VERDICTUM.IN

2025 INSC 1154

REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO.3577 OF 2008

M/s. U.P. ASBESTOS LIMITED ... APPELLANT

VERSUS

STATE OF RAJASTHAN & OTHERS ... RESPONDENTS

WITH

CIVIL APPEAL NO.3578 OF 2008

M/s. EVEREST INDUSTRIES LIMITED ... APPELLANT

VERSUS

STATE OF RAJASTHAN & OTHERS ... RESPONDENTS

AND

CIVIL APPEAL NO.2692 OF 2013

M/s. U.P. ASBESTOS LIMITED ... APPELLANT

VERSUS

STATE OF RAJASTHAN & OTHERS ... RESPONDENTS

Signature Not Verified
Digitally signed by
BORRA LAKSHMI
Date: 2025.09.24
19:44:33 IST
Reason:

VERDICTUM.IN

J U D G M E N T

NAGARATHNA, J.

I N D E X

VERDICTUM.IN

Since these Civil Appeals involve common questions of facts and law, they have been heard and are disposed of by this common judgment.

2. The instant appeals have been preferred by the appellants-assessees against the following three separate orders of the High Court of Judicature for Rajasthan at Jaipur:

i) Order dated 02.08.2007 in D.B. Civil Writ Petition No.3580/2007;

ii) Order dated 23.08.2007 in D.B. Civil Writ Petition No.2222/2007; and

iii) Order dated 05.09.2012 in D.B. Civil Writ Petition No.4447/2011.

2.1 All the three Writ Petitions were dismissed on the basis of reasons given in judgment and order dated 02.08.2007 in ***D.B. Civil Writ Petition No.3506/2007*** titled ***M/s. Hyderabad Industries Ltd. vs. State of Rajasthan and Ors. ("Hyderabad Industries")*** passed by the High Court of Judicature for Rajasthan. Aggrieved by the orders of dismissal, the appellants are before this Court.

VERDICTUM.IN

Bird's Eye View of the Controversy:

3. Briefly stated, the issue for determination in these appeals concern the validity of the impugned Notification No. S.O.377, dated 09.03.2007, issued by the Government of Rajasthan in exercise of its powers conferred by Section 8(3) of the Rajasthan Value Added Tax Act, 2003 ("2003 Act", for short). Specifically, the issue concerns whether Notification No.S.O.377 dated 09.03.2007 issued by Respondent State granting exemption from payment of Value Added Tax on sale of asbestos cement sheets and bricks, manufactured in the State of Rajasthan, having contents of fly ash 25% or more by weight subject to specific conditions, is violative of Article 304(a) of the Constitution of India being discriminatory *vis-à-vis* goods imported from outside the State of Rajasthan.

3.1 The notification, in effect, exempted from tax the manufacturers within the State of Rajasthan of asbestos cement sheets and bricks having content of fly ash 25% or more. Specifically, the challenge concerned sub-clauses (ii) and (iii) of the above notification, on the ground, *inter alia,* that they violate free movement of trade and commerce as envisaged in Articles 301 to 304 of the Constitution of India.

VERDICTUM.IN

3.2 For immediate reference, the notification dated 09.03.2007 is extracted below:

"FINANCE DEPARTMENT
(TAX DIVISION)

NOTIFICATION
JAIPUR, MARCH 9, 2007

S.O.377 – In exercise of the powers conferred by sub-section (3) of section 8 of the Rajasthan Value Added Tax Act, 2003 (Rajasthan Act No.4 of 2003), the **State Government being of the opinion that it is expedient in the public interest so to do**, hereby exempts from payment of tax the sale of asbestos cement sheets and bricks manufactured in the State having contents of fly ash twenty five percent or more by weight, on the following conditions, namely:-

(i) that the goods shall be entered in the registration certificate of the selling dealer.

(ii) that the exemption shall be for such goods manufactured by the dealer **who commenced commercial production in the State** by 31.12.2006; and

(iii) that the exemption shall be available up to 23.01.2010.

No.F.12 (28) FD/Tax/2007/141)
By Order of the Governor

(Arun Gupta)
Deputy Secretary to Government"

(emphasis supplied by us)

VERDICTUM.IN

3.3 In the course of the determination, this Court is also required to examine the applicability of the judgment of this Court in ***Video Electronics Pvt. Ltd. vs. State of Punjab, (1989) Supp. 2 SCR 731 ("Video Electronics")*** to the facts of this case, especially in light of the nine-Judge Constitution Bench judgment of this Court in ***Jindal Stainless Ltd. vs. State of Haryana, (2017) 12 SCC 1 ("Jindal Stainless Ltd.").***

Factual Background:

4. The facts emanating from all the three appeals are similar. The appellants herein are engaged in the business of manufacture and sale of fly ash based asbestos cement products. They do not have their manufacturing units in the State of Rajasthan, but have their sales depots in the State. These sales depots are duly registered with the Commercial Tax Department under Central and local State Tax Acts.

4.1 Initially, the State of Rajasthan issued a notification dated 24.01.2000 under the erstwhile Section 15 of the Rajasthan Sales Tax Act, 1994 (hereinafter "1994 Act") in the form of exemption from sales tax, to encourage industries of asbestos cement sheets

VERDICTUM.IN

and bricks manufactured in the State by an industrial unit having fly ash as its main raw material on certain conditions mentioned therein. The benefit was given to industries starting commercial production upto 31.12.2001 and the notification was to remain in force upto 23.01.2010.

4.2 In supersession of the above notification dated 24.01.2000, another notification dated 16.03.2005 was issued to exempt from tax the sale of asbestos cement sheets and bricks manufactured in the State by an industrial unit having fly ash as its main raw material on the condition that such fly ash shall constitute 25% or more in content by weight of such asbestos cement sheets or bricks. The benefit was given to industries starting commercial production by 31.12.2006 and the notification was to remain in force upto 23.01.2010. Admittedly, the above notifications dated 24.01.2000 and 16.03.2005 were never challenged by the appellants herein before any forum.

4.3 From 01.04.2006, the Rajasthan Value Added Tax Act, 2003 (hereinafter "VAT Act") came into operation on repeal of the 1994 Act. In order to continue the operation of the above-mentioned

VERDICTUM.IN

notifications issued under the 1994 Act, the State issued notifications dated 01.06.2006 and 05.07.2006 under Section 8 of the VAT Act which are *in pari materia* to Section 15 of the 1994 Act.

4.4 The above notifications dated 01.06.2006 and 05.07.2006 were challenged by one of the appellants herein before the Rajasthan High Court in W.P.No.7149 of 2006. While the matter was pending, the State Government withdrew the notification dated 05.07.2006 and issued the impugned notification dated 09.03.2007. It is relevant to note that, under this notification also, the benefit was given to industries starting commercial production by 31.12.2006 and the notification was to remain in force upto 23.01.2010. This notification was challenged before the Rajasthan High Court in D.B. Civil Writ Petition Nos.3580/2007 and 2222/2007 and the impugned judgments were passed on 02.08.2007 and 23.08.2007 respectively.

4.5 While the present appeals were pending before this Court, the State by way of notification dated 28.12.2010 amended clause (iii) of the impugned notification dated 09.03.2007 as follows:

VERDICTUM.IN

> "(iii) that maximum exemption benefits shall be available for 10 years from the date of commencement of first commercial production, but in no case exemption shall be available after 23.1.2016."

4.6 One of the appellants herein, namely M/s. U.P. Asbestos Ltd., filed a writ petition being D.B. Civil Writ Petition No.4447/2011 challenging the notification dated 28.10.2010. The said writ petition was also dismissed by way of impugned order dated 05.09.2012.

4.7 As the High Court dismissed all the three writ petitions by the impugned orders based on the judgment of that Court in ***Hyderabad Industries,*** it is necessary to dilate the reasoning provided therein.

4.8 The High Court in ***Hyderabad Industries*** first discussed the judgments of this Court in ***Firm A.T.B. Mehtab Majid and Co. vs. State of Madras, (1963) Supp. 2 SCR 435 ("Firm Mehtab Majid"); Shree Mahavir Oil Mills vs. State of J&K, (1996) Supp.9 SCR 356 ("Shree Mahavir Oil Mills"); State of U.P. vs. M/s Laxmi Paper Mart, (1997) 1 SCR 914 ("Laxmi Paper Mart");***

VERDICTUM.IN

Loharn Steel Industries Ltd. vs. State of Andhra Pradesh, (1996) Supp. 10 SCR 898 ("Loharn Steel Industries Ltd."); Video Electronics and ***Shree Digvijay Cement Co. Ltd. vs. State of Rajasthan, (1999) Supp. 5 SCR 428 ("Digvijay Cements").***

4.9 Based on a reading of the above judgments, the High Court opined that the decision on the question whether, there has been discrimination between the imported and the local goods depends on diverse factors. That where there is no intentional discrimination but the concession from sales tax is given in respect of goods manufactured in a particular State which is not so developed, in furtherance of economic development and where such concession is granted to new industries for a specific time which came into existence for a specific period, such concession or exemption may not offend Part XIII of the Constitution of India.

4.10 The High Court also observed that there was no challenge either to the constitutional validity of Section 8 of the VAT Act or to the notifications dated 24.01.2000 and 16.03.2005 which were on identical terms to the impugned notification. That there is no dispute that fly ash coming out of thermal power plants is

VERDICTUM.IN

abundantly available in the State of Rajasthan and is not unreasonable to presume that the State Government gave incentives for asbestos manufacturing plants within the State of Rajasthan to promote the use of fly ash as raw material for the production of asbestos cement sheets and bricks.

4.11 The High Court further noted that it was for the above reason that way back in the year 2000, the State Government passed the notification dated 24.01.2000 and that the benefit was extended from time to time. It accepted the stand of the State that it was bound even otherwise by the principle of promissory estoppel to continue with the exemption since in the notification dated 24.01.2000 itself, the benefit was to continue until 23.01.2010.

4.12 The High Court acknowledged that this Court in ***Shree Mahavir Oil Mills*** distinguished ***Video Electronics***. However, the High Court noted that ***Shree Mahavir Oil Mills*** justified the decision in ***Video Electronics*** to grant exemption to a special class for a limited period on specific conditions when there are justifiable and national reasons for differentiation.

VERDICTUM.IN

4.13 Hence, the High Court held that the impugned notification, in the backdrop of earlier notifications dated 24.01.2000 and 16.03.2005, fell within the exceptional category covered in ***Video Electronics*** and hence cannot be held to be offending Article 304(a) of the Constitution of India. Therefore, the question would also arise as to whether the Rajasthan High Court decided ***Hyderabad Industries*** correctly.

Submissions:

5. Learned senior counsel Sri Nikhil Goel appearing for the appellant M/s U.P. Asbestos Ltd. and Smt. Kavita Jha appearing for appellant M/s. Everest Industries Ltd., strenuously argued that the impugned notification was unconstitutional and violated Article 304(a) of the Constitution of India. To substantiate, the following submissions were put forth:

5.1 That the impugned notification is discriminatory in nature and falls foul of Article 304(a) of the Constitution of India as it did not provide for any reason for the blanket exemption from payment of tax provided to locally manufactured goods in the State of Rajasthan as compared to goods imported from outside the State.

VERDICTUM.IN

In this regard, they relied on ***Shree Mahavir Oil Mills, Laxmi Paper Mart***, and ***Anand Commercial Agencies vs. Commercial Tax Officer VI Circle, Hyderabad, (1998) 1 SCC 101***.

5.2 Referring to the text of the impugned notification, it was contended that it does not require the industries within the State to only manufacture or procure fly ash from within the State. That the lack of such a requirement *ex-facie* falsifies the justification of the State that the exemption provided for in the impugned notification was to encourage industries to utilise the excess fly ash from the State. They further contended that *arguendo*, even if the impugned notification required the fly ash to be purchased within the State of Rajasthan, the notification would still have to be quashed in light of the judgment of this Court in ***State of U.P. vs. Jaiprakash Associates Ltd., (2014) 4 SCC 720 ("Jaiprakash Associates").***

5.3 Reliance was placed on the observations of the nine-Judge bench judgment in ***Jindal Stainless Ltd.*** to contend that the differentiation made through the impugned notification was intended or inspired by an element of unfavourable bias in favour

VERDICTUM.IN

of the goods produced or manufactured in the State of Rajasthan as against those imposed from outside. They submitted that, in ***Jindal Stainless Ltd.***, this Court held that every differentiation is discrimination if it involved an element of "intentional and unfavourable bias". Learned senior counsel Ms. Kavita Jha also provided us a summary of the relevant observations in ***Jindal Stainless Ltd.*** which we shall discuss later in this judgment.

5.4 That the High Court was not right in relying on ***Video Electronics*** as the facts of that case are distinguishable. They highlighted that in ***Video Electronics,*** this Court upheld the notifications impugned therein on the ground that they related to a specific class of industrial units and that the benefit under the same was admissible only for a limited period of time. However, in the present case, the restriction was not limited to a specific class or period, but such exemption has been extended from time to time from the year 2000 till the year 2016, to all the old and new dealers of asbestos sheets, without assigning any reason. Hence, the finding in paragraph 17 of the judgment in ***Hyderabad Industries*** that the exemption was only to a limited class, i.e. those who commenced production by 31.12.2006 and was only for a limited

VERDICTUM.IN

period, i.e. till 23.01.2010 was not accurate. Rather, they contended that the facts of the present case are akin to that in ***Shree Mahavir Oil Mills*** and ***Jaiprakash Associates.***

5.5 Learned senior counsel also sought to repel the objection that the appellants herein had not challenged the earlier notifications by relying on the dictum in ***Shree Mahavir Oil Mills*** that there can be no estoppel or acquiescence in a matter relating to constitutional rights of citizens.

5.6 Referring to the submission of the State in its reply before the High Court, they contended that the only justification put forth by them was that it was empowered to grant exemption to a class of industries to boost industrialisation within its State. The learned senior counsel questioned this rationale by submitting that if the same was accepted as a general proposition justifying discrimination between two States while applying a tax regime, such proposition would practically nullify the entire Chapter XIII of the Constitution. That every State would then exempt local manufacturers from tax simply by saying that it wants to boost industrial growth. They submitted that Article 301 of the

VERDICTUM.IN

Constitution cannot be stretched to its unnatural limits to justify such a vague rationale.

6. In response to the above submissions, learned senior counsel Dr. Manish Singhvi made the following submissions:

6.1 Highlighting the implications of the Constitution Bench judgment in ***Jindal Stainless Ltd.,*** it was contended that the plenary power to tax under Articles 245 and 246 of the Constitution read in conjunction with the Entries in the Seventh Schedule to the Constitution is *per se* not subject to Article 301 of the Constitution. That the plenary power is restrained only if it discriminates in terms of Article 304(a) of the Constitution.

6.2 That, in ***Jindal Stainless Ltd.***, this Court upheld the ratio laid down in ***Video Electronics***. He highlighted that, so long as the differentiation made by the States is not intended to create an unfavourable bias and so long as the differentiation is intended to benefit a distinct class of industries and the life of the benefit is limited in terms of period, the benefit must be held to flow from a legitimate desire to promote industries within its territories. That this Court also distinguished ***Shree Mahavir Oil Mills*** by noting

VERDICTUM.IN

that if the incentive/exemption in taxation to spur industrialisation was for a limited period and for achieving some objective, then it shall not be violative of Article 304(a) of the Constitution.

6.3 Our attention was drawn to the observations of this Court in ***Digvijay Cements*** wherein this Court stated that all States have powers to grant exemption to specified class of goods for a limited period and that such grant of exemption cannot be held to be contrary to the concept of economic unity. It was submitted that the power to grant exemptions is thus a dynamic concept and they must be viewed at keeping in mind the overall objectives sought to be achieved.

6.4 Learned senior counsel for the State of Rajasthan submitted that, after the judgment in ***Jindal Stainless Ltd.,*** it is not clear if the ratio in ***Jaiprakash Associates*** still holds field. He referred to paragraph 32 of the judgment in ***Jaiprakash Associates*** to contend that it relied on the judgment rendered in ***Atiabari Tea Co. Ltd. vs. State of Assam, AIR 1961 SC 232 ("Atiabari Tea Co. Ltd.")***, which was partly overruled in ***Jindal Stainless Ltd.***

VERDICTUM.IN

6.5 Dealing with the facts of the case, learned senior counsel submitted that prior to the notification dated 24.01.2000, there was no asbestos sheet plant/industry in the State of Rajasthan. That fly ash is an abundant raw material available in the State and the intention of the exemption from sales tax was to promote the use of fly ash coming out of thermal power plants as a raw material for the production of asbestos cement sheets and bricks for which there was no manufacturing plant in the State. He also submitted that various notifications issued by the Ministry of Environment and Forests required the compulsory use of fly ash and hence the exemption as provided in the impugned notification was envisaged. That additionally, having contents of fly ash twenty five percent or more in asbestos sheets by weight also improves the environment which was another laudable objective.

6.6 Learned senior counsel also submitted that if such an exemption was not granted, then no asbestos sheet industry would have come to the State of Rajasthan and the fly ash in the State would go unutilised/unused, considering huge transportation costs associated with transporting fly ash. That the economics of transportation itself would repel any argument that the

VERDICTUM.IN

notifications did not specifically require the manufacturers to utilise the fly ash generated in the State. He also submitted that, it was not the case of the appellants herein that they would use the fly ash manufactured in the State of Rajasthan, despite having manufacturing units elsewhere.

6.7 For the above reasons, Dr. Manish Singhvi emphasised that the exemption provided for in the notification qualifies as 'differentiation', rather than discrimination and is saved as per Article 304(a) of the Constitution.

6.8 To our query that the reasons for the notification could not be found in the notification itself, learned senior counsel submitted that the reasons for the notification can be discerned from the records available and the counter affidavit filed before the High Court. He therefore drew our attention to the relevant portions in the counter-affidavit filed by the State before the High Court where the reasons mentioned above were elucidated. He submitted that there is presumption of constitutionality of any law enacted by a State and that the State, though could have provided the reasons for such an enactment in the notification itself, was not incumbent

VERDICTUM.IN

to so spell out and the same could always be gathered by surrounding circumstances.

6.9 In response to the submissions of learned senior counsel Dr. Manish Singhvi, learned senior counsel Ms. Kavita Jha added that the object behind the impugned notification, as stated by the learned senior counsel in his submissions, was not provided/ expressed in the impugned notification. That from its bare perusal, no object, purpose or rationale was mentioned to provide impetus to any industry but on the other hand to discriminate among indigenous goods and imported goods.

7. Learned senior counsel for the appellants relied on the judgment of this Court in ***Mohinder Singh Gill vs. Chief Election Commissioner, (1978) 1 SCC 405 ("Mohinder Singh Gill")*** to substantiate that any order passed by any public authority exercising administrative/executive or statutory powers must be judged by the reasons so mentioned in that order and cannot be supplemented by fresh reasons in the shape of an affidavit or otherwise.

VERDICTUM.IN

Points for Consideration:

8. The following points would arise for our consideration:

(i) Whether the High Court was right in dismissing the writ petitions filed by the appellants herein by holding that the impugned notification dated 09.03.2007 did not violate Article 301(a) of the Constitution of India?

(ii) If the answer to point No.(i) is in the negative, then, what order?

Relevant Constitutional Provisions:

9. Articles 301 to 304, which are under Part XIII of the Constitution are relevant for our discussion and are extracted as under:

> **"301. Freedom of trade, commerce and intercourse.-** Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.
>
> **302. Power of Parliament to impose restrictions on trade, commerce and intercourse**.—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.
>
> **303. Restrictions on the legislative powers of the Union and of the States with regard to trade and commerce**.—(1) Notwithstanding anything in article 302,

VERDICTUM.IN

neither Parliament nor the Legislature of a State shall have power to make any 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, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

(2) Nothing in clause (1) shall prevent Parliament from making any law giving, or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India.

304. Restrictions on trade, commerce and intercourse among States. - 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 Legislature of a State without the previous sanction of the President."

10. The significant judgments of this Court on the interpretation of Articles 301 to 304 could be discussed at this stage.

VERDICTUM.IN

Atiabari Tea Co. Ltd.:

10.1 In ***Atiabari Tea Co. Ltd.,*** the constitutionality of the Assam Taxation (on Goods Carried by Roads or Inland Waterways) Act (Assam Act) 13 of 1954 was questioned in a petition filed under Article 32 of the Constitution before this Court. The question that fell for determination in this case was, whether, the said Act infringed the provisions of Part XIII of the Constitution, with particular reference to Article 301. While analysing Part XIII of the Constitution, it was observed that Article 301 was subject to other provisions of Part XIII and not subject to other provisions of the Constitution and the generality of the words used in Article 301 is cut down only by the provisions of the other Articles of Part XIII ending with Article 307. Article 301 emphatically declares that trade, commerce and intercourse throughout the territory of India is free, but there is wide divergence of views on the answer to the question "free from what". It was observed that having regard to the divergence and nature of States in pre-Constitution India, it was necessary for the abolition of all those trade barriers and tariff walls so that the entire country was knit into one political unit in

VERDICTUM.IN

the interest of national solidarity, economic and cultural unity as also of freedom of trade, commerce and intercourse.

10.1.1 Adverting to Article 304, it was observed that the said Article would show that it is divided into two parts, namely, (i) dealing with imposition of non-discriminatory taxes by a State Legislature; and (ii) relating to imposition of reasonable restrictions, thus showing that imposition of taxes is a class apart from imposition of reasonable restrictions on freedom of trade, commerce and intercourse.

10.1.2 It was further observed that if a law is passed by the Legislature imposing a tax which in its true nature and effect is meant to impose an impediment to the free flow of trade, commerce and intercourse, for example, by imposing a high tariff wall, or by preventing imports into or exports out of a State, such a law is outside the significance of taxation, as such, but assumes the character of a trade barrier which it was the intention of the Constitution-makers to abolish by Part XIII, but taxation on movement of goods and passengers is not necessarily an impediment. Article 304, while recognising the power of a State Legislature to tax goods imported inter-State, insists that a similar

VERDICTUM.IN

tax is imposed on goods manufactured or produced within the State. The Article thus brings out the clear distinction between taxation as such for the purpose of revenue and taxation for purposes of making discrimination or giving preference.

10.1.3 It was observed by Sinha, C.J. that the Union and State Legislature have the power to legislate by way of taxation in respect of trade, commerce and intercourse, so as not to erect trade barriers, tariff walls or imposts, which have a deleterious effect on the free flow of trade, commerce and intercourse.

10.1.4 Consequently, he did not concur with the majority of the Court by observing that his reading of Part XIII of the Constitution did not justify the inference that taxation simpliciter is within the terms of Article 301 of the Constitution.

10.1.5 The majority judgment delivered by Gajendragadkar, J. (as he then was) referred to the constitutional background of Part XIII and observed that prior to 1950, the flow of trade and commerce was impeded at several points which constituted the boundaries of Indian States. The main object of Article 301 obviously was to allow the free flow of the stream of trade,

VERDICTUM.IN

commerce and intercourse throughout the territory of India. The reason being that economic unity was absolutely essential for the stability and progress of the federal policy which had been adopted by the Constitution for the governance of the country.

10.1.6 The majority then proceeded to consider whether tax laws are wholly outside the purview of Part XIII. In this regard, Cooley's *Constitutional Limitations* on the power of taxation was referred to observe that "*the power to impose taxes is one so unlimited in force and so searching in extent, that the courts scarcely venture to declare that it is subject to any restriction whatever, except such as rest in the discretion of the authority which exercises it*". *(Cooley's Constitutional Limitation Vol. 2, 8th Edn., p.986).* It was observed that the power of levying tax is essential for the very existence of the government, its exercise must inevitably be controlled by the constitutional provisions made in that behalf. It cannot be said that the power of taxation *per se* is outside the purview of any constitutional limitations.

10.1.7 Referring to ***Ramjilal vs. Income Tax Officer, AIR 1951 SC 97,*** it was observed that protection against the imposition and collection of taxes, save by the authority of law, directly comes

VERDICTUM.IN

under Article 265 and cannot be said to be covered by clause (1) of Article 301. Therefore, levy of a tax *per se* cannot be a violation of Article 14 of the Constitution. It was also held that the power to levy tax would ultimately be based on Article 245 which deals with the extent of laws made by Parliament and by the Legislatures of States, as it begins with the words "Subject to the provisions of the Constitution". Therefore, the power of Parliament and the Legislatures of the States to make laws including laws imposing taxes is subject to the provisions of the Constitution and therefore, the application of Part XIII also. However, Article 301 which is in Part XIII is not subject to the other provisions of the Constitution but is made subject only to other provisions of only Part XIII. Therefore, once the width and amplitude of the freedom enshrined in Article 301 are determined, they cannot be controlled by any provision outside Part XIII. The freedom guaranteed under Article 301 is made subject to the exceptions provided by the other Articles in Part XIII and is not limited by any other provisions of the Constitution outside Part XIII. It was also observed that the legislative competence of the Legislature in question would have to be judged in light of the relevant Articles of Part XIII. Hence,

VERDICTUM.IN

it was observed that the argument that tax laws are outside Part XIII, cannot be accepted.

10.1.8 It was noted that the freedom of trade guaranteed by Article 301 is freedom from all restrictions except those which are provided by the other Articles in Part XIII. While examining the other Articles of Part XIII, it was stated that the effect of Article 304(a) is to treat imported goods on the same basis as goods manufactured or produced in any State; and it authorises tax to be levied on such imported goods in the same manner and to the same extent as may be levied on goods manufactured or produced inside the State. In other words, taxation can be levied by the State Legislature on goods manufactured or produced within its territory and it provides that outside goods cannot be treated any worse. The *non-obstante* clause referring to Article 301 would go with Article 304(a) and that tax on goods would not have been permissible but for Article 304(a) with the *non-obstante* clause. In other words, Article 304(a) is another exception to Article 301.

10.1.9 Analysing Article 304(a), it was observed that a tax could be levied by a State Legislature on goods manufactured or produced or imported in the State and thereby reasonable

VERDICTUM.IN

restrictions can be placed on the freedom of trade either with another State or between different areas of the same State. Tax legislation, thus authorised, must therefore be deemed to be included in Article 301, for that is the obvious inference from the use of the *non-obstante* clause.

