

**KERALA HIGH COURT**

Gannon Dunkerley and Co

Vs.

Sales Tax Officer

O.P. No. 25 of 1957

(Sankaran and M.S. Menon, JJ.)

11.03.1957

**JUDGMENT**

**M.S. Menon, J.**

1. The petitioner (Gannon Dunkerley and Co. (Madras) (Private) Ltd., was assessed to sales tax by the Sales Tax Officer, Second Circle, Mattancherry, on a total turnover of Rs. 2,23,197 in respect of the period 1-4-1955 to 31-3-1956. A portion of the said turnover, viz., Rs. 1,96,486 relates to "works contracts" and it is the liability to assessment of that portion of the turnover that is challenged before us.

2. Ext. A, the order of assessment dated 31-10-1956, shows that the sum of Rs. 1,96,486 was arrived at as follows :

"M.E.S. Department Willingdon Island.	Rs. 1,26,546-0-0
Power House construction at Perunjalkuthu.	Rs. 1,04,762-0-0
Caltex Petrol Pump at Ernakulam.	Rs. 19,058-0-0
	30,328-0-0
	Rs. 2,80,694-0-0
Less 80% ... ..	Rs. 84,208-0-0
Balance turnover ... ..	Rs. 1,96,486-0-0

3. Section 2 (1) of the Travencore-Cochin General Sales Tax Act, 1125 defines the expression "works contract" as follows :

"works contract' means any agreement for carrying out for cash or for deferred payment or other valuable consideration the construction fitting out, improvement or repair of any building, road, bridge, or other immovable property or the fitting out, improvement or repair of any movable property".

That the contracts concerned do come within the ambit of the definition is not disputed by the petitioner.

4. The main contention before us is the same as that advanced by the petitioner with success before the High Court of Madras in *Gannon Dunkerley and Co. (Madras), Ltd., v. The State of Madras*<sup>1</sup>, In that case it was held :

"The legislative power of the Provincial Legislature under the Government of India Act, 1935, to levy a tax on the sale of goods is confined and restricted only to the transaction of sale as understood by the Parliament of the United Kingdom in the law relating to the sale of goods and any attempt by the legislature to tax under the guise of or under the pretence of such a power transactions, which are wholly outside it, will be ultra vires and invalid. In the case of building contracts, where the amount is to be paid to the contractor either on a lump sum basis or according to a schedule of rates after measuring the quantities unless there is a contrary intention specifically to pass the property in the materials as and when they are brought to the site, the property in the materials passes only when they are fixed to the building whether they are bricks, doors or door frames or other materials.

There is no element of sale of materials in such a contract, as the contract is not in substance and in effect a contract to sell the materials as goods for a price stipulated between the parties, the ownership in which is to pass in accordance with the principles applicable to them and laid down in the Sale of Goods Act. The ultimate result of executing such a contract is to bring into existence immovable property and not movable property, and the contract therefore does not become a contract relating to sale of goods but it is only a contract to build. If the amendments relating to taxing of works contracts introduced in 1947 by the Madras Legislature are intended to catch in the net of tax the aforesaid building contracts, to that extent the amendments are ultra vires the Madras Legislature. Having regard to the terms of particular contracts, there may be an intention to pass the ownership in the materials for a price agreed upon between the parties, in which case there might be an element of sale of goods". (Head-note)

5. In *Banarsi Das v. State of Madhya Pradesh, 1955-6 STC 93*, the Nagpur High Court dissented from the Madras view and held :

"The imposition of sales tax on the supply of building materials used in the execution of building contracts was not ultra vires the Provincial Legislature. But the definition of "sale price" in Section 2(h) (ii) of the C. P. and Berar Sales Tax Act, 1947 and rule 4 of the C. P. and Berar Sales Tax Rules, 1947, were beyond the powers of the Legislature, inasmuch as they involved taxation on an artificial basis having no relevance to the price of the goods sold or supplied by a builder. The definitions of "contract", "dealer", "goods", "sale" and "turnover" in Section 2 of the C. P. and Berar Sales Tax Act, 1947, which not only bring within the taxing field a "sale" unmixed with any other transaction but also pick out a sale from the composite transaction of a building contract were not beyond the powers of the

