CHAPTER III
TAKING POWERS OF THE UNION AND THE STATES UNDER THE INDIAN CONSTITUTION

INTRODUCTION

India, that is Bharat, is a 'Union of States'. Significantly the word Federal has been omitted from the text of the Constitution. Thus the Constitution of India established a 'Union of States'. The term 'Union of States' as used in our Constitution was made clear by Dr. Ambedkar, who while moving the draft Constitution in the Constituent Assembly on November 4, 1948 said, 'the draft Constitution is Federal Constitution in as much as it established what may be called dual polity. The dual polity under the Constitution will consist of the Union and States at the periphery each endowed with sovereign powers to be exercised in the field assigned to them respectively in the Constitution.'

In a Federal set up, no doubt the National Government is superior either politically or financially as compared to its Constituent Units, yet both of them function in coordination to serve the common ends. A Federation

1. Constitution of India, Article 1(1).
is established as a result of series of compromises and an important aspect of the compromise is expressed through the division and separation of powers, often outlined in a Constitution.

A written Constitution dividing the functional powers and sources of revenue between the National Government and its units is a *sine qua non* of a Federation. The division of powers between the Union and States is thus an essential feature of Federation. This distribution is effected by the Federal Constitution in order to avoid chaos and conflicts between the two competing jurisdictions. In a Federal set up economy, efficiency and administrative convenience are the leading principles in the distribution of functions between the two layers of government. In fact, the essence of Federalism lies in proper division of powers between the various levels of government, of these however, finances are the backbone of political economic strength and thus essential pre-requisite of a government. The division of functions

5. *Supra* note 3 at 12.
require division of resources also. The division of resources is governed by the principle of division of functions as K.T. Shah rightly observed, 'financial resources placed at the disposal of either have to correspond to the functions and obligations assigned to them'.

The Constitution of India is a Federal Constitution as it established a dual polity, a two tier governmental system with the Central Government at one level and the State Governments at the other end. The Constitution demarcates the extensive field of operation of each organ of government by devising an elaborate scheme of distribution of revenue and resources.

In this chapter an attempt has been made to critically examine the taxing powers of the Union and the States.

(A) Division of Taxing Powers

Federation being a device for distributing powers and functions between the Central and Regional Governments, a division of taxing powers between these governments is a

necessary corrolory. The object of dividing taxing powers is to secure adequate resources for each of them and provide necessary and desired freedom and flexibility in their efficient operations consistently with the needs of unity and security.

A sound Federal system, therefore, envisages that taxing power between the Centre and States are allocated in such a way that there exists a balance, an equilibrium between the functions and resources at each governmental level. Absence of such a balance may create strains and stresses within the Federal polity making it unstable and jeopardise its smooth functioning.

The allocation of fields of taxation between the Union and States is designed to promote maximum possible efficiency in tax administration without impairing economic unity of the nation.

Since Indian Constitution is largely based on Government of India Act 1935, thus the present division of

13. Supra note 11 at 294.
taxing powers is virtually a product of history. It was Montague Chelmsford who initiated the process of separation between tax resources of the Centre and States and the process was completed under Government of India Act 1935. In fact our Constitution effects a complete separation between the taxing powers of Centre and State Governments. Since the Constitution demarcates the sources of taxes of each level of government, hence our Constitution is a true Federal Constitution. While effecting division of taxing powers, the framers had allotted those taxes which have inter State base to the Union and those having regional base are assigned to States. Thus the taxes with wide economic base had been assigned to the Union Government and the taxes which touch intimately the lives of people had been assigned to the States under the Constitution of India.

The Constitution provides for the following types of taxing power:

1. Taxing Power of the Union
2. Taxing Power of the States.
3. Taxing Power under the Concurrent List.
4. Residuary Taxing Power.

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15. K. Santhanam, 'Union State Relations in India', 30 (1960).
(1) **Taxing Power of the Union**

The Parliament had been given exclusive power to levy taxes on those entries which are contained in Union List. The tax entries as contained in the Union List are follows:

**Entry 82 - Taxes on income other than agricultural income**

Entry 82 gives exclusive power to the Union to levy tax on non-agricultural income whereas the tax on agricultural income has been assigned to States under entry 46, List II. The Constitution of India does not define the term "income" but when interpreted literally and grammatically it means, "a thing that comes in." The Supreme Court of India while interpreting the term 'income' had given it wider meaning so as to include any profit or gain which is actually received. Thus this entry includes any tax on capital gains or pensions. However, Parliament can not choose to tax an item which in no rational sense can be regarded as a citizen's income. In **Navnit Lal v. Appellate Assistant Commissioner of Income Tax**, the Supreme Court has held that a loan advanced to a share holder of a company can not be treated as his income and hence


21. Supra note 19 at 1178.

22. AIR 1965 SC 1375.
cannot be taxed. While giving the entry widest interpreta-
tion, the Supreme Court has held that computation of income
of the assessee from any property is the income for the
purpose of Income-tax. Besides a tax on income includes
a tax in the nature of an excess profits tax.

Entry 83 - Duties of customs including export duty

Under this entry Parliament has been given power
to levy custom duty including export duty on all those items
which may either be imported into the country or exported from
the country.

Entry 84 - Duties of customs on tobacco and other goods
manufactured or produced in India except

(a) alcoholic liquors for human consumption; (b) opium,
Indian hemp and other narcotic drugs and narcotics but including
medicinal and toilet preparations containing alcohol or any
other substance included in sub paragraph (b) of this entry.