10.1.10 It was concluded that while determining the limits of the width and amplitude of the freedom guaranteed by Article 301, a rational and workable test should apply and that only such restrictions as directly and immediately restrict or impede the free flow or movement of trade, are barred. Therefore, it cannot be held that all taxes should be governed by Article 301, whether or not their impact on trade is immediate or mediate, direct or remote. Thus, an extreme approach cannot be upheld. Therefore, Article 301 envisages that the flow of trade shall run smooth and unhampered by any restriction either at the boundaries of the States or at any other points inside the States themselves.

10.1.11 Consequently, it was held that the Assam Act had imposed a direct restriction on the freedom of trade and since it had not complied with the provision of Article 304(b), it was declared to be void.

VERDICTUM.IN

10.1.12 In the said case, Shah, J. in his opinion observed that the power of taxation is essentially an attribute of the sovereignty of the State and is not exercised in consideration of the protection it affords or the benefit that it confers upon citizens and aliens. Its content is not measured by the apparent need of the amounts sought to be collected and its incidence does not depend upon the ability of the citizens to meet the demand. But it is still not an unrestricted power. By Article 265 of the Constitution, the power to tax can be exercised by authority of law alone. The power of taxation has therefore to be exercised by the Legislature strictly within the limits prescribed by the Constitution and any alleged transgression either by Parliament or the State Legislature of the limits imposed by the Constitution is justiciable.

10.1.13 Discussing on the guarantee of freedom of trade and commerce, it was observed by Shah, J. that the guarantee is not addressed merely against prohibitions, complete or partial; it is addressed to tariffs, licensing, marketing regulations, price-control, nationalisation, economic or social planning, discriminatory tariffs, compulsory appropriation of goods, freezing or stand still orders and similar other impediments operating

VERDICTUM.IN

directly and immediately on the freedom of commercial intercourse as well. It was clarified that what is guaranteed is freedom in its widest amplitude — freedom from prohibition, control, burden or impediment in commercial intercourse. Not merely discriminative tariffs restricting movement of goods are included in the restrictions which are hit by Article 301, but all taxation on commercial intercourse even imposed as a measure for collection of revenue is so hit.

10.1.14 It was also stated that between discriminatory tariffs and trade barriers on the one hand and taxation for raising revenue on commercial intercourse, the difference is one of purpose and not of quality. Both these forms of burden on commercial intercourse trench upon the freedom guaranteed by Article 301.

10.1.15 While interpreting Article 304(a), it was observed that the State Legislature has the power to impose tax on the imports of goods to which similar goods manufactured or produced in the State are subject, provided that by taxing the goods imported from another State or Union Territory, no discrimination is practised. Consequently, Shah, J. held that the Assam Act was infringing the guarantee of freedom of trade and commerce under Article 301.

VERDICTUM.IN

10.1.16 However, in view of the majority opinion, the writ petitions were allowed.

Automobile Transport Ltd.:

10.2 A seven-Judge Bench of this Court in ***Automobile (Rajasthan) Transport Ltd. vs. State of Rajasthan, AIR 1962 SC 1406 ("Automobile Transport Ltd.")*** heard the appeals having regard to the importance of the constitutional issues involved and the views expressed in ***Atiabari Tea Co. Ltd.*** while considering the validity of Rajasthan Motor Vehicles Taxation Act, 1951. The contours of the freedom envisaged under Article 301 was considered inasmuch as the question, whether, regulatory measures or compensatory taxes were restrictions on the freedom of trade came up for consideration and more particularly, the State law imposing tax on motor vehicles carrying passengers and goods within or throughout the State. The majority view was expressed through S.K. Das, J. (as he then was) who observed that the taxes imposed under the Rajasthan Motor Vehicles Taxation Act, 1951 are compensatory taxes which did not hinder the freedom of trade, commerce and intercourse assured by Article 301 and hence, the Act did not violate the provisions of that Article. This was because

VERDICTUM.IN

regulatory measures imposing taxation for use of trading facilities do not come within the purview of the restrictions contemplated under Article 301 and such measures need not comply with the requirements of the proviso to Article 304(b) of the Constitution.

10.2.1 While analysing the issues raised in the said case, it was observed that those which facilitate trade and commerce are not a restriction, and those which in reality hampers or burdens trade and commerce are a restriction. That, it is the substance of the matter that has to be considered and it is not possible *a priori* to draw a dividing line between that which would really be a charge for a facility provided and that which would really be a deterrent to a trade; but the distinction is real and clear. For the tax to become a prohibited tax, it has to be a direct tax, the effect of which is to hinder the movement part of trade. So long as a tax remains compensatory or regulatory, it cannot operate as a hindrance. A working test for deciding whether a tax is compensatory or not is to enquire whether the trades people are having the use of certain facilities for the better conduct of their business and paying not patently much more than what is required for providing the facilities. It would be impossible to judge the compensatory nature

VERDICTUM.IN

of a tax by a meticulous test, and in the nature of things that cannot be done. If a statute fixes a charge for a convenience or service provided by the State or an agency of the State and imposes it upon those who choose to avail themselves of the service or convenience, the freedom of trade and commerce may well be considered unimpaired. In such a case, the imposition assumes the character of remuneration or consideration charged in respect of an advantage sought and received.

10.2.2 The minority, speaking through Hidayatullah, J. (as he then was) observed that a law which prohibits trade, commerce and intercourse and releases them on the fulfilment of some unreasonable condition including the payment of an unreasonable or discriminatory tax will just as much be a restriction offending the freedom as a tariff wall or any other barrier. No question of pith and substance in this context arises. Therefore, taxation laws directly impinging on trade and commerce cannot be upheld on the ground that they are regulatory. A tax which is made the condition precedent of the right to enter upon and carry on business is a restriction on the right to carry on trade and commerce and the restriction is released on the payment of the tax, which is the price

VERDICTUM.IN

of such release. A regulation of trade and commerce, on the other hand, may achieve some public purpose which affects trade and commerce incidentally but without impairing the freedom. It was observed that the tax is evidently not a fee for administrative purposes. Therefore, it cannot be justified as representing payment of services. Its object is the raising of revenue. Therefore, such a tax is neither a compensatory tax nor a regulatory Act. It was further held that the said tax offended Article 301 of the Constitution and since resort to the procedure prescribed by Article 304(b) was not taken, it was *ultra vires* the Constitution.

Firm Mehtab Majid:

10.3 The validity of Rule 16 of the Madras General Sales Tax (Turnover and Assessment) Rules, 1939, (hereinafter, called "the Madras Rules") was impugned in ***Firm Mehtab Majid***. The Constitution Bench of this Court, speaking through Raghubar Dayal, J. noted the contention of the petitioner therein to the effect that under the impugned rule, tanned hides or skins imported from outside the State and sold within the State were subject to a higher rate of tax than the tax imposed on hides or skins tanned and sold within the State, inasmuch as sales tax on the imported hides or

VERDICTUM.IN

skins tanned outside the State is on their sale price while the tax on hides or skins tanned within the State, though ostensibly on their sale price, was, in view of the proviso to clause (ii) of sub-rule (2) of rule 16, really on the sale price of these hides or skins when they were purchased in the raw condition and which was substantially less than the sale price of tanned hides or skins. Further, for similar reasons, hides or skins imported from outside the State after purchase in their raw condition and then tanned inside the State were also subject to higher taxation than hides or skins purchased in the raw condition in the State and tanned within the State, as the tax on the former was on the sale price of the tanned hides or skins and, on the latter, was on the sale price of the raw hides or skins. Such a discriminatory taxation was said to offend Article 304(a) of the Constitution.

10.3.1 Taking note of the earlier decision in ***Atiabari Tea Co. Ltd.,*** it was observed that in the majority judgment in ***Automobile Transport Ltd.***, the interpretation of the majority in ***Atiabari Tea Co. Ltd.*** was held to be correct but subject to a clarification. That, regulatory measures or measures imposing compensatory taxes for the use of trading facilities do not come within the purview of

VERDICTUM.IN

restrictions contemplated by Article 301. That, such regulatory measures which do not impede the freedom of trade, commerce and intercourse and compensatory taxes for the use of trading facilities are not hit by the freedom declared by Article 301. They are excluded from the purview of the provisions of Part XIII of the Constitution for the simple reason that they do not hamper trade, commerce and intercourse but rather facilitate them. Subba Rao, J, had also concurred with this view in ***Automobile Transport Ltd.***

10.3.2 It was observed that taxing laws can be restrictions on trade, commerce and intercourse, if they hamper the flow of trade and if they are not what can be termed to be compensatory taxes or regulatory measures. On the other hand, sales tax, which has the effect of discriminating between goods of one State and goods of another, may affect the free flow of trade which offends against Article 301 and will be valid only if it comes within the terms of Article 304(a). That Article 304(a) enables the Legislature of a State to make laws affecting trade, commerce and intercourse by imposition of taxes on goods from other States if similar goods in the State are also subjected to similar taxes, so as not to

VERDICTUM.IN

discriminate between the goods manufactured or produced in that State and the goods which are imported from other States.

10.3.3 Applying the said principles to the said case, it was held that the effect of the sales tax on tanned hides or skins imported from outside was that the latter becomes subject to a higher tax by the application of the proviso to sub-rule (2) of rule 16 of the Rules, and was discriminatory and unconstitutional and was hence, struck down.

10.3.4 On the aspect of whether the rule discriminated between hides or skins imported from outside the State and those manufactured or produced in the State, this Court examined the grievance ventilated on the amount of tax levied being different on account of the existence of a substantial disparity in the price of the raw hides or skins and of those hides or skins after they had been tanned, though the rate was the same. It was explained that if the dealer has purchased the raw hide or skin in the State, he would have had to pay on the purchase price only. But if the dealer purchased raw hides or skins from outside the State and tanned them within the State, he would be liable to pay sales tax on the sale price of the tanned hides or skins. He too would have had to

VERDICTUM.IN

pay more tax even though the hides and skins were tanned within the State, merely on account of his having imported the hides and skins from outside and having not therefore paid any tax under sub-rule (1). Thus, there was discriminatory nature of tax imposed. As a result, Rule 16(2) was held to discriminate against the imported hides or skins which had been purchased or tanned outside the State and therefore it contravened the provisions of Article 304(a) of the Constitution. Hence, the petition was allowed and the State was directed to refund of tax illegally collected from the petitioner.

Kalyani Stores:

10.4 In ***Kalyani Stores vs. State of Orissa, AIR 1966 SC 1686, ("Kalyani Stores")*** the notifications issued under Section 27 of the Bihar and Orissa Excise Act, 1915, imposing countervailing duty on foreign liquor imported into the State and later enhancing the duty by another notification, were assailed. The contention of the appellant therein was that the State could levy under Section 27 of the said Act duty on excisable articles produced or manufactured in the State and a countervailing duty on excisable articles imported into the State, imposed with a view to equalize the burden

VERDICTUM.IN

on the imported articles with the burden on manufactured articles in the State, but no countervailing duty on liquor imported could be levied if there was in the year of licence no liquor similar to the imported liquor manufactured within the State and as there was no distillery in the State manufacturing "foreign liquor", the levy of countervailing duty was without authority of law.

10.4.1 It was observed that exercise of power under Article 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 that there is no discrimination against imported goods. As no foreign liquor was produced or manufactured in the State of Orissa, the power to legislate provided under Article 304 was not available and the restriction which is declared on the freedom of trade, commerce or intercourse by Article 301 of the Constitution remained unfettered. Hence, the appeal was partially allowed by this Court by declaring that the notification enhancing duty on foreign liquor was invalid as offending Article 304 of the Constitution and therefore unenforceable. However, the right of the State to enforce the liability against the appellants to pay duty at the rate prescribed in

VERDICTUM.IN

the earlier notification which held the field, remained however unaffected.

10.4.2 Hidayatullah, J. (as he then was) however observed that Article 304(a) was not applicable to the case. That, in the matter of excise duties, the State Legislature has competence even apart from Article 304(a) because the power to impose duties of excise on alcoholic liquors for human consumption produced in the State and countervailing duties on similar liquors produced outside the State in India was already conferred by the legislative list. Therefore, it was held that the notification issued in the year 1961 under Section 27 was valid and the new notification did not run against any constitutional provision. Therefore, he dismissed the appeal. However, the majority partially allowed the appeal.

Weston Electronics:

10.5 The case in ***Weston Electronics vs. State of Gujarat, (1988) 2 SCC 568 ("Weston Electronics")*** concerned manufacturers of electronic goods, including television sets, television cameras and television monitors at factories located at Delhi and the goods sold through sales organisations spread all

VERDICTUM.IN

over India, including the State of Gujarat. The petitioners therein filed a writ petition before this Court questioning the Notification dated 29.03.1986 under which the rate of sales tax in respect of television sets imported from outside the State was reduced from 15 per cent to 10 per cent, and for goods manufactured within the State the sales tax was reduced to 1 per cent. It was contended that there was an invidious discrimination which adversely affected the free flow of inter-State trade and commerce, resulting in a contravention of Article 301 of the Constitution. It was contended that the sale of electronic goods manufactured by the petitioner has been prejudicially affected within the State of Gujarat. Based on the rulings of this Court in ***Firm Mehtab Majid*** as well as in ***H. Anraj vs. Government of Tamil Nadu, (1986) 1 SCC 414 ("H. Anraj")*** - wherein this Court struck down the levy of tax imposed by the State of Tamil Nadu on lottery tickets issued by other States and sold within the State of Tamil Nadu while exempting from such levy lottery tickets issued by the Government of Tamil Nadu - the writ petition was allowed and Notifications dated 23.07.1981 and 29.03.1986 prescribing a lower rate of tax for local manufacturers

VERDICTUM.IN

in respect of television sets and other electronic goods were quashed.

