The State Of Madras vs Voltas Limited on 28 November, 1962

Equivalent citations: [1963]14STC446(MAD)

JUDGMENT

Srinivasan, J.

1. The Bombay Mutual Insurance Building, which houses the units of the Life Insurance Corporation, is a building which consists of six floors besides the ground floor. The construction of the building called for as an integral unit thereof provision for air-conditioning the entire building. The building space consists of nearly 67,000 sq. ft., the cubic contents calling for air-conditioning being nearly 8 1/4 lakhs c. ft. When the construction of the building was undertaken Messrs Voltas Limited were assigned the contract for providing the building with a system of air-conditioning of the building. This air-conditioning called for a complete air change of fresh chilled air within the space of 45 to 50 minutes to serve the needs of an approximate number of 1,000 persons distributed throughout the building. The design had to take into account the temperatures inside and outside the building during different parts of year and the humidity of the air as well. Provision had to be made for locating the complicated machinery required for the purpose in the basement of the building, and the layout had to be specially designed to carry the heavy load and to be free against vibration. It also called for integral air-ducts or passages to be constructed to take the chilled air from floor to floor and for the removal of the used air from the conditioned space. Messrs Voltas Limited submitted its proposals in this regard, and finally a contract was entered into on the 23rd July, 1952. The value of the contract was Rs. 6,95,500 for the supply and installation of an air-conditioning plant. The contract contained detailed particulars of the work that had to be done by Messrs Voltas. It specified in particular the manner in which the distribution of the conditioned air had to be made throughout the building ; to the provision of false ceilings as a measure of insulation, the fabrication on the spot and fixing to the building, and embedding in the structure various parts of the machinery, including pipes, etc. It also set out in some detail the different types of machinery that would be utilised in the fabrication of the air-conditioning unit and the insulation material that would be employed. It specified in particular that the material that would be imported would be of the value of Rs. 2,75,000, but that the overall price of the contract of Rs. 6,95,500 was not subject to any change in the factory prices ruling at the time of the shipment. The price was however subject to fluctuation arising from the exchange rate or freight, insurance or import duty.

2. The Deputy Commercial Tax Officer assessed Messrs Voltas on an amount of Rs. 5,02,773, representing the assessable turnover of the works contract. The contention of the assessee was that it was a composite works contract and that there was no basis for making an assessment on a presumed sale of goods. This contention was not accepted by the assessing authority, nor did it find any favour with the Appellate Assistant Commissioner, whose reasoning, though far from clear, purported to hold that the air-conditioning plants can be fixed or removed and they cannot form part of the building as in a works contract considered in the Gannon Dunkerley case [1958] 9 S.T.C.

353. On a further appeal to the Tribunal, the assessee succeeded in establishing that on a proper construction of the terms of the contract, the agreement did not call for the sale of the various component parts of the machinery, and that the contract was one which involved the supply of these materials by the appellants and using their technical skill for linking up these materials by suitable pipe connections and so on and further linking them up with the structure of the building, so that the plant may form an integral part of the whole structure. The Tribunal referred to the decisions in Gannon Dunkerley case1 and Sundaram Motors case [1958] 9 S.T.C. 687 and concluded that the contract was a composite one for the supply of materials and labour, and further, as a result of a personal inspection of the building and the installation, the Tribunal came to the conclusion that the refrigerating plant had become an integral part of the building and an accretion to it. The result was that the assessment was set aside.

3. The State of Madras through the Deputy Commissioner of Commercial Taxes is the petitioner and the conclusion reached by the Tribunal is attacked as erroneous. It is urged that the agreement amounts in substance to a sale of the air-conditioning plant and does not cease to be a sale merely because the seller has undertaken to fix the machinery in the purchaser's premises.

