Some Important Judicial Decisions under MVAT and CST on Saturday, 21st December,2013

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SALE IN COURSE OF IMPORT IN CASE OF SALE FROM FREE TRADE WAREHOUSING ZONE (FTWZ)

A burning issue is going on about exempted sale by way of sale in course of import u/s 5(2) of the CST Act, 1956. The section provides exempted sale as under;

"S.5. When is a sale or purchase of goods said to take place in the course of import or export –

(1) ----

(2) A sale or purchase of goods shall be deemed to take place in the course of the import of the goods into the territory of India only if the sale or purchase either occasions such import or is effected by a transfer of documents of title to the goods before the goods have crossed the customs frontiers of India……."

When the sale is before crossing the Customs Frontiers of India by way of transfer of documents of title to goods, it is exempt. What is crossing Customs Frontiers of India is a debatable issue and not settled till today. There are different judgments on the issue.

For example, in case of **State Trading Corporation of India Ltd. (129 STC 294)**, Hon'ble Madras High Court has held that the sale from bonded warehouse is also allowable u/s 5(2) of the CST Act, 1956. Based on above, Hon'ble MST Tribunal has also considered sale from bonded warehouse as exempted sale u/s 5(2) of the CST Act, 1956 vide judgment in case of **Radha Sons International (S.A.1358 & 1359 of 9.10.2007).** However, from judgment of Tribunal further reference is made to Hon'ble Bombay High Court and the outcome of the same will decide the fate of exempted sale.

The further issue arises about exempted sale from FTWZ. FTWZ is a new concept and broadly, it is on line of bonded warehouse. However, there is still no clarity about exempted sale from the FTWZ.

M/s LG Electronics India Pvt. Limited have filed DDQ before Commissioner of Sales Tax, Maharashtra State to know about status of exempted sale for the sales effected from FTWZ. The Commissioner of Sales Tax has decided the issue vide order in **DDQ-11/2011/Adm-3/16/B-7 dated 30/11/2013.**

The sequence of the transaction is noted in the DDQ as under;

"I have reproduced the facts of the case and the contention of the applicant in detail. The question for determination is

'Whether sale of goods by M/s.L.G. International Singapore vide invoice No.LGIS-091A dated 17/09/2010 to M/s. L.G. Electronics India Pvt. Ltd. Pune for USD 70 by effecting delivery of the goods through Arshiya Supply Chain Management Pvt. Ltd., duly authorized warehousing agent from Free Trade and Warehousing Zone, Dist. Raigad , Maharashtra is a sale effected in the course of import covered by section 5(2) of the CST Act or a sale effected within the State of Maharashtra liable for payment of VAT under the MVAT Act ?'

To ensure a proper understanding of the issue, I would enlist the course of events in the impugned transaction thus:

a. In the **Bill of Lading Is of dt.30.08.2010** LGIS is mentioned as the consignor. ASCMPL On behalf of LGIS is mentioned as consignee. There is mention of the name of 'LGEIPL Ord. No.6010501050 alongwith other details' in the column for Marks and Numbers Container & Seal No. The name of the vessel is 'Hyundai Advance V.253W'
b. In the **Stock Transfer Invoice dt.25.08.2010** raised by LGIS it is mentioned – Consignee / Shipped To: ASCMPL On behalf of LGIS. The value is mentioned as USD 67. It is further mentioned thus – CIF NHAVA SHEVA FINAL DESTINATION ARSHIYA FTWZ CARGO, Village Sai, Panvel.
c. LGIS has addressed **an Authority letter' of nil date** to Dy. Commissioner of Custom, Arshiy FTWZ about appointing M/s. Swen Agencies Pvt. Ltd. to handle customs clearing forwarding & delivery including relevant documentation on their behalf.
d. There is no document titled **'Final Delivery Order' of dt.14.09.2010** by Hyundai Merchant Marine India Pvt. Ltd. addressed to the Manager, Seabird CFS, Nhava Sheva to

give delivery to Swen Agencies Pvt. Ltd. It is mentioned therein that the order is granted to consignee against Letter of Guarantee/Original Bill of Lading.

e. **Bill of Entry for Home Consumption of dt.13.09.2010** mentions Importer's name as ASCMPL on behalf of LGIS. There is mention of the name of 'LGEIPL' Ord. No.6010501050' alongwith other details in the columns for 'Marks and Numbers'. The Declaration on the bills of Entry which is to be signed by the Custom House Agent is signed by Swen Agencies Pvt. Ltd.. This declaration bears a Note that – Where a declaration is made by the importer of the goods. Accordingly on the reverse of the BOE, a declaration is signed by ASCMPL. Here Importer Code and BIN is mentioned as 0309063892. This IE code belongs to LGIS.

f. A **Commercial invoice dt.17.9.2010** is raised by LGIS on LGEIPL. Here consignee is mentioned as LGEIPL and the value is mentioned as USD 70. The Delivery term mentioned on the Commercial Invoices is "Ex Warehouse- Arshiya FTWZ."

g. A **Delivery Order dt.11.10.2010** is issued by LGIS in favor of ASCMPL directing delivery of goods to LGEIPL or in the event of endorsement as per directions mentioned in the endorsements.

h. **In the Bill of Entry for Home Consumption of dt.14.10.2010**, there is mention of the name of 'LGEIPL Ord. No.6010501050' alongwith other details in the column for 'Marks and Numbers'. The importer is mentioned as LGEIPL unlike the Bill of Entry of dt.13.09.2012 where the importer was mentioned as 'ASCMPL on behalf of LGIS'. In this BOE too, a note to the Declaration is signed by Swen Agencies Pvt. Ltd. . However, the declaration on the reverse of the BOE to be signed by the importer is left unfilled and unsigned . Here Importer Code and BIN is mentioned as 0596063211. This IE Code belongs to LGEIPL.

i. Challan dt.14.10.2010 showing amount of payment of duty by LGEIPL is furnished."