The excise duty had been divided between Union
and States and those items which are excluded from the purview

of Union had been assigned to the States for levying excise duty. The term duties of excise, if interpreted literally may include 'sales tax' also which is an entry in the Provincial List. The question how to reconcile between both entries was considered by the Supreme Court in a special reference case named re the Central Provinces and Bearer Act No.XIV of 1938. In this case the Provinces levied a sale tax under sec.3(1) of the Provincial Act on retail sales of petrol and lubricant. The tax as levied by the Provinces was challenged by Central Government, on the ground that it was an excise duty and not 'sales tax'. The Federal Court while rejecting the plea of Central Government held that primary and fundamental meaning of the term 'excise' is that of tax on articles produced and manufactured in a country. Thus the court restricted the term 'excise duty', to be a duty on manufacture or production of goods. However, both the manufacturer and producer of goods can be asked to pay excise duty to Centre and sales tax to States in respect of sales of goods produced by him. An excise duty may be collected at any stage subsequent to its manufacture or production. The excise duty may even be

25. AIR 1939 F C.I.

26. Ibid., at 6.


collected at the consumption stage. The Calcutta High Court in *Aluminium Corporation v. Coal Board* has held that though coal is a national product yet the operation required for making it usable are expensive and hence it may be regarded as goods produced and thereby covered under entry 84.

The *Central Excise and Salt Act 1944* as enacted by Parliament when challenged before Supreme Court on the ground that it encroaches upon entries 26 and 27 of the List II, the Supreme Court held that the Act is a fiscal measure to levy and realise duty on tobacco and that Parliament's power of taxation should not be restricted so as to exclude the raising of revenue by imposing licence fees. Similarly, in another case named *M.B.S. Oushdhalava v. Union of India* the Supreme Court has held that 'Mritosanjivani' is a medicinal preparation containing alcohol and hence falls under this entry. Prior to 1973, the excise duty was being computed on the manufacturer's price but after 1973, the *Central Excise and Salt Act* had been amended so as to include post manufacturing expenses also. In a recent case, when this amendment
was challenged before Supreme Court, the court has upheld this broader concept whereby the revenue resources of the Centre had been enlarged to a great extent.

**Entry 25 - Corporation tax**

The 'Corporation Tax' has been defined to mean any tax on income payable by companies and is a tax in the case of which the following conditions are fulfilled.

(a) that it is not chargeable in respect of agricultural income.

(b) that the companies paying the tax are not authorised to deduct the same from dividends payable by the companies to individuals.

(c) that no provision exists for taking the tax so paid into account in computing for the purposes of income-tax the total income of individuals receiving such dividends, or in computing the income tax payable by or refundable to such individuals.

The corporation tax is the most elastic source of revenue of the Union and the States are not being given


any share of this source of revenue.

**Entry 86 - Taxes on capital value of the assets, exclusive of agricultural land of individuals and companies; taxes on the capital of companies**

The Supreme Court in *Sudhir Chandra Nawn v. The Wealth Tax Officer Calcutta* defined the term 'taxes on capital value of assets' as a tax on the total assets owned by the assessee as distinguished from a tax on the components of the assets. The Parliament had been authorised to levy wealth tax under this entry and the Parliament while exercising the power under this entry enacted **Wealth Tax Act, 1957**. The Act as such was challenged before Supreme Court on the ground that expression 'net wealth' includes non-agricultural lands and buildings of an assessee and power to levy tax on lands and buildings were reserved to State legislation by entry 49, List II, 7th Schedule, hence Parliament was incompetent to legislate for the levy of wealth tax on the capital value of assets which included agricultural lands and buildings. Rejecting this contention the Supreme Court has held that the tax imposed by entry 86, List I was not directly a tax on lands and buildings but it was a tax


imposed on the total capital value of assets including lands and buildings minus the debts and liabilities. The term 'individuals' as used in the entry includes a Hindu undivided family.

**Entry 87 - Estate duty in respect of property other than agricultural land**

Estate duty on any property other than agricultural land can be levied by the Parliament under entry 87. Clause (9) of Article 366 defines the term 'estate duty' as a duty to be assessed on or by reference to the principal value ascertained in accordance with such rules as may be prescribed by or under laws made by Parliament or the Legislature of a State relating to the duty of property passing upon death or demand, under the provisions of said laws, so to pass.

**Entry 88 - Duties in respect of succession to property other than agricultural land**

This entry is to be read with entry 87. Under entry 88 Parliament had been authorised to levy a duty on succession to any property other than agricultural land. The common element between both duties is that the occasion for their levy is the death of a person. While the 'estate duty' has reference to the value of the property constituting

37. Ibid., at 61.
38. Supra note 11 at 298.
the estate of a deceased, whereas 'succession duty' relates to the extent or benefit derived by the succession. Thus the 'estate duty' is levied on the property itself and it has no relevance who takes it. The 'succession and estate duty' is also a divided subject as 'succession and estate duty' on non agricultural property falls within the Central power whereas the duty on agricultural property falls within the States power. Prior to 1953, the 'estate duty' could only be levied on non agricultural property and agricultural property could not be taxed. To have uniformity in 'estate duty', the Parliament while exercising power under Article 252 had legislated 'Estate Duty Act, 1953', which provides for imposition of 'estate duty' on agricultural and non agricultural property.

Entry 89 - Terminal taxes on goods or passengers carried by railway, sea or air; taxes on railway fares and freights

The Parliament had been empowered to impose terminal taxes on goods or passengers which may be carried either by railway, sea or air and taxes on railway fares and

39. In re Estate Duty, AIR 1944 FC 73.

freights under this entry. However, this tax must be (i) terminal (ii) confined to goods and passengers carried by railway, sea or air (iii) chargeable at a rail, sea or air terminus and (iv) be referable to services rendered by some railway, sea or air transport organisation. However, the tax under this entry is not related to the fact whether the goods subjected to tax are being used locally or not.

**Entry 90 - Taxes other than stamp duties on transactions in stock exchanges and future markets**

Under this entry, Parliament has been given power to levy any tax other than stamp duties on any transaction in stock exchanges and future markets. This wide power had been given to the Parliament keeping in view the far reaching effects of stock exchange transactions on public credit and finance.