4. One important feature that has to be mentioned is that in the carrying out of a contract of this description, the assessees had in fact to supervise the construction of the building itself in order that the air-conditioning of the building as a whole could be efficiently designed and erected. A note in this regard was submitted to the Tribunal, the contents of which were accepted as substantially correct by the department, and this note was to a large extent relied upon by the Tribunal in reaching its conclusion. An examination of both the contract and the note clearly indicates that this is not analogous to a case where a dealer in refrigerating machinery supplies a self-contained unit for the purpose of air-conditioning one or more rooms. Where such air-conditioning on a small scale is called for, there are units indicated as I ton, 2 tons, etc. up to 5 tons, which can, without modification air-condition spaces of limited area and volume. Provision of such air-conditioning calls for nothing more than making the room more or less air-tight and fixing the unit in question to a window or other apperture and sealing off any draught of air except through the air-conditioning apparatus. Had it been a case of a dealer supplying air-conditioning units of that type in large numbers to air-condition individual rooms even of a large building, it might perhaps follow that what was really involved was a sale of the air-conditioning unit, though certain charges might be levied for the purpose of fixing the unit. The present is not a case of that type. Admittedly there is no air-conditioning unit which is available as such for the purpose of providing air-conditioning for a building as a whole. Where the air-conditioning of a building of this type consisting of several floors is called for, the contractor undertaking the work has in fact to design the lay-out and the various items of machinery involved in the fabrication of such a unit and provide for its installation in a particular manner, the method of installation necessarily varying with the type of the building, the space available and other attendant features. A work of this description had necessarily to go hand in hand with the construction of the building itself, with the assessees rendering the required technical assistance to the architects and other construction contractors during the course of the erection of the building. This was clearly not a case where Messrs Voltas could pick up various pieces of machinery from the market and just put them together and leave it there. In addition to designing the machinery which would be capable of handling the amount of air-conditioning required, the

contractors had to set it up in a particular manner, insulate the air passages carrying dehumidified and chilled air to the various parts of the building, provide false ceilings specially designed for each floor and design the passages in such a manner that the entire volume of the building would receive the advantage of the air-conditioning. Among a multitude of other features which are inherent in a work of this complicated description, special reference has also to be made to the construction of under-ground tanks to hold water, the laying of pipes to circulate 1000 gallons of water per minute employed in cooling the refrigerator and the erection of a cooling tower to cool the water to render it capable of use over and over again. The note submitted by the assessees, which, as we have pointed out, is accepted as correct by the department, shows that when once the entire unit is connected up in the manner required, it is virtually impossible to remove any part of the machinery.

5. It is perhaps hardly necessary for us to set out these features, for, in order to determine whether any taxable transaction, taxable under the Madras General Sales Tax Act, is involved, it is the agreement between the parties that has to be scrutinized. We have nevertheless thought it fit to specify these details, which have also been referred to by the Tribunal in its judgment in even greater detail, in order that the scope of the work undertaken by the assessees may be clearly understood.

6. It seems to us that the decisions of the Supreme Court dealing with this line of cases are against the contention advanced by the department. We may refer to State of Madras v. Gannon Dunkerley & Co. [1958] 9 S.T.C. 353. There the question arose whether the imposition of tax on the supply of materials used in building contracts was warranted by the. provisions of the Madras General Sales Tax Act and whether in fact that provision of the Act bringing to tax the turnover or any part of the turnover represented by a building contract was intra vires of the Legislature. The ultimate decision in the case is almost a matter of history, but nevertheless certain passages in the judgment of the Supreme Court which are very instructive richly deserve, if we may say so, with respect, to be quoted. At page 365, their Lordships say, Thus, according to the law both of England and of India, in order to constitute a sale it is necessary that there should be an agreement between the parties for the purpose of transferring title to goods, which of course presupposes capacity to contract, that it must be supported by money consideration, and that as a result of the transaction property must actually pass in the goods. Unless all these elements are present, there can be no sale. Thus, if merely title to the goods passes but not as a result of any contract between the parties, express or implied, there is no sale....

7. Later at page 377, dealing with the argument that it would be sufficient if there is an agreement between the parties and in the carrying out of that agreement there is a transfer of title to the movables belonging to one person to another for consideration to bring the transaction within the taxable scope of the provisions of the Act, their Lordships repelled the contention and observed :

> If the words 'sale of goods' have to be interpreted in their legal sense, that sense can only be what it has in the law relating to sale of goods. The ratio of the rule of interpretation that words of legal import occurring in a statute should be construed in their legal sense is that those words have, in law, acquired a definite and precise sense, and that, accordingly, the Legislature must be taken to have intended that they