## Provincial Legislature.

When entry No. 48 in List II of the Seventh Schedule of the Government of India Act, 1954-5 STC 216 : (AIR 1954 Mad 1130)

1935, was framed it conferred on the Provincial Legislature powers of the widest amplitude to tax the sale of goods in all its aspects and forms. The necessary condition for the impost, however, was that there should be a sale of goods. The selection of the taxable event and the severance of transactions of sale from other transactions in which they might be embedded was a necessary part of the power. If a building contract is not split up into its component parts, that is to say, material and labour, in legislative practice relating to the ordinary regulation of sale of goods there is no warrant for holding that it cannot be so split up even for purposes of taxation. Building materials are goods and there is payment for materials although it is not made separately but as part of a larger amount. The supply of goods is tantamount to the sale thereof". The Nagpur view was adopted in *Badrudin v. State of Vindhya Pradesh*<sup>2</sup> (C).

6. In *Mohamed Khasim v. State of Mysore*<sup>3</sup>, the Mysore High Court also dissented from the Madras view and held :

"The construction of a building or the repair of a car comes under the definition of works contract with taxable turnover under the Mysore Sales Tax Act. Although the material that is supplied for construction of a building merges in the immovable property, its value has to be apportioned for the purposes of taxation as contemplated in the Mysore Sales Tax Act. The contract to supply labour and work cannot however be taxed under the Act. The meaning of sale in the Sales Tax Act cannot be confined or limited to the meaning of that expression as understood in the Sale of Goods Act". (Head-note).

7. In *Jubilee Engineering Co. Ltd. v. Sales Tax Officer, Hyderabad City*<sup>4</sup>, the High Court of Hyderabad followed the Madras decision and held :

"The provisions of explanation (I) (i) to Section 2(m) of the Hyderabad General Sales Tax Act, 1950 and rule 5 (3) of the Rules made thereunder which authorize the levy of sales tax on the turnover of the materials used in a works contract have not been made in the proper exercise of legislative power conferred by entry 54 of List II of Schedule VII of the Constitution of India and are therefore ultra vires the Legislature. Where under a works contract a person undertakes to build a particular building or to make a particular thing, the materials involved in the building or making of the finished product, are not the subject matter of sale because there is no agreement to sell the materials nor is the price of the goods fixed nor is there a passing of the title in these goods as such, except as part of the building or the thing in which they are embedded. The building contractor in such a case cannot be said to have sold any goods or materials used in the building in order to bring them within the power of taxation conferred on a State by Entry 54 of List II of Schedule VII".

8. In all these cases the contention was that the relevant provisions of the Acts

<sup>2</sup> AIR 1956 Vin. Pra. 41

<sup>4</sup>1956-7 STC 423: (AIR 1956 Hyd 79)

<sup>36</sup> STC 211: (AIR 1956 Mys 41)

concerned were ultra vires of the powers of the Provincial or State Legislatures under either Entry 48 (Taxes On the sale of goods and on advertisements) of List II of the Seventh Schedule of the Government of India Act, 1935, or Entry 54 (Tax on the sale or purchase of goods other than newspapers) of List II of the Seventh Schedule of the Constitution of India. The Travencore-Cochin General Sales Tax Act, 1125, received the assent of His Highness the Rajpramukh on the 5th January 1950 and was published in the Government Gazette dated 17-1-1950. The Government of India Act, 1935, had no application to Travencore or Cochin and we entertain no doubt that the validity of a pre-Constitution enactment like the Travencore Cochin General Sales Tax Act, 1125, is not dependent on any of the entries in the Seventh Schedule to the Constitution.

9. Section 1 (3) of the Travencore-Cochin General Sales Tax Act, 1125, provides :

"It shall come into force on such date as the Government may, by notification in the Gazette, appoint".