After examining the issue, in light of various submissions, the Commissioner of Sales Tax has come to conclusion that above transaction cannot be held as exempt u/s 5(2) of the CST Act, 1956.

In other words, the transaction is denied exemption and considered as liable to tax under MVAT Act, 2002. Amongst others, the observations for holding the transaction liable to tax are reproduced below;

"The applicant has argued that the transaction is covered by the provisions of sub-section (2) of section 5 of the Central Sales Tax Act,1956 (CST Act). The present proceedings are under the provisions of section 56 of the MVAT Act,2002 and to determine whether the impugned transaction is covered under the provisions of the MVAT Act,2002, I have to examine the possibility of coverage of the impugned transaction under the aforesaid sub-section of the CST Act. The sub-section reads thus:

"A sale or purchase of goods shall be deemed to place in the course of import of the goods into the territory of India only if the sale or purchase either occasion such import or is effected by a transfer of documents of titles of tile to the goods before the goods have crossed the customs frontiers of India."

Thus, what the above section says is that a sale or purchase shall deem to take place in the course of the import of the goods into the territory of India only if –

a. the sale or purchase either occasions such import

OR

b. the sale or purchase is effected by a transfer of documents of title to the goods before the goods have crossed the customs frontiers of India.

The impugned transaction is a purchase of the applicant claimed to be in the course of import. With regard to the facts and discussion as held above, I find that both the above contingencies are not fulfilled in respect of the transaction in the present case as follow:

a. The first limb of the above sub-section says that the purchase should occasion the import. The same is not so in the present case when it is seen that the goods are brought into India by LGIS. LGIS is the consignor and by acting through an agent has consciously remained the consignee too. It was LGS who had caused to bring the goods into India. Thus when the goods were brought in India, it cannot be said that the purchase by the applicant had occasioned the import.

b. The second limb says that the purchase is effected by a transfer of documents of title to the goods before the goods have crossed the customs frontiers of India. The

document of title to the goods in the present case is the Bill of Lading. There is no transfer of document of title to the goods in the present case. There is a sale of the goods to the applicant after the goods have reached India and the delivery order directing delivery is a normal course of events between a seller and a buyer. However, it has been contended that LGIS has effected sale to the applicant before the goods have crossed the customs frontiers of India by transfer of delivery order which is a document of title to the goods. With regard to this argument, I have to say that the Delivery Order is prepared at a later date (dt.11.10.2010) than the Commercial invoice (dt.17.9.2010) evidencing sale to the applicant. The Delivery order in the present case is a mere direction to the agent directing delivery to the applicant and it comes after it has been decided to sell the goods to the applicant whereas the second limb of sub-section (2) of section 5 contemplates a sale or purchase which is effected by a transfer of document of title to the goods. Thus, the essential ingredient of the second limb of section 5(2) is that the sale should be by transfer of document of title to the goods. In the present case, the delivery order is not transferred or endorsed in the name of the applicant. Hence, there is no sale by a transfer of document of title to the goods. Here the sale has been effected first and what follows thereafter is an essential concomitant of sale i.e. delivery of the goods. A 'Delivery Order' in the present case cannot be said to be indicating a sale to the applicant and is in fact for an event which come 'after' the sale to the applicant has been finalized. The sale has already been effected and once a sale is effected, a delivery of goods is to follow. By virtue of the sale, the applicant has already become the owner of the goods and thereby has obtained the title to the goods. In this view of the matter, the 'Delivery Order', in the present case, cannot be said to be documents of title to the goods. The document of title to the goods, in the present case, is the Bill of lading. In the present case when ASCMPL takes the goods to the FTWZ, the Bill of lading is surrendered. Thus, there could be no endorsement thereon or transfer thereof to the applicant. Thus, it is seen that the course of import was already over when ASCMPL filed the Bill of Entry for Home Consumption and the imported goods were assessed to duty. The sale transaction thereafter would be a local sale transaction liable to tax under the respective State Act. The document of title to the goods being the Bill of lading, in the present case, there is no endorsement or transfer of the same. Also, the sub-

section contemplates a transfer of documents of title whereas the present delivery order has the effect of directly giving delivery of the goods to the applicant. There is no transfer of delivery or title to the goods from any other person to the applicant. The party holding the goods is ASCMPL which is an agent the LGIS and therefore, it cannot be said that there is delivery by transfer of documents from self to self i.e. LGIS to LGIS and thereafter to the applicant. The word "transfer" implies transferring over of something already in existence which is not the case in the present facts. Thus, there is no transfer of document of title to the goods in the present case as understood by the second limb of sub-section (2) of section 5 of the CST Act. The argument of the applicant that directing the delivery order to the applicant amounts to transfer of document of title to the goods is not well founded. The delivery order in the present case is simply a direction by the seller to the delivery to the purchaser. Since, ASCMPL is appointed as an agent, a direction to the agent to give delivery to LGEL is in effect a direction of the seller only. A possibility of diversion of the goods could not have been ruled out and it is in keeping with the same that LGIS has preferred to remain as the importer into India through its agent ASCMPL.