**Entry 91 - Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipts.**

**Entry 92 - Taxes on the sale or purchase of newspapers and on advertisements published therein.**
Although general sales tax is a State subject, yet the sales tax on newspapers has been made a Central subject. This has been done with a view to protect newspapers from indiscriminate taxation.

**Entry 92-A** - Taxes on the sale or purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce.

This entry was not originally in the Constitution rather it had been added by **Sixth Amendment Act of 1956**, on the recommendations of Taxation Enquiry Committee appointed in 1953. Although the Committee recommended that sales tax must continue with the States and the States should levy and administer it but it also recommended that inter-State sale of goods other than newspapers should be within the ambit of Union.

Clause (1)(g) of Article 269 serves as a proviso to this entry as it provides that under this entry no doubt the Centre is authorised to levy and collect taxes, yet the total net proceeds are to be given to the States in whose

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41. Seventh Schedule, List II, Entries 53 and 54.
42. Supra note 35 at 203.
Entry 92-B - Taxes on the consignment of goods (whether the consignment is to the person making it or any other person) where such consignment takes place in the course of inter-State trade or commerce.

Entry 96 - Fees in respect of any of the matter but not including fees taken in any court, except Supreme Court.

Fees taken in other than Supreme Court is a State subject and the fees taken in Supreme Court is a Central subject. The present entry relates to any fee that may be charged in respect of any matter contained in the Union List.

Entry 97 - Any other tax not contained in List II & III

By virtue of this entry the Union becomes vested with the residuary powers to levy any tax which does not fall either under List II and List III. This entry is in line with Article 248 which makes the union repository of residuary powers.

44. This entry was not originally in the Constitution, it has been added by Forty-sixth Amendment Act, 1982.
(II) **Taxing Power of the States**

Unlike Union, States had also been given exclusive power to levy taxes on the following entries of List II of 7th Schedule. The entries are:

**Entry 45 - Land revenue including its assessment and collection**

The States had been given exclusive power to levy land revenue. This power includes assessment and collection of revenue, maintenance of land records, power to conduct surveys for revenue purposes and records of rights and alienation of revenues. Land revenue is a tax on net produce of land which is levied at a flat rate with no exemption limit, it is not a rent for land. The Gujarat High Court has held that the expression 'Land records' is to be construed in a broad sense. During British days land revenue was the most lucrative source of tax of the Provinces but now because of political reasons it had lost its importance as the amount being collected by the Provinces in the shape of land revenue is meagre. It is because of this reason that Planning Commission in its various reports

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had stressed to raise additional resources from the agricultural sector.

Entry 46 - Taxes on agricultural income

Whereas the levying of income tax generally comes within the purview of Parliament, levying of agricultural income tax comes within the competence of taxing powers of the States. 'agricultural income', has been defined to mean agricultural income as defined for the purposes of the enactments relating to Indian income-tax. Thus the Parliament had been given power, to define the term 'agricultural income' and Parliament while exercising this power had defined the term in Indian Income-tax Act as any rent or revenue derived from land which is situated in India and is used for agricultural purposes. This definition is a controlling for the States and the States legislature can not extend their jurisdiction by adopting a wider definition of the term 'agricultural income'. For modifying the definition, a bill can not be moved in Parliament without President's recommendation. Although there exists

47. Supra note 40 entry 82.
48. Constitution of India, Article 366, clause (1).
51. Constitution of India, Article 274, clause (1).
a demarcation between 'agriculture income' and 'forestary' for the legislative purposes, but the term 'agricultural income' may include for purposes of taxation income from forestary.

Entry 47 - Duties in respect of succession to agricultural land

The States had been given power to levy duties in respect of succession to agricultural land. As regards succession duty in respect of other than agricultural land, it falls within the ambit of Parliament.

Entry 48 - Estate duty in respect of agricultural land

As the Parliament had been given power to levy estate duty on other than agricultural land similarly the States had also been given power to levy estate duty on agricultural land. Estate duty is a duty to be assessed with reference to the principal value of all property passing upon death or deemed to pass under the said law. Parliament while exercising powers under Article 252 had enacted Estate Duty Act 1953 which applies to all properties. As the entry refers to passing of property to another on the


53. *Supra* note 40, entry 88.
death of a person and do not apply transfers inter vivos hence gift tax would not fall within this entry.

**Entry 49 - Taxes on lands and buildings**

This entry empowers the States to levy taxes on lands and buildings both as units. Tax on the lands and buildings is directly imposed on 'lands and buildings' and thus bears a definite relation to it. The word 'lands' in this entry has been interpreted to include all lands whether agricultural or not. It also includes not only the surface but also the area beneath the surface. The tax under this entry may be levied with reference to the annual valuation of lands and buildings, payable by the owner. Thus the tax under this entry is based either on its capital value or on the annual letting value of the property. It cannot be based on the floor area of the building as that tax will be discriminatory. While interpreting this entry the Supreme Court has held that the tax may be imposed on land alone as the entry must be construed as 'taxes on lands' and 'taxes on buildings' In 1980, the question came up before Supreme

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54. **Supra** note 11 at 299.
was about the validity of tax on buildings levied by State of Kerala. The tax was based on capital value of a building which was to be measured by its annual value. It was argued before Supreme Court that since it was a wealth tax, it could be levied only by the Parliament. The Supreme Court upheld the tax stating that the method of determining the capital value of a building on the basis of its annual value cannot be regarded as arbitrary.

Entry 50 - Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development.

No doubt, it is the competence of States to levy taxes on mineral rights but this right is subject to limitation which may be imposed by law by Parliament for the development of minerals in the public interest. However, there is no unanimity among the various High Courts whether the royalty payable on minerals extracted from the mines is a tax or not. Some High Courts regard royalty as a tax, whereas others term it a price being paid for exploring the minerals.


61. Saurashtra Cement and Chemical Industries (P) Ltd. v. Union of India, 1976 Guj. 180; Also see Dr. Shanti Saroop Sharma v. State of Punjab, AIR 1969, P & H 79.
Entry 51 - Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India

(a) alcoholic liquors for human consumption.

(b) opium, Indian hemp and other narcotic drugs and narcotics but not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.

A State may levy duties of excise on certain goods manufactured or produced within its jurisdiction including countervailing duties at the same or lower rates on similar goods manufactured or produced in any other part of the country. These duties can only be levied on the goods entering from outside to the State if similar goods being manufactured in States are subjected to excise duties. The power under this entry had been given to the State Legislature so that the local manufacturer are not put to any disadvantage. However, entry 84, List I, does not come.

in the way to levy excise duty under this entry on alcoholic 63 
liquors for human consumption. It is interesting to note 
here that States can levy excise duty under entry 51 and sale 
tax under entry 54 on the same commodity. The entry tax 
under this entry is leviable only on the entry of goods and 
not on goods taken out from the State. Hence this entry 
does not allow any tax on consumption of the commodity brought 
from outside the State. Thus it is not necessary to consume 
the commodity in the same State which imposes duty.

Entry 52 - **Taxes on the entry of goods into a local area** 
for consumption, use or sale therein.

The tax which may be levied under this entry is 
commonly known as octroi duty and is distinguishable from 
terminal tax which Union may levy under entry 89, List I. 
A tax under this entry must satisfy two conditions:—
(i) that it is a tax on the entry of goods into a definite 
local area; (ii) that the goods must enter the area for 
the purpose of consumption, use or sale therein.

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Initially there was some difficulty in interpreting 'local area' in the context of this entry but now it has been finally settled that the expression refers to an area administered by a local body like municipality, a district board, a local board, a panchayat or the like.

Under this entry no tax is leviable on goods for any purpose other than consumption, use or sale. Octoral refers to goods and not to passengers and hence it can only be imposed on the entry of goods. Consumption means consumption by a purchaser or consumption as part or whole even outside the local limits. Once sale is complete within local area its resale outside the area is immaterial. Thus what is prohibited under this entry is the taxing of goods in transit i.e. goods passing through a local area. Similarly if goods brought into the local area exported within a stipulated period not taxable under this entry.

Entry 63 - Taxes on the consumption or sale of electricity

A State is authorised to levy taxes on the consumption or sale of electricity under this entry. Thus the

State had been given power to tax consumption of electricity whether produced by the consumer himself or purchased from somebody else. However, the tax under this entry differed from excise duty falling under entry 84, List I, because excise duty is charged on production and not consumption.

**Entry 54** - Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I.

The expression newspaper as contained in this entry means a paper which contains a report on recent events and thus the papers carrying astrological and numerological predictions are not newspapers and thus not covered under this entry. The expression 'sale of goods' under this entry convey the same meaning as under 'Sale of Goods Act'. For constituting a sale, there must be elements required under the 'Sale of Goods Act' such as agreement, money consideration and actual transfer of property in lieu of money. Sale by auction is a complete sale and hence covered under this entry, but forward contracts are not covered under this entry as such contracts are not a complete sale.

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73. **Chowringhee Sales Bureau (P) Ltd. v. C.I.T. West Bengal**, AIR 1973 SC 376.
Before 1982, a number of transactions were not held to be sale and thus kept outside the purview of this entry. With a view to enhance taxing power of States and to remove certain judicially imposed restrictions Constitution (Forty-sixth Amendment) Act, 1982 was enacted. This amendment provided that the following transactions were to be included within the expression "a tax on the sale or purchase of goods".

(a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration.

(b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of works contract.

(c) a tax on the delivery of goods on hire purchase or any system of payment by instalments.

(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period)

74. This overrides the Supreme Court's decision in New India Sugar Mills v. S.T. Commissioner, AIR 1963 SC 1207.

75. This overrides the Supreme Court's decision in State of Madras v. Cannon Dunckerly's, AIR 1958 SC 560.

76. This overrides the Supreme Court's decision in K.L.Johar & Co. v. Dy.C.I.O., AIR 1965 SC 1082.
for cash, deferred payment or other valuable considerations.

(e) a tax on the supply; by way of or as part of any service or in any other manner whatsoever, of goods, being goods or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service is for cash, deferred payment or other valuable consideration.

Thus after the amendment any of the above mentioned supply, transfer or delivery of any goods is to be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of these goods by the person to whom such transfer, delivery or supply is made.

Entry 55 - Taxes on advertisements other than those published in the newspapers and advertisements broadcast by radio or television

This entry had been inserted by Constitution (42nd Amendment) Act 1976. It gives power to the States to levy tax on the advertisements excepting newspapers, radio or television advertisements.

77. This overrides the Supreme Court's decision in Associated Hotels v. Excise and Tax Officer, AIR 1966 Punjab 429.

78. Supra note 11 at 306.
Entry 56 - Taxes on goods and passengers carried by road or inland waterways

This entry gives power to the States to levy a tax on passengers and goods carried on national highways and national waterways. It is a tax on the physical carriage of goods or passengers either through or within the jurisdiction of the State levying the tax and has no relevance to the purpose of travel or carriage. Thus physical carriage of goods is a necessity for levying the tax under this entry. Such a tax may be levied with reference to fares and freights, or the distance of travel or carriage. However, the goods which simply enter or leave the municipal limits and having no relation to their transport cannot fall within this category. The tax under this category may be realised from producer instead of one who carries them.

As a State spends large amounts on the maintenance of national highways and also provides certain basic facilities

79. Supra note 40, entry 23.
for passengers etc. hence the State is justified in imposing tax on goods and passengers carried on such national highways. However, under this entry, a State could impose only a tax of 'compensatory' and 'regulatory' nature.

