STATE OF KERALA

v.

A. B. ABDUL KHADIR & ORS.

July 30, 1969

[J. C. SHAH, ACTING C.J., V. RAMASWAMI AND A. N. GROVER, JJ.]

Constitution of India, Arts, 301 *and* 304—*Prohibition under Art.* 301 —*When a tax is saved.*

To avoid the decision of this Court in *A. B. Abdul Khadir* v. *The State of Kerala*, [1962] 2 S.C.R. 741, wherein rules framed for the issue of licences and payment of fee for storage of tobacco were held to be invalid, the appellant-State promulgated Ordinance I of 1963 which was later replaced by Luxury Tax on Tobacco (Validation) Act 9 of 1964. Consequently the appellant-State made a demand on the respondent to repay the amount which had been refunded to the respondent in accordance with the aforesaid judgment. Thereupon, the respondent filed a writ petition in the High Court. The High Court relying upon the decision of this Court in *Kalyani Stores* v. *State of Orissa*, [1966] 1 S.C.R. 865, held that in the absence of any production of tobacco inside the appellant-State it was not competent for the State Legislature to impose a tax on tobacco imported from outside the State and therefore, the provisions of the Act (9 of 1964) violated the guarantee contained in Arts. 301 and 304 of the Constitution.

HELD : The High Court had not correctly appreciated the import of the decision in *Kalyani Stores'* case. The decision was based on the assumption that the notifications therein enhancing duty on foreign liquor infringed the guarantee under Art. 301 and may be saved if it fell within the exceptions contained in Art. 304 of the Constitution. As no liquor was produced or manufactured within the State the protection of Art. 304 was not available. This Court did not intend to lay down the proposition that the imposition of a duty or tax in every case would be tantamount *per se* to an infringement of Art. 301.

Only such restrictions or impediments which directly and immediately impede the free flow of trade, commerce and intercourse fall within the prohibition imposed by Art. 301. A tax may in certain cases directly and immediately restrict or hamper the flow of trade, but every imposition of tax does not do so. Every case must be judged on its own facts and in its own setting of time and circumstance.

In the present case the High Court had not gone into the question whether the provisions of the Act and the notifications constituted such restrictions or impediments as directly and immediately hamper the free

A flow of trade, commerce and intercourse, and, therefore, fell within the prohibition imposed under Art. 301 of the Constitution. Unless the High Court first comes to the finding whether or not there is the infringement of the guarantee under Art. 301 of the Constitution the further question as to whether the statute is saved under Art. 304(b) does not arise and the principle laid down in *Kalyani Stores'* case cannot be invoked. This B case, therefore must go back to the High Court. [709 E—710 E]

Atiabari Tea Co. Ltd. v. *The State of Assam*, [1961] 1 S.C.R. 809, *Automobile Transport (Rajasthan) Ltd.* v. *The State of Rajasthan*, [1963] 1 S.C.R. 491, *Andhra Sugars Ltd.* v. *State of Andhra Pradesh*, [1968] 1 S.C.R. 705 and *State of Madras* v. *K. Nataraja Mudaliar*, [1968] 3 S.C.R. C 829, referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 517 of 1967.

Appeal from the judgment and order dated October 3, 1966 of the Kerala High Court in Original Petition No. 934 of 1964.

D

M. R. K. Pillai, for the appellant.

R. Gopalakrishnan, for the respondents.

The Judgment of the Court was delivered by

E **Ramaswami, J.** This appeal is brought by certificate from the judgment of the Kerala High Court in O.P. No. 934 of 1964.

The respondents are dealers in tobacco and tobacco preparations and are doing business in Mattancherry in the name and style of A. S. Bava, Tobacconist. In the year 1909, Cochin Tobacco Act 7 of 1084 (M.E.) was enacted by the Maharaja of Cochin. F Section 4 of that Act prohibited the transport, import of export, sale and cultivation of tobacco except as permitted by the Act and Rules framed thereunder. Section 6 of the Act gave power to the Dewan to make rules from time to time consistent with the Act, to permit absolutely or subject to any condition the possession for sale, or cultivation of tobacco. In pursuance of the power given G by this section the Dewan was making rules from time to time relating to the matters specified in the Act. Cochin State was integrated with Travancore on April 1, 1960 in order to form the new State of Travancore-Cochin. On that date, after the Constitution came into force the State of Travancore-Cochin became a Part B State and by the Finance Act, 1960 the Central Excise and Salt Act 1 of 1944 was extended to the Travancore- H Cochin State. Section 13(2) of the Act provided that if immediately before the first day of April, 1960 there was in force in any State other than Jammu & Kashmir a law corresponding to, but

