THE HIGH COURT OF MADHYA PRADESH: JABALPUR

(Division Bench)

CEA No. 1/2013

APPELLANT : M/s Agrawal Colour Advance Photo System

Versus

RESPONDENTS : Commissioner of Central Excise and Another

WITH

CEA No. 2/2013

APPELLANT : M/s Agrawal Colour Quick System

Versus

RESPONDENTS : Commissioner of Central Excise and Another

AND

CEA No. 3/2013

APPELLANT : M/s Agrawal Colour Photo Industry

Versus

RESPONDENTS : Commissioner of Central Excise and Another

Coram:

Hon'ble Shri Justice Ajay Kumar Mittal, Chief Justice
Hon'ble Shri Justice Vijay Kumar Shukla, Judge

Appearance:

Shri Nitin Agrawal, Advocate for the appellants.

Shri Himanshu Shrivastava, Advocate for the respondents.

JUDGMENT (Oral)

[13.03.2020]

Per: Ajay Kumar Mittal, Chief Justice:

This judgment shall govern the disposal of CEA No.1/2013, CEA No.2/2013 and CEA No.3/2013 preferred by the appellants under Section

35G of the Central Excise Act, 1944 (hereinafter referred to as "the Act") against the common order dated 07.06.2012 passed by the Custom, Excise and Service Tax Appellate Tribunal, New Delhi (for short "the Tribunal") in Service Tax Appeal Nos.301/2006, 303/2006 and 302/2006 respectively, as common questions are involved therein and moreover, these appeals were admitted vide order dated 08.03.2012 on the common substantial questions of law, which read, thus:-

> "1. Whether, while providing photography service whether the use of the paper upon which an image is printed using certain consumables and chemicals, being incidental to the provision of service, amount to sale of goods in terms of Article 366(29A)(b) of the Constitution and whether value of photography service shall be determined in isolation of cost of such goods?
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> 2. Whether the term 'sale' appearing in exemption Notification No.12/03-ST dated 20.06.2003, is to be given the same meaning as given by Section 2(h) of the Central Excise Act, 1944, read with Section 65(121) of the Finance Act, 1994 or this term would also include the deemed "sale" as defined by Article 366(29A)(b) of the Constitution?

However, for the convenience sake, the facts are being extracted from CEA No.1/2013.

2. The appellant is engaged in the business of processing, printing and exposure of colour photographic film and obtained service tax registration for providing service on photography as provided under Section 65(63) of the Service Tax Chapter V of Finance Act, 1994 (for short "the Finance Act") made applicable to service tax w.e.f. 16.07.2001. During the scrutiny of ST-3 returns, it was found that the appellant had not paid the service tax

correctly. In reply to the notice, the appellant informed the Superintendent, Central Excise, Service Tax that it was paying service tax on 30% of the value of the invoices raised on account of service rendered to the customers and that the value of photography paper and processing chemicals used by it in developing of photographic films should be allowed to be deducted for the purposes of computing service tax liability as it falls in the category of storage device. The appellant also assailed the circular F No.B-11/01/2001-TRU dated 09.07.2001 whereby it was clarified that cost of photographic paper and chemicals is not excludable from the taxable value. The appellant was issued show cause notices for contravention of the provisions of the Finance Act inasmuch as not only the appropriate service tax was not paid but it also failed to produce material facts required for verification of the correctness of the service tax paid. It was proposed as to why service tax of ₹6,76,386/- for the period 16.07.2001 to 31.03.2005 should not be recovered on escaped 70% taxable value of ₹95,36,540/- under Section 73(a) along with the interest under Section 75 of the Act and penalty under Section 76 and 78 of the Act. Against the show cause notices the appellant preferred a writ petition before this Court being W.P. No.1433/2002 inter alia contending that the explanation to Section 67 of the Act did not include the cost of unexposed photography on recorded magnetic tapes on such other storage device if any sold to customers during the course of providing services. The said writ petition was dismissed vide order dated 22.03.2002 and against the same, letters patent appeal forming subject matter of LPA No.311/2002 also failed vide order dated 06.09.2005. Thereafter, the appellant appeared before the Adjudicating Authority and submitted that applicable service tax was paid on service part on photographic service and

in respect of balance amount which stands for material sold to customers they are exempted in terms of Notification No.12/2003-ST dated 20.06.2003. In this manner, the appellant was originally assessed by the Assessing Officer i.e. Assistant Commissioner, Central Excise Division, Jabalpur vide order dated 25.11.2005 (Annexure A-1) whereby relying upon the judgment of the Apex Court in Writ Petition (Civil) No.507/2002 (C.K. Jidheesh vs. Union of India), demand of service tax amounting to ₹6,76,386/- was levied on the appellant on the material consumed in the course of its business of photography along with equal penalty under Section 76 of the Act. The findings recorded by the Assistant Commissioner, are reproduced as under:-

> "Discussion & Findings:-
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> I have carefully gone through the case records & find that M/s Agrawal Colour, Advance Photo System Russel Chouk, Jabalpur is engaged in Photographic Service on which Service Tax was levied w.e.f. 16/07/2001. I observed that on this issue number of show cause notices have been issued. This issue has also been raised in the Supreme Court in the writ petition (civil) No.507 of 2002 (C.K. Jidheesh V/S U.O.I.) The honourable Supreme Court has turned down the petitioner's prayer for an order directing the Respondent to bifurcate the gross receipts or processing of photographs into the portion attributable to goods & that attributable to services. The petitioner claims that the respondent must tax only that portion of the receipts which is attributable to the services rendered. The Supreme Court has also held that contracts of the type entered into by persons like the petitioner are nothing else but services contracts pure & simple. It is held that in such contracts there is no element of sale of goods. In the light of the Supreme Court judgment the noticee's submission that they are correctly paying service tax is not correct. After considering every aspect of the case and respectfully following the Supreme Court's judgment I pass the following order….."

3. Against the order in original dated 25.11.2005, the appellant preferred an appeal before the Commissioner (Appeals), Custom & Central Excise,

Bhopal on the ground that it is paying service tax on service part of the photographic service and VAT/commercial tax on the balance amount representing material/printing material sold to its customers. The Commissioner (Appeals) vide order dated 17.04.2006 (Annexure A-2) although reduced the amount of penalty under Section 76 of the Act to the tune of ₹1,50,000/- from ₹6,76,386/- but affirmed the order of the Assessing Officer with the reasoning that under Section 65(105)(zb) of the Finance Act, taxable service would mean "any service provided or to be provided to a customer, by a photography studio or agency in relation to photography in any manner" and therefore, all services rendered relating to photography in any manner are covered under the ambit of photography services and therefore, liable to service tax. The relevant extract of the findings recorded by the Commissioner (Appeals) is reproduced as under:-

> "10…… When the photography services were first brought into the tax net with effect from 16.07.2001, there was confusion over the value of the photographic services. The Kerala Colour Lab Association had filed a Writ Petition before the Honourable High Court of Karnataka and the Honourable High Court had dismissed the petition filed vide their judgment dated 31.01.2002 as reported in 2003 (156) ELT (17) (Kar.) (Kerala Colour Lab Association vs. UOI), Honourable High Court, inter alia, upheld the constitutional validity of service tax on services rendered by photographic studios, etc. and held that the exclusion of cost of unexposed photographic film, unrecorded magnetic tape or such other storage devices sold to the client during the course of providing the services from the value of the taxable services was neither discriminatory nor violation of the fundamental rights guaranteed under Article 14 of the Constitution. This decision was later on affirmed by the Honourable Supreme Court in C.K. Jidheesh vs. UOI – 2006 (1) STR 3 (SC). Accordingly, the value of the taxable services would include the entire gross amount charged from the customer excluding only the cost of unexposed photographic film, unrecorded magnetic tape or such other

storage devices, if any, sold to the client during the course of providing the services.

11. The appellant, at the time of filing appeal against the Order-in-Original passed by the Divisional Assistant Commissioner, has raised a new ground that he is not providing any photography services, rather he is manufacturing excisable goods falling under chapter 37 & chapter heading 49.11 of the Central Excise Tariff Act, 1985. The short point to be decided here is that whether the activity of photographing persons/subjects, processing & developing of photographic films and printing of photographs etc. amounts to providing "photography services" under Section 65(78) of the Finance Act, 1994. The point raised by the appellant at this stage, about him being the manufacturer of excisable goods, is neither material here nor the subject matter of the present proceedings. In any case, this new point raised by the appellant at the appellate stage should be viewed in the background of the dismissal of his writ petition by the Honourable High Court of Jabalpur, as also the categorical decision of the Honourable Supreme Court mentioned in para supra. Under Section 35A of the Central Excise Act, 1944, I therefore, find this new ground of appeal to be both willful and unreasonable and as a result not deserving of consideration on this score alone.

12. Under Section 65(78), photography has been defined "to include still photography, motion picture photography, laser photography, aerial photography or fluorescent photography". Similarly, under section 65(79) ibid, photography studio or agency has been defined to mean "any professional photographer or a commercial concern engaged in the business of rendering services relating to photography". Under Section 65(105)(zb), ibid the taxable service would mean "any service provided or to be provided to a customer, by a photography studio or agency in relation to photography in any manner". From the above definitions, it is clear that any service rendered relating to photography in any manner is covered under the vast ambit of photography services as per the Act and as a result liable to service tax. The appellant, therefore, has to pay service tax on the activity undertaken by him as it was under the category of photography services. The appellant has also to pay the interest chargeable on the service tax amount. However, since the value of the taxable services was the subject matter of dispute, I am inclined to reduce the penalty imposed under Section 76 by the lower authority from ₹6,76,386/- to ₹1,50,000/- (Rupees One Lac & Fifty Thousand only)."

4. The order of the Commissioner (Appeals), thereafter, was assailed by the appellant by filing second appeal before the Tribunal on the ground that the law laid down in **C.K. Jidheesh vs. Union of India** (2005) 13 SCC 37, was overruled by the Larger Bench of the Apex Court in **Bharat Sanchar Nigam Limited vs. Union of India and others,** (2006) 3 SCC 1 wherein it was held that service tax can only be levied on the service portion and not on the cost of material. The Tribunal vide order dated 25.05.2010 (Annexure A-4) referred the matter to a Larger Bench by framing certain questions including the questions which are involved in this batch of appeals. The crux of the issues was: whether for the purpose of Section 67 of the Finance Act, the value of service provided in relation to photography would be the "gross amount charged" including the cost of material, goods used/consumed minus the cost of unexposed film. The Larger Bench of the Tribunal answered the questions against the appellant vide order dated 11.08.2011 (Annexure A-5) and held that unless documentary proof indicating the value of goods and material is submitted, the benefit of the Notification would not be available to the assessee. The burden of proof was on the assessee to establish the value of the goods and material. The Larger Bench while answering the questions referred to it, came to the conclusion that the gross value of service rendered is liable to service tax, as no amount is paid separately for photography service and the goods used and consumed in providing such taxable service. The relevant findings read as under:-

