

STATE OF UTTAR PRADESH AND ANR. ETC. ETC.

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v.

UNION OF INDIA AND ANR. ETC. ETC.

FEBRUARY 4, 2003

[SYED SHAH MOHAMMED QUADRI AND K.G.  
BALAKRISHNAN, JJ.]

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*U.P. Trade Tax Act, 1948—Section 2(aa), (c), (d), (h) and section 3, 3-F (as amended by U.P. Act 31 of 1995)—Rentals collected by Department of Telecommunication (DoT) from subscribers of telephone—Assessibility to tax—Held, rentals assessable to tax since DoT is dealer as defined in Section 2(c), it collects rentals for supply of transfer of use of telephone connection which is a service, supply of telephone satisfies the requirement of transfer the right to use the goods within the meaning of sale in Section 2(h) and it also receives consideration—Constitution of India, 1950—Article 366 clause 29-A.*

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*Words and Phrases:*

*Meaning of—Term ‘goods’ in the context of Section 2(d) of the U.P. Trade Tax Act, 1948.*

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The question which arose for consideration in these appeals was whether the rentals collected by the Department of Telecommunications (DoT) from the subscribers of telephone in the State could be assessed to tax under the Uttar Pradesh Trade Tax Act, 1948.

Appellant-State contended that High Court erred in holding that DoT is not a ‘dealer’ within the meaning of the Act; that section 3-F applies to work contracts only and not to the rental charges collected by DoT, and that there is no legislative competence in the State to levy trade tax as the Parliament authorized imposition of service tax under the Finance Act 1994 on the use of the telephone service by the subscribers; that by U.P. Act 31 of 1995 sub-clauses (vii) and (viii) to section 2 (c) of the U.P. Act were added in the definition of the term ‘dealer’ to remove difficulties in the assessment of tax in the transaction relating to transfer of a right to use any goods; that addition of sub-clause (viii) in the definition of ‘dealer’ did not mean that prior to 1995, in various

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- A** Ordinances and the U.P. Act, having regard to the extended definition of 'sale' did not include a person or a government 'transferring the right to use any goods' within the meaning of 'dealer'; that if 'DoT', whether in the course of business or otherwise, transferred a right to use any goods, it was covered by the definition of 'dealer' even before the 1995 amendment inserted sub-clause (viii) in Section 2(c) and that position continued even thereafter; that in supplying instruments, accompaniments and the telephone connection to a subscriber, the DoT is transferring the rights to use those goods; that providing a telephone to a subscriber was a service, and 'transfer of the right to use the instrument, appliances and the whole exchange system was involved; and that in a composite contract,
- C** the dominant object test will have to be applied.

- Respondents-DoT contended that the DoT would not fall within the definition of 'dealer' under the U.P. Act; that the activity of providing telephone service is not 'the transfer of right to use the goods' so as to attract liability under the U.P. Act; that in a contract providing telephone
- D** by the DoT the service and sale—transfer of the right to use the goods—are so inter-twined that the rentals cannot be attributed to one or the other part and, therefore, such a composite contract cannot be dissected so as to attribute one part of the rentals to service and the other part to the transfer of the right to use the goods and accordingly assess that part of rentals to tax; that as there was no such provision to tax service in
- E** sub-clause (d) of clause 29-A no tax could be levied by the State; and that it is providing a service which does not involve transfer of a right to use any goods and that by the Finance Act, 1997, Parliament has imposed service tax, as such the State cannot levy any tax under the Act.

- F** Intervenor contended that the contract of the subscribers with the DoT for installation of telephone was an indivisible contract for providing service which cannot be split into two separate contracts- one for transfer of the right to use any goods and the other for the service provided; that under the Indian Telegraph Act, 1885 and the Rules no agreement can be spelt out to transfer the right to use any goods by the DoT to the
- G** subscriber; that supply of goods, if any, was incidental to the performance of contract of service; and that the instrument could be used only when access to the whole system is provided by DoT and that when the contract was a composite contract involving service and the transfer of the right to use any goods, in the absence of any provision in the Constitution
- H** enabling the State to levy tax for service separately, no tax could be

levied and collected under the Act.

Allowing the appeal, the Court

HELD: 1.1. Under Section 2 (c) of the Uttar Pradesh Trade Tax Act, 1948 the word 'dealer' means a person who (whether regularly or otherwise) carries on the business in U.P. and includes, inter alia, a government which (whether in the course of business or otherwise) undertakes buying, selling, supplying or distributing goods directly or indirectly for cash or deferred payment or for commission, remuneration or other valuable consideration [sub-clause (iv)]. The word 'buy' is not defined. It is antonym of 'sell' and has to be construed in the light of the definition of 'sale' in clause (h) of Section 2(c) (viii). It is an inclusive definition. It means any transfer of property in goods and includes among other transactions, a transfer of the right to use any goods for any purpose (whether or not for a specified period), for cash, deferred payment or other valuable consideration. Thus, in regard to a transfer of the right to use any goods both a person and a government will be within the ambit of the definition of 'dealer' subject to the following distinction: a person to be a 'dealer' should *carry on the business of buying, selling etc.*, whether regularly or otherwise, but a government which buys, sells etc. (*whether in the course of business or otherwise*) will be a 'dealer' for purposes of the U.P. Act. Inasmuch as the definition of 'sale' includes any transfer of property in the goods and a transfer of the right to use any goods for any purpose, the DoT which engages in transfer of right to use any goods will be a 'dealer' within the meaning of sub-clause (iv) of clause (c) of Section 2 of the U.P. Act. [798-C-F]

*M/s. Vrajlal Manilal and Co. and Anr. v. State of M.P.*, [1996] Supp. SCC 201, referred to.

1.2. After insertion of clause 29-A in Article 366 of the Constitution and consequential amendments of the term 'sale' in the Act, if 'sale' is construed in the sense it was understood before the said amendments, it will be a clear negation of the constitutional and statutory provisions, therefore, such a contention cannot be accepted. Before insertion of sub-clause (viii) in Section 2(c) of the Act, the activity of a transfer of the right to use any goods fell within the meaning of 'sale' in clause (h) so the DoT while so doing could not but be a 'dealer' within the meaning of Section 2(c) of the Act. If that was the position before the enactment of U.P. Act 31 of 1995 which inserted, inter alia, sub-clause (viii), then

A unless a contrary intention appears from the amended provisions, the pre-amendment position shall continue. Had the intention of the legislature been to change that position and exclude 'a government' from the definition of 'dealer' in regard to a transfer of the right to use the goods, it would have said so specifically. It follows that in view of the extended meaning of sale of goods, the DoT would continue to be within the ambit

B of a 'dealer' under the U.P. Act even in regard to transfer of a right to use any goods after insertion of sub-clause (viii) in clause (c) of Section 2 by U.P. Act 31 of 1995. The reasoning of the High Court that in view of amendment of Section 2(c) in 1995, adding sub-clause (viii), sub-clause (vi) had to be interpreted differently so as to exclude the DoT from the

C meaning of dealer and also the contention of the respondent-DoT cannot be accepted. Therefore, insertion of sub-clauses (vii) and (viii) in clause (c) of Section 2 was by way of abundant caution. This is not an unusual feature of the legislation. [800-D-H; 801-A]

D *The Wakefield Local Board of Health v. The West Riding and Grimsby Railway Company*, LR [1865] QB 84 and *Re: Sir Stuart Samuel*, [1913] Appeal Cases 514, referred to.