other than, an Act referred to in sub-s. (1) or (2) of s. 11, such law was repealed with effect from such date. In consequence of this provision in the Finance Act rules which were in force on April 1, 1950 were changed in Cochin and by a notification dated August 3, 1950 the system of auction sales of A and B Class shops was done away with and instead graded licence fees were introduced for various classes of licences including 'C' class licences. The State of Travancore-Cochin was collecting licence fee from the respondents for the period from August 17, 1950 to December 31, 1967 on the strength of the said rules framed by the Travancore-Cochin State. In 1956 the respondents filed O. P. No. 70 of 1956 in the High Court of Kerala for the refund of the licence fee collected after April 1, 1950 on the ground that the Cochin Tobacco Act stood repealed by the Finance Act, 1960 because of the extension of the Central Excise and Salt Act 1 of 1944 to the Part B State of Travancore-Cochin and in consequence the notifications issued in August 1950 and January 1961 framing new rules for the issue of licences and prescribing fees therefor under the powers conferred by the Cochin and Travancore Acts were *ab initio* void because the Acts under which the notifications were purported to be issued stood repealed from April 1, 1950. The petition was opposed by the appellant on the ground that the Act and the rules were not repealed by the extension of the Central Excise and Salt Act 1 of 1944 to Travancore-Cochin State. The High Court dismissed the writ petition holding that the tax levied by virtue of the rules framed under the Travancore-Cochin Tobacco Acts was not a duty of excise coming within the Union List but it was a tax on luxuries coming within entry 62 of the State List. The respondents took the matter in appeal to this Court which held that the rules framed under the Cochin Tobacco Act of 1084 (M.E.) and the Travancore Tobacco Regulation of 1087 (M.E.) requiring licences to be taken out for storage and sale of tobacco and for payment of licence fee in respect thereof were law corresponding to the provisions of the Central Excise and Salt Act, 1944 and hence were superseded on April 1, 1960 by virtue of s. 13(2) of the Finance Act, 1960. Consequently, the new rules framed in August 1950 and January 1951 for the respective areas of Cochin and Travancore for the issue of licences and payment of fee for storage of tobacco were invalid *ab initio*. The Court did not consider it necessary to decide whether the Cochin and Travancore Acts were within the competence of the State Legislature under Entry 62 of List II for that question would only arise if those Acts were not repealed as corresponding law under s. 13(2) of the Finance Act.

Soon after the decision of this Court the respondent complained to the appellant that a sum of Rs. 1,11,750 had been illegally collected as licence fee from 1125 to 1133 M.N. On

April 29, 1962 the appellant refunded a sum of Rs. 73,500 but did not return the balance.

On December 16, 1963 the Government of Kerala Promulgated Ordinance I of 1963 which was later replaced by Act 9 of 1964. The Ordinance was promulgated in order to avoid the effect of the decision of this Court in *A. B. Abdulkhadir & Ors* v. *The State of Kerala*(1) in respect of the period from August 17, 1950 to December 31, 1957. Section 3 of the Act provides :

> "For the period beginning with the 17th day of August, 1950 and ending on the 31st day of December, 1957 every person vending or stocking tobacco within any area to which this Act extends shall be liable and shall be deemed always to have been liable to pay a luxury tax on such tobacco in the form of a fee for licence for the vend and stocking of the tobacco, at such rates as may be prescribed not exceeding the rates specified in the schedule."

Section 4 confers rule making power and states :

> "(1) The Government may, by notification in the Gazette, make rules to carry out the purposes of this Act.
>
> (2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for :—
>
> (i) the prohibition of the vending of tobacco except under a licence;
>
> (ii) the issue of licences for the vend and stocking of tobacco and the procedure therefor;
>
> (iii) classification of licences and the rate at which tax in the form of a fee for licence may be levied for each class of licences;
>
> (iv) appeals from orders under the rules.
>
> (3) The rules and notifications specified below purported to have been issued under the Tobacco Act of 1087 (Travancore Act I of 1087) or the Cochin Tobacco Act VII of 1084 as the case may be, in so far as they relate or purport to relate to the levy and collection of fees for licences for the vend and stocking of tobacco, shall be deemed to be rules issued under this

(1) [1962] Supp. S.C.R. 741.

section and shall be deemed to have been in force at all material times : A

. . . . . ."