It is true that the Act was brought into force only on the 30th May 1950 by virtue of a notification published after the Constitution came into force (Notification No. SR 1-353-A/49/R. D. dated 29-5-1950 and published in the Travencore-Cochin Government Gazette dated 30-5-1950), Article 372 of the Constitution provides for the continuance in force of all the existing laws and their adaptation. Article 372 (1) reads :

"Notwithstanding the repeal by this Constitution of the enactments referred to in Article 395 but subject to the other provisions of this Constitution, all the laws in force in the territory of India immediately before the commencement of this Constitution shall continue in force therein until altered or repealed or amended by a competent Legislature or other competent authority".

and the first of the four Explanations given in Article 372 defines the expression "law in force" as follows :

"The expression "law in force" in this article shall include a law passed or made by a Legislature or other competent authority in the territory of India before the commencement of this Constitution and not previously repealed, notwithstanding that it or parts of it may not be then in operation either at all or in particular areas".

10. The term "existing law" is defined in Article 366 (10) :

"existing law" means any law, Ordinance, order, bye-law, rule or regulation passed or made before the commencement of this Constitution by any Legislature, authority or person having power to make such a law, Ordinance, order bye-law, rule or regulation".

The difference in wording is not material and it can now be taken as settled that both the expressions cover the same ground. In *Edward Mil's Co. Ltd., Bewar v. State of Ajmer*<sup>5</sup> their

Lordships said :

"We do not think that there is any material difference between 'an existing law' and 'a law in force'".

11. The learned counsel for the petitioner emphasises the words "subject to the other provisions of this Constitution" in Article 372 and says that in view of those words we must still see whether the Travencore-Cochin General Sales Tax Act, 1125, is supported by Entry 54 of List II of the Seventh Schedule to the Constitution (Taxes on the sale or purchase of goods other than newspapers). The problem of the distribution of legislative powers between the centre and the constituent units is a matter of difficulty in every federation and what the Constitution of India has done is to give an almost exhaustive enumeration of all the topics of legislation (including taxation) and to arrange them in three separate Lists in the Seventh Schedule: the Union List (List I which enumerates 97 subjects which will come under the exclusive powers of the Union Parliament), the State List (List II which enumerates 65 subjects which will come within the exclusive competence of the State Legislature) and the Concurrent List (List III which enumerates 47 items in respect of which both the Union and State Legislatures will have concurrent powers of legislation, provision being made for a union law in the concurrent field overriding a State law in the event of a conflict between them). The partition of legislative power in this fashion, however, is for the purposes of legislation subsequent to the Constitution and it is impossible to accede to the contention that the validity of an Act passed by a competent Legislature prior to the Constitution has also to be tested in the light of the legislative distribution of powers effected by the Seventh Schedule.

12. In *Sagar Mal v. The State*<sup>6</sup>, Malik, C. J., dealt with a similar contention as follows :

"Article 246 of the Constitution distributes the legislative powers between the Parliament of the Union and the State Legislatures. It has nothing to do with laws already made and, if those laws are not contrary to any provisions of the Constitution, it cannot be said that those laws are not valid. The words 'subject to the other provisions of this Constitution,' in Article 372, do not mean that laws which had been passed by the Central Legislature before 26-1-1950, automatically cease to have effect because the subject has now been made a State subject".

In *Kanpur Oil Mills Harriesganj v. Judge (Appeals) Sales Tax, Kanpur Range, Kanpur*<sup>7</sup> Bhargava, J., said :

"Existing laws were continued in force by Article 372 of the Constitution but that Article, in continuing the existing laws, clearly provided that the existing laws were to continue in force 'subject to the other provision in the

<sup>5</sup> AIR 1955 SC 25

<sup>7</sup> AIR 1955 All 99

<sup>6</sup> AIR 1951 All 816

Constitution'. The effect of this provision in Article 372 is that, if any law happens to be contrary to any provision of the Constitution, to that extent that law would cease to continue in force. What this really means is that, if any existing law contains any provision which is in conflict with any provision in the Constitution, that provision of the

existing law would be void. Of course, it does not mean that a law, which was made by a competent legislature before the Constitution and which the legislature may not be competent to make after the Constitution, will also be void. All that is required is that the law should have been made by a competent legislature at the time when it was made and, after the passing of the Constitution, it should not be contrary to any provision of the Constitution and should not violate any fundamental right or other ban imposed by the Constitution against such a law".