E *Raj Bahadur Kanwar Raj Nath and Ors. v. Pramod C. Bhatt, Custodian of Evacuee Property*, [1955] 2 SCR 977 and *Bhikoba Shankar Dhumal (dead) by Lrs. and Ors. v. Mohan Lal Punchand Tathed and Ors.*, [1982] 1 SCC 680, referred to.

F 1.3. The term 'goods' is defined in very wide terms so as to bring in both tangible and intangible objects. Telephone instruments and other movables, including wiring, cable etc. are undoubtedly goods. However, the position of telephone exchange was not without demur on the ground that they were housed in immovable properties. That objection need not detain this Court because intangible object, like electricity which is generated in projects and transmitted through sub-stations, housed in buildings, has been held to be goods. Therefore, the telephone connection and all other accessories which give access to the telephone exchange

G with or without instruments are 'goods' within the meaning of Section 2(d) of the U.P. Act. [802-F, H; 803-A-D]

H *Commissioner of Sales Tax, Madhya Pradesh, Indore v. Madhya Pradesh Electricity Board, Jabalpur*, [1969] 1 SCC 200 and *State of A.P. etc. v. National Thermal Power Corpn. Ltd. and Ors. etc.*, [2002] 5 SCC 203, referred to.

*Mekinley Telephone Company v. Cumberland Telephone Company*, 152 A  
Wis. 359; 140 N.W. 38; 1913 Wisc. Lexis 77, referred to.

1.4. The submission that any activity in the nature of mere service or profession is excluded from the definition of the term "business" and as the DoT is providing service, the same cannot be subjected to tax, though attractive, is devoid of any substance. The definition of a 'dealer' takes in 'a Government', when it sells, supplies, etc. whether in the course of business or otherwise. Therefore, it is not necessary that the activity of sale, etc. by the DoT should be in the course of business. Even assuming that the supply of the telephone to a subscriber, being a service, falls outside the meaning of the term 'business', the DoT would nonetheless be liable to pay tax under the U.P. Act as a 'dealer' for the simple reason of transferring the right to use the telephone instrument/apparatus and the whole system as that falls within the extended meaning of 'sale' under clause (h) of Section 2 of the U.P. Act. Further only such service is excluded from the definition of the term 'business' which does not involve the purchase or sale of goods. In the instant case, it cannot be legitimately disputed that the service involves installation of instrument and access to the exchange and telephone system as a whole which has been found to fall within the meaning of the term 'sale'. Therefore, the second part of the definition of the term 'business' is of no help to the DoT. [807-A-D]

1.5. When DoT provides telephone service, a number is allotted, an instrument/apparatus and other appliances are installed at the premises of a subscriber and the same are connected with the exchange to enable him to have access to the whole system, to dial and to receive calls. It makes no difference whether any subscriber replaces instrument of the DoT with his own instrument because the most important thing is the connection of the subscriber's telephone number with the area exchange and that was provided by the DoT. It needs to be borne in mind that handing over of the possession or the control of the whole system of exchange is not sine qua non of completing the transfer of the right to use any goods. The submission that the area telephone exchange and other systems would remain under the control of the DoT, are irrelevant to complete such a transfer. Even otherwise, after installation of the instrument and other appliances, once the DoT connects the telephone line of the assigned number of the subscriber to the area exchange, access to other telephones is established. There cannot be denial of the fact that giving such an access would complete the transfer of the right to use the

**A goods. [807-F-H; 808-A-C]**

*20th Century Finance Corporation Ltd. and Anr. v. State of Maharashtra*, [2000] 6 SCC 12 and *Rashtriya Ispat Nigam Ltd. v. Commercial Tax Officer*, [1990] 77 STC 182 and *State of Andhra Pradesh and Anr. v. Rashtriya Ispat Nigam Ltd.*, [2002] 126 STC 114, referred to.

**B** 1.6. No provision of the U.P. Act or the said Finance Act, 1994 or the Constitution is brought to the notice to hold that rentals collected by the DoT from the subscriber cannot be subjected to tax as is done under the U.P. Act. Merely because service tax is imposed by the Parliament under the Finance Act in respect of telephone connection to a subscriber

**C** is no ground to hold that the State cannot levy tax under the U.P. Act. Therefore, providing telephone service by the DoT which comprises of allotment of number, installation of an instrument/apparatus and other appliances at the premises of a subscriber, which are connected with a telephone line to the area exchange to enable him to have access to the

**D** whole system, to dial and to receive calls, in effect, falls within the meaning of the extended definition of 'sale', viz., within the meaning of 'the transfer of the right to use any goods' and the fact that it is described as service under the ITA 1885 and the Rules made thereunder or under the Finance Act, 1994 would not militate against the same being a 'sale' within the meaning of the U.P. Act. [808-F-H; 809-A, B]

**E** 1.7. In the case of a composite contract, where the service is the dominant object of the contract, the supply of goods is incidental to the enjoyment of the service, it is not possible to separate service from the supply of goods. In regard to sale of goods where the service is incidental,

**F** the principle of non-separability will apply in the absence of a specific valid statutory provision; and it would not be permissible to treat such service as a transfer of right to use the purpose of taxation under the relevant Sales Tax Act. Where, however, the supply of service as well as supply of goods are prominent objectives and they have been clubbed together under a composite contract, it would be possible to treat them

**G** separately; though covered under the same contract. [810-B, C, F, G, H]

*State of Himachal Pradesh v. Associated Hotels of India Ltd.*, [1972] 29 STC SC, referred to.

**H** *British Railways Board v. Customs and Excise Commissioners*, *Simon's Tax Cases*, [1977] 221; *British Airways Plc v. Customs and Excise*

*Commissioners Simon Tax Case*, [1990] 643; *Customs and Excise Commissioners v. British Telecommunications Plc Simon Tax Case* [1999] 758, referred to. A

1.8. The insertion of clause 29-A in Article 366 of the Constitution did not altogether obliterate the distinction between sale and service, except in a case falling under sub-clause (f) thereof. In such a case, the transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply is made. In other respects the distinction between sale and service for imposing tax is maintained. [810-D, E] B

1.9. In the instant case, the service of telephone connection cannot be artificially split into various categories—supply of instruments and accompaniment on the one hand and supply of telegraphic line/connection on the other, to name the former as ‘sale’ and the latter as ‘service’. The analogy of composite contract will apply where ‘sale’ and ‘service’ are two different independent objects. Inasmuch as it is found that the DoT is a ‘dealer’ as defined in Section 2(c) of the U.P. Act and it collects rentals for the supply of transfer of use of telephone connection, which is compendiously called ‘service’ and that the supply of telephone satisfies the requirements of a transfer of the right to use the goods within the meaning of ‘sale’ in Section 2(h); it also receives consideration, therefore, the requirements of charging under Section 3 read with Section 3(f) are satisfied. [812-C-F] C D E

*Union of India and Ors. v. Secretary, Revenue Department, (CTII), Government of Andhra Pradesh and Ors.*, (1999) 113 STC 203 and *Union of India and Anr. v. State of Haryana and Anr.*, [2001] 123 STC 539, disapproved. F

*M/s. Northern India Caterers (India) Ltd. v. Lt. Governor of Delhi*, [1980] 2 SCC 167; *The Senior Electric Inspector and Ors. v. Laxmi Narayan Chopra and Ors.*, [1962] 3 SCR 146; *State of Bihar v. Mangal Sao*, [1963] 1 SCR 148; *Delhi Science Forum and Ors. etc. v. Union of India and Anr. etc.*, [1996] 2 SCC 405 and *The State of Punjab v. M/s. Associated Hotels of India Ltd.*, [1972] 1 SCC 472, referred to. G

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 5781 of 1999.

A From the Judgment and Order dated 13.9.1999 of the High Court of U.P. in W.P. 115 of 1995.

WITH

B C.A. Nos. 5782-92/99, 3283-3286, 3530-3533, 3705, 3706, 3757, 4336, 4107/2000, 3778-3780, 5886 of 2000, C.A. Nos. 877-937/2003.

C Sunil Gupta, S. Ganesh, T.L.V. Iyer, Ashok H. Desai, Joseph Vellapally, R.C. Verma, Mukesh Verma, Vivek Vishnoi, Punit Dutt Tyagi, Ms. Vibha Mahajan Seth, A. Subba Rao, Tara Chandra Sharma, Hemant Sharma, Y.P. Mahajan, P. Parmeswaran, Ramesh Babu, M.R., K.R. Sasiprabhu, Rajesh Kumar, Manjul Bajpai, Ms. Bina Gupta, Ms. Vanita Bhargava, Ms. Divya Roy Jha and Ms. Garima Dewan for the appearing parties.

The Judgment of the Court was delivered by

D **SYED SHAH MOHAMMED QUADRI, J.** The State of Uttar Pradesh and the Sales Tax Officer (referred to in this judgment as, 'the State') are in appeal against the common judgment of a Division Bench of the High Court of Judicature at Allahabad in Writ Petition No.115 of 1995 *Union of India and Anr. v. State of U.P. and Anr.* and batch dated September 1, 1998.

E The State, being of the opinion that the second respondent (The Manager, Department of Telecommunications, of the first respondent hereinafter collectively referred to as the 'DoT') failed to file return of the turnover of the rentals collected from the subscribers for 'the transfer of right to use' the telephone system during the year 1988, under the provisions of the Uttar Pradesh Trade Tax Act, 1948 (for short, 'the U.P. Act'), called upon the F 'DoT to file return therefor. However, no return was filed by the DoT. The State assessed the tax payable by the DoT in exercise of the power conferred under sub-section (3) of Section 7 of the U.P. Act. The DoT challenged the validity of the orders of assessment in the writ petitions before the High Court on various grounds. The State pleaded justification for passing the order of assessment in view of the extended definition of the expression 'Tax on the sale or purchase of goods' in clause 29-A\*\* of Article 366 of the Constitution of India and the relevant provisions of the U.P. Act. The High Court, by the impugned judgment and order, allowed the writ petitions taking G the view that (i) the DoT (Union of India) is not a 'dealer' within the meaning

\* [Reported in [1999] 114 STC 288]

H \* By the Constitution (Forty-sixth Amendment) Act. 1982]

of the Act; (ii) Section 3-F of the Act applies to work contracts only and not to the rental charges collected by the DoT; (iii) there is no legislative competence in the State to levy Trade Tax in view of the fact that the Parliament authorised imposition of service tax under the Finance Act, 1994 on the use of the telephone service by the subscribers; (iv) Article 285(1) of the Constitution of India prohibits the State from imposing any tax on the property of the Union of India; and (v) in providing telephone service through the DoT, Union of India is discharging its sovereign function which cannot be subjected to trade tax.

Mr. Sunil Gupta, the learned senior counsel appearing for the appellants-State, assailed the validity of the reasoning and conclusions of the High Court on all the points, referred to above.

Mr. Mukul Rohtagi, the learned Additional Solicitor General, appearing for the respondents-DoT, conceded in our view rightly, that he would not be supporting the judgment of the High Court on the grounds (iv) and (v) mentioned above. But he contended, rather vehemently, that the DoT would not fall within the definition of 'dealer' under the U.P. Act and that the activity of providing telephone service would not answer the definition of 'the transfer of right to use the goods' and, therefore, the High Court rightly quashed the impugned orders of assessment.

Mr. Joseph Vellapally, the learned senior counsel appearing for the intervenor contended that the contract of the subscribers with the DoT for installation of telephone was an indivisible contract for providing service which cannot be split into two separate contracts - one for transfer of the right to use any goods and the other for the service provided. He elaborated the contention by pointing out that under the Indian Telegraph Act, 1885 and the Rules made thereunder, no agreement can be spelt out to transfer the right to use any goods by the DoT to the subscriber. In any event, submitted the learned senior counsel, supply of goods, if any, was incidental to the performance of the contract of service. Relying on the decision of this Court in *The State of Punjab v. M/s. Associated Hotels of India Ltd.* [1972] 1 SCC 472 he argued that such composite contracts are indivisible as the parties never contracted to sell/supply any goods; such incidental sale/supply, being merely concomitant of the performance of the service contracted for, would equally apply to a telephone service contract which incidentally involved supply of instrument. He further contended that in providing telephone service, it could not be said that the right to use the whole system of the telephone exchange was transferred as the possession and control of the whole system





- A Government. The prescribed rate cannot exceed twenty five per cent but the State Government may, by notification, declare different rates for different goods or different classes of dealers. The net turnover in respect of a transfer referred to in clause (a) of sub-section (1), has to be determined after making deductions enumerated in sub-section (2) read with Rule 44C of the Tax Rules, Unfortunately, the High Court failed to notice Section 3F in its entirety and erred in confining it only to 'goods involved in the execution of works contract'.

- C For understanding the true import of the aforementioned provisions, it would be appropriate to notice the definitions of the terms 'business', 'dealer', 'goods', and 'sale' defined in clauses (aa), (c), (d) and (h) respectively, of Section 2 of the U.P. Act, which read as under:

“(aa) ‘business’, in relation to business of buying or selling goods, includes -

- D (i) xxx xxx xxx
- (ii) the execution of any works contract or the transfer of the right to use any goods for any purpose (whether or not for a specified period.

