CHAPTER - V
FREEDOM OF TRADE AND LEGISLATIVE POWERS OF UNION AND STATES

5.1. Introduction

The framers of the Constitution of India visualised for India a federal Constitution providing for a strong Central Government, strong enough not only to take care of its own responsibilities but to guide and coordinate the activities of the States also. The framers of the Constitution, on the one hand makes a clear demarcation of legislative subjects between the Union and the States adhering to the basic federal principle, on the other hand, it contains a large Concurrent List, embodying a typical Indian set-up, in which, ultimately, the balance tilts in favour of the Union. From a strong Centre, the framers did not mean weak States, which were allowed, in normal times, to act independently in designated and by no means insignificant areas of government. In the United States of America and in Australia the Constitution contains only the powers of the Federal Legislature. The remaining powers vested in the States. In the Constitution of Canada there are two Lists, the Union List and the State List. The Government of the India Act, 1935 classified all possible topics of legislation in three Lists. The

Constitution of India has in this regard also, as in many others, adopted the 3-fold List system of the Government of India Act, 1935.²

List I of the Seventh Schedule called the Union List contains 100 entries.³ These entries includes matters of national importance. List II of the Seventh Schedule called the State List contains 61 entries,⁴ the List comprises of subjects, over which the State has exclusive power to legislate. List III of the Seventh Schedule is the Concurrent List, it comprises of 52 entries.⁵ Both Union and the States are competent to make laws in relation to these entries.

In the present chapter, an attempt has been made to highlight the limitations on the legislative powers of the Parliament and State Legislature by the ‘Freedom of Trade Clause’, and analysed the distribution of taxing powers and examines how far freedom of inter-State trade is burdened by taxing laws. It throws light on the conflict between the two lists and how judicial mind has responded to solve it. This chapter presents a critical study of the conditions and circumstances under which tax laws can be said to hamper freedom of trade and commerce. Cases under different heads of taxation have been analysed critically in this chapter.

³ The last entry is numbered as 97 but a close reading would reveal that entries numbered as 2A, 92A, 92B and 92C has been added and entry 33 has been omitted. Thus the total number of entries is 100.
⁴ The last entry is numbered 66. It should be noted that by the Seventh Amendment entry 36 was omitted. After that by the 42th Amendment entries 11, 19, 20 and 29 were omitted. Thus the total number of entries is 61.
⁵ Originally the List had 47 entries. By subsequent 5 entries were added. They are 11A, 17A, 17B, 20A and 33A. The total number is 52.
5.2. **Scope of Legislative Powers of Parliament**

The Constitution of India in Article 245(1) confers powers upon the Parliament of India to legislate for the whole or any part of the territory of India. Article 246(1) confers exclusive power upon Parliament to legislate with respect to matters enumerated in List I of Seventh Schedule. Further, Parliament, under Article 246(2) has also concurrent power with respect to any of the matters enumerated is List III. The Article 248 provides that Parliament has exclusive power to make law with respect to any matter not enumerated in the Concurrent List or State List. Article 249 enables Parliament to legislate with respect to a matter in the State List, if the Rajya Sabha by a two-thirds majority passes a resolution that it will be expedient in

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6 Subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the Legislature of a State may make laws for the whole or any part of the State.

7 Notwithstanding anything in clauses (2) and (3), Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule. (in this Constitution referred to as the “Union List”).

8 Notwithstanding anything in clause (3), Parliament, and, subject to clause (1), the Legislature of any State also, have power to make laws with respect to any of the matters enumerated in List III in the Seventh Schedule. (in this Constitution referred to as the “Concurrent List”).

9 Article 248(1) read as: Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List. (2) Such power shall include the power of making any law imposing a tax not mentioned in either of those Lists.

10 Article 249(1) Notwithstanding anything in the foregoing provisions of this Chapter, if the Council of States has declared by resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in the national interest that Parliament should make laws with respect to any matter enumerated in the State List specified in the resolution, it shall be lawful for Parliament to make laws for the whole or any part of the territory of India with respect to that matter while the resolution remains in force.

(2) A resolution passed under clause (1) shall remain in force for such period not exceeding one year as may be specified therein: Provided that, if and so often as a resolution approving the continuance in force of any such resolution is passed in the manner provided in clause (1), such resolution shall continue in force for a further period of one year from the date on which under this clause it would otherwise have ceased to be in force.

(3) A law made by Parliament which Parliament would not but for the passing of a resolution under clause (1) have been competent to make shall, to the extent of the incompetency, cease to have effect on the expiration of a period of six months after the resolution has ceased to be in force, except as respects things done or omitted to be done before the expiration of the said period.
the national interest to do so. The life of such a legislation cannot exceed one and a half years. Parliament may also legislate with respect to any matter in the State List if a Proclamation of Emergency is in operation. Parliament may also legislate for two or more States by consent with respect to a matter in the State List. Any other State can also adopt such a legislation. Parliament can also legislates in the State field to the extent necessary for giving effect to an international agreement.

In order to examine how far the freedom of trade affects the legislative powers of Parliament, the Investigator consider some of the important powers conferred by the Constitution in the Seventh Schedule, List I and List III.

5.2.1. Inter-State trade and commerce

Entry 42, List I authorises Parliament to legislate with respect to ‘inter-State trade and commerce’. In Article 269(3) Parliament is empowered to

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11 Article 250(1) Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to any of the matters enumerated in the State List.

(2) A law made by Parliament which Parliament would not but for the issue of a Proclamation of Emergency have been competent to make shall, to the extent of the incompetency, cease to have effect on the expiration of a period of six months after the Proclamation has ceased to operate, except as respects things done or omitted to be done before the expiration of the said period.

12 Article 252(1) read as: If it appears to the Legislatures of two or more States to be desirable that any of the matters with respect to which Parliament has no power to make laws for the States except as provided in Articles 249 and 250 should be regulated in such States by Parliament by law, and if resolutions to that effect are passed by all the Houses of the Legislatures of those States, it shall be lawful for Parliament to pass an Act for regulating that matter accordingly, and any Act so passed shall apply to such States and to any other State by which it is adopted afterwards by resolution passed in that behalf by the House or, where there are two Houses, by each of the Houses of the Legislature of that State.

(2) Any Act so passed by Parliament may be amended or repealed by an Act of Parliament passed or adopted in like manner but shall not, as respects any State to which it applies, be amended or repealed by an Act of the Legislature of that State.

13 Article 253 read as: Notwithstanding anything in the foregoing provisions of this Chapter, Parliament has power to make any law for the whole or any part of the territory of India for implementing any treaty, agreement or convention with any other country or countries or any decision made at any international conference, association or other body.

14 Article 269(3) read as: Parliament may by law formulate principles for determining when a [sale or purchase of, or consignment of, goods] takes place in the course of inter-State trade or commerce.
‘formulate principles for determining when a sale or purchase of goods takes place in the course of inter-State trade or commerce’. Though this Article mainly deals with taxation it seems that the principle formulated in this Article would be relevant in determining the scope of the inter-State trade power.\textsuperscript{15}

Parliament, under this entry, may regulate inter-State trade in dangerous things or prohibit an inter-State trade agency which promotes immorality or dishonesty or spreads any evil or harm among the people of other States.\textsuperscript{16}

Parliament, under entry 42 List I, restricts the free flow of trade, perhaps, the Act would have to satisfy the condition of ‘public interest’\textsuperscript{17} laid down in Article 302, however a law passed under this entry is a valid law and is in the public interest then freedom of trade provided under Article 301 will not infringed.\textsuperscript{18}

This power of Parliament is also restricted by Article 303(1). It prohibits preferential or discriminatory laws. Such laws would not be validated on the ground of public interest. The only exception is that

\textsuperscript{15}Parliament of India, in exercise of the power in Article 269(3), has enacted Section 3 of the Central Sale Tax Act, 1956 which says: A sale or purchase of goods shall be deemed to be take place in the course of inter-State trade or commerce if the sale or purchase (a) occasion the movement of goods from one State to another, or (b) is effected by a transfer of document of the title to the goods during their movement from one State to another. Explanation-I: where goods are delivered to a carrier or other bailee for transmission, the movement of the goods shall, for the purposes of Clause (b), be deemed to commence at the time of such delivery and terminate at the time when delivery is taken from such a carrier or bailee. Explanation-II: where the movement of goods commences and terminates in the same State it shall not be deemed to be a movement of goods from one State to another by reason merely of the fact that in the course of such movement the goods pass through the territory of any other State.

\textsuperscript{16}R.M.D. Chamarbaugwalla v. Union of India, AIR 1957 SC 628.

\textsuperscript{17}The words “in the public interest” covers a wider field, so as to include public security, public order, public convenience and public morality held in the case of Guru Datta Sharma v. State of Bihar, AIR 1961, SC 1684

\textsuperscript{18}Ibid.
Parliament can discriminate in dealing with a scarcity of goods.\(^{19}\) It is the duty of the Judiciary to apply Article 303(1) and examine whether the power exercised under entry 42, List I, is in fact discriminatory or not; if it were satisfied that the Parliamentary legislation came with the mischief of Article 303(1), then such a law would be declared unconstitutional.

5.2.2. Productions, supply and distribution of essential commodities

Entry 33 of List III\(^{20}\) has to be read with entry 52 of List I,\(^{21}\) which empowers Parliament to vest the control of particular industries in the Union\(^{22}\)

\[^{19}\text{Article 303(2) read as: Nothing in clause (1) shall prevent Parliament from making any law giving, or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India.}\]

\[^{20}\text{Trade and commerce in, and the production, supply and distribution of,}\]

\[\text{(a) the products of any industry where the control of such industry by the Union is declared by Parliament by law to be expedient in the public interest, and imported goods of the same kind as such products;}\]

\[\text{(b) foodstuffs, including edible oilseeds and oils;}\]

\[\text{(c) cattle fodder, including oilcakes and other concentrates;}\]

\[\text{(d) raw cotton, whether ginned or unginned, and cotton seed; and}\]

\[\text{(e) raw jute.}\]

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<th>Before the Constitution (Third Amendment) Act, 1955, entry 33 List III</th>
<th>After the Constitution (Third Amendment) Act, 1955, entry 33 List III</th>
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| Trade and commerce in, and the production, supply and distribution of, the products of industries where the control of such industries by the Union is declared by Parliament by law to be expedient in the public interest. | Trade and commerce in, and the production, supply and distribution of,—  
(a) the products of any industry where the control of such industry by the Union is declared by Parliament by law to be expedient in the public interest, and imported goods of the same kind as such products;  
(b) foodstuffs, including edible oilseeds and oils;  
(c) cattle fodder, including oilcakes and other concentrates;  
(d) raw cotton, whether ginned or unginned, and cotton seed; and  
(e) raw jute. |

\[^{21}\text{Industries, the control of which by the Union is declared by Parliament by law to be expedient in the public interest.}\]

and legislate\(^\text{23}\) with respect to ‘trade and commerce in, and the production supply and distribution’ of certain commodities; for example, products of declared industry and similar imported products, food stuffs, cattle fodder, raw cotton and raw jute. Before the Constitutional (Third Amendment) Act, 1955 entry 33 provided for only one commodity which is a product of declared Industry. In addition, Parliament was empowered by Article 369,\(^\text{24}\) for a period of five years, to legislate in respect of certain specified essential commodities.

Before the expiration of the period stipulated in Article 369, the Government of India in the year 1952 appointed a Commodity Control Committee to examine the position with respect to trade and commodity control. The Committee, after examining the existing position, came to the conclusion that the control of essential commodities must be continued for a


\(^{24}\) Notwithstanding anything in this Constitution, Parliament shall, during a period of five years from the commencement of this Constitution, have power to make laws with respect to the following matters as if they were enumerated in the Concurrent List, namely-

\((a)\) trade and commerce within a State in, and the production, supply and distribution of, cotton and woollen textiles, raw cotton (including ginned cotton and unginned cotton or kapas), cotton seed, paper (including newsprint), food-stuffs (including edible oilseeds and oil), cattle fodder (including oil-cakes and other concentrates), coal (including coke and derivatives of coal), iron, steel and mica;

\((b)\) offences against laws with respect to any of the matters mentioned in clause \((a)\), jurisdiction and powers of all courts except the Supreme Court with respect to any of those matters, and fees in respect of any of those matters but not including fees taken in any court;

but any law made by Parliament, which Parliament would not but for the provisions of this article have been competent to make, shall, to the extent of the incompetency, cease to have effect on the expiration of the said period, except as respects things done or omitted to be done before the expiration thereof.
considerable time on an all-India basis and that such an important power should not be left with the State Legislatures. The Committee therefore recommended that this power should be permanently vested in Parliament.  
Parliament accepted this recommendation and passed the Constitution (Third Amendment) Act, 1954, adding four classes of essential commodities together with imported goods of some kind as the products of declared Industries in entry 33 of List III.

It may be mentioned that, before the Constitution came into force, the Central Legislature had similar powers under the Indian (Central Government and Legislature) Act, 1946, the Central Legislature was empowered to make laws with respect to trade and commerce in and the production, supply and distribution of certain specified goods, for a temporary period of one year. It was in exercise of this power that the Central Legislature enacted the Essential Supplies (Temporary Powers) Act, 1946, for controlling the above mentioned activities in specified goods. The Central Act, of 1946 was passed while a proclamation of Emergency was is operation. The Governor-General was authorised by the British Act of 1946 to extend the operation of the Central Act, of 1946 for one more year and it was subsequently kept in force upto 1950, when Parliament passed the Essential Supplies (Temporary Powers) Amendment Act, 1950. Finally, in 1955, after the amendment of

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entry 33 of List III, Parliament passed the Essential Commodities Act, providing for the control of production, supply and distribution of the commodities mentioned in the present entry.

To provide effective measures for controlling offence in respect of essential commodities and for the prevention of black marketing and hoarding, the act has been amended by the Essential Commodities (Special Provisions) Act, 1957, 1981 and 1987. 26

The powers in entry 33 of List III were conferred on the Parliament to ensure uniformity in the control of essential commodities. Article 303(1) was also incorporated to Part XIII with the same object.27

The Essential Commodities Act, 1955, authorises the Central Government to control the prices of essential commodities.28

The question arises whether such control would attract freedom of trade under Article 301. The Supreme Court of India held that reasonable price fixing could be permissible for regulation of inter-State trade.29

The Essential Commodities Act, 1955, provided that the Central government may require any person holding a stock of essential commodities

26 Supra, note 22, p.12196.
27 Ibid.
to sell the whole or a specified part of the stock to the government or to such person or class of persons as may be required by the government.\textsuperscript{30} Though this provision restricts freedom of trade perhaps, it would get protection on the ground of public interest provided under Article 302. This measure, though, discriminatory would not be held unconstitutional in Article 303(1) because the provision of scarcity of goods under Article 303(2) would apply.

Entry 33 of List III provides the Central Government with a mechanism for ensuring that unreasonable restrictions are not imposed on trade, commerce and intercourse thereby affecting the economic unity of the country. The problems regarding production, supply and distributions of essential commodities have national dimension and Entry 33 enables the Central Government to efficiently manage essential commodities.\textsuperscript{31}

\subsection*{5.2.3. Adulteration of food}

Adulteration of food means the mixing with any substance intended to be sold of any ingredient which is dangerous to health or which makes the substance other than that as which it is sold or intended to be sold.\textsuperscript{32}

Entry 18 of List III, confers concurrent power on Parliament and the State Legislatures with respect to ‘adulteration of food stuffs and other goods’.

\begin{flushright}
\textsuperscript{30} Section 3(2)(f).
\textsuperscript{31} Supra, note, 26.
\textsuperscript{32} Ibid p.12160.
\end{flushright}
Parliament has enacted under this entry, the Prevention of Food Adulteration Act, 1954. This Act provides in section 7 that no person shall himself or by any person on his behalf, manufacture for sale or store, sell or distribute any adulterated food or any misbranded food. Furthermore, Section 23 of the Act empowered the Central Government to prohibit or regulate the manufacture, transport or sale of any article known to be used as an adulteration of food.

So far as the provision of Section 7 is concerned, it does not directly restrict the freedom of inter-State trade. As far as restriction on manufacture is concerned, the application of freedom of trade under Article 301 does not arise. As regards Section 23, if the Central Government under that Section restricted the transportation of such food stuffs, still it would not attract

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34 Prohibitions of manufacture, sale, etc., of certain articles of food-No person shall himself or by any person on his behalf manufacture for sale, or store, sell or distribute-
(i) any adulterated food;
(ii) any misbranded food;
(iii) any article of food for the sale of which a licence is prescribed, except in accordance with the conditions of the licence;
(iv) any article of food the sale of which is for the time being prohibited by the Food (Health) Authority [in the interest of public health;]
(v) any article of food in contravention of any other provision of this Act or of any rule made there under; or
(vi) any adulterant.
Explanation-For the purposes of this Section, a person shall be deemed to store any adulterated food or misbranded food or any article of food referred to in clause (iii) or clause (iv) or clause (v) if he stores such food for the manufacture there from of any article of food for sale.]

35 The Central Government may, after consultation with the Committee and after previous publication by notification in the Official Gazette, make rules to prohibiting or regulating the manufacture, transport or sale of any article known to be used as an adulterant of food.
freedom of trade, because no one can claim a right to carry on business in such food stuffs.\textsuperscript{36}

5.2.4. Transport and communications

The Constitution of India contains a detailed scheme regarding transport and communication powers of Parliament. Entry 22 List I, provides exclusive power upon Parliament to legislate with respect to all railways and all matters relating to it.\textsuperscript{37}

Entry 23 of List I, provides for ‘Highways declared by or under law made by Parliament to be national highways’. The State Legislature in entry 13 of List II is authorized to legislate for road communications perhaps, Parliament by law declares any road to be of national importance, and then such road becomes a Union subject.\textsuperscript{38}

Power of Parliament with respect to shipping\textsuperscript{39} and navigation\textsuperscript{40} on inland waterways is provided in List I, entry 24. This entry is limited to shipping and navigation on inland waters, which are declared by Parliament by law to be national waterways. Further, in entry 32, List III Parliament has been bestowed with concurrent powers in respect to ‘shipping and navigation on inland waterways, as regards mechanically propelled vessels, the rule of

\textsuperscript{36} H. P. Barua v. State of Assam, AIR 1952 Ass. 149.
\textsuperscript{37} Supra, note 22, p.11794.
\textsuperscript{38} Ibid, p.11797.
\textsuperscript{39} Ibid, p. 11800/ Shipping includes every kind of business relating to ships, and may includes ship building.
\textsuperscript{40} Ibid, p.11801/ Navigation is the art of sailing at sea, also the manner of trading.
the road on such waterways and the carriage of passengers and goods on inland waterways.’

Parliament has exclusive power in entry 29 of List I over airways, aircraft and air navigation; regulation and organization of air traffic and of aerodromes.41

List I entry 30 empowers Parliament to legislate with respect to carriage of passengers and goods by railways, sea or air or by national waterways in mechanically propelled vessels.42 Entry 31 of List I, which says that ‘posts and telegraphs; telephones; wireless; broadcasting and other like forms of communication’ are within the exclusive power of Parliament.

In India, certain instruments of transport and communications are under the control of the Central Government. For example, railways are under Central administration and posts, telegraphs, telephones, wireless, broadcasting and internal air traffic, are the exclusive privilege of the Central Government. In such cases, the regulation of these instruments of transport or communication will therefore not come within the scope of Article 301. In Sanjeeviah case43 where the Supreme Court held that a State law banning the transport of wood between sunset and sunrise as unconstitutional, this

41 Ibid, p. 11805/ Section 2(2) of the Aircraft Act, 1934 read as: “Aerodrome” means any definite or limited ground or water area intended to be used, either wholly or in part for the landing or departure or aircrafts, and including building vessels, piers, and other structures thereon or appertaining thereto.
42 Ibid, p.11806/ Carriage of passengers and goods by roads comes under the State List (entry 13 of List II); while carriage by inland waterways comes within the Concurrent List (entry 32 of List III.
restriction would also attract the provisions of freedom of trade under Article 301. Perhaps, if the restriction were imposed so as to carry on war effectively, such a restriction would come within the protection of Article 302 on the ground of public interest.

5.3. **Scope of Legislative Powers of States on Freedom of Trade**

Article 245(1) in Part XI of the Constitution of India provides that the Legislature of a State shall make laws for the whole or any part of the State. The legislative power of the State Legislature is thus confined to the territory of the State.\(^4^4\)

The distribution of the head provided in the Seventh Schedule of the Constitution of India is subject to Article 246. Article 246 provides the manner in which the legislative heads may be distributed among Parliament and the State Legislature. Article 246(3) provides that the State Legislature has exclusive power to make laws with respect to any of the matters enumerated in List II in the Seventh Schedule. It may be noted that the State Legislature in Article 246(2) is given concurrent power over subject matters provided in List III.

Article 245, read with Article 246 along with Seventh Schedule to the Constitution of India, begins with the worlds “Subject to the provisions of this Constitution,” which means that the powers granted to the Legislatures in

\(^{44}\) Supra, note 2, p.286.
those Articles are not sovereign powers. Those powers are subject to the limitations provided by the Constitution. Article 301 begins with the words “Subject to the others provisions of this Part” which means that this Article constitute a limitations on the legislative power of the State Legislature. The question arises, which power of the State Legislature attracts the limitation in Article 301 is effective. The above question may be examined with reference to some of the legislative heads in List II and List III of the Seventh Schedule.

5.3.1. Trade and commerce

Entry 26 in List II, read with Article 246(3), confers exclusive power on the State Legislature in respect of “trade and commerce within the State, Subject to the provisions of entry 33 of List III”. 45

Under the entry 26 in List II, the State Legislature can –

a) Provide for the fixation of a minimum price payable to cultivators of jute, authorize the Government to control stocking of raw jute and make it compulsory to enter into contracts for the sale of raw jute only through a Jute Board constituted under the Act. Such legislation is not ultra virus even though it may have some indirect effect upon export of raw jute in certain cases. 46

45 Supra, note 20.
46 Supra, note 22, p.12032.
b) Regulate the hours, place, date and manner of sale of any particular commodity or commodities.\(^{47}\) It could, for example, state that the sale of explosive or other dangerous substances should only be in selected areas, at specified times or on specified days when extra precautions or the general safety of the public and those directly concerned could be arranged for. In the same way, it could say that there shall be no sales on a particular day or on days of religious festivals and so forth.

Provisions of Bihar Agricultural Produce Markets Act, 1960, regulating purchases and sale of products of rice milling industry are not repugnant to Rice Milling Industry (Regulations) Act, 1958, as that Act does not deal with regulations of purchase and sale of products of such mills. The State legislation is covered by entries 26 and 28 of List II.\(^{48}\)

5.3.2. Production, supply and distribution of goods

The Constitution of India, in entry 27 of List II authorises the State Legislature to legislate with respect to ‘production, supply and distribution of goods’. The exclusive jurisdiction conferred by entry 27 of List II is subject to the provisions of entry 33, List III.\(^{49}\)

Fixation of price is included within the present power.\(^{50}\) The State Government in exercise of its regulatory power can fix the price of sugarcane.

\(^{47}\) Ibid, p.12033.
\(^{49}\) Supra, note 20.
\(^{50}\) Supra, note 22, p.12034.
Though the Central government has fixed a ‘minimum price’ for sugar, the State government can fix a higher price in exercise of its regulatory power and same is not repugnant or inconsistent. On the other hand, if a lower price is fixed by the State, the same will amount to inconsistency or will be repugnant.\textsuperscript{51}

An ordinance and subsequent takeover, by legislation, the management of certain tea units and vesting the same with the State Government for five to seven years is a valid law passed under entry 27 of List II read with entry 33 of List III.\textsuperscript{52}

The Constitution of India contains in Part XIII a detailed free trade scheme. It not only restricts any discrimination against goods from outside the State, made in the exercise of trade and commerce powers, but also any restriction which directly and immediately restricts the free flow of trade. Article 301 uses the words ‘throughout the territory of India’, which implies that the State Legislature in exercise of its power of trade and commerce cannot restrict the flow of trade, either at the State frontiers or within the State.\textsuperscript{53}

5.3.3. Marketing and price control

The Constitution of India in Article 303(1) prohibits the State Legislature from enacting any legislation by virtue of trade and commerce

\textsuperscript{51} Uttar Pradesh Cooperative Cane Union Federation v. West Uttar Pradesh Sugar Mille Association, AIR 2004 SC 3697.
\textsuperscript{52} Tufanialonga Tea Company Limited v. State of Tripura, AIR 1999 Gau. 109.
\textsuperscript{53} Jindal Stainless Ltd. v. State of Haryana, AIR 2006 SC 2555.
power which has a discriminatory effect on the outside trade. A State Legislature enacts marketing legislations, which makes discrimination against goods from outside the State, it would also have to satisfy the conditions in Article 304(b).\textsuperscript{54}

Price control is provided in entry 34 of List III. Under this entry, Parliament or the State Legislature can authorize the fixing of maximum and minimum prices.\textsuperscript{55}

Price control is a method of controlling inflation or allocation of resources in a centrally planned economy by pegging prices within specified limits. Market forces make it difficult to control prices in that way in the long term and the method is normally used only for short term crisis management.\textsuperscript{56}

Price control imposed by the State Legislature if independently and discriminates against outside goods or subjects the goods to excessive control it would be hit by Article 301 which provides freedom of trade and Article 303(1) which prohibits preference to one State over another and discrimination between one State and another.

\textsuperscript{54} Legislature of a State may by law impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest:

Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President.

\textsuperscript{55} Secretary to Government v. A.G. Factory, AIR 1959 AP 538.

\textsuperscript{56} Supra, note 22, p.12198.
5.3.4. Transport regulations

The State Legislature under entry 13 of List II,\(^{57}\) is given power over ‘Communications’. It provides that the State Legislature shall legislate with respect to roads, bridges and ferries. The power in entry 13 List II also includes municipal tramways, ropeways, island waterways and traffic thereon. The power conferred by entry 13 of List II is subject to the provision of List I and List III.\(^{58}\)

It has been well settled that the words ‘trade and commerce’ include communication.\(^{59}\) Consequently the question arise how far does the regulation of communications impair freedom of inter-State trade and commerce. This question may be discussed under the following heads:

5.3.4.1. Regulatory legislation

In India the most common means of inter-State transportation which the State Legislature can regulate is the motor vehicle. In regulatory legislations, the State Legislature might authorise the making of rules governing the construction of cars, headlights, inspection facilities, and number of passengers, speed and other matters relating to road traffic.

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\(^{57}\) Communications, that is to say, roads, bridges, ferries, and other means of communication not specified in List I; municipal tramways; ropeways; inland waterways and traffic thereon subject to the provisions of List I and List III with regard to such waterways; vehicles other than mechanically propelled vehicles.

\(^{58}\) Supra, pp. 190-192.

The question arises whether these measures violate the free trade clause. Justice Das, in *Automobile Transport Ltd. v. State of Rajasthan*[^60] opined that regulatory measures did not come within the purview of Article 301 which provides freedom of trade. In Article 301, it is the direct and immediate effect that is relevant. Till the time, the regulatory measures facilitates free flow of trade it would not attract the provisions of this Article. Perhaps, the measure directly restricts the flow of trade; it will have to satisfy the conditions in Article 304(b).[^61]

### 5.3.4.2. Monopolies

The legislative subject of State monopolies is dealt with in the Seventh Schedule, entry 21 of List III.[^62] This entry also empowers the State to make laws conferring monopoly on itself to the exclusion of citizens doing a particular business.[^63] It is not confined to the grant or creation of commercial or industrial monopolies.[^64]

Prevention of concentration of means of production to the common detriment is of the directive principles of State policy.[^65] For this purpose the State may impose reasonable restrictions upon the freedom of trade or business.[^66]

[^60]: Infra, note 72.
[^61]: Supra, note 54.
[^63]: Supra, note 22, p.121.
[^64]: Ibid.
[^65]: Supra, Chapter IV, pp.170-171.
Under entry 21 of List III, Parliament enacted Monopolies and Restrictive Trade Practices Act, 1969. A law creating a monopoly in favour of the State is also immune from attack on the ground of contravention of Article 301 or 303. This protection is available only where (a) the law made by the Parliament and State Legislature (b) the monopoly was created in favour of the State or a corporation owned or controlled by the State. It is to be mentioned that if any one of these conditions is not fulfilled the laws will be infringe the freedom of trade.

5.3.4.3. Licensing

Licensing is a regulatory measure imposed with a view of promoting the general welfare of society. The licensing authority generally lays down certain conditions, which a licensee has to fulfill in order to get permission to have certain advantages. Regulation of trade through a licensing system is the order of the day. It is now clearly settled that a system of licensing of a trade is not unreasonable provided that the licensing officer are not left with uncontrolled power to grant, revoke or cancel a license. There should be reasonable norms, policy or principles to guide administrative powers as well as some procedural safeguards.

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68 Supra, note 2, p.318.


70 Ibid.
The question arises whether a licensing system restricts the freedom of inter-State trade. There exists no direct case on this point, but in the *Atiabari* case, Justice, *Shah*, pointed out the *obiter* that the guarantee of freedom of trade and commerce was addressed to licensing laws as well. On the other hand Justice, *Subba Rao*, in the *Automobiles* case took the view that a licensing system did not restrict the free movement of trade, but facilitated the same.

It is not correct to say that a licensing measure restricts directly and immediately, it may facilitate the flow of trade. Perhaps, such a measure is utilized to restrict the flow of trade, it would attract the freedom of trade under Article 301. However, if the law which confers discretionary power satisfies the test in Article 304(b), it would not be void under Article 301.

It seems that Justice *Subba Rao’s* view in the *Automobile* case is correct, subject to the reservations mentioned above. The individualist theory of Article 301 as expounded by Justice *Shah*, in the *Atiabari* Case seems inconsistent with the other provisions of the Constitution. A license is without doubt a restriction on the individual’s right to carry on trade, but this aspect of trade is within the ambit of Article 19(1)(g) and not in Article 301.

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71 Supra, note 59.
73 Supra, note 54.
74 Supra, note 72.
75 Supra, note 59.
76 Supra, Chapter IV, pp. 153-154.
5.3.5. Prohibition laws

The Constitution of India makes special provision in the Seventh Schedule List II, entry 8, for prohibition laws. This entry authorise the State Legislature to legislate in respect of the following matters:-

“Intoxicating liquors, that is to say, the production, manufacture, possession, transport purchase and sale of intoxicating liquors.”

Duties of excise on alcoholic liquors is also a State subject, but not medicinal and toilet preparations containing alcohol.

The expression ‘intoxicating liquor’ covers not only those alcoholic liquors which are generally used as beverages and produce intoxication, but also all liquids containing alcohol, including methylated spirit, which may be used as substitutes for intoxicating drinks, to the detriment of health.

This entry also empowers the State to prohibit against the possession of rotten gur in excess of the prescribed limit and regulation of manufacture, use or consumption of the produce from which alcohol is made.

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77 Ram Krishna v. Union of India, AIR 1969 Cal. 18.
78 Entry 51 List II-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.
80 Supra, note 22, p.11997.
The State has every authority to regulate the supply of liquor within its territorial jurisdiction to ensure that what is supplied is ‘liquor of good quality’ in the interest of health, moral and welfare of the people.\textsuperscript{82}

The Supreme Court of India in \textit{Khoday Distilleries v. State of Karnataka},\textsuperscript{83} observed that a citizen has no right to trade or business in intoxicating liquors and that trade or business in such liquors can be completely prohibited. Dealing in intoxicating liquors is considered to be \textit{res-extra commercium}.\textsuperscript{84} The State can create a monopoly either in itself or in an agency created by it for manufacture, procession, sale and distribution of liquor as a beverage. The State can impose restrictions, limitations and even prohibition on intoxicating liquors.\textsuperscript{85}

The State Legislature, in entry 8 of List II is authorised to legislate with respect to ‘Intoxicating liquors’ and free to include any substance which is, in fact an intoxicating liquor. A State prohibition law regulating articles would not attract the provisions of freedom of trade under Article 301.

\textsuperscript{82} Ugar Sugar Works Limited v. Delhi Administration, AIR 2001 SC 1447.
\textsuperscript{83} (1995)1 SCC 574.
\textsuperscript{84} Supra, note 16.
\textsuperscript{85} Ugar Sugar Works Limited v. Delhi Administration, AIR 2001 SC 1447.
5.3.6. Public order and public health

The State Legislature under entry 1 of List II\textsuperscript{86} is authorised to legislate with respect to ‘public order’. Public order implies absence of violence and an orderly State of affairs, in which citizens can peacefully pursue their normal avocation of life.\textsuperscript{87} Anything which disturbs public tranquility disturbs public order.\textsuperscript{88} This entry also includes ‘public safety’ in its relation to the maintenance of public order.\textsuperscript{89} In short, ‘public order’ is synonymous with public peace, safety and tranquillity.\textsuperscript{90} A law on public order must essentially adverse itself to the preservation and maintenance of public order.\textsuperscript{91} In order to maintain public order, the State Legislature can impose restrictions on movements and it can order requisition of movable property.

It may be noted that the State Legislature, in order to control public disorder, might restrict the movement of certain persons. This restriction has nothing to do with the freedom of inter-State trade and so it will not come within the inhibition of Article 301, though such a restriction might attract the provisions of Article 19(1)(d), which guarantees the right to move freely throughout the territory of India.

\textsuperscript{86} Public order (but not including [the use of any naval, military or air force or any other armed force of the Union or of any other force subject to the control of the Union or of any contingent or unit thereof] in aid of the civil power).
\textsuperscript{87} Supra, note 22, p.11980./ Superintendent v. Ram Manohar, AIR 1960 SC 633.
\textsuperscript{88} Id.
\textsuperscript{89} Id.
\textsuperscript{90} Ibid. / Bhupendra v. State of Maharashtra, AIR 2008 SC 2306.
\textsuperscript{91} Vijay C. Puljal v. State of Maharashtra, AIR 2005 SC 613.
The Constitution of India in entry 6 of List II authorises the State Legislature with respect to “public health and sanitation, hospital and dispensaries”. The State Legislature under this entry may regulate or prohibit the use of certain articles which are injurious to public health.\(^92\)

The mere fact that the State Legislature exercise powers relating to public health does not mean that laws made in its exercise are necessarily immune from attract under Article 301. The provisions of Article 301 would operate if the State Legislatures put a restriction on the import, introduction or bringing into the State of any goods which are likely to introduce any disease into the State.\(^93\) Administrative bodies are generally given wide powers in order to administer the police powers effectively. Perhaps, absolute discretionary powers were conferred on administrative bodies without laying down any policy or guidelines for its exercise, this would come within the inhibition of the Free Trade Clause. Further, if a law passed in exercise, of the State police power discriminated against inter-State trade, such law would have to comply with the conditions in Article 304(b).\(^94\)

\(^{92}\) Centre for Public Interest Litigation v. Union of India, Writ Petition (Civil) No. 681 of 2004/ http://www.foodsafetynews.com/2013/10/indias-supreme-court-declares-constitutional-right-to-unadulterated-food/ retrieved on 27-12-2014, time 12.20 p.m.


\(^{94}\) Supra, note 54.
5.3.7. Betting and gambling

The State Legislature, in entry 34 List II, is authorised to legislate with respect to ‘betting and gambling’. Betting is a form of wagering contract.\textsuperscript{95} Gambling includes any dealing involving risk and uncertainty.\textsuperscript{96} It has been held by the Supreme Court of India\textsuperscript{97} that gambling includes all lotteries other than those organised by the Government. Lotteries are based on chance and constitute gambling. The fact that it is run by the State will not alter its character as ