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REPORTABLE

IN THE SUPREME COURT OF INDIA
CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO. 703 OF 2012
(Arising out of Special Leave Petition (Civil) No. 15476/2011)

M/S. ARISTO PRINTERS PVT. LTD. ...APPELLANT

VERSUS

COMMISSIONER OF TRADE TAX,
LUCKNOW, U.P. ...RESPONDENT

WITH

CIVIL APPEAL NO. 705 OF 2012
(Arising out of Special Leave Petition (Civil) No. 15478/2011)

J U D G M E N T

J.B. PARDIWALA, J.

For the convenience of exposition, this judgment is divided into the following parts:

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1. These appeals are at the instance of an assessee and are directed against the judgment and order passed by the High Court of Judicature at Allahabad, dated 8.12.2010, in Trade Tax Revision Nos. 106 & 121 of 2003 respectively (hereinafter, the "**Impugned Judgment**"), by which the revisions filed by Revenue came to be allowed and the order passed by the Trade Tax Tribunal, Ghaziabad, was set aside.

A. FACTUAL MATRIX

2. The appellant-assessee is engaged in the business of printing lottery tickets. It would undertake the work of printing on the paper that was supplied to it by the parties. The ink and processing material, including the necessary chemicals used in the process of printing, were procured by the appellant itself.

3. The Trade Tax Officer, Ward 5, Ghaziabad (hereinafter, the "**Assessing Authority**") *vide* orders dated 28.10.1999 for AY 1996-1997 and AY 1997-1998 respectively, levied trade tax on the value of ink, processing material and packing material used by the appellant for executing the printing work on the basis of Section 3F of the Uttar Pradesh Trade Tax Act, 1948 (for short, "**the Act, 1948**").

4. The appellant, being aggrieved by the aforementioned orders of the Assessing Authority, preferred appeals before the Deputy Commissioner (Appeals)-II, Trade Tax, Ghaziabad (hereinafter, the "**Appellate Authority**"). It was argued by the appellant before the Appellate Authority that the ink, chemicals and other processing materials had not been passed on with the lottery tickets and thus the value of such goods could not have been made liable to tax under Section 3F of the Act, 1948. The Appellate Authority *vide* order dated 14.03.2000 accepted the claim of the

appellant and accordingly deleted the tax assessed on the value of ink and other processing materials. However, the Appellate Authority upheld the levy of tax on the packing materials. The relevant finding of the Appellate Authority is as follows:

> *"Goods on the sale of which tax has been levied on the trader which includes processing material, chemicals, film founta etc. and which is not transferred to the principal after getting job-work/work contract undertaken done under any circumstances. These material are film, chemical print etc and these are used for preparing plate for screen printing and after the use, either it becomes a waste or its nature gets changed, but it is not transferred to principal who get job-work/work contact done under any of the circumstances. It would be pertinent to mention the referred portion of the judgment given by Hon'ble Bombay High Court about Messrs. R.M.A.C. Press (supra), according to which before levying tax on work contract, the necessary test is that transfer of goods either actual or in deemed manner in the contract is essential, while in the above-said case, no transfer of above-said goods viz. ink, film developer, chemicals, founta, disc plate etc. has taken place. Therefore, levying tax on the ink and other uncategorized goods in five appeals is unjustifiable, therefore, it is being set-aside."*
>
> (Emphasis supplied)

5. In the circumstances referred to above, two sets of appeals were filed before the Trade Tax Tribunal, Bench-I, Ghaziabad (hereinafter, the "**Tribunal**") against the order dated 14.03.2000 passed by the Appellate Authority. One set of appeals by the Commissioner of Trade Tax, Uttar Pradesh, against the deletion of tax on the ink and processing material. Another set of appeals by the assessee assailing the levy of tax on the packing material.

6. The Tribunal *vide* an order dated 06.08.2002 allowed the appellant's appeals and set aside the levy of tax on the packaging material. Furthermore, the Tribunal dismissed the Revenue's

appeals and affirmed the order of the Appellate Authority, which had deleted the tax on the value of ink and other processing materials, including chemicals. The Tribunal based its decision on this Court's decision in ***Rainbow Colour Lab & Anr v. State of M.P & Ors.***, reported in **(2000) 2 SCC 385**, and the Bombay High Court's decision in ***Commissioner of Sales Tax, Maharashtra, Bombay v. R.M.D.C. Press Pvt Ltd***, reported in **1998 SCC OnLine Bom 435**.

7. The Revenue, being aggrieved by the aforementioned order passed by the Tribunal, challenged it before the High Court *vide* two Revision Applications, i.e., Trade Tax Revision No. 106 of 2003 and Trade Tax Revision No. 121 of 2003, respectively. The High Court, *vide* the impugned judgment, allowed both the Revision Applications and thereby quashed and set aside the order of the Tribunal as well as the order passed by the Appellate Authority, so far as they set aside the tax on the value of ink and processing material, i.e., chemical. The relevant findings of the High Court are as follows:

> *"In my view the order of the Tribunal is not sustainable. Section 3-F of the Act levies tax on the value of goods involved in execution of works contract. The printing work has been held to be works contract by the Apex Court in the case of State of Maharashtra Vs. M/s. Sarvodaya Printing Press Fine Art Printer (Supra). The question for consideration is whether in the printing of lottery tickets, ink and processing materials, namely, chemicals, etc. are passed on to the customers. Undoubtedly, ink passed on to the customers as it is apparent on the printing paper. The inks are diluted in chemicals (processing material) and such ink in the diluted forms are being used in the printing, therefore, both ink and chemical (processing material) are passed on to the customers. It was not the case of the assessee at any stage that the chemical (processing material) was consumable and evaporates*

in the process of printing and is not passed on to the customers. Therefore, I am of the view that both the ink and chemical used in the printing are passed on to the customers. It may be mentioned here that the assessee had also purchased and used consumable but the same has not been taxed.

The Division Bench of the Bombay High Court in the case of Commissioner of Sales Tax v. Matushree Textile Limited (supra) has held that the contract of dyeing and printing of cloth is a work contract and there is a transfer of property in colours, dyes and chemical.

In the case of Commissioner of Sales Tax, Mumbai, vs. Hari and Company (supra), the Division Bench of Bombay High Court has held that the contract for bringing out the Xerox copies amounts to works contract and the ink used for providing Xerox copies is passed on to the customers and, therefore, its value is liable to tax.

It may be mentioned here that the decision in the case of R.M.D.C. Press Pvt. Ltd. relied upon by the Tribunal is no longer a good law in view of the decision of the Apex Court in the case of Associated Cement Companies Ltd. vs. C.C. reported in 2002 NTN (Vol. 20)-73 and in view of the decision of the Apex Court in the case of State of Maharashtra vs. Sarvodaya Printing Press Fine Art Printer.

In view of the above, the order of the Tribunal as well as the order of the first appellate authority are not sustainable and liable to be set aside, so far it deletes the tax on the value of ink and processing materials, namely, chemical, the order of the assessing authority in this regard is restored."

(Emphasis Supplied)

8. The High Court allowed the revision applications on the ground that the diluted ink (consisting of the ink and the chemicals) was passed onto the customers and thus the ink and the processing material, i.e., the chemical, could not be considered as consumables.

9. In such circumstances referred to above, the appellant assessee is here before this Court with the present appeals.

B. SUBMISSIONS ON BEHALF OF THE PARTIES

(i) Submissions on behalf of the Appellant

10. Mr. Niraj Kumar, the Learned counsel appearing for the appellant, vehemently submitted that the High Court committed a gross error in passing the impugned judgment. According to the learned counsel, the High Court fundamentally misunderstood the nature of lottery tickets, erroneously treating them as "goods". It was submitted that the legal status of lottery tickets is already settled law, establishing them as "actionable claims", which are explicitly excluded from the definition of "goods" under the Act, 1948. Since the very foundation of the tax is on the transfer of property in goods, and lottery tickets are not goods, the entire basis for the tax on the printing of these tickets is incorrect from the outset.

11. The Learned counsel further submitted that the ink and chemicals used in the printing process were essentially consumables whose property is never transferred to the customer. These materials are entirely used up and consumed during the execution of the printing job. Since the customer does not receive the ink or chemicals in any form, but only the service of printing, these items should not be treated as goods that are transferred in execution of the works contract. Reliance was placed on ***Pest Control India Ltd v. Union of India & Ors.***, reported in **1989 SCC OnLine Pat 288**, and ***Deputy Commissioner of Sales Tax (Law), Board of Revenue (Taxes), Ernakulam v. M.K Velu***, reported in **1993 SCC OnLine Ker 577.**

12. In such circumstances referred to above, the Learned counsel prayed that there being merit in his appeals, the same may be

allowed and the impugned judgment passed by the High Court be set aside.

(ii) Submissions on behalf of the Respondent

13. On the other hand, Mr. Bhakti Vardhan Singh, Learned counsel appearing for the State, submitted that the High Court did not commit any error, not to mention any error of law, in passing the impugned judgment.

14. Mr. Singh, placing reliance on ***Commissioner of Sales Tax v. Matushree Textile Limited***, reported in **2003 SCC OnLine Bom 830**, and ***Commissioner of Sales Tax, Mumbai v. Hari and Company***, reported in **2006 SCC OnLine Bom 1466,** submitted that in the facts at hand, it is evident that ink and chemicals have been transferred to the customer and thereby are liable to the levy of tax under Section 3F(1)(b) of the Act, 1948.

15. In such circumstances referred to above, the Learned counsel prayed that, there being no merit in the appeals, the same may be dismissed.

C. ISSUE TO BE DETERMINED

16. Having heard the learned counsel appearing for the parties and having gone through the materials on record, the following question falls for our consideration:

    I. Whether tax can be levied under Section 3F of the Act, 1948, on the ink and processing material used by the appellant in undertaking the printing work?

D. ANALYSIS

(i) Relevant provisions under the Act, 1948

17. Before adverting to the rival submissions canvassed on either side, we must look into a few relevant provisions of the Act, 1948. Section 2(d) of the Act, 1948, defines "goods". The same reads thus:

> *"2(d) "goods" means every kind or class of movable property and includes all materials, commodities and articles involved in the execution of a works contract, and growing crops, grass, trees and things attached to, or fastened to anything permanently attached to the earth which, under the contract of sale, are agreed to be severed, but does not include actionable claims, stocks, shares, securities or postal stationery sold by the Postal Department;"*

18. Section 2(h) of the Act, 1948, defines "Sale". The same reads thus:

> *"2(h) 'Sale', with its grammatical variations and cognate expressions, means any transfer of property in goods (otherwise than by way of a mortgage, hypothecation, charge or pledge) for cash or deferred payment or other valuable consideration, and includes-*
>
> *(i) a transfer, otherwise than in pursuance of a contract of property in any goods for cash, deferred payment or other valuable consideration;*
>
> ***(ii) a transfer of property in goods (whether as goods, or in some other form) involved in the execution of a works contract**;*
>
> *(iii) the delivery of goods on hire purchase or any system of payment by instalments;*
>
> *(iv) a 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;*
>
> *(v) the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration; and*
>
> *(vi) 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 or deferred payment or other valuable consideration ;

Explanation I.--A sale or purchase shall be deemed to have taken place in the State,--

(i) in a case falling under sub-clause (ii) if the goods are in the State at the time of transfer of property in such goods (whether as goods or in some other form) involved in the execution of the works contract, notwithstanding that the agreement for the works contract has been wholly or in part entered into outside the State*;*

(ii) in a case falling under sub-clause (iv), if the goods are used by the lessee within the State during any period, notwithstanding that the agreement for the lease has been entered into outside the State or that the goods have been delivered to lessee outside the State.

Explanation II.--Notwithstanding anything contained in this Act, two independent sales or purchases shall, for the purposes of this Act, be deemed to have taken place-

(a) when the goods are transferred from a principal to his selling, agent and from the selling agent to his purchaser,

(b) when the goods are transferred from the seller to a buying agent and from the buying agent to his principal, if the agent is found, in either of the cases aforesaid,--

(i) to have sold the goods at one rate and passed on the sale proceeds to his principal at another rate; or

(ii) to have purchased the goods at one rate and passed them on to his principal at another rate; or

(iii) not to have accounted to his principal for the entire collection or deductions made by him, in the sales or purchases effected by him on behalf of his principal; or

(iv) to have acted for a fictitious or non-existent principal;"

19. Section 2(m) of the Act, 1948, defines "Works contract". The same reads thus:

"2(m) 'Works contract' includes any agreement for carrying out, for cash, deferred payment or other valuable consideration, the building construction, manufacture, processing, fabrication, erection, installation, fitting out, improvement, modification, repair or commissioning of any movable or immovable property;"

20. Section 3F of the Act, 1948, deals with the taxation of goods involved in the execution of the works contract. The relevant portion of the same reads thus:

"Section 3F - Tax on the right to use any goods or goods involved in the execution of works contract:
(1) Notwithstanding anything contained in Section 3A or Section 3AAA or Section 3D but subject to the provisions of Sections 14 and 15 of the Central Sales Tax Act, 1.956, every dealer shall, for each assessment year, pay a tax on the net turnover of--
(a) [...]
(b) transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract.
at such rate not exceeding twenty percent as the State Government may, by notification, declare and different rates may be declared for different goods or different classes of dealers.
(2) For the purposes of determining the net turnover referred to in sub-section (1), the following amounts shall be deducted from the total amount received or receivable by a dealer in respect of a--
(a) [...]
(b) transfer referred to in clause (b) of sub-section (1),-
(i) the amount representing the sales value of the goods covered by Sections 3, 4 and 5 of the Central Sales Tax Act, 1956;
(ii) the amount representing the value of the goods exempted under Section 4;
(iii) the amount representing the value of the goods, on the sale or purchase whereof tax has been levied or is leviable under this Act at some earlier stage;

(iv) the amount representing the value of the goods manufactured in a new unit exempted under Section 4A or Section 4AAA;

(v) the amount representing the value of the goods supplied to the contractor by the contractee:

Provided that the ownership of such goods remains with the contractee under the terms of the contract;

(vi) the amount representing the labour charges for the execution of the works contract;

(vii) all amounts paid to the sub-contractor as the consideration for execution of the works contract, whether wholly or in part:

Provided that no deduction under this sub-clause shall be allowed unless the dealer claiming deduction produces proof that the sub-contractor is a registered dealer liable to tax under this Act and that such amount is included in the return of turnover filed by such sub-contractor under the provisions of this Act;

(viii) the amount representing the charges for planning, designing and architect's fees;

(ix) the amount representing the charges for obtaining on hire or otherwise machinery and tools used for execution of the works contract;

***(x) the amount representing the cost of consumables used in the execution of the works contract, the property in which is not transferred in the execution of the works contract**;*

(xi) the amount representing the cost of establishment and other similar expenses of the contractor to the extent it is relatable to supply of labour and services;

(xii) the amount representing the profit earned by the contractor to the extent it is relatable to the supply of labour and services.

(3) Where in respect of transfer referred to in clause (b) of subsection (1), the contractor does not maintain proper accounts or the accounts maintained by him are not found by the assessing authority to be worthy of credence and the amount actually incurred towards charges for labour and other services and profit relating to supply of labour and services are not

ascertainable, such charges for labour and other services and such profit may, for the purposes of deductions under clause (b) of sub-section (2), be determined on the basis of such percentage of the value of the (a) transfer referred to in clause (a) of sub-section (1), whether such transfer was agreed to during that assessment year or earlier, works contract as may be prescribed and different percentages may be prescribed for different types of works contract."

(ii) Works Contract – Pre and Post 46th Amendment

21. We deem it necessary and appropriate to briefly refer to the history of the law relating to works contracts. Entry 54 in List II of the Seventh Schedule to the Constitution of India enables the State Legislature to enact legislation providing for levying and collecting tax in respect of the sale and purchase of goods. Article 286 of the Constitution prohibits the State Legislatures from imposing tax on the sale or purchase of goods where such sale or purchase takes place outside the State, or in the course of the import of the goods into, or export of the goods out of, the territory of India.

22. The scope and ambit of the powers of the States to levy sales tax on goods involved in the execution of works contracts have been the subject matter of several judicial pronouncements. The decision of this Court in ***State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd.***, reported in **1958 SCC OnLine SC 100** (hereinafter, **"*Gannon Dunkerley-I*"**), is the leading case on the subject. That was a case where the assessee's (Gannon Dunkerley) business primarily consisted of executing contracts for the construction of buildings, bridges, dams, roads, and other structural projects. During the relevant assessment year under consideration, sales tax was levied under the Madras General Sales Tax Act, 1939, on the value of materials used by the assessee in execution of the works contracts. The assessee

questioned the levy of sales tax on the ground that there was no sale of goods as understood in India and therefore, no sales tax could be levied on any portion of the amount which was received by the assessee from the persons for whose benefit it had constructed buildings. The Constitution Bench of this Court held:

a. In a building contract where the agreement between the parties was that the contractor should construct the building according to the specifications contained in the agreement and in consideration received payment as provided therein, there was neither a contract to sell the materials used in the construction nor the property passed therein as movables. It was held that in a building contract, which is one entire and indivisible contract, there was no sale of goods, and it was not within the competence of the Provincial State Legislature to impose tax on the supply of the materials used in such a contract, treating it as a sale. In a building contract, the title to the materials used in the construction passes to the owner of the land as an accretion, and there is no question of title to the materials passing as movables in favour of the other party to the contract.

b. The expression "sale of goods" in Entry 48 in List II of the Seventh Schedule to the Government of India Act, 1935 (similar to Entry 54 in List II) must be construed in the same sense it has been understood under the Sale of Goods Act, 1930 (for short, "**the Act, 1930**") and to constitute "sale of goods", the essential ingredients are: (a) there should be an agreement to sell movables; (b) it should be for a price; and (c) there should be passing of goods pursuant to the agreement.

Thus, by virtue of this Court's decision in ***Gannon Dunkerley-I*** (*supra*), no sales tax could be levied on the amounts received under a works contract by a building contractor even though it had supplied goods for the construction of the building.

23. The decision of this Court in ***Gannon Dunkerley-I*** (*supra*) was applied in various other decisions wherein courts were dealing with the issue of transfer of goods in execution of works contracts. One such example is the case of ***Northern India Caterers (India) Ltd. v. Lt. Governor of Delhi***, reported in **(1978) 4 SCC 36**. In this case, this Court held that there was no sale when food and drink were supplied to guests residing in a hotel and that the supply of meals was essentially in the nature of a service provided to the guests and could not be identified as a transaction of sale. This Court declined to accept the position that the revenue was entitled to split up the transaction into two parts, one of service and the other of the sale of food items. Accordingly, the proprietor of the restaurant, who provided many services in addition to the supply of food, was not liable to pay sales tax on the value of the goods supplied by him.

24. A summary of the position of law with regard to taxation of goods transferred in execution of works contracts before the enactment of the Forty-sixth Amendment is as follows: (i) works contracts are indivisible, i.e., the revenue could not split a single works contract into two – one pertaining to the provision of goods and another pertaining to the provision of services; (ii) to constitute 'Sale' all ingredients as mentioned under the Act, 1930 had to be fulfilled; and (iii) to determine whether a particular contract was a works contract or a contract for sale, the dominant nature of the contract

was looked into on a fact specific basis *via* the terms and conditions of contract and other related aspects.

25. To overcome the effect of various judicial decisions, the Parliament amended the Constitution by the Constitution (Forty-sixth Amendment) Act, 1982. The constitutional amendments relevant for the purpose herein are as follows:

> ***Amendment of Article 366 – Insertion of clause (29-A)***
>
> *"366. Definitions.-In this Constitution, unless the context otherwise requires, the following expressions have the meanings hereby respectively assigned to them, that is to say-*
>
> *(29-A) 'tax on the sale or purchase of goods' includes—(a) […]*
>
> ***(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) to (f) […]*
>
> *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;"*
>
> ***Amendment of Article 286 – Insertion of clause (3)***
>
> *"286. Restrictions as to imposition of tax on the sale or purchase of goods*
>
> *(3) Any law of a State shall, in so far as it imposes, or authorises the imposition of,*
>
> *(a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or*
>
> *(b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause (29-A) of article 366,*
>
> *be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify."*
>
> ***Amendment of the Seventh Schedule – Insertion of entry 92B***

> *"92B. Taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State or commerce"*

26. In light of the Forty-sixth Amendment to the Constitution, several state governments amended their sales tax laws and made provisions for the imposition of sales tax in relation to works contracts. Each State adopted its own method of determining taxable turnover either by framing rules under its sales tax law or by issuing administrative directions. The method adopted by the States for determining the taxable turnover relating to works contracts for purposes of levy of sales tax were such that sales tax had to be paid by the building contractors not merely on the value of materials supplied by them in connection with the works contracts but also on the expenditure they had incurred in securing the services of architects and engineers who had supervised the execution of the works, and also on the amount which they were entitled to receive for supervising the execution of the works. While levying sales tax on the price of the materials supplied for the construction of houses, factories, bridges, etc., the sales tax authorities of the States did not take into account the conditions and restrictions imposed by Article 286 of the Constitution and the provisions of the Central Sales Tax Act, 1956 (for short, "**the Act, 1956**").

27. The validity of such State legislations as well as the constitutional validity of the Forty-sixth Amendment was considered by this Court in ***Builders Association of India & Ors. v. Union of India & Ors.***, reported in **(1989) 2 SCC 645**. The Court upheld the constitutionality of the Forty-sixth Amendment. On the issue of

the validity of the State legislations, it was contended by the States that:

a. When a works contract is executed, what is handed over is a 'conglomerate' of all the goods used, and the goods pass in an indivisible manner. In such cases, it was not possible to disintegrate the contract into a contract for sale and a contract for work, and thus, Article 366(29-A)(b) of the Constitution has conferred on the legislatures of States the power to levy tax on works contract; and
b. The power to levy tax provided under Article 366(29-A)(b) was independent of the power conferred on the legislatures of states under Entry 54, and the same was not bound by restrictions imposed under Article 286 and the Act, 1956.

28. Rejecting the aforesaid contentions, this Court made the following pertinent observations:

> *"32 [...]Sub-clause (b) of clause (29-A) states that 'tax on the sale or purchase of goods' includes among other things a tax on the transfer of property in the goods (whether as goods or in some other form) involved in the execution of a works contract. It does not say that a tax on the sale or purchase of goods included a tax on the amount paid for the execution of a works contract. It refers to 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. The emphasis is on the transfer of property in goods (whether as goods or in some other form). The latter part of clause (29-A) of Article 366 of the Constitution makes the position very clear. While referring to the transfer, delivery or supply of any goods that takes place as per sub-clauses (a) to (f) of clause (29-A), the latter part of clause (29-A) says that "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. Hence, a transfer of*

property in goods under sub-clause (b) of clause (29-A) is deemed to be a sale of the goods involved in the execution of a works contract by the person making the transfer and a purchase of those goods by the person to whom such transfer is made. The object of the new definition introduced in clause (29-A) of Article 366 of the Constitution is, therefore, 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) thereof wherever such transfer, delivery or supply becomes subject to levy of sales tax. 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. The tax leviable by virtue of sub-clause (b) of clause (29-A) of Article 366 of the Constitution thus becomes subject to the same discipline to which any levy under entry 54 of the State List is made subject to under the Constitution. The position is the same when we look at Article 286 of the Constitution.[...]We are of the view that all transfers, deliveries and supplies of goods referred to in clauses (a) to (f) of clause (29-A) of Article 366 of the Constitution are subject to the restrictions and conditions mentioned in clause (1), clause (2) and sub-clause (a) of clause (3) of Article 286 of the Constitution and the transfers and deliveries that take place under sub-clauses (b), (c) and (d) of clause (29-A) of Article 366 of the Constitution are subject to an additional restriction mentioned in sub-clause (b) of Article 286(3) of the Constitution.

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36. Even after the decision of this Court in the State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd. it was quite possible that where a contract entered into in connection with the construction of a building consisted of two parts, namely, one part relating to the sale of materials used in the construction of the building by the contractor to the person who had assigned the contract and another part dealing with the supply of labour and services, sales tax was leviable on the goods which were agreed to be sold

under the first part. But sales tax could not be levied when the contract in question was a single and indivisible works contract. After the 46th Amendment the works contract which was an indivisible one is by a legal fiction altered into a contract which is divisible into one for sale of goods and the other for supply of labour and services. After the 46th Amendment, it has become possible for the States to levy sales tax on the value of goods involved in a works contract in the same way in which the sales tax was leviable on the price of the goods and materials supplied in a building contract which had been entered into in two distinct and separate parts as stated above. It could not have been the contention of the Revenue prior to the 46th Amendment that when the goods and materials had been supplied under a distinct and separate contract by the contractor for the purpose of construction of a building the assessment of sales tax could be made ignoring the restrictions and conditions incorporated in Article 286 of the Constitution. If that was the position can the States contend after the 46th Amendment under which by a legal fiction the transfer of property in goods involved in a works contract was made liable to payment of sales tax that they are not governed by Article 286 while levying sales tax on sale of goods involved in a works contract? They cannot do so. When the law creates a legal fiction such fiction should be carried to its logical end. There should not be any hesitation in giving full effect to it. If the power to tax a sale in an ordinary sense is subject to certain conditions and restrictions imposed by the Constitution, the power to tax a transaction which is deemed to be a sale under Article 366(29-A) of the Constitution should also be subject to the same restrictions and conditions[…]

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39.In view of the foregoing statements with regard to the passing of the property in goods which are involved in works contract and the legal fiction created by clause (29-A) of Article 366 of the Constitution it is difficult to agree with the contention of the States that the properties that are transferred to the owner in the execution of a works contract are not the goods involved in the execution of the works contract, but a conglomerate, that is the entire building that is actually

constructed. After the 46th Amendment it is not possible to accede to the plea of the States that what is transferred in a works contract is the right in the immovable property.

40. We are surprised at the attitude of the States which have put forward the plea that on the passing of the 46th Amendment the Constitution had conferred on the States a larger freedom than what they had before in regard to their power to levy sales tax under Entry 54 of the State List. The 46th Amendment does no more than making it possible for the States to levy sales tax on the price of goods and materials used in works contracts as if there was a sale of such goods and materials. We do not accept the argument that sub-clause (b) of Article 366(29-A) should be read as being equivalent to a separate entry in List II of the Seventh Schedule to the Constitution enabling the States to levy tax on sales and purchases independent of Entry 54 thereof. As the Constitution exists today the power of the States to levy taxes on sales and purchases of goods including the "deemed" sales and purchases of goods under clause (29-A) of Article 366 is to be found only in Entry 54 and not outside it. We may recapitulate here the observations of the Constitution Bench in the case of Bengal Immunity Co. Ltd.- in which this Court has held that the operative provisions of the several parts of Article 286 which imposes restrictions on the levy of sales tax by the States are intended to deal with different topics and one could not be projected or read into another and each one of them has to be obeyed while any sale or purchase is taxed under Entry 54 of the State List"

(Emphasis supplied)

Thus, this Court in ***Builders Association*** (*supra*) clarified that the power to levy tax under Article 366(29A)(b) did not vest in the States the power to tax works contracts themselves, nor did it allow the States to levy taxation *dehors* the restrictions imposed under Article 286 of the Constitution and the Act, 1956.

29. In ***Gannon Dunkerley & Co. & Ors. v. State of Rajasthan & Ors.***, reported in **(1993) 1 SCC 364** (hereinafter, "***Gannon Dunkerley-II***"), once again, this Court was faced with a host of questions pertaining to the imposition of tax on the transfer of property in goods involved in the execution of works contracts. One of the contentions raised herein was that after the enactment of the Forty-sixth Amendment, no amendment was brought to the Act, 1956, applying its provision to the transfer of property in goods involved in the execution of the works contracts. Consequently, Sections 3, 4 and 5 of the Act, 1956 would not be applicable to such transfers. This Court held as follows:

> *"31. The legislative power of the States 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. Under Entry 92-A of List I, Parliament has the power to make a law in respect of taxes on sale or purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce. The levy and collection of such tax is governed by Article 269. This shows that the legislative power under Entry 54 of the State List is not available in respect of transactions of sale or purchase which take place in the course of inter-State trade or commerce. Similarly clause (1) of Article 286 prohibits the State from making a law imposing or authorising the imposition of a tax on the sale or purchase of goods where such sale or purchase takes place (a) outside the State or (b) in the course of the import of goods into or export of the goods out of the territory of India. As a result of the said provision, the legislative power conferred under Entry 54 of the State List does not extend to imposing tax on a sale or purchase of goods which takes place outside the State or which takes place in the course of import or export of goods. In view of the aforesaid limitations imposed by the Constitution on the legislative power of the States under Entry 54 of the State List, it is beyond the competence of the State Legislature to make a law*

imposing or authorising the imposition of a tax on transfer of property in goods involved in the execution of a works contract, with the aid of sub-clause (b) of clause (29-A) of Article 366, in respect of transactions which take place in the course of inter-State trade or commerce or transactions which constitute sales outside the State or sales in the course of import or export. Consequently, it is not permissible for a State to frame the legislative enactment in exercise of the legislative power conferred by Entry 54 in State List in a manner as to assume the power to impose tax on such transactions and thereby transgress these constitutional limitations. Apart from the limitations referred to above which curtail the ambit of the legislative competence of the State Legislatures, there is clause (3) of Article 286 which enables Parliament to make a law placing restrictions and conditions on the exercise of the legislative power of the State under Entry 54 in State List in regard to the system of levy, rates and other incidents of tax. Such a law may be in relation to (a) goods declared by Parliament by law to be of special importance in inter-State trade or commerce, or (b) to taxes of the nature referred to in sub-clauses (b), (c) and (d) of clause (29-A) of Article 366. When such a law is enacted by Parliament the legislative power of the States under Entry 54 in State List has to be exercised subject to the restrictions and conditions specified in that law. In exercise of the power conferred by Article 286(3)(a) Parliament has enacted Sections 14 and 15 of the Central Sales Tax Act, 1956. No law has, however, been made by Parliament in exercise of its power under Article 286(3)(b).

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34. The question is whether in the absence of an amendment in the Central Sales Tax Act specifically applying its provisions to a transfer of property in goods involved in the execution of a works contract, the provisions of Sections 3, 4 and 5 contained in Chapter II can be held applicable to such a transfer. In this context, it may be mentioned that prior to the Forty-sixth Amendment, a distinction was being made between a 'works contract' which was entire and indivisible and a works contract composed of two distinct and separate contracts — one, for transfer of

materials and other, for payment of remuneration for services and for work done. The non-availability of the legislative power of the States under Entry 54 of the State List, as construed by this Court in the Gannon Dunkerley case was confined, in its application, to works contracts falling in the first category, i.e., contracts which were entire and indivisible and it was permissible for the States to impose tax on sale or purchase of goods where the parties had entered into distinct and separate contracts one for the transfer of materials and other for payment of service and for work done. The provisions of Sections 3, 4 and 5 of the Central Sales Tax Act were applicable where there were two separate contracts[...]

35. This would mean that as a result of the Forty-sixth Amendment, the contract which was single and indivisible has been altered by a legal fiction into a contract which is divisible into one for sale of goods and other for supply of labour and services and as a result such a contract which was single and indivisible has been brought on a par with a contract containing two separate agreements. Since the provisions of Sections 3, 4 and 5 were applicable to such contracts containing two separate agreements, there is no reason why the said provisions should not apply to a contract which, though single and indivisible, by legal fiction introduced by the Forty-sixth Amendment, has been altered into a contract which is divisible into one for sale of goods and other for labour and services[...]

36. If the legal fiction introduced by Article 366(29-A)(b) is carried to its logical end it follows that even in a single and indivisible works contract there is a deemed sale of the goods which are involved in the execution of a works contract. Such a deemed sale has all the incidents of a sale of goods involved in the execution of a works contract where the contract is divisible into one for sale of goods and the other for supply of labour and services.

37. For the reasons aforesaid, we are of the view that even in the absence of any amendment having been made in the Central Sales Tax Act (after the Forty-sixth Amendment) expressly including transfers of property

in goods involved in execution of a works contract, the provisions contained in Sections 3, 4 and 5 would be applicable to such transfers and the legislative power of the State to impose tax on such transfers under Entry 54 of the State List will have to be exercised keeping in view the provisions contained in Sections 3, 4 and 5 of the Central Sales Tax Act. For the same reasons Sections 14 and 15 of the Central Sales Tax Act would also be applicable to the deemed sales resulting from transfer of property in goods involved in the execution of a works contract and the legislative power under Entry 54 in State List will have to be exercised subject to the restrictions and conditions prescribed in the said provisions in respect of goods that have been declared to be of special importance in inter-State trade or commerce.

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41. It must, therefore, be held that 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 (29-A) of Article 366 of the Constitution, 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 an outside sale under Section 4 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 permissible 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)

30. After laying down the scope of power of the State legislatures to enact laws imposing tax on the transfer of property in goods involved in the execution of a works contract, the Court discussed various aspects relating to such laws. One important aspect discussed by the Court was when the tax could be imposed, on

what value it was to be imposed, and how to measure such value. The relevant observations read thus:

> *"45. On behalf of the contractors, it has been urged that under a law imposing a tax on the transfer of property in goods involved in the execution of a works contract under Entry 54 of the State List read with Article 366(29-A)(b), the tax is imposed on the goods which are involved in the execution of a works contract and the measure for levying such a tax can only be the value of the goods so involved and the value of the works contract cannot be made the measure for levying the tax. The submission is further that the value of such goods would be the cost of acquisition of the goods by the contractor and, therefore, the measure for levy of tax can only be the cost at which the goods involved in the execution of a works contract were obtained by the contractor. On behalf of the States, it has been submitted that since the property in goods which are involved in the execution of a works contract passes only when the goods are incorporated in the works, the measure for the levy of the tax would be the value of the goods at the time of their incorporation in the works as well as the cost of incorporation of the goods in the works. We are in agreement with the submission that measure for the levy of the tax contemplated by Article 366(29-A)(b) is the value of the goods involved in the execution of a works contract. In Builders' Association case it has been pointed out that in Article 366(29-A)(b), "[t]he emphasis is on the transfer of property in goods (whether as goods or in some other form)".)This indicates that though the tax is imposed on the transfer of property in goods involved in the execution of a works contract, the measure for levy of such imposition is the value of the goods involved in the execution of a works contract. We are, however, unable to agree with the contention urged on behalf of the contractors that the value of such goods for levying the tax can be assessed only on the basis of the cost of acquisition of the goods by the contractor. Since the taxable event is the transfer of property in goods involved in the execution of a works contract and the said transfer of property in such goods takes place when the goods are incorporated in the works, 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 the works and not the cost of acquisition of the goods by the contractor. We are also unable to accept the contention urged on behalf of the States that in addition to the value of the goods involved in the execution of the works contract the cost of incorporation of the goods in the works can be included in the measure for levy of tax. Incorporation of the goods in the works forms part of the contract relating to work and labour which is distinct from the contract for transfer of property in goods and, therefore, the cost of incorporation of the goods in the works cannot be made a part of the measure for levy of tax contemplated by Article 366(29-A)(b).

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47. Keeping in view the legal fiction introduced by the Forty-sixth Amendment whereby the works contract which was entire and indivisible has been altered into a contract which is divisible into one for sale of goods and other for supply of labour and services, the value of the goods involved in the execution of a works contract on which tax is leviable must exclude the charges which appertain to the contract for supply of labour and service[...]The value of the goods involved in the execution of a works contract will, therefore, have to be determined by taking into account the value of the entire works contract and deducting therefrom the charges towards labour and services which would cover—

(a) Labour charges for execution of the works;

(b) amount paid to a sub-contractor for labour and services;

(c) charges for planning, designing and architect's fees;

(d) charges for obtaining on hire or otherwise machinery and tools used for the execution of the works contract;

(e) cost of consumables such as water, electricity, fuel, etc. used in the execution of the works contract the property in which is not transferred in the course of execution of a works contract; and

(f) cost of establishment of the contractor to the extent it is relatable to supply of labour and services;

(g) other similar expenses relatable to supply of labour and services;

(h) profit earned by the contractor to the extent it is relatable to supply of labour and services.

The amounts deductible under these heads will have to be determined in the light of the facts of a particular case on the basis of the material produced by the contractor."

(Emphasis supplied)

Thus, this Court in ***Gannon Dunkerley -II*** (*supra*) held that the taxable event is the transfer of property in goods involved in the execution of a works contract, and that transfer occurs when the goods are incorporated in the "works". Consequently, it is the value of goods at the time of incorporation which have to constitute the measure for the levy of the tax.

31. A Three-judge Bench of this Court in ***Larsen and Toubro Limited & Anr. v. State of Karnataka & Anr.***, reported in **(2014) 1 SCC 708**, was faced with the question whether taxing the sale of goods in an agreement for the sale of a flat by a developer/promoter was permissible. This Court, when dealing with the said issue, made some pertinent observations with regard to: (i) the interpretation of Article 366(29-A)(b) of the Constitution; (ii) the scope and meaning of works contract; and (iii) the application of the dominant intention test. They read as follows:

"56. It is important to ascertain the meaning of sub-clause (b) of clause (29-A) of Article 366 of the Constitution. As the very title of Article 366 shows, it is the definition clause. It starts by saying that in the Constitution unless the context otherwise requires the expressions defined in that article shall have the meanings respectively assigned to them in the article. The definition of expression "tax on sale or purchase of the goods" is contained in clause (29-A). If the first part of clause (29-A) is read with sub-clause (b) along with latter part of this clause, it reads like this: "tax on the sale or purchase of the goods" 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 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. The definition of "goods" in clause (12) is inclusive. It includes all materials, commodities and articles. The expression "goods" has a broader meaning than merchandise. Chattels or movables are goods within the meaning of clause (12). Sub-clause (b) refers to transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract. The expression "in some other form" in the bracket is of utmost significance as by this expression the ordinary understanding of the term "goods" has been enlarged by bringing within its fold goods in a form other than goods. Goods in some other form would thus mean goods which have ceased to be chattels or movables or merchandise and become attached or embedded to earth. In other words, goods which have by incorporation become part of immovable property are deemed as goods. The definition of "tax on the sale or purchase of goods" includes a tax on the transfer of property in the goods as goods or which have lost its form as goods and have acquired some other form involved in the execution of a works contract.

57. Viewed thus, 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.

58. The States have now been conferred with the power to tax indivisible contracts of works[…]The taxable event is a deemed sale.

59. […] It is open to the States to divide the works contract into two separate contracts by legal fiction : (i) contract for sale of goods involved in the works contract, and (ii) for supply of labour and service. By the Forty-sixth Amendment, the States have been empowered to bifurcate the contract and to levy sales

tax on the value of the material in the execution of the works contract.

60. Whether the contract involved a dominant intention to transfer the property in goods, in our view, is not at all material. It is not necessary to ascertain what is the dominant intention of the contract. Even if the dominant intention of the contract is not to transfer the property in goods and rather it is the 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 it otherwise has elements of works contract. The view taken by a two-Judge Bench of this Court in Rainbow Colour Lab that the division of the contract after the Forty-sixth Amendment can be made only if the works contract involved a dominant intention to transfer the property in goods and not in contracts where the transfer of property takes place as an incident of contract of service is no longer good law, Rainbow Colour Lab has been expressly overruled by a three-Judge Bench in Associated Cement.

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68. There is no doubt that to attract Article 366(29-A)(b) there has to be a works contract but then what is its meaning. The term "works contract" needs to be understood in a manner that Parliament had in its view at the time of the Forty-sixth Amendment and which is more appropriate to Article 366(29-A)(b).

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72. In our opinion, the term "works contract" in Article 366(29-A)(b) is amply wide and cannot be confined to a particular understanding of the term or to a particular form. The term encompasses a wide range and many varieties of contract. Parliament had such wide meaning of "works contract" in its view at the time of the Forty-sixth Amendment. The object of insertion of clause (29-A) in Article 366 was to enlarge the scope of the expression "tax on sale or purchase of goods" and overcome Gannon Dunkerley (1). Seen thus, even if in a contract, besides the obligations of supply of goods and materials and performance of labour and services, some additional obligations are imposed, such contract does not cease to be works contract. The additional obligations in the contract would not alter the nature of

contract so long as the contract provides for a contract for works and satisfies the primary description of works contract. Once the characteristics or elements of works contract are satisfied in a contract then irrespective of additional obligations, such contract would be covered by the term "works contract". Nothing in Article 366(29-A)(b) limits the term "works contract" to contract for labour and service only. The learned Advocate General for Maharashtra was right in his submission that the term "works contract" cannot be confined to a contract to provide labour and services but is a contract for undertaking or bringing into existence some "works". We are also in agreement with the submission of Mr K.N. Bhat that the term "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. Parliament had all genre of works contract in view when clause (29-A) was inserted in Article 366.

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87. It seems to us (and that is the view taken in some of the decisions) that a contract may involve both a contract of work and labour and a contract of sale of goods. In our opinion, the distinction between contract for sale of goods and contract for work (or service) has almost diminished in the matters of composite contract involving both a contract of work/ labour and a contract for sale for the purposes of Article 366(29-A)(b). Now by legal fiction under Article 366(29-A)(b), it is permissible to make such contract divisible by separating the transfer of property in goods as goods or in some other form from the contract of work and labour. A transfer of property in goods under clause (29-A)(b) of Article 366 is deemed to be a sale of 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. For this reason, the traditional decisions which hold that the substance of the contract must be seen have lost their significance. What was viewed traditionally has to be now understood in light of the philosophy of Article 366(29-A)."

(Emphasis supplied)

32. This Court in the ***Kone Elevator India Private Limited v. State of Tamil Nadu,*** reported in **(2014) 7 SCC 1**, and in ***State of Karnataka & Ors v. M/s Pro Lab & Ors.,*** reported in **(2015) 8 SCC 557** respectively, once again reiterated that the dominant intention test is not applicable when determining whether a particular contract is a works contract for the purposes of Article 366 (29-A) (b). In ***Larsen and Toubro*** (*supra)* and ***Pro lab*** (*supra)* respectively, this Court specifically reiterated that the ruling in ***Rainbow Colour Lab*** (*supra)* was overturned by a Three-judge Bench of this Court in ***Associated Cement Companies Ltd v. Commissioner of Customs***, reported in **(2001) 4 SCC 593**.

33. The position of law with regard to taxation of goods transferred under works contracts after the enactment of the Forty-sixth Amendment may be summarised as follows:

    a. *Vide* Article 366(29-A)(b), the States can only tax the *transfer of property in goods* (whether as goods or in some other form) involved in the execution of a works contract and not the works contract itself;

    b. States cannot exercise the power conferred upon them under Article 366(29-A)(b) *dehors* the restrictions imposed under Article 286 of the Constitution and the Act, 1956 (specifically Sections 3, 4, 5, 14 and 15 respectively);

    c. Indivisible works contracts are now, by virtue of the legal fiction created under Article 366(29-A)(b), divided into two parts, one for the sale of goods and the other for the supply of labour and services;

    d. A transfer of property in goods under Article 366(29-A)(b) is deemed to be a sale of the goods. Article 366(29-A)(b) serves

to bring transactions where essential ingredients of "sale" defined in the Act, 1930 are absent within the ambit of sale or purchase for the purposes of levy of sales tax. In other words, the transfer of movable property in a works contract is deemed to be a sale even though it may not be considered as "sale" within the meaning of the Act, 1930;

e. The term "works contract" in Article 366(29-A)(b) takes within its fold all genres of works contracts and is not restricted to one particular specie of contract to provide for labour and services alone; and

f. The dominant nature test is no longer applicable and has lost its significance where transactions are of the nature contemplated in Article 366(29-A).

(iii) Whether the ink, chemical and other processing materials are liable to the levy of tax under Section 3F(1)(b) of the Act, 1948?

34. Section 3F(1)(b) of the Act, 1948, levies tax on the "*transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract*".

35. In the case at hand, the principal question that falls for our consideration is whether there has been a transfer of property in the ink and other processing materials used for the purpose of printing lottery tickets, thereby making them liable to the levy of tax under Section 3F(1)(b) of the Act, 1948.

36. The principal contention put forward by the appellant is that the lottery tickets are not 'goods' and are rather 'actionable claims'. Since 'actionable claims' are not considered as 'goods' under

Section 2(d) of the Act, 1948, according to the appellant, the lottery tickets cannot be brought within the ambit of Section 3F(1)(b) of the Act, 1948. Consequently, it is not liable to pay any tax under the said section.

37. The aforesaid contention of the appellant is devoid of any merit. On a close reading of Section 3F(1)(b) of the Act, 1948, it is amply clear that the tax levied is not on the *'goods' produced in pursuance of a works contract*, i.e., the lottery tickets in the case at hand. The tax under Section 3F(1)(b) of the Act, 1948, is rather on the *'goods' which* are *involved in the execution of the works contract*. Thus, the appellant's contention is misplaced, as it equates lottery tickets with goods involved in the execution of the works contract, which is clearly not the case.

38. In order to sustain a levy of tax under Section 3F(1)(b) of the Act, 1948, three conditions must be fulfilled: (i) there must be a works contract; (ii) the goods should have been involved in the execution of the works contract; and (iii) the property in those goods must be transferred to a third party either as goods or in some other form.

39. In the facts of the present case, it is not in dispute that the first two conditions are fulfilled. The appellant has admitted that the contract for printing lottery tickets is a works contract. Based on the judgments of this Court discussed above, it cannot be said otherwise. Further, from the record, it is clear that the ink, chemical and other processing material were involved in the printing of the lottery tickets.

40. The primary subject of disagreement is with regard to the third condition. On one hand, the appellant contends that the ink and

chemical are consumed in the process of printing the tickets and thus, there is no transfer of property in those goods. Consequently, no tax under Section 3F(1)(b) of the Act is maintainable. On the other hand, the Revenue contends that the ink and chemicals have been transferred to the third party in execution of the work contract, i.e., printing work.

41. This Court and various High Courts have, in a plethora of judgments, discussed this aspect of the transfer of property in goods involved in the execution of works contracts. For the convenience of exposition, these cases are categorised under three broad heads, in accordance with the ratio laid down in the judgments: (a) tangible transfer of property; (b) no transfer of property due to consumption of goods; and (c) transfer of property despite consumption of goods.

a. Tangible Transfer of property

42. In ***Matushree*** (*supra*) the question before the Bombay High Court was whether the coloured shade/print passed on to the fabric in the course of dyeing and printing amounts to transfer of property of the materials used in dyeing and printing under the Maharashtra Sales Tax on the Transfer of Property in Goods involved in the Execution of Works Contracts Act, 1989 (for short, "**Maharashtra Works Contracts Act**"). In the said case, the primary contention of the respondent was that the colours, dyes and chemicals are consumed in the process of dyeing and therefore, the property in those goods was not transferred as goods or in any other form. Rejecting the said contention, the Bombay High Court held as follows:

> *"32. […]According to Mr. Joshi, unless the materials used in dyeing and printing pass in some or the other physical form, there is no passing of property in goods.*

In other words, according to Mr. Joshi if the property in goods passes as a result of some chemical reaction, then such passing of the property in goods is by accretion and not by transfer of the property in goods. The arguments put forth by Mr. Joshi can be best understood by referring to the different forms of water (as and by way of analogy), as stated hereinbelow:

> *"Water in the normal temperature is in liquid form, in high temperature it is in the vapour form and in low temperature it is in the solid form. These are all different physical forms of water. However, when the water is subjected to electrolysis and an electric current is passed through water, due to chemical reaction, the water molecules break into two, namely, hydrogen and oxygen. Thus, on chemical reaction the water is converted into a chemical form or gaseous form comprising of hydrogen and oxygen. According to Mr. Joshi, property in water can be said to pass, only if, there is transfer in any physical form (i.e., either in liquid form, solid form or vapour form) and not in its chemical form or gaseous form (i.e., as hydrogen and oxygen)."*

33. We see no merit in the contentions raised by the respondents. When the term "sale" in the Works Contracts Act has been defined to include by a deemed fiction, the transfer of property in goods in any form, there is no reason to restrict the definition to cover only those transactions which involve transfer of goods in some physical form and not in some chemical form. In our opinion, the words "some other form" used in the definition of "sale" in the Works Contracts Act apply to the transfer of property in goods in its every form, i.e., physical form or any other form, including the chemical form. In other words, transfer of property in goods used in the execution of a works contract, either in its physical form or any other form including the chemical form constitutes sale under the Works Contracts Act. In the present case, the coloured shade is passed to the fabrics due to the chemical reaction of the materials used in the process of dyeing. Coloured shade may be due to the chemical reaction of one or more materials. The coloured shade represents the inherent chemical property of the materials used. Once there is passing of the chemical property of the materials used in the

execution of works contract, then under the Works Contracts Act, there is a deemed sale of the materials used in the execution of the works contract. Accordingly we hold that in the process of dyeing, the coloured shade passed on to the fabrics constitutes sale of the materials used in dyeing, under the Works Contracts Act.

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36. […]In the present case, due to the chemical reaction of colours, chemicals and dyes, the inherent property in those goods are passed on to the fabrics. The fact that after the inherent property in those goods is transferred to the fabrics the remaining solution is thrown out as waste or affluent, does not in any way affect the taxability on transfer of the property in goods already effected on the fabrics. Admittedly, after dyeing, the solution made of colours, chemicals and dyes is thrown as waste, because, on transfer of the property in the form of coloured shade, the said solution becomes worthless. Therefore, the Legislature has sought to tax the property in goods which passes and not the remnants or the affluent that remain after the passing of the inherent property in those goods.

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39. Now, turning to the second question, the Tribunal has held that the coloured shade passed on to the fabrics represents very small quantity of the materials used in dyeing and hence the Works Contracts Act is not applicable. As rightly contended by the counsel for the Revenue, under the Works Contract Act, what is relevant is the passing of property in goods used in the execution of the works contract and not the quantity of the material that passes. It is not the case of the respondents that the chemical solution used for dyeing retains its property even after dyeing. In fact, it is the specific case of the respondents that the solution prepared for dyeing the grey fabrics of one customer, cannot be used for dyeing the grey fabrics of another customer. It is the case of the respondents that on completion of dyeing, of a particular fabric, the chemical solution becomes worthless and is thrown as a waste. Therefore, it is clear that on completion of dyeing, the entire property of the materials used in dyeing are passed on and what remains as solution is nothing but the residue or the waste. In other words,

> *the coloured shade on the fabrics represents the entire property of the materials used in dyeing. Therefore, it was not open to the Tribunal to hold that the coloured shade represents only very small quantity of the materials used for dyeing and, therefore, the Act is not applicable[…]"*
>
> (Emphasis supplied)

Thus, the Bombay High Court interpreted the meaning of the phrase "*some other form*" to include the transfer of goods not just in their physical form but also in other forms, such as in their chemical form. Having regard to the facts at hand, the High Court held that the inherent property in the colours, dyes and chemicals could be said to have been transferred in their chemical form to the cloth which was being dyed.

43. In ***Teaktex Processing Complex Limited v. State of Kerala,*** reported in **2002 SCC OnLine Ker 720**, the Kerala High Court addressed a similar question, i.e., whether dyes and chemicals used in the process of dyeing should be considered as consumables under Section 5C of the Kerala General Sales Tax Act, 1963. The Kerala High Court held that the 'dye' used in the process cannot be treated as a consumable. According to the High Court, if an item which is used in the process is not in existence in any form in the end-product, then it is to be treated as a consumable. Since the dyes used existed in the form of colour, the High Court held that it was inevitable that the property in them was transferred.

44. In ***Hari and Company*** (*supra*), the respondent-assessee was engaged in the business of photocopying, and for this purpose, it used its own paper and ink. The question before the Bombay High Court was whether the paper and ink used by the respondent-assessee in the course of executing photocopying works would

constitute a transfer of property, and thus be liable to the levy of tax under the Maharashtra Works Contracts Act. The Bombay High Court, relying on its own decision in ***Matushree*** (*supra*), held that the moment paper and ink changed hands, it could be construed as a sale within the works contract.

45. In ***Commissioner of Sales Tax, Maharashtra State, Bombay v. Ramdas Sobhraj***, reported in **2012 SCC OnLine Bom 1608**, a reference was made by the Maharashtra Sales Tax Tribunal to the Bombay High Court. The respondent-assessee was engaged in the works of plate and film making. The activities undertaken by the respondent-assessee are described as follows by the Bombay High Court:

> *"In the job-work of plate making the customers of the respondent-assessee supplies to the respondent-assessee duly grained zinc or aluminium plates. On receipt, plates are coated by dipping in water wherein gun bio chromate is dissolved. Thereafter positives are exposed on the treated plates by halogen lamps. The image is formed by the positives on the plates and the same is developed in the solution of calcium, lactic acid ferric chloride, cupric chloride and hydrochloride. The plates are thereafter washed in industrial solvent, as a result of which all the chemicals are washed out and only the images remain on the plates. Thereafter, lacquer and ink are applied on the plates. On a specific query, we were informed that lacquer and ink are applied on the plates so as to ensure that the images on the plates do not get disturbed/smudged by constant use. After the above process the plates are dried and again washed with water and returned to the customers.*
>
> *The activity of pure labour job consists of positive making. In this activity, the customer supplies a design to the respondent-assessee for the purpose of positive making. The respondent-assessee thereafter takes a photograph of the design in four different colours, i.e., yellow, red, blue and black for obtaining the final*

negatives. Out of the aforesaid final negatives the respondent-assessee obtains/prepares a number of positives as required by its customers. It is the case of the respondent-assessee that the aforesaid activity is highly skilled activity requiring expertise and skill."

The question that fell for consideration before the Bombay High Court was whether the tribunal was justified in holding that there was no transfer of property in ink and lacquer when undertaking the works in the post Forty-sixth Amendment era. The Bombay High Court, relying upon its decision in ***Matushree*** (*supra*), held that lacquer and ink were materials used in the plate making process, and the property in the same is passed on in the execution of the contract under the Maharashtra Works Contracts Act.

46. In ***M/s Mohan Offset Printers v. State of Tamil Nadu***, reported in **2010 SCC OnLine Mad 587**, the petitioner-assessee was engaged in the business of printing and supplying labels, cartons and drapers for notebooks on a work contract basis. While the paper was supplied by the customers, the printing ink was prepared by the petitioner-assessee. The petitioner in the said case sought to challenge the tribunal's decision, which held that the printing ink used by the petitioner in the works contract would amount to a transfer of property, and thus was liable to sales tax under Section 3B of the Tamil Nadu General Sales Tax Act, 1959. Section 3B of the Tamil Nadu General Sales Tax Act, 1959 dealt with "*levy of tax on the transfer of goods involved in works contract*". It was the petitioner's contention that when ink is used for printing the materials on a work contract basis, such ink is consumed and no transfer of property in the ink occurs. Rejecting the contention of the petitioner, the Madras High Court held that in the printing work undertaken, the ink is transferred onto the

papers in a tangible manner and without it, the works contract would not be completed. Therefore, the printing ink could not be considered a consumable and is liable to be taxed under Section 3B of the Tamil Nadu General Sales Tax Act, 1959.

47. In ***Unique Traders v. Commercial Tax Officer-1***, reported in **2020 SCC OnLine Mad 1155**, a Three-judge Bench of the Madras High Court was hearing a reference that originated when a Division Bench, noting conflicting decisions among other Division Benches of the High Court, deemed it necessary for the law on the subject to be settled. The appellant in this case was involved in performing job work, wherein it would receive polythene rolls from various parties and thereafter print on them using purchased ethyl acetate, toluene, and ink. The question before the court was whether the ink used in printing would amount to a transfer of property and thus be liable to tax under Section 3B of the Tamil Nadu General Sales Tax Act, 1959. In resolving this issue, the Three-judge Bench extensively examined the various precedents of this Court, its own decisions, and those of other High Courts. The court answered the reference in favour of the revenue and held that the ink used in printing would be liable to be taxed under Section 3B of the Tamil Nadu General Sales Tax Act, 1959. In addition, the court in the case also delineated very clearly as to which precedents of its High Court on this aspect of law were binding and which were erroneous in law.

48. The issue before this Court in ***Xerox Modicorp Ltd v. State of Karnataka***, reported in **(2005) 7 SCC 380**, was whether toners and developers supplied in pursuance of maintenance contracts entered into between the parties were subject to the levy of sales tax. It was the contention of the appellant-assessee therein that

the toners and developers are consumed in the process of the execution of the maintenance agreement itself, and by virtue of Explanation I to Rule 6(4) of the Karnataka Sales Tax Rules, such consumables could not be made subject to the levy of sales tax. Rejecting this contention, this Court held as follows:

> *"16. We have considered the rival submissions. As set out hereinabove the word consumable in Explanation I to Rule 6(4) refers to such items which get consumed before the property in the goods can pass. We are informed that toners and developers are liquids which are put in the Xerox machine. They perform, to put it simply, the same function as ink in printers. Under the Sale of Goods Act if specified goods in a deliverable state are delivered the property in the goods passes. It could not be disputed that the toner and developer will be delivered in bottles/containers. In FSMA supplies are left with the customer. Thus clause 9 of the section dealing with the customer's obligation provides as follows:*
>
> > *"The Customer*
> > ***
> > *9. shall be accountable to MX for xerographic supplies stock left in trust with the customer who shall ensure that such stock is used only in the equipment under this agreement. MX reserves the right to charge the customer for any stocks which are unaccounted for, to MX's satisfaction, at the then prevailing MX prices."*
>
> *Thus for the extra stock there is a provision which provides that it is left in trust. However once the toner and developer are put into the machine they are no longer in trust. <u>This is because the property in the toner and developer passed the moment they are put into the Xerox machine. Now they belonged to the customer. At this stage they are tangible movables in which property can pass. This is clear from the provision that the appellants will charge for unaccounted stock at prevailing prices. That they are goods in which property can pass is also clear from the fact that in SSMA the customer has to buy the toner and developer. If as now claimed they are consumables in which property cannot be transferred how are the appellants charging for toners and developers. In our view, Mr Iyer</u>*

is right. The sale i.e. transfer of property takes place before the goods are consumed. The transfer takes place in respect of tangible goods. Just like petrol is consumed after sale or ink is consumed after sale in this case also the toners and developers get consumed after sale. The property passes the moment they are put in the machine. At that stage they are not consumed but are tangible goods in which property can pass."

(Emphasis supplied)

49. In the aforementioned cases, the Courts were primarily dealing with situations where the transfer of property resulted in a tangible and observable presence in the final product. The judicial reasoning focused on how the inherent properties of the goods were physically incorporated and remained as a component of the works delivered to the customer.

b. No transfer of property due to consumption of goods

50. In ***Pest Control*** (*supra*), the petitioner was engaged in providing services such as pest control, household disinfection, and anti-termite treatment. The question before the Patna High Court was whether there was a transfer of property in the chemicals that were involved in providing the aforementioned services. The court upheld the contention of the petitioner that there was no transfer of property in the chemicals and held as follows:

> *"12. From the plain reading of sub-clause (b) of clause (29-A) of article 366 of the Constitution of India it appears that there must be a transfer of property in goods whether as goods or in some other form involved in the execution of a works contract. Clause (12) of article 366 and section 2(h) of the Bihar Finance Act, 1981 give some indication as to what is meant by "goods". The inclusive definition in the Constitution as well as in the Bihar Finance Act refers to materials, commodities and articles or all kinds of movable property, all materials, commodities and articles, as such or in some other form. Before a tax can be levied*

on a works contract, it must be established that there is transfer of property in goods involved in the execution of a works contract. The goods may have undergone a change of form. But in whatever form, there must be transfer of property in goods. This presupposes that the goods existed and that either in its original form or in some other form, it is transferred to the principal by the contractor. If the goods do not exist in any form whatsoever and are consumed in the processor execution of the work, can it be said that in such a case there is a transfer of property in goods? In my view, the transfer of goods implies the existence of the goods in some form or the other. If the goods do not exist, there is no question of transfer of property in goods. In Northern India Caterers (India) Ltd. v. Lt. Governor of Delhi [1978] 42 STC 386 ; (1978) 1 SCR 557, the Supreme Court quoted with approval a passage from Electa B. Merrill v. James W. Hodson LRA 1915-B 481, dealing with a case of supply of food or drink to customers, wherein it was held that such supply did not partake the character of a sale of goods. It was observed: "The necessary incident of this service or ministry is the consumption of the food required. This consumption involves destruction and nothing remains of what is consumed to which the right of property can be said to attach. Before consumption title does not pass; after consumption there remains nothing to become the subject of title."

13. While it is true that in view of the Constitution (Forty-sixth Amendment) Act, 1982, what was earlier considered to be one indivisible contract is by legal fiction altered into a contract which is divisible into one for the sale of goods and the other for supply of labour and services. It is now possible for the State to levy sales tax on the value of goods involved in a works contract. But even so this presupposes the existence of goods, because there can be no transfer of property in goods unless the goods themselves exist. In the instant case, it is not disputed that the chemicals are used for the purpose of eradicating pests. The chemicals are sprayed through machines so that when the process ends, nothing tangible remains in which property is transferred. By the process of spraying or applying chemicals, a place is treated against insects and pests

but in the process the chemicals are themselves consumed and there remains nothing in which property is transferred. I am of the view that a transaction as the one in question really does not involve transfer of any goods as understood in sub-clause (b) of clause (29-A) of article 366 of the Constitution of India or under the provisions of the Bihar Finance Act, 1981. It is a service contract pure and simple and does not involve any sale of goods since there are no goods in which property can be transferred. I am, therefore, of the view that the contract between the petitioner-company and M/s. Tata Iron & Steel Co. Ltd. is a mere service contract for eradication of pests, rodents, termites, etc., and does not fall within the purview of a contract for the supply of goods as envisaged under the Constitution of India and the Bihar Finance Act, 1981. In such a transaction, there being no transfer of property in goods, no sales tax is leviable under the provisions of the Bihar Finance Act, 1981."

(Emphasis supplied)

51. The Kerala High Court in ***M.K. Velu*** (*supra*) dealt with whether sales tax could be levied on the fireworks used in execution of a contract for fireworks display. Holding in the negative, the court held as follows:

"*4. […]The only further question is whether the Appellate Tribunal was justified in holding that no transfer of property takes place in the display of fireworks. As the explosives are consumed, nothing tangible remains, in which property could be transferred. It is a matter of common knowledge that in the display of fireworks, the explosives are spent and do not remain, once the display takes place. In the process of execution of the work, the goods themselves (explosives) ceased to exist. No tangible property remains. So, there could be no transfer of property. We concur with the decision of the Patna High Court in Pest Control India Ltd. v. Union of India [1989] 75 STC 188. There can be no transfer of property unless the goods themselves exist. That is not the case herein. The*

decision of the Appellate Tribunal taking the said view is justified in law."

(Emphasis supplied)

52. In ***Dynamic Industrial and Cleaning Services (P) Ltd. v. State of Kerala & Anr***, reported in **1994 SCC OnLine Ker 379**, the petitioner company was engaged in the business of cleaning of boilers in plants like thermal power stations and fertiliser complexes. For the process of cleaning, the petitioner used chemicals like citric acid, hydrochloric acid and the like, after determining the precise type of cleaning agent to be used in a particular plant. The petitioner, being aggrieved by the levy of sales tax on these chemicals, contended that the chemicals are consumed in the process of cleaning and removing the impurities in the plants, and as such no transfer of goods was involved. Accepting the said contention, the Kerala High Court held as follows:

"2. A bare perusal of the above Explanation is sufficient to show that transfer of property in goods (whether as goods or in some other form) is the sine qua non for its application. The mere execution of a works contract does not by itself attract liability for tax under the Act unless it is accompanied by transfer of property in goods, involved in the execution of the contract. The emphasis is on the transfer of property in goods-Builders Association of India v. Union of India [1989] 73 STC 370 (SC) at page 396. <u>When goods used in the process of executing a works contract are consumed in the process, as in the case of the chemicals used by the petitioner or fuel and power, there is no transfer of any goods from the contractor to the awarder of the contract, attracting liability to tax.</u> I draw inspiration for this conclusion from the decision of this Court in Deputy Commissioner of Sales Tax v. Thomas Stephen and Co. Ltd. [1987] 66 STC 34 ; (1987) 1 KLT 161, (paragraph 5) which was affirmed by the Supreme Court in Deputy Commissioner v.

Thomas Stephen & Co. Ltd. [1988] 69 STC 320 (at pages 324-325); (1988) 1 KLT 568 (paragraph 12).

3. The chemicals are being used by the petitioner only in aid of the work undertaken by it, as a cleaning agent for cleaning the boilers in the plant and they are extinguished in the process. They are not transferred to the awarder in any form, either as goods or otherwise. The work is more or less a labour contract, in which the petitioner utilises the chemicals just as it uses any other item of its machinery or fuel or power in the performance of the work. There is no transfer of property in goods and no sale liable for tax under Explanation 3(A)."

(Emphasis supplied)

53. In ***Microtol Sterilization Services Pvt Ltd v. State of Kerala*** reported in **2009 SCC OnLine Ker 1480** the question before the Kerala High Court was whether there was any transfer of property in ethylene oxide, which was used in the process of sterilization of goods. The Court held as follows:

"5. Besides the above, section 5C(1)(c)(iii) provides for cost of consumables used in the execution of works contract eligible for deduction in the determination of taxable turnover on works contract. It is obvious from the section and the provisions providing for determination of taxable turnover on works contract that sales tax is payable only on the value of goods that got transferred from the contractor in the execution of the works contract. Consumables are items which are lost in the course of execution of works contract. Even though consumables are lost to the contractor, it is not a gain for the awarder. In other words, they are used up in the process of executing the work. Sterilisation is a process by which goods are made free of germs and in order to retain the quality of goods, only packed commodities are subject to sterilisation with the use of ethylene oxide. The assessee's representative present in court explained the sterilisation process as one involving the use of a compact airtight room wherein the goods to be sterilised in packed form are exposed to ethylene oxide for around six hours and then the said gas is allowed to escape after mixing

with carbon dioxide at higher levels through chimney. Ethylene oxide is a toxic gas which is highly inflammable. After the duration of sterilisation, the gas is released to air after neutralising it with carbon-dioxide. Admittedly after sterilisation goods do not retain any trace of ethylene oxide which is completely released in the air. Therefore, there is no transfer of ethylene oxide from the assessee to the customers in the course of sterilisation of the goods. On the other hand, it is used up as a consumable in the service rendered by the assessee, the value of which is to be excluded in the determination of taxable turnover of works contract under section 5C of the Act. The decision of the Patna High Court in the case of application of pesticide and the other decisions of this court in the case of fireworks squarely apply to the facts of this case. The decisions cited by the Government Pleader will not apply to this case because those are cases involving dyeing work where the dye is transferred to the fabric supplied by the customer and is retained in the cloth. We are therefore unable to uphold the order of the Tribunal confirming the levy and demand of tax on the value of ethylene oxide used up in sterilisation work. We therefore allow the sales tax revision by reversing the order of the Tribunal confirming the assessment and by declaring that no tax is leviable on the value of ethylene oxide used in sterilisation work."

(Emphasis supplied)

54. In the cases of ***Pest Control*** (*supra*), ***M.K. Velu*** (*supra*), ***Dynamic Cleaning*** (*supra*) *and* ***Microtol Sterilization*** (*supra*) respectively, the overwhelming focus of the courts was on the continued existence of the good as a prerequisite for a transfer of property. The courts in these cases operated on the notion that if the goods are completely consumed or disappear during the execution of the works, leaving no physical trace in the final product, then no transfer can logically occur. Since a third party does not receive the goods themselves in any form, the transaction is purely one of service, and the material used is merely a consumable whose property is extinguished rather than transferred.

c. Transfer of property despite consumption of goods

55. In ***Enviro Chemicals v. State of Kerala***, reported in **2011 SCC OnLine Ker 3685**, the petitioner was engaged in providing a service of chemical treatment of effluent water. For the purpose of treating the effluent water, the petitioner used "envirofloc", a chemical product developed by it. Envirofloc was consumed during the treatment of the effluent water. In such circumstances, the question before the Three-judge Bench of the Kerala High Court was whether to treat envirofloc as a consumable and exempt it from the levy of sales tax under the Kerala General Sales Tax Act, 1963. The contention of the petitioner in the said case was that since the chemical was consumed and used up, there was no transfer of property. On the other hand, the revenue contended that the chemical was transferred the moment it was put into the effluent water, and the fact that it was subsequently consumed would not absolve the petitioner of its liability to pay tax as there was transfer of property. By a 2:1 majority, the court accepted the contention of the revenue. Justice K.M. Joseph (as His Lordship then was), speaking for the majority, made the following pertinent observations:

> *"32. That the chemical in question is goods, is beyond doubt. It cannot be disputed that the assessee was the owner of the goods in question, namely, the chemical. It is obviously the intention of the parties that the assessee must use the chemical in the effluent treatment process. It is equally indisputable that the assessee has actually used it. No doubt, in the judgment of the apex court in Xerox Modicorp Ltd. v. State of Karnataka [2005] 142 STC 209, the apex court found that the toners and developers are liquids put into the xerox machine and they perform essentially the same function as ink in the printers and the court also relied on the provision in the contract that the assessees in the said case would charge for the unaccounted stock at prevailing prices. By using the chemical, the petitioner/assessee rendered the effluent*

compliant with the standards. It could probably be said that in the case of the toner and developers as the function is that of ink in printers, it shows up in the final product of the xerox machines. But, the decision of the apex court is not based on there being any requirement that the items which are used should exist in any form in the resultant product which is the principle laid down by this court in Teaktex Processing Complex Limited v. State of Kerala [2004] 136 STC 435 and also in Microtrol Sterilization Services Pvt. Ltd. v. State of Kerala [2009] 26 VST 213 (Ker).

33. We would think that the principle "quicquid plantatur solo, solo cedit" is a principle which is apposite in the context of a building and engineering contract. We get the following account of the principle "quicquid plantatur solo, solo cedit":

> *"The well-known principle is that the property in all materials and fittings, once incorporated in or affixed to a building, will pass to the free-holder quicquid plantatur solo, solo cedit. As soon as materials of any description are used in a building or other erection, they cease to be the contractor's property and become that of the free-holder. The employer under a building contract may not necessarily be the free- holder, but may be a lessee or licensee, or even have no interest in the land at all, as in the case of a sub-contract. However, once the builder has affixed materials, the property in them passes from him, and at least as against him, they become the absolute property of his employer, whatever the latter's tenure of or title to the lands. The builder has no right to detach them from the soil or building, even though the building owner may himself be entitled to sever them as against some other person—for example, tenant's fixtures. Nor can the builder reclaim them if the building owner or anyone else has subsequently severed from the soil.*
>
> *Materials worked by one, into the property of another, becomes part of that property. This is equally true whether it be fixed or moveable property. Bricks built into a wall becomes part of the house, thread stitched into a coat which is under repair, or planks and nails and pitch worked into a ship under repair, become part of the coat or the ship. Until, however, the materials are actually built into the work, in the absence of some*

stipulation intended to pass the property in them, when delivered on the site, they remain the property of the contractor, notwithstanding that they might have been approved by the employer or his agent or brought into the site unless the agreement between the parties evinces a clear intention to the contrary."

34. We would think that the said principle as such may not advance the case of the Revenue in a case where the works contract involves the effluent treatment process wherein chemical is poured into the effluent.

35. When the assessee has used it, will it remain the owner of the chemical any longer? Will not the property in the goods pass to the awarder? We would think that the moment the assessee pours the chemicals into the effluent, he will cease to be the owner and at that point of time the awarder must be deemed to have taken delivery of the same. In our view the fact that upon it being poured into the effluent, it loses its identity and that it is consumed will not detract from the fact that there is delivery of the same to the awarder. The assessee does not have a case that the effluent belongs to the assessee. We do not think that it can be their case that the effluent does not belong to the awarder. Let us pose a question, if a complaint by a third party is raised about the treated effluent, can the awarder absolve itself of the ownership of the same? We would think, it may not be possible. Therefore we would be justified in holding that the effluent and the treated effluent both belonged to the awarder. It is, therefore, into the property of the awarder, namely the effluent, that the assessee supplies the chemical. The apex court in its decision in Gannon Dunkerley & Co. v. State of Rajasthan [1993] 88 STC 204 ; (1993) 1 SCC 364 had, inter alia, held that cost of consumables, such as, water, electricity, fuel, etc., used in the execution of the works contract, the property in which is not transferred in the course of execution of a works contract, is to be deducted. In section 5C also, the words "not involving any transfer of property in goods" have been incorporated. Just like the toner and developer having been put into xerox machine becoming the property of the customer in the case before the apex court in Xerox Modicorp Ltd. case [2005] 142 STC 209 and the sale taking place before the goods are consumed, in the

same way, the property in the chemical passed to the awarder the moment they are put into the effluent by the assessee and its subsequent consumption is the consumption after sale and it does not detract from the factum of sale and consequently the exigibility to tax becomes unquestionable."

(Emphasis supplied)

56. In ***State of Tamil Nadu v. S.S.M. Processing Mills***, reported in **2013 SCC OnLine Mad 2539**, the issue before the Madras High Court was whether the chemicals used in the process of bleaching were liable to the levy of sales tax under Section 3B of the Tamil Nadu General Sales Tax Act, 1959. The court, relying on the Kerala High Court's decision in ***Enviro Chemicals*** (*supra*), answered in the affirmative. The relevant observation reads thus:

"9. The fact that the chemicals used for bleaching is washed away in the process, by itself, would not be a justifiable ground to accept the case of the assessee that there was no transfer of property of any goods. The very fact of the yarn being bleached by a chemical process, by applying the chemical, will clearly point out that there is transfer of property of the chemical, hence, bleaching contract attracts sales tax as in the case of dyeing contract, when the chemicals are purchased from outside the State. Consequently, this court allow the tax case (revisions) filed by the State."

(Emphasis supplied)

57. In the cases of ***Enviro Chemicals*** (*supra*) and ***S.S.M. Processing Mills*** (*supra*) respectively, the focus of the courts decisively shifted from the final existence of the good to the precise moment a transfer of property occurred. The Kerala High Court, in ***Enviro Chemicals*** (*supra*), held in the facts of that case that the transfer occurs the moment the chemical is poured into the effluent water. Its subsequent consumption does not negate the fact that a "deemed sale" has already taken place.

d. Application to the facts at hand

58. It is true that determining whether a transfer of property in goods has occurred is a fact-intensive enquiry, heavily dependent on the circumstances surrounding a particular case, such as the subject and terms of the work contract itself. In such a scenario, it is neither possible to lay down any "general principles" nor is it advisable to do so. At this juncture, it is apt to take note of the observations made by this Court in ***Collector of Central Excise, New Delhi v. Ballarpur Industries Limited***, reported in **(1989) 4 SCC 566**:

> *"18. Now a word about Shri Ganguly's insistence on drawing a line of strict demarcation between what can be said to be "goods" merely "used" in the manufacture and what constitute goods used as "raw material" for the purpose.*
>
> *19. We are afraid, in the infinite variety of ways in which these problems present themselves it is neither necessary nor wise to enunciate principles of any general validity intended to cover all cases. The matter must rest upon the facts of each case. Though in many cases it might be difficult to draw a line of demarcation, it is easy to discern on which side of the borderline a particular case falls.*
>
> *20. Shri Ganguly's insistence, however, serves to recall the pertinent observations of an eminent author on the point. It was said:*
>
> > *"A common form of argument used by counsel in legal cases is to suggest that if the court decides in favour of the opposing counsel's arguments, it will become necessary to draw lines which may be very difficult or impossible to draw. "Where will you draw the line?" is, of course, a question which must be faced by a legislator who is actually proposing to lay down lines for all future cases, but it is not a question which needs in general to be faced by common law courts who proceed in slow stages, moving from case to case…"*

The learned Author recalls Lord Lindley's "robust answer" to the question — Where will you draw the line?

> *"Nothing is more common in life than to be unable to draw the line between two things. Who can draw the line between plants and animals? And yet, who has any difficulty in saying that an oak-tree is a plant and not an animal?"*

Again, Lord Coleridge in Mayor of Southport v. Morriss said:

> *"The Attorney General has asked where we are to draw the line. The answer is that it is not necessary to draw it at any precise point. It is enough for us to say that the present case is on the right side of any reasonable line that could be drawn."*

(Emphasis supplied)

59. Whilst acknowledging that there are no general rules that can be universally applied, it is fundamental that any analysis must begin with the correct identification of the taxable event. From the rulings of this Court in ***Builders Association*** (*supra*), ***Gannon Dunkerley-II*** (*supra*) and ***Larsen and Toubro*** (*supra*) respectively, it is clear that the taxable event with respect to the transfer of property in goods involved in works contracts is when the deemed sale occurs.

60. In ***Gannon Dunkerley-II*** (*supra*), this Court clarified that *the transfer of property in such goods takes place when the goods are incorporated in the works.* The Court's use of the word 'incorporated' should not be mechanically interpreted to mean that a transfer of property occurs only when a physical or tangible good is passed on when executing a works contract. Rather, 'incorporation' is to be understood contextually, defined by the specific nature of "the works" contracted for.

61. Considering it from the aforesaid perspective, it is evident that the Courts in ***Pest Control*** (*supra*), ***M.K. Velu*** (*supra*), ***Dynamic***

Cleaning (*supra*) and ***Microtol Sterilization*** (*supra*) respectively, proceeded on the wrong footing. The emphasis of the courts on 'consumption' in the aforesaid cases is incorrect on the following grounds:

a. *First*, the courts in the said cases completely overlooked the taxable event as prescribed under Article 366(29A)(b) and the relevant statute. The focal point of analysis by the courts should have been not whether the *goods have been consumed*, but rather whether the *transfer of property* has occurred. However, the courts wrongly presumed that the transfer could not have occurred as the goods had already been consumed.

b. *Secondly*, the courts in the said cases proceeded on the incorrect assumption that all "consumables" were deductible and exempt from the levy of tax. However, on reading the observations of this Court in ***Gannon Dunkerley-II*** (*supra*) and the relevant statutory provisions, it is amply clear that only those consumables were exempt from tax, the property in which was not transferred in the execution of the works contract. Thus, if the transfer of property has occurred, and thereafter the goods are consumed, it would still be liable to the levy of sales tax. The position is the same even under the Act, 1948.

62. This Court in ***Xerox Modicorp*** (*supra*) and the Kerala High Court in ***Enviro Chemicals*** (*supra*) correctly identified the taxable event as the precise moment the contractor's goods are incorporated into the 'works', i.e., when the toner is fitted into the machine or the chemical is introduced into the effluent water. The subsequent consumption of these items is irrelevant, as it does not negate the transfer of property that has already occurred. The cardinal principle, which must serve as the guiding light for any court or

tribunal adjudicating such disputes, is that the analysis must be anchored to a singular question: has transfer of property in goods involved in the execution of the works contract occurred?

63. In ***Enviro Chemicals*** (*supra*), the Kerala High Court correctly noted that the items need not exist in any form in the resultant product. To insist that a transfer of property is contingent upon the good's tangible presence in a final product is to impose a condition that Article 366(29A)(b) does not contemplate and, in fact, is textually contradictory. The statutory framework only requires that the goods be "*involved in the execution of the works contract*". It does not mandate that the works contract must yield a physical end-product or that the transfer must be tangible. To impose such a limitation would not only lead to a gross misapplication of the law but would also defeat the legislative intent of the Forty-sixth Amendment and the dictum of this Court in various rulings. This Court allowed a broad interpretation of the term 'works contract' in order to enable the taxing transfer of property in goods in *all genres* of works contracts.

64. Many works contracts, particularly those for services and transformations, do not result in a new end product or a tangible transfer of property. For example, a works contract for providing pest control or cleaning service (as was the case in ***Pest Control*** (*supra*) and ***Dynamic Cleaning*** (*supra*), respectively) would not lead to the creation of a new end product or a very tangible transfer of property in goods. However, the chemicals used are indeed being transferred, as without such transfer of goods, it would be impossible to make an area clean or pest-free. Similarly, in ***M.K. Velu*** (*supra*) *and* ***Microtol Sterilization*** (*supra*), the works contracts therein could not have been executed successfully

without the transfer of property in the fireworks and ethylene oxide, respectively. The chemicals, fireworks, and ethylene oxide are the primary goods *facilitating* the works under the respective contracts. It is in this context that they may said to be incorporated in the 'works' of the respective contracts. Consequently, it is undeniable that the property in such goods is being transferred when the respective works contracts are executed. These goods differ from consumables such as water and electricity, which merely *aid* in executing works contracts and the property in them is not transferred before they are consumed.

65. Determining whether a transfer of property in goods has occurred is undoubtedly more challenging when the good is consumed or the transfer is intangible, as opposed to when it is tangibly present in a final product. Thus, the courts and tribunals must be extra vigilant when faced with such scenarios and must scrutinize the specific facts and the nature of each works contract with great care to make a correct determination as to whether or not a said item has been incorporated in the 'works' of a contract.

66. In the facts of the present case, the levy of sales tax under Section 3F of the Act, 1948, is on the ink and the processing material used by the appellant in printing the lottery tickets. The appellant has, however, not provided an item-wise breakdown of such processing material. The same was also noted by the Assessing Authority in its orders dated 28.10.1999. If the appellant had provided an item-wise breakdown, it would have facilitated in determining whether there was a transfer of property with regard to each such item. Consequently, we proceed to determine the issue on the basis of the assumption the High Court seems to have drawn in its impugned

judgment, i.e., equating processing material with the chemical used for diluting the ink.

67. Applying the principles laid down in the preceding paragraphs to the facts at hand, we have no doubt in our mind that there is a transfer of property in the ink and chemicals used in the printing of the lottery tickets. The works contract in this instance is for the printing of lottery tickets, and "the works" refers to the final, tangible printed ticket. The taxable event, or the "deemed sale", occurs at the precise moment the ink is applied to the paper. This act constitutes "incorporation in the works", as the ink and the chemicals (with which the ink is mixed) are involved in the execution of the work contract and become a part of the lottery ticket. In this process, there is a tangible transfer of the diluted ink, a composite good comprising both the ink and the processing chemicals.

68. As rightly held by the Bombay High Court in ***Matushree*** (*supra*), the transfer of ink and chemicals in their chemically altered form constitutes a valid transfer of property. Therefore, since it is impossible to transfer the ink without also transferring the chemicals it is diluted with, it can be conclusively inferred that the property in both the ink and the chemicals has been transferred.

69. Thus, in the facts of the present case, all conditions required to sustain a levy of tax under Section 3F(1)(b) of the Act, 1948, are fulfilled. Consequently, the appellant is liable to pay tax under Section 3F(1)(b) of the Act, 1948 on the ink and processing material.

E. CONCLUSION

70. In order to sustain a levy of tax under Section 3F(1)(b) of the Act, 1948, three conditions must be fulfilled: (i) there must be a works

contract; (ii) the goods should have been involved in the execution of the works contract; and (iii) the property in those goods must be transferred to a third party either as goods or in some other form.

71. The appellant has admitted that the contract for printing lottery tickets is a works contract. Based on the judgments of this Court, it cannot be said otherwise as well. From the record, it is clear that the ink, chemical and other processing material were involved in the printing of the lottery tickets.

72. Further, there is a transfer of property in the ink and chemicals used in the printing of the lottery tickets. The works contract in this instance is for the printing of lottery tickets, and "the works" refers to the final, tangible printed ticket. The taxable event, or the "deemed sale", occurs at the precise moment the ink is applied to the paper. This act constitutes "incorporation in the works", as the ink and the chemicals (with which the ink is mixed) are involved in the execution of the work contract and become a part of the lottery ticket. In this process, there is a tangible transfer of the diluted ink, a composite good comprising both the ink and the processing chemicals.

73. Thus, in the facts of the present case all three conditions required to sustain a levy of tax under Section 3F(1)(b) of the Act, 1948, are fulfilled : (i) a works contract exists for printing of lottery tickets; (ii) ink and chemicals have been involved in the execution of the works contract; and (iii) the property in the ink and chemicals has been transferred in execution of the works contract. Consequently, the appellant is liable to pay tax under Section 3F(1)(b) of the Act, 1948 on the ink and processing material.

74. For the foregoing reasons, the appeals fail and are hereby dismissed.

75. Before we close, we must clarify that we had heard in all four appeals. This judgment disposes of Civil Appeal Nos. 703 & 705 of 2012 respectively. In so far as, the Civil Appeal Nos. 9189 & 8313 of 2015 respectively are concerned, we order that they be de-tagged as we need to rehear them on a particular issue. Registry to notify these two appeals for rehearing on any final hearing day in the month of November 2025.

..... J.
(J.B. PARDIWALA)

..... J.
(K.V.VISWANATHAN)

New Delhi.
October 07, 2025.