THE HIGH COURT OF SIKKIM: GANGTOK

(Civil Extra Ordinary Jurisdiction)

DATED : 29.11.2012

CORAM

HON'BLE MR. JUSTICE PERMOD KOHLI, CHIEF JUSTICE
HON'BLE MR. JUSTICE S. P. WANGDI, JUDGE

Writ Petition (Civil) No. 36 of 2011

M/s. Future Gaming Solutions Pvt. Ltd.,
a private limited company registered
under the Companies Act, 1956, having
its registered office at –
355-359, Daisy Plaza, 6th Street,
Gandhipuram,
Coimbatore (Tamil Nadu),
and branch office at Samdrupling Building,
Kazi Road, Gangtok.
Sikkim. ... **Petitioner**

- versus -

1. Union of India,
Through its Secretary
Ministry of Finance,
Department of Revenue,
North Block, New Delhi.

2. Commission of Service Tax, Siliguri,
C.R. Building,
Harendra Mukherjee Road,
Hakimpara, Siliguri HO,
District : Darjeeling, West Bengal.

3. Superintendent of Central Excise,
Gangtok Range, Jeewan Theeing Marg,
Development Area, Gangtok,
East Sikkim, PIN – 737 101.

4. State of Sikkim,
Through Chief Secretary,
State of Sikkim. ...**Respondents**

For Petitioner : M/s. A. R. Madhav Rao, Krishna Rao, Laxmi Chakraborty and Manju Rai, Advocates.

For Respondents No. 1, 2 & 3 : M/s. Farooq Md. Razzak, Addl. Solicitor General (Kolkata) with B. K. Gupta and Jigme P. Bhutia, Advocates.

For Respondent No. 4 : M/s. Karma Thinlay Namgyal, Govt. Advocate and S. K. Chettri, Asstt. Govt. Advocate.

Writ Petition (Civil) No. 23 of 2011

1. Summit Online Trade Solutions Pvt. Ltd.
Formerly known as (M/s. Sugal & Damani Enterprises Pvt. Ltd.)
A company registered under the Companies Act,
Through the Director Mr. Naresh Mangal,
Baluwakhani, Gangtok, East Sikkim.

2. Mr. Naresh Mangal, Director,
Summit Online Trade Solutions Pvt. Ltd.
A company registered under the Companies Act,
Baluwakhani, Gangtok, East Sikkim.

3. Mr. Prem Kishor Parashar,
Officer In charge,
Summit Online Trade Solutions Pvt. Ltd.
A company registered under the Companies Act,
Baluwakhani, Gangtok, East Sikkim.

..... **Petitioners.**

- versus -

1. Union of India,
Through Secretary
Ministry of Finance,
Department of Revenue,
North Block, New Delhi.

2. Deputy Commissioner of Central Excise,
C.R. Building, Gangtok Range,
Hakimpara, Siliguri, West Bengal.

3. State of Sikkim,
Through the Secretary,
Finance, Revenue & Expenditure Deptt.,
Government of Sikkim,
Tashiling Secretariat,
Gangtok, East Sikkim.

4. Sikkim State Lotteries,
Government of Sikkim,
Through the Director,
State Lotteries, Baluwakhani,
Gangtok, East Sikkim - 737 101.

...**Respondents**

For Petitioner	:	M/s. A. K. Upadhyaya, Sr. Advocate with E.R. Kumar, Rajat Nair, Binita Chhetri and Dawa Jangmu Sherpa, Advocates.
For Respondents No. 1 & 2	:	M/s. Farooq Md. Razzak, Addl. Solicitor General (Kolkata) with B. K. Gupta and Jigme P. Bhutia, Advocates.
For Respondent No. 3 & 4	:	M/s. Karma Thinlay Namgyal, Govt. Advocate and S. K. Chettri, Asstt. Govt. Advocate.

J U D G M E N T

KOHLI, C.J.

Petitioners have called in question the constitutional validity of clause (zzzzn) of Sub-section (105) of Section 65 of the Finance Act, 1994 as inserted by the Finance Act, 2010 introducing the activity of “promotion,

marketing, organising or in any other manner assisting in organising game of chance, including lottery" as a new category of "taxable service". It is relevant to note the facts leading to filing of the present petitions.

2. Both the petitioners are companies incorporated as Private Limited companies under the Indian Companies Act, 1956. The petitioners are engaged in the business of sale of paper and online lottery tickets respectively organised by the Government of Sikkim. Petitioner in W.P. (C) No.36 of 2011, namely, M/s. Future Gaming Solutions Pvt. Ltd. dealing with paper lottery tickets, entered into an Agreement for the sale of lottery tickets on behalf of the State of Sikkim on 10.08.2009 (Annexure-3), whereas the petitioner in W.P. (C) No.23 of 2011, namely, Summit Online Trade Solutions Pvt. Ltd. dealing with online lottery tickets, entered into an Agreement with the State of Sikkim on 09.05.2005 (Annexure-P3 colly.) followed by a Supplementary Agreement dated 25.04.2008. Mutual terms and conditions concerning the sale and purchase of lottery tickets between the State Government and the petitioners are governed and regulated by the contractual stipulations contained in the aforesaid Agreements. The relevant conditions are reproduced hereunder:-

"WHEREAS in pursuant of an open tender called by the Government. The Second Party was appointed as the Purchaser for sale of conventional weekly paper (3 digit and above) lottery and bumper lottery with denomination of rupee one and above organised by the Government for a period of five years vide an agreement dated 6th October, 2004;

……..

4. That in consideration of the appointment of the Second party as sole purchaser of the conventional paper lottery of the Government for a maximum of 50 (fifty) weekly lottery schemes per day, the sole purchaser shall pay a sum of Rs.8 crores (Rupees Eight Crores) per annum to the Government for the 1st year of the extended period i.e. w.e.f. 18th October, 2009 to 17th October, 2010 and a sum of Rs.10 crores (Rupees Ten Crores) per annum only from the second year of the extended period effective from 18th October, 2010 to 17th October, 2014. ……..

……...

13. That the Government shall deliver the tickets to the sole purchaser at the destination as may be agreed upon.

14. That the Government shall deliver to and the sole purchaser shall take delivery from the Government whole of the lottery tickets printed for a draw of a particular scheme with a clear understanding that if the sole purchaser is not able to sell the whole tickets, he shall return the unsold tickets to the Government within 15 (fifteen) days from the date of draw, which shall then be destroyed after verification. The whole sale price of tickets sold shall be determined by the Government on the basis of the prize amount, cost of paper, cost of printing, draw expenses, transportation charges and the Government share of revenue as fixed under clause 4:

Provided that the prices of the tickets may be changed under the following circumstances, namely:-

(i) Change in the price structure of the lottery schemes.

(ii) Change in paper cost, printing charges and freight, and

(iii) Market conditions."

15. That the full payment of the tickets resold by the sole purchaser shall be realized by the Government from the sole purchaser at wholesale rates as per clause 14 above.

……...

20. That the Government shall immediately after each draw supply to the sole purchaser a copy of the result of the draw duly authenticated by the Director who shall immediately thereafter make arrangements to publicize the result of each draw:

Provided that the sole purchaser is at liberty, on his own cost and expenses, to take up any kind of publicity of Sikkim state lotteries including telecast of result on any

> Satellite T.V. Channel every day, provided the publicity shall in no way undermine the prestige of the government. No claim for cost on these accounts will be entertained by the Government.
>
> .....
>
> 23. The sole purchaser may appoint stockists, selling agents or sellers for further resale in different parts of the country on his own terms and at his own risk and responsibility.
>
> .....
>
> 26. The sole purchaser shall pay the full amount for the tickets actually sole purchaser upon receipt of the invoice from the Government which shall be raised indicating the amount of wholesale rate and adjustment of prizes up to Rs.5000/- (Rupees five thousand) to be disbursed by the sole purchaser for each lottery draw on the lottery tickets actually sold by the sole purchaser.
>
> 27. The sole purchaser shall pay State tax or any other kind of taxes imposed by the other State Governments on sale of lottery tickets.
>
> .....
>
> 30. The sole purchaser shall be entitled to appoint stockists, selling agents or sellers in the discharge of any obligations hereunder or as a result of this agreement. However, the Government shall have no responsibility or liability towards such stockists, selling agents or sellers and shall have no privity of contract with them. Any dispute whether as result of non-payment or otherwise, shall not discharge the Sole purchaser's obligation towards the State Government under this Agreement."

3. Parliament of India introduced a new concept of tax, namely, "Service Tax" vide Finance Act, 1994 under Chapter V thereof, which came to be enacted on 01.07.1994. Vide Finance Act, 2003, Finance Act, 1994 was amended so as to introduce a new category of taxable service, i.e. "Business Auxiliary Service", under Sub-section (19) of Section 65 of the Finance Act, 1994 with effect from 01.07.2003. Section 65(19) is reproduced hereunder:-

> "(19) "business auxiliary service" means any service in relation to;-

(i) promotion or marketing or sale of goods produced or provided by or belonging to the client; or

(ii) promotion or marketing of service provided by the client; or

Explanation.- For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, "service in relation to promotion or marketing of service provided by the client: includes any service provided in relation to promotion or marketing of games of chance, organized, conducted or promoted by the client, in whatever form or by whatever name called, whether or not conducted online, including lottery, lotto, bingo; [Explanation inserted vide Finance Act, 2008 w.e.f. 16th May, 2008]

(iii) any customer care service provided on behalf of the client; or

(iv) procurement of goods or services, which are inputs for the client; or

Explanation. – For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, "inputs" means all goods or services intended for use by the client;

(v) production or processing of goods for, or on behalf of the client; or

(vi) provision of service on behalf of the client; or

(vii) a service incidental or auxiliary to any activity specified in a sub-clauses (i) to (vi), such as billing, issue or collection or recovery of cheques, payments, maintenance of accounts and remittance, inventory management, evaluation or development of prospective customer or vendor, public relation services, management or supervision, and includes services as a commission agent, but does not include any activity that amounts to "manufacture" within the meaning of clause (f) of section 2 of the Central Excise Act, 1944 (1 of 1944).

Explanation. – For the removal of doubts, it is hereby declared that for the purposes of this clause, -

(a) "commission agent" means any person who acts on behalf of another person and causes sale or purchase of goods, or provision or receipt of services, for a consideration, and includes any person who, while acting on behalf of another person -

(i) deals with goods or services or documents of title to such goods or services; or

(ii) collects payment of sale price of such goods or services; or

(iii) guarantees for collection or payment for such goods or services; or

> (iv) undertakes any activities relating to such sale or purchase of such goods or services."

4. Service Tax Department issued a notice to the petitioners under the amended Finance Act in 2007 requiring the petitioners to register under the said Act for payment of service tax. Disputing the liability, W.P. (C) No.19 of 2007, titled Martin Lottery Agencies Ltd. v. Union of India & Ors. came to be filed before this Court challenging the levy of service tax upon the sale of lottery tickets. This petition was allowed by this Hon'ble Court vide Judgment dated 18.09.2007 declaring that no service tax was payable on the activity undertaken by the petitioner. The relevant observations are quoted hereunder:-

> "..... The arguments this time centered out whether lottery tickets are goods or not. The statutory provisions which are material in this regard are extracted in my earlier order. On the authority of the Constitution Bench of the Supreme Court which delivered its judgment in the *Sunrise Associates* case (2006) 5 SCC 603 lottery tickets have to be held to be actionable claims. As such those would not be goods within the meaning of the definition clause in the Sale of Goods Act. If the lottery tickets are not goods, the writ petitioners cannot said to be rendering any service in relation to the promotion of their client's goods, or marketing of their client's goods, or sale of their client's goods."

The aforesaid judgment came to be challenged before the Hon'ble Supreme Court in Civil Appeal No.3239 of 2009.

5. During the pendency of this Civil Appeal, the Finance Act, 1994 was further amended with the

introduction of an "Explanation" to Section 65(19)(ii) of the Finance Act. The Explanation is reproduced hereunder: -

> **"***Explanation*.- For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, "service in relation to promotion or marketing of service provided by the client: includes any service provided in relation to promotion or marketing of games of chance, organized, conducted or promoted by the client, in whatever form or by whatever name called, whether or not conducted online, including lottery, lotto, bingo; [Explanation inserted vide Finance Act, 2008 w.e.f. 16th May, 2008]**"**

6. Hon'ble Supreme Court was apprised of the aforesaid amendment. Taking note of the Explanation and its impact on the judgment delivered by this Court, the Hon'ble Supreme Court held the Explanation to be a substantive law and declared it to be prospective. Regarding the validity of the Explanation, the issue was left open. However, the judgment of this Court was not interfered. The Hon'ble Supreme Court delivered its judgment on 05.05.2009 reported in ***2009(14) S.T.R. 503 (SC) : (2009) 12 SCC 209***, titled ***Union of India & Ors. v. Martin Lottery Agencies Ltd.*** The relevant observations of the Hon'ble Supreme Court in this regard are quoted hereunder: -

> **"** **36.** It is, therefore, evident that by reason of an explanation, a substantive law may also be introduced. If a substantive law is introduced, it will have no retrospective effect.
>
> The notice issued to the assessee by the appellant has, thus, rightly been held to be liable to be set aside. Subject to the constitutionality of the Act, in view of the explanation appended to this, we are of the opinion that the

> service tax, if any, would be payable only with effect from May, 2008 and not with retrospective effect.
>
> **37.** In a case of this nature, the Court must be satisfied that the Parliament did not intend to introduce a substantive change in the law. As stated hereinbefore, for the aforementioned purpose, the expressions like 'for the removal of doubts' are not conclusive. The said expressions appear to have been used under assumption that organizing games of chance would be rendition of service. We are herein not concerned as to whether it was constitutionally permissible for the Parliament to do so as we are not called upon to determine the said question but for our purpose, it would be suffice to hold that the explanation is not clarificatory or declaratory in nature.
>
> **38.** For the views we have taken, we have no other option but to hold that the High Court judgment albeit for different reasons warrants no interference. This appeal is dismissed with costs. Counsel fee assessed at Rs.1,00,000/-."

7. In view of the observations of the Hon'ble Supreme Court, the petitioner filed Writ Petition (C) No.36 of 2009 challenging the validity of the Explanation to Section 65 (19)(ii) of the Finance Act, 1994, titled M/s. Future Gaming Solutions Pvt. Ltd. v. Union of India & Ors. This Writ Petition was dismissed by this Court vide its judgment dated 30.07.2010. Aggrieved by the dismissal of this petition, the petitioner filed a Special Leave Petition before the Hon'ble Supreme Court, being SLP (C) No.26771 of 2010, wherein Union of India has been put on notice and petition is pending consideration.

8. While the aforesaid issue is pending consideration before the Hon'ble Supreme Court, the Finance Act, 1994 again came to be amended with the deletion of the

Explanation to Section 65(19)(ii) and introduction of a new category of "taxable service" vide clause (zzzzn) to Sub-section (105) of Section 65 vide the Finance Act of 2010 with effect from 01.07.2010. The relevant amendment thus introduced reads as under:-

> **"**(105) "taxable service" means any service provided or to be provided,-
>
> ...
>
> (zzzzn) to any person, by any other person, for promotion, marketing, organising or in any other manner assisting in organizing games of chance, including lottery, Bingo or Lotto in whatever form or by whatever name called, whether or not conducted through internet or other electronic networks;**"**

9. The petitioners got themselves registered under the provision of the amended Act. It is alleged that this registration is under mistaken fact and they are paying service tax since then under protest. It is further alleged that now the petitioners have realised that no service tax is payable on the activity undertaken by them in terms of the amended clause (zzzzn) to Section 65(105) of the Finance Act, 1994 and have challenged the same in these petitions before us.

10. Challenge to the amended Clause (zzzzn) to Sub-section (105) to Section 65 of the Finance Act, 1994 is primarily on the following two grounds –

(A) that the activity being performed by the petitioners does not fall within the purview of "Taxable Service", the transaction between the petitioners and the State of Sikkim simpliciter being a purchase and sale of lottery tickets or at the best an actionable claim; and

(B) the conduct of lottery is an act of "betting and gambling", the same being a game of chance, the State Legislature under entry 62 of List II of Schedule 7 to the Constitution of India has exclusive competence to enact law to impose taxes. The Parliament under its residuary legislative power under entry 97 of List I, Schedule 7 to the Constitution of India lacks legislative competence to levy any tax in respect to the activity falling under entries 34 and 62 of List II.

11. The learned counsel appearing for the parties have addressed lengthy arguments. Before the above questions are considered, it is useful to note the relevant constitutional provisions whereunder legislative powers are exercisable by the Parliament and the State Legislatures respectively.

12. Article 246 of the Constitution of India deals with the distribution of the legislative powers amongst the Parliament and the Legislatures of States, whereas Article

248 deals with the residuary powers of legislation. Both the Articles are reproduced hereunder: -

> " 246. Subject-matter of laws made by Parliament and by the Legislatures of States. – (1) Notwithstanding anything in clauses (2) and (3), Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule (in this Constitution referred to as the "Union List").
>
> (2) Notwithstanding anything in clause (3), Parliament and, subject to clause (1), the Legislature of any State also, have power to make laws with respect to any of the matters enumerated in List III in the Seventh Schedule (in this Constitution referred to as the "Concurrent List").
>
> (3) Subject to clauses (1) and (2), the Legislature of any State has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List Ii in the Seventh Schedule (in this Constitution referred to as the 'State List').
>
> (4) Parliament has power to make laws with respect to any matter for any part of the territory of India not included in a State notwithstanding that such matter is a matter enumerated in the State List.
>
> xxxxxxxxxxxxxxx xxxxxxxxxxxxxxxxxxx
>
> 248. Residuary powers of legislation. – (1) Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List of State List.
>
> (2) Such power shall include the power of making any law imposing a tax not mentioned in either of those Lists."

13. Clause (1) of Article 246 confers exclusive power upon the Parliament to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule referred to as the "Union List", whereas Clause (3) of Article 246 confers exclusive power upon the Legislature of any State to make laws for such State with respect to any of the matters enumerated in List II in the Seventh Schedule referred to as the "State List". As regards the residuary

powers of Legislation are concerned under Article 248, Parliament alone has the power to make any law with respect to any matter not enumerated in the Concurrent List or State List. Clause (2) of Article 248 further empowers the central Parliament to make laws imposing a tax not mentioned in either of the above two lists. In the context of lottery which is "*res extra commercium"*, entry 40 in List I empowers the Parliament to make laws whereas under entry 34 and entry 62 of List II, the State Legislature has power to make laws in respect to "betting and gambling" and levy of taxes thereon respectively. Entries 40 and 97 under List I and entries 34 and 62 under the List II are quoted hereunder:-

> "
>
> *SEVENTH SCHEDULE*
>
> *[Article 246]*
>
> **List I – Union List**
>
> .....
>
> 40. Lotteries organized by the Government of India or the Government of a State.
>
> .....
>
> 97. Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists.
>
> **List II – State List**
>
> .....
>
> 34. Betting and gambling.
>
> .....
>
> 62. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.
>
> ....."

14. In exercise of the power under entry 40, List I, the Parliament enacted the Lotteries (Regulation) Act, 1998 (hereinafter referred to as 'the Act') to regulate the lotteries and to provide for matters connected therewith and incidental thereto. Section 3 of the Act prohibits the conduct or promotion of lottery by any State Government except under the conditions contained in Section 4. Section 4 prescribes the conditions subject to which the State Government may organize, conduct or promote a lottery. For the purpose of the present petitions, some of the relevant conditions are quoted hereunder: -

> "4. .....
>
> (b) the State Government shall print the lottery tickets bearing the imprint and logo of the State in such manner that the authenticity of the lottery ticket is ensured;
>
> (c) the State Government shall sell the tickets either itself or through distributors or selling agents;
>
> .....
>
> (e) the State Government itself shall conduct the draws of all the lotteries;
>
> .....
>
> (k) such other conditions as may be prescribed by the Central Government."

15. Section 11 confers power on the Central Government to make rules to carry out the provisions of the Act whereas under Section 12, the State Government has been empowered to make rules for the same purpose. The

Central Government in exercise of rule making power under sub-section (1) of Section 11 of the Act has framed rules known as the Lotteries (Regulation) Rules, 2010. Rule 2 of the Rules defines various expressions. The relevant being reproduced hereunder: -

> "2. .....
>
> (c) "distributor or selling agent" means an individual or a firm or a body corporate or other legal entity under law so appointed by the Organising State through an agreement to market and sell lotteries on behalf of the Organising State;
>
> .....
>
> (e) "online lottery" means a system created to permit players to purchase lottery tickets generated by the computer or online machine at the lottery terminals where the information about the sale of a ticket and the player's choice of any particular number or combination of numbers is simultaneously registered with the central computer server;
>
> (f) "Organising State" means the State Government which conducts the lottery either in its own territory or sells its tickets in the territory of any other State;
>
> .....
>
> (h) "sale proceeds" means the amount payable by the distributor to the Organising State in respect of sale of tickets calculated at the face value printed on each ticket in respect of lotteries of a particular draw or scheme of both;"

16. Rule 3 further permits the State Government to organize a paper or online lottery subject to conditions specified in the Act and the Rules. One of the conditions contained in sub-Rule 3(e) is to furnish information regarding name or names of the distributors or selling

agents with their addresses and contact information. Rule 4 deals with the appointment of distributors or selling agents by the organising State and lay down terms and conditions for such appointment. Rule 4 is reproduced hereunder: -

> " **4. Appointment of distributor or selling agent. –** (1) The Organising State may specify qualifications, experience and other terms and conditions for the appointment of distributors or selling agents.
>
> (2) The distributors or selling agents shall furnish a security deposit or a bank guarantee, as may be specified by the Organising State.
>
> (3) The distributors or selling agents shall maintain a record of the tickets obtained from the Organising State, tickets sold and those which remain unsold up to the date and time of draw along with other details, as may be specified by the Organising State.
>
> (4) The Organising State shall pay to the distributors or selling agent any commission due to them and the prize amounts disbursed by the distributors or selling agents to the winners, if any, out of the money so deposited in the Public Ledger Account or in the Consolidated Fund of the Organising State.
>
> (5) The distributors or selling agents shall return the unsold tickets to the Organising State with full accounts along with the challans of the money deposited in the Public Ledger Account or in the Consolidated Fund of the Organising State through the sale of tickets.
>
> (6) The unsold tickets and unused counterfoils of lottery tickets shall be disposed of in the manner specified by the Organising State from time to-time."

17. From the constitutional scheme contained in entry 40 of List I and consequential law enacted by the Parliament, it is abundantly clear that the entry 40 empowers the Parliament to make a regulatory law in respect to the lotteries. It is the common case of the parties that power to tax does not emanate from the power to make

regulatory law. Similarly, entry 34 of the List II deals with the subject of "betting and gambling" and the State legislature has power to make regulatory law in respect of "betting and gambling". It goes without saying and as interpreted by a plethora of judicial pronouncements, the conduct of lottery which is a game of chance falls within the ambit, scope and purview of expression "betting and gambling". Entry 34, however, does not empower the State to enact any law imposing any tax upon the activity of betting and gambling like entry 40 of List I. It is Entry 62 that specifically provides for levy of taxes on "betting and gambling".

18. In the backdrop of aforesaid constitutional and statutory provisions, we shall take up the grounds noticed hereinabove for consideration *in seriatim*.

GROUND - A

(I) Terms and conditions of Agreement dated 10.08.2009 (Annexure 3) depict the mutual relationship between M/s. Future Gaming Solutions Pvt. Ltd. (petitioner) and the State Government. The preface of the Agreement shows that open tenders were invited for appointment of a purchaser for sale of lottery tickets of denomination of

Re.1/- and above organized by the State Government for a period of 5 (five) years. Clause 4 of the Agreement further demonstrates that the petitioner was appointed as a sole purchaser on payment of lump sum amount of Rs.8.00 crores p.a. for the first year of extension and Rs.10.00 crores p.a. from the second year commencing from 18.10.2010 till 17.10.2014. Clause 13 further shows that the petitioner's company is a sole purchaser of the lottery tickets organized by the State Government and unsold tickets are to be returned to the Government within 15 (fifteen) days from the date of draw which would be destroyed after verification. Clause 20 of the Agreement permits the sole purchaser to take up any kind of publicity etc. through electronic media and other modes at its own cost and expense without any contribution from the State Government in this regard. Clause 23 further grants liberty to the sole purchaser to appoint stockists, selling agents or sellers for further resale of lottery tickets in different parts of the country on its own terms, risk and responsibility. Under Clause 26, the purchaser, i.e. the petitioner is required to pay full sale price of the tickets and to pay further Rs.5,000/- for each lottery draw on the lottery tickets actually sold by the purchaser. Clause 30 of the Agreement in no uncertain terms makes the sole purchaser (petitioner)

responsible for appointment of stockists, selling agents or sellers for the sale of lottery tickets with further stipulation that the Government shall have no privity of contract with any such stockists, selling agents, etc.

(II) Based upon these contractual stipulations, it is contended on behalf of the petitioners that the relationship between the petitioners and the State Government is that of buyer and seller with further liberty to the buyer for re-sale to stockists, selling agents etc. on its own without any interference of the State Government. It is thus submitted that the appointment of the petitioner as a distributor and purchaser of lottery tickets is on principal to principal basis whereunder the petitioner purchases the tickets subject to right of resale, which is one of the permitted jural relationship between the seller and the purchaser in common law.

(III) Mr. A. R. Madhav Rao, learned arguing counsel appearing for the petitioner, while explaining the conduct of lottery business, submits that lottery tickets are goods and actionable claim and thus excluded from various State sales tax legislations. To harness, he has referred to the definition of sale and purchase as provided under the Central

Excise Act. Section 2(h) of the Central Excise Act, 1944 defines sale and purchase and reads as under: -

> "(h) "sale" and "purchase", with their grammatical variations and cognate expressions, mean any transfer of the possession of goods by one person to another in the ordinary course of trade or business for cash or deferred payment or other valuable consideration;"

(IV) Regarding the applicability of the above definition to the service tax, reference is made to Section 65-A (121) of the Finance Act, 1994, which reads as under: -

> "(121) words and expressions used but not defined in this Chapter and defined under Central Excise Act, 1944 (1 of 1944) or the rules made thereunder, shall as far as may be, in relation to service tax as they apply in relation to a _____ excise."

(V) Admittedly, the expression "sale and purchase" has not been defined in the Finance Act and thus the above definition prescribed in the Central Excise Act shall be applicable to all such transactions which may fall within the purview of the expression "sale and purchase" in relation to service tax. In ***Sunrise Associates* v. *Government of NCT of Delhi* : (2006) 5 SCC 603**, the Hon'ble Supreme Court has held that the lottery tickets are goods in the wider sense of the term though the lottery ticket is an actionable claim and it is only on account of statutory exclusion from definition of goods in various State sales tax laws that it has

been held to be not goods. The relevant observations are contained in paragraph 36 quoted hereunder: -

> **"**36. We have noted earlier that all the statutory definitions of the word "goods" in the State sales tax laws have uniformly excluded, inter alia, actionable claims from the definition for the purposes of the Act. Were actionable claims, etc., not otherwise includible in the definition of "goods" there was no need for excluding them. In other words, actionable claims are "goods" but not for the purposes of the Sales Tax Acts and but for this statutory exclusion, an actionable claim would be "goods" or the subject-matter of ownership. Consequently, an actionable claim is movable property and "goods" in the wider sense of the term but a sale of an actionable claim would not be subject to the sales tax laws.**"**

It is pertinent to note that the earlier Writ Petition i.e. **W.P. (C) No.19 of 2007**, titled ***Martin Lottery Agencies Ltd.*** v. ***Union of India & Ors.*** was decided by this Court holding the lottery ticket to be actionable claim and thus beyond the scope of "service" relying upon the judgment in ***Sunrise Associates (supra)***. The judgment of this Court in ***Martin Lottery Agencies Ltd. (supra)*** has not been interfered with by the Apex Court in Civil Appeal No.3239 of 2009 (supra) but dismissed the Appeal on some other reasons as noted above.

(VI) Opposing the contention of the learned counsel for the petitioners, Mr. Farooq Md. Razzak, Ld. Addl. Solicitor General (Kolkata) appearing for the Union of India, submits that the definition of "taxable service" has been statutorily provided under the impugned provision contained in Clause (zzzzn) to sub-section 105 of Section 65 of the Finance Act,

1994 as amended vide Amendment Act of 2010 with effect from 01.07.2010, which, *inter alia*, includes the promotion and organising etc. of lotteries as a "taxable service". The activities of the petitioners fall within the above mentioned provision. According to Mr. Razzak, the petitioners arrangement with the State Government for appointment as a buyer and distributor is dehors the provision of Section 4 of the Lotteries (Regulation) Act, 1998. Referring to Section 4(c), it is argued that the State Government alone is entitled to sell the tickets either itself or through distributors or selling agents and thus any other arrangement whereby the sale of the tickets is made by the State Government to a distributor who buys the tickets in bulk and then further sells to selling agents, is impermissible in law. His further submission is that the State sells the lottery tickets on commission basis. The MRP of the ticket is Re.1/- and it is sold at 70 paise per ticket to the petitioners in bulk and the 30% commission received by the petitioners is for purposes of organizing and promoting the sale of the lottery ticket for the State, which activity is nothing but a "service" rendered to the State. Referring to various conditions of the Agreement between the petitioners and the State, it is argued that unsold tickets are returned to the State and refunded. According to him, the only conclusion which can

thus be, is that the petitioners are rendering services to the State of Sikkim and hence liable to "service tax" in terms of the Section 65 (105) (zzzzn) of the Finance Act, 1994. He submits that similar provision introduced by way of an explanation to Section 65(19)(ii) of the Finance Act vide Amendment Act dated 16.05.2008 has been interpreted by this Court in W.P. (C) No.21 of 2009 (Annexure-6) titled ***M/s. Tashi Delek Gaming Solutions Pvt. Ltd. & Anr.*** v. ***Union of India & Ors.*** and other connected matters decided vide judgment dated 30.07.2010 upholding the vires of the Explanation. This Court has held that the Explanation is a substantive law and thus the activity of the petitioner falls within the definition of "taxable service". The relevant observations are noticed hereunder: -

> **"15.** ..... The fact remains that lottery tickets are purchased not for their consumption but for the purpose of marketing the same. In order to market lottery tickets petitioner is required, in terms of the agreement it has with the State Government, to put up and the petitioner in fact puts up advertisements. It thereby entices the ultimate buyer of lottery tickets to purchase the same. It thus promotes the activity of its client, the State Government, in organizing lottery. In the matter of enabling its client to sale a lottery ticket worth Rs.1/- at Rs.1/- to the ultimate buyer of lottery tickets petitioner renders service thus. The value of lottery tickets without the promotional and marketing activity of the petitioner is 70 paise, which by reason of marketing and promotional activity of the petitioner becomes Rs.1/- when the same reaches the ultimate purchaser of lottery tickets. Petitioner thus makes a value addition to the activity of organizing or conducting or promoting games of chance as that of lottery by the State Government from 70 paise to Rs.1/- by providing marketing and promotional service thereto by its activities as above. There is thus value addition by the petitioner in relation to game of chance, organized, conducted or promoted by the client of the petitioner namely, the State Government."

(VII) It is submitted that these observations denote correct interpretation of the law and are applicable with all force notwithstanding the deletion of the Explanation and introduction of the new provision akin to the Explanation. His submission is that the judgment though challenged before the Hon'ble Supreme Court is operative, there being no interim stay on it.

(VIII) To counter the above arguments, Mr. A. R. Madhav Rao, learned counsel appearing for the petitioner, submits that the activity of the petitioners of purchasing and selling the lottery tickets through its stockists and selling agents is a normal business activity of any purchaser of any goods. His submission is that the State has right to sell the tickets either itself or through distributors or selling agents and where the sale is absolute without any further prohibition on resale against the full sale consideration even to a distributor or a selling agent, the transaction is in the nature of sale and purchase and not between the principal and agent. It does not constitute an agency as submitted on behalf of the respondents. As regards the 30% discounted price of the lottery tickets carrying MRP Re.1/- is concerned, his contention is that 30 paise difference

between the MRP of the lottery ticket at Re.1/- and the purchase price of 70 paise, is not a commission but a discount to the petitioner. This discount is towards the establishment expenditure of business and margin of profit for the petitioners and their stockists/selling agents, which is a normal and common business practice in every case of sale and purchase in commercial parlance.

(IX) On the first question whether the appointment of the petitioner as a distributor can constitute an agency, it is submitted that where the distributor or the purchaser acts as a wholesaler on payment of the total sale price, he is a buyer and not an agent. In ***Pioneer Tools & Appliances Pvt. Ltd.*** v. ***Union of India*** **: (1989) 42 ELT 484**, it has been held as under:-

> **"**5. This judgment clearly demonstrates the fallacy of the reasoning adopted by the first respondent in the order passed in revision. Mr. R.L. Dalal, learned counsel for the respondents, however, laid emphasis upon the fact that Rallis India was described as the first petitioner's distributor. He referred me to the decision of the division bench of this court in Amar Dye-Chem Limited and another v. Union of India and another, 1981 E.L.T. 348. The court held that the distributor normally was an agent of the manufacturer for the purpose of distributing the goods to the consumers. He was not a buyer of the goods from the manufacturer on his own account and did not himself pay the price of the goods purchased before the goods were passed on to the consumer. But, merely by the use of the word 'distributor' in the list filed by the petitioner, it could not be said that the distributor was a related person. What was material was the real substance of the transaction. <u>If the distributor bought the goods and the price was the sole consideration of the sale and the transaction was at arms length, he could not be categorized as a related person. In the case of a buyer who purchased, the goods on payment of a commercial price, from the manufacturer and the transaction in effection was a</u>

> sale, such a buyer even though a kind of distributor was different from the distributor who acted as an agent of or on behalf of the manufacturer. In such a case the distributor was in fact the wholesale buyer and the property and the goods passed such a buyer. It is difficult to see how this judgment furthers the respondents' case. It is averred in the petitioner and, indeed, has been averred at all the times by the first petitioners before the authorities that they sold their products to Rallis India on an outright basis in a arms length transaction. There is no statement by the authorities which disputes this. There is no affidavit-in-reply which disputes the correctness of the averment made in the petition. It must, therefore, be accepted that this was the real nature of the transaction between them. This being so, it is immaterial that Rallis India is described as the distributor of the first petitioners." **[Emphasis supplied]**

(X) Above observations are sought to be applied to the present case on the basis of the agreemental stipulations which, *inter alia*, provide for payment of lump sum sale considerations for the entire financial year. Under Clause 4 of the Agreement the petitioner is required to pay Rs.10.00 crores p.a. as the minimum guaranteed amount to the State Government for purchase of the tickets irrespective of the fact whether petitioners suffer any loss or earn profit. The contractual stipulations noticed and discussed hereinabove further make it clear that the State Government has no concern with the further sale of the tickets by the petitioners except to comply the regulatory statutory provisions contained in the Lotteries (Regulation) Act, 1998 and rules made thereunder in public interest. The State Government is also not concerned with the amount of discount or margin of profit given by the petitioners to their stockists or selling agents. Rather condition 26 of

Agreement clearly stipulates that the State Government shall have no privity of contract with the stockists, selling agents or the ultimate purchaser of lottery ticket in the street and it shall be the absolute responsibility and liability of the purchaser, i.e. the petitioners, in case of any dispute or claim. As regards the return of the unsold tickets is concerned, the statutory rules framed under the Lotteries (Regulation) Act, 1998 and the contractual stipulations therefor is again a question of regulation to prevent any fraud, mischief or unlawful enrichment by the purchaser if any unsold ticket carries any price after the draw, apart from it being an established legal and permissible trade practice.

(XI) The distinction between an agent and a purchaser has been defined in ***Benjamin's Sale of Goods, 8th Edition*** in the following words: -

> **"**1-048. Sale distinguished from contract of agency. A supplier who agrees to procure goods from another may do so an the latter's agent or as a principal party in the relationship of a seller. The situation is parallel that already discussed in which the agreement is to manufacture and supply goods, the manufacturer may produce the goods on its own account and sell them when completed, or may be employed to work on the other party's behalf. A supplier who is a seller ordinarily contracts to supply the goods at an agreed price; this is an absolute undertaken and the actual cost to the supplier of the goods is irrelevant. A supplier who is an agent is merely bound to use due diligence to fulfill the order, although there is an obligation to obtain the goods as cheaply as is reasonably possible, and the agent's remuneration is normally by way of commission.
>
> ...

> 1-049. To determine the nature of the transaction in these cases, the whole agreement must be looked at: "the test is ultimately one of substance rather than form". There are certain indicators. It is not conclusive that the consignee should be described in the contract as an 'agent' or even 'sole agent', or conversely that the transaction should be called as 'sale', although the way in which the parties label the transaction will, typically, play a significant part in the court's determination of the issue. Certain stipulations may be consistent with both sale (and especially sale or return) and agency, and, therefore, cannot be taken as indicative of either: for instance, the transfer to the consignee of the property in goods shipped upon the acceptance of drafts; a provision that the property in goods shall remain in the consignor until disposed of; of the fact that the price of sale to third parties is fixed by the consignor. Exceptionally an agent may be remunerated by keeping the surplus over and above a specified price which is received on account of the principal, while the buyer may be paid a sum described as commission.
>
> It is, however, evidence towards a sale that the recipient is entitled to sell at whatever price the recipient thinks fit, accounting to the supplier only for a predetermined sum, and this interpretation is given further support if the recipient is free to alter or improve the goods. An agent, even a *del credere* agent, acts in accordance with the principal, and is normally remunerated by commission. The nature of the consignee's obligation to account to the consignor is perhaps the strongest indication. The consignee is probably an agent if there is an obligation to furnish particulars of sale and customers or to account periodically for the proceeds of sales. Otherwise the consignee is likely to be acting as a principal in the sales and this conclusion is reinforced where the consignee pays wholesale prices of goods. If when the consignee sells (whether for cash or on credit) to a retail purchaser, this immediately gives rise to a debt to the supplier for the listed price, the transaction is quite inconsistent with agency, including *del credere* agency, and consistent only with sale or return."

(XII) To same effect is the noted treatise on the attributes of agency by ***Bowstead & Reynolds on Agency, 16th Edition (1996)***.

> "1-030. Agent and seller; agent and buyer. The above discussion raises the distinction between agency and sale. These relationships, unlike the others dealt with above, are mutually exclusive: in respect of a particular transaction a person cannot be acting as agent if he is a buyer or seller to his principal and vice versa. Sale is a commercially adverse relationship; agency involves a fiduciary relationship of trust and confidence. The solution to commercial disputes may frequently turn on whether the parties are to be regarded as parties to one or the other relationship. Thus a manufacturer may contract not to market his goods through anyone but a particular supplier. Who is said to be 'sole' or

'exclusive agent'. If the supplier is on the true construction of the agreement a buyer from the manufacturer, the manufacturer may be in breach of contract if he sells the goods himself; but if the supplier is a true agent the manufacturer will usually be entitled to sell personally as well. If the supplier buys from the manufacturer and resells, it is he who answers to the ultimate buyer for the quality of the goods, and the manufacturer is liable. …

...

The distinction between agent and buyer for resale normally turns on whether the person concerned acts for himself to make such profit as he can, or is remunerated by pre-arranged commission. A supplier who himself fixes the resale price is likely to be a buyer for resale: but the fact that the resale price if fixed by the manufacturer does not necessarily make the supplier an agent, for resale prices are frequently fixed by manufacturers. Exceptionally a buyer for resale may also be paid commission, or an agent remunerated by being allowed to keep the excess over and above a stipulated price. But the making of such a profit by an agent would normally be improper.

Conversely, there may be difficulty in deciding whether a person who has agreed to procure goods for another is acting as that other's agent or selling to him. Again, the first question is to ask whether he takes a profit on the resale which will make him a seller, or a commission, in which case he is likely to be an agent and indeed the making of any further profit would usually be improper.**"**

(XIII) The Hon'ble Supreme Court in ***Alwaye Agencies*** v. ***Deputy Commission of Agricultural Income Tax*** **: 1998 (Supp) SCC 394**, has held as under: -

"6. In our opinion, since both the parties have proceeded on the footing that the transactions in question were effected pursuant to the said agreement, the primary task to which we must address ourselves is to examine whether under the agreement the assessee firm was an agent of the said company, or whether the assessee firm was really a purchaser of the goods which were booked by it. In this connection, it must be noticed that sub-clause (a) of clause 2 provides that the distributor has the right of the sale of the product within the stipulated area. Bulk supplies were effected in wagon-load or lorry-load by the said company direct to the consumer, but only provided that the distributor arranged the payment as per the agreement and also took the responsibility to bear entirely the resultant effects and risk from said direct despatches. It is true that the price at which the goods were to be sold to the customers was fixed by the company but that itself does not necessarily lead to the conclusion that the assessee acted merely as an agent of the said company. In fact, it is well settled that the mere

fact that the manufacturer fixes the sale price, by itself, cannot lead to the conclusion that the distributor is merely an agent. It is significant that under the agreement what the distributor got is described as a "rebate" and not as "commission". As one would normally expect in an agreement of agency. This is a factor which is by no means conclusive, but to a certain extent indicative of the relationship between the said company and the assessee. What is most important is, however, that the supplies were made to the distributor against payment either immediate or deferred as provided in the agreement, and even when the goods were destined directly to the customer, it was the distributor who had to guarantee to arrange the payment. Clause 8 makes it quite clear that the arrangement for effecting payment had to be made by the distributor either in cash or by demand draft or by irrevocable letter of credit in the company's favour negotiable against R/R or other documents of dispatch of goods. It is also significant that where there was some time lag between the sending of the goods and the payment, the goods were to be insured at the cost of the assessee. This circumstance, in our opinion, clearly shows that in respect of the goods despatched under orders placed by the distributors, the distributors really acted as purchasers of the goods which they in turn sold to the customers and does not merely act as agents of the said company. In respect of the goods in question which were despatched through public carriers, although the invoices were prepared in the names of the consumers of the goods, and the goods were consigned to the destination through public carrier booked to self, as pointed out by the Tribunal, the bills were endorsed and handed over to the assessee. When considered in the light of the agreement, these circumstances clearly show that in respect of these transactions the property in the goods despatched passed to the distributor on the bills being endorsed and handed over to the distributors."

(XIV) A similar view has been expressed by the Hon'ble Supreme Court in ***Gordon Woodroffe & Co.*** v. ***Shaik M.A. Majid & Co.*** **: AIR 1967 SC 181**.

"9. It is well-established that even an agent can become a purchaser when as agent pays the price to the principal on his own responsibility. In *Ex parte White, in re Nevil,* (1871) 6 Ch. 397 t & Co. were in the habit of sending goods for sale to N who was a partner in the firm of N & Co., but received these goods on his private account. The course of de3aling between T & Co. and N was that the goods were accompanied by a price list, N sold the goods on what terms he pleased, and each month sent to T & Co., an account of the goods he had sold, debiting himself with the prices named for them in the price list, and at the expiration of another month he paid the amount in cash without any regard to the prices at which he had sold the goods, or the length of credit he had given. On these facts it was held by

> the Court of Appeal in Chancery that though both the parties might look upon the business as an agency, N did not, in fact, sell the goods as agent of T & Co., but on his own account, upon the terms of his paying T & Co. for them at a fixed rate if he sold them, and the moneys he received for them were therefore his own moneys, which T & Co., had no right to follow.
>
> 10. A similar principle has been expressed in *W. T. Lamb and Sons v. Goring Brick Company, Ltd.* [1932] 1 K.B. 710. In that case, certain manufacturers of bricks and other building materials, by an agreement in writing, appointed a firm of builders' merchants as "sole selling agents of all bricks and other materials manufactured at their works". The agreement was expressed to be for three years and afterwards continuous subject to twelve e months' notice by either party. While the agreement was in force the manufacturers informed the merchants that they intended in the future to sell their goods themselves without the intervention of any agent, and thereafter they effected sales to customers directly. An action was then brought by the merchants for breach of the agreement. It was held by the Court of Appeal that the effect of the agreement was to confer on the plaintiffs the sole right of selling the goods manufactured by the defendants at their works, so that neither the defendants themselves nor any agent appointed by them, other than the plaintiffs, should have the right of selling such goods. It was also held that the agreement was one of vendor and purchaser and not one of principal and agent. Through the term 'agent' was used in the agreement, the Court of Appeal considered that the substance of the transaction was that the manufacturers sold their bricks to the so-called agent who in turn sold them on their own responsibility to customers. The price charged by the manufacturers to the sole selling agents was the ruling market price and the sole selling agents were allowed a deduction of 10 per cent by way of commission on that price, the manufacturers had no concern at what rate the sole selling agents sold the goods to customers, it was clear from these facts that the sale by the selling agents to customers was a transaction in which the manufacturers were not interested and there was no privity of contract between the manufacturers and the ultimate purchasers."

(XV) In furtherance of his submission on the above questions, Mr. A. R. Madhav Rao, Ld. Counsel appearing for the petitioner, has also produced a Model Agreement circulated by the Ministry of Home Affairs, Government of India, vide its letter dated 28.12.2011 to all the Chief Secretaries of States to be signed by the State Government

and agent for running the lottery business including Online lottery. Referring to some of the conditions of this Agreement, it is stated that mutual arrangement between the State Government organising and conducting lottery business and the distributor/agent referred to under the provisions of the regulatory law and the rules made thereunder is also understood by the Government of India as that of a seller and purchaser and it is in that context that the conditions/arrangement between the State Government and the distributor have been settled. In particular, reference has been made to the following -

> "
> ……
>
> 8.1 The Agent shall purchase the lottery tickets from the Government and payments shall be made by the Agent to the Government for such tickets.
>
> ……
>
> 11.1 Minimum guaranteed revenue of the Government of State of <<.>> shall be Rs.<<… crores>> upto the turnover of Rs. <<… crores>> per annum.
>
> 11.2 On additional turnover over and above Rs.<<… crores>>, the Agent shall pay of <<… %>> of the additional turnover to the Government.
>
> ……
>
> 13.1 The Agent may use all necessary advertisement and promotion to create and enchance the image for the Lottry schemes (Online and Paper Lotteries) of the State of <<…..>>. These shall include coverage through press and advertisement and promotion through direct mail and publicity through events like road shows etc.
>
> 13.2 All publicity in respect of the lotteries shall be at the option of the Agent. However, the Agent shall ensure that the manner in which the lotteries of the State are portrayed in written,

visual or electronic media do not tarnish the image of the Government.

13.3 All costs towards such publicity shall be exclusively borne by the Agent.

……

16.3 The Government shall not ordinarily interfere in the internal administration of the Agent's office established but reserves the right to inspect periodically, to ensure that no activities are carried out to the detriment of the interest of the Government.

……."

This Model Agreement is said to have been circulated by the Central Government in exercise of its power under Section 10 of the regulatory Act, wherein the Central Government is entitled to give directions to the State Government to carry out the provision of the Lotteries (Regulation) Act, 1998 and the rules made thereunder.

(XVI) Admittedly, this Circular issued in December, 2011 has not been enforced so far and at least the State of Sikkim has not desired the Model Agreement to be executed by the petitioners. This Agreement thus cannot render much assistance to the petitioner. Mr. Rao, however, submits that the Agreement may not be construed to lay down any condition of contract between the State Government and the petitioner, nonetheless, it does indicate the intention of the Central Government in what manner the provisions of the regulatory law and the rules made thereunder have been understood and interpreted by the Central Government, the State Government as also the distributor appointed by the

State. His submission is that all the lottery organising States like Sikkim and Kerala have entered into similar kinds of agreements with their distributors wherein the relationship between the State Government organising lottery and the distributors are that of a seller and buyer and not principal and agent. There is absolutely no dispute that from the nature of arrangement made between the State Government and the petitioner, who is termed as a distributor, it is evident that the State Government is selling its entire lot of lottery tickets published by it through the distributor (petitioner) for minimum guaranteed sale price with complete liberty to the distributor, the purchaser of the lottery tickets to further sell it by appointing selling agents, sub-agents etc. without any interference by the State Government except to monitor the adherence of the regulatory provisions contained in the Regulatory Act and the rules made thereunder.

(XVII) Another related issue raised by the respondents is that the mutual arrangement between the State Government and the distributor for re-purchase of the unsold lottery tickets and refund thereon goes against the very concept of the sale and purchase of goods. To appreciate, it is necessary to understand the basis for such

stipulation. Firstly, the re-deposit of the unsold lottery tickets is a statutory requirement under Sub-rule (5) of Rule 4 of the Rules framed under the Act and additionally, the object is to prevent any fraudulent claim of the prize money on any unsold ticket by the distributor or its selling agent etc. Secondly, such an arrangement is legally permissible in case of sale of goods, which, in normal and common trade practices, is known as "on sale or return". Mr. Rao submits that it is one of the recognized modes of sale where unsold goods can be returned to the manufacturer or the seller and such an arrangement does not tamper with the concept of sale and purchase. He has referred to the well-known commentary of ***Benjamin's Sale of Goods, 8th Edition,*** which reads as under: -

> **"5-041. Approval or on sale or return.** The rule requires that the goods must have been delivered to the buyer "on approval or on sale or return or other similar terms". Goods will be considered to have been delivered on approval where it is agreed by the parties that they shall be retained and purchased by the buyer at the notified prices if he approves them, but not if they are disapproved. The meaning of a contract 'on sale or return' is that the goods are to be taken as sold at the option of the buyer, if not previously rejected, unless returned to the seller within the time fixed by the contract or within a reasonable time. A contract can be one on sale or return whether or not the recipient of the goods under the contract intends to buy them himself or sell them to third parties. Goods are delivered on 'other similar terms' where, for example, they are sent on trial or on approbation. But, in order to bring a transaction within this rule, the circumstances must show that the buyer has an option to purchase on the statutory terms, that is to say, if and when the specific acts or conduct on his part set out in the rule have occurred. For this reason, it is necessary to distinguish certain closely related forms of transaction where a different intention appears."

(XVIII) The sum and substance of the above discussion is that once the transaction between two contracting parties involves only sale and purchase including "on sale or return", the relationship is simply that of a seller and purchaser, it does not constitute any service. In **Bharat Sanchar Nigam Ltd. & Anr.** v. **Union of India & Ors. : *(2006) 3 SCC 1***, it has been held as under: -

> **"** **88.** No one denies the legislative competence of the States to levy sales tax on sales provided that the necessary concomitants of a sale are present in the transaction and the sale is distinctly discernible in the transaction. This does not however allow the State to entrench upon the Union List and tax services by including the cost of such service in the value of the goods. Even in those composite contracts which are by legal fiction deemed to be divisible under Article 366 (29-A), the value of the goods involved in the execution of the whole transaction cannot be assessed to sales tax. As was said in *Larsen & Toubro* v. *Union of India* : (SCC p.395, para 47)
>
> > "The cost of establishment of the contractor which is relatable to supply of labour and services cannot be included in the value of the goods involved in the execution of a contract and the cost of establishment which is relatable to supply of material involved in the execution of the works contract only can be included in the value of the goods."
>
> **89.** <u>For the same reason the Centre cannot include the value of the SIM cards, if they are found ultimately to be goods, in the cost of the service.</u> As was held by us in *Gujarat Ambuja Cements Ltd.* v. *Union of India,* SCC at p.228, para 23:
>
> > "This mutual exclusivity which has been reflected in Article 246(1) means that taxing entries must be construed so as to maintain exclusivity. Although generally speaking, a liberal interpretation must be given to taxing entries, this would not bring within its purview a tax on subject matter which a fair reading of the entry does not cover. If in substance, the statute is not referable to a field given to the State, the court will not by any principle of interpretation allow a statute not covered by it to intrude upon this field.".**"**

(XIX) In ***Imagic Creative (P) Ltd.*** *v.* ***Commissioner of Commercial Taxes & Ors.*** **: (2008) 2 SCC 614**, while considering the question of levy of service tax as also VAT on a transaction, it has been held that payment of service tax as also VAT are mutually exclusive and both the kind of taxes can be levied in a composite transaction having regard to the respective parameters of service tax and the sales tax. The relevant observations are made in the following paragraph:

> **"**32. Payments of service tax as also VAT are mutually exclusive. Therefore, they should be held to be applicable having regard to the respective parameters of service tax and the sales tax as envisaged in a composite contract as contradistinguished from an indivisible contract. It may consist of different elements providing for attracting different nature of levy. It is, therefore, difficult to hold that in a case of this nature, sales tax would be payable on the value of the entire contract, irrespective of the element of service provided. The approach of the assessing authority, to us, thus, appears to be correct.**"**

(XX) In ***Indian Railways C. & T. Corpn. Ltd.*** v. ***Govt. of NCT of Delhi*** **: 2010 (20) S.T.R. 437 (Del.)**, the question before Delhi High Court was whether the supplier of food and beverages to the Railways for consumption of passenger travelling therein includes the element of service and subject to levy of service tax. Considering this question, Delhi High Court observed as under:

> **" 4.** The next question raised is with regard to the respondent's liability for service tax on collections for disposal of garbage. Even though there is no written agreement for the collections, the Tribunal, on facts, found that the charges represent value for the materials sold and

> not for any service rendered by the respondent. So much so, we do not find any ground to interfere with the Tribunal's order vacating the service tax demands from the respondent for the collections and from the parties referred above. We do not find any merit in the appeals filed by the Department. Consequently, the appeals are dismissed."

(XXI) From the discussion and consideration of judgments noticed hereinabove, it clearly emerges that where the transaction is purely that of sale and purchase and does not involve any component of service in it, which cannot be clearly segregated and discernible, no service tax is payable. However, where two components in a transaction, i.e. "sale" and "service", are capable of compartmentalisation so as to segregate the element of service from the transaction of sale, service tax may be leviable on the service component in a transaction.

(XXII) Another related question that was forcefully and vehemently argued on both the sides was regarding the amount of discount provided on the MRP of the lottery ticket. Both the sides have argued on this issue in their own manner. At the cost of repetition, Mr. Farooq Md. Razzak, Addl. Solicitor General submits that a 30% discount on the lottery ticket granted to the petitioner is by way of commission in lieu of the services rendered by it to the State Government. To the contrary it has been urged on behalf of the petitioners that the 30% discount on MRP i.e. the

actual/final sale price meant for the last purchaser, is in fact a normal business discount in any transaction of sale. His further submission is that none of the activities of the petitioner amounts to rendering any service to the Government nor is there any consideration received by the petitioner from the Government for such activities. On the contrary, the petitioner is paying the sale consideration and other amounts on regular draws leviable under law to the Government. Undisputedly, the MRP for a lottery ticket organized by the State of Sikkim is Re.1/- and the same is sold to the petitioner on a discounted price of 70 paise in bulk. However, the petitioner is under contractual obligation to pay minimum guaranteed price of Rs.10.00 crores per year. It is argued that since the unsold tickets are required to be returned to the Government, there is no absolute sale. It is also stated that clause 20, which grants liberty to the purchaser to take up any kind of publicity for the sale of the lottery tickets through electronic media or any other mode, further suggests that the petitioner is facilitating the organisation of the lottery, its promotion and sale in various parts of the Country. According to Mr. Razzak, this, in true spirit, constitutes a service for which the petitioner is getting 30% commission by way of discounted price. Opposing this contention, the petitioner's case is that the 30% discounted

price is for the purposes of the petitioner and his stockists/sellers profit components and other expenditure that would be incurred for sale of the lottery tickets. According to Mr. Rao, the discounted price in any sale transaction is normal and common business practice between a seller and a purchaser. After the lottery tickets are printed by the State Government, the same are required to be delivered to the petitioner at the agreed destination in terms of clause 13 of the Agreement and thereafter, it is the sole responsibility of the petitioner to sell the lottery tickets through stockists, selling agents or retail sellers as may be deemed convenient and the State Government can neither interfere with nor have any control over the stockists and selling agents appointed by the petitioner. Thus the State Government receiving the minimum guaranteed price sits pretty safe without any liability for profit or loss as the case may be. It becomes the exclusive responsibility of the petitioner to sell the tickets and, even if the petitioner is unable to sell the entire lot and sale proceeds of the sold tickets are less than the minimum guaranteed price paid by it to the Government, the Government is not liable to refund any part of the sale consideration including the unsold tickets. It is contended on behalf of the petitioner that after the purchase of the tickets, the petitioner becomes the sole

owner of the lottery tickets with liberty to re-sell according to its own scheme and management. The discounted amount is to be distributed as component of profit and expenditure by the petitioner, his stockists, selling agents and retail sellers. The advertisement for the lottery is not being made for the benefit of the State but for promotion of petitioner's own business activity. Rather than being reimbursed with the amounts spent for such advertisements, clause 20 of the Agreement clearly stipulates that the petitioner shall be liable for incurring all expenses for the advertisements and, even the result is to be published by the petitioner at its own expense. It is thus submitted by Mr. Rao that unless there is a consideration for services rendered, it would not fall within the meaning of "taxable service" as defined under clause (zzzzn) to Sub-section (105) of Section 65, which prescribes that the service provided by one person to another necessarily has to be for consideration. It is stated that the petitioner is not rendering any service to the Government rather it is promoting its own business interest and the State Government is not paying any consideration in any form whatsoever to the petitioner for such promotional and sale activities and such activities are primarily for the benefit of the petitioner though enhanced sale is beneficial to State as

well. According to Mr. Rao, the discounted amount cannot be said to be a consideration for services, particularly, when it is optional for the petitioner to make any advertisement.

(XXIII) In ***Mahindra and Mahindra Ltd.*** v. ***Union of India & Anr.*** reported as **1984 (16) E.L.T. 76 (Bom.)**, it has been held that where distributor purchases goods on payment of a commercial price from the manufacturer, such a buyer is different from a distributor and does not create an agency. The relevant observations are noticed hereunder:-

> " **10.** Shri Dalal submitted that the agreement between the petitioners and Voltas is really not a distributorship agreement but is in the nature of agreement agency. The learned counsel relied upon Division Bench decision of this Court in the case of *Amer Dye-Chem Limited and another* v. *Union of India and another* reported in 1981 Excise Law Times, 348 and submitted that the mere use of the word 'Distributor' would not lead to the conclusion that the agreement is not an agreement of agency. The Division Bench observed that the distributor in the commercial world is understood to be person who distributes goods of the manufacturer to the consumer and in so doing he acts for and on behalf of the manufacturer. The distributor normally is, therefore, an agent of the manufacturer for the purpose of reaching out the goods to the consumers. Shri Dalal relied upon this observation and claims that Voltas were merely acting as Agents of the petitioners for reaching out the tractors to the consumers. The submission is not correct, as the Division Bench has further observed in the judgment that in the case of the buyer who purchases goods on payment of a commercial price to the manufacturer and transaction in effect is a sale, such a buyer is different from the distributor earlier noticed, though even such a buyer is sometimes described as a distributor. The distributor in such a case is in fact a wholesale buyer and the property in the goods passes to such a buyer. The submission of Shri Dalal, therefore, that as the agreement between the petitioners and the Voltas was described as a distributorship agreement, it should be treated as an agreement of agency cannot be accepted.
>
> **11.** Shri Dalal then submitted that under the agreement, the Voltas were required to carry out the activities of the manufacturers and, therefore, want the petitioners intended to do was to transfer some of the

activities of the manufacturers to Voltas with a view to reduce the assessable value for the purpose of excise. In support of this submission, reliance is placed on three or four conditions under the agreement. It was urged that the Voltas were required to maintain a Sales Organisation and such a condition was not necessary in the agreement if the petitioners had sold the tractors to Voltas because then it was wholly irrelevant to provide as to how the Voltas should dispose of those tractors to the consumers. The condition under the agreement which provides that Voltas were to store the tractors till they are sold to the consumers was also relied upon to claim that the agreement was not at arms length. The provision which required Voltas to carry out afte4r-sale service and the condition which required the petitioners to share half the amount spent on advertisements were highlighted to claim that the price for which the tractors were sold to Voltas did not reflect the true price. It was urged that the price at which the tractors were sold by the petitioners to Voltas was far less than the market price because certain activities required to be performed by the manufacturers were taken over by the Voltas. It is not possible to accept this submission. In the first instance, on the date when the agreement was entered into, the tractors were not liable to be assessed for excise duty and, therefore, there was no occasion to prepare an agreement with an intention to avoid the duty. Secondly, the conditions requiring Voltas to set up Sales Organisation and to provide after-sale service are the usual conditions provided in the agreement with the wholesale buyer and such conditions were also in existence in the agreement which was considered by the Supreme Court in the *Voltas'* case. The fact that the Voltas were required to store the tractors till they are sold to the consumers cannot be treated as transfer of manufacturer's activity in favour of the buyer. The fact that the expenses in regard to the advertisements were to be shared by the petitioners and Voltas merely indicate that both the wholesale buyer and the petitioners were interested in having greater production and sale thereof and that condition, in my judgment, cannot be considered as relevant to reach the conclusion that the agreement was not at arms length.**"**

(XXIV) In ***Pioneer Tools and Appliances (P) Ltd.*** v. ***Union of India*** **: 1989 (42) E.L.T. 384 (Bom.)**, it has been held as under:-

"5**.** This judgment clearly demonstrates the fallacy of the reasoning adopted by the first respondent in the order passed in revision. Mr. R. L. Dalal, learned counsel for the respondents, however, laid emphasis upon the fact that Rallis India was described as the first petitioner's distributor. He referred me to the decision of the division bench of this court in *Amar Dye-Chem Limited and another* v. *Union of India and another,* 1981 E.L.T. 348. The court held that the distributor normally was an agent of the manufacturer for

> the purpose of distributing the goods to the consumers. He was not a buyer of the goods from the manufacturer on his own account and did not himself pay the price of the goods purchased before the goods were passed on to the consumer. But, merely by the use of the word 'distributor' in the list filed by the petitioner, it could not be said that the distributor was a related person. What was material was the real substance of the transaction. If the distributor bought the goods and the price was the sole consideration of the sale and the transaction was at arms length, he could not be categorized as a related person. In the case of a buyer who purchased, the goods on payment of a commercial price, from the manufacturer and the transaction in effection was a sole, such a buyer even though a kind of distributor was different from the distributor who acted as an agent of or on behalf of the manufacturer. In such a case the distributor was in fact the wholesale buyer and the property and the goods passed such a buyer. It is difficult to see how this judgment furthers the respondent's case. It is averred in the petition and, indeed, has been averred at all the times by the first petitioners before the authorities that they sold their products to Rallis India on an outright basis in a arms length transaction. There is no statement by the authorities which disputes this. There is no affidavit-in-reply which disputes the correctness of the averment made in the petition. It must, therefore, be accepted that this was the real nature of the transaction between them. This being so, it is immaterial that Rallis India is described as the distributor of the first petitioners."

(XXV) In ***Philips India Ltd.*** v. ***Collector of Central Excise*** **: (1997) 91 E.L.T. 540**, it has been held as under:-

> "**6.** As to the after sales service that the dealer was required under the agreement to provide, it did of course enhance in the eyes of intending purchasers the value of the appellant's product, but such enhancement of value ensured not only for the benefit of the appellant; it also ensured for the benefit of the dealer for, by reason thereof, the dealer got to sell more and earn a larger profit. The guarantee attached to the appellant's products specified that they could be repaired during the guarantee period by the appellant's dealers anywhere in the country. Thus, though one dealer might have to repair goods sold by another dealer and incur costs in that regard, he also had the benefit of having the goods he sold reparable throughout the country. The provision as to after sales service, therefore, benefitted not only the appellant; it was a provision of mutual benefit to the appellant and the dealer."

(XXVI) Similarly, in ***Collector of Central Excise, Baroda*** v. ***Besta Cosmetics Ltd.*** reported as **2005 (183)**

E.L.T. 122 (SC), it has been held that the clause of advertisement being purely optional would not militate against the price which is at arm's length. The following observations are relevant: -

> **"** **2.** In addition, we may note that the relevant clause in the agreement between the assessee and its Marketing Agent relating to advertisements reads as follows (wherein the marketing agent is referred to as BHPL) :
>
> > "BHPL shall market the said product in the trade name or the trademark of BCL in respect of the said product. BHPL may, at its own free will, make it known generally that the products of BCL are marketed by them. BHPL for this matter, may adopt such ways and means and may incur such expenses on Advertising and Business promotion as it may deem fit and necessary. At the same time, BHPL should ensure that it does not infringe or in any way prejudicially effect the trade name and or trademark of the said product."
>
> **3.** The appellant has sought to rely upon the decision of this Court in *Commissioner of Central Excise, Surat* v. *Surat Textile Mills Ltd.* – 2004 (5) SCC 201. In that decision the Court appears to have upheld the view that where the advertisement cost is incurred by the manufacturers/customers compulsorily or mandatorily, and where the manufacturer has an enforceable legal right against the customers to insist on incurring of such advertisement expenditure by the customers, the advertisement cost would be includible in the assessable value. Without in any fashion affirming the view taken therein it is clear even on the basis of the judgment that the clause in question gave the manufacturers/marketing agent, the discretion whether or not to advertise the assessee's products. There was no 'enforceable legal right' with the assessee to insist on the advertisement under the agreement.**"**

(XXVII) A question whether discount granted by the State of Kerala on sale of lotteries to distributors was in the nature of commission liable to income tax deduction at source under Income Tax Act came to be considered by High Court of Kerala in the case of ***Commissioner of Income Tax, Thiruvananthapuram v. M. S. Hameed.*** It has been held

that the relationship between the distributors in the trade of lottery as being one of principal to principal and the discount of lottery is not a commission, the provision of Section 194(G) of the Income Tax Act, 1961 which obliged a person to deduct tax at source on payment of commission, will not be attracted. The relevant extract of the judgment is reproduced hereunder:-

> "4. The petitioners receive in bulk quantities of lottery tickets from the State Government. They are given a discount which is on a slab system. Exhibit P-1 is the governing order issued in 1998. The agents commission presently payable is as follows:
>
> . For the purchase of 100 tickets 25%
>
> . For the purchase of 101 and above 27.5%
>
> . For the purchase of 50,001 and above 28%
>
> . For the purchase of 70,00,001 and above 28.5%
>
> 5. The import of the order will be that for a ticket worth Re. 1 an agent need pay between 75 paise to 71.5 paise only, depending on the off take. The petitioner submits that there is no agency agreement, and the petitioners are termed as agents only on a loose basis. From the nature of the transactions, the Government and the petitioners deal as principal to principal. The tickets purchased are thereafter distributed through other agents, and sub-agents, according to them, on commission basis. They point out that after purchase of the tickets, it is not the Government's look out as to how and when they are divided or distributed, and there is no control over the affairs thereafter. Therefore, the principal contention of the petitioner is that there is only payment of the price of the tickets fixed as payable by the principal, and no commission or discount are paid to them by the Government. As such, it is the contention of the petitioners that Section 194G of the Act has no application, and hence the demand of tax, as coming through exhibit P-4 is unsustainable and without jurisdiction.
>
> .....
>
> 7. Before exhibit P-4, the deduction of ten per cent, was not being made, and the petitioners submit that thereafter the tax deduction has commenced. The submission of Mr. K. R. Prasad, senior counsel, appearing on instructions, for the petitioners, could be summarized as following: The provisions for collection and recovery of Income Tax appearing in Chapter XVII of the Act refers to various methods, viz., deduction at source, collection at source,

advance payment of tax, collection by recovery and levy of interests, etc. Since Section 194G comes within the sub-heading "Deduction at source", for the mechanism, according to counsel, a statutory authorization is essential. When the petitioners purchase tickets, they became absolute owners thereof. He also referred to Rule 25 of the Kerala State Lottery Rules, to the effect that in the case of loss of tickets, no compensation was payable. The petitioners were never agents of the State, and in no capacity, render any service to the State. For the face value of a ticket of Rs. 1, the petitioners were expected to pay 71.5 paise and they could have purchased a ticket worth one rupee by raising only 71.5 paise. That the ticket might be worth one rupee did not mean that the balance of 28.5 paise was the petitioner' income. Referring to the text book (Kanga and Palkiwala on Income-tax) (page 92, 7th edition) he referred to the discussion based on the authorities to urge that mere relief from expense cannot be income. A person is chargeable to tax not on what he saves in his pocket, but what goes into his pocket. Counsel urged that Section 194G, as it stands in the statute book, cannot have application to the petitioners, as has been attempted to the explained by exhibit P-4.

.....

16 If the face value of the ticket, for example, is Re. 1, notwithstanding the circumstance the petitioners receive it for 72 paise. The State, therefore, releases a ticket, receiving 72 paise. The petitioner may sell the ticket so obtained at any price of their choice. It is not the State's business to enquire into the matter at all. Therefore, it is difficult to assume that the petitioners have in all cases made a margin of 28 paise by the mere purchase of the ticket. His case is that resells it for 72.5 paise, and he derives a profit of half paise per ticket. He may be right or that may be a misleading statement. But he has been able to obtain a ticket worth Re. 1 for 72 paise. His total input therefore is 72 paise, and in that context it is difficult to describe the transaction as one whereby because of investment of 72 paise he has simultaneously made a profit of 28 paise. Several "ifs" have to be employed, which do not exist in real life, for this court to accept the case of the Department that by the factum of purchase he had already made a profit.

.....

23. Therefore, the demand of tax is to be shown as one on the income of the person concerned. There is neither payment of cash or by cheque, and the Government never credits any income to the account of the persons like the petitioners. When the deduction is contemplated at the time of payment to the person concerned and when it is shown that there is no payment to the agent at the time of purchase of the ticket, the section automatically becomes inapplicable. If any prize or remuneration is payable by the Government, to any person, deduction at source as envisaged under the section, may arise. But when no payment is made in view of the mandate of the section, no deduction is envisaged. That the ticket is given on a discount of 28 per cent., can by no imagination be pressed into service for an interpretation that, none the less, ten per cent, of 28 paise is deductible as tax. Perhaps the intention

might have been to bring the agents within the tax net, but the section as it stands, according to me, is not authority for taxation at source, as is envisaged by exhibit P-4.**"**

This decision has been upheld by a Division Bench of Kerala High Court and SLP filed against it already stands dismissed.

(XXVIII) Delhi High Court in ***Commissioner of Income Tax*** v. ***Jai Drinks Pvt. Ltd.*** reported as **2011 (336) ITR 383 (Del.)** expressed similar view and observed as under: -

"3. A survey was conducted under Section 133A of the Act and the assessing officer passed an order holding that the payment made by the Assessee to the distributor constituted commission under Section 194H of the Act. The assessing officer held that the Assessee defaulted in not deducting the tax at source on the amount of commission paid to the distributor and consequently, determined the total tax liability of Rs.40,06,679/- under Section 201(1) & 201 (1A) of the Act. Assessee preferred an appeal before the Commissioner of Income Tax (Appeals) (hereinafter referred to as Commissioner (Appeals) which was allowed. The Commissioner (Appeals) held the payments made by the Assessee as incentives in the normal course of buying and selling. The revenue preferred an appeal against this order before the ITAT which was dismissed holding that the nature of transaction between the Assessee and the distributor is not that of principal-agent, but principal-to-principal and that the payment given by Assessee to the distributor is nothing but a discount and did not have the characteristics of commission.

.....

9. From all that has been noted above, it is evident that the distributor was to purchase products at pre-determined price from the Assessee for selling the same within specified area. The products were to be purchased by the distributor against 100% advance payment or may be some times on credit at the discretion of the Assessee. Both the Assessee and the distributor have been collecting and paying their sales tax separately. Both the parties have clearly understood and accepted the agreement between them. That being the arrangement between the Assessee and the distributor, it could not be said that the relation between them was that of principal-agent. On the other hand it was clearly stipulated to be an agreement between them on principal-to-principal basis. Both the Commissioner (Appeals) and also the ITAT rightly held that the payments being made by the Assessee to the distributor were

incentives and discounts and not commissions. We find no infirmity in the findings of the Commissioner (Appeals) and also ITAT.”

(XXIX) It is the common case of the parties that the service tax has been levied vide Finance Act, 1994 as amended in 2010 by introducing organization, promotion of lottery etc. as a taxable service. Section 66 prescribes 12% as the rate of service tax of the value of the taxable service whereas Section 67 deals with valuation of taxable services for charging service tax. The relevant extract of both the sections are reproduced hereunder: -

“ **66. Charge of service tax**

There shall be levied a tax (hereinafter referred to as the service tax) at the rate of twelve per cent of the value of taxable services referred to in sub-clauses ……
……
……..

(zzzzn) ……. of clause (105) of section 65 and collected in such manner as may be prescribed.

67. Valuation of taxable services for charging service tax.- (1) Subject to the provisions of this Chapter, where service tax is chargeable on any taxable service with reference to its value, then such value shall,—

(i) in a case where the provision of service is for a consideration in money, be the gross amount charged by the service provider for such service provided or to be provided by him;

(ii) in a case where the provision of service is for a consideration not wholly or partly consisting of money, be such amount in money as, with the addition of service tax charged, is equivalent to the consideration;

(iii) in a case where the provision of service is for a consideration which is not ascertainable, be the amount as may be determined in the prescribed manner.

(2) .....

(3) .....

(4) .....

Explanation.—For the purposes of this section,—

(a) "consideration" includes any amount that is payable for the taxable services provided or to be provided;

(b) .....

(c) ....."

(XXX) Rule 6 of the Service Tax Rules, 1994 provides modes for payment of service tax. The Government of India issued Notification No. 49/2010-Service Tax dated 8th October, 2010 introducing sub-rule 7(C) under Rule 6 providing for the mode of payment of service tax as regards the promotion, marketing, organizing or in any manner assisting in organizing lottery is concerned. The relevant extract of the said Rule reads as under: -

"(7C) The distributor or selling agent, liable to pay service tax of promotion, marketing, organizing or in any other manner assisting in organizing lottery, shall have the option to pay an amount at the rate specified in column (2) of the Table given below, subject to the conditions specified in the corresponding entry in column (3) of the said Table, instead of paying service tax at the rate specified in section 66B of Chapter V of the said Act:

Table

Sl. No.	Rate	Condition
(1)	(2)	(3)
1.	Rs.7000/- on every Rs.10 Lakh (or part of Rs.10 Lakh) of aggregate face value of lottery tickets printed by the organizing State for a draw	If the lottery or lottery scheme is one where the guaranteed prize payout is more than 80%
2.	Rs.11000/- on every Rs.10 Lakh (or part of Rs.10 Lakh) of aggregate face value of	If the lottery or lottery scheme is one where the guaranteed prize

	lottery tickets printed by the organizing State for a draw.	payout is less than 80%

Provided that in case of online lottery, the aggregate face value of lottery tickets for the purpose of this sub-rule shall be taken as the aggregate value of tickets sold, and service tax shall be calculated in the manner specified in the said Table.

Provided further that the distributor or selling agent shall exercise such option within a period of one month of the beginning of each financial year and such option shall not be withdrawn during the remaining part of the financial year.

Provided also that the distributor or selling agent shall exercise such option for financial year 2010-11, within a period of one month of the publication of this sub-rule in the Official Gazette or, in the case of new service provider, within one month of providing of such service and such option shall not be withdrawn during the remaining part of that financial year. **"**

The petitioners' case falls in Sl. No. 2, the prize money being less than 80%.

(XXXI) On a conjoint reading of Sections 66, 67 and Rule 7(C) it appears that the service tax payable by a service provider for promotion, marketing, organizing or in any manner assisting in organizing lottery is @ 12% or assessed in the manner indicated in the table above on the value of the service provided or to be provided. In respect of the online lotteries the aggregate value of the lottery ticket is to be taken as the value of the service on which service tax is payable. In respect to the paper lottery also the same mode has been adopted and gross value of the lottery ticket has been taken as the valuation for the purpose of levy of service tax. During the course of argument, Mr. Razzak

after seeking instructions admitted that the service tax is being charged at the gross value of the lottery ticket i.e. Re.1/- or in the manner prescribed in the Rule 7(C) as introduced vide Notification dated 8th October, 2010. It is relevant to note that according to Mr. Razzak's submission the 30% discount allowed by the State Government to the petitioners is for rendering service, whereas admittedly 70 paise is the price of the lottery ticket. According to respondents own case only 30% of the gross value can be taken as the valuation for providing service if at all the activity of petitioners is to be construed as a service falling within the definition of "taxable service". The Ministry of Finance (Department of Revenue), Central Board of Excise and Customs, Government of India has also issued a clarificatory circular dated 10.11.2006 laying down the criterion for levy of service tax. The relevant extract is reproduced hereunder:-

> "4. To levy service tax, the following criteria are to be satisfied:
>
> - The service provided or to be provided satisfies the definition of taxable service.
> - There should be receipt of consideration for the taxable service provided."

(XXXII) In view of the above clarification, it is pleaded on behalf of the petitioners that receipt of consideration for providing "taxable service" is one of the essential ingredients

to establish that any service is a “taxable service”. It is submitted that in the instant case, the Government does not pay any consideration in any form for the activities to be performed by the petitioner for promotion of the sale by advertisement etc. To the contrary, the petitioner is paying the minimum guaranteed sum towards the full sale consideration to the Government and thus the entire claim of the respondents that the petitioner is providing taxable service is belied by its own circular and understanding of the nature of the petitioner’s activity.

GROUND (B)

(I) This ground comprises of different limbs, i.e.

(i) whether the conduct of lottery is an Act of “Betting and Gambling” envisaged under entries 34 and 62 of List II to Schedule 7;

(ii) whether it is within the exclusive domain of State legislature to impose taxes on organising lotteries being an act of “Betting and Gambling”;

(iii) whether the Parliament has the competence to enact law in exercise of its residuary legislative power under entry 97 of List I to Schedule 7 dehors the entries 34 and 62 of List II;

(iv) whether the State legislature and Parliament both can simultaneously impose taxes on the conduct of lottery by the State Government under entry 62 of List II and entry 97 of List I to Schedule 7, if so, under what circumstances; and

(v) whether such circumstances exist in the case in hand?

(II) We would like to deal with each limb of Ground-B separately.

(i) <u>whether the conduct of lottery is an Act of "Betting and Gambling" envisaged under entries 34 and 62 of List II to Schedule 7</u>

(a) "Lottery" has been defined under Section 2(b) of the regulatory Act of 1998, which reads as under:-

> **"**(b) "lottery" means a scheme, in whatever form and by whatever name called, for distribution of prizes by lot or chance to those persons participating in the chances of a prize by purchasing tickets;**"**

From the above definition, it transpires that lottery is a game of chance of those persons who participate in the chances of a prize by purchasing tickets. The expressions "betting and gambling" have been defined in the Black's Law Dictionary separately in the following manner: -

> **"betting** – A system of gambling in which bets placed on a race are pooled and then paid to those holding winning tickets.**"**
>
> **"gambling** – The act of risking something of value, esp. money, for a chance to win a prize.**"**

Above definitions include any act by which a person participates in a game of chances by risking money for purchase of ticket to win a prize. From these definitions and the definition of lottery under the regulatory Act, it is apparent that lottery is also a game of chance where a ticket-holder risks his money to win a prize on a chance. Section 294A of the IPC punishes a person who keeps any office or place for the purpose of drawing any lottery or even the proposal to pay any money or to deliver any goods on any event or contingency of any ticket or any figure in the lottery as an offence except where it is run or authorized by the State Government. The lottery, *per se*, does fall within the expressions "betting and gambling" which Act is pernicious in nature. It gets a legal umbrella only if it is run or authorized by the State Govt. subject to the conditions enumerated under Section 4 of the Lotteries (Regulation) Act, 1998. It is a privilege of the State which can be partially parted to any other person subject to the performance of statutory conditions contained in the regulatory Act.

(b) Lottery has been declared to be falling within the expressions "betting and gambling" by the Hon'ble Supreme Court in **B*. R. Enterprises*** v. ***State of U.P. & Ors.* :**

(1999) 9 SCC 700. The relevant observations are quoted hereunder:-

> **" 64.** For this, we revert to scrutinize as to what made lotteries gambling and how State lotteries cleanses this character. As we have already recorded, the difference between gambling and trade is that gambling inherently contains a chance with no skill, while trade contains skill with no chance. What makes lottery pernicious is its gambling nature. Can it be said that in the State-organised lotteries this element of gambling is excluded? There could possibly be no two opinions that even in the State lotteries the same element of chance remains with no skill. It remains within the boundaries of gambling. The stringent measures and the conditions imposed under the State lotteries are only to inculcate faith in the participant of such lottery, that it is being conducted fairly with no possibility of fraud, misappropriation or deceit and assure the hopeful recipients of high prizes that all is fair and safe. That assurance if from stage one to the last with full transparency. No doubt, holding of the State lotteries for public revenue has been authorised, legalised and once this having been done it is expected from the State to take such measure to see that people at large, faithfully and hopefully participate in larger number for the greater yield of its revenue with no fear in their mind. The Act further ensures by virtue of Section 4(d) that the proceeds of the sale of such lottery tickets is credited to the public accounts of the State. This is to give clear message to the participants that the proceeds are not in the hands of an individual group or association but is ensured to be credited in the State accounts. But, as we have said, this by itself would not take it outside the realm of gambling. It remains within the same realm. In this regard, there is no difference between lotteries under Entry 34 List II and a lottery organised by the State under Entry 40 List I. when character of both the State-organised lotteries and other lotteries remains the same, by merely placing the apparel of the State with authority of law, would not make any difference; it remains gambling as element of chance persists with no element of skill. ……. **"**

(c) A similar view has been expressed by the Hon'ble Supreme Court in case of ***Union of India & Ors.*** v. ***Martin Lottery Agencies Limited*** **: (2009) 12 SCC 209**. The relevant observations are reproduced hereunder:-

> **" 17.** We fail to persuade ourselves to agree with the aforementioned submission. The law, as it stands today (although it is possible that this Court in future may take a different view), recognises lottery to be gambling.

> Gambling is res extra commercium as has been held by this Court in *State of Bombay* v. *R.M.D. Chamarbaugwala* and *B.R. Enterprises* v. *State of U.P.*"

Thus, in view of the clear and categorical opinion of the Apex Court, we have no hesitation in concluding that the conduct of lottery is an act of "betting and gambling" envisaged under entries 34 and 62 of List II to Schedule 7.

(ii) whether it is within the exclusive domain of State legislature to impose taxes on organising lotteries being an act of "Betting and Gambling"

(iii) whether the Parliament has the competence to enact law in exercise of its residuary legislative power under entry 97 of List I to Schedule 7 dehors the entries 34 and 62 of List II;

Since both these limbs are interrelated, the same are being taken up for consideration conjointly.

(d) Entry 34 of List II to Schedule 7 prescribes "Betting and Gambling" as a field of legislation within the domain of the State. Entry 40 also provides lotteries organized by the Government of India or the Government of a State as a field of legislation for which the Union legislature can enact a law. Entry 34 has much wider field and it may include many other activities apart from the lotteries for which the State legislature may enact a law. However, under entry 40 the Parliament is competent to enact law only in respect to lotteries as a species of betting and gambling. Lottery thus is a common subject matter for

which both the Union Parliament and State Legislature can enact laws and fall in their respective legislative competence under Article 246 of the Constitution of India. The laws to be enacted under both these entries, however, could only be regulatory in nature and nothing beyond that. Where any field of legislation is available to both the Parliament and the legislature of a State and both the legislative bodies enact laws having competence to do so, in the event of conflict the State law to the extent of repugnancy shall be void if such law is enacted pursuant to any entry under List III (Concurrent List). However, the situation where the Parliament enacts a law on the subject matter under any one of the entries in List I and the State legislature also enacts a law touching the same subject matter pursuant to an entry in List II or vice versa, the position would be different. This seems to be the spirit underlying Article 246 read with Article 254 of the Constitution of India subject to exceptions under various Articles in Part XI Chapter I. This should not detain us as admittedly the Parliament alone has enacted the Lotteries (Regulation) Act, 1998 under entry 40 and there is no corresponding law enacted by the State legislature under entry 34 in respect to the regulation of the lotteries. As noticed above power to regulate does not

include power to tax, taxing powers having been conferred and specified under separate entries in Seventh Schedule.

(e) In case of ***State of West Bengal & Ors.*** v. ***Purvi Communication (P) Ltd. & Ors.*** **: (2005) 3 SCC 711**, it has been held by the Hon'ble Supreme Court that the power to regulate does not include power to tax. The relevant observations are noticed hereunder:-

> **" 35.** The Cable Television Networks (Regulation) Act, 1995, a Central legislation, has been enacted to regulate the operation of cable television networks in the country and for matters connected therewith. This enactment does not, in our opinion, fetter the legislative power or competence of the State to levy tax on luxuries including taxes on entertainments, amusements, betting and gambling falling under Entry 62 of List II of the Seventh Schedule to the Constitution. The power of regulation or control under the said Central enactment is separate and distinct from the power of taxation by the State Legislature under Entry 62 of List II; being a specific power, the power of taxation cannot be cut down or fettered by the general power of regulation as exercised by Parliament in enacting the said 1995 Act. ……..
> ……..…"

(f) Indubitably, there is no specific entry under List I empowering the Parliament to levy tax on lotteries or even on "betting and gambling". The service tax sought to be imposed is in exercise of the residuary power vested in the Parliament under entry 97 of List I read with Article 248 of the Constitution of India. In so far the List II is concerned, entry 62 specifically provides for levy of taxes on "betting and gambling". As observed by us above and held by

Hon'ble Supreme Court in ***B.R. Enterprises and Martin Lottery Agencies Ltd.*** (supra), lottery does fall within the expressions "betting and gambling". The first question for consideration would be whether the power to impose tax on lotteries is same thing as to impose tax on "betting and gambling". Though no entry in any of the Lists to Seventh Schedule specifically provides for levy of taxes on lotteries, the power to enact law for imposition of tax on lotteries have to be construed as inherent in the expressions "betting and gambling", lottery being one of such activity.

(g) Entry 97 of List I authorizes the Parliament to enact a law including imposition of taxes in respect of any other matter not enumerated in List II or List III. Article 248, which is the source of power, confers exclusive jurisdiction upon the Parliament to make any law in respect of any matter not enumerated in "State List" or "Concurrent List" and under Sub-clause (2). Such power also includes power to make law for imposition of tax not mentioned in either of those Lists, i.e. Lists II and III respectively.

(h) The scope of legislative competence of the Parliament to make laws under entry 97 of List I came up for consideration before a Constitution Bench of the Hon'ble

Supreme Court in ***Union of India*** v. ***Shri Harbhajan Singh Dhillon*** **: 1971 (2) SCC 779**. In this case, vires of the Section 27 of the Finance Act, 1969, in so far as it amended the Wealth Tax Act, 1957 to include the capital value of the agricultural land for the purposes of commuting wealth, came to be challenged as being beyond the exclusive competence of the Parliament. The petitioners, who challenged the vires of the Act, claimed that the power to tax on agricultural land was within the exclusive competence of the State Legislature under entry 49 of List II – i.e. Taxes on lands and buildings. It was held by the High Court and approved by the Apex Court that the power to levy tax on agricultural land is not contemplated by entry 49, List II. However, the amended Act was struck down by the High Court being beyond the competence of the Parliament by interpreting entry 86 of List I whereunder agricultural land was excluded from capital value of the assets. The amendment brought by the Finance Act was claimed to be under the residuary power under entry 97, List I. While considering this question, the Constitution Bench of the Hon'ble Supreme Court held as under:-

> **"10.** It was further urged by Mr. Setalvad that the proper way of testing the validity of a parliamentary statute under our Constitution was first to see whether the parliamentary legislation was with respect to a matter or tax mentioned in List II, if it was not, no other question would arise. The learned counsel for the respondent contended tha this manner of enquiry had not been even

hinted in any of the decisions of the Court during the last 20 years of its existence and there must accordingly be something wrong with this test. He urged that in so far as this test is derived from the Canadian decisions, the Canadian Constitution is very different and those decisions ought not to be followed here and applied to our Constitution.

11. It seems to us that the best way of dealing with the question of the validity of the impugned Act with the contentions of the parties is to ask ourselves two questions first is the impugned Act legislation with respect to Entry 49, List II and secondly if it is not, is it beyond the legislative competence of Parliament.

12. We have put these questions in this order and in this form because we are definitely of the opinion, as explained a little later, that the scheme of our Constitution and the actual terms of the relevant articles, namely, Article 246, Article 248 and Entry 97, List I, show that any matter, including tax, which has not been allotted exclusively to the State Legislatures under List II or concurrently with Parliament under List III, falls within List I, including Entry 97 of that list read with Article 248.

.....

21. It seems to us that the function of Article 246(1), read with Entries 1-96, List I, is to give positive power to Parliament to legislate in respect of these entries. Object is not to debar Parliament from legislating on a matter, even if other provisions of the Constitution enable it to do so. Accordingly we do not interpret the words “any other matter” occurring in Entry 97, List I, to mean a topic mentioned by way of exclusion. These words really refer to the matters contained in each of the Entries 1 to 96. The words “any other matter” had to be used because Entry 97, List I follows Entries 1-96, List I. It is true that the field of legislation is demarcated by Entries 1-96, List I, but demarcation does not mean that if Entry 97, List I confers, additional powers, we should refuse to give effect to it. At any rate, whatever doubt there may be on the interpretation of Entry 97, List I is removed by the wide terms of Article 248. It is framed in the widest possible terms. On its terms the only question to be asked is : Is the matter sought to be legislated or included in List II or in List III or is the tax sought to be levied mentioned in List II or in List III : No question has to be asked about List I. If the answer is in the negative then it follows that Parliament has power to make laws with respect to that matter of tax.

.....

47. The last sentence applies much more to the Constitution of a sovereign democratic republic. It is true that there are some limitations in Part III of the Constitution on the Legislatures in India but they are of a different character. They have nothing to do with legislative competence. If this is the true scope of

residuary powers of Parliament, then we are unable to see why we should not, when dealing with a Central Act, enquire whether it is legislation in respect of any matter in List II for this is the only field regarding which there is a prohibition against Parliament. If a Central Act does not enter or invade these prohibited fields there is no point in trying to decide as to under which entry or entries of List I or List III a Central Act would rightly fit in.

67. ..... Be that as it may, we have the three lists and a residuary power and therefore it seems to us that in this context if a Central Act is challenged as being beyond the legislative competence of Parliament, it is enough to enquire if it is a law with respect to matters or taxes enumerated in List II. If it is not, no further question arises.

103. The expression "any matter not enumerated in the Concurrent List or State List" in Article 248 must mean, in the context of clause (1) of Article 246, which gives Parliament exclusive power in respect of matters in List I, any matter other than those enumerated in any of the three Lists. Obviously, the residuary power given to Parliament in Article 248 cannot include power which is exclusively given to Parliament on matters in List I already conferred under clause (1) of Article 246, so that an attempt to distinguish the words "any matter" in Article 248 and "any other matter" in Entry 97 in List I is a distinction without difference. There had to be difference in language in the provisions in the context of the content of Entry 97 as that entry speaks about matters other than those enumerated before in List I and those enumerated in the other Lists. Notwithstanding the fact that the residuary power has been vested in the Central Legislature under Article 248 and its consequence translated in Entry 97 in List I, there can be no gainsaying that the idea was to assign such residuary power over matters which at the time of framing three Lists could not be thought of or contemplated. This is clear from the fact as pointed out by counsel, that the Lists contain as many as 209 matters which are couched in careful and elaborate words with inclusive and excluding language in the case of some, which has made the Constitution, to use the words of Gwyer, C.J., in *In re the C. P. and Berar Act No.XIV of 1938* (supra), "unique among federal constitutions in the length and detail of its legislative Lists". In the layout of such elaborately worded matters in the Lists and in the context of Article 246(1), the residuary power contained in Article 248 and Entry 97, List I must be construed as meaning power in respect of matters not enumerated in any of the three Lists. Such a residuary power cannot, therefore, be ordinarily claimed in respect of a matter already dealt with under an article or an entry in any one of the three Lists."

(i) Another Constitution Bench of the Hon'ble Supreme Court in ***West Bengal*** v. ***Kesoram Industries Ltd. & Ors.*** **: (2004) 10 SCC 201** again examined the scope of entry 97 List I and Article 248 to levy tax under the residuary power. The relevant observations are quoted as under:-

> **" 100.** Article 265 mandates – no tax shall be levied or collected except by authority of law. The scheme of the Seventh Schedule reveals an exhaustive enumeration of legislative subjects, considerably enlarged over the predecessor Government of India Act. Entry 97 in List I confers residuary powers on Parliament. Article 248 of the Constitution which speaks of residuary powers of legislation confers exclusive power on Parliament to make any law with respect to any matter not enumerated in the Concurrent List or the State List. At the same time, it provides that such residuary power *shall include* the power to making any law imposing a tax *not mentioned in either of those Lists*. It is, thus, clear that if any power to tax is clearly mentioned in List II, the same would not be available to be exercised by Parliament based on the assumption of residuary power.**"**

(j) Hon'ble Bench relied upon the Constitution Bench judgment in ***Union of India*** v. ***Shri Harbhajan Singh Dhillon (supra)*** and the commentary on constitutional law by H. M. Seervai, 4th Edition (Silver Jubilee Edition). The relevant observations quoted in the above judgment are reproduced hereunder: -

> **" 102.** Vide para 22.194 the eminent jurist poses a question:
>
> "*22.194.* Does Article 248 add anything to the exclusive residuary power of Parliament under Article 246(1) read with Entry 97 List I, to make laws in respect of 'any other matter' not mentioned in List II and List III, including any tax not mentioned in those Lists?"
>
> and answers by saying – "The answer is 'No'.**"**

(k) The Hon'ble Court further observed that there is nothing like an implied power to tax and the burden is always upon the taxing authority to point to the act of assembly which authorizes the imposition of the tax claimed. Hon'ble Court further relied upon Justice G.P. Singh's commentary on Principles of Statutory Interpretation (8th Edn., 2001). The relevant quotes are reproduced hereunder: -

> **"106.** The judicial opinion of binding authority flowing from several pronouncements of this Court has settled these principles : *(i)* in interpreting a taxing statute, equitable considerations are entirely out of place. Taxing statutes cannot be interpreted on any presumption or assumption. A taxing statute has to be interpreted in the light of what is clearly expressed; it cannot imply anything which is not expressed; it cannot import provisions in the statute so as to supply any deficiency; *(ii)* before taxing any person it must be shown that he falls within the ambit of the charging section by clear words used in the section; and *(iii)* if the words are ambiguous and open to two interpretations, the benefit of interpretation is given to the subject. There is nothing unjust in the taxpayer escaping if the letter of the law fails to catch him on account of the legislature's failure to express itself clearly. *(See Justice G. P. Singh, ibid.,* pp. 638-39.)
>
> **107.** Power to tax is not an incidental power. According to Seervai, although legislative power includes all incidental and subsidiary power, the power to impose a tax is not such a power under our Constitution. It is for this reason that it was held that the power to legislate in respect to inter-State trade and commerce (Entry 42 List I Schedule 7) did not carry with it the power to tax the sale of goods in inter-State trade and commerce before the insertion of Entry 92-A in List I and such power belonged to the States under Entry 54 in List II. Entry 97 in List I also militated against the contention that the power to tax is an incidental power under our Constitution (See Seervai, H.M. : *Constitutional Law of India,* 4th/Silver Jubilee Edn., Vol. 3, para 22.20.)**"**

(I) In ***N. V. Marketing Pvt. Ltd.*** v. ***State of Maharashtra & Ors.*** **: 2009 (III) (8) Bom. L.R. 3397**, it has been ruled that even though the power of regulation of lotteries vest in the Parliament in terms of entry 40 of List I, power to tax is not an incidental power. The Hon'ble Bombay High Court relying upon ***West Bengal*** v. ***Kesoram Industries Ltd. & Ors.*** **: (2004) 10 SCC 201** and various other judgments, while considering the validity of State law enacted by the Maharashtra State imposing tax on lotteries, observed as under:-

> **"3.** It is the contention of the Petitioners that the legislature of State of Maharashtra has no legislative power to enact Laws relating to State Lotteries including Laws relating to taxation, and therefore, according to the Petitioners, the State Act is beyond the legislative competence of the legislature of State of Maharashtra. The second submission is that the enactment of the State Act is colourable exercise of the legislative power in as much as it is another method of levying tax on lottery tickets. The third submission is that the State Act seeks to levy tax on lottery schemes, tax is collected in advance in respect of each draw in the lottery scheme at the rate specified in Section 3 of the State Act. It is submitted that lottery scheme of all other State organising and conducting lotteries save and except that of Maharashtra are formulated outside the State of Maharashtra and therefore, the law has extra territorial application. The fourth submission is that the State Act levies tax on lottery schemes but the term "lottery scheme" is not defined anywhere and therefore, it is violative of guarantee under Article 14 of the Constitution of India. It was also contended that the State Act has been enacted to impose tax on sale of lottery tickets conducted by other State in State of Maharashtra so as to make selling of lottery tickets by the other States uneconomical, unviable and thereby creating monopoly in the lottery tickets of the lotteries conducted by the State of Maharashtra.
>
> .....
>
> **10.** It was then contended before us that though there is specific power vested in the State legislature under Entry 62 of List II of the Seventh Schedule, because of Entry 40 in List I of the Seventh Schedule of the Constitution of India, the Parliament will have legislative

competence to levy tax under Article 248 and Entry 97 in List I of the Seventh Schedule of the Constitution of India. In our opinion, this submission has also no force, because power to tax is not an incidental power and under the residuary power the Parliament will be entitled to impose tax only if that power is not specifically vested in the State legislature by any entry in List II of the Seventh Schedule. ……."

(Emphasis supplied)

(m) In ***Godfrey Philips India Ltd.*** v. ***State of U.P.*** **: (2005) 2 SCC 515**, the Hon'ble Supreme Court upholding the legislative power of State under entry 62 of List II, held as under: -

"**46.** Therefore, taxing entries must be construed with clarity and precision so as to maintain such exclusivity, and a construction of a taxation entry which may lead to overlapping must be eschewed. If the taxing power is within a particular legislative field, it would follow that other fields in the legislative lists must be construed to exclude this field so that there is no possibility of legislative trespass.

……

49. Under the three lists of the Seventh Schedule to the Indian Constitution a taxation entry in a legislative list may be with respect to both. Article 246 makes it clear that the exclusive powers conferred on Parliament or the States to legislate on a particular matter includes the power to legislate with respect to that matter. Hence, where the entry describes an object to tax, all taxable events pertaining to the object are within that field of legislation unless the even is specifically provided for elsewhere under a different legislative head. Where there is the possibility of legislative overlap, courts have resolved the issue according to settled principles of construction of entries in the legislative lists.

……

72. In view of the decision in *Sea Customs Act case* the second premise propounded by Mr. Salve is unacceptable. As we have seen, in that case this Court held that the taxable event of ownership is implicit in the concept of taxes on goods. That the entries on taxable events in the legislative lists are not exhaustive is also recognized and provided for in Article 248(2) which provides for the power of Parliament to make any law imposing a tax not mentioned in either the Concurrent or State Lists. This residuary power is reflected in Entry 97 of List I. Furthermore if an article or goods are taxable only with respect to a taxable event, and if, as contended by Mr. Salve, all taxable events have been provided for in the different legislative heads, then by that token no object or goods could be taxable. This would render the various entries in the State List including

> Entries 57 and 58 contentless. As we cannot accept that the taxation entries exhaustively enumerate all taxable events, it does not follow that Entry 62 of List II does not cover goods. It is not possible therefore to hold merely on such a construction of the legislative lists and the taxation entries therein, that Entry 62 List II does not permit the States to levy tax on articles of luxury.
>
> **73.** Having rejected the second premise contended for by Mr. Salve, the next question is whether the language of Entry 62 List II would resolve the issue. The juxtaposition of the different taxes within Entry 62 itself is in our view of particular significance. The entry speaks of "taxes on luxuries *including* taxes on entertainments, amusements, betting and gambling". The word "including must be given some meaning. In ordinary parlance it indicates that what follows the word "including" comprises or is contained in or is a part of the whole of the work preceding. The nature of the included items would not only partake of the character of the whole, but may be construed as clarificatory of the whole.
>
> **74.** It has also been held that the word "includes" may in certain contexts be a word of limitation (*South Gujarat Roofing Tiles Manufacturers Assn.* v. *State of Gujarat*). In the context of Entry 62 of List II this would not mean that the word "luxuries" would be restricted to entertainments, amusements, betting and gambling but would only emphasise the attribute which is common to the group. If luxuries is understood as meaning something which is purely for enjoyment and beyond the necessities of life, there can be no doubt that entertainments, amusements, betting and gambling would come within such understanding. Additionally, entertainments, amusements, betting and gambling arfe all activities. "Luxuries" is also capable of meaning an activity and has primarily and traditionally been defined as such. It is only derivatively and recently used to connote an article of luxury. One can assume that the coupling of these taxes under one entry was not fortuitous but because of these common characteristics.**"**

(n) It has been vehemently argued by Mr. Razzaq that the service tax levied vide clause (zzzzn) under sub-section (105) of Section 65 is a tax on various activities comprising services rendered by the distributors to the State in promotion, marketing, organizing of lottery, etc. It is not a

tax on betting and gambling, per se and is beyond the purview of entry 62 of List II.

Entry 62 empowers the State Legislature to impose tax on luxuries, entertainment, amusement, betting and gambling.

(o) For the purpose of the present petition, the relevant subject matter under entry 62 is "betting and gambling". As held by the Hon'ble Supreme Court in ***Express Hotels Private Ltd.*** v. ***State of Gujarat*** **& Anr. : (1989) 3 SCC 677,** the entries must be construed by giving them the widest possible meaning. Relevant observations are:-

> "**15.** .....The entries should not be read in a narrow or pedantic sense but must be given their fullest meaning and the widest amplitude and be held to extend to all ancillary and subsidiary matters which can fairly and reasonably be said to be comprehended in them."

In the same judgment the vires of various provisions enacted by States of Gujarat, Tamil Nadu, Karnataka and West Bengal, imposing taxes on luxuries provided in hotels and lodging houses came to be challenged. The question that arose in those cases was as to whether the luxury taxes can be levied only on the articles of luxury or persons enjoying the luxuries under Entry 62 and, the activity of lodging in a hotel or lodge being not a thing tangible, the tax

is ultra vires the Constitution. Interpreting the scope of the legislative entry particularly the expression 'luxury' used in entry 62, the Hon'ble Supreme Court held as under:

> **"21.** The concept of a tax on 'luxuries' in Entry 62, List II cannot be limited merely to tax things tangible and corporeal in their aspect as 'luxuries'. It is true that while frugal or simple food and medicine may be classified as necessities; articles such as jewellery, perfume, intoxicating liquor, tobacco, etc., could be called articles of luxury. But the legislative entry cannot be exhausted by these cases, illustrative of the concept. The entry encompasses all the manifestations or emanations, the notion of 'luxuries' can fairly and reasonably (*sic*) can be said to comprehend the element of extravagance or indulgence that differentiates 'luxury' from 'necessity' cannot be confined to goods and articles. There can be elements of extravagance or indulgence in the quality of services and activities."

(p) In ***State of Bombay vs. R.M.D. Chamarbaugwala and another : AIR 1957SC 699***, tax was levied under entry 62 on the promoters of the lotteries. The question that fell for consideration was whether tax on promoters of lotteries, who do not gamble is tax on betting and gambling under entry 62 List II. Rejecting the challenge and upholding the validity of the levy on promoters, the Hon'ble Supreme Court observed as under:-

> "(23) The next point urged is that although the Act may come under Entry 34, the taxing provisions of s. 12A cannot be said to impose a tax on betting and gambling under Entry 62 but imposes tax on trade under Entry 60. Once it is held that the impugned Act is on the topic of betting and gambling under Entry 34, the tax imposed by such a statute, one would think, would be a tax on betting and gambling under Entry 62. The Appeal Court has expressed the view that s. 12A does not fall within Entry 62, for it does not impose a tax on the gambler but imposes a tax on the petitioners who do not themselves gamble but who only promote the prize competitions. So far as the promoters are concerned, the tax levied from them can only be regarded as tax on the trade of prize competitions carried on by them.
>
> This, with respect, is taking a very narrow view of the matter. Entry 62 talks of taxes on betting and

gambling and not of taxes on the men who bet or gamble. It is necessary, therefore, to bear in mind the real nature of the tax. The tax imposed by s. 12A is, in terms, a percentage of the sums specified in the declaration made under s. 15 by the promoter or a lump sum having regard to the circulation and distribution of the news paper or publication in the State.

.....
.....

If taxation on betting and gambling is to be regarded as a means of controlling betting and gambling activities, then the easiest and surest way of doing so is to get at the promoters who encourage and promote the unsocial activities and who hold the gamblers' money in their hands. To collect the tax from the promoters is not to tax the promoters but is a convenient way of imposing the tax on betting and gambling and indirectly taxing the gamblers themselves.

.....
....."

(q) In ***Purvi Communication (P) Ltd.*** (supra) Hon'ble Supreme Court considered the scope of Entry 62 and held that the tax under this Entry may be levied on the person spending on entertainment, on the act of person entertaining or the subject of entertainment. Relevant observations are quoted hereunder: -

"**38.** A tax under Entry 62 of List II of the Seventh Schedule to the Constitution may be imposed not only on the person spending on entertainment but also on the act of a person entertaining, or the subject of entertainment. It is well settled by this Court that such tax may be levied on the person offering or providing entertainment or the person enjoying it. The respondents are admittedly engaged in the business of receiving broadcast signals and then instantaneously sending or transmitting such visual or audio-visual signals by coaxial cable, to subscribers' homes through their various franchisees. It has been made possible for the individual subscribers to choose the desired channels on their individual TV sets because of cable television technology of the respondents and of sending the visual or audio-viisual signals to sub-cable operators, and instantly retransmitting such signals to individual subscribers for entertaining them through their franchisees. The respondents' act is, no doubt, an act of offering entertainment to the subscribers and/or viewers. The respondent is very much directly and closely involved in the act of offering or providing

> entertainment to subscribers who are on his record. For the fact of offering or providing entertainment to the subscribers and/or viewers, the respondents receive charges, which are realized or collected by their franchisee from the ultimate subscribers. Their franchisee, called as sub-cable operator under the said 1982 Act having no independent role to ofer or provide entertainments to the subscribers inasmuch as franchisees have to depend entirely on the respondents' communication network and this communication network of the respondents consists of receiving and sending visual images and audio and other information for preparation of the subscribers and/or viewers; without the communication network service of the respondents, no entertainments can be offered or provided to the subscribers and/or viewers.
>
> **39.** In the tax matters, the State Legislature is free, if it has legislative competence, to choose the persons from whom the tax levied on entertainments is to be collected. In other words, what are taxed are the entertainments, which is very much within the ambit of Entry 62 of List II of the Seventh Schedule. It is the respondents who as cable operator for the purpose of the said 1982 Act are engaged in the business of providing or offering entertainments which include showing of films, various serials, cricket matches and dramatic performances to the subscribers, and the tax is imposed on the act of offering such entertainments in this way to such subscribers and/or viewers. The entire communication network service is built up and controlled by the respondents. Whatever amount is received or receivable by the respondent in respect of providing such entertainments is taxable under sub-section (4-a) of Section 4-A of the said 1982 Act which has a direct and sufficient nexus with the entertainments.**"**

(r) Similarly entry 50 under Section 100 of the Government of India Act, 1935 relating to tax on luxuries or entertainment or amusement has been interpreted by the Constitution Bench of the Hon'ble Supreme Court in ***1959 Supp (2) SCR 63=AIR 1959 SC 582 : Western India Theaters Ltd. vs. Cantonment Board***, wherein it has been held that "the entries in legislative list should not be read in a narrow or restricted sense and that each general word should be held to extend to all ancillary or subsidiary

matters which can fairly and reasonably be said to be comprehended in it."

(s) In the matter of organizing, marketing and promotion of lotteries, the State Government who is the promoter and publisher of the lotteries, the distributor, i.e. the petitioner, selling agent and the ultimate purchaser of the lottery ticket who participates in the game of chance, are all players in the activity of the betting and gambling. Thus tax envisaged under entry 62 on "betting and gambling" is tax on the activity as held by the Constitution Bench in ***State of Bombay vs. R.M.D. Chamarbaugwala's*** case (supra). The betting and gambling itself is an activity though the lottery ticket is a tangible thing which carries with its right to participate in the game of chance. Thus all activities right from the publishing of the lottery tickets till participation in the game of chance, declaration of draw and even distribution of prize to the winner fall within the purview of expression 'betting and gambling'. Thus power to levy tax on organization, promotion and marketing of lottery being an act of betting and gambling comes within the exclusive domain of entry 62 of List II.

(t) It is also settled legal position that where the entries under different Lists empower the respective legislatures to enact law on any subject matter and the question arises regarding the legislative competence of the legislative bodies, the doctrine of pith and substance is to be applied to find out the real intention of the legislative entry and the object of enacting a law. As observed in ***State of West Bengal*** v. ***Kesoram Industries Ltd. (supra)*** if any law enacted by Parliament is not traceable to any legislative entry in List II or List III, it is irrelevant whether the power of the Parliament is traceable to a specific entry and Parliament shall be deemed to have legislative competence. Its natural corollary would be if power to enact law on a subject matter including levy of taxes is traceable to any entry in List II and List III, residuary power under entry 97 of List I read with Article 248 of the Constitution of India will not be available to it, the same having been specifically restricted under entry 97 of List I and Article 248 of the Constitution.

(u) In the instant case, the power to tax on lotteries or even “betting and gambling” is not available under any of the entries of List I. However, such power is germane to and emanates from entry 62 of List II in Seventh Schedule, meaning thereby that the residuary power to enact a law

imposing tax on lotteries would not be available to the Parliament.

(v) Mr. Razzak, Learned Additional Solicitor General, submits that since the service tax is a new concept and a new tax regime, it could not be said that at the time of enacting the entries the intention of the Framers of the Constitution was to include all kinds of future taxes within the purview of taxes under Entry 62 or for that matter any other entry in Seventh Schedule, wherein the power to enact a law imposing taxes has been indicated. His submission is that service tax is not mentioned in any of the entries and thus it should be deemed to be excluded from Entry 62 or for that matter any other entry in Lists II and III to Seventh Schedule. This argument apparently appears to be attractive but its fallacy is exposed if the proposition is applied to all taxing entries irrespective of Lists. On the same analogy, the power to impose a tax not prevalent or envisaged when entry 97 was incorporated in List I, the service tax would also be beyond its purview. "Tax" has been defined under the Black's Law Dictionary in the following manner: -

> **"tax,** *n.* A monetary charge imposed by the government on persons, entitles, transactions, or property to yield public revenue. ● Most broadly, the term embraces all governmental impositions on the person, property, privileges, occupations, and enjoyment of the people, and includes duties, imposts, and excises.

> Although a tax is often thought of as being pecuniary in nature, it is not necessarily payable in money.**"**

(w) Article 366 of the Constitution of India defines various expressions used in the Constitution. "Taxation and Tax" being one of such expressions defined under clause (28) thereof. The relevant extract reads as under:-

> **" 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 –
> .....
> .....
>
> (28) "taxation" includes the imposition of any tax or impost, whether general or local or special, and "tax" shall be construed accordingly;
> .....
> .....**"**

(x) This definition is of widest possible amplitude and encompasses within its field any kind of tax that could be visualized or conceptualized. In ***D. G. Gose and Co. Pvt. Ltd. & Ors.*** v. ***State of Kerala & Anr.*** **: (1980) 2 SCC 410**, a Constitution Bench of the Hon'ble Supreme Court, while considering clause (28) of Article 366 of the Constitution, observed as under:-

> **"5.** The word "tax" in its widest sense includes all money raised by taxation. It therefore includes taxes levied by the Central and the State legislatures, and also those known as "rates", or other charges, levied by local authorities under statutory powers. "Taxation" has therefore been defined in clause (28) of Article 366 of the Constitution to include "the imposition of any tax or impost, whether general or local or special", and it has been directed that "tax" shall be "construed accordingly".**"**

(y) Various entries empowering the Parliament and State Legislatures to enact laws for levy of tax do not mean or confine the kind of taxes prevalent or in vogue at the time these entries were enacted in Seventh Schedule. The word “tax” includes all kinds of taxation present or future that may be thought of by the competent legislative body. Thus the argument of Mr. Razzak that service tax does not find mention in entry 62 and thus is beyond its purview cannot be accepted or appreciated. Any kind of tax that may be envisaged and can be legally conceptualized by the legislative body falls within the purview of tax in view of all embracing definition of expressions “tax (taxation)” under clause (28) of Article 366. Service tax though a new regime, it would be antithesis of the term “tax” if considered to be a category of tax not envisaged by any of the entries in Seventh Schedule empowering to levy tax. Applying the principle of pith and substance, the power to levy tax on lottery being a game of chance and included in the expressions “betting and gambling” in entry 62 List II, the State Legislature has the exclusive legislative competence and jurisdiction of Parliament to levy such a tax in exercise of its residuary power under entry 97 of the List I read with Article 248 of the Constitution stand excluded. There is another important aspect; entry 92C – ‘Taxes on services’

was also incorporated in List I Seventh Schedule by Eighty-eighth Constitutional Amendment Act, 2003. However, this entry has not been notified till date.

(z) Our opinion that the Parliament lacks legislative competence to levy service tax on lotteries in exercise of its legislative power flowing from entry 97 List I read with Article 248 of the Constitution should not be construed to mean that the Parliament has no jurisdiction whatsoever to levy service tax in respect of any of the subject matter. The legislative competence of the Parliament to impose service tax has to be conceded by virtue of entry 97 List I read with Article 248 of the Constitution as held by Hon'ble Supreme Court in various judgments noticed by us hereinbefore and later part of this judgment. However, such legislative power is prohibited in respect to any subject matter where the power to impose or levy tax has been conferred upon the State Legislature in List II (State List) or the Provincial Legislature and the Parliament under List III (Concurrent List). It is also pertinent to say that Parliament would also be deprived of the residuary power in respect to any subject matter falling even in the List I where such power is traceable to any of the entries contained therein i.e. entries 1 to 96. In our view the residuary powers of the Parliament would come into play only where none of the entries in any

of the Lists provide for a legislative field. As held by the Hon'ble Apex Court in ***State of West Bengal*** v. ***Kesoram Industries Ltd. (supra)***, the only embargo in the exercise of the residuary power of Parliament under entry 97 List I read with Article 248 of the Constitution would be non-existence of legislative power of any of the Legislatures under Lists II and III, Schedule 7. At the cost of repetition we may say that where the legislative power whether to enact a law in general or for levy of tax in particular, is not envisaged under Lists II and III, the Parliament would be fully competent to enact a law including imposing a tax (Service Tax) under entry 97 List I. We are of the considered view that Parliament would have had the legislative competence to impose tax including service tax upon lotteries but for entry 62, List II. It is the exclusive legislative domain of the State Legislature to levy tax of any nature on lotteries by virtue of entry 62 List II, Schedule 7.

(iv) <u>whether the State legislature and Parliament both can simultaneously impose taxes on the conduct of lottery by the State Government under entry 62 of List II and entry 97 of List I to Schedule 7, if so, under what circumstances;</u>

(aa) Mr. Farooq Md. Razzak, Addl. Solicitor General, appearing for the Union of India, submits that the service tax levied vide the impugned clause (zzzzn) to Sub-section

(105) of Section 65 is not a tax on the activity of “betting and gambling” but on services like promotion, marketing, organising or in any other manner assisting in organising games of chance including lottery. His further submission is that the service tax is on an activity and is a Value Addition Tax. In other words, his contention is that the value addition is on account of the activities like marketing, organising and promoting the lottery and such activities render value addition to the lotteries held by the State of Sikkim and, thus, does not fall within the purview of “betting and gambling” in entry 62 of List II. It is his submission that on account of non-application of entry 62, the Parliament is entitled to exercise its legislative jurisdiction to enact the law under its residuary power under entry 97 of List I. According to Mr. Razzak, a lottery ticket of Re.1/- is being given to the petitioner’s company for 70 paise for providing various services as noticed by us in the earlier part of this judgment and the service tax is chargeable on the gross amount of the lottery tickets under Section 67 of the Finance Act, 1994 as amended by Finance Act, 2010. It is further argued that the measure of tax cannot be questioned by the petitioner that too in writ proceedings and that it is for the competent adjudicating authority to decide the issue. It is contended that the

petitioner has directly approached this Court without having approached the competent adjudicating authority in this regard. Under such circumstances, the petitioner should be directed to approach the competent adjudicating authority for seeking adjudication regarding levy of service tax on the service rendered by it. He has placed reliance upon the judgment of the Apex Court reported as ***Association of Leasing & Financial Service Companies*** v. ***Union of India*** **: (2011) 2 SCC 352.**

(ab) In the above case the controversy before the Hon'ble Supreme Court was with regard to levy of service tax on the transaction of equipment leasing and hire purchases undertaken by non-banking financial companies. The plea of the writ petitioners who challenged the vires of the levy was that the transaction of equipment leasing and hire purchase and financing has been constitutionally defined as sale and purchase under Article 366 (29A) and thus falls within the exclusive competence of State Legislature under entry 54 of List II, hence the Parliament in exercise of its legislative competence under entry 97 of List I of Seventh Schedule of the Constitution is not competent to levy service tax. Hon'ble Apex Court on consideration of entire issue came to the conclusion that part of the transaction constitute sale for which the State Legislature is

competent to impose tax under entry 54 of List II whereas the components of the transaction constituting service fall within the legislative competence of the Parliament under its residuary power under entry 97 of List I. Validity of the service tax imposed under Section 65(105)(zm) was thus upheld. The relevant observations in this regard are quoted hereunder:-

> "**59.** Applying the above decisions to the present case, on examination of the impugned legislation in its entirety, we are of the view that the impugned levy relates to or is with respect to the particular topic of "banking and other financial services" which includes within it one of the several enumerated services viz. financial leasing services. These include long-term financing by banks and other financial institutions (including NBFCs). These are services rendered to their customers which comes within the meaning of the expression "taxable services" as defined in Section 65(105)(zm). The taxable event under the impugned law is the rendition of service. The impugned tax is not on material or sale. It is on activity/service rendered by the service provider to its customer. Equipment leasing/hire-purchase finance are long-term financing activities undertaken as their business by NBFCs. As far as the taxable value in case of financial leasing including equipment leasing and hire purchase is concerned, the amount received as principal is not the consideration for services rendered. Such amount is credited to the capital account of the lessor/hire-purchase service provider. It is the interest/finance charge which is treated as income or revenue and which is credited to the revenue account. Such interest or finance charges together with the lease management fee/processing fee/documentation charges are treated as considerations for the services rendered and accordingly they constitute the value of taxable services on which service tax is made payable.
>
> **60.** In fact, the Government has given exemption from payment of service tax to financial leasing services including equipment leasing and hire purchase on that portion of taxable value comprising of 90% of the amount representing as interest i.e. the difference between the instalment paid towards repayment of the lease amount and the principal amount in such instalments paid (see Notification No. 4/2006 — Service Tax dated 1-3-2006). In other words, service tax is leviable only on 10% of the interest portion. (See also Circular F. No. B.11/1/2001-TRU dated 9-7-2001 in which it has been clarified that service tax, in the case of financial leasing including equipment leasing and hire purchase, will be leviable only

> on the lease management fees/processing fees/documentation charges recovered at the time of entering into the agreement and on the finance/interest charges recovered in equated monthly instalments and not on the principal amount.) Merely because for valuation purposes inter alia "finance/interest charges" are taken into account and merely because service tax is imposed on financial services with reference to "hiring/interest" charges, the impugned tax does not cease to be service tax and nor does it become tax on hire-purchase/leasing transactions under Article 366(29-A) read with Entry 54, List II. Thus, while the State Legislature is competent to impose tax on "sale" by legislation relatable to Entry 54 of List II of the Seventh Schedule, tax on the aspect of the "services", vendor not being relatable to any entry in the State List, would be within the legislative competence of Parliament under Article 248 read with Entry 97 of List I of the Seventh Schedule to the Constitution.**"**

(ac) It may be noticed that the Hon'ble Supreme Court split the transaction into two components i.e. "sale" and "service". It is pertinent to note that the service tax was imposed only on the component of the service @ 10 % of the contract value. While considering the nature of transaction it was noticed by the Hon'ble Supreme Court that the part of the transaction like interest/ financing charges with lease management fee, processing fee and documentation charges are consideration for rendering service by the non-banking financial companies and thus held that it fell within the definition of "taxable service" defined in Section 65 (105)(zm).

(ad) Another judgment heavily relied upon by Mr. Razzak is (***2004) 5 SCC 632 : T.N. Kalyanamandapam Association vs. Union of India & Others***. In this case

vires of Sections 65(19), (20), (41)(p), and 66, 67(o) of the Finance Act, 1994 as amended from time to time were assailed being ultra vires. Under the above provisions service tax was levied on the services rendered by the mandap-keepers in respect of the temporary leasing of land for organizing official, social or business functions and even for catering services which *inter alia* included furniture, fixtures, light fittings, floor covering etc. on 60% of the gross amount charged by the mandap-keepers. The vires of the provision was challenged on the ground that it was a tax on land and building under entries 18 and 49 of List II of the Seventh Schedule. It also amounted to tax on sale under entry 54 of List II particularly in view of definition of 'sale' and 'purchase' under Article 366 (29A)(f).

(ae) The High Court rejected the contention and in appeal the Hon'ble Supreme Court affirmed the judgment holding that the activity of mandap-keepers does not fall in any of the entries i.e. 18 and 49 of the State List. As regards the entry 54, it has been held that the tax had been levied on 60% of the gross receipts. It was further held that predominantly the activity of the mandap-keepers was rendering various kinds of services. Applying the aspect doctrine, the Hon'ble Supreme Court held as under: -

> **"58.** A tax on services rendered by mandap-keepers and outdoor caterers is in pith and substance, a tax on services and not a tax on sale of goods or on hire-purchase activities. Section 65 clause (41) sub-clause (*p*) of the Finance Act, 1994, defines taxable service (which is the subject-matter of levy of service tax) as any service provided to a customer
>
> > "by a mandap-keeper in relation to the use of a mandap in any manner including the facilities provided to [a customer] in relation to such use and also the services, if any, rendered as a caterer".
>
> The nature and character of this service tax is evident from the fact that the transaction between a mandap-keeper and his customer is definitely not in the nature of a sale or hire-purchase of goods. It is essentially that of providing a service. In fact, as pointed out earlier, the manner of service provided assumes predominance over the providing of food in such situations which is a definite indicator of the supremacy of the service aspect. The legislature in its wisdom noticed the said supremacy and identified the same as a potential region to collect indirect taxes. Moreover, it has been a well-established judicial principle that so long as the legislation is in substance, on a matter assigned to a legislature enacting that statute, it must be held valid in its entirety even though it may trench upon matters beyond its competence. Incidental encroachment does not invalidate such a statute on the grounds that it is beyond the competence of the legislature (*Prafulla Kumar* v. *Bank of Commerce* [AIR 1947 PC 60 : 74 IA 23]). Article 246(1) of the Constitution specifies that Parliament has exclusive powers to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule to the Constitution. As per Article 246(3), the State Government has exclusive powers to make laws with respect to matters enumerated in List II (State List). In respect of matters enumerated in List III (Concurrent List) both Parliament and State Governments have powers to make laws. The service tax is made by Parliament under the above residuary powers.

(af) Another judgment on which emphasis has been laid on behalf of respondents is ***(2007) 7 SCC 527 : All India Federation of Tax Practitioners & Others vs. Union of India & Others***. In this case levy of service tax on practicing Chartered Accountants, Cost Accountants and Architects vide the Finance Act, 1994 was assailed. The challenge was based upon the legislative competence of

State Legislature to levy tax on professions, etc. under entry 60 of List II and Article 276 of the Constitution of India. It was contended on behalf of the petitioners that the service tax on professionals is a tax on profession and thus beyond the legislative competence of the Parliament. Repelling the argument and drawing distinction between the tax on profession and services rendered by the professionals, the Hon'ble Supreme Court observed as under:

> **"34.** As stated above, Entry 60, List II refers to taxes on professions, etc. It is the tax on the individual person/firm or company. It is the tax on the status. A chartered accountant or a cost accountant obtains a licence or a privilege from the competent body to practise. On that privilege as such the State is competent to levy a tax under Entry 60. However, as stated above, Entry 60 is not a general entry. It cannot be read to include every activity undertaken by a chartered accountant/cost accountant/architect for consideration. Service tax is a tax on each activity undertaken by a chartered accountant/cost accountant or an architect. The cost accountant/chartered accountant/architect charges his client for advice or for auditing of accounts. Similarly, a cost accountant charges his client for advice as well as doing the work of costing. For each transaction or contract, the chartered accountant/cost accountant renders profession based services. The activity undertaken by the chartered accountant or the cost accountant or an architect has two aspects. From the point of view of the chartered accountant/cost accountant it is an activity undertaken by him based on his performance and skill. But from the point of view of his client, the chartered accountant/cost accountant is his service provider. It is a tax on "services". The activity undertaken by the chartered accountant or cost accountant is similar to saleable or marketable commodities produced by the assessee and cleared by the assessee for home consumption under the Central Excise Act.
>
> **35.** For each contract, tax is levied under the Finance Acts, 1994 and 1998. Tax cannot be levied under that Act without service being provided whereas a professional tax under Entry 60 is a tax on his status. It is the tax on the status of a cost accountant or a chartered accountant. As long as a person/firm remains in the profession, he/it has to pay professional tax. That tax has nothing to do with the commercial activities which he undertakes for his client. Even if the chartered accountant has no work throughout the accounting year, still he has to pay

> professional tax. He has to pay the tax till he remains in the profession. This is the ambit and scope of Entry 60, List II which is a taxing entry. Therefore, Entry 60 contemplates tax on professions, as such. Entry 60, List II refers to "tax on employments".**"**

(ag) From the ratio of above judgments, the emergence of proposition of law is that where the transaction or contract comprises of twin elements of sale and service, both, the State Legislature under entry 54 of List II and simultaneously the Parliament in exercise of residuary power under entry 97 of List I is competent to levy "sales tax" and "service tax" respectively provided the components of sale and service are visible and are capable of compartmentalization.

(v) <u>whether such circumstances exist in the case in hand?</u>

(ah) The facts of the present case are clearly distinguishable as noticed in the earlier part of the discussion. We have opined that the State Government is not paying any consideration to the petitioners nor the petitioners are rendering any service to the State. To the contrary the petitioners are paying minimum guaranteed amount for the purchase of entire lot of lotteries at the discounted price of 70 paise against the MRP of Re.1/- to the State. The nature of discount has already been discussed in detail.

(ai) It has been held by the Hon'ble Supreme Court in ***All India Federation of Tax Practitioners*** (Supra) that the service is an activity and service tax is in the nature of VAT i.e. Value Added Tax. The Hon'ble Supreme Court in ***State of Bombay vs R.M.D. Chamarbaugwala*** (supra) has also defined the betting and gambling as an activity.

(aj) In ***T.N. Kalyanamandapam Association***'s case (supra) the clear view of the Hon'ble Supreme Court is that the predominant activity of the service provider was rendering of service and levy of service tax on 60% of the gross value was upheld. Similarly in ***Assn. of Leasing & Financial Service Companies*** case levy of service tax on 10% of the gross contract value was upheld being a tax on component of service.