13. Article 277 of the Constitution provides :

"Any taxes, duties, cesses or fees which immediately before the commencement of this Constitution, were being lawfully levied by the Government of any state or by any municipality or other local authority or body for the purposes of the State, municipality, district or other local area may, notwithstanding that those taxes, duties, cesses or fees are mentioned in the Union List, continue to be levied and to be applied to the same purposes until provision to the contrary is made by Parliament by law".

Sales tax in respect of works contracts was being levied immediately before the commencement of the Constitution under the provisions of the Cochin General Sales Tax Act, XV of 1121, in the Cochin area of the State and under the provisions of the Travencore General Sales Tax Act, 1124, in the Travencore area of the State. Those Acts were repealed only by Section 27 of the Travencore-Cochin General Sales Tax Act, 1125, when it came into force on 30-5-1950. It follows that in view of the specific provision of article 277 also it has to be held that such a tax can continue to be levied after the commencement of the Constitution irrespective of the partition of the legislative power effected by Article 246 and the entries in the three Lists of the Seventh Schedule.

14. In *Firm L. Hazari Mal Kuthiala v. Income-Tax Officer, Special Circle, Ambala Cantt*<sup>8</sup>, Bhandari, C. J., said that the three expressions, levy, assessment and collection occurring in Section 13 of the Finance Act, 1950, "are of the widest significance and embrace in their broad sweep all the proceedings which can possibly be imagined for raising money by the exercise of the power of taxation". According to him "assessment" is the official determination of liability of a person to pay a particular tax. 'Collection' is the power to gather in money for taxes, by enforced payment if necessary. The levy of taxes is generally a legislative function; assessment is a quasi-judicial function and collection an executive function."

15. Article 277 uses the word levy. In this case it is unnecessary to say whether the word levy in Article 277 is confined to the meaning given above as the Travencore-Cochin Government was "levying, assessing and collecting" sales tax in respect of

<sup>8</sup> AIR 1957 Pun 5

works contracts throughout the State and at the same rates immediately before the commencement of the Constitution.

16. *Maharaja Kishangarh Mills Ltd. v. Union of India*<sup>9</sup>, dealt with Article 277 of the Constitution as follows :

"Under this Article, all taxes, duties, cesses or fees, which were being lawfully levied by the Government of any State for purposes of the State were to continue to be levied and be applied to the same purposes notwithstanding that those taxes, duties, cesses or fees are mentioned in the union list, until provision to the contrary is made by Parliament or law. This Article obviously, therefore, modified the recommendation of the report that all federal sources of revenue with current outstanding will be taken over by the Union Government. It clearly allowed, till such time as the Union Parliament made provision to the contrary, the State to continue to levy duties which came within the Union List (like the cotton excise duties), and to use the income for its own purposes".

17. The second contention is that even if the Travencore-Cochin General Sales Tax Act, 1125, is not ultra vires of the Constitution, the legislative intent was only to tax the sale of goods strictly so called and that the intent is manifest from the preamble which says :

"Whereas it is expedient to provide for the levy of a general tax on the sale of goods in the State of Travencore-Cochin; it is hereby enacted as follows". That the legislative intent is not so restricted is clear from the definition of "goods" in Section 2 (e) of the Act:

" 'goods' means all kinds of movable property and includes all materials, commodities and articles including those to be used in the construction, fitting out, improvement or repair of immovable property; or in the fitting out, improvement or repair of movable property; and also includes all growing crops, grass and things attached to or forming part of the land which are agreed to be served before sale or under a contract of sale, but does not include actionable claims, stocks and shares securities" of "sale" in Section 2 (j) :

" 'Sale' with all its grammatical variations and cognate expressions means every transfer of the property in goods by one person to another in the course of trade or business for cash or for deferred payment or other valuable consideration and includes also a transfer of property in goods involved in the execution of a works contract, but does not include a mortgage, hypothecation, charge or pledge";

and of "turnover" in Section 2 (k):

" 'turnover' means the aggregate amount for which goods are either brought by or sold by a dealer, whether for cash or for deferred payment or other valuable consideration, provided that the proceeds of the sale by a person of agricultural or horticultural produce grown by himself or grown on any land in which he

<sup>9</sup> AIR 1953 Raj145

has an interest whether as owner, usufructuary mortgagee, tenant or otherwise, shall be excluded from his turnover :

Subject to such conditions and restrictions, if any, as may be prescribed in this behalf:-

(i) the amount for which goods are sold shall, in relation to a works contract, be deemed to be the amount payable to the dealer for carrying out such contract less such portion as may be prescribed of such amount, representing the usual proportion of the cost of labour to the cost of materials used in carrying out such contract.

18. The third and last argument advanced before us is based on that portion of the definition of the term "turnover" which says that :

"the amount for which goods are sold shall, in relation to a works contract be deemed to be the amount payable to the dealer for carrying out such contract less such portion as may be prescribed of such amount, representing the usual proportion of the cost of labor to the cost of materials used in carrying out such contract".

The contention is that there has been no valid prescription of the percentage of admissible deduction and that until such a prescription is made assessments are not possible.

19. The expression "prescribed" means prescribed by rules made under the Act (Section 2(b)). The only rule framed by the Government on the subject is Rule 4 (3) of the Travencore-Cochin General Sales Tax Rules, 1950, which provides that :

"the amount for which goods are sold by a dealer shall, in relation to a works contract, be deemed to be the amount payable to the dealer for carrying out such contract less a sum not exceeding such percentage of the amount payable as may be fixed by the Board of Revenue from time to time for different areas, representing the usual proportion in such areas of the cost of labour to the cost of materials used in carrying out such contract, subject to the following maximum percentages :-

Per cent.

- (a) in the case of an electrical contact 20
- (b) in the case of a structural contract 30
- (c) in the case of a sanitary contract 33 1/3
- (d) in the case of other contracts 30".

It is admitted that the Board of Revenue has not fixed any percentage and the argument is that in the absence of such a fixation the assessment should be considered as illegal. The petitioner has been allowed the maximum deduction of 30 per cent, and even if the Board of Revenue had fixed a maximum percentage for the works contracts involved in this case it could never have exceeded 30 per cent. We do not consider the non-fixation of maximum percentages by the Board of Revenue as permitted by rule 4 (3) as fatal to the assessment or as sufficient to compel an inference under article 226 of the Constitution.

20. A further contention of the learned counsel for the petitioner is that sub-rule (3) of Rule 4

should be considered as ultra vires of the Act. According to him the delegation of the duty to fix the actual percentages of admissible deduction to the Board of Revenue is not warranted by the Act and cannot be sustained. The Board of Revenue constituted by the Travencore-Cochin Board of Revenue Act, 1950, is not a body corporate like, for example, the Travencore and Cochin Devaswom Boards constituted under the Travencore-Cochin Hindu Religious Institutions Act, 1950, but only a part of the Government of the State. It may not be correct to say that the duty cast upon such a Board by the said sub-rule amounts to a delegation of the rule making power of the Government under Section 24 of the Travencore-Cochin General Sales Tax Act, 1125. It is however, unnecessary to consider this question as the petitioner has been allowed a deduction not on the basis of any percentage fixed by the Board of Revenue but at the maximum percentage fixed by the State itself.

21. In the light of what is stated above the petition has to be dismissed and is hereby dismissed, though in the circumstances of the case, without any order as to costs.  
Petition dismissed.