Section 5 provides : B

"Notwithstanding any judgment, decree or order of any court, all fees for licences for the vend or stocking of tobacco levied or collected or purported to have been levied or collected under any of the rules or notifications specified in sub-section (3) of section 4 for the period beginning with the 17th day of August, 1950 and ending on the 31st day of December, 1957 shall be deemed to have been validly levied or collected in accordance with law as if this Act were in force on and from the 17th day of August, 1960 and the fees for licences were a luxury tax on tobacco levied under the provisions of this Act and accordingly (a) no suit or other proceeding shall be maintained or continued in any court for the refund of any fees, paid or purported to have been paid under any of the said rules or notifications; C D

(b) no court shall enforce a decree or order directing the refund of any fees paid or purported to have been paid under any of the said rules or notification." E

Section 6 enacts :

"Where any amount paid or purported to have been paid as a fee for licence under any of the rules or notifications specified in sub-section (3) of section 4 has been refunded after the 24th day of January, 1962 and such amount would not have been liable to be refunded if this Act had been in force on the date of the refund, the person to whom the refund was made shall pay the amount so refunded to the credit of the Government in any Government treasury on or before the 16th day of April, 1964 where such amount is not so paid, the amount may be recovered from him as an arrear of land revenue under the Revenue Recovery Act for the time being in force." F G

The notification dated January 25, 1951 issued under the Cochin Tobacco Act of 1084 reads as follows : H

"In exercise of the powers conferred by section 5 of the Cochin Tobacco Act VII of 1084 as subsequently

amended and as continued in force by the Travancore-Cochin Administration and Application of Laws Act VI of 1125 and in supersession of all previous notifications and Rules on the subject, the following Rules are prescribed under sanction of His Highness the Raj Pramukh for the import, export, sale, transport, possession, disposal of things confiscated and the grant of rewards under the said Act and for generally carrying out the provisions thereof.

. . . . . .

Clause 16 :

(i) Holders (stockist or 'A' Class licences shall be entitled to purchase tobacco from any dealer within or without the State without any quantative restriction. This class of licencees shall sell only to other 'A' Class licencees or to 'B' class licencees.

(ii) the annual fees for these licencees shall be as follows :

Variety of tobacco stocked	Maximum quantity Cds	Minimum fee prescribed Rs.	Fee payable for stocking additional quantities Rs.
A. Jaffna tobacco	100	1500	100 for additional quantity of 100 Cds or fraction thereof.
B. Tobacco produced in India (Mfd)	100	1000	Rs. 750 Do.
C. Beedi or Beedi tobacco	25	1000	Rs. 750 for additional quantity of 25 Cds or fraction thereof.
D. Tobacco preparation of all kinds	to the value of 20,000	1000	Rs. 750 for additional quantity to the value of Rs. 20,000 or fraction thereof.

N.B. : For the purpose of calculating stockist licence fee in respect of tobacco preparations, the cost price of the article will be taken into account. The licence fee will be realised only for the quantities brought in from outside the State."

After the enactment of Act 9 of 1964 the appellant made a demand on the respondent to repay the amount of Rs. 73,500 which had been refunded to the respondent in accordance with the Supreme Court judgment. Thereupon the respondent filed writ petition

No. C.P. 984 of 1964 which was allowed by the High Court on the ground that Act 9 of 1964 and the rules were *ultra vires* the Constitution of India.

It was held by the High Court that in the absence of any production of tobacco inside the Kerala State it was not competent for the Kerala Legislature to impose a tax on tobacco imported from outside the State and therefore the provisions of the Luxury Tax on Tobacco (Validation) Act, 1964 violated the guarantee contained in Arts. 301 and 304 of the Constitution. In reaching this conclusion the High Court purported to follow the decision of this Court in *Kalyani Stores* v. *The State of Orissa*(1).

It is necessary at this stage to set out the relevant Articles in Part XIII of the Constitution as it stood at the material time:

"Article 301:

Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.

Article 302:

"Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part of the territory of India as may be required in the public interest."

Article 304:

"Notwithstanding anything in Article 301 or Article 303, the Legislature of a State may by law:

(a) impose on goods imported from other States (or the Union territories) any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced and

(b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest;

Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the

(1) [1966] 1 S.C.R. 865.

A Legislature of a State without the previous sanction of the President."

The true scope and effect of those Articles was the subject matter of consideration in *Atiabari Tea Co. Ltd.* v. *The State of Assam*(1). The majority view was expressed by Gajendragadkar B J. at p. 860 as follows:

"In construing Art. 301 we must, therefore, have regard to the general scheme of our Constitution as well as the particular provisions in regard to taxing laws. The construction of Art. 301 should not be determined on a C purely academic or doctrinnaire considerations; in construing the said Articles we must adopt a realistic approach and bear in mind the essential features of the separation of powers on which our Constitution rests. It is a federal Constitution which we are interpreting, and so the impact of Art. 301 must be judged accordingly. Besides, it is not irrelevant to remember in this connec- D tion that the Article we are construing imposes a constitutional limitation on the power of the Parliament and State Legislatures to levy taxes, and generally, but for such limitation, the power of taxation would be presumed to be for public good and would not be subject to judicial review or scrutiny. Thus considered we think E it would be reasonable and proper to hold that restrictions freedom from which is guaranteed by Art. 301, would be such restrictions as directly and immediately restrict or impede the free flow or movement of trade. Taxes may and do amount to restrictions; but it is only such taxes as directly and immediately restrict trade that F would fall within the purview of Art. 301. The argument that all taxes should be governed by Art. 301 whether or not their impact on trade is immediate or mediate, direct or remote, adopts, in our opinion, an extreme approach which cannot be upheld. If the said argument is accepted it would mean, for instance, that even a G legislative enactment prescribing the minimum wages to industrial employees may fall under Part XIII because in an economic sense an additional wage bill may indirectly affect trade or commerce. We are, therefore, satisfied that in determining the limits of the width and amplitude of the freedom guaranteed by Art. 301 a rational and workable test to apply would be: Does the H impugned restriction operate directly or immediately on trade or its movement ?"

(1) [1961] 1 S.C.R. 809.

In the *Automobile Transport (Rajasthan) Ltd.* v. *The State of Rajasthan*(1) the view of Gajendragadkar, J., was accepted as correct by the majority of the Judges. The principle was reiterated by this Court in *Andhra Sugars Ltd.* v. *State of Andhra Pradesh*(2). In that case the question which arose was whether s. 21 of the Andhra Pradesh Sugarcane (Regulation of Supply and Purchase) Act which authorised the State Government to levy a tax at such rate not exceeding five rupees per metric tonne as may be prescribed on the purchase of cane required for use, consumption or sale in a factory was constitutionally valid. It was held by this Court that normally a tax on the sale of goods did not directly impede or hamper the flow of trade and s. 21 was no exception and was not violative of Art. 301 of the Constitution. A similar view was expressed in the *State of Madras* v. *K. Nataraja Mudaliar*(3) in which the question at issue was whether ss. 8(2) and 8(5) of the Central Sales Tax Act, 1956 were *intra vires* of Arts. 301 and 303 of the Constitution. It was pointed out that an Act which was merely enacted for the purpose of imposing tax which was to be collected and to be retained by the State did not amount to a law giving or authorising the giving of, any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, merely because of varying rates of tax prevailing in different States. At p. 150 of the report Shah, J., speaking for the Court observed :

> "The flow of trade does not necessarily depend upon the rates of sales tax : it depends upon a variety of factors, such as the source of supply, place of consumption, existence of trade channels, the rates of freight, trading facilities, availability of efficient transport and other facilities for carrying on trade. Instances can easily be imagined of cases in which notwithstanding the lower rate of tax in a particular part of the country goods may be purchased from another part, where a higher rate of tax prevails. Supposing in a particular State in respect of a commodity the rate of tax is 2 per cent, but if the benefit of that low rate is offset by the freight which a merchant in another State may have to pay for carrying that commodity over a long distance, the merchant would be willing to purchase the goods from a nearer State even though the rate of tax in that State may be higher. Existence of long-standing business relations, availability of communications, credit facilities and a host of other factors—natural and business—enter into the maintenance of trade relations and the free flow of

(1) [1963] 1 S.C.R. 491. (2) [1968] 1 S.C.R. 705.
(3) [1968] 3 S.C.R. 829.

A trade cannot necessarily be deemed to have been obstructed merely because in a particular State the rate of tax on sales is higher than the rates prevailing in other States.