(ak) In the present case, undisputedly the lottery ticket is sold as a good by the State Government to the petitioners at the discounted value of 70 paise per ticket as against its gross value/ MRP of Re.1/-. The predominant part of the transaction is sale of goods. While considering the discount of 30% to the petitioners on the MRP, we have held that the discount is a normal trade practice in any transaction of sale and purchase. If the seller sells the goods at the MRP to its ultimate consumer, no intermediary will sell the goods

unless he gets a discount to meet the expenditure for establishment, logistics and some component of profit. The State Government is unable to sell the tickets to the ultimate buyers and for that purpose the petitioners are appointed as stockists or distributors on payment of full sale consideration on discounted price. Further the sale by the petitioners to their stockists, selling agents etc is on discounted price from MRP after keeping the establishment and other expenditure and margin of profit for themselves. The last sale to the consumer of the lottery is on the MRP of Re.1/- per ticket. Thus, all the intermediaries have to be given discount from MRP for the purpose of meeting their expenditure and some component of profit. The advertisement etc. is only to popularize the State lottery but that does not mean that it is a service rendered to the State Government. As argued by Mr. Madhav Rao, this is for promotion of their own sale at their own expense without recovering it from the State Government. In any case service tax is being levied and collected on the gross amount without even isolating the discounted cost of lottery ticket. Thus in the present case there does not seem to be any circumstance where the activity of sale of State organized lottery by the petitioners through its various stockists, agents etc. can be construed to be a service rendered to the

State Government so as to enable the Central Government to impose service tax on any component or element of the transaction between the State and the petitioners

Conclusions: -

(i) In the backdrop of discussion on Ground (A) we have no hesitation to conclude that the activities of the lottery distributors i.e. the petitioners herein do not constitute a service and thus beyond the purview of “taxable service” as statutorily defined under clause (zzzzn) of sub-section 105 of Section 65 of the Finance Act, 1994 as amended vide Finance Act, 2010.

(ii) The activity of promotion, marketing, organizing or in any other manner assisting in organising game of chance including lottery is an activity included in the expression “betting and gambling” as incorporated under Entry 34 and 62 of List II to Seventh Schedule of Constitution of India.

(iii) The activity of promotion, marketing, organizing or in any other manner assisting in organising game of chance including lottery being an activity of “betting and gambling” under Entry 62, List II

to Seventh Schedule of Constitution of India, the State Legislature alone is competent to levy any tax on such activity under Entry 62.

(iv) The Parliament has the competence and jurisdiction to levy taxes on any subject matter including “service tax” under Entry 97, List I, read with Article 248 of the Constitution of India except where such powers are traceable to any of the entries in List II and III to Seventh Schedule of Constitution of India.

(v) Power to tax the activity of “betting and gambling” as explained above being within the exclusive domain of State Legislature under Entry 62, List II, the Parliament in exercise of its residuary power under Entry 97, List I to Seventh Schedule of Constitution of India lacks legislative competence to impose any tax including “service tax” on such activity.

19. In view of the above conclusions, we allow these petitions, strike down the clause (zzzzn) to sub-section 105 of Section 65 of Finance Act, 1994 as introduced vide Finance Act, 2010 as ultra vires to Constitution of India

having been enacted in contravention to Entry 97, List I to Seventh Schedule read with Article 248 of Constitution of India.

20. We also set aside all the consequential actions of respondents imposing service tax upon the petitioners being distributors of lottery organized by State of Sikkim.

21. Since the petitioners secured registration and paid service tax under the impugned provision on their own, this judgment shall operate prospectively.

22. In the facts and circumstances no order as to costs.

(Permod Kohli)
Chief Justice
29.11.2012

(S.P. Wangdi)
Judge
29.11.2012

Approved for reporting : Yes / No
Internet : Yes / No

pm/jk

(XXIII) In ***Mahindra and Mahindra Ltd.*** v. ***Union of India & Anr.*** reported as **1984 (16) E.L.T. 76 (Bom.)**, it has been held that where distributor purchases goods on payment of a commercial price from the manufacturer, such a buyer is different from a distributor and does not create an agency. The relevant observations are noticed hereunder:-

> **" 10.** Shri Dalal submitted that the agreement between the petitioners and Voltas is really not a distributorship agreement but is in the nature of agreement agency. The learned counsel relied upon Division Bench decision of this Court in the case of *Amer Dye-Chem Limited and another* v. *Union of India and another* reported in 1981 Excise Law Times, 348 and submitted that the mere use of the word 'Distributor' would not lead to the conclusion that the agreement is not an agreement of agency. The Division Bench observed that the distributor in the commercial world is understood to be person who distributes goods of the manufacturer to the consumer and in so doing he acts for and on behalf of the manufacturer. The distributor normally is, therefore, an agent of the manufacturer for the purpose of reaching out the goods to the consumers. Shri Dalal relied upon this observation and claims that Voltas were merely acting as Agents of the petitioners for reaching out the tractors to the consumers. The submission is not correct, as the Division Bench has further observed in the judgment that in the case of the buyer who purchases goods on payment of a commercial price to the manufacturer and transaction in effect is a sale, such a buyer is different from the distributor earlier noticed, though even such a buyer is sometimes described as a distributor. The distributor in such a case is in fact a wholesale buyer and the property in the goods passes to such a buyer. The submission of Shri Dalal, therefore, that as the agreement between the petitioners and the Voltas was described as a distributorship agreement, it should be treated as an agreement of agency cannot be accepted.
>
> **11.** Shri Dalal then submitted that under the agreement, the Voltas were required to carry out the activities of the manufacturers and, therefore, want the petitioners intended to do was to transfer some of the

activities of the manufacturers to Voltas with a view to reduce the assessable value for the purpose of excise. In support of this submission, reliance is placed on three or four conditions under the agreement. It was urged that the Voltas were required to maintain a Sales Organisation and such a condition was not necessary in the agreement if the petitioners had sold the tractors to Voltas because then it was wholly irrelevant to provide as to how the Voltas should dispose of those tractors to the consumers. The condition under the agreement which provides that Voltas were to store the tractors till they are sold to the consumers was also relied upon to claim that the agreement was not at arms length. The provision which required Voltas to carry out afte4r-sale service and the condition which required the petitioners to share half the amount spent on advertisements were highlighted to claim that the price for which the tractors were sold to Voltas did not reflect the true price. It was urged that the price at which the tractors were sold by the petitioners to Voltas was far less than the market price because certain activities required to be performed by the manufacturers were taken over by the Voltas. It is not possible to accept this submission. In the first instance, on the date when the agreement was entered into, the tractors were not liable to be assessed for excise duty and, therefore, there was no occasion to prepare an agreement with an intention to avoid the duty. Secondly, the conditions requiring Voltas to set up Sales Organisation and to provide after-sale service are the usual conditions provided in the agreement with the wholesale buyer and such conditions were also in existence in the agreement which was considered by the Supreme Court in the *Voltas'* case. The fact that the Voltas were required to store the tractors till they are sold to the consumers cannot be treated as transfer of manufacturer's activity in favour of the buyer. The fact that the expenses in regard to the advertisements were to be shared by the petitioners and Voltas merely indicate that both the wholesale buyer and the petitioners were interested in having greater production and sale thereof and that condition, in my judgment, cannot be considered as relevant to reach the conclusion that the agreement was not at arms length.**"**

(XXIV) In ***Pioneer Tools and Appliances (P) Ltd.*** v. ***Union of India*** **: 1989 (42) E.L.T. 384 (Bom.)**, it has been held as under:-

"5**.** This judgment clearly demonstrates the fallacy of the reasoning adopted by the first respondent in the order passed in revision. Mr. R. L. Dalal, learned counsel for the respondents, however, laid emphasis upon the fact that Rallis India was described as the first petitioner's distributor. He referred me to the decision of the division bench of this court in *Amar Dye-Chem Limited and another* v. *Union of India and another,* 1981 E.L.T. 348. The court held that the distributor normally was an agent of the manufacturer for

> the purpose of distributing the goods to the consumers. He was not a buyer of the goods from the manufacturer on his own account and did not himself pay the price of the goods purchased before the goods were passed on to the consumer. But, merely by the use of the word 'distributor' in the list filed by the petitioner, it could not be said that the distributor was a related person. What was material was the real substance of the transaction. If the distributor bought the goods and the price was the sole consideration of the sale and the transaction was at arms length, he could not be categorized as a related person. In the case of a buyer who purchased, the goods on payment of a commercial price, from the manufacturer and the transaction in effection was a sole, such a buyer even though a kind of distributor was different from the distributor who acted as an agent of or on behalf of the manufacturer. In such a case the distributor was in fact the wholesale buyer and the property and the goods passed such a buyer. It is difficult to see how this judgment furthers the respondent's case. It is averred in the petition and, indeed, has been averred at all the times by the first petitioners before the authorities that they sold their products to Rallis India on an outright basis in a arms length transaction. There is no statement by the authorities which disputes this. There is no affidavit-in-reply which disputes the correctness of the averment made in the petition. It must, therefore, be accepted that this was the real nature of the transaction between them. This being so, it is immaterial that Rallis India is described as the distributor of the first petitioners."

(XXV) In ***Philips India Ltd.*** v. ***Collector of Central Excise*** **: (1997) 91 E.L.T. 540**, it has been held as under:-

> "**6.** As to the after sales service that the dealer was required under the agreement to provide, it did of course enhance in the eyes of intending purchasers the value of the appellant's product, but such enhancement of value ensured not only for the benefit of the appellant; it also ensured for the benefit of the dealer for, by reason thereof, the dealer got to sell more and earn a larger profit. The guarantee attached to the appellant's products specified that they could be repaired during the guarantee period by the appellant's dealers anywhere in the country. Thus, though one dealer might have to repair goods sold by another dealer and incur costs in that regard, he also had the benefit of having the goods he sold reparable throughout the country. The provision as to after sales service, therefore, benefitted not only the appellant; it was a provision of mutual benefit to the appellant and the dealer."

(XXVI) Similarly, in ***Collector of Central Excise, Baroda*** v. ***Besta Cosmetics Ltd.*** reported as **2005 (183)**

E.L.T. 122 (SC), it has been held that the clause of advertisement being purely optional would not militate against the price which is at arm's length. The following observations are relevant: -

> **"** **2.** In addition, we may note that the relevant clause in the agreement between the assessee and its Marketing Agent relating to advertisements reads as follows (wherein the marketing agent is referred to as BHPL) :
>
> > "BHPL shall market the said product in the trade name or the trademark of BCL in respect of the said product. BHPL may, at its own free will, make it known generally that the products of BCL are marketed by them. BHPL for this matter, may adopt such ways and means and may incur such expenses on Advertising and Business promotion as it may deem fit and necessary. At the same time, BHPL should ensure that it does not infringe or in any way prejudicially effect the trade name and or trademark of the said product."
>
> **3.** The appellant has sought to rely upon the decision of this Court in *Commissioner of Central Excise, Surat* v. *Surat Textile Mills Ltd.* – 2004 (5) SCC 201. In that decision the Court appears to have upheld the view that where the advertisement cost is incurred by the manufacturers/customers compulsorily or mandatorily, and where the manufacturer has an enforceable legal right against the customers to insist on incurring of such advertisement expenditure by the customers, the advertisement cost would be includible in the assessable value. Without in any fashion affirming the view taken therein it is clear even on the basis of the judgment that the clause in question gave the manufacturers/marketing agent, the discretion whether or not to advertise the assessee's products. There was no 'enforceable legal right' with the assessee to insist on the advertisement under the agreement.**"**

(XXVII) A question whether discount granted by the State of Kerala on sale of lotteries to distributors is in nature of commission liable to income tax deduction at source under Income Tax Act came to be considered by High Court of Kerala in the case of ***Commissioner of Income Tax, Thiruvananthapuram v. M. S. Hameed.*** It has been held

that the relationship between the distributors in the trade of lottery as being one of principal to principal and the discount of lottery is not a commission and thus, provision of Section 194(G) of the Income Tax Act, 1961 which obliged a person to deduct tax at source on payment of commission, will not be attracted. The relevant extract of the judgment is reproduced hereunder:-

> "4. The petitioners receive in bulk quantities of lottery tickets from the State Government. They are given a discount which is on a slab system. Exhibit P-1 is the governing order issued in 1998. The agents commission presently payable is as follows:
>
> . For the purchase of 100 tickets 25%
>
> . For the purchase of 101 and above 27.5%
>
> . For the purchase of 50,001 and above 28%
>
> . For the purchase of 70,00,001 and above 28.5%
>
> 5. The import of the order will be that for a ticket worth Re. 1 an agent need pay between 75 paise to 71.5 paise only, depending on the off take. The petitioner submits that there is no agency agreement, and the petitioners are termed as agents only on a loose basis. From the nature of the transactions, the Government and the petitioners deal as principal to principal. The tickets purchased are thereafter distributed through other agents, and sub-agents, according to them, on commission basis. They point out that after purchase of the tickets, it is not the Government's look out as to how and when they are divided or distributed, and there is no control over the affairs thereafter. Therefore, the principal contention of the petitioner is that there is only payment of the price of the tickets fixed as payable by the principal, and no commission or discount are paid to them by the Government. As such, it is the contention of the petitioners that Section 194G of the Act has no application, and hence the demand of tax, as coming through exhibit P-4 is unsustainable and without jurisdiction.
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> .....
>
> 7. Before exhibit P-4, the deduction of ten per cent, was not being made, and the petitioners submit that thereafter the tax deduction has commenced. The submission of Mr. K. R. Prasad, senior counsel, appearing on instructions, for the petitioners, could be summarized as following: The provisions for collection and recovery of Income Tax appearing in Chapter XVII of the Act refers to various methods, viz., deduction at source, collection at source,

advance payment of tax, collection by recovery and levy of interests, etc. Since Section 194G comes within the sub-heading "Deduction at source", for the mechanism, according to counsel, a statutory authorization is essential. When the petitioners purchase tickets, they became absolute owners thereof. He also referred to Rule 25 of the Kerala State Lottery Rules, to the effect that in the case of loss of tickets, no compensation was payable. The petitioners were never agents of the State, and in no capacity, render any service to the State. For the face value of a ticket of Rs. 1, the petitioners were expected to pay 71.5 paise and they could have purchased a ticket worth one rupee by raising only 71.5 paise. That the ticket might be worth one rupee did not mean that the balance of 28.5 paise was the petitioner' income. Referring to the text book (Kanga and Palkiwala on Income-tax) (page 92, 7th edition) he referred to the discussion based on the authorities to urge that mere relief from expense cannot be income. A person is chargeable to tax not on what he saves in his pocket, but what goes into his pocket. Counsel urged that Section 194G, as it stands in the statute book, cannot have application to the petitioners, as has been attempted to the explained by exhibit P-4.

.....

16 If the face value of the ticket, for example, is Re. 1, notwithstanding the circumstance the petitioners receive it for 72 paise. The State, therefore, releases a ticket, receiving 72 paise. The petitioner may sell the ticket so obtained at any price of their choice. It is not the State's business to enquire into the matter at all. Therefore, it is difficult to assume that the petitioners have in all cases made a margin of 28 paise by the mere purchase of the ticket. His case is that resells it for 72.5 paise, and he derives a profit of half paise per ticket. He may be right or that may be a misleading statement. But he has been able to obtain a ticket worth Re. 1 for 72 paise. His total input therefore is 72 paise, and in that context it is difficult to describe the transaction as one whereby because of investment of 72 paise he has simultaneously made a profit of 28 paise. Several "ifs" have to be employed, which do not exist in real life, for this court to accept the case of the Department that by the factum of purchase he had already made a profit.

.....

23. Therefore, the demand of tax is to be shown as one on the income of the person concerned. There is neither payment of cash or by cheque, and the Government never credits any income to the account of the persons like the petitioners. When the deduction is contemplated at the time of payment to the person concerned and when it is shown that there is no payment to the agent at the time of purchase of the ticket, the section automatically becomes inapplicable. If any prize or remuneration is payable by the Government, to any person, deduction at source as envisaged under the section, may arise. But when no payment is made in view of the mandate of the section, no deduction is envisaged. That the ticket is given on a discount of 28 per cent., can by no imagination be pressed into service for an interpretation that, none the less, ten per cent, of 28 paise is deductible as tax. Perhaps the intention

> might have been to bring the agents within the tax net, but the section as it stands, according to me, is not authority for taxation at source, as is envisaged by exhibit P-4.**"**

This decision has been upheld by a Division Bench of Kerala High Court and SLP filed against it already stands dismissed.

(XXVIII) Delhi High Court in ***Commissioner of Income Tax*** v. ***Jai Drinks Pvt. Ltd.*** reported as **2011 (336) ITR 383 (Del.)** expressed similar view and observed as under: -

> **"**3. A survey was conducted under Section 133A of the Act and the assessing officer passed an order holding that the payment made by the Assessee to the distributor constituted commission under Section 194H of the Act. The assessing officer held that the Assessee defaulted in not deducting the tax at source on the amount of commission paid to the distributor and consequently, determined the total tax liability of Rs.40,06,679/- under Section 201(1) & 201 (1A) of the Act. Assessee preferred an appeal before the Commissioner of Income Tax (Appeals) (hereinafter referred to as Commissioner (Appeals) which was allowed. The Commissioner (Appeals) held the payments made by the Assessee as incentives in the normal course of buying and selling. The revenue preferred an appeal against this order before the ITAT which was dismissed holding that the nature of transaction between the Assessee and the distributor is not that of principal-agent, but principal-to-principal and that the payment given by Assessee to the distributor is nothing but a discount and did not have the characteristics of commission.
>
> .....
>
> 9. From all that has been noted above, it is evident that the distributor was to purchase products at pre-determined price from the Assessee for selling the same within specified area. The products were to be purchased by the distributor against 100% advance payment or may be some times on credit at the discretion of the Assessee. Both the Assessee and the distributor have been collecting and paying their sales tax separately. Both the parties have clearly understood and accepted the agreement between them. That being the arrangement between the Assessee and the distributor, it could not be said that the relation between them was that of principal-agent. On the other hand it was clearly stipulated to be an agreement between them on principal-to-principal basis. Both the Commissioner (Appeals) and also the ITAT rightly held that the payments being made by the Assessee to the distributor were

incentives and discounts and not commissions. We find no infirmity in the findings of the Commissioner (Appeals) and also ITAT.”

(XXIX) It is common case of the parties that the service tax has been levied vide Finance Act, 1994 as amended in 2010 by introducing organization, promotion of lottery etc. as a taxable service. Section 66 prescribes 12% as the rate of service tax of the value of the taxable service whereas Section 67 deals with valuation of taxable services for charging service tax. The relevant extract of both the sections are reproduced hereunder: -

> **“ 66. Charge of service tax**
>
> There shall be levied a tax (hereinafter referred to as the service tax) at the rate of twelve per cent of the value of taxable services referred to in sub-clauses ……
> ……
> ……..
>
> (zzzzn) ……. of clause (105) of section 65 and collected in such manner as may be prescribed.
>
> **67. Valuation of taxable services for charging service tax**.- (1) Subject to the provisions of this Chapter, where service tax is chargeable on any taxable service with reference to its value, then such value shall,—
>
> (i) in a case where the provision of service is for a consideration in money, be the gross amount charged by the service provider for such service provided or to be provided by him;
>
> (ii) in a case where the provision of service is for a consideration not wholly or partly consisting of money, be such amount in money as, with the addition of service tax charged, is equivalent to the consideration;
>
> (iii) in a case where the provision of service is for a consideration which is not ascertainable, be the amount as may be determined in the prescribed manner.

(2) .....

(3) .....

(4) .....

Explanation.—For the purposes of this section,—

(a) "consideration" includes any amount that is payable for the taxable services provided or to be provided;

(b) .....

(c) ....."

(XXX) Rule 6 of the Service Tax Rules, 1994 provides modes for payment of service tax. The Government of India issued Notification No. 49/2010-Service Tax dated 8th October, 2010 introducing sub-rule 7(C) under Rule 6 providing the mode of payment of service tax as regards the promotion, marketing, organizing or in any manner assisting in organizing lottery is concerned. The relevant extract of the said Rule reads as under: -

"(7C) The distributor or selling agent, liable to pay service tax of promotion, marketing, organizing or in any other manner assisting in organizing lottery, shall have the option to pay an amount at the rate specified in column (2) of the Table given below, subject to the conditions specified in the corresponding entry in column (3) of the said Table, instead of paying service tax at the rate specified in section 66B of Chapter V of the said Act:

Table

Sl. No.	Rate	Condition
(1)	(2)	(3)
1.	Rs.7000/- on every Rs.10 Lakh (or part of Rs.10 Lakh) of aggregate face value of lottery tickets printed by the organizing State for a draw	If the lottery or lottery scheme is one where the guaranteed prize payout is more than 80%
2.	Rs.11000/- on every Rs.10 Lakh (or part of Rs.10 Lakh) of aggregate face value of	If the lottery or lottery scheme is one where the guaranteed prize

	lottery tickets printed by the organizing State for a draw.	payout is less than 80%

Provided that in case of online lottery, the aggregate face value of lottery tickets for the purpose of this sub-rule shall be taken as the aggregate value of tickets sold, and service tax shall be calculated in the manner specified in the said Table.

Provided further that the distributor or selling agent shall exercise such option within a period of one month of the beginning of each financial year and such option shall not be withdrawn during the remaining part of the financial year.

Provided also that the distributor or selling agent shall exercise such option for financial year 2010-11, within a period of one month of the publication of this sub-rule in the Official Gazette or, in the case of new service provider, within one month of providing of such service and such option shall not be withdrawn during the remaining part of that financial year. **“**

The petitioners’ case falls in Sl. No. 2, the prize money being less than 80%.

(XXXI) From the conjoint reading of Sections 66, 67 and Rule 7(C) it appears that the service tax payable by a service provider for promotion, marketing, organizing or in any manner assisting in organizing lottery @ 12% or in the manner indicated in the table above on the value of the service provided or to be provided. In respect to the online lotteries the aggregate value of the lottery ticket is to be taken as the value of the service on which service tax is payable. In respect to the paper lottery also the same mode has been adopted and gross value of the lottery ticket has been taken as the valuation for the purpose of levy of service tax. During the course of argument, Mr. Razzak

after seeking instructions admitted that the service tax is being charged at the gross value of the lottery ticket i.e. Re.1/- or in the manner prescribed in the Rule 7(C) as introduced vide Notification dated 8th October, 2010. It is relevant to note that according to Mr. Razzak's submission the 30% discount allowed by the State Government to the petitioners is for rendering service, whereas admittedly 70 paise is the price of the lottery ticket. According to respondents own case only 30% amount of the gross value can be taken as the valuation for providing service if at all the activity of petitioners is to be construed as a service and falls within the definition of "taxable service". The Ministry of Finance (Department of Revenue), Central Board of Excise and Customs, Government of India has also issued a clarificatory circular dated 10.11.2006 laying down the criterion for levy of service tax. The relevant extract is reproduced hereunder:-

> "4. To levy service tax, the following criteria are to be satisfied:
>
> - The service provided or to be provided satisfies the definition of taxable service.
> - There should be receipt of consideration for the taxable service provided."

(XXXII) In view of the above clarification, it is pleaded on behalf of the petitioners that receipt of consideration for providing "taxable service" is one of the essential ingredients

to establish that any service is a “taxable service”. It is submitted that in the instant case, the Government does not pay any consideration in any form for the activities to be performed by the petitioner for promotion of the sale by advertisement etc. To the contrary, the petitioner is paying the minimum guaranteed sum towards the full sale consideration to the Government and thus the entire claim of the respondents that the petitioner is providing taxable service is belied by its own circular and understanding of the nature of the petitioner’s activity.

GROUND (B)

(I) This ground comprises of different limbs, i.e.

(i) whether the conduct of lottery is an Act of “Betting and Gambling” envisaged under entries 34 and 62 of List II to Schedule 7;

(ii) whether it is within the exclusive domain of State legislature to impose taxes on organising lotteries being an act of “Betting and Gambling”;

(iii) whether the Parliament has the competence to enact law in exercise of its residuary legislative power under entry 97 of List I to Schedule 7 dehors the entries 34 and 62 of List II;

(iv) whether the State legislature and Parliament both can simultaneously impose taxes on the conduct of lottery by the State Government under entry 62 of List II and entry 97 of List I to Schedule 7, if so, under what circumstances; and

(v) whether such circumstances exist in the case in hand?

(II) We would like to deal with each limb of Ground-B separately.

(i) <u>whether the conduct of lottery is an Act of "Betting and Gambling" envisaged under entries 34 and 62 of List II to Schedule 7</u>

(a) "Lottery" has been defined under Section 2(b) of the regulatory Act of 1998, which reads as under:-

> **"**(b) "lottery" means a scheme, in whatever form and by whatever name called, for distribution of prizes by lot or chance to those persons participating in the chances of a prize by purchasing tickets;**"**

From the above definition, it transpires that lottery is a game of chance of those persons who participate in the chances of a prize by purchasing tickets. The expressions "betting and gambling" have been defined in the Black's Law Dictionary separately in the following manner: -

> **"betting** – A system of gambling in which bets placed on a race are pooled and then paid to those holding winning tickets.**"**
>
> **"gambling** – The act of risking something of value, esp. money, for a chance to win a prize.**"**

Above definitions include any act by which a person participates in a game of chances by risking money for purchase of ticket to win a prize. From these definitions and the definition of lottery under the regulatory Act, it is apparent that lottery is also a game of chance where a ticket-holder risks his money to win a prize on a chance. Section 294A of the IPC punishes a person who keeps any office or place for the purpose of drawing any lottery or even the proposal to pay any money or to deliver any goods on any event or contingency of any ticket or any figure in the lottery as an offence except where it is run or authorized by the State Government. The lottery, *per se*, does fall within the expressions "betting and gambling" which Act is pernicious in nature. It gets a legal umbrella only if it is run or authorized by the State Govt. subject to the conditions enumerated under Section 4 of the Lotteries (Regulation) Act, 1998. It is a privilege of the State which can be partially parted to any other person subject to the performance of statutory conditions contained in the regulatory Act.