- E (iii) xxx xxx xxx

but does not include any activity in the nature of mere service or profession which does not involve the purchase or sale of goods.”

- F (c) ‘dealer’ means any person who carries on in Uttar Pradesh (whether regularly or otherwise) the business of buying, selling, supplying or distributing goods directly or indirectly, for cash or deferred payment or for commission, remuneration or other valuable consideration and includes -

- G (i) to (iii) xxx xxx xxx
- (iv) a Government which, whether in the course of business or otherwise buys, sells, supplies or distributes goods, directly or otherwise for cash or for deferred payment or for commission, remuneration or other valuable consideration;
- H

- (v) every person who acts within the State, as an agent of a dealer residing outside the State, and buys, sells, supplies or distributes goods in the State or acts on behalf of such dealer as - **A**
- (a) a mercantile agent as defined in the Sale of Goods Act, 1930; or **B**
- (b) an agent for handling of goods or documents of title relating to goods; or
- (c) an agent for the collection or the payment of the sale price of goods or as a guarantor for such collection or such payment; **C**
- (vi) a firm or a company or other body corporate, the principal office or headquarters whereof is outside the State having a branch or office in the State, in respect of purchases or sales, supplies or distribution of goods through such branch or office. **D**
- (vii) xxx xxx xxx
- (viii) every person who carries on business of transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration. **E**
- Provided xxx xxx”
- “(d) ‘goods’ means every kind or class of movable property and includes all material commodities and articles involved in the execution of a works contract, and growing crops, grass, trees and things attached to or fastened to anything permanently attached to the earth which under the contract of sale are agreed to be severed but does not include actionable claims, stocks, shares, securities or postal stationery sold by the Postal Department.” **F**
- “(h) ‘sale’ with its grammatical variations and cognate expressions, means any transfer of property in goods (otherwise than by way of a mortgage, hypothecation, charge or pledge) for cash or deferred payment or other valuable consideration, and include - **H**

- A (i) to (iii) xxx xxx xxx
- (iv) a transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;”

B Inasmuch as under Section 3 read with Section 3F of the U.P. Act the liability to pay tax, *inter alia*, on ‘the transfer of the right to use any goods’ at the specified rate is on a dealer, as defined in Section 2(c) thereof, extracted above, we shall examine the scope of the definition to ascertain - is the DoT a dealer?

C The word ‘dealer’ means a person who (whether regularly or otherwise) carries on the business in U.P. and includes, *inter alia*, a government [sub-clause (iv)] which (whether in the course of business or otherwise) undertakes buying, selling, supplying or distributing goods directly or indirectly for cash or deferred payment or for commission, remuneration or other valuable consideration. Now it becomes necessary to look into the definition of ‘buy’ and ‘sell’.

D The word ‘buy’ is not defined. It is an antonym of ‘sell’ and has to be construed accordingly in the light of the definition of ‘sale’ in clause (h), quoted above, It is an inclusive definition. It means any transfer of property in goods and includes among other transactions, a transfer of the right to use any goods for any purpose (whether or not for a specified period)

E for cash, deferred payment or other valuable consideration. It is thus clear that in regard to a transfer of the right to use any goods both a person and a government will be within the ambit of the definition of ‘dealer’ subject to the following distinction: A person to be a ‘dealer’ should *carry on the business of buying selling* etc., whether regularly or otherwise, but a government which buys, sells etc. (*whether in the course of business or otherwise*) will be a ‘dealer’ for purposes of the U.P. Act.

F Inasmuch as the definition of ‘sale’ includes any transfer of property in the goods and a transfer of the right to use any goods for any purpose, the DoT which engages in transfer of right to use any goods will be a ‘dealer’ within the meaning of sub-clause (iv) of clause (c) of Section 2 of the U.P. Act.

G In *M/s. Vrajlal Manilal and Co. and Anr. v. State of M.P. and Anr.*, [1986] Supp. SCC 201, this Court considered the meaning of Explanation II to Section 2 (d) of the Madhya Pradesh General Sales Tax Act, 1959, which was similar in terms to sub-clause (iv) of clause (c) of Section 2 of the U.P. Act and held:

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“The language of Explanation II shows that its purpose is to create a legal fiction, and that while under the main clause, for a person to be a dealer, he must carry on the business of buying, selling, supplying or distributing goods, even if the Central Government or a State Government or any of their departments or offices does not carry on such business, if it buys, sells, supplies or distributes goods, it is to be deemed to be a dealer for the purposes of the M.P. Sales Tax Act, that is, for the purposes of the levy and collection of tax under M.P. Sales Tax Act. After the amendment of clause (d) by the 1971 Act, it is irrelevant for the purposes of the levy of tax under the M.P. Sales Tax Act whether the Central Government or a State Government or any of their departments or offices have bought or sold goods in the course of business.”

While so, by U.P. Act 31 of 1995, sub-clauses (vii) and (viii) which deal with ‘person’ were inserted in clause (c) of Section 2 with effect from September 3, 1985. Sub-Clause (vii) incorporates business of transfer of property in goods involved in the execution of a work contract and sub-clause (viii) incorporates business of transfer of the right to use any goods for any purpose.

In the present discussion, we are concerned with the effect of insertion of sub-clause (viii) in clause (c) of Section 2 on the aforementioned conclusion that the DoT is a ‘dealer’ falling in sub-clause (iv) of the said clause. It was contended by the learned Additional Solicitor General that in sub-clause (iv) about ‘a government,’ it was not specifically provided as was done in sub-clause (viii) in regard to a person, that he must be carrying on the business of a transfer of the right to use any goods for any purpose; in the absence of those words in clause (iv), the DoT, even if it transferred a right to use any goods for any purpose for rentals, would not fall within the meaning of the term ‘dealer’. He urged that every section, every clause and every word in a legislation should be given some meaning; it could not be presumed that the legislature carried out the exercise in futility in adding sub-clause (viii) to Section 2(c). The intention of the legislature, it was submitted, in adding sub-clause (viii) to Section 2(c) was only to make it clear that ‘a government’ would not be a ‘dealer’ in regard to the extended meaning of ‘sale’ which included the transfer of a right to use any goods but only in regard to sale of goods in its traditional meaning. Mr. Gupta countered that contention by inviting our attention to the Statement of Objects and Reasons of U.P. Act 31 of 1995 that the sub-clauses (vii) and (viii) were added in the definition of

A the term 'dealer' to remove difficulties in the assessment of tax in the transaction relating to transfer of a right to use any goods. The legislature, submitted the learned counsel, earlier amended the definition of 'sale' in Section 2(h) leaving the definition of 'dealer' static but later it was thought that *ex abundanti cautela* the definition of 'dealer' might also be amended like the definition of 'sale' and by U.P. Act No. 31 of 1995 a new package of amendments was introduced relating to the transfer of a right to use any goods by adding sub-clause (viii) to clause (c) of Section 2. He argued that addition of sub-clause (viii) in the definition of 'dealer' did not mean that prior to 1995, in various Ordinances and the U.P. Act, having regard to the extended definition of 'sale', did not include a person or a government 'transferring the right to use any goods' within the meaning of 'dealer'. It was emphasised that if 'the DoT', whether in the course of business or otherwise, transferred a right to use any goods, it was covered by the definition of 'dealer' even before the 1995 amendment inserted sub-clause (viii) in clause (c) of Section 2 and that position continued even thereafter.