> should be understood in that sense. In interpreting an expression used in a legal sense, therefore, we have only to ascertain the precise connotation which it possesses in law. It has been already stated that, both under the common law and the statute law relating to sale of goods in England and in India, to constitute a transaction of sale there should be an agreement, express or implied, relating to goods to be completed by passing of title in those goods. It is of the essence of this concept that both the agreement and the sale should relate to the same subject-matter. Where the goods delivered under the contract are not the goods contracted for, the purchaser has got a right to reject them, or to accept them and claim damages for breach of warranty. Under the law, therefore, there cannot be an agreement relating to one kind of property and a sale as regards another. We are accordingly of opinion that on the true interpretation of the expression 'sale of goods' there must be an agreement between the parties for the sale of the very goods in which eventually property passes. In a building contract, the agreement between the parties is that the contractor should construct a building according to the specifications contained in the agreement, and in consideration therefor receive payment as provided therein, and as will be presently shown there is in such an agreement neither a contract to sell the materials used in the construction, nor does property pass therein as movables. It is therefore impossible to maintain that there is implicit in a building contract a sale of materials as understood in law.

8. They next dealt with a composite contract under which the contractor undertook to supply materials, contribute labour and produce a construction, and proceeded to enquire whether it is open to the State in execution of its tax laws to split up that agreement into its constituent parts, single out that which relates to supply of materials and to impose the tax thereon treating it as a sale. After referring to several English cases, they rejected the contention in these words at page 385 :

> Another difficulty in the way of accepting the contention of the appellant as to splitting up a building contract is that the property in materials used therein does not pass to the other party to the contract as movable property. It would so pass if that was the agreement between the parties. But if there was no such agreement and the contract was only to construct a building, then the materials used therein would become the property of the other party to the contract only on the theory of accretion.

9. They finally held that in so far as the relevant entry in the Constitutional list provided, the meaning of the expression "sale of goods" could not be interpreted more widely than what was conveyed by that expression in the Sale of Goods Act and that in a building contract, there is no sale as such of materials used and that the Provincial Legislature has no competence to impose a tax thereon under Entry 48. They concluded in these words :

> To avoid misconception, it must be stated that the above conclusion has reference to works contracts, which are entire and indivisible, as the contracts of the respondents have been held by the learned Judges of the Court below to be. The several forms

> which such kinds of contracts can assume are set out in Hudson on Building Contracts, at page 165. It is possible that the parties might enter into distinct and separate contracts, one for the transfer of materials for money consideration, and the other for payment of remuneration for services and for work done. In such a case, there are really two agreements, though there is a single instrument embodying them, and the power of the State to separate the agreement to sell from the agreement to do work and render service and to impose a tax thereon cannot be questioned, and will stand untouched by the present judgment.

10. The principle laid down in this decision has received even greater emphasis in a more recent decision of the Supreme Court in Carl Still v. State of Bihar [1961] 12 S.T.C. 449. That was a contract where the appellant undertook to set up a complete coke oven battery ready for production as well as a by-products plant and to erect and construct buildings, plants and machineries and deliver and supply accessories and articles and render services for an all-inclusive price. The Taxing Department sought to impose sales tax on the appellant on the materials supplied in the execution of the contract on the ground that such a supply was a sale. It was held that the contract was entire and indivisible for the construction of certain specified works for a lump sum and not a contract for sale of materials as such. Their Lordships set out the point for determination thus :

> Whether on its true construction, the contract in question is a combination of two distinct agreements, one to sell materials and the other to supply labour and services, or whether it is only one agreement entire and indivisible for execution of the works?

11. They referred to the relevant provisions in the contract. One of the clauses, Clause 15, in the contract stipulated that all materials and plant brought by the contractor upon the site in connection with the construction "shall immediately they are brought upon the site become the owner's property and the same shall not on any account whatsoever be removed or taken away by the contractor or by any other person without the owner's prior authority in writing." From this clause it was apparently contended that there was a contract of sale of the materials by the contractor as distinct from the works contract. Their Lordships made reference to an earlier decision of theirs in Peare Lal Hari Singh v. State of Punjab [1958] 9 S.T.C. 412, where they had to construe a similar term of the contract and observed that the object of such a provision was only to ensure that materials of the right sort were used in the construction and that such a term in the agreement did not constitute a contract of purchase of the materials. The same conclusion was reached in the case which they had before them. They observed:

> If, as held by us, Clause 15 does not embody an agreement for the sale of materials as such, there is no contract of sale with respect to them and Section 9 of the Sale of Goods Act can have no application. The contention, therefore, that Clause 15 of the agreement could be read as amounting to a contract of sale of materials, and that the price therefor could be fixed as provided in Section 9 of the Sale of Goods Act by recourse to the account books of the appellants or ,the invoices or the course of dealings between them and the owner, must be rejected as untenable. It follows that the agreement...being a contract for the construction of works, one and indivisible,

> the respondents have no right to impose a tax on the materials supplied in execution of that contract on the footing that such supply is a sale.

12. Though the above two decisions deal with building contracts, the principle is applicable even to works contracts relating to movable goods. The principle was in fact so applied by this Court in Sundaram Motors v. State of Madras [1958] 9 S.T.C. 687, where the question arose whether repairs to motor vehicles involved an element of sale of goods. After referring to Gannon Dunkerley's case [1958] 9 S.T.C. 353], the learned Judges stated at page 696:

> Two more elements at least are therefore necessary in addition to a transfer of a movable property to constitute a sale. (1) There should be an agreement between the parties to sell and purchase, and (2) that agreement should be with reference to the particular goods. A mere incorporation of a movable thing into a larger property and transferred when the latter is delivered over to the customer cannot by itself amount to a sale.

13. Again at page 697, it was observed:

> Rarely customers know or even care to know anything about the parts to be replaced; the necessity for replacement is often discovered only during the process of repair. To them the transaction is very often an integral one; on the part of the assessee, the parts were needed in the course of effecting repairs to the car and were fabricated ad hoc, i.e., for that purpose. It was a manufacture of the material occasioned by reason of the undertaking to repair the car and not one done as part of a commercial undertaking; to quote the words of the learned advocate for the petitioners, it was 'an ad hoc manufacture in connection with the repair of the car.' The elements necessary for constituting a sale of the part as such are therefore lacking in the case.

14. We have examined the entire contract, each and every term thereof, and we can find no indication therein that there was any agreement between the contracting parties that there was to be a sale of any part of the machinery as such. The present case accordingly falls squarely within the scope of the principles laid down in the cases to which we have made detailed reference. It should, therefore, follow that no part of the turnover in this case became taxable.

15. Learned counsel for the department contends however that there is a reference made in the contract to the value of the imported material which had to be supplied and a further reference to material which had to be procured in India towards the fulfilment of the contract. He argues that under the heading "Prices and Exchange" it is stated that "the price quoted above is based on price lists now available with us and in view of the uncertainty of the future cost of manufacture, you will appreciate that it will not be possible for us to predict what the final price will be, as the same will depend upon our supplier's price ruling at the moment of shipment." The contention advanced, which to our minds is not really precise, is that if the contract was an indivisible one calling for the fabrication of a unit for an overall price, there was no need for splitting up this contract into what is apparently a quotation for the price of the material to be supplied. It has to be noticed however that

it is only the probable cost of the material that had to be imported from abroad that is specified herein. There is no indication as to the cost of the material which had to be locally procured and which had also to be employed in the execution of the contract. It seems to us to be clear in a contract of this description, where the overall price was fixed at very nearly Rs. 7 lakhs, the customer had at least a right to know what proportion of the price that he was paying would go towards the value of the materials supplied and what proportion towards the cost of labour, technical skill, etc. No contracting party would accept a quotation which gave no particulars and indeed, it is the invariable practice when tenders are called for to require such particulars to be furnished. The mere break-up of the figure in this manner does not lead to the conclusion that there was a stipulation of the sale of the machinery simpliciter.

16. Learned counsel for the department also refers to that clause of the contract which deals with the terms of payment. It is in these terms:

1. 10 per cent with order;

2. 20 per cent on intimation of the receipt of import licences;

3. 50 per cent against delivery, pro rata of the value of the goods delivered at site....

17. Special reference has been made to item 3 above and it is argued that because the contractors asked for payment of 50 per cent. of the value of the goods delivered at site, it must be inferred that there was a sale of that item of machinery. Such an inference appears to us to be very far-fetched. By no stretch of imagination can it be construed that Messrs Voltas were engaging in a sale of certain items of machinery to the Bombay Mutual Insurance. They contracted for the performance of a particular item of work which involved as part thereof supply and utilisation of certain materials. Obviously no contractor would be willing to wait for the payment till the completion of the work when the contract called for purchase and utilization of material at a high cost for the purpose of the contract. The mode of payment does not carry with it any implication that there was a sale of the goods as such at any stage of the contract.

18. We are accordingly of the opinion that the Tribunal reached the only possible conclusion on the facts and circumstances of the case. There was no agreement which stipulated for the sale of materials as such as a divisible part of the contract entered into.

19. The petition fails and is dismissed with costs.

20. Counsel's fee Rs. 100.