State Of Andhra Pradesh vs M/S Kone Elevators (India) Ltd on 17 February, 2005

Equivalent citations: AIR 2005 SUPREME COURT 1581, 2005 (3) SCC 389, 2005 AIR SCW 1222, 2005 (2) SLT 679, (2005) 2 JT 314 (SC), 2005 (2) JT 314, 2005 (2) SCALE 178, (2005) 28 ALLINDCAS 467 (SC), (2005) 2 CTC 134 (SC), (2005) 181 ELT 156, (2005) 123 ECR 189, (2005) 140 STC 22, (2005) 2 SCALE 178, (2005) 3 MAD LJ 40, (2005) 3 SCJ 176, (2005) 59 KANTLJ(TRIB) 23, (2005) 3 SUPREME 85

Bench: S.N. Variava, Ar. Lakshmanan, S.H. Kapadia

CASE NO.:
Appeal (civil) 6585 of 1999

PETITIONER:
State of Andhra Pradesh

RESPONDENT:
M/s Kone Elevators (India) Ltd.

DATE OF JUDGMENT: 17/02/2005

BENCH:
S.N. VARIAVA,Dr. AR. LAKSHMANAN & S.H. KAPADIA

JUDGMENT:

J U D G M E N T KAPADIA, J.

The question involved in this civil appeal filed by the department is whether contracts entered into and executed by the assessee were contracts for sale and not works-contract.

M/s Kone Elevators (India) Ltd. (hereinafter referred to as "the assessee") is a unit of M/s Kone Corporation, Finland who are one of the pioneers in the manufacture of Hi-tech New Generation Elevators in the world. M/s Kone Corporation, Finland has its operations spread over 37 countries in the world. The assessee herein is a registered dealer falling in the jurisdiction of the Commercial Tax Officer, R.P. Road Circle, Secunderabad, having its head office at 50, Vanagaram Road, Aynambakkam, Madras, with branches at Vijaywada and Vizag. The assessee filed monthly returns in form A-2 for the months of April and May, 1995. It was assessed by the said Commercial Tax Officer provisionally for the period 1.4.1995 to 31.5.1995 and for the period from 1.6.1995 to 31.7.1995 under the Andhra Pradesh General Sales Tax Act, 1957 (hereinafter referred to for the sake of brevity as "the 1957 Act"). The said two provisional assessments were made by the Commercial Tax Officer vide orders dated 19.8.1995 and 5.9.1995 respectively. The assessee claimed deductions

of labour charges for composition of tax under section 5G read with section 5F of the said Act saying that nature of the work undertaken by it constituted "works-contract" involving manufacture, supply, installation and commissioning of elevators and lifts. The assessing authority however did not allow the deduction sought for and passed the provisional assessment orders giving rise to two appeals against the said assessment orders. By judgment and order dated 9.10.1995, the Deputy Commissioner, Secunderabad Division, Hyderabad, in turn dismissed the appeals filed by the assessee and thereby confirmed the aforestated assessment orders. Both the lower authorities treated the disputed turnover of the assessee as falling under Entry 82 of the First Schedule to the said 1957 Act, which was objected to by the assessee by filing two separate appeals bearing T.A. Nos.676 and 677 of 1995 before the Sales Tax Appellate Tribunal, Hyderabad. The point that arose before the Tribunal in the aforestated two appeals, heard and disposed of jointly, was whether the transactions related to "works-contract" or to "sale" of lifts. By judgment and order dated 22.12.1995, the said appeals bearing T.A. Nos.676 and 677 of 1995 were allowed in favour of the assessee setting aside the impugned orders of the lower authorities by holding that the disputed turnover related to the manufacture, supply, fabrication and erection involved in the works-contract and that the said transaction did not amount to a contract of sale. The original assessing authority was accordingly directed to allow the deduction of labour charges and to complete the assessment under section 5G read with section 5F of the 1957 Act, as amended, without treating it under Entry 82 of the first schedule to the Act. Aggrieved by the decision of the Tribunal dated 22.12.1995, the department preferred Tax Revision Case no.129 of 1999 under section 22(1) of the 1957 Act, to the High Court. By impugned judgment and order dated 2.7.1999, the Tax Revision Case filed by the department was dismissed. Hence, this civil appeal.