(b) Lottery has been declared to be falling within the expressions "betting and gambling" by the Hon'ble Supreme Court in **B*. R. Enterprises*** v. ***State of U.P. & Ors.* :**

(1999) 9 SCC 700. The relevant observations are quoted hereunder:-

> **" 64.** For this, we revert to scrutinize as to what made lotteries gambling and how State lotteries cleanses this character. As we have already recorded, the difference between gambling and trade is that gambling inherently contains a chance with no skill, while trade contains skill with no chance. What makes lottery pernicious is its gambling nature. Can it be said that in the State-organised lotteries this element of gambling is excluded? There could possibly be no two opinions that even in the State lotteries the same element of chance remains with no skill. It remains within the boundaries of gambling. The stringent measures and the conditions imposed under the State lotteries are only to inculcate faith in the participant of such lottery, that it is being conducted fairly with no possibility of fraud, misappropriation or deceit and assure the hopeful recipients of high prizes that all is fair and safe. That assurance if from stage one to the last with full transparency. No doubt, holding of the State lotteries for public revenue has been authorised, legalised and once this having been done it is expected from the State to take such measure to see that people at large, faithfully and hopefully participate in larger number for the greater yield of its revenue with no fear in their mind. The Act further ensures by virtue of Section 4(d) that the proceeds of the sale of such lottery tickets is credited to the public accounts of the State. This is to give clear message to the participants that the proceeds are not in the hands of an individual group or association but is ensured to be credited in the State accounts. But, as we have said, this by itself would not take it outside the realm of gambling. It remains within the same realm. In this regard, there is no difference between lotteries under Entry 34 List II and a lottery organised by the State under Entry 40 List I. when character of both the State-organised lotteries and other lotteries remains the same, by merely placing the apparel of the State with authority of law, would not make any difference; it remains gambling as element of chance persists with no element of skill. …….. **"**

(c) A similar view has been expressed by the Hon'ble Supreme Court in case of ***Union of India & Ors.*** v. ***Martin Lottery Agencies Limited*** **: (2009) 12 SCC 209**. The relevant observations are reproduced hereunder:-

> **" 17.** We fail to persuade ourselves to agree with the aforementioned submission. The law, as it stands today (although it is possible that this Court in future may take a different view), recognises lottery to be gambling.

> Gambling is res extra commercium as has been held by this Court in *State of Bombay* v. *R.M.D. Chamarbaugwala* and *B.R. Enterprises* v. *State of U.P.*"

Thus, in view of the clear and categorical opinion of the Apex Court, we have no hesitation in saying that the conduct of lottery is an act of "betting and gambling" envisaged under entries 34 and 62 of List II to Schedule 7.

(ii) whether it is within the exclusive domain of State legislature to impose taxes on organising lotteries being an act of "Betting and Gambling"

(iii) whether the Parliament has the competence to enact law in exercise of its residuary legislative power under entry 97 of List I to Schedule 7 dehors the entries 34 and 62 of List II;

Since both these limbs are interrelated, the same are being taken up for consideration conjointly.

(d) Entry 34 of List II to Schedule 7 prescribes "Betting and Gambling" as a field of legislation within the domain of the State. Entry 40 also provides lotteries organized by the Government of India or the Government of a State as a field of legislation for which the Union legislature can enact a law. Entry 34 has much wider field and it may include many other activities apart from the lotteries for which the State legislature may enact a law. However, under entry 40 the Parliament is competent to enact law only in respect to lotteries as a species of betting and gambling. Lottery thus is a common subject matter for

which both the Union Parliament and State Legislature can enact laws and fall in their respective legislative competence under Article 246 of the Constitution of India. The laws to be enacted under both these entries, however, could only be regulatory in nature and nothing beyond that. Where any field of legislation is available to both the Parliament and the legislature of a State and both the legislative bodies enact laws having competence to do so, in the event of conflict the State law to the extent of repugnancy shall be void if such law is enacted pursuant to any entry under List III (Concurrent List). However, the situation where the Parliament enacts a law on the subject matter under any one of the entries in List I and the State legislature also enacts a law touching the same subject matter pursuant to an entry in List II or vice versa, the position would be different. This seems to be the spirit underlying Article 246 read with Article 254 of the Constitution of India subject to exceptions under various Articles in Part XI Chapter I. This should not detain us as admittedly the Parliament alone has enacted the Lotteries (Regulation) Act, 1998 under entry 40 and there is no corresponding law enacted by the State legislature under entry 34 in respect to the regulation of the lotteries. As noticed above power to regulate does not

include power to tax, taxing powers having been conferred and specified under separate entries in Seventh Schedule.

(e) In case of ***State of West Bengal & Ors.*** v. ***Purvi Communication (P) Ltd. & Ors.*** **: (2005) 3 SCC 711**, it has been held by the Hon'ble Supreme Court that the power to regulate does not include power to tax. The relevant observations are noticed hereunder:-

> **" 35.** The Cable Television Networks (Regulation) Act, 1995, a Central legislation, has been enacted to regulate the operation of cable television networks in the country and for matters connected therewith. This enactment does not, in our opinion, fetter the legislative power or competence of the State to levy tax on luxuries including taxes on entertainments, amusements, betting and gambling falling under Entry 62 of List II of the Seventh Schedule to the Constitution. The power of regulation or control under the said Central enactment is separate and distinct from the power of taxation by the State Legislature under Entry 62 of List II; being a specific power, the power of taxation cannot be cut down or fettered by the general power of regulation as exercised by Parliament in enacting the said 1995 Act. ……..
> ……..…….."

(f) Indubitably, there is no specific entry under List I empowering the Parliament to levy tax on lotteries or even on "betting and gambling". The service tax sought to be imposed is in exercise of the residuary power vested in the Parliament under entry 97 of List I read with Article 248 of the Constitution of India. In so far the List II is concerned, entry 62 specifically provides for levy of taxes on "betting and gambling". As observed by us above and held by

Hon'ble Supreme Court in ***B.R. Enterprises and Martin Lottery Agencies Ltd.*** (supra), lottery does fall within the expressions "betting and gambling". The first question for consideration would be whether the power to impose tax on lotteries is same thing as to impose tax on "betting and gambling". Though no entry in any of the Lists to Seventh Schedule specifically provides for levy of taxes on lotteries, the power to enact law for imposition of tax on lotteries have to be construed as inherent in the expressions "betting and gambling", lottery being one of such activity.

(g) Entry 97 of List I authorizes the Parliament to enact a law including for imposition of taxes in respect to any other matter not enumerated in List II or List III. Article 248, which is the source of power, confers exclusive jurisdiction upon the Parliament to make any law in respect to any matter not enumerated in "State List" or "Concurrent List" and under Sub-clause (2) such power also includes power to make law for imposition of tax not mentioned in either of those Lists, i.e. Lists II and III respectively.

(h) The scope of legislative competence of the Parliament to make laws under entry 97 of List I came up for consideration before a Constitution Bench of the Hon'ble

Supreme Court in ***Union of India*** v. ***Shri Harbhajan Singh Dhillon*** **: 1971 (2) SCC 779**. In this case, vires of the Section 27 of the Finance Act, 1969, in so far it amended the Wealth Tax Act, 1957 so as to include the capital value of the agricultural land for purposes of commuting wealth came to be challenged as being beyond the exclusive competence of the Parliament. The petitioners, who challenged the vires of the Act, claimed that the power to tax on agricultural land was within the exclusive competence of the State Legislature under entry 49 of List II – i.e. Taxes on lands and buildings. It was held by the High Court and approved by the Apex Court that the power to levy tax on agricultural land is not contemplated by entry 49, List II. However, the amended Act was struck down by the High Court being beyond the competence of the Parliament by interpreting entry 86 of List I whereunder agricultural land was excluded from capital value of the assets. The amendment brought by the Finance Act was claimed to be under the residuary power under entry 97, List I. While considering this question, the Constitution Bench of the Hon'ble Supreme Court held as under:-

> **"10.** It was further urged by Mr. Setalvad that the proper way of testing the validity of a parliamentary statute under our Constitution was first to see whether the parliamentary legislation was with respect to a matter or tax mentioned in List II, if it was not, no other question would arise. The learned counsel for the respondent contended tha this manner of enquiry had not been even

hinted in any of the decisions of the Court during the last 20 years of its existence and there must accordingly be something wrong with this test. He urged that in so far as this test is derived from the Canadian decisions, the Canadian Constitution is very different and those decisions ought not to be followed here and applied to our Constitution.

11. It seems to us that the best way of dealing with the question of the validity of the impugned Act with the contentions of the parties is to ask ourselves two questions first is the impugned Act legislation with respect to Entry 49, List II and secondly if it is not, is it beyond the legislative competence of Parliament.

12. We have put these questions in this order and in this form because we are definitely of the opinion, as explained a little later, that the scheme of our Constitution and the actual terms of the relevant articles, namely, Article 246, Article 248 and Entry 97, List I, show that any matter, including tax, which has not been allotted exclusively to the State Legislatures under List II or concurrently with Parliament under List III, falls within List I, including Entry 97 of that list read with Article 248.

.....

21. It seems to us that the function of Article 246(1), read with Entries 1-96, List I, is to give positive power to Parliament to legislate in respect of these entries. Object is not to debar Parliament from legislating on a matter, even if other provisions of the Constitution enable it to do so. Accordingly we do not interpret the words “any other matter” occurring in Entry 97, List I, to mean a topic mentioned by way of exclusion. These words really refer to the matters contained in each of the Entries 1 to 96. The words “any other matter” had to be used because Entry 97, List I follows Entries 1-96, List I. It is true that the field of legislation is demarcated by Entries 1-96, List I, but demarcation does not mean that if Entry 97, List I confers, additional powers, we should refuse to give effect to it. At any rate, whatever doubt there may be on the interpretation of Entry 97, List I is removed by the wide terms of Article 248. It is framed in the widest possible terms. On its terms the only question to be asked is : Is the matter sought to be legislated or included in List II or in List III or is the tax sought to be levied mentioned in List II or in List III : No question has to be asked about List I. If the answer is in the negative then it follows that Parliament has power to make laws with respect to that matter of tax.

.....

47. The last sentence applies much more to the Constitution of a sovereign democratic republic. It is true that there are some limitations in Part III of the Constitution on the Legislatures in India but they are of a different character. They have nothing to do with legislative competence. If this is the true scope of

residuary powers of Parliament, then we are unable to see why we should not, when dealing with a Central Act, enquire whether it is legislation in respect of any matter in List II for this is the only field regarding which there is a prohibition against Parliament. If a Central Act does not enter or invade these prohibited fields there is no point in trying to decide as to under which entry or entries of List I or List III a Central Act would rightly fit in.

67. ..... Be that as it may, we have the three lists and a residuary power and therefore it seems to us that in this context if a Central Act is challenged as being beyond the legislative competence of Parliament, it is enough to enquire if it is a law with respect to matters or taxes enumerated in List II. If it is not, no further question arises.

103. The expression "any matter not enumerated in the Concurrent List or State List" in Article 248 must mean, in the context of clause (1) of Article 246, which gives Parliament exclusive power in respect of matters in List I, any matter other than those enumerated in any of the three Lists. Obviously, the residuary power given to Parliament in Article 248 cannot include power which is exclusively given to Parliament on matters in List I already conferred under clause (1) of Article 246, so that an attempt to distinguish the words "any matter" in Article 248 and "any other matter" in Entry 97 in List I is a distinction without difference. There had to be difference in language in the provisions in the context of the content of Entry 97 as that entry speaks about matters other than those enumerated before in List I and those enumerated in the other Lists. Notwithstanding the fact that the residuary power has been vested in the Central Legislature under Article 248 and its consequence translated in Entry 97 in List I, there can be no gainsaying that the idea was to assign such residuary power over matters which at the time of framing three Lists could not be thought of or contemplated. This is clear from the fact as pointed out by counsel, that the Lists contain as many as 209 matters which are couched in careful and elaborate words with inclusive and excluding language in the case of some, which has made the Constitution, to use the words of Gwyer, C.J., in *In re the C. P. and Berar Act No.XIV of 1938* (supra), "unique among federal constitutions in the length and detail of its legislative Lists". In the layout of such elaborately worded matters in the Lists and in the context of Article 246(1), the residuary power contained in Article 248 and Entry 97, List I must be construed as meaning power in respect of matters not enumerated in any of the three Lists. Such a residuary power cannot, therefore, be ordinarily claimed in respect of a matter already dealt with under an article or an entry in any one of the three Lists."

(i) Another Constitution Bench of the Hon'ble Supreme Court in ***West Bengal*** v. ***Kesoram Industries Ltd. & Ors.*** **: (2004) 10 SCC 201** again examined the scope of entry 97 List I and Article 248 to levy tax under residuary power. The relevant observations are quoted as under:-

> **" 100.** Article 265 mandates – no tax shall be levied or collected except by authority of law. The scheme of the Seventh Schedule reveals an exhaustive enumeration of legislative subjects, considerably enlarged over the predecessor Government of India Act. Entry 97 in List I confers residuary powers on Parliament. Article 248 of the Constitution which speaks of residuary powers of legislation confers exclusive power on Parliament to make any law with respect to any matter not enumerated in the Concurrent List or the State List. At the same time, it provides that such residuary power *shall include* the power to making any law imposing a tax *not mentioned in either of those Lists*. It is, thus, clear that if any power to tax is clearly mentioned in List II, the same would not be available to be exercised by Parliament based on the assumption of residuary power.**"**

(j) Hon'ble Bench relied upon the Constitution Bench judgment in ***Union of India*** v. ***Shri Harbhajan Singh Dhillon (supra)*** and the commentary on constitutional law by H. M. Seervai, 4th Edition (Silver Jubilee Edition). The relevant observations quoted in the above judgment are reproduced hereunder: -

> **" 102.** Vide para 22.194 the eminent jurist poses a question:
>
> "*22.194.* Does Article 248 add anything to the exclusive residuary power of Parliament under Article 246(1) read with Entry 97 List I, to make laws in respect of 'any other matter' not mentioned in List II and List III, including any tax not mentioned in those Lists?"
>
> and answers by saying – "The answer is 'No'.**"**

(k) The Hon'ble Court further observed that there is nothing like an implied power to tax and the burden is always upon the taxing authority to point to the act of assembly which authorizes the imposition of the tax claimed. Hon'ble Court further relied upon Justice G.P. Singh's commentary on Principles of Statutory Interpretation (8th Edn., 2001). The relevant quotes are reproduced hereunder: -

> **"106.** The judicial opinion of binding authority flowing from several pronouncements of this Court has settled these principles : *(i)* in interpreting a taxing statute, equitable considerations are entirely out of place. Taxing statutes cannot be interpreted on any presumption or assumption. A taxing statute has to be interpreted in the light of what is clearly expressed; it cannot imply anything which is not expressed; it cannot import provisions in the statute so as to supply any deficiency; *(ii)* before taxing any person it must be shown that he falls within the ambit of the charging section by clear words used in the section; and *(iii)* if the words are ambiguous and open to two interpretations, the benefit of interpretation is given to the subject. There is nothing unjust in the taxpayer escaping if the letter of the law fails to catch him on account of the legislature's failure to express itself clearly. *(See Justice G. P. Singh, ibid.,* pp. 638-39.)
>
> **107.** Power to tax is not an incidental power. According to Seervai, although legislative power includes all incidental and subsidiary power, the power to impose a tax is not such a power under our Constitution. It is for this reason that it was held that the power to legislate in respect to inter-State trade and commerce (Entry 42 List I Schedule 7) did not carry with it the power to tax the sale of goods in inter-State trade and commerce before the insertion of Entry 92-A in List I and such power belonged to the States under Entry 54 in List II. Entry 97 in List I also militated against the contention that the power to tax is an incidental power under our Constitution (See Seervai, H.M. : *Constitutional Law of India,* 4th/Silver Jubilee Edn., Vol. 3, para 22.20.)**"**

(I) In ***N. V. Marketing Pvt. Ltd.*** v. ***State of Maharashtra & Ors.*** **: 2009 (III) (8) Bom. L.R. 3397**, it has been ruled that even though the power of regulation of lotteries vest in the Parliament in terms of entry 40 of List I, power to tax is not incidental power. The Hon'ble Bombay High Court relying upon ***West Bengal*** v. ***Kesoram Industries Ltd. & Ors.*** **: (2004) 10 SCC 201** and various other judgments, while considering the validity of State law enacted by the Maharashtra State imposing tax on lotteries, observed as under:-

> **"3.** It is the contention of the Petitioners that the legislature of State of Maharashtra has no legislative power to enact Laws relating to State Lotteries including Laws relating to taxation, and therefore, according to the Petitioners, the State Act is beyond the legislative competence of the legislature of State of Maharashtra. The second submission is that the enactment of the State Act is colourable exercise of the legislative power in as much as it is another method of levying tax on lottery tickets. The third submission is that the State Act seeks to levy tax on lottery schemes, tax is collected in advance in respect of each draw in the lottery scheme at the rate specified in Section 3 of the State Act. It is submitted that lottery scheme of all other State organising and conducting lotteries save and except that of Maharashtra are formulated outside the State of Maharashtra and therefore, the law has extra territorial application. The fourth submission is that the State Act levies tax on lottery schemes but the term "lottery scheme" is not defined anywhere and therefore, it is violative of guarantee under Article 14 of the Constitution of India. It was also contended that the State Act has been enacted to impose tax on sale of lottery tickets conducted by other State in State of Maharashtra so as to make selling of lottery tickets by the other States uneconomical, unviable and thereby creating monopoly in the lottery tickets of the lotteries conducted by the State of Maharashtra.
>
> .....
>
> **10.** It was then contended before us that though there is specific power vested in the State legislature under Entry 62 of List II of the Seventh Schedule, because of Entry 40 in List I of the Seventh Schedule of the Constitution of India, the Parliament will have legislative

competence to levy tax under Article 248 and Entry 97 in List I of the Seventh Schedule of the Constitution of India. In our opinion, this submission has also no force, because power to tax is not an incidental power and under the residuary power the Parliament will be entitled to impose tax only if that power is not specifically vested in the State legislature by any entry in List II of the Seventh Schedule. ……..”

(Emphasis supplied)

(m) In ***Godfrey Philips India Ltd.*** v. ***State of U.P.*** **: (2005) 2 SCC 515**, the Hon’ble Supreme Court upholding the legislative power of State under entry 62 of List II, held as under: -

“46. Therefore, taxing entries must be construed with clarity and precision so as to maintain such exclusivity, and a construction of a taxation entry which may lead to overlapping must be eschewed. If the taxing power is within a particular legislative field, it would follow that other fields in the legislative lists must be construed to exclude this field so that there is no possibility of legislative trespass.

……

49. Under the three lists of the Seventh Schedule to the Indian Constitution a taxation entry in a legislative list may be with respect to both. Article 246 makes it clear that the exclusive powers conferred on Parliament or the States to legislate on a particular matter includes the power to legislate with respect to that matter. Hence, where the entry describes an object to tax, all taxable events pertaining to the object are within that field of legislation unless the even is specifically provided for elsewhere under a different legislative head. Where there is the possibility of legislative overlap, courts have resolved the issue according to settled principles of construction of entries in the legislative lists.

……

72. In view of the decision in *Sea Customs Act case* the second premise propounded by Mr. Salve is unacceptable. As we have seen, in that case this Court held that the taxable event of ownership is implicit in the concept of taxes on goods. That the entries on taxable events in the legislative lists are not exhaustive is also recognized and provided for in Article 248(2) which provides for the power of Parliament to make any law imposing a tax not mentioned in either the Concurrent or State Lists. This residuary power is reflected in Entry 97 of List I. Furthermore if an article or goods are taxable only with respect to a taxable event, and if, as contended by Mr. Salve, all taxable events have been provided for in the different legislative heads, then by that token no object or goods could be taxable. This would render the various entries in the State List including

> Entries 57 and 58 contentless. As we cannot accept that the taxation entries exhaustively enumerate all taxable events, it does not follow that Entry 62 of List II does not cover goods. It is not possible therefore to hold merely on such a construction of the legislative lists and the taxation entries therein, that Entry 62 List II does not permit the States to levy tax on articles of luxury.
>
> **73.** Having rejected the second premise contended for by Mr. Salve, the next question is whether the language of Entry 62 List II would resolve the issue. The juxtaposition of the different taxes within Entry 62 itself is in our view of particular significance. The entry speaks of "taxes on luxuries *including* taxes on entertainments, amusements, betting and gambling". The word "including must be given some meaning. In ordinary parlance it indicates that what follows the word "including" comprises or is contained in or is a part of the whole of the work preceding. The nature of the included items would not only partake of the character of the whole, but may be construed as clarificatory of the whole.
>
> **74.** It has also been held that the word "includes" may in certain contexts be a word of limitation (*South Gujarat Roofing Tiles Manufacturers Assn.* v. *State of Gujarat*). In the context of Entry 62 of List II this would not mean that the word "luxuries" would be restricted to entertainments, amusements, betting and gambling but would only emphasise the attribute which is common to the group. If luxuries is understood as meaning something which is purely for enjoyment and beyond the necessities of life, there can be no doubt that entertainments, amusements, betting and gambling would come within such understanding. Additionally, entertainments, amusements, betting and gambling arfe all activities. "Luxuries" is also capable of meaning an activity and has primarily and traditionally been defined as such. It is only derivatively and recently used to connote an article of luxury. One can assume that the coupling of these taxes under one entry was not fortuitous but because of these common characteristics.**"**

(n) It has been vehemently argued by Mr. Razzaq that the service tax levied vide clause (zzzzn) under sub-section (105) of Section 65 is a tax on various activities comprising services rendered by the distributors to the State in promotion, marketing, organizing of lottery, etc. It is not a

tax on betting and gambling, per se and is beyond the purview of entry 62 of List II.

The entry 62 empowers the State Legislature to impose tax on luxuries, entertainment, amusement, betting and gambling.

(o) For the purpose of the present petition, the relevant subject matter under entry 62 is "betting and gambling". As held by the Hon'ble Supreme Court in ***Express Hotels Private Ltd.*** v. ***State of Gujarat*** **& Anr. : (1989) 3 SCC 677,** the entries must be construed in the widest possible meaning. Relevant observations are:-

> "**15.** .....The entries should not be read in a narrow or pedantic sense but must be given their fullest meaning and the widest amplitude and be held to extend to all ancillary and subsidiary matters which can fairly and reasonably be said to be comprehended in them."

In the same judgment the vires of various provisions enacted by States of Gujarat, Tamil Nadu, Karnataka and West Bengal, imposing taxes on luxuries provided in hotels and lodging houses came to be challenged. The question arose whether the luxury taxes can be levied only on the articles of luxury or persons enjoying the luxuries under entry 62 and the activity of lodging in a hotel or lodge being not a thing tangible the tax is ultra vires the Constitution. Interpreting the scope of legislative entry particularly the

expression 'luxury' used in entry 62, the Hon'ble Supreme Court held as under:

> **"21.** The concept of a tax on 'luxuries' in Entry 62, List II cannot be limited merely to tax things tangible and corporeal in their aspect as 'luxuries'. It is true that while frugal or simple food and medicine may be classified as necessities; articles such as jewellery, perfume, intoxicating liquor, tobacco, etc., could be called articles of luxury. But the legislative entry cannot be exhausted by these cases, illustrative of the concept. The entry encompasses all the manifestations or emanations, the notion of 'luxuries' can fairly and reasonably (*sic*) can be said to comprehend the element of extravagance or indulgence that differentiates 'luxury' from 'necessity' cannot be confined to goods and articles. There can be elements of extravagance or indulgence in the quality of services and activities."

(p) In ***State of Bombay vs. R.M.D. Chamarbaugwala and another : AIR 1957SC 699***, tax was levied under entry 62 on the promoters of the lotteries. The question that fell for consideration was whether tax on promoters of lotteries, who do not gamble is tax on betting and gambling under entry 62 List II. Rejecting the challenge and upholding the validity of the levy on promoters, the Hon'ble Supreme Court observed as under:-

> "(23) The next point urged is that although the Act may come under Entry 34, the taxing provisions of s. 12A cannot be said to impose a tax on betting and gambling under Entry 62 but imposes tax on trade under Entry 60. Once it is held that the impugned Act is on the topic of betting and gambling under Entry 34, the tax imposed by such a statute, one would think, would be a tax on betting and gambling under Entry 62. The Appeal Court has expressed the view that s. 12A does not fall within Entry 62, for it does not impose a tax on the gambler but imposes a tax on the petitioners who do not themselves gamble but who only promote the prize competitions. So far as the promoters are concerned, the tax levied from them can only be regarded as tax on the trade of prize competitions carried on by them.
>
> This, with respect, is taking a very narrow view of the matter. Entry 62 talks of taxes on betting and gambling and not of taxes on the men who bet or gamble. It is necessary, therefore, to bear in mind the real nature of the tax. The tax imposed by s. 12A is, in

terms, a percentage of the sums specified in the declaration made under s. 15 by the promoter or a lump sum having regard to the circulation and distribution of the news paper or publication in the State.

.....
.....

If taxation on betting and gambling is to be regarded as a means of controlling betting and gambling activities, then the easiest and surest way of doing so is to get at the promoters who encourage and promote the unsocial activities and who hold the gamblers' money in their hands. To collect the tax from the promoters is not to tax the promoters but is a convenient way of imposing the tax on betting and gambling and indirectly taxing the gamblers themselves.

.....
....."