D We are afraid, we cannot accede to the contentions of the learned Additional Solicitor General. After insertion of clause 29-A in Article 366 of the Constitution and consequential amendments of the term 'sale' in the U.P. Act, if 'sale' is construed in the sense it was understood before the said amendments, it will be a clear negation of the constitutional and statutory provisions, therefore, such a contention cannot be accepted. We have already held above that before insertion of sub-clause (viii) in Section 2(c) of the U.P. Act, the activity of a transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration, fell within the meaning of 'sale' in clause (h) so the DoT while so doing could not but be a 'dealer' within the meaning of Section 2(c) of the U.P. Act. If that was the position before the enactment of U.P. Act 31 of 1995 which inserted, *inter alia*, sub-clause (viii), then unless a contrary intention appears from the amended provisions, in our view, the pre-amendment position shall continue. Had the intention of the legislature been to change that position and exclude 'a government' from the definition of 'dealer' in regard to a transfer of the right to use the goods, it would have said so specifically. It follows that in view of the extended meaning of sale of goods, the DoT would continue to be within the ambit of a 'dealer' under the U.P. Act even in regard to transfer of a right to use any goods after insertion of sub-clause (viii) in clause (c) of Section 2 by U.P. Act 31 of 1995. We are, therefore, unable to uphold the reasoning of the High Court that in view of amendment of Section 2(c) in 1995, adding sub-clause (viii),

sub-clauses (vi) had to be interpreted differently so as to exclude the DoT from the meaning of 'dealer' and also the contention of the learned Additional Solicitor General. In our view, insertion of sub-clauses (vi) and (vii) in clause (c) of Section 2 was, as submitted by Mr. Gupta, by way of abundant caution. This is not an unusual feature of the legislation. As long back as in 1865 in *The Wakefield Local Board of Health v. The West Riding and Grimsby Railway Company*, LR (1865) QB 84, Cockburn, C.J. held:

"I am opinion that the objection raised by the respondents was untenable. I think the words inserted at the end of the definition in the interpretation clause, section 3 of the 8 Vict.c.20, were inserted, as Mr. Cleasby argues, from excess of caution, in the apprehension that justices, if not warned of what the law is, might act although inserted; and the legislature thought that, if they did not actually include what would be virtually implied, it might be assumed that it was excluded."

In *Re: Sir Stuart Samuel*, (1913) Appeal Cases 514, the Privy Council observed:

"It is desirable to notice an argument derived from s.4 of 41 Geo.3,c.52, passed in 1801. This section disqualifies for a seat in the Parliament of the United Kingdom any one who makes a contract with a Commissioner of His Majesty's Treasury in Ireland or with any other person whomsoever for or on account of the public service in Ireland. This was surplusage (such is the argument) if the Act of 1782 had already made such contracts, irrespective of place, a ground of disqualification for the British Parliament, since all persons disqualified for the British Parliament were by s.1 of the Act of 1801 already disabled from sitting in the Parliament of the United Kingdom, at all events for British constituencies. There are several answers to this contention. It is not a conclusive argument as to the construction of an earlier Act to say that unless it be construed in a particular way a later enactment would be surplusage. The later Act may have been designed, *ex abundante cautela*, to remove possible doubts."

To the same effects are the views expressed by this Court in *Raj Bahadur Kanwar Raj Nath and Ors. v. Pramod C. Bhatt Custodian of Evacuee Property*, [1955] 2 SCR 977:

"The operative portion of the section which confers power on the

A Custodian to cancel a lease is unqualified and absolute and could not be abridged by reference to the non-obstante clause which was only inserted *ex abundanti cautela* with a view to repel a possible contention that the section does not by implication repeal statutes conferring rights on lessees."

B And in *Bhikoba Shankar Dhumal (dead) by Lrs. and Ors. v. Mohan Lal Punchand Tathed and Ors.*, [1982] 1 SCC 680. This Court held :

C "It appears to us that the said paragraph was introduced by way of abundant caution to get over the possible objection raised on the basis of the decision in the case of *Dadarao v. State of Maharashtra*, AIR (1970) Bom. 144. The said paragraph is merely declaratory of what the true legal position had always been even from the commencement of the Act. The introduction of an express provision to the above effect does not have the effect of altering the true legal position as explained by us above even without the aid of such express provision. This becomes further clear from the observations found in the decision of this Court in *Raghunath Laxman Wani v. State of Maharashtra*, [1971] 3 SCC 391."

E It may be that the same amount of precaution was not taken by the legislature in defining 'dealer' with respect to ' a government, in sub-clause (iv) as was done regarding 'a person' by inserting sub-clauses (vii) and (viii) in clause (c) of Section 2; but that, in our view, in the light of the above discussion, would hardly make any difference in construing the provisions of sub-clause (iv) of clause (c) in Section 2 of the U.P. Act.

F Before taking up the other contentions we may conveniently dispose of a short point - ambit of the definition of the term 'goods' - quoted above. It is defined in very wide terms so as to bring in both tangible and intangible objects. It takes in its fold every kind or class of movables, including all material commodities and articles involved in the execution of a works contract and growing crops, grass, trees and things attached to or fastened to anything permanently attached to the earth which under the contract of sale are agreed to be severed but excluding actionable claims, stocks, shares, securities or postal stationery sold by the Postal Department. According to the DoT, what is being supplied as service is a telephone connection with an instrument which is connected with permanent telephone lines laid up to the subscriber's place where the telephone system is installed and the same is connected with

G H the exchange. Telephone instruments and other movables, including wiring,

cable etc., are undoubtedly goods. However, the position of telephone exchange was not without demur on the ground that they were housed in immovable properties. That objection need not detain us because intangible object, like electricity which is generated in projects and transmitted through sub-stations, housed in buildings, has been held to be goods. In *Commissioner of Sales Tax, Madhya Pradesh, Indore v. Madhya Pradesh Electricity Board, Jabalpur*, [1969] 1 SCC 200, a Bench of three learned Judges of this Court took the view that the electricity falls within the meaning of 'goods' under the Madhya Pradesh General Sales Tax Act, 1959. That view was affirmed in a recent judgment of a Constitution Bench of this Court in *State of A.P. etc. v. National Thermal Power Corpn. Ltd. and Ors. etc.*, [2002] 5 SCC 203 holding that electricity though an intangible object is 'good' covered by Entry 54 of List II of Schedule VII to the Constitution as also Section 2(d) of the Central Sales Tax Act, 1956. The Supreme Court Wisconsin (U.S.A.) in *Mckinley Telephone Company v. Cumberland Telephone Company*, [152 Wis. 359; 140 N.W. 38; 1913 Wisc. Lexis 77] held the view that the furnishing of telephone service might be classed as the supplying of a commodity constituting a subject of commerce. We, therefore, have no hesitation in holding that telephone connection and all other accessories which give access to the telephone exchange with or without instruments are 'goods' within the meaning of Section 2(d) of the U.P. Act.

