decided on August 20, 1962.]."

275. In the above case submission of the assessee was that in the event benefit of exemption is not granted to the assessee the exemption notification may itself be invalid creating a
discrimination between similar manufacturer of outside the State traveling in the State and selling hand-made shoes wherein small manufacturer has not to travel in order to get the benefit of the exemption. The Court rejected the above argument stating that it is really an argument of inconvenience. In any view of the matter, this Court in the above case held that assessee did not fulfill the condition of the notification, i.e., sale was exempted only when it is by a manufacturer or a family member of his family. Hence, there was no error in assessing him to the tax. The issue whether it was permissible to grant exemption to local goods and not to grant such exemption to the goods coming from outside was not the issue in the above case. In the above case, this Court has

noticed that there was no discrimination with regard to the exemption in regard to the goods manufactured outside the State or within the State. The above case, thus, does not decide the issue which has cropped up before us.

276. The power of exemption flows from legislation enacted by the State Legislature, wherever exemptions are granted, normally, statutes so provide with legislative policy. What is exemption, has been succinctly explained by this Court in *Union of India and others vs. Wood Papers Ltd. And another*[37], following was stated in paragraph 4:

> "4 Literally exemption is freedom from liability, tax or duty. Fiscally it may assume varying shapes, specially, in a growing economy. For instance tax holiday to new units, concessional rate of tax to goods or persons for limited period or with the specific objective etc. That is why its construction, unlike charging provision, has to be tested on different touchstone. In fact an exemption provision is like an exception and on normal principle of construction or interpretation of statutes it is construed strictly either because of legislative intention or on economic justification of inequitable burden or progressive approach of fiscal provisions intended to augment State revenue."

277. Reverting to provision of 304(a), for a legislation to be within four corners of 304(a), two conditions are necessary to be fulfilled (1) State can impose on goods imported from other States any tax to which similar goods manufactured or produced are subject, (2) so however, as not to discriminate between goods so imported and goods so manufactured or produced. The first condition is that goods manufactured or produced in the State are subject to tax, when exemption is granted in payment of tax to a specified category on fulfillment of certain condition, it pre-supposes that goods are subject to tax. The exemption granted on a specified class of goods, subject to condition, does not militate against the tax to which the goods are subject. Thus in cases of grant of exemption to a specified category on conditions mentioned therein, first condition as noted above is not breached. Now coming to the second condition i.e. so, however, as not to discriminate goods exported and goods locally manufactured or produced. Goods exempted fall in a different category then the bulk of goods produced and manufactured in the State. Exemptions under different statutes have been upheld due to legislative policy as delineated in a particular statute. In the Video Electronics, three Judge Bench upheld the exemption noticing the fact that the exemption granted was to a special class for limited period on specific conditions of maintaining the general rate of tax on the goods manufactured by all those producers in the State who do not fall within that category. Video Electronics, however, further states that if tax is imposed in a colourable manner intentionally or purposely to create unfavourable bias by prescribing a general lower rate on locally manufactured goods either in the shape either of general exemption to locally manufactured goods or in the shape of lower rate of tax, such an exercise of power can always be struck down by the Courts. Following was observed in paragraph 30:

> "These cases were not at all concerned with granting of exemption to a special class for a limited period on specific conditions of maintaining the general rate of tax on the goods manufactured by all those producers in the State who do not fall

within the exempted category at par with the rate applicable to import- ed goods as we have read these cases. Hence, it was not necessary in those decisions to consider the problem in its present aspect. If, however, the said power is exercised in a colourable manner intentionally or purposely to create unfavorable bias by prescribing a general lower rate on locally manufactured goods either in the shape of general exemption to locally manufactured goods or in the shape of lower rate of tax, such an exercise of power can always be struck down by the courts. That is not the situation in the instant cases. The aforesaid decisions, therefore, are not authorities for the general proposition that while, maintaining the general rate at par, special rates for certain industries for a limited period could not be prescribed by the States."

278. Two Judge Bench in Shree Mahavir Oil Mills had noticed earlier cases including Video Electronics. It was observed that exception carved out in Video Electronics cannot be widened or expanded to cover cases of a different kind, following observation was made in Shree Mahavir Oil Mills in paragraph 23: is not necessary for us to say anything about the correctness of Video Electronics. Suffice it to say that the limited exception carved out therein cannot be widened or expanded to cover cases of a different kind. It must be held that the total exemption granted in favour of small scale industries in Jammu & Kashmir producing edible oil [there are no large scale industries in that State producing edible oil] is not sustainable in law."

279. The exception carved out in Video Electronics upheld exemption notification where it is limited to specified type with short period. The general exemption and exemption in wider term has never been approved. The ratio of Video Electronics has to be read as justifying only exemption limited to a specified category for a short period. Exemption in general terms of unlimited in nature cannot be approved. The exemption cannot be used as measure of discrimination between goods imported from other States and goods manufactured or produced in the State. The exemption has to be a limited exemption to the tax which is imposed on the similar goods. In the event exemption is total and general in nature, the said exemption is clearly violative of Article 304(a). Similarly, set off of a particular tax which is general and not limited to specified category has also to be disapproved. In view of above, the ratio of three Judge Bench judgment in Video Electronics have to be read to the above extent and with the limitation as noticed above.

280. We, thus, come to the conclusion that State Legislature in exercise of its taxing power can grant exemption/set off to local goods, only to a limited extent based on intelligible differentia which is not in the nature of general/unspecified exemption. The exemption/set off which tend to become general exemption violates Article 304(a).

G. ENTRY 52 OF LIST II OF VIITH SCHEDULE OF THE CONSTITUTION

281. Legislative field under State List, Entry 52 is 'taxes on the entry of goods into a local area for consumption, use or sale therein'. The Entry 52 itself demonstrate that there are inherent limitations as regard the nature and character of the levy. In order to have a levy of tax to come within the purview of Entry 52, such levy has to satisfy three

conditions:

(i) The levy under the State Entry must be 'on the entry of goods' which constitutes the taxable events.

(ii) The levy in question must be in respect of 'into a local area'. The local area has been defined as ' an area administered by local body like a municipality, a district board, a local board, a union board, a panchayat or the like'.

(iii) The goods must enter into the local area for the purpose of 'consumption, use or sale therein'.

282 . The expression Entry Tax has to be understood in its plain meaning and also in the backdrop of historical imposition of taxes of this kind. The tax commonly known as octroi was in force in 1901 and it was subsequently included in VIIth Schedule of List II of Government of India Act, 1935. The Constitution of India does not use the word octroi. List I Entry 89 provides for 'terminal tax on goods and passengers carried by railways, sea or air; taxes on railway fares and flights'.
283. Taxes levied under Entry 52 is commonly known as entry tax. While noticing the Constituent Assembly debates, we have seen that freedom of trade and commerce was envisaged as freedom from border taxes, custom barriers etc., which was prevalent in Indian States. Section 297 of 1935 Act had contained a prohibition for imposing taxes on entry of goods from other States. The Constitution framers decided that States have to be conceded some taxing powers for revenue purposes and for purpose of carrying out various development projects. Article 301 provides freedom of trade, commerce and intercourse throughout the territory of India, simultaneously, exception to such freedom have been engrafted in Article 302 – 306. 284. Article 304(a), although permits the State to levy tax but it is hedged with two important conditions, which we have already noticed above. Article 304(a) thus expressly permits the State to impose any tax which includes entry tax also subject to conditions mentioned therein.

285. The Entry Tax is related to movement of goods. Movement of goods have been treated to be an integral part of trade and commerce. In Atiabari, referring to the content of freedom
Provided by Article 301, it was held that it certainly includes movement of trade follo-wing was observed by Gajendragadkar, J., at Page 859:

"the conclusion appears to us to be Inevitable that the content of freedom provided for by Article 301 was larger than the freedom contemplated by s. 297 of the Constitution Act of 1935, and whatever else it may or may not include, it certainly includes movement of trade which is of the very essence of all trade and is its int-egral part. If the transport or the movement of goods is taxed solely on the Basis that goods are thus carried or transported that, in our opinion, directly affects the freedom of trade as contemplated by Article 301."

286. This Court, while construing the Karnataka tax on entry of goods into local area for

consumption, use or sale therein Act, 1979 in *State of Karnataka Vs. Hansa Corporation*[38] has held that the tax on the entry of goods falls within the inhibition of Article 301. Following was observed:

> "To the extent the impugned tax is levied on the entry of goods in a local area it cannot be gainsaid that its immediate impact would be on movement of goods and the measure would fall within the inhibition of Article 301."

287. A law, made under the subject matter of Entry 52 List II, would thus clearly be a tax on the movement of goods and thus would fall within the purview of the inhibition of Article 301 and the said law can only be saved if it complies with the Article 304 . Learned counsel for the States have contended that Entry Tax does not prohibit the entry of goods and tax is collected, only subsequently and normally, on the basis of returns filed by the persons taking the goods into a local area. Hence, there is no restriction on the borders of a State or border of a local area. It is contended that on the entry of goods merely a transit slip is given hence there is no barrier to the flow of goods. It is well settled that there is a clear distinction between incidence of a levy and the machinery provisions contained in law to give effect to such levy. The incidence of levy is on entry of goods hence incidence of tax is complete as the goods enters into the local area, whether the tax is collected immediately or subsequently has no relevance with the incidence of taxation.

288. The trade and commerce being contemplated to be free throughout the territory of India, any restriction on movement of goods per se has to be treated as violating Article 301 unless the tax is saved by exceptions provided in Part XIII. However, there may be a tax which though complies Article 304(a) but still contains the restriction to trade and commerce which is an area where much difficulty has been felt. We have already concluded that all taxes which comply with Article 304(a) need not to be routed through Article 304(b) and it is only those taxes which contain restrictions on trade, commerce and intercourse which need to be routed through 304(b). This can be demonstrated by taking a simple example. An Entry tax legislation is passed complying Article 304(a) levying Entry Tax on goods imported from outside the State as well as local goods at the rate of one percent of value of goods. Normally, such levy cannot be treated as any restriction on the trade and commerce and shall pass muster of Article 304(a) and need no compliance of Article 304(b). But in a case where, Entry Tax is levied to the extent of hundred per cent of the value of goods both on imported goods and locally produced or manufactured goods, the said levy is clear restriction on trade and commerce and has to be routed through Article 304(b). For taking out such levy, from the effect of Article 301 both 304(a) and 304(b) needs to be complied with.

289. We thus conclude that Entry Tax legislation which is a tax on movement of goods, trade and commerce is inhibited by Article 301 and such State legislation can be saved under Article 304. Whether a particular Entry Tax Legislation is valid and does not contravene Part XIII of the Constitution, can be decided only after looking into the nature, content and extent of legislation and its impact on trade, commerce and intercourse.

H. MEANING OF "RESTRICTION" AS USED IN PART XIII

290. Freedom of trade, commerce and intercourse throughout the territory of India is guaranteed under Article 301. The framers of the Constitution were conscious that the freedom cannot be absolute and it may be necessary in several circumstances to restrict the freedom in public interest. Article 302 – 306 enumerates exceptions to the freedom as guaranteed under Article 301. What is the meaning and contents of word 'restriction' as used in Part XIII? The word 'restriction' has also been used under Article 19 (2) to 19 (6) while empowering the State to impose reasonable Article 19(1) (a) to 19 (1) (g). The word 'restri-ction' is defined in New Webster Dictionary in the following manner:

> "The act of restricting, or state of being restricted; that which restricts; a restraint; limitation."

291. The Black's Law Dictionary also defines 'restriction in following manner:

> 1. "restriction.l.Confinement within bounds or limits; a limitation or qualification.
>
> 2. A limitation (esp. in a deed) placed on the use or enjoyment of property."

292 . The restriction thus is an act to limit, confine and restrain. The 'restriction', in Part XIII has been used in the context of restriction to freedom of trade, commerce and intercourse. The law, which restrict or limit such right are called restrictions.

293. In the present case, since we are concerned with the taxing legislation, our discussions shall confine to find out the nature of restriction which can be put on the freedom of trade and commerce by tax legislation. The Constitution Bench of this Court in Firm A.T.B. *Mehtab and Majid and Company V. State of Madras and Others*[39] *at P. 442* has stated 'it is, therefore, now well settled that taxing laws can be restrictions if they hamper the flow of trade and if there are not what can be termed to be compensatory tax or regulatory Measures ". In *Indian Cement and Others V. State of Andhra Pradesh*[40] this Court has held that as a result of favourable or unfavourable treatment by way of taxation the course of flow of trade gets restricted:-

either adversely or favourably. Following observations were made in para 12, 14:-

> "12. There can be no dispute that taxation is a deterrent against free flow. As a result of favourable or unfavourable treatment by way of taxation, the course of flow of trade gets regulated either adversely or favourably. If the scheme which Part XIII guarantees has to be preserved in national interest, it is necessary that the provisions in the article must be strictly complied with. One has to recall the farsighted observations of Gajendragadkar, J. in Atiabari Tea Co. case and the observations then made obviously apply to cases of the type which is now before us."
>
> "14. Variation of the rate of interstate sales tax does affect free trade and

commerce and creates a local preference which is contrary to the scheme of Part XIII of the Constitution. The notification extends the benefit even to unregistered dealers and the observations of Hegde, J. on this aspect of the matter are relevant. Both the notifications of the Andhra Pradesh Government are, therefore, bad and are hit by the provisions of Part XIII of the Constitution.

They cannot be sustained in law."

294. Now, we proceed to examine Part XIII of the Constitution in so far as it expressly refer to various acts, actions which are treated to be restrictions in freedom of trade and commerce. Article 302 – 306 contain provisions, by which restriction can be put on the freedom of trade and commerce. Some restrictions have been expressly mentioned in said articles. Article 303 provides for 'restrictions on the legislative powers of the Union and of the States with regard to the trade and commerce'. As per Article 303, sub-article Clause 1 following are treated to be restrictions:-

(i) Any law giving or authorizing the giving of any preference to one State over another,

(ii) Any law making or authorizing the making of, any discrimination between one State and another.

295. Thus preferences and discrimination both are treated as restriction in the context of freedom of trade and commerce. Coming to Article 304(a) any law framed by legislature is restriction on freedom of trade and commerce which:-

a). Imposes on goods imported from other State, any tax when no such tax is imposed on similar goods other States any tax which discriminates between goods so imported and goods so manufactured or produced.

296. Again in Article 304 sub-clause(b) State is empowered to impose reasonable restrictions in the public interest. Article 306, as it was initially enacted, contained heading 'power of certain States in Part B of the Schedule to impose restriction on trade and commerce'. Article 306 permitted any tax on duty on import of goods into the State from other States or on the export of goods from the State to another States which was being imposed by a State specified in Part B to continue by an agreement between Government of India and Government of States for a period, not exceeding ten years. The article contemplates contin-uance of tax or duty which was treated to be restriction and was allowed to continue only
with an agreement for a maximum period of ten years.

297. We have already noticed a series of judgments of this Court holding that imposition of discriminatory taxes violates Article 304(a). Such discriminatory tax imposed by State have been struck down as being violative of Article 304(a) reference is made to the judgment of this Court in *State of Madhya Pradesh V. Bhailal Bhai and Others*[41] *Shree Mahavir Oil Mills and Another Vs. State of Jammu & Kashmir and Others*[42]

298. The restriction which can be imposed, as contemplated by above provisions of law, have to be such limitation on the right of freedom of trade and commerce which should not be arbitrary or of excessive nature beyond what is required in the context of the power. The Constitution Bench, speaking through Patanjali Sastri, CJ., in *State of Madras Vs. V. G. Row*[43] while considering the concept of reasonable restriction under Article 19 has stated:-

> "It is important in this context to bear in mind that the test of reasonableness, wherever prescribed, should be applied to each individual statue impugned, and no abstract standard, or general pattern of reasonableness can be laid down as applicable to all cases. The nature of the right alleged to have been infringed, the underlying purpose of the restrictions imposed, the extent and urgency of the evil sought to be remedied thereby, the disproportion of the imposition, the prevailing conditions at the time, should all enter into the judicial verdict. "

2 99. Although the word 'restriction' may also in certain circumstances includes prohibitions but restriction is not to be understood with complete prohibition or stoppage of business, effect of tax when it hinders the trade & commerce, it becomes restriction and prohibited under Article 301. This Court in *Laxmi Khandsari Etc. Vs. State of U.P.*[44] While considering the concept of reasonable restriction has held that reasonable restriction would depend on the nature and circumstances of the case following was laid down in page 105:

> "As to what are reasonable restrictions would naturally depend on the nature and circumstances of the case, the character of the statute, the object which it seeks to serve, the existing circumstances, the extent of the evil sought to be remedied as also the nature of restraint or restriction placed on the rights of the citizen. It is difficult to lay down any hard or fast rule of universal application but this Court has consistently held that in imposing such restrictions the State must adopt an objective standard amounting to a social control by restricting the rights of the citizens where the necessities of the situation demand."

300. Further, it was held in *Laxmi Khandsari Etc. Etc. Vs. State of U.P.*[45] that incurring of the loss in trade is not a ground to trade restrictions as un-reasonable. Following was laid down:

> "Finally, in determining the reasonableness of restrictions imposed by law in the field of industry, trade or commerce, the mere fact that some of the persons engaged in a particular trade may incur loss due to the imposition of restrictions will not render them unreasonable because it is manifest that trade and industry pass through periods of prosperity and adversity on account of economic, social or political factors. In a free economy controls have been introduced to ensure availability of consumer goods like food-stuffs, cloth or the like at a fair price and the fixation of such a price cannot be said to be an unreasonable restriction in the circumstances. "

301. This Court, in *G. K. Krishnan and Others Vs. State of Tamil Nadu and Others*[46], has

held that the regulation like rules of traffic facilitate the freedom of trade whereas restriction impede that freedom, it was held that a discriminatory tax against outside goods is not a tax simpliciter but is a barrier to trade and commerce. Following was laid down in para 15 and 27:

> "15. Regulations like rules of traffic facilitate freedom of trade and commerce whereas restrictions impede that freedom. The collection of toll or tax for the use of roads, bridges, or aerodromes, etc., do not operate as barriers or hindrance to trade.
> For a tax to become a prohibited tax, it has to be a direct ax, the effect of which is to hinder the movement part of the trade. If the tax is compensatory or regulatory, it cannot operate as a restriction on the freedom of trade or commerce. "
>
> "27. A discriminatory tax against outside goods is not a tax simpliciter but is a barrier to trade and commerce."

302. A Constitution Bench in Federation of *Hotel and Restaurant Association of India, Etc. Vs. Union of India and Others*[47] was considering the validity of a taxing law in the context of Article 14 of the Constitution. The Constitution Bench held that legislature enjoys a wide
latitude in the matter of selection of persons, subject matter, events etc. for taxation. Further, it was held that some excessiveness of taxation or its imposition tends towards diminution of earnings or profits, does not violate rights under Article 19 (1) (g):

> "46. It is now well settled that though taxing laws are not outside Article 14, however, having regard to the wide variety of diverse economic criteria that go into the formulation of a fiscal policy legislature enjoys a wide latitude in the matter of selection of persons, subject matter, events etc., for taxation. The tests of the vice of discrimination in a taxing law are, accordingly, less rigorous. "
>
> Further in para 52 following was stated:
>
> "62. Then again, the mere excessiveness of a tax or even the circumstance that its imposition might tend towards the diminution of the earnings or profits of the persons of incidence does not, per se, and without more, constitute violation of the rights under Article 19(1)(g)."

303. It is, however, relevant to note that the issue as to whether the restriction contained in any taxing statute impede the freedom of trade and commerce is a question which will vary from case to case. The nature of restriction and the magnitude of the restriction are all relevant factors to determine whether trade is impeded or not. It is well settled that provisions in a statute which is regulatory in nature which facilitates the trade have not been treated as restriction impeding the freedom of trade and commerce. Traffic regulations, registration of motor vehicles for plying in the State, collection of toll have not been treated to be restriction in freedom of trade and commerce.

304 . The above discussion makes it clear that what has been expressly prohibited in

Article 302 – 306 are all restrictions in the freedom of trade and commerce which shall obviously contravene Article 301, but there may be other instances when a law is treated to be restriction although not expressly enumerated in Part 302 to 306 . We may clarify that Article 301 is not attracted in a legislation which does not contain any kind of restriction to the freedom of trade and commerce. The question of applicability of Part XIII arises only when the legislation contains restrictions which hamper, restrict, impede and adversely affect the freedom of trade and commerce directly & immediately.

I. WHETHER 'DIRECT AND IMMEDIATE EFFECT TEST' AS LAID DOWN IN ATIABARI AND APPROVED IN AUTOMOBILE TRANSPORT IS NO LONGER A CORRECT TEST

305. Gajendragadkar, J., speaking for majority in Atiabari and immediately impede the trade are hit by Article 301. Following was held at page 860:

> "Thus considered we think it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Article 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that would fall within the purview of Article 301."

306. Das J.,in Automobile Transport also approved the direct and immediate effect test. Following was stated at page 523:

> "....For the tax to become a prohibited tax it has to be a direct tax the effect of which is to hinder the movement part of trade."

307. Subba Rao, J., concurring with the above view has also stated at page 550:

> " If a law directly and immediately imposes a tax for general revenue purposes on the movement of trade, it would be violating the freedom. On the other hand, if the impact in indirect and remote, it would be unobjectionable."

308. Gajendragadkar, J., in Atiabari Tea Company had also referred to two Privy Council judgments, namely, *James Vs. Commonwealth of Australia* [48] and judgment of Lord Porter in, *Commonwealth of Australia and Others Vs. Bank of New South Wales and Another*[49] It is further relevant to note that Gajendragadkar, J., was conscious of the fact that political and historical background of the federal polity adopted by Australian Commonwealth and the setting of the Constitution of India, the distribution of powers and general scheme is entirely different. The caution noted by Gajendragadkar, J., was in following words:

> "Before we conclude we would like to refer to two decisions in which the scope and effect of the provisions of S. 92 of the Australian Constitution came to be considered. We have deliberately not referred to these decisions earlier because we thought it would be unreasonable to refer to or rely on the said section or the

decisions thereon for the purpose of construing the relevant Articles of Part XIII of our Constitution. It is commonplace to say that the political and historical background of the federal polity adopted by the Australian Commonwealth, the setting of the Constitution itself, the distribution of powers and the general scheme of the Constitution are different, and so it would not be safe to seek for guidance or assistance from the Australian decisions when we are called upon to construe the provisions of our Constitution."

309. It is useful to refer to observations made by Lord Porter in Commonwealth of Australia & others(supra), which are "In this labyrinth there is no golden thread. But it seems that two general propositions may be accepted; (I.) that regulation of trade, commerce and intercourse among the States is compatible with its absolute freedom, and (2.) that s.92 is violated only when a legislative or executive act operates to restrict such trade, commerce and intercourse directly and immediately as distinct from creating some indirect or consequential impediment which may fairly be regarded as remote."

310. Shri Rakesh Dwivedi, learned Senior Advocate has contended that the Australian cases laying down 'direct and immediate effect test', which were relied by this Court in Atiabari, having been subsequently not followed by Australia High Court itself, the direct and immediate effect test should not be recognised for purposes of Article 301. Shri Dwivedi has referred to *Cole Vs. Whitfield* [50]He submits that 7-Judges Bench in Cole Vs. Whitfield has held that the operation test has failed to achieve unanimity. Shri Dwivedi submits that now the test which has been approved both by Australian High Court and U.S. Supreme Court is non-discriminatory test. He submits that preventing preferences and discrimination is the main factor for achieving the goal of creating free trade as accepted in Cole Vs. Whitfield. He submits that in Cole Vs. Whitfield following

> "In relation to both fiscal and non-fiscal measures, history and context alike favour the approach that the freedom guaranteed to interstate trade and commerce under s. 92 is freedom from discriminatory burdens in the protectionist sense already mentioned."

311. James Vs. Commonwealth of Australia (supra) was treated to have provided support for the development of the doctrine of criteria of operation. Cole Vs. Whitfield gave various reasons for disapproving the operation theory. Some of the reasons given are as follows:

> "First, in some respects the protection which it offers to interstate trade is too wide. Instead of placing interstate trade on an equal footing with intrastate trade, the doctrine keeps interstate trade on a privileged or preferred footing, immune from burdens to which other trade is subject."
>
> "The second major reason for rejecting the doctrine as an acceptable interpretation of s. 92 is that it fails to make any accommodation for the need for laws genuinely regulating intrastate and interstate trade. The history of the movement for abolition of colonial protection and for the achievement of intercolonial free trade does not indicate that it was intended to prohibit genuine non-protective regulation of intercolonial or interstate trade. The criterion of

operation makes no concession to this aspect of the section's history. In the result there has been a continuing tension between the general application of the formula and the validity of laws which are purely regulatory in character. Judged by reference to the doctrine, the validity of a regulatory law hinged on whether it imposed a burden on an essential attribute or on a mere incident of trade or commerce."

312. As noted above, our Constitution framers were well aware of the provisions of the Australian Constitution and the difficulties which arose in the Australia and different views expressed on the interpretation of Section 92, the Constitution framers though took inspiration from Section 92 but they did not stop there, rather they expressly provided for qualification to the right and freedom guaranteed under Article 301 by Article 302 – 306. Learned counsel for the State also in their submissions have contended that the Australian judgments pertaining to Constitution of Australia as well as the judgments of the U. S. Supreme Court are not directly applicable with regard to the interpretation of Part XIII. However, now it is contended by Shri Dwivedi that since the Australian High Court has now abandoned the operation test, this Court may also review the test as was laid down in Atiabari.

313. We have already noticed that in Atiabari in all the three opinions expressed by Sinha, C.J., and Gajendragadkar, J., and Shah, J., it was noted that in our Constitution, there is a departure from Australian Constitution and the Australian judgments are not relevant. Justice Gajendragadkar, has referred to two Privy Council judgments dealing with Australian Constitution to know how judicial minds have responded to the challenge presented by similar provisions. In the above spirit, references of those two Privy Council judgments were made. Thus Gajendragadkar, J., did not base his judgment on the test, which was laid down in the Australian judgments but found justification for his conclusion from the aforesaid judgments. Further, the primary reason why the Australian High Court in Cole Vs. Whitfield rejected the 'trade and immediate effect test' is, that because the freedom guaranteed under Section 92 applies only "between the States" i.e. to the interstate trade, i.e., The doctrine accordingly ended up discriminating against intrastate trade as it provided some sort of immunity to interstate transactions which intrastate transaction did not enjoy. We have already extracted the reasons given by Cole Vs. Whitfield, whereas in Part XIII of the Constitution, the Constitution framers had provided for non-discriminatory taxation between the intrastate and interstate trade with provision for dealing with all situation including a case whether restriction has to be imposed, on both interstate or intrastate trade that is Article 304(b). Although the Australian High Court rejected the idea of 'direct and immediate effect test' as being artificial, this Court has continued to adopt the said doctrine whenever legislation is decided on the touchstone of reasonable restriction and the doctrine has been applied consistently in the vast number of cases for decades which have stood the test of time.

314. Shri Dwivedi has also referred to American cases and contends that free trade immunity, which was propounded in *Spector Motor Services, Inc. Vs. O'Connor*[51] *had been overruled in Complete Auto Transit Vs. Brady*[52] Shri Dwivedi submits that in Complete Auto, it was held that 'it was not the purpose of the commerce class to relieve

those engaged in interstate commerce from their just share of State tax burden even though it increases the cost of doing business'. Shri Dwivedi, further relies on *State of Maryland Vs. State of Louisiana*[53] where it was observed, “one of the fundamental principles of commerce class jurisprudence is that no State, consistent with the commerce class, may or impose tax which discriminates against interstate commerce ". Shri Dwivedi submits that the U.S. Supreme Court has also moved to non-discriminatory test. He submits that even in Cole Vs. Whitfield, the Complete Auto Transit Vs. Brady was noticed. The commerce class of the American Constitution Article 1, Section 8, Clause 3 provides "to regulate commerce with foreign nations and among the several States and with the Indian tribes;" Part XIII of the Constitution has not adopted the American model and the interpretation on the commerce class is hardly relevant for interpretation of Part XIII.

315. Non-discriminatory taxation by State in reference to interstate and intrastate trade is ingrained in Article 304(a) itself, and no abstract theory needs to be referred to for following Non-discriminatory Theory.

316. We are thus of the view, that the concept as evolved in Australia and America with regard to freedom of trade and commerce, cannot be adopted in respect of interpretation of our Constitution, despite arguing against the relevance of foreign judgments, the States themselves are now relying on the foreign judgments in context of 'direct and immediate effect test theory'. The change in the legal position in Australia and America does not have any bearing on the Indian legal position as our Constitutional framework is different from those countries.

317. It is further contended before us that sometimes, it becomes difficult to draw a line as and when, legislation/taxation shall impede freedom of trade, commerce And intercourse and it becomes difficult for Court to apply any objective criteria for finding out the demarcation line. No hard and fast formula can be laid down to determine as to whether a particular legislation/taxation violates rights of freedom of trade and commerce under Article 301. It is for the Court to examine facts of each case and come to a conclusion. In this context, observation of Subba Rao , J., is pertinent to be referred to. Referring to observation of Dixson, C.J., following was stated by Subba Rao, J.:

> "Dixon, C.J., in Commonwealth Freighters Proprietary Limited v. Sneddon, gives a very cogent answer to such an argument in a Different context. The learned chief
> Justice said:
>
> "Highly inconvenient as it may be, it is true of some legislative powers limited by definition, whether according to subject-matter to purpose or otherwise, that the validity of the exercise of the power must sometimes depend on facts, facts which some how must be ascertained by the court responsible for deciding the validity of the
> Law All that is necessary is to make the point that if a criterion of constitutional validity consists in matter of fact, the fact must be ascertained by the court as best it

can, when the court is called upon to pronounce upon validity."

I entirely agree with these observations. It is common place to point out that intricate problems come before a court involving decision on different and complicated aspects of human activity. Questions involving science, medicine, engineering, geology, biology, economics, Psychology, etc. all come for judicial scrutiny, and I have never heard any court saying that it is difficult to decide upon such a question and, therefore, the proceeding raising such a question is outside the jurisdiction of such a court. In saying this, I am not ignoring the difficulties inherent in a problem of fixing the rate of taxes by a court. Experience shows that the court applies certain presumptions, such as that of the wisdom, knowledge and the good intentions of the Legislature, and does not also meticulously go in to the question, but only looks at the broad features. On the argument of learned counsel when it is permissible and possible for a court to ascertain whether a tax is fiscal or regulatory, I do not see how it becomes impossible, though it may be difficult, to hold whether a fiscal tax is reasonable or not. The distinction lies not in the nature of the enquiry but only in degree. That apart, no restriction, if it is unreasonable, can be more deleterious to the freedom than the imposition of fiscal burden on it, which may in certain circumstances destroy the very freedom."

318. In view of foregoing discussion, we are of the view that submission raised on behalf of the learned counsel for the State that 'direct and immediate effect test' is no longer a correct test, cannot be accepted. As observed above, each case has to be determined on facts of each case. The 'direct and immediate effect test' as laid down in Atiabari and approved in Automobile Transport still holds good.

J. COMPENSATORY TAX THEORY

319. Two related issues pertaining to a tax which is compensatory in nature have been framed by us in the beginning of hearing. Those are a part of Question No.2, i.e., "Can a tax which is compensatory in nature also fall foul Article 301 of the Constitution ?" and "What are the tests for determining whether the tax or levy is compensatory in nature"? Learned counsel appearing for the parties have made elaborate submissions on the concept of compensatory tax and other related issues. Most of the learned counsel appearing for the petitioners as well as respondents-States have expressed their reservation regarding compensatory tax theory. Majority of counsel are at agreement that judicial evaluation of compensatory tax theory was uncalled for and the compensatory tax theory is not compatible with a constitutional provision of Part XIII. It is submitted that compensatory theory has been judicially evolved by Seven Judge Bench in Automobile Transport case (supra) and the majority opinion had upheld the provisions of Rajasthan Motor Vehicles Taxation Act, 1951 holding it to be compensatory tax. In view of the serious reservation expressed by the learned counsel for the parties on the compensatory tax theory, it is necessary for us to examine the concept in some detail.

320. The compensatory tax theory as evolved in Automobile Transport was soon

doubted by the Constitution Bench in *Khyerbari Tea Company Ltd. v. State of Assam*[54], Gajendragadkar, J. looking into the nature of the compensatory tax theory, opined that the same is required to
be reconsidered by a larger Bench, he, however, noted that since the legislation was not tried to be saved on the basis of compensatory tax theory, the question was not further pursued. Gajendragadkar, J. made following observation:

> "According to the majority view in the case of Atiabari Tea Co., if an Act is passed under Art. 304(b) and its validity is impeached, then the State may seek, to justify the Act on the ground that the restrictions imposed by it are reasonable and in the public interest, and in doing so, it may, for instance, rely on the fact that the taxes levied by the impugned Act are compensatory in character. On the other hand, according to the majority decision in the Automobile Transport (Rajasthan) case, compensatory taxation would be outside Art.301 and cannot therefore, fall under Art.304(b). If in the present case it had been urged before us that the tax levied by the Act is compensatory in character, it would have been necessary to consider the question once again by constituting a larger Bench."

321. The question as to what are the tests for determining whether a tax or levy is compensatory in nature becomes secondary when we have to examine sustainability of the compensatory theory itself.

322. What is the tax ? What are the ingredients of taxation ? Thomas M. Cooley in “A Treatise on the Constitutional Limitations" defined the taxes in following words:

> “Taxes are defined to be burdens or charges imposed by the legislative power upon persons or property, to raise money for public purposes. The power to tax rests upon necessity, and is inherent in every sovereignty. The legislature of every free State will possess it under the general grant of legislative power, whether particularly specified in the constitution among the powers to be exercised by it or not.. "

323. Chief Justice, *Marshall in M'Culloch vs. State of Maryland*[55], while examining the nature of taxing power stated:

> “It is admitted, that the power of taxing the people and their property, is Essential to the very existence of government, and may be legitimately government may choose to carry it. The only security against the abuse of this power, is found in the structure of the government itself. In imposing a tax, the legislature acts upon its constituents. This is, in general, a sufficient security against erroneous and oppressive taxation."

324. A Seven Judge Bench of this Court in *Commissioner, Hindu Religious Endowments, Madras vs. Sri Lakshmindra Thirtha Swamiar of Sri Shirur Mutt*[56], has given definition of tax which has been repeatedly quoted and relied by this Court in large number of subsequent judgments. In paragraph 45 following was stated:

"45. A neat definition of what "tax" means has been given by Latham, C.J. of the High Court of Australia in Matthews v. Chicory Marketing Board. "A tax", according to the learned Chief Justice, "is a compulsory exaction of money by public authority for public purposes enforceable by law and is not payment for services rendered". This definition brings out, in our opinion, the essential characteristics of a tax as distinguished from other forms of imposition which, in a general sense, are included within it. It is said that the essence of taxation is compulsion, that is to say, it is imposed under statutory power without the taxpayer's consent and the payment is enforced by law. The second characteristic of tax is that it is an imposition made for public purpose without reference to any special benefit to be conferred on the payer of the tax. This is expressed by saying that the levy of tax is for the purposes of general revenue, which when collected forms part of the public revenues of the State. As the object of a tax is not to confer any special benefit upon any particular individual, there is, as it is said, no element of quid pro quo between the taxpayer and the public authority. Another feature of the taxation is that as it is a part of the common burden, the quantum of imposition upon the taxpayer depends generally upon his capacity to pay."

325. It is an accepted proposition that one of the characteristics of tax is that it is an imposition made for public purpose without reference to any special benefit to be conferred on the payer of the tax. The taxes imposed by the Legislature, apart from being source of Revenue is also expended for various public welfare measures and when it's object is in no way connected with the public interest or public welfare it loses its character of taxation, becomes a levy which is unconstitutional.

326. Das, J. delivering majority opinion in Automobile Transport case, in his judgment has referred to Rajasthan Motor Vehicles Taxation Act, 1951 as compensatory with whose opinion Subba Rao, J. also concurred.

327. Das, J. for coming to the conclusion that 1951 Act is a compensatory in nature has referred to judgments of Australian High Court and the judgment of the Privy Council wherein validity of various statutes in the context of freedom of trade and commerce granted under Section 92 of the Constitution of Australia were considered. Das, J. has referred to following judgments:

(i) Duncan v. The State of Queensland, (1916) 22 C.L.R. 556;

(ii) Mc Carter v. Brodie, (1950) 80 C.L.R. 432;

(iii) Hughes and Vale Proprietary Ltd. v. State of New South Wales, (1955) A.C. 241;

(iv) Armstrong v. State of Victoria No.2, (1957) 99 C.L.R. 28;

(v) Commonwealth of Australia v. Bank of New South Wales, (1950) A.C. 235;

(vi) Commonwealth Freighters Property Ltd. v. Sneddon, (1959) 102 C.L.R. 280.

328. The Australian Constitution provides under Section 92 'trade, commerce and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free'. In the above cases, Australian High Court and Privy Council had occasion to examine the challenge to various statutes framed by the States on the ground that these St-atutes violate freedom of trade and commerce, as guaranteed under Section 92. Section 92 itself does not provide for any qualification or exception to the freedom, in *Duncan and Others V. State of Queensland and Another*[57] Chief Justice Griffith, while construing the expression free had made following observations:

> "But the word 'free' does not mean extra legam and any more than freedom means 'anarchy' we boast of being absolutely free people, but that does not mean that we are not subject to law. "

329. The most of the cases of Australian High Court which have been referred to and relied by Das, J. were the transport cases wherein various sections were enacted for registration, licensing and realisation of fee/charge from motor vehicles, goods carriages in course of inter-State and intrastate trade and commerce.

330. Justice Das has specifically referred to dissenting opinion of Fullagar, J. in *McCarter and Another V. Brodie*[58], in which case the Parliament of Victoria had passed an Act, namely, Transport Regulation Act, 1933-47 which provided that a commercial goods vehicle should not operate on any public highway unless licensed in accordance with Act. A fee was to be paid for license, by an amendment further fee was imposed to be calculated at an annual rate determined from time to time by referring to the load capacity of the vehicle in respect of which license was sought to.

331. Chief Justice Latham delivered his opinion for the Court, after referring to various earlier decision of Australian High Court and Privy Council. Chief Justice held that the regulation of trade, commerce and intercourse in the States is compatible with absolute freedom envisaged under Section 92 and the freedom is violated only when statute operates to restrict such trade and commerce, directly and immediately, it was said:-

> "This quotation follows an express statement that regulation of trade, commerce and intercourse among the States is compatible with absolute freedom and that s. 92 is violated only when a legislative or executive act operates to restrict such trade, commerce and intercourse directly and immediately, as distinct from creating some indirect or consequential impediment which may fairly be regarded as remote. Thus the Privy Council in the Banking Case expressly rejected the proposition that s. 92 precluded Parliaments (Commonwealth or State) from in any way regulating or controlling inter-State trade and commerce, and a statement of the law was selected for approval which defined the relevant criterion as the distinction between regulation which was permitted, and prohibition, which was not permitted. The result is that s.92 does not mean that inter-State trade and commerce is to be free from control by law. In a

passage to which I have just referred their Lordships held that if laws have only an indirect effect in relation to inter-State trade and commerce they are not invalidated by s. 92."

332. Justice Fullagar, who delivered a dissenting opinion had examined in detail the nature of legislation which can be termed as regulatory and those which cannot be held to be prohibiting the trade. In his opinion, His Lordship has illustrated his point by giving various examples. He was of the view that permitted regulations as explained do not impede freedom carrying out under Section 92, however, there may be circumstances when even regulatory statutes impede the freedom. Following was observed:

"....The distinction between what is merely permitted regulation and what is a true interference with freedom of trade and commerce must often, as their Lordships observed, present a problem of great difficulty, though it does not, in my opinion, present any real difficulty in the present case. We may begin by taking a few examples, confining out attention to the subject matter of transportation, which is now under consideration. The requirements of the Motor Car Acts of Victoria afford very good examples of what is clearly permissible. Every motor car must be registered : we may note in passing that there is no discretionary power to refuse registration. A fee, which is not on the face of it unreasonable, must be paid on registration. Every motor car must carry lamps of a specified kind in front and at the rear, and in the hours of darkness these lamps must be alight if the car is being driven on a road. Every motor car must carry a warning device, such as a horn. A motor car must not be driven at a speed or in a manner which is dangerous to the public having regard to all
the circumstances of the case. Other legislation of the State-Parliamentary or subordinate-prescribes other rules. In certain localities a motor car must not be driven at more than a certain specified speed. The weight of the load which may be carried by a motor car on a public highway is limited. The driver of a motor car must keep to the left in driving along a highway. He must not overtake another vehicle on a curve in the road which is marked by a double line in the centre. He must observe certain "rules of the road" at intersections: for example, the vehicle on the right has the right of way. Such examples might be multiplied indefinitely. Nobody would doubt that the application of such rules to an inter-State trader will not infringe s.92. And clearly in such matters of regulation a very wide range of discretion must be allowed to the legislative body. When we ask why such rules do not infringe s.92, I think that commonsense suggests a fairly clear and satisfactory answer. The reason is that they cannot fairly be said to impose a burden on a trader or deter him from trading: I w-ould be foolish, for example, to suggest that my freedom to trade between Melbourne and Albury is impaired or hindered by laws which require me to keep to the left of the road and not drive in a manner dangerous to the public. Of course, even rules of the kind which I have taken as examples could be made to operate as a burden or deterrent in a high degree. Let me take an example. The town of Wangaratta is in Victoria, some fifty miles by road from the border between Victoria and New South Wales. It is on the Hume Highway, which is the busy main highway between Melbourne and Sydney. A law which provided that a motor car should

not travel on that highway at greater speeds than thirty miles per hour within the limits of towns and sixty miles per hour outside towns would not impede or interfere with the trade of persons carrying goods for reward between Melbourne and Sydney; their trade would remain 'free.' But let me suppose a law that no person should drive a motor car between Wangaratta and the border at a speed exceeding one mile per hour. We should instantly say that such a law interfered with the freedom of inter-State trade. It would operate as a burden and a deterrent to the trader by making the journey economically impossible. The examples which I have taken seem clear. On which side of the line a particular case falls will, of course, be a question of fact "

333. The above opinion, expressed by Fullagar, J. was specifically approved by Privy Council in *Hughes and Vale Proprietary Ltd. V. State of New South Wales and Others*[59] The Privy Council has noticed that the problem before the Australian High Court has been to define The qualification in the Constitution which is left unqualified. It held that the expression free 'under Section 92 though emphasized by the accompanying, absolutely must
receive some qualification'. Privy Council laid down following two general propositions:

"But it seems that two general propositions may be accepted: (1) that regulation of trade, commerce and intercourse among the States is compatible with its absolute freedom, and (2) that section 92 is violated only when a legislative or executive act operates to restrict such trade, commerce and intercourse directly and immediately as distinct from creating some indirect or consequential impediment which may fairly be regarded as remote. In the application of these general propositions, in determining whether an enactment is regulatory or something more, or whether a restriction is direct or only remote or incidental, there cannot fail to be differences of opinion. The problem to be solved will often be not so much legal as political, social, or economic, yet it must be solved by a court of law."

334. In Armstrong and Others (supra), the provisions of Commercial Goods Vehicle Act, 1955 were under challenge on the ground that it violated Section 92. The provisions require
the owner of every commercial goods vehicle of loading capacity exceeding four tonnes and not engaged in conveying certain specified classes of goods to pay contribution towards the compensation for wear and tear costs to public highways. The High Court held that imposition of charge for using the roads of State is not necessarily inconsistent with the freedom of interstate trade and commerce.

335. The Chief Justice Dixson has held that a State can not single out inter-State transport or transport generally for particular charge, such charge was held not to be compensatory
for the use made of them. Following observations were made:

"It appears to me that on a proper scrutiny of Pt. II of the Motor Car Acts 1951-56 (Vict.) and the second schedule it must be seen that no room exists for the

grounds upon which it has been sought to reconcile with s. 92 the imposition upon vehicles exclusively engaged in inter-State commerce of the rates contained in sub-par.(b) of par. B of the schedule. (1) The exaction cannot be regarded simply as a fee contributing to the cost of registration a service in the interest of motor car owners and drivers and others so that it is nothing but an incident or adjunct of the traffic. (2)
It cannot be treated as another contribution to the maintenance of the highways compensatory for the use made of them. (3) It cannot be justified as a tax upon the ownership or possession of a chattel considered independently of the use of the chattel in the carriage of persons or goods, including the inter-State carriage of persons or goods. (4) It cannot be treated as involving no appreciable burden upon the possession of a motor vehicle as a means of inter-State carriage and movement."

336. Referring to an earlier judgment of the High Court, William, J. in his concurring opinion has referred to indicia presence of which may prove a charge as truly compensatory:

"In the joint judgment of Dixon C.J., McTiernan and Webb JJ. in Hughes & Vale Pty.
Ltd. v. State of New South Wales [No. 2] (3) the following passage appears: "Prima facie it" (that is the legislation imposing the charge" "will present that appearance" (that is the appearance of a real attempt to fix a reasonable recompense for the use of the highway) "if it is based on the nature and extent of the use made of the roads (as for example if it is a mileage or ton-mileage charge or the like); if the proceeds are devoted to the repair, upkeep, maintenance and depreciation of relevant highways, if inter-State transportation bears no greater burden than the internal transport of the State and if the collection of the exaction involves no substantial interference with the
journey. The absence of one or all of these indicia need not necessarily prove fatal, but in the presence of them the conclusion would naturally be reached that the charge was truly compensatory."

337. From the above, it is clear that Australian High Court have read qualifications under Section 92 of the Act. The statutes regulating the trade which have no direct effect on trade and commerce and levying compensatory charge were held to be compatible with freedom under Section 92.

338. Another judgment of the Privy Council which have been referred to by Das, J. was judgment in Commonwealth of *Australian and Others V. Bank of New South Wales and Others*[60]. The Privy Council laid down as following:

"But it appears to their Lordships that, if these two tests are applied: first, whether
the effect of the Act is in a particular respect direct or remote; and, secondly, whether in its true character it is regulatory, the area of dispute may be considerably narrower. It is beyond hope that it should be eliminated."

339. After referring to above cases, Das, J. recorded the conclusion in following words:

> "We have, therefore, come to the conclusion that neither the wide interpretation nor the narrow interpretations canvassed before us are acceptable. The interpretation which was accepted by the majority in the Atiabari Tea Co. case is correct, but subject to this clarification. Regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of the restrictions contemplated by Article 301 and such measures need not comply with the requireme4nts of the proviso to Article 304(b) of the Constitution."

340. The law that if a statute is compensatory in nature, it is beyond Part XIII and does not violate Article 301, was consistently followed after the above pronouncement in Automobile Transport. All State Legislations, after the above pronouncement have been challenged and saved on many grounds including on the above exceptions, as laid down in Automobile Transport. There have been various tests laid down in different cases decided by this Court to find out as to whether State Legislation is compensatory in nature or not. In Messers Bhagatram Rajiv kumar, this Court had held that if there is some link between the tax and trading facility, directly or indirectly, the statute is compensatory and is not open to challenge under Article 301. State of Bihar and Others (supra) following the earlier judgment again reiterated the test of some connection between the tax and trading facility provided. Both the above judgments were doubted and referred to a Constitution Bench. A Constitution Bench of this Court in Jindal Stainless Steel Ltd. Vs. State of Haryana (supra) had already overruled the aforesaid two judgments. Even the test as laid down by the Constitution Bench in Jindal Stainless Steel Ltd.(2) did not quell the controversy and in the reference made by the Constitution Bench in Jaiprakash Associates(Supra), one of the questions referred was with regard to the test to prove whether levy is compensatory levy.

341. At this juncture, it is also relevant to refer to concept of "compensatory tax" as developed in United States of America.

342. The first case to be noticed is *Hinson v. Lott, 8 Wall*[61], The State of Alabama passed a statute by Section 13 of which all dealers on sale of liquor within the limit of the State were required to pay tax of 5 0 cent per gallon. A merchant of another state against whom collection of tax was sought to be enforced, questioned the tax. Tax was held to be valid by Supreme Court of Alabama and the matter was taken by the merchant to the Supreme Court of the United States. The Supreme Court held that tax is not violative of inter-State trade and commerce. It was noticed that no greater tax is held on the liquor brought into the State than on those manufactured out of the State and the tax on the liquor necessary to make tax equal on all liquors sold in the States. Following was laid down:

> "A tax is imposed by the previous sections of the same act of fifty cents per gallon on all whiskey and all brandy from fruits manufactured in the State. In order to collect this tax, every distiller is compelled to take our a license and to make

regular returns of the amount of distilled spirits manufactured by him. On this he pays fifty cents per gallon. So that when we come in the light of these earlier sections of the act, to examine the 13th, 14th, and 15th sections, it is found that no greater tax is laid on liquors brought into the State than on those manufactured within it. And it is clear that whereas collecting the tax of the distiller was supposed to be the most expedient mode of securing its payment, as to liquors manufactured within the State, the tax on those who sold liquors brought in from other States was only the complementary provision necessary to make the tax equal on all liquors sold in the State. As the effect of the act is such as we have described, and it institutes no legislation which discriminates against the products of sister States, but merely subjects them to the same rate of taxation which similar articles pay that are manufactured within the State, we do not see in it an attempt to regulate commerce, but an appropriate and legitimate exercise of the taxing power of the States."

343. The next case needs to be noted is judgment of the U.S. Supreme Court in *Harold H. Henneford et al., V. Silas Mason Company, Inc.*[62],

344. Justice Cardozo delivered the opinion of the Court and upheld the compensatory tax. The facts of the case had been noted in the judgment which reads as follows:

"A statute of Washington taxing the use of chattels in that state is assailed in this suit as a violation of the commerce clause (Constitution of the United States, article I, 8) in so far as the tax is applicable to chattels purchased in another state and used in Washington thereafter."

"Only two of these taxes are important for the purposes of the case at hand, the 'tax on retail sales,' imposed by title III and the compensating tax,' imposed by title IV on the privilege of use. Title III provides that after May 1, 1935, every retail sale in Washington, with a few enumerated exceptions, shall be subject to a tax of 2% of the selling price. Title IV with the heading 'compensating tax,' provides that there s-hall be collected from every person in the state 'a tax or excise for the privilege of using within this state any article of tangible personal property purchased subsequent to April 30, 1935, ' at the rate of 2% of the purchase price, including in such price the cost of transportation from the place where the article was purchased."

345. However, there were several exceptions. Sub Division(b) provides that the use tax shall not be laid unless the property has been brought at retail and (c) tax shall not apply to the use of any article of tangible personal property, the sale or use of which had already been subject to a tax equal to or in excess of that imposed. Those users of the State who have produced in the State were thus not to pay the use tax whereas use tax was always payable where the user had acquired the property by retail purchase in or from another State, Unless he has paid sales or use tax elsewhere before bringing it to Washington. Challenge was made on the ground that it violates the commerce class of the U.S. Constitution. Justice Cardozo held that the equality is a theme that runs through the above sections. Following are the reasons which

were given for upholding the above compensating tax:

> "Equality is the theme that runs through all the sections of the statute. There shall be a tax upon the use, but subject *to an offset if another use or sales tax has been paid for the same thing. This is true where the offsetting tax became payable to Washington by reason of purchase or use within the state. It is true in exactly the same measure where the offsetting tax has been paid to another state by reason of use or purchase there. No one who uses property in Washington after buying it at retail is to be exempt from a tax upon the privilege of enjoyment except to the extent that he has paid a use or sales tax somewhere. Every one who has paid a use or sales tax anywhere, or, more accurately, in any state, is to that extent to be exempt from the payment of another tax in Washington. When the account is made up, the stranger from afar is subject to no greater burdens as a consequence of ownership than the dweller within the gates. The one pays upon one activity or incident, and the other upon another, but the sum is the same when the reckoning is closed. Equality exists when the chattel subjected to the use tax is bought in another state and then carried into Washington. It exists when the imported chattel is shipped from the state of origin under an order received directly from the state of destination. In each situation the burden borne by the owner is balanced by an equal burden where the sale is strictly local."

346. The contents of the compensatory tax doctrine were reiterated by the U.S. Supreme Court in Associated Industries Of Missouri, et al., *V. Janette M. Lohman*[63] In the above cases State of Missouri imposed a uniform state-wide use tax on all goods purchased outside the State and stored, used or consumed within the State. The tax was purportedly designed to compensate for sales tax imposed by local jurisdiction on sales of goods in the State. Local sales tax varied very widely, on several occasions the use tax exceeded the sales tax. The tax was challenged, as violating interstate commerce on the ground that it placed greater burden on interstate trade, referring to judgment of Justice Cardozo in Silas Mason; Following was stated:

> "In Silas Mason, Justice Cardozo was explicit in explaining for the Court that the compensatory tax doctrine requires precision to ensure that, upon the "reckoning" of "account(s)," the "sum" on the interstate side of the ledger is "the same" as that on the intrastate side. 300 US, at 584, 81 L Ed 814, 57 S Ct 524. More recently, we have reiterated that strict parity is demanded by the compensatory tax doctrine as we have explained that a compensatory tax leaves a consumer free to make choices "without regard to the tax consequences"; if he purchases within the State he may pay a tax, but if he purchases from outside the State he will pay a "tax of the same amount."

347. Another case which needs to be noted is *Oregon Waste Systems V. Department of Environmental Quality of the State of Oregon* [64]The U.S. Supreme Court noticed that compensatory tax doctrine has been recognised at least since 1869. Following was stated by the U.S. Supreme Court:

"At least since our decision in Hinson V. Lott, 8 Wall. 148 (1869), thes principl-es have found expression in the "compensatory" or "complementary" tax doctrine. Though our cases sometimes discuss the concept of the compensatory tax as if it were a doctrine unto itself, it is merely a specific way of justifying a facially discriminatory tax as achieving a legitimate local purpose that cannot be achieved through non-discriminatory means. See Chemical Waste, supra, at 346, n. 9 (referring to the compensatory tax doctrine as a "justification" for a facially discriminatory tax). Under that doctrine, a facially discriminatory tax that imposes on interstate commerce the rough equivalent of an identifiable and "substantially similar" tax on intrastate commerce does not offend the negative Commerce Clause. Maryland, supra, at 758-759. See also Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue, MANU/USSC/0058/1987: 483 U.S. 232, 242-243(1987); Armco, U.S., AT 643. To justify a charge on interstate commerce as a compensatory tax, a State must, as a threshold matter, "identify... the [intrastate tax] burden for which the State is attempting to compensate." Maryland, supra, at 758. Once that burden has been identified, the tax on interstate commerce must be shown roughly to approximate — but not exceed — the amount of the tax on intrastate commerce. See. e.g., Alaska v. Arctic Maid, MANU/USSC/0062/1961 : 366 U.S. 199, 204-205 (1961). Finally, the events on which the interstate and intrastate taxes are imposed must be "substantially equivalent"; that is, they must be sufficiently similar in substance to serve as mutually exclusive "proxies" for each other. Armco, supra, at 643. As Justice Cardozo explained for the Court in Henneford, under a truly compensatory tax scheme, "the stranger from afar is subject to no greater burdens as a consequence of ownership than the dweller within the gates."

348. Another judgment which needs to be noted is Fulton Corporation *V. Jenice H. Folkner, Secretary of Revenue of North Carolina*[65]. For valid compensatory tax three conditions were noticed by the U.S. Supreme Court in following words:

"Since Silas Mason, our cases have distiled three conditions necessary for a valid compensatory tax. First, "a State must, as a threshold matter, 'identify ... the [intrastate tax] burden for which the State is attempting to compensate.'" Oregon Waste, supra, at 103, 128 L Ed 2d 13, 114 S Ct 1345 (quoting Maryland v Louisiana, 451 US 725, 758, 68 L Ed 2d 576, 101 S Ct 2114 (1981). Second, "the tax on interstate commerce must be shown roughly to approximate-but not exceed-the amount of the tax on intrastate [516 US 333] commerce." Oregon Waste, 511 US, at 1103, 128 L Ed 2d 13, 114 S Ct 1345.

"Finally, the events on which the interstate and intrastate taxes are imposed must be 'substantially equivalent'; that is, they must be sufficiently similar in substance to serve as mutually exclusive 'proxies' for each other."

349 . The above cases of Supreme Court give different concept of compensatory tax as compared to cases in Australia as well as in Automobile Transport. In U.S., The compensatory tax doctrine was invoked to save facially discriminatory taxes imposed on interstate trade, to make interstate commerce bear a burden already borne by

intrastate commerce. In Automobile Transport compensatory tax has been referred to a tax or charge to provide for trade facilities like construction of road, bridges etc. which was treated as recompense to the traders who were required to pay tax.

350. Law of compensatory charge as developed in Australia was due to the fact that Section 92 did not contain any qualification to the absolute freedom of trade and commerce granted therein. Various qualifications and restrictions to the above freedom were culled out by judicial decisions of the High Court of Australia and Privy Council to justify the said qualifications and restrictions. The ratio contained in various judgments of the High Court of Australia and the Privy Council on Section 92 of the Constitution of Australia cannot
be a guiding factor for interpreting Part XIII of the Constitution of India.

351. The Constitution Bench of this Court in *State of Bombay v. R.M.D. Chamarbaugwala and another*[66], had sounded a caution in paragraph 35:

> "35. In construing the provisions of our Constitution the decisions of the American Supreme Court on the commerce clause and the decisions of the Australian High Court and of the Privy Council on Section 92 of the Australian Constitution should, for reasons pointed out by this Court in State of Travancore-Cochin v. Bombay Co. Ltd. be used with caution and circumspection. Our Constitution differs from both American and Australian Constitutions. There is nothing in the American Constitution corresponding to our Article 19(1)(g) or Article 301. In the United States the problem was that if gambling did not come within the commerce clause, then neither the Congress nor any State Legislature could interfere with or regulate inter- State gambling. Our Constitution, however, has provided adequate safeguards in clause (6) of Article 19 and in Articles 302-305. The scheme of the Australian Constitution also is different from that of ours, for in the Australian Constitution there is no such provision as we have in Article 19(6) or Articles 302-304 of our Constitution. The provision of Section 92 of the Australian Constitution being in terms unlimited and unqualified the judicial authorities interpreting the same had to import certain restrictions and limitations dictated by common sense and the exigencies of modern society. This they did, in some cases, by holding that certain activities did not amount to trade, commerce or intercourse and, in other cases, by applying the doctrine of pith and substance and holding that the impugned law was not a law with respect to trade, commerce or intercourse. The difficulty which faced the judicial authorities interpreting Section 92 of the Australian Constitution cannot arise under our Constitution, for our Constitution did not stop at declaring by Article 19(1)(g) a fundamental right to carry on trade or business or at declaring by Article 301 the freedom of trade, commerce and intercourse but proceeded to make provision by Article 19(6) and Articles 302-305 for imposing in the interest of the general public reasonable restrictions on the exercise of the rights guaranteed and declared by Article 19(l)(g) and Article 301."

352. Hidayatullah, J. in Automobile Transport itself held that the technique justifying laws as regulatory as evolved in Australia is not applicable while interpreting Article 301

of Constitution. Following observations were made by Hidayatullah, J. at page 639:

> "The technique of justifying laws as regulatory was evolved in Australia in view of the intractable language of s.92 without any indication of the circumstances in which the absolute freedom could be curtailed. The detailed provisions contained in Part XIII render such a construction of Art.301 at once unnecessary and impermissible. "

353. Gajendragadkar, J. in Khyerbari Tea Company Ltd.(supra) had also expressed opinion that compensatory or regulatory tax theory as introduced in the Australian decisions is not to be made applicable in Part XIII. Following was observed:

> "The majority view in the Atiabari case proceeded on the basis that the Australian decisions which dealt with the scope and effect of s.92 of the Australian Constitution would be of no assistance in constructing the effect of the provisions in Part XIII of our Constitution, because the legislative, historical and political background, the structure and the effect of the relevant provisions contained in Part XIII were in material particulars different from those of s. 92 of the Australian Constitution; s.92 is absolute in terms and on its literal construction, admits of no exceptions. The Australian decisions, therefore, had to introduce distinctions, such as compensatory or regulatory tax laws in order to take laws answering the said description out of the purview of s.92. In our Constitution, however, though Art. 301 is worded substantially in the same way as s.92, Art.302 and 304 provide for reasonable restrictions being imposed on the freedom of trade subject to the requirements of the said two Articles, and so, the problem facing of the said two Articles, and so, the problem facing judicial decisions in Australia and in this country in regard to the freedom of trade and the restrictions which it may be permissible to impose on it, is not exactly the same."

354. The answer to the question as to whether a compensatory tax is out of reach of Article 301 has to be found out from the Scheme of Part XIII of the Constitution itself and not from the theory of compensatory charge as evolved in Australia or United States of America. Two fundamental principles of taxes are:

> (i) that it is an imposition made for public purpose,
>
> (ii) without reference to any special benefit to be conferred on the payer of the tax.

355. The compensatory doctrine evolved in Automobile Transport is that compensatory tax is to compensate for facility extended, for example, wear and tear of the Road. The compensatory tax can be imposed only for public purpose which fact is not denied by any of the parties before us. Can it be said that a tax which is a compensatory in nature need not to be subject to restriction as contained in part XIII ? If it is accepted that once a tax is held compensatory tax it goes out of reach of Part XIII, it will be carving a new exception to Article 301 which is not contemplated in the constitutional scheme. The framers of the Constitution after providing for freedom of trade, commerce and

intercourse in Article 301 laid down exceptions to the said freedom in Article 302 to 306 . The exceptions laid down in the constitutional scheme are self-contained and no new exception can be added by judicial interpretation. Can a compensatory tax not impede trade, commerce and intercourse even if it is a non-discriminatory tax ? We take an example to illustrate the point. Entry Tax is imposed on vehicles carrying goods in a local area to the extent of 50% of the value of goods, the statute further declares that entire amount received from tax will be expended for providing facilities to the entrants in the local area, i.e., on roads, lights, free fooding, free lodging, facility for free servicing, repairs of the vehicles, etc.etc. Can the mere fact that entire amount collected is expended for providing facilities shall take out the statute from the scrutiny of Part XIII ? Answer has to be in negative. The fact that a tax statute compensates the payer of the tax does not take out the statute beyond Part XIII, all taxes, being for one or other public purposes. The tax legislation which professes to compensate the payer cannot take the tax legislation on a higher pedestal beyond the reach of Part XIII, making such legislation "not subject to Constitution". When all legislative power is "subject to Constitution" as per Article 245 and 246 of the Constitution, a legislation, namely, compensatory tax legislation cannot be said to be beyond Part XIII. Any such interpretation is clearly against the constitutional scheme.

356. Thus the judgments of the High Court of Australia and the Privy Council relied in Automobile Transport did not furnish a foundation for evaluation of compensatory tax theory in part XIII of the Constitution.

357. The scheme of Constitution of India indicates that wherever it was contemplated to insulate any provision from challenge, expressed provisions have been made to provide for such insulation. Article 31B is one of such examples which provides that none of the Acts and Regulations specified in IXth Schedule shall be deemed to be void or ever to have become void on the ground of such Act, Regulation or provision is inconsistent with or takes away or abridges any of the rights conferred by Part III. The Constitutional Scheme as delineated by Part XIII does not indicate that a particular type of legislation, i.e., compen-satory tax is out of Part XIII. Reading any such protection to compensatory tax legisla-tion is against the constitutional provision. We, thus, are of the opinion that the compensatory theory as evolved in Automobile Transport (supra) is not compatible to the constitutional scheme and a compensatory tax legislation cannot be insulated from challenge under Part XIII of the Constitution.

358. We may, however, observe that it is always open to scrutinize the true nature and character of legislation to decipher as to whether it contains any restriction on freedom of trade, commerce and intercourse violating Article 301. A legislation which is compensatory in nature may shed light while determining whether it contains restriction on trade, commerce and intercourse or facilitate the trade, commerce and intercourse. But all legislations be it a compensatory tax legislation or otherwise has to be tested in accordance with provisions of Part XIII of the Constitution. The ratio of judgment of Automobile Transport is overruled in so far as it lays down that the compensatory tax legislations are out of part XIII of the Constitution.

PART V "OUR CONCLUSIONS"

1. All legislative powers of the State are "subject to the Constitution" as per article 245 of the Constitution of India. Legislative power of the State is also subject to the limitation as provided in Part XIII of the Constitution.

2. Part XIII of the Constitution covers tax legislation which restrict freedom of trade, commerce and intercourse.

3. Word 'restriction' as used in Part XIII as well as in Article 304(b) of the Constitution includes tax legislation also.

4. For enabling a State to make a law under Article 3 04 (a) following two pre-conditions which are independent of each other have to be satisfied:-

(i) It may impose on goods imported from other States or the Union Territory any tax to which similar goods manufactured or produced in that State are subject.

(ii) So, however, as not to discriminate between goods so imported and goods so manufactured and produced.

5. Word "and" between Clause(a) and Clause(b) of Article 304 has to be read as joint and several. Both the meaning can be assigned, as per requirement of State legislation.

6. A law made by State legislature exercising the power under Clause(a) in Article 304 , which does not impose any restriction on the freedom of trade, commerce and intercourse need not comply with Article 304 (b), however, a law even though complying with Article 304(a) containing restriction on freedom of trade, commerce and intercourse is to obtain sanction of the President, as contemplated by proviso to Clause(b). The requirement of obtaining the previous sanction of the president has to be decided in accordance with the nature and content of the State Legislation.

7. The proviso of Article 304(b) is part of Constitutional Scheme which is neither against the federal structure of the Constitution nor affects the State's sovereignty.

8. Word 'restriction' used in Article 304(b) is wide enough to include restrictions placed both by fiscal or non-fiscal law.

9. State Legislature in exercise of its taxing power can grant exemption\set off to locally produced and manufactured goods only to a limited extent based on intelligible differentia which is not in nature of general\unspecified exemption.

10. The ratio of judgment of Video Electronics(supra) has to be read as justifying only exemption limited to specified category for a short period. Exemption in general terms for unlimited period cannot be approved. Any exemption can not be used as measure of discrimination between goods imported from

11. A law passed by State Legislature imposing tax only on the imported goods coming from other States and Union Territories and there being no similar tax imposed to the locally produced\manufactured goods, the law is not saved by Article 304(a) and violates Article 301.

12. A law imposing tax on goods imported from other States and Union Territories, facially taxing goods locally manufactured and produced but granting set off \exemption in general terms is discriminatory and violates Article 301.

13. What have been expressly prohibited under Article 302, 303 and 304 are restrictions in the freedom of trade and Commerce violating Article 301.Alawcontaining restriction impeding freedom of trade and commerce and intercourse which is not saved by Article 302, 303 and 304 violates Article 301.

14. The compensatory tax theory as judicially evolved in Automobile Transport is not compatible with the Constitutional provisions contained in Part XIII. The ratio in judgment of this Court in Automobile Transport to the extent that the legislation which is compensatory in nature is out of Article 301, cannot be approved and is overruled

15. All legislation, including a compensatory or regulatory as contained in Part XIII of the Constitution. The nature and content of legislation at best may shed light on the aspect as to whether it impede/restrict the freedom of trade, commerce and intercourse or facilitate the same.

PART VI OUR ANSWERS
QUESTION NO.1

Levy of a non-discriminatory tax may constitute infraction of Article 301 of the Constitution of India if it impedes the freedom of trade, commerce and intercourse. All taxes which contain restrictions to trade, commerce and intercourse, discriminatory or non-discriminatory infringe Article 301 unless they are saved under Article 302 – 304. Question NO.2 and

Question No.3

The compensatory tax theory as judicially evolved in Automobile Transport is not compatible to constitutional scheme as delineated by Part XIII of the Constitution. The Automobile Transport case in so far as it lays down that compensatory taxes are out of the reach of Article 301 cannot be approved. The nature and content of taxation at best may throw light on the aspect as to whether it contains restriction on freedom of trade, commerce and intercourse. The compensatory tax theory being not compatible with the Constitution, it is not necessary to answer Question No.3.

Question No.4

To find out as to whether Entry Tax levied by different States in the present batch of cases violates Article 301 of the Constitution, each statute has to be looked into and

examined as per our discussions and conclusions as above. A law made by State Legislature complying clause(a) of Article 304 and not containing any restriction on the freedom of trade, commerce and intercourse need not comply Article 304(b). However, a law even though complies with Article 304(a)but contains restrictions on freedom of trade, commerce and intercourse has to be routed through proviso to clause (b) of Article 304 of the Constitution. The compliance of Article 304(b) proviso whether required or not shall depend on the nature and content of the State legislation.

Answer to incidental questions.

(1) Levy of taxes is an attribute of a sovereign State as per Constitutional scheme and limited to the extent as provided in the Constitution.

(2) Article 245 read with Article 246 recognises the levying taxes on subject matter enumerated in List II of VIIth Schedule in accordance with limitations and restrictions contained in the Constitution of India.

(3) The power to make law and levy taxes reserved in favour of the State under Article 246 read with List II of VIIth Schedule is subject to Part XIII of the Constitution. Article 245 has to be read along with Article 246 for finding out the source of the legislative power.

(4) Part XIII (including Article 301) of the Constitution to which legislative power of State is subject, does not have effect of denuding any sovereign power of the State or effecting the federal structure of the Constitution.

(5) The levy of taxes is presumed to be in public interest.

(6) Levy of taxes which may be presumed to be in public interest still has to comply with Part XIII of the Constitution for it to be justified as reasonable restriction.

(7) Imposition of restriction by way of tax legislation under Article 304(b) is part of constitutional scheme and Presidential sanction has been provided to keep a check on the legislative power of the State impeding freedom of trade, commerce and intercourse. All legislative powers under the Constitution are subject to judicial review and the mere fact that a legislation passed under Article 304(b) is also subject to judicial review, in no manner, militants against the Constitutional scheme.

(8) There is no question of affecting the separation of power between the Legislature and judiciary on the ground that levy of taxes under Article 304(b) which contains restriction to the freedom of trade, commerce and intercourse have to be routed through the President of India as per the Constitutional scheme. The Constitution contains large number of provisions including Article 304(b) where a State legislation is subject to Presidential sanction which provisions are in accordance with the Constitutional scheme and does not affect the separation of power between the Legislature and judiciary. Article 304(b) enables the State Legislature to frame legislations containing restriction on freedom of trade, commerce and intercourse after routing the legislation

through proviso to Article 304(b). The question of judicial review arises only when there is challenge to such legislation. Judicial review of such legislation in no manner affects the separation of power.

(9) The compensatory tax theory as propounded in Automobile Transport is not compatible with the Constitutional scheme as delineated in the Part XIII of the Constitution. Framers of the Constitution have provided for all exceptions under which freedom of trade, commerce and intercourse guaranteed under Article 301 can be overridden, the compensatory tax not being included as one of the exceptions, the same cannot be added as an exception by any judicial interpretation. The compensatory tax theory brings dichotomy which is inconsistent with the language employed in Article 301.

[1](2010) 4 SCC 0595
[2](1961) 1 SCR 0809
[3](1963) 1 SCR 0491
[4](1995) Supp. (1) SCC 673
[5](1996) 9 SCC 0136
[6](2003) 8 SCC 060
[7](2006) 7 SCC 0241
[8](2006) 7 SCC 0271
[9](2009) 7 SCC 0339
[10](2010) 4 SCC 0595
[11](1961) 1 SCR 0809
[12](1965) 2 SCR 0908
[13](1975) 1 SCC 0375
[14](1980) 4 SCC 0697
[15](1960) 3 S.C.R. 0887
[16](1961) 3 S.C.R. 0077
[17](2005) 2 SCC 0215
[18](2005) 2 SCC 0215
[19](1936) AC 0578
[20](1973) 4 SCC 0225
[21](1977) 3 SCC 0592
[22](1994) 3 SCC 0001
[23](1955) 2 SCR 0164
[24](2012) 7 SCC 0106
[25](1966) AIR SC 0619
[26](1980) 4 SCC 0697
[27](1974) 4 SCC 0408
[28](1975) 1 SCC 0375
[29](2007) 7 VST 0367
[30](2002) 8 SCC 0182
[31](1963) Suppl. (2) SCR 435
[32](1988) 2 SCC 0568
[33](1988) 1 SCC 0743
[34](1990) 3 SCC 87
[35](1990) (Suppl.) SCC 0617
[36]AIR 1963 SC 1237
37(1990) 4 SCC 256
[38](1980) 4 SCC 0697
[39](1963) 2 SCR 0435
[40](1988) 1 SCC 743
[41](1964) 6 SCR 0261
[42](1996) 11 SCC 0039
[43](1952) SCR 607
[44](1981) 3 SCR 0092
[45](1981) 3 SCR 0107
[46](1975) 1 SCC 375
[47](1989) 3 SCC 0634
[48](1936) A.C. 0578
[49](1950) A.C. 235
[50](1988) 78 ALR 0042
[51]430 U.S. 289(1951)
[52]430 U.S. 274(1977)
[53]451 U.S. 0725
[54](1964)5 SCR 0975
[55]17 US 316 (1819)
[56](1954) SCR 1005: AIR 1954 SC 282
[57](1916) 22 CLR 0556
[58](1950) 80 CLR 432
[59](1955) A.C. 0241
[60](1950) A.C. 0235
[61]75 U.S. 148 (1869)
[62]300 U.S. 0577
[63]128 L Ed 2d 0639
[64]511 U.S. 93 (1994)
[65]516 US 325, 133 L Ed 2d 796
[66]AIR 1957 SC 0699