On behalf of the appellant it was contended that the High B Court was not right in holding that the ratio of *Kalyani Stores case*(1) applied to the present case and, that, Kerala Act 9 of 1964 was violative of Art. 301 of the Constitution. The view taken by the High Court was that in the absence of any production of tobacco inside Kerala State it was not competent for the Kerala Legislature to enact the impugned Act under Art. 304(a) C of the Constitution. In support of this view the High Court relied upon the following passage from the judgment of this Court:

> "Exercise of the power under Art. 304(a) can only be effective if the tax or duty imposed on goods imported from other States and the tax or duty imposed on similar goods manufactured or produced in that State are such D that there is no discrimination against imported goods. As no foreign liquor is produced or manufactured in the State of Orissa the power to legislate given by Art. 304 is not available and the restriction which is declared on the ground of trade, commerce or intercourse by Art. 301 of the Constitution remains unfettered."

E

In our opinion the High Court has not correctly appreciated the import of the decision of this Court in the *Kalyani Stores case*(1). The appellant in that case challenged the imposition of a duty of excise on 'foreign liquor' imported into the Orissa State which had been levied at Rs. 40 per L.P. Gallon until March 31, F 1961 by virtue of a notification issued in 1937 under s. 27 of the Bihar and Orissa Excise Act, 1915 and which had been enhanced with effect from April 1, 1961 by a fresh notification. It was contended on behalf of the appellant that since no 'foreign liquor' was manufactured within the State and consequently no excise duty was being levied on any locally manufactured 'foreign liquor' countervailing duty could not be charged on such liquor G brought from outside the State and that the impost was in violation of Arts. 301, 303 and 304 of the Constitution. It was held by the majority of Judges that the notification dated March 31, 1961 enhancing the levy by Rs. 30 per L.P. Gallon infringed the guarantee of freedom under Art. 301 and may be saved only if it falls within the exception contained in Art. 304. As no liquor H was produced or manufactured within the State, the protection of Art. 304 was not available. The decision was based on the

(1) [1966] 1 S.C.R. 865.

assumption that the notification dated 31-3-1961 enhancing duty on foreign liquor infringed the guarantee under Art. 301 and may be saved if it fell within the exceptions contained in Art. 304 of the Constitution. The Court did not intend to lay down the proposition that the imposition of a duty or tax in every case would be tantamount *per se* to an infringement of Art. 301. As we have already pointed out it is well established by numerous authorities of this Court that only such restrictions or impediments which *directly and immediately* impede the free flow of trade, commerce and intercourse fall within the prohibition imposed by Art. 301. A tax may in certain cases directly and immediately restrict or hamper the flow of trade, but every imposition of tax does not do so. Every case must be judged on its own facts and in its own setting of time and circumstance. In the present case the High Court has not gone into the question whether the provisions of Act 9 of 1964 and the notification dated January 25, 1951 issued under the Cochin Tobacco Act constitute such restrictions or impediments as directly and immediately hamper free flow of trade, commerce and intercourse and, therefore, fall within the prohibition imposed under Art. 301 of the Constitution. Unless the High Court first comes to the finding on the available material whether or not there is infringement of the guarantee under Art. 301 of the Constitution the further question as to whether the statute is saved under Art. 304(b) does not arise and the principle laid down by this Court in *Kalyani Stores case*(1) cannot be invoked.

It was also said on behalf of the respondents that the State Legislature had no power to levy and collect licence fee under the impugned Act as it was in substance a duty of excise falling under the Union List. The contrary viewpoint was presented on behalf of the appellant and it was contended that the legislation falls under Entry 62 of List II and the State Legislature was competent to enact. It is open to the parties to argue this matter before the High Court at the time of re-hearing.

For the reasons already expressed we hold that the appeal should be allowed and the judgment of the Kerala High Court dated October 3, 1966 in O.P. 934 of 1964 should be set aside and the case should go back for hearing in the light of the law laid down in this judgment.

It is desirable that the High Court should give an opportunity to the parties to file further affidavits before taking up the case for re-hearing.

(1) [1966] 1 S.C.R. 865.

A On behalf of the appellants Mr. Chagla has given an undertaking that the provisions of the Act would not be enforced against the respondents for a month from this date. The respondents say that they will apply to the Kerala High Court for stay in the meanwhile.

B Y.P. *Appeal allowed.*