Entry 57 - Taxes on vehicles, whether mechanically propelled or not, suitable for use on roads, including tramcars subject to the provision of entry 35 List III.

Under this entry the States could only impose a tax of compensatory or regulatory nature. Such tax must have some relation with vehicles using the roads i.e. public roads. But if vehicles do not use the road they can not be taxed under this entry. In Travancore Tea Co. v. State of Kerala, the Supreme Court has held that a law providing for tax on vehicles 'used or kept for use' on the public roads of the State is a valid law.

Entry 58 - Taxes on animals and boats

Under this entry the States had been given power to levy tax on animals and boats.


88. AIR 1980 SC 1547.
**Entry 59 - Tolls**

Under this entry the States may levy taxes which may be of various kinds and not limited to any particular type. Allahabad High Court while interpreting the term 'toll' has held that it is to be broadly interpreted to include payments realised for some benefit such as the use of markets or bridges or a temporary use of any land.

**Entry 60 - Taxes on professions, trades, callings and employments**

The States under this entry may levy taxes on professions, trades, callings and employments of persons whether natural or juristic. The expression profession, trade, calling or employment has been construed to include any recognised means of earning livelihood. However, pension receipts are not taxable as a pension is not a profession or employment. Under this entry a tax may be levied on professions and employments including service on trades or callings. A tax may be imposed on the commodity of trade or earnings. The tax under this entry may be determined with reference to total business turnover even though there

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91. Supra note 19.
is no income. Evidently the tax under this entry is similar to that of income-tax and this fact had been recognised by Article 276 of the Constitution which declares that a tax under this entry shall not be treated as income tax. However, this article provides that the tax under this entry shall not exceed Rs.250/- per annum in respect of a person, but if prior to the commencement of the Constitution, excess amount was being charged, that was to remain in force until Parliament otherwise provides. In Agra Municipality v. A.B.K.O. Association, however, the Supreme Court has held that both State as well as municipality can separately levy the profession tax upto Rs.250/- each on a person.

In another case, it was argued before the Supreme Court that 'circumstances and property tax' levied by the District Board U.P. was Income-tax, thus, within the competence of Parliament, but Supreme Court while rejecting this argument has held that it is a tax not on income but on a man's financial position.

93. Constitution of India, Article 276, clause (2).
94. AIR 1976 SC 160.
96. Ibid.
Entry 61 - Capitation Tax

This tax is levied on each human head or person without reference to his property, profession or income. The States had been given power to levy this tax under this entry.

Entry 62 - Taxes on luxuries including taxes on entertainments, amusements, lettings and gamblings

The word 'luxury' in this entry refers to goods of luxury such as tobacco and cosmetics etc. A luxury tax imposed on tobacco will not be invalid even though excise tax is levied by Centre on tobacco. Amusements and entertainments have been interpreted so as to include theatres and dramatic performances, cinemas, sports and the like. Since the entry envisages a tax on the act of entertaining hence it may be levied on the giver or receiver of an entertainment or both. Similarly a tax on wagering contracts may fall within this entry.

Entry 63 - Rates of stamp duty in respect of documents other than those specified in the provisions of List I, with regard to rates of stamp duty.

The States are empowered to levy stamp duty in respect of documents other than the documents dealt with in entry 91, List I. The occasion for levy of the duty of stamp is the execution of a document and not the transaction contained in the document.

Entry 66 - Fees in respect of any of the matters in this List, but not including fees taken in any court.

Under this entry the States are empowered to charge fee on any of the matter contained in List II, but States are barred from charging court fee as the same falls under List III.

(III) Taxing Power under the Concurrent List

The Concurrent List contains only three tax entries. These are:-

Entry 35 - Principles on which taxes on mechanically propelled vehicles are to be levied.

whereas entry 57, List II, provides for the levying of taxes on vehicles, whether mechanically propelled or not suitable for use on roads, this entry _inter alia_, speaks of principles on which taxes on mechanically propelled vehicles are to be levied. Power had been given to the States under this entry to compensate for the services and facilities provided for the motors operating in its territory by enacting a law to that effect. But since there may be great difficulty in involving all India permits and the buses passing through various territories may have to give heavy tax, to solve this problem and to introduce uniform taxation throughout the country, Parliament had been authorised to lay down principles on which taxes on mechanically propelled vehicles may be levied by the States under Entry 57, List II. The word 'principle' in this context refers to the rules laid down for guidance in the matter of taxation. No doubt, Parliament may lay down guidelines for levying of taxes but the right to levy taxes as such rests solely with the State legislature.

102. The committee on co-ordination of Transport has suggested to transfer this tax subject from State to the Concurrent List in order to achieve uniformity throughout the country. See M.P. Jain, _Indian Constitutional Law_, 345 (1970).


The difference between entry 57 and entry 35 is that whereas entry 57 covers both vehicles i.e. mechanically propelled or not, the entry 35 relates only to mechanically propelled vehicles.

**Entry 44** - **Stamp duties other than duties and fees collected by means of judicial stamp, but not including rates of stamp duty**

The Union is competent to levy stamp duties in respect of documents specified in entry 91 List I, under entry 63 List II, the States have power to determine the rates of a stamp duty in regard to document excepting those covered by entry 91 List I. Entry 44 of Concurrent List provides for stamp duties other than duties and fees collected by means of judicial stamps. This entry does not, however, include sales of stamp duty.

**Entry 47** - **Fees in respect of any matter in this List but not including fees taken in any court.**

The present entry relates to any fee that may be charged in respect of any matter contained in Concurrent List.