Having seen that the transaction is not covered by both the first limb as well as the second limb, I have to conclude that the impugned transaction is not covered by sub-section (2) of the section 5 of the CST Act.

In the circumstances, the situation before me now is as to where the transaction could be said to have taken place. The delivery of the goods is taken at Arshiya SEZFTWZ which is located in Maharashtra and the applicant too is located in Maharashtra. Does this mean that the transaction is a sale within the State of Maharashtra ? I find that the Hon. Supreme Court in the case of M/s. Madras Marine and Co. v. State of Madras (1986)(63 STC 169) had an opportunity to deliberate on a similar situation. The verdict of the Hon. Court in the aforementioned case is worth reproducing thus:

"It was rightly urged that the appropriation of goods took place in the State of Tamil Nadu when the goods were segregated in the bonded warehouse to be delivered to the foreign going vessels. It was not a case of export as there was no destination for the goods to a foreign country. The sale was for the purpose of consumption on board the ship. It was not as if only on delivery on board the vessel that the sale took place. The mere fact that shipping bill was

prepared for sending it for customs formalities which were designed to effectively control smuggling activities could not determine the nature of the transaction for the purpose of sales tax nor does the circumstances that delivery was to the captain on board the ship within the territorial waters make it a sale outside the State of Tamil Nadu.

The goods were within the State of Tamil Nadu in case of ascertained goods at the time when the contract of sale was made and in case of unascertained goods at the time of their appropriation to the contract by the seller, sale must be deemed to be within the State of Tamil Nadu. Such appropriate took place in the bounded warehouses which were within the territory of the State of Tamil Nadu. Therefore, under sub-section (2), sub-clause (a) and (b) of section 4 of the Central Sales Tax Act,1956, the sale of goods in question shall be deemed to have taken place inside the State because the contract of sale of ascertained goods was made within the territory of Tamil Nadu and furthermore in case of unascertained goods appropriation had taken place in that State in terms of clause (b) of sub-section (2) of section 4 of the Central Sales Tax Act,1956.

There is no question of sale taking place in the course of export or import under section 5 in this case. From that point of view the amendment introduced by Act 103 of 1976 by incorporating in clause (ab) of section 2 of the Central Sales Tax Act,1956, does not affect the position. In this connection reference may be made from the observations of this Court in Burmah Shell Oil Storage Ltd. (1960) 11 STC 764 (SC) where it has been held that customs barrier does not set a territorial limit to the territory of the State for sales tax purposes. Sale, therefore, beyond the customs barrier is still a sale within the State. The amendment introduced in section 2 by the Act 103 of 1976 does not affect the position because the customs station is within the State of Tamil Nadu. That question might have been relevant if we were considering the case of sale by the transfer of documents of title to the goods as contemplated by section 5 of the Central Sales Tax Act,1956."

"The High Court in Civil Appeal No.642 of 1974 has based its decision on the decision of this Court in State of Madras v. Davar and Co. (1969) 24 STC 481 (SC). In that case the assessee, a dealer in timber, had imported two consignments to timber from Burma and sold it to buyer in India. The ship carrying the first consignment arrived at the Madras Harbour on 17th October,

1957. The assessee obtained money from the buyers on 24th October,1957, retired the documents of title from the bank and banded over the documents on the same day to the buyer to enable them to clear the goods. All charges and expenses by way of import duty, clearance charges, etc., were paid by the buyer on behalf of the assessee. The second consignment reached Madras by ship on 17th December,1957, and the assessee obtained on 23rd December,1957, from the buyers the value of the consignment after handing over to the buyers the necessary shipping documents. The assessee claimed that these sales were in the course of import and these were not liable to tax under the Madras General Sales Tax Act,1959, as there were covered by article 286(1)(b) of the Constitution. It was held that the expression "custom frontiers" in section 5(2) of the Central Sales Tax Act,1956, did not mean "customs barrier". "Customs frontiers" meant the boundaries of the territory, including territorial waters, of India. The sales in this case were effected by transfer of documents of title long after the goods had crossed the customs frontiers of India; the ships carrying the goods in question were all in the respective harbours within the State of Madras when the sale were effected by the assessee by transfer of documents of title to the buyer. The sale were therefore not effected in the course of import."

Thus it can be seen from the above extracts, that the Hon. Apex court has held sale from a bonded warehouse to be within the state in which the same was located. The Hon. Apex court observed that a sale beyond the customs barrier is still within the State. It was further observed that the words 'customs frontiers' as appearing in the second limb of sub-section 2 of the section 5 might have been relevant if there was a case of sale by transfer of documents of title to the goods as contemplated by the said limb. In the present case, as observed earlier, there is no occasion to observe that there is a sale by way of transfer of documents of title to the goods.