Shri Debojit Borkakati, learned counsel for the department submitted that the main object of the contract in question was to sell the lifts and the works done by the assessee for installation was incidental to the sale of lifts. It was urged that the Legislature had classified the commodity "lift" under Entry 82 of the first schedule to the Act keeping in mind that the word "installation" was ancillary to the "sale" of lifts. It was urged that the High Court had erred in holding that the installation of the lift involved skill and technical know-how, which was to be treated as works-contract.

Shri M.N. Rao, learned senior counsel for the assessee, on the other hand, submitted that the assessee was engaged in the manufacture, supply, erection, installation and commissioning of lifts by undertaking works-contract; that the lifts/elevators as such cannot be delivered to the customer; that various accessories and components were required to be taken to the site where after carrying out the civil work, lifts were installed and commissioned. It was further urged that only after all the parts stood assembled at site, the lifts came into being; that installation and commissioning of lifts involved skill and only after installation and commissioning of the lifts, the ownership stood transferred to the customer. Consequently, the assessee was entitled for deduction of labour charges and was entitled to composition of tax under section 5G of the said Act. It was urged that the assessing authority had erred in treating the transaction as a sale assessable to tax under Entry 82 of the first schedule to the said Act. It was further submitted on behalf of the assessee that manufacture, supply, erection, installation and commissioning of lift came under definition of the words "works-contract" under section 2(1)(t) of the said Act and, therefore, the tax leviable fell

under section 5F of the said Act. It was urged that lifts and elevators cannot be delivered like A/Cs as standard units; that manufacture, supply, erection, installation and commissioning of lifts involved skill and labour as well as technical know-how. Reliance was placed, in support of above contentions, on various invoices raised by the assessee for manufacture, supply, erection, installation and commissioning of lifts. Reliance was also placed on the copy of the contracts entered into by the assessee. Reliance was also placed on Indian Standards Institution's specifications and code of practice for installation of lifts and elevators to show the amount of skill, labour and technical know-how involved in the manufacture, supply, erection, installation and commissioning of lifts. In the circumstances, it was submitted that no interference was called for in this matter.

It can be treated as well settled that there is no standard formula by which one can distinguish a "contract for sale" from a "works-contract". The question is largely one of fact depending upon the terms of the contract including the nature of the obligations to be discharged thereunder and the surrounding circumstances. If the intention is to transfer for a price a chattel in which the transferee had no previous property, then the contract is a contract for sale. Ultimately, the true effect of an accretion made pursuant to a contract has to be judged not by artificial rules but from the intention of the parties to the contract. In a "contract of sale", the main object is the transfer of property and delivery of possession of the property, whereas the main object in a "contract for work" is not the transfer of the property but it is one for work and labour. Another test often to be applied to is : when and how the property of the dealer in such a transaction passes to the customer: is it by transfer at the time of delivery of the finished article as a chattel or by accession during the procession of work on fusion to the movable property of the customer? If it is the former, it is a "sale"; if it is the latter, it is a "works- contract". Therefore, in judging whether the contract is for a "sale" or for "work and labour", the essence of the contract or the reality of the transaction as a whole has to be taken into consideration. The pre-dominant object of the contract, the circumstances of the case and the custom of the trade provides a guide in deciding whether transaction is a "sale" or a "works- contract". Essentially, the question is of interpretation of the "contract". It is settled law that the substance and not the form of the contract is material in determining the nature of transaction. No definite rule can be formulated to determine the question as to whether a particular given contract is a contract for sale of goods or is a works-contract. Ultimately, the terms of a given contract would be determinative of the nature of the transaction, whether it is a "sale" or a "works-contract. Therefore, this question has to be ascertained on facts of each case, on proper construction of terms and conditions of the contract between the parties.

Before proceeding further, an insight into the relevant provisions more especially the definitions of "sale" and "works- contract" have to be noticed. Section 2(1)(n) which defines "sale" and section 2(1)(t) which defines the "works-contract"

> are extracted hereunder:
>
> "2(1)(n). 'Sale' with all its grammatical variations and cognate expressions means every transfer of the property in goods (whether as such goods or in any other form in pursuance of a contract or otherwise) by one person to another in the course of trade or business, for cash, or for deferred payment, or for any other valuable consideration

> or in the supply or distribution of goods by a society (including a co-operative society), club, firm or association to its members, but does not include a mortgage, hypothecation or pledge of, or a charge on goods.
>
> Explanation VI: Whenever any goods are supplied or used in the execution of a works contract, there shall be deemed to be a transfer of property in such goods, whether or not the value of the goods so supplied or used in the course of execution of such works contract is shown separately and whether or not the value of such goods or material can be separated from the contract for the service and the work done.
>
> 2(1)(t). 'Works Contract' includes any agreement for carrying out for cash or for deferred payment or for any other valuable consideration, the building construction, manufacture, processing, fabrication, erection, installation, fitting out, improvement, modification, repair or commissioning of any movable or immovable property."