(q) In ***Purvi Communication (P) Ltd.*** (supra) Hon'ble Supreme Court considered the scope of Entry 62 and held that the tax under this Entry may be levied on the person spending on entertainment, on the act of person entertaining or subject of entertainment. Relevant observations are quoted hereunder: -

"**38.** A tax under Entry 62 of List II of the Seventh Schedule to the Constitution may be imposed not only on the person spending on entertainment but also on the act of a person entertaining, or the subject of entertainment. It is well settled by this Court that such tax may be levied on the person offering or providing entertainment or the person enjoying it. The respondents are admittedly engaged in the business of receiving broadcast signals and then instantaneously sending or transmitting such visual or audio-visual signals by coaxial cable, to subscribers' homes through their various franchisees. It has been made possible for the individual subscribers to choose the desired channels on their individual TV sets because of cable television technology of the respondents and of sending the visual or audio-viisual signals to sub-cable operators, and instantly retransmitting such signals to individual subscribers for entertaining them through their franchisees. The respondents' act is, no doubt, an act of offering entertainment to the subscribers and/or viewers. The respondent is very much directly and closely involved in the act of offering or providing entertainment to subscribers who are on his record. For the fact of offering or providing entertainment to the subscribers and/or viewers, the respondents receive

> charges, which are realized or collected by their franchisee from the ultimate subscribers. Their franchisee, called as sub-cable operator under the said 1982 Act having no independent role to ofer or provide entertainments to the subscribers inasmuch as franchisees have to depend entirely on the respondents' communication network and this communication network of the respondents consists of receiving and sending visual images and audio and other information for preparation of the subscribers and/or viewers; without the communication network service of the respondents, no entertainments can be offered or provided to the subscribers and/or viewers.
>
> **39.** In the tax matters, the State Legislature is free, if it has legislative competence, to choose the persons from whom the tax levied on entertainments is to be collected. In other words, what are taxed are the entertainments, which is very much within the ambit of Entry 62 of List II of the Seventh Schedule. It is the respondents who as cable operator for the purpose of the said 1982 Act are engaged in the business of providing or offering entertainments which include showing of films, various serials, cricket matches and dramatic performances to the subscribers, and the tax is imposed on the act of offering such entertainments in this way to such subscribers and/or viewers. The entire communication network service is built up and controlled by the respondents. Whatever amount is received or receivable by the respondent in respect of providing such entertainments is taxable under sub-section (4-a) of Section 4-A of the said 1982 Act which has a direct and sufficient nexus with the entertainments.**"**

(r) Similarly entry 50 under Section 100 of the Government of India Act, 1935 relating to tax on luxuries or entertainment or amusement has been interpreted by the Constitution Bench of the Hon'ble Supreme Court in ***1959 Supp (2) SCR 63=AIR 1959 SC 582 : Western India Theaters Ltd. vs. Cantonment Board***, saying that "the entries in legislative list should not be read in a narrow or restricted sense and that each general word should be held to extend to all ancillary or subsidiary matters which can fairly and reasonably be said to be comprehended in it."

(s) In the matter of organizing, marketing and promotion of lotteries, the State Government who is the promoter and publisher of the lotteries, the distributor, i.e. the petitioner, selling agent and the ultimate purchaser of the lottery ticket who participates in the game of chance are all players in the activity of the betting and gambling. Thus tax envisaged under entry 62 on "betting and gambling" is tax on the activity as held by the Constitution Bench in ***State of Bombay vs. R.M.D. Chamarbaugwala's*** case (supra). The betting and gambling itself is an activity though the lottery ticket is a tangible thing which carries with its right to participate in the game of chance. Thus all activities right from the publishing of the lottery tickets till participation in the game of chance, declaration of draw and even distribution of prize to the winner fall within the purview of expression 'betting and gambling'. Thus power to levy tax on organization, promotion and marketing of lottery being an act of betting and gambling comes within the exclusive domain of entry 62 of List II.

(t) It is also settled legal position that where the entries under different Lists empower the respective legislatures to enact law on any subject matter and the

question arises regarding the legislative competence of the legislative bodies, the doctrine of pith and substance is to be applied to find out the real intention of the legislative entry and the object of enacting a law. As observed in ***State of West Bengal*** v. ***Kesoram Industries Ltd. (supra)*** if any law enacted by Parliament is not traceable in any legislative entry in List II or List III, it is irrelevant whether the power of the Parliament is traceable to a specific entry and Parliament shall be deemed to have legislative competence. Its natural corollary would be if power to enact law on a subject matter including levy of taxes is traceable to any entry in List II and List III, residuary power under entry 97 of List I read with Article 248 of the Constitution of India will not be available to it, the same having been specifically restricted under entry 97 of List I and Article 248 of the Constitution.

(u) In the instant case, the power to tax on lotteries or even "betting and gambling" is not available under any of the entries of List I. However, such power is germane to and emanates from entry 62 of List II in Seventh Schedule, meaning thereby that the residuary power to enact a law imposing tax on lotteries would not be available to the Parliament.

(v) Mr. Razzak, Learned Additional Solicitor General, submits that since the service tax is a new concept and a new tax regime, it could not be said that at the time of enacting the entries the intention of the Framers of the Constitution was to include all kind of future taxes within the purview of taxes under entry 62 or for that matter any other entry in Seventh Schedule, wherein the power to enact a law imposing taxes has been indicated. His submission is that service tax is not mentioned in any of the entries and thus it should be deemed to be excluded from the entry 62 or for that matter any other entry in Lists II and III to Seventh Schedule. This argument apparently appears to be attractive but its fallacy is exposed if the proposition is applied to all taxing entries irrespective of Lists. On the same analogy, the power to impose a tax not prevalent or envisaged when entry 97 was incorporated in List I, the service tax would also be beyond its purview. "Tax" has been defined under the Black's Law Dictionary in the following manner: -

> **"tax,** *n.* A monetary charge imposed by the government on persons, entitles, transactions, or property to yield public revenue. ● Most broadly, the term embraces all governmental impositions on the person, property, privileges, occupations, and enjoyment of the people, and includes duties, imposts, and excises. Although a tax is often thought of as being pecuniary in nature, it is not necessarily payable in money."

(w) Article 366 of the Constitution of India defines various expressions used in the Constitution. "Taxation and Tax" being one of such expressions defined under clause (28) thereof. The relevant extract reads as under:-

> **" 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 –
> .....
> .....
>
> (28) "taxation" includes the imposition of any tax or impost, whether general or local or special, and "tax" shall be construed accordingly;
> .....
> ....."

(x) This definition is of widest possible amplitude and encompasses within its field any kind of tax that could be visualized or conceptualized. In ***D. G. Gose and Co. Pvt. Ltd. & Ors.*** v. ***State of Kerala & Anr.*** **: (1980) 2 SCC 410**, a Constitution Bench of the Hon'ble Supreme Court, while considering clause (28) of Article 366 of the Constitution, observed as under:-

> **"5.** The word "tax" in its widest sense includes all money raised by taxation. It therefore includes taxes levied by the Central and the State legislatures, and also those known as "rates", or other charges, levied by local authorities under statutory powers. "Taxation" has therefore been defined in clause (28) of Article 366 of the Constitution to include "the imposition of any tax or impost, whether general or local or special", and it has been directed that "tax" shall be "construed accordingly"."

(y) Various entries empowering the Parliament and State Legislatures to enact laws for levy of tax do not mean

or confine the kind of taxes prevalent or invogue at the time these entries were enacted in Seventh Schedule. The word “tax” includes all kinds of taxation present or future that may be thought of by the competent legislative body. Thus the argument of Mr. Razzak that service tax does not find mention in entry 62 and thus is beyond its purview cannot be accepted or appreciated. Any kind of tax that may be envisaged and can be legally conceptualized by the legislative body falls within the purview of tax in view of all embracing definition of expressions “tax (taxation)” under clause (28) of Article 366. Service tax though a new regime but it would be antithesis of the term “tax” if considered to be a category of tax not envisaged by any of the entries in Seventh Schedule empowering to levy tax. Applying the principle of pith and substance, the power to levy tax on lottery being a game of chance and included in the expressions “betting and gambling” in entry 62 List II, the State Legislature has the exclusive legislative competence and jurisdiction of Parliament to levy such a tax in exercise of its residuary power under entry 97 of the List I read with Article 248 of the Constitution shall stand excluded. There is another important aspect; entry 92C – ‘Taxes on services’ was also incorporated in List I Seventh Schedule by Eighty-

eighth Constitutional Amendment Act, 2003. However, this entry has not been notified till date.

(z) Our opinion that the Parliament lacks legislative competence to levy service tax on lotteries in exercise of its legislative power flowing from entry 97 List I read with Article 248 of the Constitution should not be construed to mean that the Parliament has no jurisdiction whatsoever to levy service tax in respect to any of the subject matter. The legislative competence of the Parliament to impose service tax has to be conceded by virtue of entry 97 List I read with Article 248 of the Constitution as held by Hon'ble Supreme Court in various judgments noticed by us hereinbefore and later part of this judgment. However, such legislative power is prohibited in respect to any subject matter where the power to impose or levy tax has been conferred upon the State Legislature in List II (State List) or the Provincial Legislature and the Parliament under List III (Concurrent List). It is also pertinent to say that Parliament would also be deprived of the residuary power in respect to any subject matter falling even in the List I where such power is traceable to any of the entries contained therein i.e. entries 1 to 96. It would not be improper to say that the residuary power of the Parliament would come into life only where none of the entries in any of the Lists provide for legislative

field. However, as interpreted by the Hon'ble Apex Court in ***State of West Bengal*** v. ***Kesoram Industries Ltd. (supra)***, the only embargo on exercise of the residuary power of Parliament under entry 97 List I read with Article 248 of the Constitution would be non-existence of legislative power of any of the Legislatures under Lists II and III, Schedule 7. At the cost of repetition we may say that where the legislative power whether to enact a law in general or for levy of tax is not envisaged under Lists II and III, the Parliament would be fully competent to enact a law including imposing a tax (Service Tax) under entry 97 List I. We are of the considered view that Parliament would have legislative competence to impose tax including service tax upon lotteries but for entry 62, List II. It is the exclusive legislative domain of the State Legislature to levy tax of any nature on lotteries by virtue of entry 62 List II, Schedule 7.

(iv) whether the State legislature and Parliament both can simultaneously impose taxes on the conduct of lottery by the State Government under entry 62 of List II and entry 97 of List I to Schedule 7, if so, under what circumstances;

(aa) Mr. Farooq Md. Razzak, Addl. Solicitor General, appearing for the Union of India, submits that the service tax levied vide the impugned clause (zzzzn) to Sub-section (105) of Section 65 is not a tax on the activity of "betting

and gambling" but on services like promotion, marketing, organising or in any other manner assisting in organising games of chance including lottery. His further submission is that the service tax is on an activity and is a Value Addition Tax. To explain his contention it is stated that the value addition is on account of activity like marketing, organising and promoting the lottery and such activity renders value addition to the lotteries held by the State of Sikkim and, thus, does not fall within the purview of "betting and gambling" in entry 62 of List II. His submission is that on account of non-application of entry 62, the Parliament is entitled to exercise its legislative jurisdiction to enact the law under its residuary power under entry 97 of List I. According to Mr. Razzak, a lottery ticket of Re.1/- is being given to the petitioner's company for 70 paise for providing various services as noticed by us in the earlier part of this judgment and the service tax is chargeable on the gross amount of the lottery tickets under Section 67 of the Finance Act, 1994 as amended by Finance Act, 2010. It is further argued that the measure of tax cannot be questioned by the petitioner that too in writ proceedings and it is for the competent adjudicating authority to decide the issue. It is contended that the petitioner has straight way approached this Court without having approached the competent

adjudicating authority in this regard. Under such circumstances, the petitioner should be directed to approach the competent adjudicating authority for seeking adjudication regarding levy of service tax on the service rendered by it. He has placed reliance upon the judgment of the Apex Court reported as ***Association of Leasing & Financial Service Companies*** v. ***Union of India*** **: (2011) 2 SCC 352.**

(ab) In the above case the controversy before the Hon'ble Supreme Court was with regard to levy of service tax on the transaction of equipment leasing and hire purchases undertaken by non-banking financial companies. The plea of the writ petitioners who challenged the vires of the levy was that the transaction of equipment leasing and hire purchase and financing has been constitutionally defined as sale and purchase under Article 366 (29A) and thus falls within the exclusive competence of State Legislature under entry 54 of List II, hence the Parliament in exercise of its legislative competence under entry 97 of List I of Seventh Schedule of the Constitution is not competent to levy service tax. Hon'ble Apex Court on consideration of entire issue came to the conclusion that part of the transaction constitute sale for which the State Legislature is competent to impose tax under entry 54 of List II whereas

the components of the transaction constituting service fall within the legislative competence of the Parliament under its residuary power under entry 97 of List I. Validity of the service tax imposed under Section 65(105)(zm) has been upheld. The relevant observations in this regard are quoted hereunder:-

> "**59.** Applying the above decisions to the present case, on examination of the impugned legislation in its entirety, we are of the view that the impugned levy relates to or is with respect to the particular topic of "banking and other financial services" which includes within it one of the several enumerated services viz. financial leasing services. These include long-term financing by banks and other financial institutions (including NBFCs). These are services rendered to their customers which comes within the meaning of the expression "taxable services" as defined in Section 65(105)(zm). The taxable event under the impugned law is the rendition of service. The impugned tax is not on material or sale. It is on activity/service rendered by the service provider to its customer. Equipment leasing/hire-purchase finance are long-term financing activities undertaken as their business by NBFCs. As far as the taxable value in case of financial leasing including equipment leasing and hire purchase is concerned, the amount received as principal is not the consideration for services rendered. Such amount is credited to the capital account of the lessor/hire-purchase service provider. It is the interest/finance charge which is treated as income or revenue and which is credited to the revenue account. Such interest or finance charges together with the lease management fee/processing fee/documentation charges are treated as considerations for the services rendered and accordingly they constitute the value of taxable services on which service tax is made payable.
>
> **60.** In fact, the Government has given exemption from payment of service tax to financial leasing services including equipment leasing and hire purchase on that portion of taxable value comprising of 90% of the amount representing as interest i.e. the difference between the instalment paid towards repayment of the lease amount and the principal amount in such instalments paid (see Notification No. 4/2006 — Service Tax dated 1-3-2006). In other words, service tax is leviable only on 10% of the interest portion. (See also Circular F. No. B.11/1/2001-TRU dated 9-7-2001 in which it has been clarified that service tax, in the case of financial leasing including equipment leasing and hire purchase, will be leviable only on the lease management fees/processing fees/documentation charges recovered at the time of entering into the agreement and on the finance/interest

> charges recovered in equated monthly instalments and not on the principal amount.) Merely because for valuation purposes inter alia "finance/interest charges" are taken into account and merely because service tax is imposed on financial services with reference to "hiring/interest" charges, the impugned tax does not cease to be service tax and nor does it become tax on hire-purchase/leasing transactions under Article 366(29-A) read with Entry 54, List II. Thus, while the State Legislature is competent to impose tax on "sale" by legislation relatable to Entry 54 of List II of the Seventh Schedule, tax on the aspect of the "services", vendor not being relatable to any entry in the State List, would be within the legislative competence of Parliament under Article 248 read with Entry 97 of List I of the Seventh Schedule to the Constitution.**"**

(ac) It may be noticed that the Hon'ble Supreme Court split the transaction into two components i.e. "sale" and "service". It is pertinent to note that the service tax was imposed only on the component of the service @ 10 % of the contract value. While considering the nature of transaction it has been found by the Hon'ble Supreme Court that the part of the transaction like interest/ financing charges with lease management fee, processing fee and documentation charges are consideration for rendering service by the non-banking financial companies and thus fall within the definition of "taxable service" defined in Section 65 (105)(zm).

(ad) Another judgment heavily relied upon by Mr. Razzak is (***2004) 5 SCC 632 : T.N. Kalyanamandapam Association vs. Union of India & Others***. In this case vires of Sections 65(19), (20), (41)(p), and 66, 67(o) of the

Finance Act, 1994 as amended from time to time were assailed being ultra vires. Under the above provisions service tax was levied on the services rendered by the mandap-keepers in respect to the temporary leasing of land for organizing official, social or business functions and even for catering services which *inter alia* includes furniture, fixtures, light fittings, floor covering etc. on 60% of the gross amount charged by the mandap-keepers. The vires of the provision was challenged on the ground that it is a tax on land and building under entries 18 and 49 of List II of the Seventh Schedule. It also amounts to tax on sale under entry 54 of List II particularly in view of definition of 'sale' and 'purchase' under Article 366 (29A)(f).

(ae) The High Court rejected the contention and in appeal the Hon'ble Supreme Court affirmed the judgment holding that the activity of mandap-keepers does not fall in any of the entries i.e. 18 and 49 of the State List. As regards the entry 54 is concerned it has been held that the tax have been levied on 60% of the gross receipts. It is further held that predominantly the activity of the mandap-keepers is rendering various kinds of services. Applying the aspect doctrine, the Hon'ble Supreme Court held as under: -

> "**58.** A tax on services rendered by mandap-keepers and outdoor caterers is in pith and substance, a tax on services and not a tax on sale of goods or on hire-purchase activities. Section 65 clause (41) sub-clause (*p*)

> of the Finance Act, 1994, defines taxable service (which is the subject-matter of levy of service tax) as any service provided to a customer
>
> > "by a mandap-keeper in relation to the use of a mandap in any manner including the facilities provided to [a customer] in relation to such use and also the services, if any, rendered as a caterer".
>
> The nature and character of this service tax is evident from the fact that the transaction between a mandap-keeper and his customer is definitely not in the nature of a sale or hire-purchase of goods. It is essentially that of providing a service. In fact, as pointed out earlier, the manner of service provided assumes predominance over the providing of food in such situations which is a definite indicator of the supremacy of the service aspect. The legislature in its wisdom noticed the said supremacy and identified the same as a potential region to collect indirect taxes. Moreover, it has been a well-established judicial principle that so long as the legislation is in substance, on a matter assigned to a legislature enacting that statute, it must be held valid in its entirety even though it may trench upon matters beyond its competence. Incidental encroachment does not invalidate such a statute on the grounds that it is beyond the competence of the legislature (*Prafulla Kumar* v. *Bank of Commerce* [AIR 1947 PC 60 : 74 IA 23]). Article 246(1) of the Constitution specifies that Parliament has exclusive powers to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule to the Constitution. As per Article 246(3), the State Government has exclusive powers to make laws with respect to matters enumerated in List II (State List). In respect of matters enumerated in List III (Concurrent List) both Parliament and State Governments have powers to make laws. The service tax is made by Parliament under the above residuary powers.

(af) Another judgment on which emphasis has been laid on behalf of respondents is ***(2007) 7 SCC 527 : All India Federation of Tax Practitioners & Others vs. Union of India & Others***. In this case levy of service tax on practicing Chartered Accountants, Cost Accountants and Architects vide the Finance Act, 1994 was assailed. The challenge was based upon the legislative competence of State Legislature to levy tax on professions, etc. under entry 60 of List II and Article 276 of the Constitution of India. It

was contended on behalf of the petitioners that the service tax on professionals is a tax of profession and thus beyond the legislative competence of the Parliament. Repelling the argument and drawing distinction between the tax on profession and services rendered by the professionals, the Hon'ble Supreme Court observed as under:

> **"34.** As stated above, Entry 60, List II refers to taxes on professions, etc. It is the tax on the individual person/firm or company. It is the tax on the status. A chartered accountant or a cost accountant obtains a licence or a privilege from the competent body to practise. On that privilege as such the State is competent to levy a tax under Entry 60. However, as stated above, Entry 60 is not a general entry. It cannot be read to include every activity undertaken by a chartered accountant/cost accountant/architect for consideration. Service tax is a tax on each activity undertaken by a chartered accountant/cost accountant or an architect. The cost accountant/chartered accountant/architect charges his client for advice or for auditing of accounts. Similarly, a cost accountant charges his client for advice as well as doing the work of costing. For each transaction or contract, the chartered accountant/cost accountant renders profession based services. The activity undertaken by the chartered accountant or the cost accountant or an architect has two aspects. From the point of view of the chartered accountant/cost accountant it is an activity undertaken by him based on his performance and skill. But from the point of view of his client, the chartered accountant/cost accountant is his service provider. It is a tax on "services". The activity undertaken by the chartered accountant or cost accountant is similar to saleable or marketable commodities produced by the assessee and cleared by the assessee for home consumption under the Central Excise Act.
>
> **35.** For each contract, tax is levied under the Finance Acts, 1994 and 1998. Tax cannot be levied under that Act without service being provided whereas a professional tax under Entry 60 is a tax on his status. It is the tax on the status of a cost accountant or a chartered accountant. As long as a person/firm remains in the profession, he/it has to pay professional tax. That tax has nothing to do with the commercial activities which he undertakes for his client. Even if the chartered accountant has no work throughout the accounting year, still he has to pay professional tax. He has to pay the tax till he remains in the profession. This is the ambit and scope of Entry 60, List II which is a taxing entry. Therefore, Entry 60 contemplates tax on professions, as such. Entry 60, List II refers to "tax on employments".**"**

(ag) From the ratio of above judgments, the emergence of proposition of law is that where the transaction or contract comprises of twin elements of sale and service, both, the State Legislature under entry 54 of List II and simultaneously the Parliament in exercise of residuary power under entry 97 of List I are competent to levy “sales tax” and “service tax” respectively provided the components of sale and service are visible and are capable of compartmentalization.

(v) <u>whether such circumstances exist in the case in hand?</u>

(ah) The facts of the present case are clearly distinguishable as noticed in the earlier part of the discussion. We have opined that the State Government is not paying any consideration to the petitioners nor the petitioners are rendering any service to the State. To the contrary the petitioners are paying minimum guaranteed amount for the purchase of entire lot of lotteries at the discounted price of 70 paise against the MRP of Re.1/- to the State. The nature of discount has already been discussed in detail.

(ai) It has been held by the Hon'ble Supreme Court in ***All India Federation of Tax Practitioners*** (Supra) that the service is an activity and service tax is in the nature of VAT i.e. Value Added Tax. The Hon'ble Supreme Court in ***State of Bombay vs R.M.D. Chamarbaugwala*** (supra) has also defined the betting and gambling as an activity.

(aj) In ***T.N. Kalyanamandapam Association***'s case (supra) the clear view of the Hon'ble Supreme Court is that the predominant activity of the service provider was rendering of service and levy of service tax on 60% of the gross value was upheld and similarly in ***Assn. of Leasing & Financial Service Companies*** case levy of service tax on 10% of the gross contract value was upheld being a tax on component of service.

(ak) In the present case, undisputedly the lottery ticket is sold as a good by the State Government to the petitioners at the discounted value of 70 paise per ticket as against its gross value/ MRP of Re.1/-. The predominant part of the transaction is sale of goods. While considering the discount of 30% to the petitioners on the MRP, we have held that the discount is a normal trade practice in any transaction of sale and purchase. If the seller sells the goods at the MRP to its ultimate consumer, no intermediary will sell the goods

unless he gets a discount to meet the expenditure for establishment, logistics and some component of profit. The State Government is unable to sell the tickets to the ultimate buyers and for that purpose the petitioners are appointed as stockists or distributors on payment of full sale consideration on discounted price. Further the sale by the petitioners to their stockists, selling agents etc is on discounted price from MRP after keeping the establishment and other expenditure and margin of profit for themselves. The last sale to the consumer of the lottery is on the MRP of Re.1/- per ticket. Thus, all the intermediaries have to be given discount from MRP for the purpose of meeting their expenditure and some component of profit. The advertisement etc. is only to popularize the State lottery but that does not mean that it is a service rendered to the State Government. As argued by Mr. Madhav Rao, this is for promotion of their own sale at their own expense without recovering it from the State Government. In any case service tax is being levied and collected on the gross amount without even isolating the discounted cost of lottery ticket. Thus in the present case there does not seem to be any circumstance where the activity of sale of State organized lottery by the petitioners through its various stockists, agents etc. can be construed to be the service rendered to

the State Government so as to enable the Central Government to impose service tax on any component or element of the transaction between the State and the petitioners

Conclusions: -

(i) In the backdrop of discussion on Ground (A) we have no hesitation to conclude that the activities of the lottery distributors i.e. the petitioners herein do not constitute a service and thus beyond the purview of “taxable service” as statutorily defined under clause (zzzzn) of sub-section 105 of Section 65 of the Finance Act, 1994 as amended vide Finance Act, 2010.

(ii) The activity of promotion, marketing, organizing or in any other manner assisting in organising game of chance including lottery is an activity included in the expression “betting and gambling” as incorporated under Entry 34 and 62 of List II to Seventh Schedule of Constitution of India.

(iii) The activity of promotion, marketing, organizing or in any other manner assisting in organising game of chance including lottery being an activity

of “betting and gambling” under Entry 62, List II to Seventh Schedule of Constitution of India, the State Legislature alone is competent to levy any tax on such activity under Entry 62.

(iv) The Parliament has the competence and jurisdiction to levy taxes on any subject matter including “service tax” under Entry 97, List I, read with Article 248 of the Constitution of India except where such powers are traceable to any of the entries in List II and III to Seventh Schedule of Constitution of India.

(v) Power to tax the activity of “betting and gambling” as explained above being within the exclusive domain of State Legislature under Entry 62, List II, the Parliament in exercise of its residuary power under Entry 97, List I to Seventh Schedule of Constitution of India lacks legislative competence to impose any tax including “service tax” on such activity.

19. In view of the above conclusions, we allow these petitions, strike down the clause (zzzzn) to sub-section 105 of Section 65 of Finance Act, 1994 as introduced vide

Finance Act, 2010 as ultra vires to Constitution of India having been enacted in contravention to Entry 97, List I to Seventh Schedule read with Article 248 of Constitution of India.

20. We also set aside all the consequential actions of respondents imposing service tax upon the petitioners being distributors of lottery organized by State of Sikkim.

21. Since the petitioners secured registration and paid service tax under the impugned provision on their own, this judgment shall operate prospectively.

22. In the facts and circumstances no order as to costs.

(Permod Kohli)
Chief Justice
29.11.2012

(S.P. Wangdi)
Judge
29.11.2012

Approved for reporting : Yes / No
Internet : Yes / No

pm/jk