(IV) **Residuary Taxing Powers**

By virtue of entry 97, List I, Seventh Schedule,

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105. Entry runs: 'Any other matter not enumerated in List II or List III including any tax not mentioned in either of these lists'.
the Union becomes vested with the residuary powers to levy any tax which does not fall either under List II or List III. This entry is further reinforced by Article 248 of the Constitution when it provides, 'Parliament has exclusive power to make law with respect to any matter not enumerated either in the Concurrent List or State List'. Thus the Parliament is vested with the power to levy taxes along with residuary powers of legislation. The Supreme Court in Second Gift Tax Officer v. D.H. Hazareth while explaining the scope of residuary taxing power has observed that if any matter is not contained in any of the three Lists, then it belongs exclusively to Parliament under entry 97 of the Union List as a topic of legislation. However, the most landmark judgment on the scope of residuary powers of taxation was delivered by Supreme Court in Union of India v. H.S. Dhillon. The question of law involved in this case was whether Union could levy wealth tax under its residuary

106. Constitution of India, Article 248, clause (2).


108. Ibid., at 1001

powers or not. The Supreme Court while explaining the scope of Article 248 has held by a majority view, that if a matter is not included in either List II or List III, it automatically falls under List I. By applying this principle the Supreme Court observed that the wealth tax would be justified under entry 97 List I, either exclusively or read with entry 86 List I.

After the Supreme Court's judgment in Dhillon's case, the vacuum existing in the area of legislative powers of the Union had been filled. This judgment had in fact added a new dimension to the legislative powers of the Union. But with a view to protect the taxing powers of States from unduly curtailment, the Supreme Court in a later case named International Tourist Corporation v. State of Haryana has held that for exclusive competence of the Parliament under the Residuary powers, the States legislative incompetence must be clearly established.

(B) Limitations on the Taxing Powers of Union and States

The taxing powers of Union and States are not

110. Majority consisted of Sikri C.J., Ray, Palekar and Mitter JJ.

111. Supra note 109 at 1082. For comments on Dhillon's case also see Alice Jacob, 'Residuary Power and Wealth Tax on Agricultural Property', 14 JILI 80 (1972)

112. Supra note 11 at 318. Also see Jitendra Tiwari, 'Residuary Powers of Taxation under the Indian Constitution', 3 SCJ 17 (1988).

absolute as the Constitution of India itself imposes certain limitations on the taxing powers of both the Union and the States. These limitations have been discussed in the following pages.

(i) **No Taxation Except by Authority of Law**

Article 265 of the Constitution of India provides, 'no tax can be levied or collected except by authority of law'. This Article is a necessary corollary of the English principle, 'no taxation without representation'. The term law in this Article means statute law i.e. an Act of legislature. Thus no tax can be levied either by an executive action or by the Resolution of a House.

The 'authority of law' as used in this Article refers to a valid law which means:-

(a) the tax proposed to be imposed must be within the


118. Attorney General v. Wilts United Diaries (1921) 37 TL 834.
legislative competence of the Legislature imposing the tax.  

(b) the law must be validly enacted.  

(c) the law must not be a colourable use of or a fraud upon the legislative power to tax.  

(d) the tax must not violate any Fundamental Right.  

(e) the tax must not contravene the specific provisions of the Constitutions i.e. Articles 276, 285-286 and 289.  

(f) the tax must be authorised by such a valid law.  

Thus what is important is that not only levying of tax but the collection of tax should be under the authority of law. However, Article 265 is not a bar against giving

119. *Supra* note 69.  
121. *Supra* note 55.  
retrospective effect to taxing laws.

(a) **Distinction Between 'Tax' and 'Fee'**

The Constitution of India for the legislative purposes makes a distinction between 'tax' and 'fee', although there is no generic difference between both of them. Each List contains a number of entries and towards the end of each List there is an entry which authorises the levying of 'fee' in respect of any of the matters in the List. The first distinction between both is that whereas the respective governments have been barred from levying a 'tax' outside the tax entry, these governments, however, can levy a 'fee' in respect of a non tax entry as well. Likewise the State can levy 'fee' as well as 'tax'. Another distinction is that whereas a Bill providing for the imposition of a 'tax' is a 'Money Bill' but a Bill providing for a 'fee' is not a 'Money Bill'. The Supreme Court of India while distinguishing between 'tax' and 'fee has held 'a tax' is compulsory exaction of money by a public authority for public purposes the payment of which is enforced by law. The


127. The relevant entries are: Entry 96 List I, Entry 66 List II and Entry 41 List III.

imposition of tax is made for public purposes to meet
the general expenses of the State without reference to
any benefit ensuring to the tax payer. The money thus
collected by way of taxes becomes a part of the general
revenue of the State out of which the government spends it
for general public purpose whereas the 'fee' is a payment
made for some service rendered or some advantage conferred
or some specified work done for the payee. However,
unlike 'tax', fee usually does not form part of general
revenue of State.

Recently the Supreme Court in Sreenivasa General
Trading v. State of Andhra Pradesh had further liberalised
the concept of 'fee' by observing that there should be a
reasonable relationship between the levy of the 'fee' and
the services rendered and it is not necessary that each
individual gets the benefits of service rendered by the
authority. The Supreme Court observed that both the 'tax'
and 'fee' are compulsory exactions of money by public
authorities and compulsion lies in the fact that the payment

    see Corporation of Calcutta v. Liberty Cinema, AIR 1965
    SC 1182.


131. AIR 1983 SC 1246.

132. Ibid., at 1262. Also see Kewal Krishan v. State of
    Punjab, AIR 1980 SC 1008.
is enforceable by law against a person in spite of his unwillingness or want of consent.

(II) **Limitations on States Powers to Levy Taxes on Professions, Trades, Callings and Employments.**

Under the Constitution States have been authorised to levy taxes on professions, trades, callings and employments. This tax is similar to income tax which is levied by Union under entry 82. The Constitution-makers realised this overlapping and to overcome it a specific restriction was provided in the Constitution which lays down that the total amount payable in respect of anyone person to the State or to any one municipality, district board or other local authority in the State by way of taxes on professions, trades, callings and employments shall not exceed two hundred and fifty rupees per annum.

(III) **Limitations on States Power to Levy Taxes on the Consumption or Sale of Electricity**

Articles 287 and 288 of the Constitution debar the State from levying tax on the consumption or sale of

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133. Ibid. Also see, Om Prakash Aggarwal v. Giri Raj Kishori 1987 ITR 376.

134. Seventh Schedule, List II, Entry 60.

electricity. Article 287 provides that save in so far as permitted by Union legislation, no State shall tax the consumption of sale or electricity which is consumed by the Government of India itself or a railway company in the construction, maintenance or operation of a railway. Similarly Article 288 exempts from State taxation, subject to any order of the President to the contrary, water or electricity generated, consumed distributed or sold by any authority established for regulating or developing any inter State river or river valley. In fact, these two Articles partially incorporate the doctrine of 'immunity of instrumentalities' in relation to the Union. The intention behind these provisions is to protect the public utility services like railways and river valley projects from indiscriminate State taxation.

(IV) Limitations on States Power to Levy Sales Tax

The power to impose taxes on sale or purchase of goods other than newspapers belong to the State, but in the interest of national economy, the power of State to levy sales tax has been subjected to few constitutional limitations. These are:

136. Supra note 115 at 343.
137. Supra note 11 at 303.
(a) **Tax on Sale or purchase of goods outside the State or Inter State trade and commerce**

In the interest of economic unity of the country, it becomes necessary to regulate taxation of inter State sale or purchase. If such a taxation is not regulated it is likely to result into indiscriminate taxation which would ultimately hamper the free flow of trade and commerce.

For a complete sale or purchase it requires: existence of goods; agreement to sell; passing of the title; delivery of goods and payment of the price. Thus a sale by auction is a complete sale and sales tax can be imposed on auctioners. In case if all the requirements of sale take place in one State, the intra-State sale or purchase is complete. In that case, the State has power to levy tax on such sale or purchase. However, difficulties crop up when the ingredients of the sale take place not in one State but touch several States, such a sale is known as inter State sale and in that case each State may tax such a sale leading to multiple taxation.

Prior to 1956 with a view to avoid multiple taxation the States were not empowered to tax a sale or purchase taking place outside the State or in the course of

inter State trade or commerce. At that time a sale was regarded falling within the State in which goods under it were delivered for consumption. But after the amendment of Article 286, States are specifically debarred from levying a tax on sale or purchase in the course of inter State trade or commerce. But to ensure that inter State trade or commerce do not go untaxed, Article 286 was amended and the Parliament was given power to levy tax on inter State trade or commerce. To this effect entry 92A was added to List I. In pursuance of the power, the Parliament enacted the Central Sales Tax Act 1956 for levying a tax on inter State sale or purchase.

Section 3 and 4 of the Act incorporates various principles for deciding when a sale or purchase of goods is said to take place in the course of inter State trade or commerce and when a sale or purchase of goods can be said to take place outside a State.

While explaining the scope of Section 3 and 4 of the Act, the Andhra Pradesh High Court in Singareni Collieries Co. Ltd. v. State of Andhra Pradesh has held that if there is a sale of goods and movement of these goods crosses the

139. Constitutional (Sixth Amendment) Act 1956.
140. AIR 1962 AP 75.
border of the State under a contract of sale, it will be regarded as inter State trade or commerce.

(b) Tax on Sale or Purchase in the Course of Imports and Exports

As foreign trade is of great importance to national economy, therefore, it becomes necessary to protect it from indiscriminate taxation. Article 286(1)(b) debars a State from imposing a tax on the sale or purchase in the course of imports or exports. Article 286(2) gives power to Parliament to lay down principles for determining when a sale or purchase of goods take place in the imports or exports. While exercising the power under Article 286(2), the Parliament has enacted Central Sales Tax Act 1956. Section 5 of this Act lays down that a sale or purchase is in the course of imports or exports if it occasioned the export or import of goods out of or into India. Whether a sale has occasioned the export is a question of fact to be decided in each case. In B.G.N. Plantations v. S.T.O. Ernakulam, the Supreme Court has held that where the export

141. Ibid., at 139.
143. AIR 1964 SC 1752.
is the direct result of sale, the export being inextricably linked up with the sale so that the bond cannot be dis-associated without a breach of the obligation arising by statute, contract or mutual understanding between the parties arising from the nature of transaction, the sale is in the course of export.

(c) Tax on Goods of Special Importance

Parliament under Article 286(3) had been given power to declare certain goods to be of special importance in State trade or commerce and the Parliament may also lay down limitations on the State's power to levy tax on such goods. Parliament while exercising power under Article 286(3) had declared under Section 15 of the Central Sales Tax Act 1956, certain goods of special importance and the Section provides for certain restrictions on taxation of such goods. After Constitution (46th Amendment) 1981 the scope of this power of Parliament had been widened by providing that Parliament can impose limitations on State's power to levy tax on transfer of goods in execution of a works contract, or on delivery of goods on hire and purchase, or on the

144. Ibid., at 1756.

145. The restrictions are: (i) a tax shall be levied only on the last sale or purchase inside the State (ii) it shall be levied only at one stage and at a maximum rate of 3% of the sale price of the commodity.
transfer of the right to use any goods for any purpose for a valuable consideration.

