TIRUMALA VENKATESWARA TIMBER AND BAMBOO FIRM

v.

COMMERCIAL TAX OFFICER, RAJAHMUNDRY

November 28, 1967

[J. C. SHAH, V. RAMASWAMI AND V. BHARGAVA, JJ.]

Andhra Pradesh General Sales Tax Act 6 *of* 1957, *Explanation III to s.* 2(1) (*n*)—*Whether* ultra vires—*Whether enlarges scope of 'sale' to include transactions which are not sales—Whether discriminatory.*

The appellant firm carried on business in Andhra Pradesh and was registered as a dealer under the Andhra Pradesh General Sales Tax Act 1957. In its return for the assessment year 1962-63 the firm claimed exemption of certain turnover on the ground that it had sent the goods to its commission agents and under the contract of agency the commission agents were empowered to pay sales-tax and had paid the same directly to the Sales Tax Department. When the Commercial Tax Officer sought to assess the appellant firm on the aforesaid turnover the appellant filed a writ petition in the High Court which was dismissed. In appeal before this Court by certificate it was contended : (i) that Explanation III to s. 2(1)(n) of the Act enlarged the scope of the word 'sale' by treating mere entrustment to an agent as a sale and therefore the Explanation was *ultra vires;* (ii) that the commission agents to whom the appellant had sent the goods for sale had already paid the tax and the appellant could not be taxed again on the same transaction as there was only one sale; (iii) that the Explanation was violative of Art. 14 of the Constitution as it made an arbitrary classification.

HELD : (i) The real effect of the third Explanation is to impose the tax only when there was a transfer of title to the goods and not where there is a mere contract of agency. The Explanation says in effect that when there is in reality a transfer of property by the principal to the agent and by the agent in his turn to the buyer there are two transactions of sale. The phrase "when the goods are transferred" in cls. (1) and (2) of Explanation III on a proper construction means "when title to the goods is transferred" and so construed it is impossible to say that the Explanation enlarges the scope of the main section. Explanation III is not, therefore *ultra vires.* [480 B—E]

State of Madras v. *Gannon Dunkerley & Co. (Madras) Ltd.* 9 S.T.C. 353, referred to.

(ii) As a matter of law there is a distinction between a contract of sale and a contract of agency by which the agent is authorised to sell or buy on behalf of the principal and make over either the sale proceeds or the goods to the principal. The essence of a contract of sale is the transfer of title to the goods for a price paid or promised to be paid. The transferee in such a case is liable to the transferor as a debtor for the price to be paid and not as agent for the proceeds of the sale. The essence of agency to sell is the delivery of the goods to a person who is to sell them, not as his own property but as the property of the principal who continues to be the owner of the goods, and will therefore be liable to account for the sale proceeds. The true relationship of the parties in

A each case has to be gathered from the nature of the contract, its terms and conditions, and the terminology used by the parties is not decisive of the legal relationship. [480 G—481 B]

Whether the transactions in the present case were sales or contracts of agency was a mixed question of law and fact and must be investigated with reference to the material which the appellant might be able to place before the appropriate authority. The question was not one which could B be properly determined in an application under Art. 226 of the Constitution. [482 B]

W.T. Lamb and Sons v. *Goring Brick Company, Limited* [1932] K.B. 710, and *Hutton v. Lippert* [1883] 8 A.C. 309, referred to.

(iii) The classification contemplated by the Explanation between sales through commission agents who account fully for all collections made and C sales through commission agents who do not account for collections is based upon an intelligible differentia and it has a rational relationship with the object sought to be achieved by the statute. It did not therefore, violate Art. 14. [482 C—D]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2176 of 1966.

D Appeal from the judgment and order dated April 16, 1964 of the Andhra Pradesh High Court in Writ Petition No. 1404 of 1963.

P. Parameswara Rao for *R. V. Pillai*, for the appellant.

P. Ram Reddy and *A. V. V. Nair*, for the respondent.

E The Judgment of the Court was delivered by

Ramaswami, J. The appellant is a partnership firm carrying business in bamboos, timber and firewood at Gokavaram in the State of Andhra Pradesh. The firm had been registered as a dealer under the Andhra Pradesh General Sales Tax Act (No. VI of 1957), hereinafter referred to as the 'Act'. For the assess- F ment year 1962-63, the appellant submitted a return showing a gross turnover of Rs. 13,89,130.70 P and claimed exemption on a turnover of Rs. 13,68,174.39 P which according to the appellant represented the amount of sales effected by its commission agents and sales of firewood. By a notice dated November 28, 1963, the Commercial Tax Officer, Rajahmundry called upon the G appellant to show cause as to why it should not be assessed for the year 1962-63 on a turnover of Rs. 13,89,130.70 P at 2 per cent. Eleven items were comprised in the notice. Item No 1, relating to a turnover of Rs. 96,527.10 P was under the firewood account. It was alleged by the appellant that it paid the single point tax at 2 per cent to the Forest Department on the amounts H for which the forest goods were taken in auction. As regards items 2 to 11 the appellant claimed exemption on the ground that its agents, Messrs. Kusuma Arjayya and Batlanki Veera Venkayya, Rajahmundry, paid the tax. The case of the appellant was that

it sent goods for sale to its commission agents and under the contract of agency the commission agents were empowered to pay sales-tax and had paid the same directly to the Sales Tax Department. In accordance with the usual commercial practice the commission agents collected Dharmam on the sales conducted by them and appropriated those collections for charitable purposes. The commission agents furnished accounts to the appellant but in these accounts the amounts collected towards sales-tax and Dharmam were not specifically shown as it was understood between the parties that the amounts collected towards sales tax would be remitted to the Sales Tax Department and the amounts collected towards Dharmam would be credited to the charity account of the commission agents and suitably utilised by them. Aggrieved by the assessment notice of the respondent disallowing its claim for exemption the appellant-firm filed a writ petition No. 1404 of 1963 dated December 7, 1963 before the High Court of Andhra Pradesh under Art. 226 of the Constitution praying for the grant of a writ in the nature of *certiorari* calling for the records relating to sales-tax assessments of the appellant for the year 1962-63 and quashing the notice dated November 28, 1963 issued by the respondent. By its judgment dated April 16, 1964 the High Court dismissed the writ petition. This appeal is brought by a certificate granted by the High Court.

On behalf of the appellant it was contended, in the first place, that Explanation III to s. 2(1)(n) of the Act enlarged the scope of the word "sale" and by means of a fiction converted what are not sales in law into taxable sales for the purpose of the Act and, therefore, the Explanation was *ultra vires* of the powers of the State Legislature which had no legislative competence to impose a tax under Entry 48 in List II of Sch. VII of the Constitution. Section 2(1)(n) of the Act defines "sale" as follows :

> "'sale' with all its grammatical variations and cognate expressions means every transfer of the property in goods by one person to another in the course of trade or business, for cash, or for deferred payment, or for any other valuable consideration, (and includes any transfer of materials for money consideration in the execution of a works contract provided that the contract for the transfer of such materials can be separated from the contract for the services and the work done, although the two contracts are embodied in a single document) or in the supply or distribution of goods by a society (including a co-operative society), club, firm or associations to its members, but does not include a mortgage hypothecation or pledge of, or a charge on goods;
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> NOTE :—By Amendment Act 26, 1961, the bracketed words were substituted for the words 'and includes

A a transfer of property in goods involved in the execution of a works contract.

. . . . . .

Explanation III :—Notwithstanding anything contained in this Act or in the Indian Sale of Goods Act, 1930 (Central Act III of 1930), two independent sales or purchases shall, for the purposes of this Act, be deemed to have taken place—

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

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

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

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

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

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

In our opinion the real object of the Explanation is to prevent the misuse by the assessee of the relationship of principal and agent for the purpose of evading tax. The first situation contemplated by the legislature is that covered by cl. 2(i) of Explanation III where the agent has sold the goods at one rate and passed on the sale proceeds to its principal at another rate. The second situation is where the agent has purchased the goods at one rate and has passed them on to the principal at another rate. The third situation is where the agent has not accounted to his principal for the entire collections or deductions made by him in the sales or purchases effected by him on behalf of his principal, and the fourth is where it appears that the agent has acted for a fictitious or non-existent principal. It was contended on behalf of the appellant that the State legislature was not competent to convert by a legal fiction a mere entrustment of goods for sale into a sale and to impose a tax thereon. In our opinion, there is no warrant for this argument. The real effect of the third Explana-

tion is to impose the tax only when there was a transfer of title to the goods and not where there is a mere contract of agency. The Explanation says in effect that where there is in reality a transfer of property by the principal to the agent and by the agent in his turn to the buyer, there are two transactions of sale. In our opinion, the phrase "when the goods are transferred" in cls. (1) and (2) of Explanation III on a proper construction means "when title to the goods is transferred" and so construed it is impossible to say that the Explanation enlarges the scope of the main section. It was pointed out by this Court in *The State of Madras* v. *Gannon Dunkerley & Co. (Madras) Ltd.*(1) that the expression "sale of goods" in Entry 48 in List II of Sch. VII of the Government of India Act, 1935, cannot be construed in its popular sense but must be interpreted in its legal sense and should be given the same meaning which it has in the Sale of Goods Act, 1930. It is a *nomen juris*, its essential ingredients being an agreement to sell movables for a price and property passing therein pursuant to that agreement. In other words, it is necessary for constituting a sale that there should be an agreement between the parties for the purpose of transferring title in the goods, that the agreement must be supported by money consideration and that as a result of the transaction the title to the property must actually pass in the goods. As we have already pointed out, the third Explanation to s. 2(1)(n) of the Act must be interpreted to mean that where there is in reality a transfer of property in the goods by the principal to the agent and by the agent in his turn to the buyer, there are two transactions of sale. It is therefore impossible to accept the contention put forward on behalf of the appellant that the Explanation has converted what, in fact, is not a sale into a sale for the purpose of assessment to sales-tax.

It was contended on behalf of the appellant that in any event items Nos. 2 to 11 of the notice related to goods which the appellant had sent for sale to the commission agents and as the latter had already paid the sales-tax the appellant was not liable to be assessed to tax again on the same transaction as there was only one sale. As a matter of law there is a distinction between a contract of sale and a contract of agency by which the agent is authorised to sell or buy on behalf of the principal and make over either the sale proceeds or the goods to the principal. The essence of a contract of sale is the transfer of title to the goods for a price paid or promised to be paid. The transferee in such a case is liable to the transferor as a debtor for the price to be paid and not as agent for the proceeds of the sale. The essence of agency to sell is the delivery of the goods to a person who is to sell them, not as his own property but as the property of the

(1) 9 S.T.C. 353.

A principal who continues to be the owner of the goods and will therefore be liable to account for the sale proceeds. The true relationship of the parties in each case has to be gathered from the nature of the contract, its terms and conditions, and the terminology used by the parties is not decisive of the legal relationship. For instance, in *W. T. Lamb and Sons* v. *Goring Brick* B *Company Limited*(1) there was an agreement in writing by which certain manufacturers of bricks and other building materials appointed a firm of builders' merchants "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 months' notice by either party. While the agreement was in force the manufacturers informed the mer- C chants 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. It was held by the Court of Appeal that the agreement was one of vendor and purchaser and not one of principal and agent. The same principle is enunciated in *Hutton* v. *Lippert*(2), in which there was a contract between D the defendant and E, which in its terms purported to be one of guarantee or agency; that is to say, the defendant guaranteed the sale of E's property in whole or by lots at a fixed price, E giving the defendant a power of attorney to deal with the property as he thought fit, and agreeing that he should receive any surplus over and above the fixed price as his commission on and recom- E pense for the said guarantee. It was held by the Judicial Committee, upon a construction of the agreement, that the transaction was really a sale and that the defendant was liable to pay duty on his purchase-money under Act II of 1863. At page 313 of the Report, Sir Robert P. Collier, who delivered the opinion of the Board, stated as follows :

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> "Under these circumstances it appears to their Lordships that the Chief Justice was justified in saying that the effect of the transaction was to give Ekstein every right which a vendor could legally claim, and to confer upon the defendant every right which a purchaser could legally demand. Does it make any difference that the G parties have called this transaction by the name of a guarantee ? It appears to their Lordships that because the parties have used this term 'guarantee' in a sense which is unusual and not applicable to this case,—for Lippert really guaranteed nothing,—the nature of the transaction is not thereby changed; and because they have said that Lippert was to be entitled to whatever H surplus or balance shall remain on the resale of portions of the property, if any were resold, 'as commission and

(1) [1932] K.B. 710.

(2) [1883] 8 A.C. 309.

recompense for the said guarantee,' this expression does not convert him from a purchaser into an agent." A

It is manifest that the question as to whether the transactions in the present case are sales or contracts of agency is a mixed question of fact and law and must be investigated with reference to the material which the appellant might be able to place before the appropriate authority. The question is not one which can properly be determined in an application for a writ under Art. 226 of the Constitution. B

It was also submitted on behalf of the appellant that the third Explanation to s. 2(1)(n) of the Act violated the guarantee under Art. 14 of the Constitution since the classification contemplated, *i.e.*, sales through commission agents who account fully for all collection made and sales through commission agents who do not account for collections, was not made on any intelligible differentia and had no rational relationship to the purpose of the statute. In our opinion, there is no substance in this argument as the classification is based upon an intelligible differentia and it has a rational relationship with the object sought to be achieved by the statute. Counsel for the appellant is therefore unable to make good his submission on this aspect of the case. C D

For the reasons expressed we hold that the judgment of the High Court of Andhra Pradesh is right and this appeal must be dismissed. In the circumstances of the case we do not propose to make any order as to costs. E

G.C. *Appeal dismissed.*