The next question, that generated lengthy debates, is : Does the supply of telephone connection involve a transfer of the right to use any goods or amount to providing a service?

We have noticed above that the liability to pay tax under the U.P. Act is on every dealer on his turnover of sales of purchases; it is also concluded that telephone connection along with all accessories falls within the meaning of 'goods'; we have also opined that the definition of 'sale' in clause (h) of Section 2 is an inclusive definition and includes a transfer of the right to use any goods for any purpose.

It is necessary to notice here certain provisions governing supply of telephone connection provided by the DoT which alone has exclusive privilege and control. We have perused 'the General Rules Governing the Provision of Telephone Connections, Telex Connections and Accessories, Etc.' (for short, 'the general rules'). Rule 3 of the general rules says that all telephone connections and other similar services provided or authorised by the department shall, unless governed by a separate contract, be subject to the conditions set forth in the Indian Telegraph Rules. It further says that the Divisional Engineer

- A shall install and, subject to observance of the Indian Telegraph Rules or the specific Hiring Contract by the subscriber, maintain in good working order the equipment and apparatus provided by the department and when necessary, substitute a different apparatus in accordance with departmental instructions issued from time to time. The Indian Telegraph Act, 1885 (for short, 'the ITA 1885') defines 'telegraph' to mean, any appliance, instrument, material or apparatus used or capable of use for transmission or reception of signs, signals writing images and sounds or intelligence of any nature by wire, visual or other electro-magnetic emissions, Radio waves or Herzian waves, galvanic, electric or magnetic means. 'Telegraph line' defined in Section 3(4) of the ITA 1885, means a wire or wires used for the purpose of a telegraph, with any casing, coating, tube or pipe enclosing the same, and any appliances and apparatus connected therewith for the purpose of fixing or insulating the same. In *The Senior Electric Inspector and Ors. v. Laxmi Narayan Chopra and Ors.*, [1962] 3 SCR 146, a Bench of three learned Judges held that 'Telegraph line, is comprehensive enough and means a wire or wires used for the purpose of an appliance or apparatus for receiving telegraphic or other communications by means of electricity, and it need not be a continuous physical channel from the point of transmission to the point of reception. A wireless transmitter transmits sound as electro-magnetic waves and the said waves are detected by the aerial and fed into the receiving apparatus by wires. So the wires of the aerial as well as of the apparatus are used for the purpose of the apparatus receiving communications. Thus, the receiving apparatus employs 'telegraph lines' within the meaning of Section 3(4) of the ITA 1885. Section 4 of the ITA 1885 declares that the Central Government shall have the exclusive privilege of establishing, maintaining and working telegraphs. In *State of Bihar v. Mangal Sao*, [1963] 1 SCR 148, this Court was inclined to approve that Section 4 applied to telephone. The same view is reiterated in *Delhi Science Forum and Ors. etc. v. Union of India and Anr. etc.*, [1996] 2 SCC 405. Under Section 7 of the ITA 1885, the Central Government is empowered to make rules consistent with the Act for the conduct of all or any telegraphs, established, maintained or worked by the Government or by persons licensed under this Act. Clause (e) thereof provides that the rules may also be framed in regard to the conditions and restrictions, subject to which any telegraph line, appliance or apparatus for telegraphic communication shall be established, maintained, worked, repaired, transferred, shifted, withdrawn or disconnected. Sections 20 and 21 make unauthorised use of telegraph an offence.
- H The Indian Telegraph Rules, 1951 (for short, 'the Rules') were framed

in exercise of the power under Section 7 of the ITA 1885. Rules in Part-V thereof deal with telephones. Under the Rules, the subscribers are required to take care of the telephone apparatus and in the event of the apparatus, in the premises of the subscribers, being damaged or lost, they are obliged to pay the cost of replacing and repairing. Rule 413 says that all services will be subject to the said Rules. Rule 411 gives classification of the connections under various Heads. Rule 412 provides for supply and maintenance of equipment by the Divisional Engineer, Telegraph. The Rules also provide for disconnection of service in certain conditions. Rule 434 prescribes charges for various services, like installation and additional facilities, reconnection, transfer, shifting, etc. For 'Measured Rate System' bi-monthly rentals have to be paid by the subscriber at the prescribed rate as also the fees. Different rate is provided for 'Flat Rate System'. The Rules, referred to above, show complete control of the DoT in regard to all matters connected with the installation of the telephone by providing apparatus and matters connected therewith including the charges payable by the subscribers for the service provided. Rule 437 says that the rental for a period shall be payable before the commencement of that period. Rule 438 defined the term 'Rental periods' - Monthly, bi-monthly and annual rental periods shall commence from the first of a month or from such other day as the Telegraph Authority may fix: rentals for broken periods of a month shall be charged proportionately. Though calls whether local, STD or ISD are charged separately, rentals give allowance for certain number of free calls.

The case of the State is that in supplying instruments, accompaniments and the telephone connection to a subscriber, the DoT which is having exclusive privilege, is transferring the right to use those goods. The DoT maintains that it is providing a service which does not involve transfer of a right to use any goods and that by the Finance Act, 1997, the Parliament has imposed service tax, as such the State cannot levy any tax under the U.P. Act. The State, however, did not dispute that providing a telephone to a subscriber was a service, but what was pressed was that in providing service, 'transfer of the right to use the instrument, appliance and the whole exchange system was involved'. Now, it is clear that when the DoT provides a telephone to a subscriber, it installs instrument, accessories and gives necessary connection which enables him to access the whole system to avail of the service by making out-going calls and receiving incoming calls whether local, STD or ISD and that is compendiously termed as 'service'.

The question whether a given activity is one of sale or service is a

A vexed question. The terminology employed to describe an activity as sale or service is not conclusive in itself. By calling sale as service or vice-versa, the substance of the transaction will not get altered. The question has to be determined by discerning the substance of the transaction in the context of the contract between the parties or in a case of statutory contract in the light of the relevant provisions of the Act and the Rules. If an activity or activities are comprehensively termed as 'service' but they answer the description of 'sale' within the meaning of a Statute, they can nonetheless be regarded sale for the purpose of that Statute. In other words, it is possible, an activity may be service for purposes of one Act and sale for purposes of another Act. It may also be that in a given case, on the facts of that case, a particular activity can be treated as 'service' but in a different fact situation the same could be sale under the same Statute. In *M/s. Northern India Caterers (India) Ltd. v. Lt. Governor of Delhi*, [1980] 2 SCC 167 the question that fell for consideration of the Constitution Bench of this Court was, whether the service of meals to casual visitors in the restaurant was taxable as a 'sale', (i) when the charges were lump sum per meal or (ii) when they were calculated per dish? It was held that in both the above situations it would be 'service'. On an application filed to review the said judgment while dismissing the review petition it was observed that the judgment had rested on the factual foundation and must be understood in that light. Rejecting the contention that the respondent therein as well as the States were apprehensive that the judgment would be invoked by the restaurant-owners in cases where there was a sale of food and title in the food passes to the customers, as one which could not be reasonably entertained, it was held:

F "Indeed, we have no hesitation in saying that where food is supplied in an eating-house or restaurant, and it is established upon the facts that the substance of the transactions, evidenced by its dominant object, is a sale of food and the rendering of services is merely incidental, the transaction would undoubtedly be exigible to sales tax."

G The learned Additional Solicitor General in support of his contention submitted that the DoT was providing service so it is not liable to tax under the U.P. Act and invited our attention to the second part of the definition of the word 'business' in clause (aa) of Section 2. The definition is extracted above. The word 'business' is defined in relation to business of buying or selling goods. The definition is in two parts. The first part includes among others transfer of the right to use any goods for any purpose (whether or not H for a specified period). The second part which excludes any activity in the

nature of mere service not involving purchase or sale of goods reads, "but does not include any activity in the nature of mere service or profession which does not involve the purchase or sale of goods." "It was argued that any activity in the nature of mere service or profession is excluded from the definition of the term 'business' and as the DoT is providing service, the same cannot be subjected to tax. In our view, the contention though attractive, is devoid of any substance. There are more answers than one to this contention. The first is that the definition of a 'dealer' takes in 'a Government', when it sells, supplies, etc. whether in the course of business or otherwise. Therefore, it is not necessary that the activity of sale, etc. by the DoT should be in the course of business. Even assuming that the supply of the telephone to a subscriber, being, a service, falls outside the meaning of the term 'business', the DoT would nonetheless be liable to pay tax under the U.P. Act as a 'dealer' for the simple reason of transferring the right to use the telephone instrument/apparatus and the whole system as that falls within the extended meaning of 'sale' under clause (h) of Section 2 of the U.P. Act. And the second is, only such service is excluded from the definition of the term 'business' which does not involve the purchase or sale of goods. In the instant case, it cannot be legitimately disputed that the service involves installation of instrument and access to the exchange and telephone system as a whole which has been found to fall within the meaning of the term 'sale'. Therefore, the second part of the definition of the term business is of no help to the DoT.

It was then urged that in providing telephone service by the DoT, installation of instrument/apparatus and appliances is insignificant and in many cases subscribers themselves have their own instruments; the more important part is access to the area exchange and the whole system connected thereto without which the installation is of no consequence and the same remains under the possession and full control of the DoT so there was no transfer of the right to use any goods so as to attract liability under the U.P. Act. We are not persuaded to accept this submission. It is true that under the Rules, referred to above, as service, a number is allotted, an instrument/apparatus and other appliances are installed at the premises of a subscriber and the same are connected with the area exchange to enable him to have access to the whole system, to dial and to receive calls. In our view, it makes no difference whether any subscriber replaces instruments of the DoT with his own instrument because the most important thing is the connection of the subscriber's telephone number with the area exchange and that was provided by the DoT. Insofar as the contention of giving possession or control of the

- A** whole system of Exchange is concerned, which is said to comprise mostly of immovable property, it needs to be borne in mind that handing over of the possession is not *sine qua non* completing the transfer of the right to use any goods. It was so held by a Constitution Bench of this Court in *20th Century Finance Corporation Ltd. and Anr. v. State of Maharashtra*, [2000] 6 SCC 12. A 'transfer of the right to use any goods' will be complete according to the law laid down by the majority in that case, on completion of the contract to transfer of the right to use the goods. The contention that the area telephone exchanges and other systems would remain under the control of the DoT, are irrelevant to complete such a transfer. Even otherwise, after installation of the instrument and other appliances, once the DoT connects the telephone
- B** line of the assigned number of the subscriber to the area exchange, access to other telephones is established. There cannot be denial of the fact that giving such an access would complete the transfer of the right to use the goods. However, reliance is placed on the decision of the High Court of Andhra Pradesh in *Rashtriya Ispat Nigam Ltd. v. Commercial Tax Officer*, [1990] 77 STC 182 which was affirmed by this Court in *State of Andhra Pradesh and Anr. v. Rashtriya Ispat Nigam Ltd.*, [2002] 126 STC 114. It is unnecessary to deal with these cases in any detail; suffice it to say, in that case there was a finding of fact that the transaction did not involve transfer of the right to use the machinery in favour of contractors and that determined the issue.
- C**
- D**
- E** It may be mentioned that during the relevant period (1988) no service tax was enforced. It was in 1994 that service tax was levied for the first time as per Chapter V of the Finance Act, 1994. Section 66 thereof created charge of service tax in regard to taxable services. 'Service tax' is defined in clause (34) of Section 65 to mean tax chargeable under the provisions of that Chapter.
- F** 'Taxable service' is defined (under sub-clause (b) of clause 41 of Section 65) to mean any service provided to, *inter alia*, a subscriber by the telegraph authority in relation to a telephone connection. No provision of the U.P. Act or the said Finance Act, 1994 or the Constitution of India is brought to our notice to hold that rentals collected by the DoT from the subscriber cannot be subjected to tax as is done under the U.P. Act. Merely because service tax is imposed by the Parliament under the said Finance Act in respect of telephone connection to a subscriber, is no ground to hold that the State cannot levy tax under the U.P. Act.
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**H** For the aforementioned reasons, we hold that providing telephone service by the DoT which comprises of allotment of number, installation of an

instrument/apparatus and other appliances at the premises of a subscriber, which are connected with a telephone line to the area exchange to enable him to have access to the whole system, to dial and to receive calls, in effect, falls within the meaning of the extended definition of 'sale', viz. within the meaning of 'the transfer of the right to use any goods' and the fact that it is described as service under the ITA 1885 and the Rules made thereunder or under the Finance Act, 1994 would not militate against the same being a 'sale' within the meaning of the U.P. Act.

The contention that remains to be considered is that in a contract providing telephone by the DoT the service and sale - transfer of the right to use the goods - are so inter-twined that the rentals cannot be attributed to one or the other part and, therefore, such a composite contract cannot be dissected so as to attribute one part of the rentals to service and the other part to the transfer of the right to use the goods and accordingly assess that part of rentals to tax. Reliance was placed on a decision of this Court in *Northern India Caterers*, (supra) and it was added that it had resulted in insertion of sub-clause (f) in clause 29-A of Article 366 of the Constitution; the argument proceeded that as there was no such provision to tax service in sub-clause (d) of clause 29-A, no tax could be levied by the State. We shall deal with this argument with the contentions of Mr. Joseph Vellapally, learned senior counsel appearing for the intervenors. He focussed on the fact that the instrument could be used only when access to the whole system is provided by the DoT and argued that when the contract was a composite contract involving service and the transfer of the right to use any goods, in the absence of any provision in the Constitution enabling the State to levy tax for service separately, no tax could be levied and collected under the U.P. Act. Mr. Sunil Gupta submitted that in a case of composite contract, the dominant object test will have to be applied.

The following three situations were adverted to in the submissions:

- (1) where the service is the main object of the contract and the supply of other things are merely incidental to enable the enjoyment of the service itself;
- (2) where the service is incidental and the real contract is to sell the goods; and
- (3) where both the service as well as the sale of goods are equally prominent and they have been clubbed in one contract.

**A** Whether a given contract falls under one or the other category is essentially a question of fact to be determined on the terms of the contract between the parties or, in case of a statutory contract, the rules governing such a contract.

**B** Whereas in the case of a composite contract falling under the first category, where the service is the dominant object of the contract, the supply of goods is incidental to the enjoyment of the service; for example, in a hotel, where a room is hired, the supply of ornamental objects in the room, like chandelier, scenery, decoration pieces in the room or items, like linen, soap, shampoo etc. are incidental to make the service more useful, effective and attractive. In such a case, it is not possible to separate service from the supply of goods. This principle was laid down by this Court in *State of Himachal Pradesh v. Associated Hotels of India Ltd.*, (1972) 29 STC 474 SC and affirmed in *Northern India Caterers*, (supra).

**C**

**D** The insertion of clause 29-A in Article 366 of the Constitution of India did not altogether obliterate the distinction between sale and service, except in a case falling under sub-clause (f) thereof which enables levy of tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration. In such a case, the transfer, delivery or supply of any goods shall be deemed to be a 'sale' of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made. In other respects the distinction between sale and service for imposing tax is maintained.

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**F** In regard to sale of goods where the service is incidental, the principle of non-separability will apply in the absence of a specific valid statutory provision; for example, in a restaurant/hotel, where food or other articles are sold, the supply of service like providing cutlery washing liquid, towels, music, etc., is merely incidental and it would not be permissible to treat such service as a transfer of right to use the goods for the purpose of taxation under the relevant Sales Tax Act. Where, however, the supply of service as well as supply of goods are prominent objectives and they have been clubbed together under a composite contract, it would be possible to treat them separately; for example, where in a holiday package, transportation, boarding and lodging are separately treated, it would be possible to assess them

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separately, though covered under the same contract.

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In *British Railways Board v. Customs and Excise Commissioners*, [Simon's Tax Cases, 1977 (page 221)] the question before the Court of Appeal was : whether the supply of a student identity card constituted the supply of service of a description which qualified for zero-rating. In that case, the British Railways Board provided special facilities for rail travel by students. A student could purchase an identity card for pound 1.50 to enable him to obtain rail ticket at reduced rates. It was held that sale of identity card and the subsequent sale to the card-holder of a ticket for a particular journey at a reduced price could not be treated as separate and isolated transactions and, therefore, pound 1.50 paid for the identity card was properly to be regarded as a part payment in advance for the supply of transport service.

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*British Airways Plc v. Customs and Excise Commissioners* [Simon Tax Case, [1990] page 643; is a case wherein in the flights operated by the British Airways to transport passengers by air, food was served to the passengers, the price was the same whether or not a passenger availed the facility of food. The Court of Appeal observed that the question was : whether British Airways had made one supply or two supplies. It was held that in flights catering was part of and integral to the supply of transportation and, accordingly, British Airways had made only one supply, that of air transportation.

D

To the same effect is the view in *Customs and Excise Commissioners v. British Telecommunications Plc* [Simon Tax Cases, [1999] (page 758). In that case British Telecommunications purchased new cars for its fleet of vehicles. The question that arose was : whether the sale of cars and their transportation to the agreed delivery point comprised two distinct supplies. The Tribunal found that the two are different and distinct services. The Court of Appeal held that the supply of the service of delivery was physically and economically distinct from the supply of the car. On appeal, the House of Lords held:

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"In order to identify the supply it was necessary to consider whether the delivery was ancillary or incidental to the supply of the car or was a distinct supply. The fact that separate charges were identified in a contract or on an invoice did not on a consideration of all the circumstances necessarily prevent the various supplies from constituting one composite transaction nor did it prevent one supply from being ancillary to another supply which for value added tax (VAT) purpose was the dominant supply. Although each supply in a

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A composite transaction might be an independent separate supply, the essential features of a transaction might show that one supply was ancillary to another and that it was the latter that for VAT purposes was to be treated as the supply. In the instant case it was artificial to split the various parts of the transaction into different supplies for VAT purposes. What British Telecommunications wanted was a delivered car; the delivery was incidental or ancillary to the supply of the car and it was only on or after delivery that property in the car passed. Accordingly, if the transaction was looked at as a matter of commercial reality, there was one contract for a delivered car and one supply for VAT purposes.”

C Having given our anxious consideration to the submissions made in regard to the composite contract of service of goods and the classification, above referred, we are of the view that they will not apply to the present case. Here the service of telephone connection cannot be artificially split into various categories - supply of instruments and accompaniment on the one hand and supply of telegraphic line/connection on the other, to name the former as ‘sale’ and the latter as ‘service’. The analogy of composite contract will apply where ‘sale’ and ‘service’ are to different independent objects.

E Inasmuch as we have found that the DoT is a ‘dealer’ as defined in Section 2(c) of the U.P. Act and it collects rentals for the supply of transfer of use of telephone connection, which is compendiously called ‘service’ and that the supply of telephone satisfies the requirements of a transfer of the right to use the goods within the meaning of ‘sale’ in Section 2(h); it also receives consideration, therefore, the requirements of charging Section 3 read with Section 3 F are satisfied. The judgments and orders under challenge in these appeals are, therefore, set aside.

F In *Union of India and Ors. v. Secretary, Revenue Department (CTII), Government of Andhra Pradesh and Ors.*, (1999) 113 STC 203, the High Court of Andhra Pradesh took the view that the rentals are not subject to sales tax within the meaning of provisions of the Andhra Pradesh General Sales Tax Act, 1957. This judgment and the judgment under appeal was followed by the High Court of Punjab & Haryana in *Union of India and Anr. v. State of Haryana and Anr.*, [2001] 123 STC 539 to hold that the rentals collected by the DoT cannot be equated with sale of goods or deemed sale of goods by way of transfer of the right to use goods within the meaning of the Haryana General Sales Tax Act, 1973. For the aforementioned reasons

H we overrule those judgments.

We must, however, consider the last submission that the impugned demands relate to not only rentals but also to various other charges and, therefore, for working out the correct demand, the cases have to go back to the assessing officer for raising fresh demand. We find considerable force in that submission. We set aside the demand in question and direct the DoT (the respondent) to file the 'Returns' within three months from today. The Assessing Authority shall make order of assessment and raise fresh demand in accordance with law. A  
B

The appeals are accordingly allowed with costs.

N.J.

Appeals allowed.