> "21. Service tax law is not the law relating to commodity taxation. The Notification in question issued under that law seeks to achieve that end by exempting value of goods sold while providing taxable service. There is no doubt that papers, consumables and chemicals are used and consumed to bring photographs into existence. It is also quite true that no service recipient goes to a photography service provider to buy paper, chemicals

and other photography materials. What the service recipient expects from the photography service provider is the photograph. No consideration is paid separately for photography service and the goods used and consumed in providing such taxable service. Value of photography service includes all elements bringing that to the deliverable stage. Consumables and chemicals used for providing such service disappear when the photograph emerges. The Hon'ble Supreme Court in C.K. Jidheesh's case (supra) has upheld levy of service tax on gross value in respect of photographic service after noting in paragraph 14 that in case of photographic service, it is a contract of service pure and simple and not a composite contract of sale of goods and service. It has also endorsed the decision of Hon'ble Kerala High Court in Kerala Colour Lab's case (supra). On the other hand, the decision of Hon'ble Supreme Court in the case of CCE vs. Surabhi Colour Lab (Civil Appeal No.263/2008, decided on 23.4.2009) has been rendered remanding the matter purely on the basis of an incorrect clarification issued by an officer of the Board, subsequently withdrawn. The decision of the Hon'ble Supreme Court in the case of CC&CE vs. Technica Colour Lab (Civil Appeal No.7060 of 2009) dated 21.7.2009 merely follows that of Surabhi Colour Lab (supra). Under the circumstances, we are bound to follow the ratio of Hon'ble Supreme Court's judgment in the case of C.K. Jidheesh (supra). As pointed out by the Ld. D.R., several Hon'ble High Courts have held that there is no sale or deemed sale of goods and material such as paper, chemical etc., in photographic service and hence disapproved levy of sales tax on part of the gross value of photographic service (vide Amar Kumar Birley v. State of Bihar (CWJ Case No.3932 of 1992) – Patna High Court, Studio Sujata v. CST – Orissa High Court, V.V. Jha v. State of Megahalaya – Gauhati High Court etc.). In Rainbow Colour Lab vs. State of M.P. (2000) 2 SCC 385, the Hon'ble Supreme Court has also taken the same view. As rightly pointed out by the ld. DR, the obiter contained in Bharat Sanchar Nigam Ltd (supra) does not overrule either C.K. Jidheesh (supra) or Rainbow Colour Lab (supra)."

Ultimately, in respect of the questions referred to it, the Larger Bench held, thus:-

"22. Hence, our answers to the two questions referred to in paragraph 3 above are as follows:-

(i) For the purpose of section 67 of the Finance Act, 1994, the value of service in relation to photography would be the gross amount

charged including cost of goods and material used and consumed in the course of rendering such service. The cost of unexposed film etc., would stand excluded in terms of *Explanation* to section 67 if sold to the client.

(ii) The value of other goods and material, if sold separately would be excluded under exemption Notification No.12/2003 and the term 'sold' appearing thereunder has to be interpreted using the definition of 'sale' in the Central Excise Act, 1944 and not as per the meaning of deemed sale under Article 366(29A)(b) of the Constitution."

23. On the aforesaid analysis of the legal position it can be said that determination of value of taxable service of photography depends on the facts and circumstances of each case as the Finance Act, 1994 does not intend taxation of goods and materials sold in the course of providing all the taxable services."

In view whereof, the appeal of the appellant was also dismissed vide impugned order dated 07.06.2012 (Annexure A-6), however, the penalty was set aside. In this manner, the present appeals have been preferred by the appellants.

5. Learned counsel for the appellants submitted that the value of photography paper and processing chemicals etc. are not a part of the value of the taxable services. According to him, the appellant is not liable to pay the service tax on the gross amount charged from its customers in lieu of photography service, which includes processing and developing of photographic films and printing of photographs etc. Learned counsel invited our attention to Article 366(29A) of the Constitution of India as amended vide 46th Amendment Act, 1982 whereby definition of "tax on the sale or purchase of goods" in Clause (29A) had been inserted. It was urged that Sub-clause (b) thereof provides for levy of tax on the transfer of property in goods whether as goods or in some other form involved in the execution of a works contract. Subsequent to the said amendment, the definition of 'sale' as

contained in the Central Sales Tax Act, 1956 and respective State Acts has also been adopted/amended so as to levy sales tax on sale or purchase of goods. On that basis it was argued that since the appellant has also paid VAT on the materials and consumables used in photography, therefore, it cannot be subjected to separate service tax on the same value of materials and consumables used in the course of its business of photography. In furtherance of the said argument, learned counsel submitted that the purpose of Notification No.12/2003-ST is to exempt the value of goods and materials, which are otherwise exigible to sales tax by the States, from the levy of service tax and therefore, subjecting the appellant to service tax on the same value of goods and materials on which it has paid the sales tax would amount to double taxation. Learned counsel contended that the material and consumables are transferred by the appellant to its customers which are embedded in the photographs and therefore, the appellant is entitled to claim deduction of value of material and consumables charged from its customers while paying service tax. The term “sold” used in Notification No.12/2003-ST dated 20.6.2003 must be interpreted to cover even a mere transfer of possession of goods for consideration by the appellant to its customers. By referring to Section 2(h) of the Act, it was submitted that any transfer of possession of goods by one person to another in the ordinary course of business or trade, would constitute sale for the purposes of the Act. On the aforesaid premises, it was claimed that the transfer of possession of photographs to the customers which are prepared with the photography paper upon which an image is printed using certain consumables and chemicals etc. constitutes a deemed sale for the purposes of exemption under Notification No.12/2003. It was also the contention of

the learned counsel that the intention to sell can be gathered from the invoices wherein the appellant has charged price of material and consumables and has paid VAT on the same. On this ground, it was the stand of the appellant that the finding recorded by the Tribunal that material and consumables embedded in the photographs given to the customer are consumed by them without transfer of possession of material and consumables for some consideration, is perverse. Lastly, it was projected that since the photography involves the processing activity, therefore, it is a works contract. There is an element of both sale and service in photography, thus, service tax would not be leviable on sale portion. In this regard, heavy reliance was placed upon the Apex Court decisions in **Bharat Sanchar Nigam Limited** (**supra**), **Gujarat Ambuja Cements Ltd. vs. Union of India and others,** (2005) 4 SCC 214 and **Imagic Creative Pvt. Ltd. vs. Commissioner of Commercial Taxes,** 2008 (8) STR 337.

6. Support was also gathered from the judgment in **Safety Retreading Company Private Limited vs. Commissioner of Central Excise, Salem**, (2017) 3 SCC 640 to show that gross turnover in respect of which the appellant-assessee has paid sales tax/VAT under State Act as works contractor is excluded from purview of service tax.

7. On the other hand, learned counsel for the respondents argued in support of the impugned orders. He contended that the finding recorded by the Larger Bench of the Tribunal is just and proper that since the consumables and chemicals used for providing photography service disappear when the photograph emerges and therefore, there is no element of sale involved on those consumables. It was contended that in photography

service, the contract is predominantly a service contract and the supply, if any, of material and consumables embedded in the photograph is merely incidental. Thus, rightly the benefit of the Notification No.12/2003-ST has not been extended to the appellant. In this regard, learned counsel also invited our attention to a clarificatory circular MF(DR) F No.233/2/2003-CX dated 3.3.2006 whereby the Notification No.12/2003-ST dated 20.6.2003 has been clarified in respect of service tax on photography services to mean that where the goods consumed during the provision of service are not available for sale by the service provider, the exemption in terms of Notification No.12/2003-ST dated 20.06.2003 will not be available.

8. Controverting the said stand of the learned counsel for the respondents, learned counsel for the appellants argued that even if the gross amount charged by the respondents is treated as value of taxable service, still the case of the appellants is covered by Notification No.12/2003-ST so far as the value of the material sold to the customers is concerned. The appellants have already submitted documentary proof in the form of invoices and further no Cenvat credit has been taken on the duty paid on the said goods.

9. Having heard learned counsel for the parties, we are of the considered view that the present appeals deserve to be allowed.

10. In view of the aforesaid factual background, a moot question before the learned Authorities below was: as to whether the appellant-assessee was entitled to the benefit of Notification No.12/2003-ST dated 20.06.2003. In order to appreciate the said controversy, it would be expedient to reproduce the relevant portion of the circular, which reads as under:-

> "*Notification No.12/2003-ST, dated 20-6-2003.* – In exercise of the powers conferred by section 93 of the Finance Act, 1994 (32 of 1994), the Central Government, being satisfied that it is necessary in the public interest so to do, hereby exempts so much of the value of all the taxable services, as is equal to the value of goods and materials sold by the service provider to the recipient of service, from the service tax leviable thereon under Section 66 of the said Act, subject to condition that there is documentary proof specifically indicating the value of the said goods and materials.
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> **Provided** that the said exemption shall apply only in such cases where-
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> (a) no credit of duty paid on such goods and materials sold, has been taken under the provisions of the Cenvat Credit Rules, 2004; or
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> (b) where such credit has been taken by the service provider on such goods and materials, such service provider has paid the amount equal to such credit availed before the sale of such goods and materials."

Perhaps there had been some representation from Punjab Color Lab Association, Jalandhar and thereafter, clarification was sought by certain photographic associations whether the value of materials consumed during the provision of service by the service provider for rendering the service is also excludable from the value of taxable service. Thereupon, a clarificatory circular MF(DR) F No.233/2/2003-CX dated 3.3.2006 was issued, which reads, thus:-

> "3. The matter has been examined by the Board. The intention of the Notification No.12/2003-ST dated 20.6.2003 is to provide exemption only to the value of goods and material sold subject to documentary evidence of such sale being available. Therefore, in case, the goods are consumed during the provision of service and are not available for sale, the provision of the said notification would not be applicable. Therefore, in supersession of clarification to contrary, it is clarified that goods consumed during the provision of service, that are not available for sale, by the service provider would not be entitled to benefit under Notification No.12/2003-ST dated 20.6.2003."

11. The contention of the assessee before the Tribunal was that the term "sale" in Notification dated 20.6.2003 includes "deemed sale" under Article

366(29A) of the Constitution and therefore, if a service contract is a works contract then no service tax can be charged on the goods component. The Tribunal while dealing with the arguments of both the sides and various pronouncements on the subject of valuation of photography services found that its earlier judgments required reconsideration and therefore, referred the matter to the Larger Bench. In respect of the Notification dated 20.6.2003, the referring Bench was of the view that in a service of photography there is no sale of goods involved and service element is dominant. The word 'sale' in the Notification has to be interpreted on the basis of its definition as given in section 2(h) of the Act, which by virtue of Section 65(121) of the Finance Act is applicable to service tax. It was further opined that when there is no primary intention of the parties to sell paper, consumable or chemical in providing photography service there is no room left to plead (fiction of Article 366(29A)(b) of the Constitution) in absence of any such sale of these commodities as goods. It further rejected the contention and held that the word "sale" in Notification would not cover "deemed sale" under Article 366(29A) of the Constitution and it is of no relevance inasmuch as Notification does not override statutory provision. The Larger Bench was in agreement with the said view when it held that expression "sold" in the Notification would not include "deemed sale" of goods and material consumed by the service provider while generating and providing service, unless an assessee has discharged burden of proof adducing evidence showing value of goods and material actually sold and satisfied the conditions of Notification. However, the Larger Bench opined that value of taxable service of photography depends on the facts and circumstances of

each case as the Finance Act does not intend taxation of goods and materials sold in the course of providing all the taxable services.

12. There is no dispute to the proposition that the Notification does not override the statutory provision and hence, it is required to be seen as to whether the conclusion drawn by the Tribunal that term 'sold' appearing in Notification has to be interpreted using the definition of 'sale' in the Central Excise Act, 1944 and not as per the meaning of "deemed sale" under Article 366(29A)(b) of the Constitution, is correct or not.

13. From the aforesaid discussion, it would emerge that the crux of the substantial question of law No.1 which has arisen for consideration is: "whether for the purposes of service tax the value of photography service can be determined separately from the value of certain consumables and chemicals which are used on the paper for printing the image and whether such printed photograph can be said to be a sale of goods in terms of Article 366(29A)(b) of the Constitution". In this regard, before considering the first limb of the contention of learned counsel for the appellants that in view of amended Article 366(29A) of the Constitution, the material and consumables used in photography will qualify as sale, it would be apt to refer to relevant clauses of the definition clause as contained in Article 366(29A) of the Constitution and other enactments, which read as under:-

> "366. (29-A) 'tax on the sale or purchase of goods' includes –
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> (a) *** *** ***
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> (b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;
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> *** *** ***"

The aforesaid definition of "sale" has been adopted by the M.P. VAT Act, 2002. Sub-clause (ii) of Section 2(u) of the said Act, which is relevant for the purposes of present controversy, is reproduced as under:-

> "2(u) "Sale" with all its grammatical variations and cognate expressions means any transfer of property in goods for cash or deferred payment or for other valuable consideration and includes–
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> *** *** ***
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> ii. a transfer of property in goods whether as goods or in some other form, involved in the execution of works contract;
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> *** *** ***

Section 2(h) of the Central Excise Act, 1944 defines "sale" and "purchase" as any transfer of possession for consideration by one person to another. Section 2(h) of the Act is reproduced as under:-

> "2(h) "sale" and "purchase", with their grammatical variations and cognate expressions, mean any transfer of the possession of goods by one person to another in the ordinary course of trade or business for cash or deferred payment or other valuable consideration;"

14. According to the learned counsel for the appellants, the material and consumables are embedded in the photograph when it is transferred to the customers. The Larger Bench of the Tribunal erroneously held that the consumables and chemicals used for providing such service disappear when the photograph emerges and concluded that value of photography service includes all elements which bring that to the deliverable stage. As noticed earlier, the stand of the appellants is that under sub-clause (b) of Clause (29A) of Article 366 of the Constitution, in execution of works contract, the tax which is paid on the sale or purchase of goods should be on the transfer of property in goods only. The photograph is completed through developing and printing process by using the consumables and chemicals, which are the

essential ingredients without which the photography cannot be completed. Therefore, when value of photography paper upon which an image is printed and certain consumables and material with which the photography is done, can be separated from the photography service then both the elements cannot be remixed for the purposes of service tax particularly when the VAT is levied on the material, consumables and chemicals which are used in the photography service.

15. However, it needs to be examined whether Article 366(29A)(b) of the Constitution is attracted in the present case, for which, it is to be necessarily seen whether the photography service is a works contract.

16. This aspect of the matter has been considered by a three-Judge Bench of the Apex Court in **Civil Appeal No.1145/2006 (State of Karnataka etc. vs. M/s Pro. Lab & others)** decided on 30th January, 2015 wherein challenge put-forth was to the constitutional validity of Entry 25 of Schedule VI to the Karnataka Sales Tax Act, 1957. The Apex Court took note of six sub-clauses of Clause (29A) of Article 366 of the Constitution of India and elaborately discussing its earlier decisions and the case law on the subject, rejected the contention of the State that processing of photography was a contract for service simplicitor with no element of goods at all and, therefore, Entry 25 could not be saved by taking shelter under clause 29-A of Article 366 of the Constitution. It was further observed that Entry 54 of List II of Schedule VII of the Constitution of India empowers the State Legislature to enact a law taxing sale of goods. Sales tax, being a subject matter into the State List, the State Legislature has the competency to

legislate over the subject. The relevant extract contained in paras 18 to 23 of the said judgment reads as under:-

> "18. It is amply clear from the above and hardly needs clarification that the Court was of the firm view that two Judges Bench judgment in *Rainbow Colour Lab and Another vs. State of Madhya Pradesh and others (2000) 2 SCC 385* did not lay down the correct law as it referred to pre 46th Amendment judgments in arriving at its conclusions which had lost their validity. The Court also specifically commented that after 46th Amendment, State is empowered to levy sales tax on the material used even in those contracts where "the dominant intention of the contract is the rendering of a service, which will amount to a Works Contract".
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> 19. In view of the above, the argument of the respondent assessees that *Associated Cement Companies Ltd. vs. Commissioner of Customs, (2001) 4 SCC 593*, (ACC Ltd. case) did not over-rule Rainbow Colour Lab's case (supra) is, therefore, clearly misconceived. In fact, we are not saying so for the first time as a three member Bench of this Court in *M/s Larsen and Toubro and Another vs. State of Karnataka and another (2014) 1 SCC 708* has already stated that ACC Ltd. had expressly over-ruled Rainbow Colour Lab while holding that dominant intention test was no longer good test after 46th Constitutional Amendment. We may point out that learned counsel for the respondent assessees took courage to advance such an argument emboldened by certain observations made by two member Bench in the case of C.K. Jidheesh v. Union of India, wherein the Court has remarked that the observations in ACC Ltd. were merely obiter. In Jidheesh, however, the Court did not notice that this very argument had been rejected earlier in *Bharat Sanchar Nigam Ltd. v. Union of India (2006) 3 SCC 1*. Following discussion in Bharat Sanchar is amply demonstrative of the same:
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> > "46. This conclusion was doubted in Associated Cement Companies Ltd. v. Commissioner of Customs, (2001) 4 SCC 593 saying:
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> > > "The conclusion arrived at in Rainbow Colour Lab case (2000) 2 SCC 385, in our opinion, runs counter to the express provision contained in Article 366(29A) as also of the Constitution Bench decision of this Court in Builders Assn. of India v. Union of India - (1989) 2 SCC 645.
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> > 47. We agree. After the 46th Amendment, the sale element of those contracts which are covered by the six sub-clauses of Clause (29A) of Article 366 are separable and may be subjected to sales tax by the States under Entry 54 of List II and there is

> no question of the dominant nature test applying. Therefore, in 2005, C.K. Jidheesh v. Union of India - (2005) 8 SCALE 784 held that the aforesaid observations in Associated Cement (supra) were merely obiter and that Rainbow Colour Lab (supra) was still good law, it was not correct. It is necessary to note that Associated Cement did not say that in all cases of composite transactions the 46th Amendment would apply"

20. In M/s Larsen and Toubro, the Court, after extensive and elaborate discussion, once again specifically negated the argument predicated on dominant intention test having regard to the statement of law delineated in ACC Ltd. and Bharat Sanchar Nigam Ltd. cases. The reading of following passages from the said judgment is indicative of providing complete answer to the arguments of the respondent assessees herein: "64. Whether contract involved a dominant intention to transfer the property in goods, in our view, is not at all material. It is not necessary to ascertain what is the dominant intention of the contract. Even if the dominant intention of the contract is not to transfer the property in goods and rather it is the rendering of service or the ultimate transaction is transfer of immovable property, then also it is open to the States to levy sales tax on the materials used in such contract if it otherwise has elements of works contract. The view taken by a two-Judge Bench of this Court in Rainbow Colour Lab (supra) that the division of the contract after Forty-sixth Amendment can be made only if the works contract involved a dominant intention to transfer the property in goods and not in contracts where the transfer of property takes place as an incident of contract of service is no longer good law, Rainbow Colour Lab (supra) has been expressly overruled by a three-Judge Bench in Associated Cement.

> 65. Although, in Bharat Sanchar, the Court was concerned with Sub-clause (d) of Clause 29A of Article 366 but while dealing with the question as to whether the nature of transaction by which mobile phone connections are enjoyed is a sale or service or both, the three-Judge Bench did consider the scope of definition in Clause 29A of Article 366. With reference to Sub-clause (b) it said: "Sub-clause (b) covers cases relating to works contract. This was the particular fact situation which the Court was faced with in Gannon Dunkerley-I (*State of Madras vs. Gannon Dunkerley & Co., AIR 1958 SC 560)* and which the Court had held was not a sale. The effect in law of a transfer of property in goods involved in the execution of the works contract was by this amendment deemed to be a sale. To that extent the decision in Gannon Dunkerley-I was directly overcome". It then went on to say that all the Sub-clauses of Article 366 (29A) serve to bring transactions where essential ingredients of a 'sale' as defined in the Sale of Goods Act, 1930 are absent, within the ambit of purchase or sale for the purposes of levy of sales tax.
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> 66. It then clarified that Gannon Dunkerley-I survived the Forty-sixth Constitutional Amendment in two respects. First, with

regard to the definition of "sale" for the purposes of the Constitution in general and for the purposes of Entry 54 of List II in particular except to the extent that the clauses in Article 366(29A) operate and second, the dominant nature test would be confined to a composite transaction not covered by Article 366(29A). In other words, in Bharat Sanchar, this Court reiterated what was stated by this Court in Associated Cement that dominant nature test has no application to a composite transaction covered by the clauses of Article 366(29A). Leaving no ambiguity, it said that after the Forty- sixth Amendment, the sale element of those contracts which are covered by six Sub-clauses of Clause 29A of Article 366 are separable and may be subjected to sales tax by the States under Entry 54 of List II and there is no question of the dominant nature test applying.

67. In view of the statement of law in Associated Cement and Bharat Sanchar, the argument advanced on behalf of the Appellants that dominant nature test must be applied to find out the true nature of transaction as to whether there is a contract for sale of goods or the contract of service in a composite transaction covered by the clauses of Article 366(29A) has no merit and the same is rejected.

68. In Gannon Dunkerley-II (*Gannon Dunkerley and Co. and others vs. State of Rajasthan and others (1993) 1 SCC 364)*, this Court, inter alia, established the five following propositions: (i) as a result of Forty-sixth Amendment the contract which was single and indivisible has been altered by a legal fiction into a contract which is divisible into one for sale of goods and the other for supply of labour and service and as a result of such contract which was single and indivisible has been brought on par with a contract containing two separate agreements; (ii) if the legal fiction introduced by Article 366(29A)(b) is carried to its logical end, it follows that even in a single and indivisible works contract there is a deemed sale of the goods which are involved in the execution of a works contract. Such a deemed sale has all the incidents of the sale of goods involved in the execution of a works contract where the contract is divisible into one for sale of goods and the other for supply of labour and services; (iii) in view of Sub- clause (b) of Clause 29A of Article 366, the State legislatures are competent to impose tax on the transfer of property in goods involved in the execution of works contract. Under Article 286(3)(b), Parliament has been empowered to make a law specifying restrictions and conditions in regard to the system of levy, rates or incidents of such tax. This does not mean that the legislative power of the State cannot be exercised till the enactment of the law under Article 286(3)(b) by the Parliament. It only means that in the event of law having been made by Parliament under Article 286(3)(b), the exercise of the legislative power of the State under Entry 54 in List II to impose tax of the nature referred to in Sub-clauses (b), (c) and (d) of Clause (29A) of Article 366 would be subject to restrictions and conditions in regard to the system of levy, rates and other incidents of tax contained in the said law; (iv) while enacting law imposing a tax on sale or purchase of goods under Entry 54 of the State List read with Article 366(29A)(b), it is permissible for the State legislature to make a law imposing tax on such a deemed sale which constitutes a sale in the course of the inter-state trade or commerce under Section 3 of the Central Sales Tax Act or

> outside under Section 4 of the Central Sales Tax Act or sale in the course of import or export under Section 5 of the Central Sales Tax Act; and (v) measure for the levy of tax contemplated by Article 366(29A)(b) is the value of the goods involved in the execution of a works contract. Though the tax is imposed on the transfer of property in goods involved in the execution of a works contract, the measure for levy of such imposition is the value of the goods involved in the execution of a works contract. Since, the taxable event is the transfer of property in goods involved in the execution of a works contract and the said transfer of property in such goods takes place when the goods are incorporated in the works, the value of the goods which can constitute the measure for the levy of the tax has to be the value of the goods at the time of incorporation of the goods in works and not the cost of acquisition of the goods by the contractor.
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> 69. In Gannon Dunkerley-II, Sub-section (3) of Section 5 of the Rajasthan Sales Tax Act and Rule 29(2)(1) of the Rajasthan Sales Tax Rules were declared as unconstitutional and void. It was so declared because the Court found that Section 5(3) transgressed the limits of the legislative power conferred on the State legislature under Entry 54 of the State List. However, insofar as legal position after Forty-sixth Amendment is concerned, Gannon Dunkerley-II holds unambiguously that the States have now legislative power to impose tax on transfer of property in goods as goods or in some other form in the execution of works contract.
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> 70. The Forty-sixth Amendment leaves no manner of doubt that the States have power to bifurcate the contract and levy sales tax on the value of the material involved in the execution of the works contract. The States are now empowered to levy sales tax on the material used in such contract. In other words, Clause 29A of Article 366 empowers the States to levy tax on the deemed sale."

21. To sum up, it follows from the reading of the aforesaid judgment that after insertion of clause 29-A in Article 366, the Works Contract which was indivisible one by legal fiction, altered into a contract, is permitted to be bifurcated into two: one for "sale of goods" and other for "services", thereby making goods component of the contract exigible to sales tax. Further, while going into this exercise of divisibility, dominant intention behind such a contract, namely, whether it was for sale of goods or for services, is rendered otiose or immaterial. It follows, as a sequitur, that by virtue of clause 29-A of Article 366, the State Legislature is now empowered to segregate the goods part of the Works Contract and impose sales tax thereupon. It may be noted that Entry 54, List II of the Constitution of India empowers the State Legislature to enact a law taxing sale of goods. Sales tax, being a subject-matter into the State List, the State Legislature has the competency to legislate over the subject.

22. Keeping in mind the aforesaid principle of law, the obvious conclusion would be that Entry 25 of Schedule VI to the Act which makes that part of processing and supplying of photographs, photo prints and photo negatives, which have "goods" component exigible to sales tax is constitutionally valid. Mr. Patil and Mr. Salman Khurshid, learned senior counsel who argued for these assessees/respondents, made vehement plea to the effect that the processing of photographs etc. was essentially a service, wherein the cost of paper, chemical or other material used in processing and developing photographs, photo prints etc. was negligible. This argument, however, is founded on dominant intention theory which has been repeatedly rejected by this Court as no more valid in view of 46th Amendment to the Constitution.

23. It was also argued that photograph service can be exigible to sales tax only when the same is classifiable as Works Contract. For being classified as Works Contract the transaction under consideration has to be a composite transaction involving both goods and services. If a transaction involves only service i.e. work and labour then the same cannot be treated as Works Contract. It was contended that processing of photography was a contract for service simplicitor with no elements of goods at all and, therefore, Entry 25 could not be saved by taking shelter under clause 29-A of Article 366 of the Constitution. For this proposition, umbrage under the judgment in B.C. Kame's case (*Assistant Sales Tax Officer and others vs. B.C. Kame, Proprietor Kame Photo, AIR 1977 SC 1642*) was sought to be taken wherein this Court held that the work involving taking a photograph, developing the negative or doing other photographic work could not be treated as contract for sale of goods. Our attention was drawn to that portion of the judgment where the Court held that such a contract is for use of skill and labour by the photographer to bring about desired results inasmuch as a good photograph reveals not only the asthetic sense and artistic faculty of the photographer, it also reflects his skill and labour. Such an argument also has to be rejected for more than one reasons. In the first instance, it needs to be pointed out that the judgment in Kame's case was rendered before the 46th Constitutional Amendment. Keeping this in mind, the second aspect which needs to be noted is that the dispute therein was whether there is a contract of sale of goods or a contract for service. This matter was examined in the light of law prevailing at that time, as declared in Dunkerley's case as per which dominant intention of the contract was to be seen and further that such a contract was treated as not divisible. It is for this reason in BSNL and M/s Larsen and Toubro cases,

this Court specifically pointed out that Kame's case would not provide an answer to the issue at hand. On the contrary, legal position stands settled by the Constitution Bench of this Court in Kone Elevator India Pvt. Ltd. v. State of Tamil Nadu and Ors. (2014) 7 SCC 1. Following observations in that case are apt for this purpose:

> "On the basis of the aforesaid elucidation, it has been deduced that a transfer of property in goods under Clause (29A)(b) of Article 366 is deemed to be a sale of goods involved in the execution of a Works Contract by the person making the transfer and the purchase of those goods by the person to whom such transfer is made. One thing is significant to note that in Larsen and Toubro (supra), it has been stated that after the constitutional amendment, the narrow meaning given to the term "works contract" in Gannon Dunkerley-I (supra) no longer survives at present. It has been observed in the said case that even if in a contract, besides the obligations of supply of goods and materials and performance of labour and services, some additional obligations are imposed, such contract does not cease to be works contract, for the additional obligations in the contract would not alter the nature of the contract so long as the contract provides for a contract for works and satisfies the primary description of works contract. It has been further held that once the characteristics or elements of works contract are satisfied in a contract, then irrespective of additional obligations, such contract would be covered by the term "works contract" because nothing in Article 366(29A)(b) limits the term "works contract" to contract for labour and service only."

17. The view expressed by the Apex Court in **Bharat Sanchar Nigam Limited**'s case (supra) that after the 46th Amendment, the sale element of those contracts which are covered by the six sub-clauses of clause (29A) of Article 366 are separable and may be subjected to sales tax by the States under Entry 54 of List II and there is no question of the dominant nature test applying, was reiterated by the Apex Court in **M/s Pro. Lab**'s case **(supra)**.

Thus, the finding of the Tribunal that in **Bharat Sanchar Nigam Limited**'s case (**supra**) the Apex Court has only given the passing remarks and did not overrule either **C.K. Jidheesh** (**supra**) or **Rainbow Colour Lab and Another vs. State of Madhya Pradesh and others,** (2000) 2 SCC 385, is unsustainable, as it had been categorically held in **Bharat Sanchar Nigam Limited**'s case (**supra**) that these judgments do not lay down correct law.

18. The next contention of the learned counsel for the appellants was that appellants having once paid the VAT under the State Act as works contractor on the material and chemicals consumed in photography service, cannot be charged service tax on the same value. To bolster his submission, he placed reliance upon the judgment in **Safety Retreading Company Private Ltd**. (**supra**). In the facts of the said case, the assessee was engaged in business of tyres on job work basis and had been paying 30% service tax only on the labour component shown in invoices after deducting 70% towards material cost on the gross re-treading charges billed in terms of Notification No.12/03-ST dated 20.06.2003. A show cause notice dated 24.01.2008 was issued to the assessee alleging suppression of value of taxable services with intention to evade payment of service tax and proposing recovery of service tax together with interest and penal action under the provisions of Sections 76, 76 and 78 of the Finance Act, 1994. The said deduction of 70% was denied by the Commissioner and demand of service tax was confirmed on the assessee along with interest and penalty. The appeal preferred by the assessee was considered and decided by a three-member Special Bench of the Tribunal reported as **Safety Retreading Company (P) Ltd. vs. Commissioner of Central Excise, Salem (2012) 34 STT 64 (Chennai)**,

wherein coupled with the Notification No.12/2003-ST dated 20.06.2003 a similar issue was considered by the Larger Bench of the Tribunal: "whether in a contract for retreading of tyres, service tax is leviable on the total amount charged for retreading including the value of the materials/goods that have been used and sold in the execution of the contract or exemption to material component therein can be granted". The question was whether maintenance and repair service can be treated as service under "works contract" for service tax purposes. The Appellate Tribunal by majority view, upheld the demand, inter alia, on the ground that 'maintenance and repair service' being a specific service is to be treated as service under "works contract" for service tax purposes. On appeal, the Apex Court set aside the said majority view of the Special Bench of the Tribunal and held that Section 67 of the Finance Act clarifies that costs of parts or other material, if any, sold (deemed sale) to customer while providing maintenance or repair service is excluded from service tax subject to furnishing adequate and satisfactory proof by the assessee and this position has been further clarified in Notification dated 20.06.2003 and CBEC circular dated 7.4.2004. It was held that component of gross turnover in respect of which assessee had paid taxes under local Act with which it has registered as works contractor is excluded from service tax.

19. In view of the law laid down by the Apex Court in **M/s Pro. Lab**'s case (**supra**), it can be safely held that photography service, which has both the elements of goods and services is covered under works contract. Thus, in a works contract which involves transfer of property, the provisions as contained in Article 366(29A) of the Constitution are attracted. Therefore, in

the light of sub-clause (b) of Clause (29A) of Article 366 of the Constitution, in execution of a works contract when there is transfer of property even in some other form than in goods, the tax on such sale or purchase of goods is leviable. In this view of the matter, after the 46th Amendment, there is no question of dominant nature test applying in photography service and the works contract, which is covered by Clause (29A) of Article 366 of the Constitution where the element of goods can be separated, such contracts can be subjected to sales tax by the States under Entry 54 of List II of Schedule II. Once that is so, value of photographic paper and consumables cannot be included in the value of photography service for the purposes of imposition of service tax. Thus, in the light of the judgment of the Apex Court in **M/s Pro Lab** (**supra**), wherein it is held that part of processing and supplying of photographs, photo prints and negatives, which have "goods" component exigible to sales tax is constitutionally valid, it is held that value of photography service has to be determined in isolation of cost of goods such as photography paper, consumables and chemicals with which image is printed, negatives and other material which has "goods" component liable to sales tax. Accordingly, the substantial question of law No.1 is answered in favour of the assessee and against the Revenue.

20. Having answered the substantial question of law No.1 in favour of the assessee, the substantial question of law No.2, which already stands concluded while dealing with the question of law No.1, is also answered in favour of the assessee and it is held that the term 'sale' appearing in exemption Notification No.12/03-ST dated 20.06.2003 would also include "deemed sale" as defined by Article 366(29A)(b) of the Constitution.

21. For the reasons stated hereinabove, the impugned orders are set aside and the present appeals stand allowed. Let a signed order be placed in the file of CEA No.1/2013 and copy whereof be placed in the files of connected appeals.

(Ajay Kumar Mittal)
Chief Justice

(Vijay Kumar Shukla)
Judge

S/