The applicant has relied on a number of cases. However, the facts of the present case are different. Hence, I refrain from entering into any exercise of distinguishing these case with regard to the facts of the present case. The applicant has also cited the case to M/s. Hotel Ashoka (cited supra) wherein it has been held that the State of Karnataka has no right to tax any such transaction which takes place at the duty free shops situation at the International Airport of Bengaluru which are not within the customs frontiers of India. It

was observed that when the goods are lying in the bonded warehouses, they are deemed to have been kept outside the customs frontiers of the country and the appellant was selling the goods from the duty free shops before the said goods had crossed the customs frontiers. Even though this case is decided by a Division Bench of the Hon. Supreme Court, I have to observe that the decision in the two judges Bench of the very Supreme Court in M/s. Madras Marine (cited supra) was not before the Hon. Court while delivering the verdict in M/s. Hotal Ashoka (cited supra). In the circumstances, the law laid down in M/s. Madras Marine (cited supra) is also good law. Further, the facts in the instant case stand on firm grounds such that the transaction is not covered by any of the two limbs as found in sub-section (2) of the section 5 of the CST Act. It therefore goes without saying that the transaction represents a sale effected within the State of Maharashtra liable for payment of VAT under the MVAT Act."

Therefore, the issue is still open as to whether sale from FTWZ can be exempt or not? However, in the above case, the facts are peculiar. If there are three parties, like importer storing the goods in FTWZ, selling to another buyer and such buyer further selling to his buyer is not still within the purview of above DDQ.

It is also seen that number of other grounds like observations of Bombay High Court in case of **Narang Hotels and Resorts Pvt. Ltd. (135 STC 289)(Bom)** and that the FTWZ itself is a custom station is not considered in above DDQ.

In my opinion, the above DDQ requires reconsideration as the important aspect that it is at par with bonded warehouse and sales from bonded warehouse are considered exempt is not followed in the above DDQ. In due course of time, the legality should get decided.

'SALE PRICE / TURNOVER' FOR LEVY OF CST

Introduction

Once the transaction is held to be a sale, the next question which arises is the quantum on which such tax is leviable. This is referred to as sale price, in

relation to individual transaction and as "turnover" in relation to aggregate of transactions during particular period. There may be number of different elements which will require consideration while determining sale price/turn over.

Definitions

Under CST Act,1956, the above terms are defined as under:

"(h) 'sale price' means the amount payable to a dealer as consideration for the sale of any goods, less any sum allowed as cash discount according to the practice normally prevailing in the trade, but inclusive of any sum charged for anything done by the dealer in respect of the goods at the time of or before the delivery thereof other than the cost of freight or delivery or the cost of installation in cases where such cost is separately charged;

Provided that in the case of a transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract, the sale price of such goods shall be determined in the prescribed manner by making such deduction from the total consideration for the works contract as may be prescribed and such price shall be deemed to be the sale price for the purposes of this clause."

"(j) 'turnover' used in relation to any dealer liable to tax under this Act means the aggregate of the sale prices received and receivable by him in respect of sales of any goods in the course of inter-State trade or commerce made during any prescribed period and determined in accordance with the provisions of this Act and the rules made thereunder"

From the definition of sale price, it appears that though all amounts charged to the buyer till delivery is given are to be considered as sale price the amount charged separately for freight is not to be included in the sale price.

Interpretation of above definitions

However, interpretation of above definitions have attracted lengthy litigations. There are number of judgments interpreting above terms.

Recently, Hon'ble Supreme Court had an occasion to deal with the above aspect. Hon'ble Supreme Court has delivered judgment in case of **India Meters Ltd. v/s State of Tamil Nadu (34 VST 273).**

In this case, the facts were that the appellant, M/s. **Indian Meters Ltd**. (referred to as dealer) as sold meters manufactured by it to its customers within Tamil Nadu and outside Tamil Nadu. The dealer had charged applicable tax i.e. Tamil Nadu Sales Tax or Central Sales Tax on the price charged by it. The dealer had also collected separately amounts from the buyers towards freight charges, by raising debit notes. The dealer had not paid tax on above amounts. The sales tax authorities held that these amounts are also part of sale price and accordingly levied tax on the same under the respective Acts. Though, Tamil Nadu sales tax appellate Tribunal held in favour of dealer, the High Court held that the said amounts are part of sale price and turnover and therefore correctly held as liable to tax.

The matter came before Supreme Court. Hon'ble Supreme Court examined the facts. It was found that the clause in the sale contract provided that the transfer of title to the goods was to take place only on delivery of goods at customer's place and the customer's obligation to pay would arise only after the delivery had been so effected. Simultaneously it was also found that there was a clause in the contract dealing with price. It was provided that the price was payable per unit, ex-factory delivery. The clause further provided that sales tax and excise duty will be payable only on ex-factory price.

Based on above terms and conditions, it was argued by the dealer that since the prices are ex-factory and freight is charged separately, the said freight can not be liable to tax. Various judgments were cited before Hon'ble Supreme Court.

Supreme Court's ruling

Supreme Court has confirmed the view of the High Court.

Supreme Court observed that in the present case, the obligation to pay the freight was clearly on the dealer as no sale could have taken place unless the goods were delivered at the premises of the buyer. It was further observed that for giving such delivery incurring cost of freight was required on part of dealer. Supreme Court held that though the contract mentioned the price as ex-factory

price, the delivery was not at the factory gate. Therefore, the specification of what the price would be at the factory gate can not have any impact on the place of delivery, held Supreme Court. Supreme Court also observed that had the delivery was completed at the factory gate then the expenses incurred thereafter by way of freight could have been categorized as post sale expenses and could not have been taxable. Thus, ultimately Supreme Court confirmed the levy. Supreme Court reproduced legal position in following manner.

"In **Paprika Ltd. v. Board of Trade (1944) 1 ALL ER 372**, the court observed as under;

"Whenever a sale attracts purchase tax, that tax presumably affects the price which the seller who is liable to pay the tax demands but it does not cease to be the price which the buyer has to pay even the price is expressed as 'X' plus purchase tax."

In this case, the learned judge also quoted with approval what Goddard, L.J., said in **Love v. Norman Wright (Builders) Ltd. (1944) 1 All ER 618:**

"Where an article is taxed, whether by purchase tax, customs duty, or excise duty, the tax becomes part of the price which ordinarily the buyer will have to pay. The price of an ounce of tobacco is what it is because of the rate of tax, but on a sale there is only one consideration though made up of cost plus profit plus tax. So, if a seller offers goods for sale, it is for him to quote a price which includes the tax if he desires to pass it on to the buyer. If the buyer agrees to the price, it is not for him to consider how it is made up or whether the seller has included tax or not"

and summed up the position in the following words:

"So far as the purchaser is concerned, he pays for the goods what the seller demands, namely, the price even though it may include tax. That is the whole consideration for the sale and there is no reason why the whole amount paid to the seller by the purchaser should not be treated as the consideration for the sale and included in the turnover."

Supreme Court further referred to settled position as under:

"This court had an occasion to deal with identical issues in the case of **Hindustan Sugar Mills (1978) 4 SCC 271. P.N. Bhagwati J.** (as His Lordship then was), clearly held that by reason of the provisions of the Control Order which governed the transactions of sale of cement entered into

by the assessee with the purchasers in both the appeals before us, the amount of freight formed part of the "sale price".

In this judgment, the court comprehensively explained the entire principle of law by giving an example in para 8 of the judgment which reads as under:

"8. Take for example, excise duty payable by a dealer who is a manufacturer. When he sells goods manufactured by him, he always passes on the excise duty to the purchaser. Ordinarily, it is not shown as a separate item in the bill, but it is included in the price charged by him. The 'sale price' in such a case could be the entire price inclusive of excise duty because that would be the consideration payable by the purchaser for the sale of the goods. True, the excise duty component of the price would not be an addition to the coffers of the dealer, as it would go to reimburse him in respect of the excise duty already paid by him on the manufacture of the goods. But, even so, it would be part of the 'sale price' because it forms a component of the consideration payable by the purchaser to the dealer. It is only as part of the consideration for the sale of the goods that the amount representing excise duty would be payable by the purchaser. There is no other manner of liability, statutory or otherwise, under which the purchaser would be liable to pay the amount of excise duty to the dealer. And, on this reasoning, it would make no difference whether the amount of excise duty is included in the price charged by the dealer or is shown as a separate item in the bill. In either case, it would be part of the 'sale price'. So also, the amount of sales tax payable by a dealer, whether included in the price or added to it as a separate item, as is usually the case, forms part of the 'sale price'. It is payable by the purchaser to the dealer as part of the consideration for the sale of the goods and hence falls within the first part of the definition..."

Ratio of Supreme Court judgment

The ratio of the judgment is required to be seen carefully. Even if the freight is collected separately, if the delivery is at the door of the customer, than in spite of above exclusion of freight from definition of sale price, it will be includible in the sale price and taxable.

The further ratio which comes out is that if it is established that the delivery is given at the seller's place and the freight charges are incurred

thereafter then the said collection can be considered as post sale collection. It will also be considered as reimbursement of expenditure made on behalf of buyer. In such circumstances, it will not be taxable.

We hope the above judgment will settle down the controversy for all time to come and the dealers can determine the taxation of freight accordingly.

BRANCH TRANSFER, INTER STATE SALE vis-à-vis DISPATCH OF SEMI FINISHED GOODS

Introduction

Under Central Sales Tax Act,1956 (CST Act,1956), the transaction of 'sale' is liable to tax. A transaction of sale becomes inter state sale, if because of such sale, there is movement of subject goods from one state to another state. In other words, if there is link between inter state movement of goods and the pre-agreed sale between the transferor and buyer then there will be inter state sale.

There can be inter state movement, when the goods are sent from one branch in one state to another branch in other state of the same entity or to the agent or principal as the case may be (commonly known as 'consignment transfer/branch transfer').

There is lot of litigation about claim of branch transfer vis-à-vis inter state sale. The transferor branch may be transferring goods to another branch for compliance of requirement of a local customer of the transferee branch. Whether there is conceivable link between dispatch to branch and ultimate sale to the local customer will decide the nature of transaction. If there is conceivable link then the branch transfer will amount to inter state sale. If no such conceivable link then it will not amount to inter state sale and claim of branch transfer will remain allowable.

Whether there is conceivable link between branch transfer and ultimate sale will depend upon facts of each case. Therefore, there cannot be any general ratio about deciding the nature of transaction.

Dispatch of semi-finished goods

An interesting issue arose before Maharashtra Sales Tax Tribunal (MSTT) in case of **Multi Flex Lami Prints Ltd. (Appeal No. 61 of 2008 dated 29.7.2013).**

Facts were that the appellant/dealer was engaged in the activity of supply of packaging pouches. The packing pouches were to be supplied to one particular customer and they were printed accordingly as per his specifications. Appellant had manufacturing unit at Mahad in Maharashtra. There, on the raw materials, processes like colour separation, cylinder making, printing and lamination were carried on. After above processes, the processed goods were sent to Silvasa unit. In Silvasa unit, processes like slitting and pouching were done. Thereafter the pouches were supplied to the customers.

In the assessment, the branch transfer claim was allowed. However, in revision proceedings, the said claim was disallowed holding that the transfer is inter state sale. The fact of manufacturing the goods as per specification of customer in Mahad and dispatch to Silvasa was considered as determinative factor for holding the transfer as inter state sale.

Judgment of Hon'ble Tribunal

Before Hon'ble Tribunal number of arguments about legality of the revision order were taken. However, Hon'ble Tribunal considered the revision action as valid. On merits Hon'ble Tribunal held that the revision is not correct. The observations of Hon'ble Tribunal are reproduced below:

"It was explained in the said letter that the processes namely, colour separation, cylinder making, printing and lamination had been carried out at factory in Mahad and thereafter the laminated films were dispatched to Silvasa Unit of the appellant for further processing such as slitting and pouching. It was then explained by the appellant to the revising Officer that the goods sent to Silvasa Unit were Semi finished goods and thereafter they were slit according t the specification of width given by the customer. The slit films were then stretch wrapped and packed which is known as primary

packing. The said film rolls were thereafter put in corrugated boxes which are known as secondary packing. It was also explained by the appellant to the revising Officer that in case the customer requires the material in pouch form, the laminated/slited films is converted into pouches of types/sizes as per specification of the customers and after quality check and packing they are dispatched to the customer. It also appears that it was explained by the appellant to the revising Officer that, although the goods become identifiable to a particular customer at the time of leaving Mahad Unit but in a Semi finished condition. It was explained by the appellant that the Semi finished goods received by the Silvasa Unit were subjected to further processing of sliting and pouching at Silvasa unit and were thereafter dispatched to the customers at various places outside Silvasa in finished form. It would appear that it was the case of the appellant before the revising Officer that the goods sent to the branch were not delivered/sold as such by the Silvasa branch but they were different goods from the goods sent to the Silvasa branch. A perusal of revision order shows that the revising Officer had not controverted this factual submission of the appellant and thus accepted the contention of the appellant that the goods sent by the appellant to the Silvasa unit were the goods manufactured upto lamination stage and further process such as sliting and pouching were done at Silvasa unit and the goods ultimately delivered to the buyers outside Silvasa were after sliting and pouching made at Silvasa. In support of the claim that sliting and pouching of laminated and printed packaging film amounts to manufacturing activity, the appellant has relied upon the judgment dated 24th Sept. 2012 of the Bombay High Court in Income Tax Appeal No.741 of 2010. The revenue has however relied upon the judgment of the Delhi High Court in the case of Faridabad Iron and Steel Traders Association V/s. Union of India in Civil Writ Petition Nos. 7595 of 2001 and 94 of 2002 decided on 21-11-2003 to support it’s case that Slitting of laminated films does not amount to

manufacture. The concept of manufacture envisages that the processes to which the goods are subjected to should not only bring about change in the goods but the change should be such that the goods after subjecting to processes emerge as a different commercial commodity. In Faridabad Iron and Steel Traders Association, it was held by the Delhi High Court that mere cutting or slitting of Steel Sheet does not amount to manufacture because the identity of the product remains unchanged. We are of the view that in the context of the facts of the present case it would be most appropriate to decide the issue relying upon the judgment of the Bombay High Court in Income Tax Appeal No.741 of 2010. We agree with the appellant that the nature of goods actually delivered to the buyers by Silvasa unit are different from the goods sent by the appellant's factory at Mahad to it's Silvasa Unit. This fact is borne out from the description in the stock transfer invoices raised by the appellant on its Silvasa branch and the sales invoices issued by the Silvasa branch to the buyers."

It is further observed as under;

"In the present appeal before us, the goods manufactured and ultimately delivered to the customer by the Silvasa branch of the appellant are made as per the specifications of the customer. Manufacturing involves the processes namely, colour separation, Cylinder making, printing, lamination, slitting and pouching. Processes upto lamination stage are done at Mahad factory in Maharashtra. The goods manufactured upto lamination stages are sent to Silvasa branch. But they are not delivered to the customer in the form in which they are received by Silvasa branch because the goods in the form in which they are received by Silvasa branch are not ready to be delivered/sold to the customers as per their requirement/orders. The goods received by Silvasa branch are subjected to further processing of slitting and pouching so as to make them appropriate for delivery to the customer as per his specification. Slitting and pouching is done at Silvasa.

Thus, it is clear that the goods delivered by Silvasa branch of the appellant to the customer is a different commercial commodity from the goods sent by Mahad factory of the appellant to Silvasa branch and therefore it is difficult to hold that there is an inter-State sale of the same goods which were manufactured by the Mahad factory of the appellant and dispatched to Silvasa branch. In the case of Bharat Electronics Ltd., (46 VST179), The petitioner had manufactured night vision devices at its Marchilipatnam Unit which were transferred to other units of the petitioner outside the state to be incorporated in the equipment to be manufactured at the other units which were eventually sold therefrom to end customers. It was held by the Andhra Pradesh High Court that it is only if the goods which move from one State to another are sold as they are would the question of such transfer of goods attracting levy of tax under the C.S.T Act as an inter-state sale arise."

The above judgment will be useful for deciding the nature of transaction, when there is branch transfer of semi finished goods. However, the nature of processes carried out at relevant places is also required to be seen before arriving to conclusion. It is expected that above judgment will provide guidelines.

Judgment of Larger Bench of Hon. Supreme Court in case of Larsen & Toubro Ltd. and others in 65 VST 1 in relation to Builders and Developers.

The issue as to whether a Builder, who comes up with his own project and gives possession of premises to the prospective buyers can be liable to VAT as Works Contractor was under hot litigation. The issue has chequered history. It will be useful to refer to relevant legal back ground before coming to Supreme Court judgment.

Reference is required to be made to the important judgment of Supreme Court in **K. Raheja Construction (141 STC 298).** In this case the developer, constructing building, but selling the flats etc. before completion of construction (sale under Construction), is held liable to Works Contract Tax.

In above Supreme Court case the controversy before Supreme Court was about the meaning of 'works contract'. The Honorable Supreme Court has laid down a law which will have far reaching effects upon the builders and developers in entire India.

The facts in above case are that M/s. **K. Raheja** entered into an agreement with land owner for development of the land with construction of residential and commercial buildings. Pursuant to development agreement, M/s.K.Raheja also entered into agreements with its customers for sale of flats/shops. The terms included to handover the possession of flats/shops. The value of land and construction was shown separately. The assessing authorities in Karnataka levied sales tax on the said transactions, considering the agreements as 'sale' by way of Works Contract within the meaning of Karnataka Act. The definition of 'Works Contract' in Karnataka Act read as under:

"'Works Contract' includes any agreement for carrying out for cash deferred payment or other valuable consideration, the building construction, manufacture, processing, fabrication, errection, installation, fitting out, improvement, modification, repair and commissioning of any movable or immovable property."

The argument of assessee was that the construction was on his own property (because of development agreement with land owner) and the buyer is to take possession of flat/office. It was further argued that there is, therefore, no transfer of property in goods in execution of works contract, since a owner of land property cannot execute agreement for transfer of building materials while constructing on his own land. Therefore it was submitted that the sale was of flat and offices, i.e. immovable property, not liable to sales tax.

Supreme Court, however, negatived above submission.
Supreme Court, relying upon the above given definition, held that the scope is wider than normal meaning of Works Contract and includes the contracts entered into while the flat/office is under construction. Supreme Court observed that constructing building on one's own land (but shown as sold

separately in agreement) does not make any difference. Supreme Court further clarified that if the agreement is for sale of flats etc., after the construction is complete, then of course, it will not attract any sales tax as it will be a sale of immovable property. Therefore the above law declared by Supreme Court will bring the developers/ builders within the purview of sales tax liability if the facts are similar. To the extent of agreements entered into before Construction of flats or offices is complete, the liability as works contract can arise.

This judgment in **Raheja Development Corporation (141 STC 298)** was referred to Larger Bench by Supreme Court in case of **Larsen & Toubro Limited and another Vs. State of Karnataka and another (17 VST 460)**. The amendment in MVAT Act, 2002 contemplating tax on under construction contracts (w.e.f. from 20.6.2006) was also challenged before Bombay High Court by **Maharashtra Chamber of Housing Industry and Others v**. **State of Maharashtra and Others**.

Hon. Bombay High Court delivered judgment in case of **Maharashtra Chamber of Housing Industry and Others v**. **State of Maharashtra and Others (51 VST 168)** wherein the Constitutional validity of the amendment to bring in builders within sales tax laws was upheld. Alongwith the issue arising from **K. Raheja**, which was refereed to Hon Larger Bench of Hon. Supreme Court judgment in case of **Larsen & Toubro Limited and another V. State of Karnataka and another (17 VST 460)(SC)**, Hon. Supreme Court also dealt with issue arising from judgment of Hon. Bombay High Court in case of **MCHI**. In other words Hon. Larger Bench of Hon. Supreme Court has considered issue out of MVAT Act,2002.

<u>Judgment of Larger Bench in Larsen & Toubro Limited v. State of Karnataka, Civil Appeal No. 8672 of 2013 dated 26.9.2013 (65 VST 1)</u>

The controversy about the tax on builders is now settled by the larger bench of Hon. Supreme Court in above judgment. The main issue which was under challenge was that the composite transaction involving materials and labour is

only included in Article 366(29A)(b) i.e. transaction involving materials and labour can only be considered as works contract under Sales Tax Laws.

Therefore, the further argument was that when an element like land is involved in the transaction and the price is composite, the said transaction is not capable of being included in Article 366(29A)(b). Accordingly, it was the contention of the builders that such transaction cannot be covered within the sales tax laws.

Alongwith the above main argument the further argument was that ultimately the buyer gets premises which are immovable property and there is no transfer of property as goods during the execution of contract.

However, the above controversy is resolved by Hon. Supreme Court in favour of department and against the builders. The conclusion of the Hon. Supreme Court is contained in para 101 of the judgment which is reproduced below for ready reference.

"101. In light of the above discussion, we may summarise the legal position, as follows:

(i) For sustaining the levy of tax on the goods deemed to have been sold in execution of a works contract, three conditions must be fulfilled: (one) there must be a works contract, (two) the goods should have been involved in the execution of a works contract and (three) the property in those goods must be transferred to a third party either as goods or in some other form.

(ii) For the purposes of Article 366(29-A)(b), in a building contract or any contract to do construction, if the developer has received or is entitled to receive valuable consideration, the above three things are fully met. It is so because in the performance of a contract for construction of building, the goods (chattels) like cement, concrete, steel, bricks etc. are intended to be incorporated in the structure and even though they lost their identity as goods but this factor does not prevent them from being goods.

(iii) Where a contract comprises of both a works contract and a transfer of immovable property, such contract does not denude it of its character as works contract. The term a "works contract" in Article 366 (29-A)(b) takes within its fold all genre of works contract and is not restricted to one specie of contract to provide for labour and services alone. Nothing in Article 366(29-A)(b) limits the term a "works contract".

(iv) Building contracts are species of the works contract. (v) A contract may involve both a contract of work and labour and a contract for sale. In such composite contract, the distinction between contract for sale of goods and contract for work (or service) is virtually diminished.
(vi) The dominant nature test has no application and the traditional decisions which have held that the substance of the contract must be seen have lost their significance where transactions are of the nature contemplated in Article 366(29-A). Even if the dominant intention of the contract is not to transfer the property in goods and rather it is rendering of service or the ultimate transaction is transfer of immovable property, then also it is open to the States to levy sales tax on the materials used in such contract if such contract otherwise has elements of works contract. The enforceability test is also not determinative.
(vii) A transfer of property in goods under clause 29-A(b) of Article 366 is deemed to be a sale of the goods involved in the execution of a works contract by the person making the transfer and the purchase of those goods by the person to whom such transfer is made.
(viii) Even in a single and indivisible works contract, by virtue of the legal fiction introduced by Article 366(29-A)(b), there is a deemed sale of goods which are involved in the execution of the works contract. Such a deemed sale has all the incidents of the sale of goods involved in the execution of a works contract where the contract is divisible into one for the sale of goods and the other for supply of labour and services. In other words, the single and indivisible contract, now by Forty-sixth Amendment has been brought on par with a contract containing two separate agreements and States have now power to levy sales tax on the value of the material in the execution of works contract.
(ix) The expression a tax on the sale or purchase of goods a in Entry 54 in List II of Seventh Schedule when read with the definition clause 29-A of Article 366 includes a tax on the transfer of property in goods whether as goods or in the form other than goods involved in the execution of works contract.
(x) Article 366(29-A)(b) serves to bring transactions where essential ingredients of â€.saleâ€. defined in the Sale of Goods Act, 1930 are absent within the ambit of sale or purchase for the purposes of levy of sales tax.

In other words, transfer of movable property in a works contract is deemed to be sale even though it may not be sale within the meaning of the Sale of Goods Act.

(xi) Taxing the sale of goods element in a works contract under Article 366(29-A)(b) read with Entry 54 List II is permissible even after incorporation of goods provided tax is directed to the value of goods and does not purport to tax the transfer of immovable property. The value of the goods which can constitute the measure for the levy of the tax has to be the value of the goods at the time of incorporation of the goods in works even though property passes as between the developer and the flat purchaser after incorporation of goods.

Thus Hon. Supreme Court has come to conclusion that even if the contract involves an element like land still the transaction can be liable to sales tax as works contract. The overall effects of above judgment can be summarized as under:

Hon'ble Supreme Court has analysed the arguments of both the sides. The main argument of the dealers was that the contract involving two elements only i.e. goods and services, can be considered as works contract under above article 366 (29A)(b). However, Hon'ble Supreme Court has held that there is no such limitation and a contract involving third element like land can also be considered as works contract.

The further argument was that there is transfer of immovable property and not transfer in movable goods to attract sales tax as works contract. In this respect also, Hon'ble Supreme Court rejected the argument observing that even if the goods used get transformed into immovable property and such immovable property get transferred to the buyer, still it will be taxable works contract for sales tax purpose.

However, Hon'ble Supreme Court observed that while taxing value of goods in the contract, no portion relating to immovable property should get taxed.

Hon'ble Supreme Court has also observed that the contract will commence from the stage when the agreement is entered into with the

prospective buyer. In other words, the work completed prior to such agreement will not be taxable.

It is also held that if the sale is of completed premises then it will not be covered by the sales tax laws.

In relation to MVAT Act, 2002, Hon'ble Supreme Court has observed that rule 58(1A) of the MVAT Rules, 2005 should be relooked at by the government and the effect should be clarified by the government.

It is also observed that double taxation should be avoided.

In relation to MVAT Act, 2002 Hon'ble Supreme Court has directed for clarification of rule 58(1A), as well as, also directed to see that there is no double taxation. Under above circumstances, the builders and developers in Maharashtra should wait till such clarification is given by the government, as for proper discharge of liability such clarification is required.

CONCLUSION

Sales Tax is an ever green subject getting developed by number of judgments. It will be endeavor of every professional to keep abreast of the latest developments so as to discharge professional duties efficiently. I hope my above note will be helpful to the participants in day to day practice.