We also quote hereinbelow Entry 82 of the First Schedule to the 1957 Act:

> Sl.
>
> No. Description of Goods Point of Levy Rate of Tax Effective from
>
> 82.

Lifts, electrical or hydraulic (1082) At the point of first sale in the State.

10 paise in the rupee 16 paise in the rupee 1.8.1986 1.4.1995 The bracketed words and the transactions brought within the purview of sale by the aforestated Explanation-VI appended to section 2(1)(n) are meant to cover non-conventional sale transactions which are now specified in Clause (29A) of Article 366 introduced by the Constitution 46th Amendment Act. Before the inclusive definition of the "tax on sale or purchase of goods" was introduced by the 46th Amendment, the expression "sale of goods" occurring in Entry 48 of List II of the Government of India Act was interpreted by this Court in the classical case of State of Madras v. Gannon Dunkerley & Co. (Madras) Ltd. reported in [AIR 1958 SC 560] as a term of well- recognized legal import in the general law and as mentioned in the Sale of Goods Act. The expression "sale of goods" in Entry 48 was described as "nomen juris", its essential ingredients being an agreement to sell movables for a price and property passing therein pursuant to that agreement. It was held that in a building contract which is composite and indivisible, there is no sale of goods as there could be no agreement to sell materials as such and moreover, the property does not pass as movables. In order to enlarge the concept of sale and to arm the State Legislatures with power to tax the transactions simulating sales but not conforming to the concept of sale under the Sale of Goods Act, clause (29A) was inserted in Article 366 by the 46th Constitutional Amendment. The Andhra Pradesh State Legislature fell in line with this amendment and changed the definition of "sale" so as to bring within the tax net the transactions which are not stricto sensu sales as per the law laid down in Gannon Dunkerley's case (supra). It is important to note that the 1957 Act ordains that transfer of

property in goods for valuable consideration must be "in the course of trade or business" [vide section 2(1)(n)]. This is because the incidence of tax falls on a dealer who "carries on the business of buying, selling, supplying or distributing goods" [vide section 2(1)(e)]. A sale by a person who carries on the business of buying, selling etc. and a sale in the course of business are the twin requirements to attract the charge of tax under the said 1957 Act. The crucial question is whether these two requirements are satisfied. Is there an element of business present in the disputed transactions? Assuming there was a sale of goods, did such sale take place in the course of business and by a person who carries on the business of buying and selling goods?

In the case of Hindustan Shipyard Ltd. v. State of Andhra Pradesh reported in [(2001) 119 STC 533], this Court held that if the thing to be delivered has any individual existence before the delivery as the sole property of the party who is to deliver it, then it is a sale. If the bulk of material used in construction belongs to the manufacturer who sells the end- product for a price, then it is a strong pointer to the conclusion that the contract is in substance one for the sale of goods and not one for labour. However, the test is not decisive. It is not the bulk of the material alone but the relative importance of the material qua the work, skill and labour of the payee which also has to be seen. If the major component of the end-product is the material consumed in producing the chattel to be delivered and skill and labour are employed for converting the main components into the end-products, the skill and labour are only incidentally used, the delivery of the end-product by the seller to the buyer would constitute a sale. On the other hand, if the main object of the contract is to avail the skill and labour of the seller though some material or components may be incidentally used during the process of the end-product being brought into existence by the investment of skill and labour of the supplier, the transaction would be a contract for work and labour.

Applying the above tests, we may now proceed to notice the relevant recitals of the contracts in questions. Under the "Price Schedule", the assessee agreed to supply and install a Kone Elevator for Rs.3,30,000/-. It was agreed that the customer shall approve the drawings and shall make machine-room Hoistway and the Lift Shaft including power supply for the assessee to commence installation at the time of the delivery of the lift. The contractual obligations of the assessee regarding installation included employing labour to complete the mechanical erection, electrical wiring testing and commissioning of the lift. The assessee agreed that it shall commence installation only after the lifts arrived at the site and upon intimation from the customer that the site was ready as per the drawings. As soon as the lift stood installed, the customer was to take over. It was further agreed that any material supplied by the assessee shall remain their property till the lift was handed over to the customer. The contract in question consisted of certain obligations on the part of the customers under the heading "Customers' Contractual Obligations". Under this clause, the customer was obliged to undertake the work of civil constructions consisting of:-

a) A properly enclosed lift Hoistway;

b) A lift pit of proper depth;

c) Properly lighted machine room; and

d) Private pockets on the lift well walls.