(V) **Immunity from Mutual Taxation**

In a Federal set up where two different layers of government exist having independent functions and taxing powers, there is every likelihood of their being inserted at several points. It is always possible that the government at one end may exercise its powers in such a way which may interfere with the working of government at the other end. In such a situation the doctrine of inter-governmental immunities seeks to ensure the smooth functioning of both layers of government. Although this doctrine is of general application yet in the area of taxation in a Federal set up it works as a check on the taxing powers of the governments. This doctrine is contained in Article 285 and 289. This doctrine can be explained under the following headings:

(a) **Exemption of Union Property from State Taxation**

The States had been debarred from taxing Union property. Article 285(1) specifically provides that property

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146. M.P. Jain and S.N. Jain, 'Inter Governmental Tax Immunities in India,' *JILI* 101 (1959-60).
of the Union shall be exempted from State taxation except where Parliament may provide otherwise. The expression 'property' in this context has been used in a very general sense to give the widest possible effect to the provisions of this Article. So interpreted it includes lands, buildings, chattels, shares, debts and every kind of property i.e. movable, immovable, tangible or intangible. The protection under clause (1) is available to only Central Government, and its departments and this protection is not available to incorporated companies or corporations which is not a part of the Union but in which the Central Government has a controlling interest.

Clause (2), however, provides that unless Parliament legislates to the contrary, any authority in any State is not precluded from levying any tax on any property of the Union if such property immediately before the commencement of the Constitution was liable or treated as liable, so long as that tax is levied in that State.

(b) **Exemption of Property and Income of a State from Union Taxation**

Article 289(1) debars the Union from taxing the


State property and income. However, within the terms of clause (2) of this Article, the Union may levy any tax on any property used or occupied for trade or business or income accruing therefrom, if Parliament so provides. However, under clause (1) exemption extends only to States and not to their instrumentalities as the instrumentalities are different entities than the State itself.

Likewise in accordance with clause (3) of this Article Parliament may declare any trade or business carried on by any State Government to be incidental to the ordinary functions of government thereby excluding it from the purview of clause (2).

The Supreme Court has, however, refused to apply the doctrine of instrumentality beyond the scope laid down in Articles 285, 287, 288 and 289.

(C) Union v. States: Position in Taxing Power

The scheme of allocation of Centre-State taxing powers, though designed with many considerations in view such as convenience, simplicity, economy and uniformity, does not

create an equilibrium between responsibilities and resources at the State level. As is evident from various entries in the Union List, the major elastic and expanding sources of revenue such as income-tax, custom and export duty, excise duty, taxes on capital value of assets and taxes on the capital of companies etc. are retained by the Centre whereas the sources of revenue of States are comparatively meagre, and the taxing powers of States have been subjected to much more limitations as compared to the Union. Moreover, the States had been assigned the developmental work and had been given the responsibility to provide for welfare and social service actions like education, housing, health agriculture, but the sources of revenue of States are much meagre to meet all these activities. Though the dependence of the States, upon the Centre in financial matters was expected, yet the gap between the State revenues and their expenditure has crossed the reasonable limits because of certain subtle Central twists on the one hand and the pressure of the public on the State Governments and public

151. Supra note 11 at 332.
152. Constitution of India, Seventh Schedule, List I, Entry 82.
153. Ibid., entry 83.
154. Ibid., entry 84.
155. Ibid., entry 85.
utility services on the other which makes the rigid concept of autonomy difficult to sustain. The outcome of this system is that at present all the State Governments are in red and they owe heavy debts to the Centre. The problem of relatively inadequate financial resources of the States was also realised at the time of framing the Constitution. Various members of Constituent Assembly voiced their strong complaints. Sir A. Rama'swamy Mudaliar had expressed his fear that the resources placed at the disposal of the States would be inadequate in view of nation building activities with which the States are burdened. Similarly Sanathanam was of the view that if the States are not given more resources, 'the Provinces will be beggars at the door of the Centre.'

The complaints of meagre resources of the States are continuing from the time when Constitution was inaugurated. In fact, the revenue raising capacity of the States is too inadequate and they are left with sales tax as the only flexible source of revenue.

**REVIEW**

It may be submitted in conclusion that the

distribution of tax resources in India is more logical than
in any other Federation of the world as the distribution is
based on consideration of economy and efficiency. The
Constitution of India demarcates the taxing powers of the
Centre and States: taxes of local nature have been given
to the States while taxes with a tax base extending over
more than one State or which would be levied on a uniform
basis throughout the country or which can be collected more
efficiently and conveniently by the Centre rather than by
the States, have been assigned to the Centre. This clear
cut division of heads of taxation between the Union and the
States has minimised the scope for conflict and litigation
between them. Moreover this scheme has been found bene-
ficial to eliminate all problems of multiple and overlapping
taxation which have arisen in an acute form in the older
federations of U.S.A., Canada and Australia due to Concurrent
taxing powers. On the contrary in our Constitution the
taxing powers of the Union and the States have been completely
separated and made mutually exclusive. Thus our Constitution

160. Madhuri Bhargava, Inter-Governmental Financial Relations
in India since Independence, 26 (1976).
161. Supra note 14 at 253.
162. Supra note 157 at 204.
164. Asok Chanda, Federalism in India; A Study of Union
State Relations, 179 (1965).
in the matter of division of taxing powers be placed in the category of true Federal Constitution. The main object behind the apparently complex tax separation in which some taxes are exclusively leviable by Union and other by States, is to protect the financial autonomy of the States and at the same time to provide for uniformity where necessary. Separation is there but it is accompanied by some degree of integration. Thus the Constitution makers had tried fairly successfully to avoid anomalies and overlapping thereby making the document foolproof.

However, the scheme of separation of Centre State tax resources as discussed above has created problem of imbalance between resources and functions at the State level. A study of the division of revenue resources in India reveals that there is an obvious Constitutional tilt in favour of Union as the Centre has been favoured with a relatively larger amplitude of financial resources and the sources of the States for the discharge of their manifold responsibilities have been relatively inadequate. Most of the expansive functions have been assigned to the States but the taxes allotted to States


are not sufficient by themselves to enable the States to discharge their growing social welfare obligations.

Perhaps this situation was foreseen by the founding fathers of the Constitution and therefore, they sought to augment resources of the States by providing for transfer of funds to the States from the Centre through the technique of tax sharing and grants.

168. Supra note 157 at 204.

169. See Articles 268, 269, 270, 272, 275 and 282.