Video Electronics:

10.6 A three-Judge Bench of this Court decided a batch of writ petitions filed under Article 32 of the Constitution of India in ***Video Electronics***. The focus of the said case was on the question of harmonising the power of different States in the Union of India to legislate and/or give appropriate directions within the parameters of the subjects in List II of the Seventh Schedule of the Constitution with the principle of economic unity envisaged in Part XIII of the Constitution of India. The provision of exemption/ encouragement/incentives given by different States to boost or help economic growth and development in those States and in so doing the attempt of the States to give preferential treatment to the goods manufactured or produced in those States was also considered.

10.6.1 In one of the writ petitions, the challenge was to the constitutional validity of Notification dated 26.12.1985 issued by the State of Uttar Pradesh under the Uttar Pradesh Sales Tax Act, 1948 as well as subsequent notifications thereunder. The

VERDICTUM.IN

petitioners therein stated that they carried on business of selling cinematographic films and other equipment in the State of Uttar Pradesh and in Delhi. They were dealers on behalf of the manufacturers from outside the said State. In Uttar Pradesh, there was a single point levy of sales tax. Their contention was that the Notification dated 26.12.1985 discriminated between the manufacturers covered by the said Notification who were entitled to sell the articles manufactured by them without liability to pay sales tax and the manufacturers in other States and non-manufacturers of the same article selling the same goods in the State who were liable to pay sales tax under the local Sales Tax Act. They contended that they were subjected to gross discrimination and their business was crippled on account of the said fact and therefore, they challenged the *vires* of the said notification under Articles 14 and 19(1)(g) of the Constitution. However, this Court opined that the main question was, whether, the said notifications were valid in light of Part XIII of the Constitution.

10.6.2 This Court speaking through Sabyasachi Mukharji, J. (as he then was) made a detailed discussion of the judgment rendered in ***Atiabari Tea Co. Ltd.*** and also the decision of this

VERDICTUM.IN

Court in ***Automobile Transport Ltd.*** This was also in the context of whether regulatory measures or measures imposing compensatory taxes for using trading facilities did not come within the purview of restrictions contemplated under Article 301.

10.6.3 Reference was made to the case of ***A. Hajee Abdul Shakoor & Co. vs. State of Madras, AIR 1964 SC 1729*** and to the observations of this Court in ***State of Madras vs. N.K. Nataraja, AIR 1969 SC 147*** as well as in ***Andhra Sugars Ltd. vs. State of Andhra Pradesh, AIR 1968 SC 599***, wherein it was reiterated that a sales tax which discriminates against goods imported from other States may impede the free flow of trade and is invalid unless protected by Article 304(a) of the Constitution.

10.6.4 It was observed that Part XIII of the Constitution cannot be read in isolation. That it is part and parcel of a single constitutional instrument envisaging a federal scheme and containing a general scheme conferring legislative powers in respect of the matters relating to List II of the Seventh Schedule on the States. That the economic development of States to bring in the constitutional philosophy of equality between the States and thereby developing the economic unity of India is one of the goals

VERDICTUM.IN

or commitments of the constitutional aspirations. The economic equality of all the States is as much vital as economic unity. Thus, it held that the taxes which do not directly or immediately restrict or interfere with trade, commerce and intercourse throughout the territory of India, would therefore be excluded from the ambit of Article 301 of the Constitution. That sales tax has only an indirect effect on trade and commerce and does not directly impede the free movement of transport. On the aspect of the imposition of a rate of tax on goods, it was observed that the free flow of trade between two States does not necessarily or generally depend upon the rate of tax alone. Many factors including the cost of goods play an important role in the movement of goods from one State to another. Hence, the mere fact that there is a difference in the rate of tax on goods locally manufactured and those imported would not amount to hampering of trade between the two States within the meaning of Article 301 of the Constitution. That, since Article 304(a) and (b) is an exception to Article 301, resort to an exception will arise only if the tax impugned is hit by Articles 301 and 303 of the Constitution. If it is not, then Article 304 will not come into picture at all. Further, the imposition of a rate of sales tax is influenced

VERDICTUM.IN

by various political, economic and social factors. Prevalence of differential rate of tax on sales of the same commodity cannot be regarded in isolation as determinative of the object to discriminate between one State and another. This Court also recalled the observations in ***V. Guruviah Naidu & Sons vs. State of Tamil Nadu, AIR 1977 SC 548,*** wherein it was observed that Article 304(a) does not prevent levy of tax on goods; what it prohibits is such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. That any discrimination in that regard would constitute a tariff wall or fiscal barrier and would thus impede the free flow of inter-State trade and commerce.

10.6.5 This Court further noted that the question as to when the levy of tax would constitute discrimination would depend upon a variety of factors including the rate of tax and the item of goods in respect of the sale of which it is levied. The object is to prevent discrimination against the imported goods by imposing tax on such goods at a rate higher than that borne by local goods. It was observed that every differentiation is not discrimination. This was because the expression 'discrimination' in Article 304(a) involves

VERDICTUM.IN

an element of intentional and purposeful differentiation thereby creating economic barrier and involves an element of an unfavourable bias. That discrimination implies an unfair classification. When the general rate applicable to the goods locally made and on those imported from other States is the same, nothing more is to be shown by the State to dispel the argument of discrimination under Article 304(a), even though the resultant tax amount on imported goods may be different.

10.6.6 Further, the question, whether, the power to grant exemption to specified class of manufacturers for a limited period on certain conditions would be violative of Article 304(a) was considered. The contention was that the State should grant exemption to all goods irrespective of the fact that the goods are locally manufactured or imported from other States, else it would be violative of Article 304(a). The aforesaid argument was contested by the respondent therein by stating that if the exemptions are based on natural and business factors which do not involve any intentional bias, the impugned notifications to grant exemption for limited period on certain specific conditions cannot be held to be bad in law. Accepting the said argument, it

VERDICTUM.IN

was held that the impugned notification was not violative of the constitutional provisions since Article 301 did not apply to the case. Then, Article 304(a), which is an exception to Article 301, would also not apply. In paragraph 27, it was noted that in the said case, the general rate applicable to locally made goods was the same as on the imported goods. Hence, it did not fall within the exception of Article 304 as it was not hit by Article 301. In paragraph 28 of the judgment, this Court observed that the concept of economic barrier must be adopted in a dynamic sense with changing conditions. That in a federal polity, all the States have powers to grant exemption to specified class for limited period; such granting of exemption cannot be held to be contrary to the concept of economic unity. It was reasoned that the contents of economic unity by the people of India would necessarily include the power to grant exemption or to reduce the rate of tax in special cases for achieving industrial development or to provide tax incentives to attain economic equality in growth and development. When all the States have such provisions to exempt or reduce rates, the question of economic war between the States *inter se* or

VERDICTUM.IN

economic disintegration of the country as such did not arise. Therefore, the challenge to the exemption was upheld.

10.6.7 In the very same case, writ petitions concerning the notification issued by the Punjab Government whereby two different rates of taxes were provided, were also considered. There was a differentiation in the rate of tax between the manufacturers of electronic goods outside the State and those within the State of Punjab. It was reasoned that the lower rate of tax on those electronic goods manufactured in the State of Punjab was due to the prevailing peculiar circumstances of Punjab. It was to attract new entrepreneurs from other States and within the State to manufacture within the State of Punjab. Therefore, incentive was provided for growth of industry in Punjab which had already shifted to other States.

10.6.8 In view of the above, the concessional rate of tax introduced was held to be non-discriminatory. Taking note of the situation in the State of Punjab, it was observed that a backward State or a disturbed State cannot with parity engage in competition with advanced or developed States. Even within a State, there are often backward areas which can be developed only if some special

VERDICTUM.IN

incentives are granted. If the incentives in the form of subsidies or grant are given to any part of a State so that it may come out of its limping or infancy to compete as equals with others, that cannot contravene the spirit and the letter of Part XIII of the Constitution. However, there must be valid, justifiable and rational reasons for differentiation. If there is none, it will amount to hostile discrimination. Consequently, the notification issued by the Punjab Government under the Punjab General Sales Tax Act was also upheld.

Shree Mahavir Oil Mills:

10.7 In ***Shree Mahavir Oil Mills,*** the facts were that the cost of production of edible oil in Jammu and Kashmir was higher than in the adjoining States and as a result, the manufacturers of edible oil in the adjoining States were able to sell their products in Jammu and Kashmir at a price lower than the price at which the local manufacturers were able to sell them. Facing the prospect of closure, the manufacturers of the edible oil in the State sought exemption from the levy of sales tax on the sale of their products. With a view to protect the local edible oil industry, the Government of Jammu and Kashmir issued SRO 93 of 1991 on 07.03.1991

VERDICTUM.IN

under Section 5 of the Jammu and Kashmir General Sales Tax Act, 1962 directing that "the goods manufactured by a dealer operating as a small-scale industrial unit in the State and registered with the Director of Industries and Commerce, Handicrafts or Handloom Development, subject to certain conditions, shall be exempted from payment of tax to the extent and for the period specified in the Schedule forming Annexure A". The exemption was total and the period of exemption was five years and later extended by another five years. This led to the manufacturers of edible oil in other States being obliged to pay sales tax on the sales effected by them in the State of Jammu and Kashmir at the rate of four per cent, while the local manufacturers were totally exempted therefrom. The rate of tax was thereafter raised from four per cent to eight per cent to be paid only by the outside manufacturers, while the local manufacturers were exempt fully. The outside manufacturers approached the Jammu and Kashmir High Court by way of writ petitions which were dismissed by both learned Single Judge as well as by the Division Bench of the High Court, based mainly on the decision of this Court in ***Video Electronics.***

VERDICTUM.IN

10.7.1 B.P. Jeevan Reddy, J. observed that under Article 304(a), a State Legislature may tax goods imported from other States/Union Territories but in the process ought not to discriminate against them *vis-à-vis* goods manufactured locally. Therefore, there could not be tax barriers or fiscal barriers, in the interest of freedom of trade, commerce and intercourse throughout the territory of India, guaranteed by Article 301. In other words, for the purpose of encouraging or promoting the local industries, the weapon of taxation cannot be used to discriminate against the imported goods *vis-à-vis* the locally manufactured goods. That, Part XIII of the Constitution would indicate that no State would tax its people at a higher level merely with a view to tax the people of other States at that level. But conversely, there cannot be "tariff walls" or fiscal barriers in so far as goods manufactured outside a State and imported into the State is concerned.

10.7.2 It was further observed that the freedom guaranteed in Article 301 was "throughout the territory of India" and not merely between the States as such; the emphasis is upon the oneness of the territory of India. That, Article 301 was a general provision and

VERDICTUM.IN

Article 304(a) was not really an exception to Article 301, despite the use of the *non-obstante* clause but a restatement of a facet of the very freedom guaranteed by Article 301, namely, power of taxation by the States.

10.7.3 After referring to several decisions of this Court, in the context of the judgment ***Video Electronics*** on which strong reliance was placed by the State of Jammu and Kashmir, it was noted that in the said case there were two notifications impugned and as already noted above, the said notifications were upheld. Relying on the said judgment of the three-judge Bench, it was contended on behalf of the State of Jammu & Kashmir that a State which is technically and economically weak on account of various factors should be allowed to develop economically by granting concessions, exemptions and subsidies to new industries. That, all parts of the country are not equally developed, industrially or economically. Further, the power to grant exemption is inherent in all taxing statutes and the Government cannot be deprived of this power by invoking Articles 301 and 304. This is because a backward State or a disturbed State cannot be on par with advanced or developed States. Even within a State, there are often

VERDICTUM.IN

backward areas which could be developed only if some special incentives are granted. If there are justifiable and rational reasons for differentiation, then there will be no hostile discrimination.

10.7.4 Distinguishing the judgment in ***Video Electronics,*** it was observed that the limited exception created in the said case does not help the State of Jammu & Kashmir for the reason that exemption concerned herein is neither confined to "new industries", nor is circumscribed by other conditions of the nature stipulated in the Uttar Pradesh notification. That it is not possible to go on extending the limited exception created in the said judgment, by stages, which would have the effect of robbing the salutary principle underlying Part XIII of its substance. Consequently, it was held that the total exemption granted in favour of small-scale industries in Jammu and Kashmir producing edible oil was not sustainable in law. It was also observed that Article 304(a) of the Constitution shall not be so exercised as to bring about a discrimination between the imported goods and the similar goods manufactured or produced in a State. That the clause deals only with discrimination by means of taxation; it prohibits it. The prohibition cannot be extended beyond the power of

VERDICTUM.IN

taxation. This means that the States are free to encourage and promote the establishment and growth of industries within their States by all such means as they think proper but they cannot, in that process, subject the goods imported from other States to a discriminatory rate of taxation, i.e., a higher rate of sales tax *vis-à-vis* similar goods manufactured/produced within that State and sold within that State. The prohibition is against discriminatory taxation by the States and it matters not how this discrimination is brought about. The limited exception carved out in ***Video Electronics*** cannot be enlarged, lest it would eat up the main provision. Placing reliance on ***Firm Mehtab Majid*** and the other cases, it was held that the exemption from payment of sales tax altogether was discriminatory and prohibited under Article 304(a) of the Constitution.

10.7.5 Another contention which was urged by the State of Jammu and Kashmir was to the effect that when the rate of tax was four percent there was no challenge to the sale but when the rate of tax climbed to eight per cent there was a challenge and hence a principle of acquiescence applied. This contention was repelled by stating that there can be no question of any

VERDICTUM.IN

acquiescence in matters affecting constitutional rights or limitations. Further, the contention regarding applicability of Article 14 and there being an intangible difference between locally produced edible oil and imported edible oil was also retorted. This Court observed that Article 14 speaks of equality; whereas Article 301 speaks of freedom and Article 304(*a*) speaks of uniform taxation of both the imported goods and the locally produced goods by the States. However, the consequential direction was that the declaration of invalidity of the impugned notification was to take effect from 01.04.1997 and till that date, the impugned notification was to continue to be effective and operative. Therefore, the appellants therein were not entitled to claim any amount by way of refund or otherwise.

Loharn Steel Industries Ltd.:

10.8 In ***Loharn Steel Industries Ltd.***, the facts were that the appellant therein was a registered dealer of iron and steel in the State of Andhra Pradesh and purchased iron and steel scraps and ingots in the said State and sent to a rerolling mill in the State of Karnataka. The raw material was rerolled and brought back to the State of Andhra Pradesh and sold therein. The impugned

VERDICTUM.IN

exemption notification impugned therein, as it originally stood exempted all rerolled finished products sold in the State of Andhra Pradesh from tax provided tax had been paid in the said State on the raw material. This exemption was available to rerolled products which were manufactured even within the said State. There was no challenge to that portion of the notification. However, the exemption notification discriminated against goods manufactured outside the State of Andhra Pradesh by denying exemption to such goods (manufactured outside the State). This portion was added by an amendment to the notification. This amendment was struck down by applying the doctrine of severability on the premise that it violated Article 304(a) of the Constitution as it was discriminatory.

Laxmi Paper Mart:

10.9 Exercise books prepared from paper purchased within the State was exempted from sales tax whereas exercise books prepared outside the State and brought and sold within the State was subjected to sales tax. This was held to be in violation of Article 304(a) of the Constitution in ***Laxmi Paper Mart.*** Referring to ***Firm Mehtab Majid*** and ***Shree Mahavir Oil Mills***, it was observed that

VERDICTUM.IN

the exemption from payment of tax on locally manufactured goods *vis-à-vis* imported goods from other States was discriminatory as it created a fiscal barrier on the free flow of trade and commerce and hence, the exemption was struck down as offending Article 301 of the Constitution.

Digvijay Cements:

10.10 In ***Digvijay Cements***, the challenge was to notification dated 12.03.1997 issued by the State of Rajasthan under Section 8(5) of the Central Sales Tax Act whereby it reduced the rate of sales tax on inter-state sale of cement by any dealer from that State to 4%. The grievance of the petitioner therein was that as a consequence of such reduction of sales tax, cement from Rajasthan became much cheaper in the neighbouring States like Gujarat and that adversely affected the local sale of cement manufactured by the petitioners therein in Gujarat by reason of higher rate of sales tax on the local sales within that State. Such reduction of the rate of tax, it was contended, was contrary to the scheme contained in Part XIII of the Constitution and was liable to be struck down. The Constitution Bench of this Court did not agree with the contention that the impugned notification had the effect of preventing or

VERDICTUM.IN

hindering the free movement of goods from one State to another. As far as the State of Rajasthan was concerned, it had the opposite effect. Merely because local rate of tax in the neighbouring States on the sale of cement was higher than the inter-state sales tax on the cement sold from the State of Rajasthan cannot lead to the conclusion that the impugned notification prevented or hindered the free movement of goods from one State to another.

10.10.1 According to this Court, the impugned notification increased the movement of cement from the State of Rajasthan to the other States. There was no barrier as such but there was an increase in the volume of inter-state trade. Referring to ***Shri Digvijay Cement Co. vs. State of Rajasthan, AIR 1997 SC 2609***, it was observed that increase in revenue and its utilisation for the public of the State can generally be regarded to be in public interest but that by itself could not be regarded as sufficient, if it had the effect of going against the policy of the statute and the object of the constitutional provisions. That Section 8(5) of the Central Sales Tax Act, 1956 clearly enables the State Governments to reduce the rate of inter-state sales tax if it is satisfied that it is necessary to do so in public interest. It was observed that if the

VERDICTUM.IN

reduction of the rate of tax results in increase of revenue and of industrial activities, providing employment in the industry, it cannot be said that the notification was not issued in the public interest. On the other hand, if the lowering of tax adversely affects the movement of goods from one State to another then, the free flow of trade would be adversely affected which would be violative of Article 301 of the Constitution. Consequently, on the facts of the said case, ***Shri Digvijay Cement Co. vs. State of Rajasthan, AIR 1997 SC 2609*** was overruled.

Jaiprakash Associates:

10.11 A Notification dated 18.06.1997 issued under Section 5 of the Uttar Pradesh Trade Tax Act, 1948 ("UP Act") was the centre of controversy in ***Jaiprakash Associates.*** The substantial question of law that was considered was, whether, grant of rebate of tax by the Uttar Pradesh State Government by issuance of a notification under Section 5 of the UP Act, discriminated between the goods imported from neighbouring States and goods manufactured and produced in the State of Uttar Pradesh contravened the constitutional provisions of Articles 301 and 304(*a*) of the Constitution of India.

VERDICTUM.IN

10.11.1 The appellants therein were public limited companies, manufacturing cement in their manufacturing units in Rewa District situated in the State of Madhya Pradesh after procuring fly ash from the thermal power stations in the State of Uttar Pradesh and thereafter selling the manufactured product, namely, cement, in the districts of the State of Uttar Pradesh. Utilisation of fly ash so as to control its pollution led to cement projects being set up to make use of the fly ash generated from the power plants. To encourage manufacturers using fly ash in manufacturing of their products, the Government of Uttar Pradesh by Notification dated 18.06.1997, granted "rebate of tax" to the dealers in the State of Uttar Pradesh excluding all other dealers manufacturing cement outside the State of Uttar Pradesh using fly ash purchased in the State of Uttar Pradesh. The said notification provided the names of the districts and the period for which the rebate was allowed. The second Notification dated 27.02.1998 was issued by the Government of Uttar Pradesh which was rescinded by issuing a Notification dated 14.10.2004. Aggrieved by the Notification dated 27.02.1998, the cement industries situated in the neighbouring States approached the Allahabad High Court by filing writ petitions

VERDICTUM.IN

and seeking quashing of Condition I of the Notification dated 27.02.1998, which were dismissed.

10.11.2 Two issues fell for consideration before this Court which could be epitomised as under:

> "Firstly, whether the grant of rebate of tax was hit by the constitutional limitation on the State Legislature under Article 304(a) read with Article 301 of the Constitution of India, as and when it discriminated between the imported goods and the goods manufactured and produced outside the State.
>
> The second issue that arose was, whether the grant of rebate, directly or indirectly, restricted the free flow of trade, commerce and intercourse among States by assuming the effects of an exemption/concession which is nothing but a concept within the scope of taxation."

10.11.3 Discussing on Chapter XIII of the Constitution, it was observed that Article 304(a) does not prevent levy of tax on goods; what is prohibited is such levy of tax on goods as would result in discrimination between goods imported from other States and similar goods manufactured or produced within the State. The object was to prevent imported goods being discriminated against by imposing a higher tax thereon than on local goods. Thus, the rate of taxation on local as well as imported goods must be the same so as to discourage the States from creating fiscal barriers.

VERDICTUM.IN

10.11.4 It was noted that the principle of "non-discriminatory tax" is a *sine qua non* to free movement of goods between States as provided in Article 304(a) of the Constitution of India. Thus, the power given to the State under the said clause is not a blanket power but is restrictive, although it is an exception to Article 301. Observing thus, it was noted that in order to ascertain discrimination under Article 304(a), the effect of the tax on the flow of the goods from outside the taxing statute has to be taken into consideration and whether the overall effects of rebate of tax is such that they fall within the meaning of "concessional rate of tax".

10.11.5 Delineating on the concept of rebate of tax and its overall impact on the trade, commerce and intercourse, it was observed that a rebate is a "discount", i.e., to allow a deduction from a gross amount. It is a discount repaid to the payer. A rebate of tax can also be akin to concessional / reduced rate of tax. That in the said case, the controversy concerned the grant of rebate up to the full amount of the tax levied on any specific point in the series of sales/purchase of goods. Such rebate was only extended to the districts in the State of Uttar Pradesh. The question was, whether, this was a weapon of taxation that was discriminatory between the

VERDICTUM.IN

goods imported and manufactured in Uttar Pradesh as laid down in Article 304(a) of the Constitution. While observing that this Court in ***Shree Mahavir Oil Mills*** clarified the exception carved out by the three-judge bench in ***Video Electronics,*** it was held necessary to ascertain whether the particular exemption granted by the State affected Articles 301 and 304. This Court noted that Article 304(a) is a provision that deals with taxation to limit the power of taxation by the State so as to prevent discrimination against imported goods by imposing taxes on such goods at a higher rate than is borne by indigenous goods. It was observed that if the rebate of tax by way of repayment to the full amount of tax levied qualified within the same meaning as that of exemption, then the same would *a fortiori* mean discrimination on the rate of tax by repaying by way of a rebate to one class of local dealers the whole amount of sales tax paid and on the other hand the outside dealers are taxed higher in the absence of the benefit of rebate. This was held to be "discrimination" within the meaning of Article 304(a) of the Constitution.

10.11.6 On the aspect of exemption from tax, it was noted that it has a twofold impact: *first,* exemptions/concessional rate of tax

VERDICTUM.IN

affect consumer choice by impacting relative pricing and therefore, materially altering the economic balance. Since consumption tends to shift towards the items which are not taxed, the prices of those items and the raw materials used to produce them would increase while the prices of taxed items would decrease relatively; *second*, such exemptions unfairly burden some businesses either within the same industry or in other competing industries.

10.11.7 Speaking about rebate, it was observed that it is another device used by the Government which, when given on the rate of tax to the full amount of tax levied, gives favourable treatment to one class of dealers situated within the State barring the dealers similarly placed outside the State manufacturing goods using the same raw material. Then, grant of such rebate has the colour of exemption/concessional rate of tax along with the same deleterious effects of an exemption. While considering Article 304(a) in the context of whether rebate is within the realm of tax defined under the said clause so as to say that it discriminates between the two classes of goods, namely, locally manufactured goods and the imported goods when both the classes of dealers meet the conditions required to qualify for the grant of rebate i.e. the use of

VERDICTUM.IN

fly ash, the Court noted that the overall effect or impact of such rebate would be on the manufacturer. Following the judgments of ***Firm Mehtab Majid; W.B. Hosiery Assn. vs. State of Bihar, (1988) 4 SCC 134 ("W.B. Hosiery Assn.")*** and ***H. Anraj,*** the issue with regard to the disparity between the locally manufactured goods within the State and those manufactured in other States were discussed in light of the facts of those cases. It was observed that the rebate of tax being in the nature of an exemption in the instant case was discriminatory and violative of Article 304(a) of the Constitution of India.

Jindal Stainless Ltd.:

10.12 ***Jindal Stainless Ltd.*** is a nine-Judge Bench decision of this Court wherein by a majority, this Court, *inter alia,* observed as under:

> **"1159.1.** Taxes simpliciter are not within the contemplation of Part XIII of the Constitution of India. The word "free" used in Article 301 does not mean "free from taxation".
>
> **1159.2.** Only such taxes as are discriminatory in nature are prohibited by Article 304(*a*). It follows that levy of a non-discriminatory tax would not constitute an infraction of Article 301.
>
> **1159.3.** Clauses (*a*) and (*b*) of Article 304 have to be read disjunctively.

VERDICTUM.IN

1159.4. A levy that violates Article 304(*a*) cannot be saved even if the procedure under Article 304(*b*) or the proviso thereunder is satisfied.

1159.5. The Compensatory Tax Theory evolved in ***Automobile Transport (Rajasthan) Ltd.* v. *State of Rajasthan, AIR 1962 SC 1406 : (1963) 1 SCR 491*** and subsequently modified in ***Jindal Stainless Ltd. (2) v. State of Haryana, (2006) 7 SCC 241*** has no juristic basis and is therefore rejected.

1159.6. The decisions of this Court in ***Atiabari Tea Co. Ltd. v. State of Assam, AIR 1961 SC 232 : (1961) 1 SCR 809*** , ***Automobile Transport (Rajasthan) Ltd. v. State of Rajasthan, AIR 1962 SC 1406 : (1963) 1 SCR 491*** and ***Jindal Stainless Ltd. (2) v. State of Haryana, (2006) 7 SCC 241*** cases and all other judgments that follow these pronouncements are to the extent of such reliance overruled.

xxx

1159.8. Article 304(*a*) frowns upon discrimination (of a hostile nature in the protectionist sense) and not on mere differentiation. Therefore, incentives, set-offs, etc. granted to a specified class of dealers for a limited period of time in a non-hostile fashion with a view to developing economically backward areas would not violate Article 304(*a*). The question whether the levies in the present case indeed satisfy this test is left to be determined by the regular Benches hearing the matters."

10.12.1 The question formulated by this Court for determination by the nine-Judge Bench which are relevant to the present case read as under:

"(i) Can the levy of a non-discriminatory tax per se constitute infraction of Article 301 of the Constitution of India?"

VERDICTUM.IN

10.12.2 While answering these questions, the majority, speaking through Thakur, C.J., discussed whether levy of a tax is an attribute of sovereignty and if so, whether Article 246 of the Constitution recognises the sovereign power of the State to make laws including the power to levy taxes on subjects enumerated in List II of the Seventh Schedule to the Constitution. While holding that power to levy taxes is an essential attribute of sovereignty, it was observed that constitutional provisions relating to the power of taxation do not operate as grants of the power of taxation to the Government but instead merely constitute limitations upon a power which would otherwise be practically without limit. Since Article 265 of the Constitution provides that no tax shall be levied or collected except by authority of law, it would be necessary to first enquire whether the legislature which passes the Act was competent to pass it or not. Thus, power to tax being an incident of sovereignty, however, under the Constitution, is circumscribed by Articles 245, 246 and 265. In other words, the exercise of sovereign power of taxation is subject to constitutional limitation in a federal system like in India where the Union as well as the

VERDICTUM.IN

States have the power to make laws including laws that levy taxes, duties and fees, however, within the extent permissible under the Constitution.

10.12.3 These constitutional limitations on the power of the State Legislatures to levy taxes or for that matter enact laws are mentioned by way of relevant Entries of Lists II and III of the Seventh Schedule (there being no taxation in Entry of List III). Further, there are other provisions which provide for the constitutional limitations in the matter of taxation to be levied by the Union or the State which is not necessary to advert to in the present case.

10.12.4 After analysing other Articles in Part XIII of the Constitution, the Court dealt with Article 304 that deals with restrictions on trade, commerce and intercourse among States which could be made by the Legislature of a State. It was observed that Article 304(a) does not treat tax as a restriction so that any such levy may fall foul of Article 301. In fact, Article 304(a) recognises the State Legislature's competence to impose a tax on goods imported from other States or the Union Territories. However, the power to tax goods imported from other States or

VERDICTUM.IN

Union Territories is not unqualified or unrestricted. That there are two restrictions on the power. The words *"to which similar goods manufactured or produced in that State are subject"* impose the first restriction on the power of the State Legislature to levy such tax. These words would imply that a tax on import of goods from other States will be justified only if similar goods manufactured or produced in the State are also taxed. The second restriction comes from the expression "*so, however, as not to discriminate between goods so imported and goods so manufactured or produced*". The State Legislature cannot in the matter of levying taxes discriminate between goods imported from other States and those manufactured or produced within the State levying such a tax. The net effect of Article 304(a) therefore is that while levy of taxes on goods imported from other State and the Union Territories is clearly recognised as constitutionally permissible, the exercise of such power is subject to the two restrictive conditions referred to above. That does not however detract from the proposition that levy of taxes on goods imported from other States is constitutionally permissible so long as the State Legislatures abide by the limitations placed on the exercise of that power. To put it differently, levy of taxes on import

VERDICTUM.IN

of goods from other States is not by itself an impediment under the scheme of Part XIII or Article 301 appearing therein.

10.12.5 The next question, namely, whether clauses (a) and (b) of Article 304 have to be read conjunctively or disjunctively was also considered.

10.12.6 It was observed that clauses (a) and (b) of Article 304 deal with two distinct subjects and must, therefore, be understood to be independent of each other. While clause (a) deals entirely with imposition of taxes on goods imported from other States, clause (b) deals with imposition of reasonable restriction in public interest. The use of the word "and" between clauses (a) and (b) does not admit of an interpretation that may impose an obligation upon the legislature to necessarily impose a tax and a restriction together. The word "and" can mean "or" as well as "and" depending upon the context in which the law enacted by the legislature uses the same. Levy of taxes do not constitute a restriction under Part XIII except in cases where the same are discriminatory in nature. In paragraph 76, the discussion was summarised as under:

VERDICTUM.IN

"76. The sum total of what we have said above regarding Articles 301, 302, 303 and 304 may be summarised as under:

76.1. Freedom of trade, commerce and intercourse in terms of Article 301 is not absolute but is subject to the provisions of Part XIII.

76.2. Article 302 which appears in Part XIII empowers Parliament to impose restrictions on trade, commerce and intercourse in public interest.

76.3. The restrictions which Parliament may impose in terms of Article 302 cannot however give any preference to one State over another by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

76.4. The restriction that Parliament may impose in terms of Article 302 may extend to giving of preference or permitting discrimination between one State over another only if Parliament by law declares that a situation arising out of scarcity of goods warrants such discrimination or preference.

76.5. Article 304(*a*) recognises the availability of the power to impose taxes on goods imported from other States, the legislative power to do so being found in Articles 245 and 246 of the Constitution.

76.6. Such power to levy taxes is however subject to the condition that similar goods manufactured or produced in the State levying the tax are also subjected to tax and that there is no discrimination on that account between goods so imported and goods so manufactured or produced.

76.7. The limitation on the power to levy taxes is entirely covered by clause (*a*) of Article 304 which exhausts the universe insofar as the State Legislature's power to levy of taxes is concerned.

VERDICTUM.IN

> **76.8.** Resultantly, a discriminatory tax on the import of goods from other States alone will work as an impediment on free trade, commerce and intercourse within the meaning of Article 301.
>
> **76.9.** Reasonable restrictions in public interest referred to in clause (*b*) of Article 304 do not comprehend levy of taxes as a restriction especially when taxes are presumed to be both reasonable and in public interest."

10.12.7 Thus, it was held that Article 304(b) of the Constitution does not deal with taxes as restrictions. That those restrictions referred to in that provision are non-fiscal in nature. Therefore, any constitutional validity of any taxing statute has to be tested only on the anvil of Article 304(a) and if the law is found to be non-discriminatory, it can be declared to be constitutionally valid without the legislation having to go through the test of the process envisaged by Article 304(b). Should, however, the statute fail the test of non-discrimination under Article 304(a), it must be struck down for the same cannot be sustained even if it had gone through the process stipulated by Article 304(b). This is because what is constitutionally impermissible in terms of Article 304(a) cannot be validated and sanctioned through the medium of Article 304(b). Any challenge to a fiscal enactment on the touchstone of Article 304(a) must be tested by the same standard as in the decision of

VERDICTUM.IN

this Court in ***Kathi Raning Rawat vs. State of Saurashtra, AIR 1952 SC 123.*** The Court ought to examine whether the differentiation made is intended or inspired by an element of unfavourable bias in favour of the goods produced or manufactured in the State as against those imported from outside. If the answer be in the affirmative, the differentiation would fall foul of Article 304(a) and may tantamount to discrimination. Conversely, if the Court were to find that there is no such element of intentional bias favouring the locally produced goods as against those from outside, it must go further and see whether the differentiation would be supported by valid reasons. This is because discrimination without reason would be unconstitutional whereas discrimination with reason may be legally acceptable.

10.12.8 Regarding the decision in ***Video Electronics,*** it was observed that the differentiation made was supported by reasons. It was observed that power to grant exemption is a part of the sovereign power to levy taxes which cannot be taken away from the States that are otherwise competent to impose taxes and duties. It was further observed that ***Video Electronics***, therefore, correctly states the legal position as regards the approach to be adopted by

VERDICTUM.IN

the courts while examining the validity of levies. So long as the differentiation made by the States is not intended to create an unfavourable bias and so long as the differentiation is intended to benefit a distinct class of industries and the life of the benefit is limited in terms of period, the benefit must be held to flow from a legitimate desire to promote industries within its territory. In this context, ***Shree Mahavir Oil Mills*** was held distinguishable inasmuch as the manufacturers of edible oil therein were exempt totally and unconditionally while other manufacturers from outside the State were not so exempt. Referring to several other decisions, in paragraph 144 of the judgment, it was observed that so long as the intention behind the grant of exemption/adjustment/credit is to equalise the fall of the fiscal burden on the goods from within the State and those from outside the State, such exemption or setoff will not amount to hostile discrimination offensive to Article 304(a).

10.12.9 Bobde, J. (as he then was) concurred with Thakur, C.J. and SK Singh, J. and observed that to muster compliance with Part XIII of the Constitution, the tax must pass the twin tests embodied in Article 304(a) i.e., (i) similar goods produced locally must also be

VERDICTUM.IN

subjected to similar tax; and (ii) such State action should not attract the vice of discrimination between the two varieties of goods.

10.12.10 In paragraph 262 of the judgment, Ramana, J. (as he then was) observed that the object is to prevent discrimination against imported goods by imposing tax on such goods at a rate higher than that borne by local goods since the difference between the two rates would constitute a tariff wall or fiscal barrier and thus impede the free flow of inter-State trade and commerce. It does not prohibit levy of tax as such in the situation wherein the goods are not produced or manufactured in the State itself and does not affect the authority of the State to tax the imported goods. It only bars discrimination on the basis of taxing the products manufactured within the State *vis-à-vis* imported goods which will only occur if the precondition of manufacturing in the taxing State is satisfied.

10.12.11 Banumathi, J. while agreeing with Thakur, C.J. observed that decisions in ***Atiabari Tea Co. Ltd.*** and ***Automobile Transport Ltd.*** to the extent they declare that taxes generally are restrictions on the freedom of trade, commerce and intercourse ought to be overruled. Further, non-discriminatory taxes do not

VERDICTUM.IN

constitute infraction of Article 301 of the Constitution. The law laid down in ***Video Electronics*** was also endorsed.

10.12.12 By contrast, Dr. Chandrachud, J. (as he then was), firstly stated that a discriminatory tax is prohibited under Article 304(a) in the context of exemptions and incentives as held in the judgments of this Court in ***Video Electronics*** and ***Shree Mahavir Oil Mills.*** It was observed that in ***Video Electronics,*** this Court considered the validity of the notifications issued under the Uttar Pradesh Sales Tax Act, 1948, as well as under the Punjab General Sales Tax Act. Under the notification issued under the Uttar Pradesh legislation, an exemption from the payment of sales tax was granted for goods manufactured in new industrial units, where the date of commencement of production fell between two stipulated dates. The exemption was for a stipulated period reckoned from the date of first sale if such sale took place not later than six months from the commencement of production. The period of exemption was confined for a specified period of three to seven years. Insofar as the State of Punjab was concerned, sales tax at the rate of 12% was provided on electronic goods sold within the State irrespective of their manufacture. In pursuance of a

VERDICTUM.IN

notification issued under the Sales Tax law, the rate of sales tax payable by electronic manufacturing units producing goods specified thereunder was brought down from 12% to 1%. This was justified on the ground that it was an incentive to a backward industrial State. A Bench of three learned Judges in ***Video Electronics*** observed that this was not a case involving "a naked blanket preference in favour of locally manufactured goods, as against goods coming from outside the State". This Court therefore held that there was no discrimination under both the notifications against goods manufactured outside the State. In ***Video Electronics***, this Court distinguished the judgment in ***Weston Electronics.*** Dr. Chandrachud, J. (as he then was) observed that the *substratum* of the judgment in ***Video Electronics*** clearly is that Article 304(a) would not be breached by a classification brought about by a carefully structured notification which grants incentives to local industry of a specified class of units, with reference to a specific category of manufactured goods and for a stipulated period. The judgment in ***Video Electronics*** was distinguished on the ground that in that case, the notifications of

VERDICTUM.IN

the States of Uttar Pradesh and Punjab were carefully circumscribed.

10.12.13 Referring to paragraphs 22 and 23 of the judgment of this Court in ***Shree Mahavir Oil Mills,*** Dr. Chandrachud, J. (as he then was) observed that "the Court cautioned that a limited exception which had been carved out in ***Video Electronics*** should not be enlarged "lest it eat up the main provision"". An unconditional exemption in the case of edible oil produced within the State from sales tax while subjecting similar goods produced in other States to sales tax at 8% was held to violate Article 304(a) of the Constitution. In ***Shree Mahavir Oil Mills,*** an exemption from the payment of sales tax altogether granted to local industry was set aside as violating Article 304(a). The earlier decision in ***Video Electronics*** was distinguished on the ground that it related to a case not involving a blanket preference. In this regard, in paragraph 693, Dr. Chandrachud, J. (as he then was) observed as under:

> **"693.** A close reading of the judgment in ***Video Electronics*** would thus indicate that both sets of notifications involving the States of Uttar Pradesh and Punjab were carefully structured to cover one or more of the following circumstances:

VERDICTUM.IN

(i) Availability of a reduced rate of sales tax to new industrial units;

(ii) Applicability of a reduced rate of sales tax to producers of certain specified goods, such as electronic goods;

(iii) Limitation of the period during which the reduced rate of tax could operate; and

(iv) Applicability of the general rate of sales tax to an overwhelmingly large number of local manufacturers, on a par with imported goods."

10.12.14 Thus, Dr. Chandrachud J. (as he then was) opined that the judgment in ***Shree Mahavir Oil Mills*** left open the correctness of the view in ***Video Electronics. Shree Mahavir Oil Mills*** is a judgment rendered by a two-Judge Bench comprising B.P. Jeevan Reddy, J. and S.C. Sen, J. while ***Video Electronics*** was a judgment of three Judges of this Court. The decision in ***Video Electronics*** was distinguished on the ground that it related to a case not involving a blanket preference.

10.12.15 Ashok Bhushan, J. in his dissenting opinion but concurring on some issues, speaking about the three-Judge Bench decision of this Court in ***Video Electronics,*** observed that the exemption therein was upheld as it was granted to a special class for limited period on specific conditions of maintaining the general

rate of tax on the goods manufactured by all those producers in the State who do not fall within that category. That ***Video Electronics,*** however, further states that if tax is imposed in a colourable manner, intentionally or purposely to create unfavourable bias by prescribing a general lower rate on locally manufactured goods either in the shape of general exemption to locally manufactured goods or in the shape of lower rate of tax, such an exercise of power can always be struck down by the courts. However, in ***Shree Mahavir Oil Mills,*** it was observed that exception carved out in ***Video Electronics*** cannot be widened or expanded to cover cases of a different kind. That in ***Video Electronics,*** the exemption notification was upheld because it was limited to a specified type with short period. Therefore, even in ***Video Electronics,*** general exemption of a wider nature was not approved. In other words, the exemption cannot be used as a measure of discrimination between goods imported from other States and goods manufactured or produced in the State. The exemption has to be a limited exemption to the tax which is imposed on the similar goods. In the event such exemption is total and general in nature, the said exemption is clearly violative of

VERDICTUM.IN

Article 304(a). Similarly, set-off of a particular tax which is general and not limited to specified category has also to be disapproved. Therefore, Ashok Bhushan, J. held that the ratio of the three-Judge Bench judgment in ***Video Electronics*** has to be read to the above extent and with the limitation as noticed above. Hence, the State Legislature in exercise of its taxing power can grant exemption/set-off to local goods, only to a limited extent based on intelligible differentia which is not in the nature of general/unspecified exemption. The exemption/set-off which tend to become a general exemption violates Article 304(a) of the Constitution.

Discussion from Overseas Case Law:

11. At this instance, it is relevant to discuss a similar provision in Section 51(ii) and Section 92 of the Commonwealth of Australia Constitution Act, 1900, also known as the Australian Constitution. Sections 51(ii) and 92 provide as follows:

> "**51. Legislative powers of the Parliament**
>
> The Parliament shall, subject to tis Constitution, have power to make laws for the peace, order, and good government of the Commonwealth with respect to:
>
> xxx
>
> (ii) taxation; but **so as not to discriminate between States or parts of States**;

VERDICTUM.IN

xxx

92. Trade within the Commonwealth to be free

On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, **shall be absolutely free**."

(emphasis supplied)

11.1 A bare reading of the above provision would instantly draw our attention to Articles 301 and 304 of our Constitution.

11.2 It appears that the interpretation of Section 92 of the Australian Constitution, specifically as to *'what should the imposition be free from?',* has been a subject matter of conflicting opinions. It was the decision of the High Court of Australia in ***Cole vs. Whitfield, (1988) HCA 18*** that clarified its scope. The High Court of Australia, through a unanimous opinion, and relying on Australian federal movement, held that section 92 of the Australian Constitution prohibits measures that discriminate against interstate trade and commerce with the purpose or effect of protecting intrastate trade or industry against competition from other States.

VERDICTUM.IN

11.3 The High Court specifically held:

> "25. The task which has confronted the Court is to construe the unexpressed; to formulate in legal propositions, so far as the text of s.92 admits, the criteria for distinguishing between the burdens (including restrictions, controls and standards) to which inter-State trade and commerce may be subjected by the exercise of legislative or executive power and the burdens from which inter-State trade and commerce is immune. The history of s.92 points to the elimination of protection as the object of s.92 in its application to trade and commerce. The means by which that object is achieved is the prohibition of measures which burden inter-State trade and commerce and which also have the effect of conferring protection on intra-State trade and commerce of the same kind. The general hallmark of measures which contravene s.92 in this way is their effect as discriminatory against inter-State trade and commerce in that protectionist sense.
>
> xxx
>
> 26. In relation to both fiscal and non-fiscal measures, history and context alike favour the approach that the freedom guaranteed to inter-State trade and commerce under s.92 is freedom from discriminatory burdens in the protectionist sense already mentioned."

11.4 The High Court further explained that the concept of discrimination, so far as it relates to inter-State trade and commerce, embraces both factual as well as legal discrimination. By factual, the Court meant the operation of a law producing a disability or a disadvantage, and by legal, the Court meant the provisions, on the face of it. The Court however noted that the

VERDICTUM.IN

section accommodates laws that genuinely regulate intra-State and inter-State trade in a non-protective manner.

11.5 Finally, the Court concluded that a general law enacted under Section 51(i) of their Constitution may offend Section 92 if its effect is discriminatory and the discrimination is upon protectionist grounds. That whether such a law is discriminatory in effect and whether the discrimination is of a protectionist character are questions raising issues of fact and degree. That such answer to those questions may, in the ultimate, depend upon judicial determination.

11.6 While we are aware of the dangers involved in importing an interpretation from a judgment of a foreign jurisdiction, it is relevant to note from Australian jurisprudence that when the Court therein was called upon to interpret Section 92 of their Constitution, specifically to answer what should the imposition of uniform duties of customs, trade, commerce, and intercourse among their States be free from, the Court answered that they should be free from *discrimination of a protectionist character*. Their emphasis on the protectionist nature is of relevance to us, for the

VERDICTUM.IN

insertion of Part XIII in our Constitution was also to prevent the growth of sectional and local interests which are inimical to the interests of the nation as a whole.

Application of the Analysis to the Present Case:

12. On a perusal of the facts of the present cases and the judicial dicta relating to Articles 301 and 304(a) of the Constitution of India, we find that the issue herein could be decided by determining if the impugned notification falls within the parameters of the exception provided for in ***Video Electronics.*** In other words, if the impugned notification could be justified as falling within the parameters of the dictum in ***Video Electronics***, it could be upheld. Otherwise, it would have to be struck down as unconstitutional. Thus, the dictum in ***Video Electronics*** has to be juxtaposed with the facts of the present cases as well as in light of other judicial dicta discussed above.

12.1 On a perusal of the judgment of this Court in ***Jindal Stainless Ltd.*** as regards ***Video Electronics,*** the position of law as to when a tax merely differentiates and not discriminates, appears to be as follows:

VERDICTUM.IN

(i) Clauses (a) and (b) of Article 304 are to be read disjunctively, and hence, a tax cannot be said to merely differentiate only if the procedure under Article 304(b) is satisfied, but not Article 304(a) of the Constitution;

(ii) A tax imposed on goods imported from another state would not be discriminatory if no similar goods are produced within that State;

(iii) States are at liberty to design their fiscal legislations in such a manner to ensure that the tax burden on goods imported from other States is equal to the tax burden on those goods produced within the State. Therefore, a tax designed to impose equal burdens cannot be said to be discriminatory. However, whether the tax burden falls equally is a question of fact to be determined in each case when the question arises;

(iv) Further, a tax rebate or other relief in the form of incentives or set-off which is:

- granted to a specified class of dealers;
- for a limited period of time;
- in a non-hostile fashion;

VERDICTUM.IN

- with a view to developing economically backward areas;

would not be held to be discriminatory.

(v) However, the question whether a tax fulfils the above criteria is a question of fact to be determined depending upon the facts of each case.

12.2 Before applying the aforementioned law to the facts of this case, it is relevant to note that our analysis is not restricted to the impugned notification alone. Rather, it will be looked at *in the context of* the preceding and succeeding notifications issued by the State of Rajasthan. This is necessary because the impugned notification is merely one of the notifications out of a series of notifications effected to grant tax exemptions to the sale of asbestos cement sheets and bricks having contents of fly ash 25% or more by weight, manufactured in the State of Rajasthan. However, we make it clear that our decision would be restricted to the validity of the impugned notification only.

12.3 Applying the criteria provided for as above, we find that admittedly, the impugned notification restricted the exemption from payment of tax to a specified class of dealers, namely, those

VERDICTUM.IN

who manufactured asbestos cement sheets and bricks having contents of fly ash 25% or more by weight. We also find that, as regards the time period, the impugned notification restricted the exemption to those dealers who commenced commercial production in the State by 31.12.2006 and the exemption was available up to 23.01.2010.

12.4 However, a combined reading of the notifications dated 24.01.2000, 16.03.2005, 05.07.2006 and 28.12.2010 suggests that, initially, the benefit was restricted to dealers who commenced commercial production in the State of Rajasthan by 31.12.2001 and the benefit was upto 23.01.2010. Later, it was extended to those who commenced production by 31.12.2006. While initially the benefit was upto 23.01.2010, by notification dated 28.12.2010, the benefit was made available for ten years from the date of commencement of first commercial production, but with an outer cut-off date of 23.1.2016. There is nothing on record to suggest that the exemption was granted thereafter as well.

12.5 As far as duration is concerned, it can be observed that the maximum benefit a dealer would have obtained under these

VERDICTUM.IN

notifications was ten years. There were no serious arguments raised by the appellants herein to the question whether the benefit of a maximum of ten years would qualify as 'limited period of time' within the criteria devised in ***Jindal Stainless Ltd.***. Hence, we do not intend to decide on the same.

12.6 As regards the criterion of "with a view to developing economically backward areas", admittedly, the impugned notification is not restricted to any specific district or a set of districts within the State of Rajasthan. Rather, the notifications provide exemption to any dealer commencing production anywhere in the State.

12.7 However, the criterion of 'non-hostile fashion' was fiercely contested by both sides, as noted earlier in the submissions. The expression 'non-hostile', as expressed in ***Jindal Stainless Ltd.***, relates to discrimination of a hostile nature in the protectionist sense.

12.8 In our view, the contours of such discrimination, in essence, can be reduced to whether there are sufficient reasons to term such discrimination as 'differentiation'. In ***State of West***

VERDICTUM.IN

Bengal vs. Anwar Ali Sarkar, (1952) 1 SCC 1, this Court noted that the expressions "discriminatory" and "hostile" are found to be used by American Judges often simultaneously in connection with discussions on the equal protection clause. That if a legislation is discriminatory and discriminates one person or class of persons against others similarly situated and denies to the former the privileges that are enjoyed by the latter, it has to be regarded as "hostile" in the sense that it affects injuriously the interests of that person or class.

12.9 Similarly, the opinion of this Court in ***Twyford Tea Co. Ltd. vs. State of Kerala, (1970) 1 SCC 189*** on the meaning of 'classification without unreasonably discriminating between persons similarly situated' is relevant to this case. The Court noted then as follows:

> "18. What is meant by the power to classify without unreasonably discriminating between persons similarly situated, has been stated in several other cases of this Court. The same applies when the Legislature reasonably applies a uniform rate after equalising matters between diversely situated persons. Simply stated the law is this: Differences in treatment must be capable of being reasonably explained in the light of the object for which the particular legislation is undertaken. This must be based on some reasonable distinction between the cases differentially treated. When differential treatment is not

VERDICTUM.IN

> reasonably explained and justified the treatment is discriminatory. If different subjects are equally treated there must be some basis on which the differences have been equalised otherwise discrimination will be found. To be able to succeed in the charge of discrimination, a person must establish conclusively that persons equally circumstanced have been treated unequally and vice versa."
>
> (underlining by us)

12.10 In ***Vijay Lakshmi vs. Punjab University, (2003) 8 SCC 440***, this Court discussed the earlier judgment in ***State of J&K vs. Triloki Nath Khosa, (1974) 1 SCC 19*** and observed that discrimination is the essence of classification and does violence to the constitutional guarantee of equality only if it rests on an unreasonable basis.

12.11 Further, in ***Video Electronics***, this Court noted that the word 'discrimination' is not used in Article 14 but is used in Articles 16, 303 and 304(a). That in the context of Article 304(a), it involves an element of intentional and purposeful differentiation.

12.12 As regards the reasons behind a public authority issuing a notification, this Court in ***Commissioner of Police vs. Gordhandas Bhanji, AIR 1952 SC 16*** noted that:

VERDICTUM.IN

> "We are clear that public orders, publicly made, in exercise of a statutory authority cannot be construed in the light of explanations subsequently given by the officer making the order of what he meant, or of what was in his mind, or what he intended to do. Public orders made by public authorities are meant to have public effect and are intended to affect the actings and conduct of those to whom they are addressed and must be construed objectively with reference to the language used in the order itself."
>
> (underlining by us)

12.13 Similarly, as submitted by learned counsel for the appellants, the Constitution Bench of this Court in ***Mohinder Singh Gill*** observed that any order passed by any public authority exercising administrative/executive or statutory powers must be judged by the reasons so mentioned in that order and cannot be supplemented by fresh reasons in the shape of an affidavit or otherwise.

12.14 A perusal of the impugned notification dated 09.03.2007 would suggest that the reason stated by the State Government to exempt from payment of tax was simply that "it was expedient in the public interest so to do". The notification states no further reason for issuing the impugned notification. The exemption from

VERDICTUM.IN

payment of tax on the sale of asbestos sheets and bricks subject to the following conditions:

(i) That the asbestos sheets and bricks are manufactured in the State of Rajasthan; and

(ii) They have 25% content of fly ash or more by weight.

Further, the following condition would apply, namely –

(i) that the goods shall be entered in the registration certificate of the selling dealer.

(ii) that the exemption shall be for such goods manufactured by the dealer who commenced commercial production in the State by 31.12.2006; and

(iii) that the exemption shall be available up to 23.01.2010.

Therefore, with respect to the goods manufactured by the dealer who commenced commercial production in the State before 31.12.2006 the exemption was upto 21.03.2010. Thereafter, by subsequent notification, the benefit was extended upto 23.01.2016.

VERDICTUM.IN

12.15 There is also nothing on record to suggest that the notification was issued pursuant to, say, an industrial policy or otherwise. During the course of submissions, we had asked the learned senior counsel for the respondent State if there are any policies of the State as regards setting up of asbestos sheet or cement industry, pursuant to which the notifications were issued, the learned senior counsel could not take us to any such background policy, but submitted that the reasons for the notification can be discerned from the counter affidavit filed before the High Court. In light of the dictum of this Court in ***Mohinder Singh Gill***, we are not able to accept the contention of the learned senior counsel for the State of Rajasthan that the reasons for the notification can be discerned from the counter affidavit filed before the High Court.

12.16 Keeping aside the dictum in ***Mohinder Singh Gill***, **even otherwise**, the counter affidavit filed before the High Court attempts to provide reasons as to why the notification dated 24.01.2000 was issued. The reason stated was to promote the use of fly ash as a raw material from the production of asbestos cement sheets and bricks with the intention of utilization of fly ash coming

VERDICTUM.IN

out of thermal power plant and to promote the production of asbestos cement sheets for which there was no manufacturing plant in Rajasthan. There is no other reason stated for why the impugned notification is issued. Admittedly, the impugned notification can be said to be a continuation of the earlier notifications, including the notification dated 24.01.2000. However, there are no reasons stated even in the counter-affidavit as to why the benefit was extended to those who commenced production beyond 31.12.2001 through the impugned notification. The State ought to have explained, for e.g., the effect of the earlier notifications, the inadequacy, if any, of the notification in fulfilling the intended objectives, if any, and the consequent need for issuing the subsequent notification.

12.17 In the absence of any such explanation, we cannot, but conclude, that the impugned notification is bereft of any reason or justification. The High Court in the impugned judgment relied upon the reasoning in ***Video Electronics*** to arrive at the conclusion that the stand of the State of Rajasthan was supported by the reasoning in the aforesaid case. While acknowledging that in ***Shree Mahavir Oil Mills,*** this Court had explained and

VERDICTUM.IN

distinguished the dictum in ***Video Electronics*** wherein the exemption was granted to new industries for a specified period, the High Court in our view, fell in error in holding that the present case also falls in the exceptional category covered by the case of ***Video Electronics***. We observe that the said finding is incorrect inasmuch as the exemption was not granted to new industries and neither was it given for a limited period of time. The exemption was granted initially upto 23.01.2010 and later extended upto 23.01.2016. The exemption was granted to those asbestos sheet and bricks manufacturers in the State of Rajasthan utilizing fly ash as its main raw material on the conditions namely, (i) that such fly ash constituted 25% or more in the contents by weight; and (ii) that the unit commenced commercial production by 31.12.2001.

12.17.1 The first condition is an ingredient specific criterion. This would mean that any asbestos sheet product containing 25% fly ash manufactured outside the State of Rajasthan and sold in the said State would not have the benefit of the exemption. This would mean that the source of fly ash is not really the basis for the exemption. The asbestos products could be manufactured in the State of Rajasthan with fly ash obtained from outside the State and

VERDICTUM.IN

sold within the State. If the object of the exemption was to utilise the fly ash available in the State of Rajasthan itself, it should have been so spelt out in the impugned notification. Otherwise, we find a discrimination between asbestos products manufactured in the State of Rajasthan and manufactured outside, having content of fly ash to an extent of 25% when sold in the State of Rajasthan. On the other hand, if the notification had prescribed a condition that fly ash sourced from State of Rajasthan and products sold in the State, irrespective of their place of manufacture would have the benefit such exemption, there would not have been any discrimination between products manufactured outside the State of Rajasthan sold within the said State and those manufactured within the State, both having the benefit of exemption as both categories of products would have utilised fly ash available in the State of Rajasthan. This approach would have also met the objective of utilising the available fly ash in the State of Rajasthan. But, that is not so in the present case. Hence, we have no hesitation in holding that the impugned notification violates Article 304(a) of the Constitution as it is discriminatory in nature.

VERDICTUM.IN

12.17.2 The impugned notification initially was to remain operative upto 23.01.2010 only. The time for commencement of commercial production was extended from time to time and by the notification issued on 16.03.2005, the State Government extended the commencement of production by 31.12.2006. It was submitted that the notification dated 09.03.2007 impugned in the writ petition before the High Court came to be issued by the State Government after coming into force of the Rajasthan VAT Act so as to continue with the discriminatory exemption.

12.18 On a survey of the judicial dicta of this Court, what emerges is that in ***Atiabari Tea Co. Ltd.,*** the object and purpose of Part XIII of the Constitution of India and particularly Article 301 was considered and it was observed that while determining the width and amplitude of the freedom guaranteed by the said Article, a rational and workable test should be applied and only if the restrictions impede free flow of trade, it would be barred. Otherwise, taxes imposed on goods would not by themselves impede trade and commerce in the said case, the Assam Act was held to be void as it had not complied with Article 304(b) of the Constitution. While interpreting Article 304(a), it was observed that

VERDICTUM.IN

the State Legislatures have the power to impose tax on the import of goods to which similar goods manufactured or produced in the State are subject, provided that by taxing the goods imported from another State or Union Territory, no discrimination is practised.

12.18.1 ***Automobile Transport Ltd.*** also concerned Article 304(b) of the Constitution. It was observed that a tax to become a prohibited tax, has to be a direct tax, the effect of which is to hinder the movement of trade. So long as a tax remains compensatory or regulatory, it cannot operate as a hindrance. Taxation which impedes trade and commerce cannot be upheld on the ground that they are regulatory. A regulation of trade and commerce, on the other hand, may achieve some public purpose which affects trade and commerce incidentally but not impairing the freedom. In the said case, it was observed that the tax offended Article 301 of the Constitution since resort to the procedure prescribed by Article 304(b) was not taken.

12.18.2 In ***Firm Mehtab Majid,*** referring to the aforesaid decisions, it was held that sales tax which has the effect of discriminating between goods of one State and goods of another

VERDICTUM.IN

State may affect the free flow of trade which offends Article 301 and will be valid if it comes within the terms of Article 304(a). Thus, Article 304(a) enables the Legislature of a State to make laws by imposition of taxes on goods from other States if similar goods in the State are also subjected to similar taxes, so as not to discriminate between the goods manufactured or produced in that State and the goods which are imported from other States. In the said case, the writ petition was allowed as the sales tax was held to be discriminatory in nature and the State was directed to refund the tax illegally collected from the petitioner therein.

12.18.3 Similarly, in ***Weston Electronics***, the reduction on the rate of sales tax on television sets manufactured within the State to 1% whereas television sets imported from outside the State of Gujarat being at 10% was held to be discriminatory in nature and therefore, struck down.

12.18.4 The judgment in ***Video Electronics*** by a three-Judge Bench of this Court is a watershed in the line of precedent on the interpretation of Chapter XIII of the Constitution. In this case, the imposition of differential rate of tax on sales of the commodity

VERDICTUM.IN

imported from outside the State as compared to the same commodity manufactured within the State and sold in the State was upheld as being not discriminatory in nature. It was observed that the expression "discrimination" in Article 304(a) of the Constitution involves an element of intentional and purposeful discrimination thereby creating an economic barrier and involves an element of unfavourable bias. Insofar as the State of Punjab was concerned, it was reasoned that the lower rate of tax on those electronic goods manufactured in the State of Punjab was due to the prevailing peculiar circumstances in the said case, namely, terrorist activity. In order to attract new entrepreneurs from other States and to encourage manufacturers within the State of Punjab, incentives were provided for growth of industry in the State of Punjab which had already shifted to other States, therefore, the concessional rate of tax introduced for goods manufactured within the State of Punjab was held to be non-discriminatory. The aforesaid reasoning was given having regard to the situation then prevailing in the State of Punjab as it was observed that a disturbed State cannot with parity engage in competition with advanced or developed States. Therefore, the differential rate of taxation was

VERDICTUM.IN

upheld in the said case. The emphasis was on goods manufactured in the State having a concessional rate of tax irrespective of who manufactured the goods. The object was to attract industrial activity in the State as it was passing through a difficult phase and hence the need for a focus on economic development. Such a reason is conspicuous by its absence in the present case.

12.18.5 On the other hand in ***Shree Mahavir Oil Mills,*** it was observed that under Article 304(a), a State Legislature may tax goods imported from other States or Union Territories but in the process ought not to discriminate against them *vis-à-vis* goods manufactured locally. Therefore, there cannot be tax barriers or fiscal barriers in the interest of free trade, commerce and intercourse throughout the territory of India guaranteed by Article 301. Thus, the weapon of taxation cannot be used to discriminate against the imported goods *vis-à-vis* the locally manufactured goods.

12.18.6 Referring to ***Video Electronics,*** on which strong reliance was placed by State of Jammu and Kashmir in the aforesaid case, this Court made a distinction by observing that the

VERDICTUM.IN

said judgment created a limited exception and that it was not possible to go on extending the limited exception created in the said judgment, by stages which would have the effect of robbing the salutary principle underlying Part XIII of its substance. That States can also encourage growth of industries by all such means that are just and proper provided goods imported from other States are not discriminated against by a higher rate of sales tax being imposed. That the limited exception carved out in ***Video Electronics*** cannot be enlarged, "lest it would eat up the main provision". Placing reliance on ***Firm Mehtab Majid,*** this Court ruled in favour of the petitioners therein. ***Loharn Steel Industries Ltd., Laxmi Paper Mart*** have followed ***Shree Mahavir Oil Mills.***

12.18.7 In ***Jaiprakash Associates,*** while considering the question whether rebate is within the realm of tax defined under Article 304(a) so as to say that it discriminates between the two classes of goods, namely, locally manufactured goods and imported goods when both the classes of dealers meet the condition required to qualify for the grant of rebate i.e., use of fly ash, this Court noted that the overall effect or impact of such rebate would be on the manufacturer. Consequently, this Court held that "rebate of tax

VERDICTUM.IN

granted by the State Government to cement manufacturing units using fly ash as raw material in a unit established in the districts of the State of Uttar Pradesh alone was violative of the provisions contained in Articles 301 and 304(a) of the Constitution of India." This judgment squarely applies to the present cases.

12.18.8 While analysing Article 304(a) of the Constitution, the majority in the nine-Judge Bench in ***Jindal Stainless Ltd.*** identified two restrictions under Article 304(a) of the Constitution which are in the use of the expressions "*to which similar goods manufactured or produced in that State are subject*" and "*so, however, as not to discriminate between goods so imported and goods so manufactured or produced*". Therefore levy of taxes on goods imported from other States is constitutionally permissible so long as the State Legislature abides by the limitations placed on the exercise of that power. Thus, levy of taxes on import of goods from other States by itself, is not an impediment under the scheme of Part XIII of the Constitution.

12.18.9 With regard to ***Video Electronics,*** it was opined that so long as the differentiation is to benefit a distinct class of industries

VERDICTUM.IN

and not intended to create an unfavourable bias and if the differentiation is for a limited period, then, the benefit must be held to flow from a legitimate desire to promote industries within its territory. It was also held that ***Shree Mahavir Oil Mills*** was also distinguishable from ***Video Electronics.*** This was because the exemption for locally manufacturers of edible oil was discriminatory *vis-à-vis* other manufacturers from outside the State who had no benefit of the said exemption.

12.19 Applying the aforesaid dicta to the present cases, we find that the notification impugned in these cases are hit by the judgments referred to above and the judgment in ***Video Electronics*** being an exception having regard to the peculiar facts therein does not apply to the present cases. Therefore, the notification impugned in these cases dated 09.03.2007 is violative of Article 304(a) of the Constitution. Consequently, the impugned notification is quashed. The civil appeals are hence allowed. No cost.

12.20 Having regard to the interim order dated 09.05.2008 passed in these appeals, it is necessary to ascertain whether the

VERDICTUM.IN

differential amount which has been deposited before this Court was collected from their customers. If not, the appellants would be entitled to refund of the amount deposited with interest @ 6% per annum from the date of deposit till realisation. In order to ascertain this aspect, we post the appeals for directions.

All pending applications, if any, shall stand disposed of.

.....J.
(B.V. NAGARATHNA)

.....J.
(K.V. VISWANATHAN)

NEW DELHI;
SEPTEMBER 24, 2025.