Further, certain obligations were passed on the customer under the Delivery Schedule which are reproduced herein below:-

> "The General Agreement Drawing in triplicate will be forwarded to you in approximately six weeks from the date of receipt of complete site details along with the order and advance payment. The purpose of this drawing is to clearly indicate to you pertinent dimensional details of the lift shaft, pit, machine room, car and landing entrances etc., if any modification is required by you in our General Arrangement Drawing it is advisable to hold on construction till the revised General Arrangement Drawing is approved by you.
>
> Within six weeks from the date of receipt of all the site details, the same should be returned to us within two weeks from the date of submission, duly approved by you. We reserve the rights to charge extra for subsequent GAD revisions if full site particulars are not made available to us at the time of placing of the order (or) any modification is desired regarding the building structure resulting in revision of GAD's.
>
> We shall deliver the materials for each Elevator by the end of 6 months from the date of receipt of approved General Arrangement Drawing and shall complete the installation thereafter by the end of 2 months provided the lift shaft including power supply as per our requirements is made ready for us to commence installations at the time of delivery of materials.
>
> We shall commence the installation after the materials arrive at the job site and upon intimation from you that the site is ready as per the approved General Arrangement Drawing. If the site is not ready for taking up installation when the materials arrive at the job site, we shall depute an installation team on hearing from you that the site, is ready in all respects as required by us."

On a careful study of the aforestated clause in the Delivery Schedule, it is clear that the customer was required to do the actual work at site for installation of lift. On reading the above clause, it may be observed that the entire onus of preparation and making ready of the site for installation of lift was on the customer. It was agreed that under no circumstances, the assessee shall undertake installation of lift if the site is not kept ready by the customer. Under Clause 4(g) of the "Customers' Contractual Obligations", the assessee reserved the right to charge the customer for delays in providing the required facilities. These facts clearly indicate that the assessee divided the execution of the contract into two parts, namely, "the work" to be initially done in accordance with the specifications laid down by the assessee and "the supply" of lift by the assessee. "The work" part in the contract was assigned to the customer and "the supply" part was assigned to the assessee. This "supply" part included installation of lift. Therefore, contractual obligation of the assessee was only to supply and install the lift, while the customer's obligation was to undertake the word connected in

keeping the site ready for installation as per the drawings. In view of the contractual obligations of the customer and the fact that the assessee undertook exclusive installation of the lifts manufactured and brought to the site in knocked-down state to be assembled by the assessee, it is clear that the transaction in question was a contract of "sale" and not a "works-contract". Moreover, on perusal of the brochure of the assessee Company, one finds that the assessee is in the business of manufacturing of various types of lifts, namely, Passenger lifts, Freight elevators, Transport elevators and Scenic lifts. A combined study of the above models, mentioned in the brochure, indicate that the assessee has been exhibiting various models of lifts for sale. These lifts are sold in various colours with various capacities and variable voltage. According to the brochure, it is open for a prospective buyer to place purchase order for supply of lifts as per his convenience and choice. Therefore, the assessee satisfies, on facts, the twin requirements to attract the charge of tax under the 1957 Act, namely, that it carries on business of selling the lifts and elevators and it has sold the lifts and elevators during the relevant period in the course of its business. In the present case, on facts, we find that the major component of the end- product is the material consumed in producing the lift to be delivered and the skill and labour employed for converting the main components into the end-product was only incidentally used and, therefore, the delivery of the end-product by the assessee to the customer constituted a "sale" and not a "works- contract". Hence, transactions in question constitute "sale" in terms of entry 82 of the first schedule to the said Act and, therefore, section 5G of the said Act was not applicable.

For the aforestated reasons, the department's appeal is allowed; the impugned judgment and order of the High Court dated 2.7.1999 passed in Tax Revision Case No.129 of 1999 and the judgment and order of the Sales Tax Appellate Tribunal dated 22.12.1995 passed in T.A. Nos.676 & 677 of 1995, are set aside. However, in the facts and circumstances of this case, there will be no order as to costs.