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IN THE HIGH COURT OF KARNATAKA AT BANGALORE

DATED THIS THE 30th DAY OF JUNE 2010

BEFORE

THE HON'BLE MR. JUSTICE ANAND BYRAREDDY

WRIT PETITION Nos. 29932-29933/2009 (T-KST)

C/W WRIT PETITION No. 394/2010

WRIT PETITION No. 452/2010

WRIT PETITION No. 37800/2009 AND

WRIT PETITION Nos. 37918-928/2009

WRIT PETITION No. 62/2008

WRIT PETITION No. 15683-694/2010

WRIT PETITION No. 15695-706/2010

WRIT PETITION No. 15707-718/2010

AND

WRIT PETITION No. 11676/2010

AND

WRIT PETITION No. 29046-048/2009

WP. No. 29932-33/2009 (T-KST)

BETWEEN:

1. M/s. Nagarjuna Construction
Company Limited,
No.301, Batavia Chambers,
No.8, Kumara Krupa Road,
Kumara Park East,
Bangalore-560 001
Represented by its
Senior Vice President.

3

Sri. C. Premachander Reddy,
S/o Sri. C. Varadha Reddy.
Aged about 48 years,
R/o No. 301, Batavia Chambers,
No.8, Kumarakrupa Road,
Kumarapark East,
Bangalore-560 001.

2. Sri. A.G.Ravi
S/o Sri. A.P. Gangadhariah
Aged about 40 years,
R/o No.301, Batavia Chambers,
No.8, Kumarakrupa Road,
Kumarapark East,
Bangalore-560 001.

..... PETITIONERS

(By Shri. M.R. Naik, Senior Advocate for Y.S. Krishnamurthy,
Advocate)

AND:

1. State of Karnataka
Represented by its
Principal Secretary
Department of Finance,
Vidhana Soudha,
Bangalore-560 001.
2. Joint Commissioner of
Commercial Taxes(Admn.)
VAT Division I, 7th Floor,
VTK Building, Gandhi Nagar,
Bangalore-560 009.

3. The Deputy Commissioner of
Commercial Taxes(Audit)-13,
VAT Division I, 7th Floor,
VTK Building,
Gandhinagar,
Bangalore-560 009.

... RESPONDENTS

(By Shri K.M. Shivayogiswamy, High Court Government
Pleader)

These Writ Petitions is filed under Articles 226 and 227 of the Constitution of India, praying to declare the provisions of Section 4C that authorizes levy of Tax on works contract under item 23 of the schedule VI, as illegal, void and unenforceable in so far as petitioners are concerned and etc.,

WP 394/2010

BETWEEN:

1. M/s. Jampana Constructions
Private Limited,
Registered Office: No. 389/1,
I Floor, Judges Colony,
R.T. Nagar,
Bangalore-560 032.
Represented by its Director
Sri. J. Venugopal Krishnam Raju,
S/o Sri. J Sathyanarayana Raju,
Aged about 41 years,
R/o No. 1390, 8th Cross,
10th Main, Judicial Layout,
G.K.V.K. Post,
Bangalore-560 065.

2. Sri. J. Srinivasa Raju
S/o Sri. J Satyhanarayan Raju,
Aged about 42 years,
R/o No. 981/D, 14th Main,
Judicial Layout,
G.K.V.K. Post,
Bangalore-560 065.

.... PETITIONERS

(By Shri. M.R. Naik, Senior Advocate for Y.S. Krishna Murthy,
Advocate)

AND:

1. State of Karnataka
Represented by its
Principal Secretary,
Department of Finance,
Vidhana Soudha,
Bangalore-560 001.
2. The Commissioner of
Commercial Taxes,
VTK Building,
Gandhinagar,
Bangalore-560 009.
3. The Assistant Commissioner of
Commercial Taxes
(Audit)-52, DVO-5,
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government
Pleader)

This Writ Petition is filed under Articles 226 and 227 of the Constitution of India, praying to call for records from the respondents and declare the provisions of Section 4C that authorizes levy of Tax on works contract under item 23 to the schedule VI as illegal, void and unenforceable and etc.,

WP 452/2010

BETWEEN:

1. M/s. Shri. Aruna Constructions
Private Limited
No. 323, Sri. Ranga Nilaya,
II Floor, I Cross, III Main,
R.T. Nagar,
Bangalore-560 032.
Represented by its Director,
Sri. J. Rama Raju,
S/o J.Sathyanarayana Raju
Aged about 48 years,
R/o No. 981/D, 14th Main,
Judicial Layout,
G.K.V.K. Post,
Bangalore-560 065.
2. Sri. J. Ram Babu
S/o J. Arjun Raju
Aged about 38 years,
R/o No. 1174, 10th 'B' Cross,
Near New Town Public School,
Yelahanka New Town,
Bangalore-560 064.

... PETITIONERS

(By Shri. M.R Naik, Senior Advocate for Y.S. Krishnamurthy,
Advocate)

AND:

1. State of Karnataka
Represented by its
Principal Secretary
Department of Finance,
Vidhana Soudha,
Bangalore-560 001.
2. The Assistant Commissioner of
Commercial Taxes (Audit)-21,
DVO-II, Jeevan Sampige,
2nd Floor, LIC Building,
Near Sampige Theatre,
Malleswaram,
Bangalore-560 003.
3. The Deputy Commissioner of
Commercial Taxes,
(Audit)-13, VAT Division I,
7th Floor, VTK Building,
Gandhinagar,
Bangalore-560 009.
4. The Commissioner of
Commercial Taxes,
Karnataka State
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government
Pleader)

This Writ Petition is filed under Articles 226 and 227 of the Constitution of India, praying to call for the records from the respondents and declare the provisions of Section 4C that authorizes levy of tax on works contract item 23 to the schedule VI, as illegal, void and unenforceable so far as to the petitioners concerned and etc.,

WP 37800/2009 and WP 37918-928/2009

BETWEEN:

M/s. Mfar Constructions Private Limited
No.8 & 8A, AVS Compound,
80 Feet Road, Koramangala,
Bangalore-560 034.

Represented by its
Chief Executive Officer,
Sri. B.K. Dhar,
S/o Sri. J.L Dhar,
Aged about 57 years.

... PETITIONER

(By Shri.G.Sarangan, Senior Advocate for K.S. Ramabadran,
Advocate)

AND:

1. The Commercial Tax officer,
Audit-22, DVO-2, II Floor,
LIC Building, Sampige Road,
Malleshwaram,
Bangalore-560 003.
2. The State of Karnataka
Represented by the

Principal Secretary to
Government,
Finance Department,
Vidhana Soudha,
Bangalore-560 001.

... RESPONDENTS

(By Shri. K.M. Shivayogiwamy, High Court Government Pleader)

These Writ Petitions is filed under Articles 226 and 227 of the Constitution of India, praying to quash the re-assessment order and demand notice dated 19.11.2009, vide Annexure-D, passed by the respondent no.1, for the period 2006-07 levying Tax at 12.5% on the value of Iron & Steel used in the execution of Civil Works as without Jurisdiction and etc.,

WP 62/2008

BETWEEN:

M/s UE Development India Private Limited
60, Wellington Road,
Richmond Town,
Bangalore-560 025.

(By Mr. Yam Keong Chee, 46 years) ... PETITIONER

(By Shri G.Sarangan, Senior Advocate for Shri T.N. Keshavamurthy)

AND:

1. Commercial Tax Officer (Intelligence)-XV,
South Zone, VTK II, 6th Floor,
80 Feet Road,

Viveknagar Post,
Koramangala,
Bangalore-560 047.

2. State of Karnataka
Represented by the
Principal Secretary to
Government,
Finance Department,
Vidhana Soudha,
Bangalore-560 001.

... RESPONDENTS

(By Shri K.M. Shivayogiswamy, High Court Government Pleader
for respondent no. 1 and 2)

This Writ Petition is filed under Articles 226 and 227 of the
Constitution of India, praying to quash the re-assessment order
dated 10.12.2007 vide Annexure-A levying tax at 12.5% on the
value of steel used in the execution of civil works as without
jurisdiction and etc.,

WP 15683-94/2010

BETWEEN:

M/s. Senthuran Construction Company
No.606, 3rd Floor, 80 Feet Road,
6th Block, Koramangala,
Bangalore-560 095,
Represented by its
Proprietor Mr. J. Chandrashekar.

... PETITIONER

(By Shri. Ajit Kumar L. Raheja, Advocate)

AND:

1. The Commissioner of Commercial Taxes,
Vanijya Therige Karyalaya
I Main Road,
Gandhinagar,
Bangalore-560 009.
2. The Deputy Commissioner of
Commercial Taxes,
(Audit-41), DVO-4,
Vanijaya Therige Karyalaya,
Koramangala,
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government Pleader
for respondents)

These Writ Petitions is filed under Articles 226 and 227 of
the Constitution of India, praying to quash the impugned circular
dated 07.12.2009 issued by the respondent no.1, vide Annexure-A
and etc.,

WP 15695-706/2010

BETWEEN:

M/s. Senthuran Construction Company
No. 606, 3rd Floor, 80 Feet Road,
6th Block, Koramangala,
Bangalore-560 095,
Represented by its

Proprietor

Mr. J. Chandreshekar.

... PETITIONER

(By Shri. Ajit Kumar L Raheja, Advocate)

AND:

1. The Commissioner of Commercial Taxes,
Vanijya Therige Karyalaya,
I Main Road, Gandhinagar,
Bangalore-560 009.

2. The Deputy Commissioner of
Commercial Taxes
(Audit-41) DVO-4,
Vanijya Therige Karyalaya,
Koramangala,
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government Pleader
for respondents)

These Writ Petitions is filed under Articles 226 and 227 of
the Constitution of India, praying to quash the impugned circular
dated 07.12.2009 issued by the respondent no.1 vide Annexure-A
and etc.,

WP 15707-718/2010

BETWEEN:

M/s. Senthuran Construction Company
No. 606, 3rd Floor, 80 Feet Road,

6th Block, Koramangala,
Bangalore-560 095,
Represented by its Proprietor,
Mr. J. Chandrashekar.

... PETITIONER

(By Shri. Ajit Kumar L Raheja, Advocate)

AND:

1. The Commissioner of Commercial Taxes
Vanijya Therige Karyalaya,
I Main Road, Gandhinagar,
Bangalore-560 009.

2. The Deputy Commissioner of
Commercial Taxes
(Audit-41) DVO-4,
Vanijya Therige Karyalaya,
Koramangala,
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government Pleader
for respondent)

These Writ Petitions is filed under Articles 226 and 227 of
the Constitution of India, praying to quash the impugned circular
dated 07.12.2009 issued by the respondent no.1 vide Annexure-A
and etc.,

WP 11676 OF 2010

BETWEEN:

1. M/s. JMC Projects (India) Limited
A-104, Shapath-4,
Opposite to Karnavati club,
SG Road,
Ahmedabad-380 051.
And with its local office at
Gold Towers, No. 50, 2nd Floor,
Residency Road,
Bangalore-560 025.
Represented by its
Authorized Signatory/
Assistant Vice President (Finance).
Sri. Chinnubai Parikh,
Aged about 53 years,
R/o Ahmedabad.
2. Sri. Nithin C Parikh
S/o Chinnubai Parikh
Aged about 53 years,
R/o Ahmedabad.

... PETITIONERS

(By Shri. M.R. Naik, Senior Advocate)

AND:

1. State of Karnataka
Represented by its
Principal Secretary,
Department of Finance,

Vidhana Soudha,
Bangalore-560 001.

2. Commercial Tax Officer
(ENF)-10, South Zone,
Bangalore.
3. Additional Commercial of
Commercial Taxes (Enforcement)
South Zone,
VTK-2, 80 Feet Road,
Koramangala,
Bangalore-560 047.
4. Commissioner of Commercial Taxes,
Karnataka State,
Bangalore.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government
Pleader)

This Writ Petition is filed under Articles 226 and 227 of the
Constitution of India, praying to call for records from the
respondents and etc.,

WP 29046-48 OF 2009

BETWEEN:

M/s. G.R. Engineering Private Limited
M.R.P.L. Premises, Katipalla,
Mangalore-575 030.

(By S.G.Shinde,
aged 57 years,
Deputy General Manager
Project Accounts).

... PETITIONER

(By Shri G.Sarangan, Senior Advocate for
Shri. T.N. Keshavamurthy, Advocate)

AND:

1. The Commercial Tax Officer
(Enforcement-II),
Maidan Road,
Mangalore-575 001.
2. The Commissioner of Commercial Taxes,
Gandhinagar,
Bangalore-560 009.
3. The State of Karnataka
Represented by its
Principal Secretary to
Government,
Finance Department,
Vidhana Soudha,
Bangalore-560 001.

... RESPONDENTS

(By Shri. K.M. Shivayogiswamy, High Court Government
Pleader)

These Writ Petitions is filed under Articles 226 and 227 of
the Constitution of India, praying to quash a writ of certiorari or
directions in the nature of writ of certiorari and to read down

explanation to rule 3(1) of the Karnataka Value Added Tax Rules 2005, as opposed to the provisions of Section 4(1) (c) of the Karnataka Value Added Tax Act 2003 & Article 366 (29A)(b) of the Constitution of India in so far as petitioner conserved and etc.,

These petitions having been heard and reserved on 11.06.2010, 14.06.2010 and 23.06.2010, respectively, and coming on for Pronouncement of Orders this day, the Court delivered the following:-

ORDER

These petitions are heard and disposed of together having regard to the fact that the issues involved are identical.

2. The petitioners seek to challenge the constitutional validity of Section 4(1)(c) and Schedule VI, Item 23 of the Karnataka Value Added Tax Act, 2003 (hereinafter referred to as the 'KVAT Act', for brevity) and the Explanation appended to Rule 3(1) of the Karnataka Value Added Tax Rules, 2005 (hereinafter referred to as 'the KVAT Rules' for brevity) .

3. The petitioners are engaged in undertaking turnkey projects and other works contracts for third-parties. The

3

petitioners are assessed to tax under the Act, more particularly under Section 39(1) of the Act. The orders of assessments made in respect of each of the petitioners were sought to be revised on the ground that the turnover offered for tax at a rate of 4% on turnover of iron and steel, involved in the execution of works contracts, was not permissible for the reason that the 'works contract of civil works' is a distinct Entry in the VI Schedule and therefore, tax is attracted on the said turnover at the rate of 12.5% as provided therein.

It is pointed out that prior to 1.4.2006, there was no separate provision under which tax could be levied on works contracts. There was however, a levy of tax on transfer of property involved in the execution of works contracts under Section 3 of the KVAT Act in accordance with Schedule III. It is only from 1.4.2006, that the Legislature has introduced the impugned provisions enabling the revenue to levy tax on works contracts.

4. Heard Shri G.Sarangan, Senior Advocate, Shri Madhusudhan R. Naik, Senior Advocate, appearing for the counsel for petitioners, and Shri Ajit Kumar Raheja.

5. It is contended that the power of the States to levy value added tax on sales and purchases of goods is to be found only under Entry-54 of List-II under Schedule VII to the Constitution of India.

In the case of *State Of Madras v. Gannon Dunkerley and Company*, 9 STC 353, the Supreme Court of India held that a building contract which is entire and indivisible did not involve any sale of goods and therefore it was not within the competence of the legislature to impose a tax on the supply of materials used in such a contract treating it as a sale. It was observed by the Supreme Court as follows:

“Another difficulty in the way of accepting the contention of the appellant as to splitting up a building contract is that 'property in materials used

therein ' does not pass to the other party to the contract as movable property. It would so pass, if that were an agreement between the parties. But if there was no such agreement and the contract was only to construct a building, then the materials used therein would become the property of the other party to the contract only on the theory of accretion''.

By virtue of the above decision, no sales tax could be levied on the amount received under a works contract even though the contractor had supplied goods for construction of buildings.

It was in the wake of the above judgement that Clause 29A was introduced into Article 366 of the Constitution of India by the 46th Amendment, 1982. Clause 29A is extracted hereunder for a ready reference:

“(29A) “tax on the sale or purchase of goods includes,

(a) A tax on the transfer, otherwise than in pursuance of a contract, of property in any other goods for cash, deferred payment or other valuable consideration ;

- (b) A tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;
- (c) A tax on the delivery of goods on hire-purchase or any system of payment by instalments;
- (d) A tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration.
- (e) A tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration.
- (f) A tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration;

And such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made;”.

It is as a consequence of the above amendment that tax on sale or purchase of goods, took within its ambit a tax on works contracts. The constitutional validity of the 46th Amendment of the Constitution, whereby Clause 29A was inserted in Article 366, was challenged in the case of *Builders Association of India versus Union of India* 73 STC 370, wherein it was held by the Supreme Court that the object of a new definition of the word 'sale' is to enlarge the scope of 'tax on sale or purchase of goods ' wherever it occurs in the Constitution so that it may include within its scope the transfer, delivery or supply of goods that may take place under any of the transactions referred to in sub-clauses (a) to (f) of Clause 29A. So construed, the expression ' tax on the sale or purchase of goods ' In Entry-54 of the State List, therefore, includes a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract also. It was held that the power of the State to levy tax on the transfer of property in goods involved in the execution of

works contract is subject to restrictions and conditions in Article 286 of the Constitution.

The law laid down in the above decision was reiterated by the Supreme Court in *Gannon Dunkerley and company vs. State of Rajasthan 88 STC 204*, wherein, *inter alia*, it was held that the legislative power of the State Legislatures under Entry-54 of the State List is subject to two limitations, one flowing from the entry itself, which makes the said power subject to the provisions of Entry 92 A of List I, and the other flowing from the prohibition contained in Article 286. The provisions of Section 3, 4, 5 and Section 14 and 15 of the Central Sales Tax Act, 1956, (hereinafter referred to as 'the CST Act' for brevity) are applicable to a transfer of property in goods involved in the execution of a works contract covered by Article 366(29A)(b).

The tax on transfer of property in goods (whether as goods or in some other form) involved in the execution of a works

contract falling within the ambit of Article 366 (29A)(b) is leviable on the goods involved in the execution of a works contract and ' the value of the goods ' which are involved in the execution of works contract would constitute the measure for imposition of the tax.

In order to determine the value of the goods which are involved in the execution of a works contract for the purpose of levying the tax referred to in Article 366(29A)(b), it is permissible to take the value of the works contract as the basis and the value of the goods involved in the execution of the works contract can be arrived at, by deducting expenses incurred by the contractor for providing labour and other services from the value of the works contract. While fixing the rate of tax, it is permissible to fix a uniform rate of tax, for the various goods involved in the execution of a works contract, while rate may be different from the rate of tax fixed in respect of sales or purchase of those goods as a separate article.

This position in law was reiterated in *Builders Association of India versus State of Karnataka* 88 STC 248.

From a reading of the provisions of the KVAT Act, it is clear that Section 3 is the main 'charging section' which contemplates the levy of tax only on 'sale' of goods. The rate of tax on every such sale in respect of such goods is prescribed under Section 4 of the KVAT Act. It is contended that unlike under the Karnataka Sales Tax Act, 1957 (hereinafter referred to as 'the KST Act' for brevity), there is no '*non-obstante*' clause which overrides the main charging Section and therefore, the provisions of the present Act will have to be strictly construed.

Prior to 1.4.2006, there was no separate provision under which tax on works contracts was levied. The levy of tax, on transfer of property, involved in the execution of works contracts, was being levied under Section 3, read with the III Schedule to the KVAT Act. It is only with effect from 1.4.2006, the State

3 ^{Legislature} ~~Government~~ has introduced the new provisions by inserting ^{Clause} (C) to Section 4⁽¹⁾ of the KVAT Act, thereby seeking to levy taxes on ³ works contract while specifying the rate of tax under the Sixth Schedule. It is hence contended that in the absence of a charging section to levy tax for a class of dealers the purpose of the Sixth Schedule under the Act remains non-functional; in that, the class of dealers like the petitioners cannot be singled out to impose the levy.

It is next contended that Article 286(3)(a) of the Constitution of India authorises Parliament to declare some goods as being of special importance and to impose restrictions and conditions in regard to the power of the states to levy a tax on such goods and the rates thereof. Section 2(c) of the CST Act, defines 'declared goods' as those declared under Section 14 of the said Act, as 'goods of special importance' in inter-state trade or commerce. Section 14 of the said Act enumerates such goods. Iron and steel are listed therein as goods of special importance and are

hence declared goods. The parliament can therefore restrict the powers of the State government to tax such goods. Section 15 expressly provides for the restriction on the power of the States to tax such goods.

In the light of the above provisions, the Karnataka Value Added Tax Act, 2003, has specified declared goods at Serial No. 30 of the Third Schedule as follows :

' Declared goods as specified in Section 14 of the Central Sales Tax Act, 1956 (Central Act 74 of 1956) '

And as provided under Section 4(1)(a)(ii) of the KVAT Act, the goods listed in the Third Schedule are taxable at the rate of 4%. It is therefore clear that the restriction imposed by the Parliament under Article 286(3) is applicable to the whole definition of 'sale' defined under Article 366(29A) of the Constitution, which includes works contracts also.

It is seen that the State can levy tax "on the sale or purchase of goods" by virtue of the power vested in Article 246 Entry-54 of List-II. The expression "tax on the sale or purchase of goods" has been defined to include the term "works contracts". While simultaneously the Constitution imposes a restriction in respect of the system of levy, rates and other incidence of tax on the sale or purchase of goods.

It is contended that there is a special significance attached to the expressions "includes" and "deemed to be a sale" as employed under the provisions of the Constitution. The Supreme Court in *State of Madras vs. Gannon Dunkerley and Company (Madras) Limited*, (1958)9 STC 353, which has been followed in several subsequent judgments, has expounded on the natural import of the definition of the expression "tax on the sale or purchase of goods" as not to be construed in its popular sense, but in its legal sense. The expression 'includes' as employed in Clause 29A of Article 366 assumes importance, since it is directed

not only in respect of such things as signified according to their natural import, but includes such transfer as shall be deemed to be a sale of goods, under a legal fiction.

Section 2(15) of the KVAT Act and Section 2(1)(m) of the KST Act, define goods as meaning all kinds of moveable property other than, newspaper, actionable claims, stocks and shares and securities, but including goods, (as goods or in some other form) involved in the execution of a works contract. This would lead to a position that change of form of the goods from the form, at the stage of purchase by a contractor into some other form, at the stage of transfer to the contractee, cannot be treated as being a different one from the original one for the purpose of levy of tax in respect of a deemed sale of goods involved in the execution of a works contract. In other words, steel for instance, which is used in the execution of works contract for purposes of construction results in the same being incorporated into immov³able property, in respect of which the State cannot assume power to levy tax in respect of such immov³able property. The interpretation of the

expression as "goods or in some other form" would have to be understood *ejusdem generis*. Hence, steel which are goods used for construction of immoveable property, do not any longer answer to the definition of goods. And it is only goods on which tax can be levied under the Sales tax legislation. But tax would be leviable on the transfer of the property in steel because of the legal fiction created by the expression "deemed to be a sale of those goods". Similarly, brick, cement, and sand may change form to mortar mixture used for laying the bricks. Still it is not the mortar mixture, or the wall that is built, which is taxable, but it is the sale of cement, sand and the bricks, respectively, that are taxable. It is thus submitted that in the execution of works contract by the petitioners, the form of steel has not been changed into any different form, but has been incorporated in the same form. Therefore, the restriction imposed by the Government under Article 286(3) of the Constitution is required to be applied for levying tax on works contracts. The restriction imposed is applicable to the whole definition of "sale" as defined under

Article 366(29A) of the Constitution which would include works contracts also. It is hence emphasized that having regard to the scheme under the erstwhile Karnataka Sales Tax Act, the levy of tax based on the contents of the Schedule under the present Act is not acceptable in law. The levy of any higher rate of tax on the turnover of iron and steel would run counter to Section 7 of the KVAT Act which specifically provides as follows :-

“7(1) Notwithstanding anything contained in the Sale of Goods Act, 1930 (Central Act 3 of 1930), for the purpose of this Act, and subject to sub-section (2), the sale of goods shall be deemed to have taken place at the time of transfer of title or possession or incorporation of the goods in the course of execution of any works contract whether or not there is receipt of payment”

From a reading of the above, it is clear that the sale of goods shall be deemed to have taken place at the time of transfer of title, or possession or incorporation of the goods in the course of execution of any works contract. In other words, the sale

occurs at the time of incorporation of the goods in the course of execution of the work. It is hence contended that steel materially acquires the characteristics of construction work such as footings, slabs, beams etc., only when they are made part and parcel of the immovable property namely, the building, and when once they become immovable property, they cease to be goods. The question of a deemed sale of the said goods or otherwise would not arise. Steel is used in such construction in the same form and is not converted into any other form whereby it loses its characteristic of being steel.

It is thus contended that the respondents seeking to take a view that the petitioner's turn over assessed to tax was erroneous and that the turnover offered for tax at the rate of 4% on the turnover of steel involved in the execution of works contract is not permissible for the reason that the Entry under the Schedule namely, works contract of civil works finds a separate and distinct Entry at Serial No.23 under the head "all other works contracts not specified in any of the categories specified under the VI

Schedule” and therefore, attracts tax on the said turnover at the rate of 12.5%, has proceeded to issue proposition notices and has sought to revise assessments. Though several assessments have been made for different periods in the past and taxes have been paid on the basis that such turnover is taxed at 4%, the authorities seek to revise the assessments while seeking to read out of context - a decision of a Division Bench of this court in a Sales Tax Revision Petition in *Larsen and Toubro Limited vs. State of Karnataka*, (2006)61KLJ 452 which was a decision which proceeded to decline to interfere in the impugned order on the footing that the findings of the Tribunal being findings of fact and not involving any question of law and the respondents seeking to draw sustenance from the said decision seem to ignore given the provisions of Section 4 of the present Act, which plainly does not apply in respect of declared goods, to which Sections 14 and 15 of the Central Sales Tax Act, 1956 would apply. A large number of authorities are relied upon in support of the contentions.

6. The learned Government Advocate on the other hand seeks to sustain the action of the respondents. It is contended that the subject matter is squarely covered by a decision of this court in *B.V.Subba Reddy vs. Deputy Commissioner of Commercial Taxes*, [2008]11 VST 715 and further that the decision in *URC Construction Limited vs. Deputy Commissioner of Commercial Taxes*, [2008] 11 VST 896, was not applicable, since this court in *URC Construction Limited*, has sought to distinguish the decision in *B.V.Subba Reddy*, supra, and has observed that the assessing authority had accepted that the steel had been used in the construction of the building without being converted into any other form. Because of this factual finding by the assessing authority, this court had held that it was a case where the goods were taxable at 4% as being declared goods and therefore, did not lay down the law as sought to be contended by the petitioners and that even if iron and steel are sold in some other form, when they are incorporated in the works contracts, that the tax could not be levied in terms of the VI Schedule. It is thus contended that

whether there was a transfer of declared goods as declared goods in the execution of a works contract would depend on the facts of each case to be determined by the assessing authority.

In the instant cases, the assessing authority having held that the steel used in the execution of the works contract has not been transferred in the form of declared goods, but has changed its form when it is transferred and therefore, are not any longer declared goods are findings of fact. Hence, there is no error in the reasoning adopted by the assessing officer. It is contended that the same is not violative of the settled legal position as laid down by the Supreme Court in several cases that are cited at the bar.

It is contended that Section 3 of the KVAT Act provides for levy of tax on the sale of goods in question of different commodities. The language of Entry-54 of the Constitution of India having been incorporated – the ‘tax on sale or purchase of goods’ is to provide the State legislature the competence to levy

tax, whenever there is a purchase or sale. In view of the legal fiction created consequent to the amendment to Article 366 of the Constitution, a sale would include the transfer of property in goods –whether in the same form or in some other form, involved in the execution of works contract. Consequently, it is contended, there is a charge on the sale of goods under Section 3 of the KVAT Act and the rate has been fixed under Section 4 (1)(c) of the KVAT Act read with the VI Schedule. It is contended that the tax is not levied on a class of dealers but on the sale of goods. A comparison with the scheme of the KST Act is wholly unwarranted in contending that the levy is on a class of dealers.

Reliance is placed on the decision of *Gannon Dunkerly & Company*, 88 STC 204, to contend that the legislature has the power to prescribe a uniform rate of tax for each category of works contract, hence the rate of tax leviable even on the incorporation of iron and steel in the works contract @12.5 % was justifiable.

Reliance is placed on decisions of this court in *Larsen & Toubro v. State of Karnataka*, 2006(61) Kar.L.J 452, and *State of Karnataka v. Anantha Engineering Works*, STRP 30 of 2006 dated 26.10.2006 which have been rendered following the judgement in *B.V. Subba Reddy's* case supra .

It is thus sought to be contended that having regard to the consistent view taken by this court – iron and steel or any goods if involved in the execution of works contract of civil works, the said goods would be liable to tax under Serial no.23 of the VI Schedule to the Act @ 12.5 % only .

It is further contended that the petitioners are provided with effective and alternative remedy under the KVAT Act and therefore, the petitions would have to be dismissed on that ground alone.

7. By way of reply, it is contended that the assertion that the steel used in the execution of works contracts has been

transferred after converting the same into some other form is an incorrect statement. There is no such finding by the assessing authority in the present cases. In the light of which, the contention that the petitioners are not entitled to place reliance on the decision of this court in *URC Construction*, supra is erroneous.

8. The petitioner in WP 29046-48/2009 has also raised an additional ground, in that, it is stated that the petitioner who was engaged in the execution of a contract for the supply and installation and commissioning of manufactured "bullet tanks" which are later on installed at the site of the contracting party, had used mild steel plates and sheets as raw materials in the manufacture of the said products. This raw material was sought to be brought to tax @ 12.5% on the amounts declared by the petitioner towards the value of the same. Apart from this, certain mobilization advances received under the terms of the contract – towards preliminary work and procurement of the material was sought to be brought to tax @12.5 % apart from penalty, on the

footing that there was an understatement of the tax liability. It is contended that during the relevant period, when the petitioners received the advances, the only activity carried out was the purchase of the raw material aforesaid and preparation of sections of the plates and sheets at the site. The rate of tax on the raw material, which are declared goods, being 4% and the same having been paid – and even though the raw material was not incorporated in the works contract and no transfer of the property had taken place - the advances were apparently being treated as the consideration received for the transfer of property in the said raw material, to levy tax and penalty as aforesaid.

The petitioners submit that levy of tax @ 12.5% on the amounts representing advances received towards preliminary work involved in the execution of works contract is illegal and opposed to the provisions of charging Section 4(1)(c) of the KVAT Act that provides for levy of tax only on the amounts representing transfer of property in goods involved in the

execution of works contract. Further, the levy of tax on the value of declared goods i.e., M.S. Sections prepared at the work site @ 12.5% as against 4% declared in the returns filed in Form VAT 100 is clearly opposed to the provisions of Article 286(3)(a) of the Constitution of India read with the provisions of Section 4(1)(c) of the KVAT Act as well as Sections 14 and 15 of the CST Act, 1956 governing the levy of tax on 'declared goods' and therefore the levy is without jurisdiction. The petitioners further submit that the levy is unconstitutional as being totally opposed to the binding decisions of the Apex Court in the case of *Gannon Dunkerley and Company vs. State of Rajasthan*, 88 STC 204 and *Builders Association of India vs. Union of India*, (73 STC 370 at 394 SC) wherein it has been held that the restrictions and conditions contained in Section 15 of the Central Sales Tax Act, 1956 on the power of the States to levy tax on the sale of declared goods apply equally and fully to transfer of property in goods involved in the execution of works contracts, even as they apply to ordinary sales, and therefore, if there is a transfer of property in

declared goods, for example steel products, in the process of execution of works contract, the State can levy tax only at 4% and only at one stage. The petitioner further submits that the levy of penalty under Section 72(2) of the KVAT Act on the footing that the petitioner 'under-stated the tax liability' in the returns filed by more than 5% and also the levy of interest under Section 36(3) of the KVAT Act is also illegal and unconstitutional being highly arbitrary and confiscatory in nature.

9. In the light of the above rival contentions, the points that arise for consideration are :

a) Whether the State Government has the competence to levy tax on the transfer of property in goods, involved in the execution of works contract, (when the goods in question are 'declared goods' for the purposes of the Central Sales Tax Act, 1956)at more than one stage ?

b) Whether the Explanation to Rule 3(1) of the KVAT Rules – which provides that any advances paid to a contractor as

part of the consideration for goods involved in the execution of the works contract could be included in the total turnover in the month in which the execution of the works commences – even before the goods are incorporated in the works?

In answering the above questions, the settled position of law insofar as the interpretation of the scope of Article 366(29A) of the Constitution of India and its impact on the provisions of the CST Act, as laid down by the apex court in the cases of *Builders Association of India v. Union of India*, 73 STC 370 and *Gannon Dunkerley vs. State of Rajasthan*, 88 STC 204, is to be kept in view. In the latter decision, it has been laid down thus :

“ While enacting a law imposing a tax on sale or purchase of goods under Entry-54 of the State List, read with sub-clause (b) of Clause (29A) of Article 366 of the Constitution of India, it is not permissible for the State Legislature to make a law imposing tax on such a deemed sale which constitutes a sale in the course of inter-state trade or commerce under Section 3 of the Central Sales Tax Act or sale in the course of import

or export under Section 5 of the Central Sales Tax Act. So also it is not possible for the State Legislature to impose a tax on goods declared to be of special importance in inter-state trade or commerce under Section 14 of the Central Sales Tax Act except in accordance with the restrictions and conditions contained in Section 15 of the Central Sales Tax Act.” (emphasis supplied)

Thus, the levy of tax by the State Government in respect of declared goods, is subject to the conditions and restrictions contained in Section 15 of the CST Act. The first condition is that the tax payable under the local sales tax law in respect of any sale or purchase of declared goods inside the State shall not exceed 4% of the sale or purchase price and such tax shall not be levied at more than one stage. The apex Court has laid down in *Builders Association's* case supra, thus :

“ The restrictions and conditions contained in Section 15 of the Central Sales Tax Act, 1956 on the power of the States to levy tax on the sale of declared goods apply equally and fully to transfer of property in goods under works contracts, even as they apply to

ordinary sales. Therefore if there is a transfer of property in declared goods –for example steel products- in the process of execution of works contract , the State can levy tax only at 4 percent and only at one stage”(emphasis supplied).

As can be seen, Section 4 of the Karnataka Value Added Tax, 2003 is the charging Section and it provides as follows :

“4. Liability to tax and rates thereof

- (1) Every dealer who is or is required to be registered as specified in Sections 22 and 24, shall be liable to pay tax, on his taxable turnover,
 - (a) in respect of goods mentioned in –
 - (i) Second Schedule, at the rate of one *per cent*,
 - (ii) Third Schedule, at the rate of four *per cent*, and
 - (iii) Fourth Schedule, at the rate of twenty *per cent*.
 - (b) in respect of other goods, at the rate of [twelve and one half] *per cent*
 - (c) **in respect of transfer of property in goods (whether as goods or in some other form) involved in the execution of works contract specified in column (2) of the Sixth Schedule, subject to Sections 14 and 15 of the Central Sales Tax Act, 1956 (Central Act 74 of 1956), at**

the rates specified in the corresponding entries in column (3) of the said Schedule.”

An analysis of the Section more particularly, Clause(c) would indicate that a dealer registered under the Act shall be liable to tax and that such tax is leviable on the taxable turnover relating to transfer of property in goods, whether as goods or in some other form, involved in the execution of works contracts that are specified in the Sixth Schedule to the Act and at the rates specified therein. The levy is subject to the provisions of Section 14 and 15 of the CST Act relating to declared goods.

Though tax at 12.5% is applicable under Serial no.23 of the Sixth Schedule to the Act in respect of composite works contracts involving transfer of property in goods, an exception is provided in Section 4 (1)(c) of the KVAT Act itself, that in respect of declared goods involved in the execution of works contracts, the rate of tax shall be as provided in Section 14 of CST Act @ 4%. This is so because the provisions of Section 4(1)(c) is necessarily to be read with the Sixth Schedule to the Act and the entries in

that Schedule are subject to the provisions of Section 14 and 15 of the CST Act. Thus, as regards iron and steel products, used in the execution of works contracts, the levy of tax shall be at 4% only on the value thereof.

It is also to be seen that Section 7 of the KVAT Act reads as follows :

“7. Time of sale of goods

- (1) Notwithstanding anything contained in the Sale of Goods Act, 1930 (Central Act 3 of 1930), for the purpose of this Act, and subject to sub-section (2), the sale of goods shall be deemed to have taken place at the time of transfer of title or possession or incorporation of the goods in the course of execution of any works contract whether or not there is receipt of payment:

Provided that where a dealer issues a tax invoice in respect of such sale within fourteen days from the date of the sale, the sale shall be deemed to have taken place at the time the invoice is issued.

- (2) Where, before the time applicable in sub-section(1), the dealer, selling the goods issues a tax invoice in

respect of such sale or receives payment in respect of such sale, the sale shall, to the extent that temporary injunction is covered by the invoice or payment, be deemed to have taken at the time the invoice is issued or the payment is received.

- (3) The Commissioner may on an application of any dealer exempt such dealer subject to such conditions as he may specify, from the time specified in subsection (1).”

This provision creates a legal fiction as to the point of time the sale of goods is completed for the purposes of this Act. It could be when payment is received as advance by a dealer; or when an invoice is raised ; or when the ownership of goods is transferred ,or when possession of the goods is given, or when the goods are incorporated into the property of the contractee.

Therefore, steel and steel products used as raw material by the petitioners are incorporated into their civil works or other works contracts in the same form except that the same may be

fashioned to suit the requirement, before the same merge into the works which is thereafter identified as immovable property. At the time of incorporation , steel and steel products do not lose their nature or form and therefore cannot be subjected to tax , as the said goods are already subjected to tax as declared goods under the CST Act.

The reliance sought to be placed on the decision of this court in the case of *B.V.Subba Reddy* supra, by the Revenue, which has been followed in later decisions, also cannot be pressed into service – for the same was rendered in the backdrop of there being no dispute that iron and steel that had been purchased by the petitioner therein and had been used in the construction of a bridge and had not been used in the same form. Secondly , the said decision was with reference to the provisions of the KST Act, which did not contain any provision akin to Section 7 of the KVAT Act.

In so far as the dispute regarding the levy of tax @12.5% in respect of advance amounts received by the petitioner in WP 29046-29048/2009 is concerned, it is seen that the petitioner therein was paid the said advances to enable it to carry out preliminary work and procurement of materials. It was not engaged in any activity of manufacture and sale of any goods. The contract it appears was a composite works contract for designing, procurement of materials, construction, erection and commissioning of moulded LPG storage systems, at the site of the contractee. The petitioner is said to have received the said advances during a period when the only activity carried out under the contract was procurement of the steel material and preparation of the same by cutting and rolling into sections to be incorporated into the works. It is not in dispute that the rate of tax in respect of iron and steel i.e., mild steel sections being 4%, the said rate was declared and paid. It is also not in dispute that the said material had not been incorporated into the works. Hence the levy apparently was with reference to the Explanation appended to

Rule 3(1)(a) to (g) of the KVAT Rules. The same reads as follows :

“3. Determination of turnover – (1) The total turnover of a dealer, for the purposes of the Act, shall be the aggregate of –

- (a) the total amount paid or payable by the dealer as the consideration for the purchase of any of the goods in respect of which tax is leviable under sub-section (2) of Section 3;
- (b) the total amount paid or payable to the dealer as the consideration for the sale, supply or distribution of any goods where such sale, supply or distribution has taken place inside the State, whether by the dealer himself or through his agent;
- (c) the total amount paid or payable to the dealer as the consideration for transfer of property in goods (whether as goods or in some other form) involved in the execution of works contract including any amount paid as advance to the dealer as a part of such consideration;
- (d) the total amount paid or payable to the dealer as the consideration for transfer of the right to use any

goods for any purpose (whether or not for specified period);

- (e) the total amount payable to the dealer as the consideration in respect of goods delivered on hire purchase or any system of payment by instalments;
- (f) the aggregate of the sale prices received and receivable by the dealer in respect of sale of any goods in the course of inter-state trade or commerce and export out the territory of India and sale in the course of import into the territory of India; and
- (g) the value of all goods transferred or despatched outside the State otherwise than by way of sale.

[Explanation – Any amount paid as advance to a dealer as apart of consideration for transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract shall be included in his total turnover in the month in which execution of such works contract commences.]

.....”

The ‘Explanation’ above was inserted by a notification dated 27-5-2006 which requires a registered dealer to include the

advance amounts received as part of total turnover in the month in which the execution of works contract commences and pay tax thereon, even though there is no transfer of property in any goods involved . The Explanation certainly runs counter to the tenor of the charging Section 4(1)(c) and runs counter to the definition of 'taxable turnover', 'total turnover' and 'turnover' under the Act. It is also in direct conflict with Article 366(29A)(b) of the Constitution of India.

Similarly, Section 7 of the KVAT Act, which creates a legal fiction that a transaction of sale is completed for the purposes of the Act when payment is received as advance is akin to bringing to tax an agreement to sell goods , even before the property in the goods passes to the buyer. This is plainly contrary to the very definition of "Sale" under the Act itself. Therefore, to the said extent, the above said provisions are unconstitutional.

Hence, the following order:-

The writ petitions are allowed.

- a) It is declared that Section 4(1)(c) read with Serial No.23 of the VI Schedule to the KVAT Act does not enable the respondents to levy tax at the rate of 12.5% in respect of declared goods used in the same form, in the execution of works contracts, which fall under Section 14 of the Central Sales Tax Act, 1956. Consequently, proceedings initiated or concluded in respect of the petitioners seeking to levy tax, as questioned above, are hereby quashed to that extent.
- b) "Explanation" to Rule 3(a) to (g) of the KVAT Rules is contrary to Section 4(1)(c) of the KVAT Act and Article 366(29A)(b) of the Constitution of India and is hence, unconstitutional and invalid. Consequently, the levy of tax

and penalty on advances received by the petitioner in WP 29046-29048/2009 at Annexure-A thereof is hereby quashed.

Sd/—
Judge

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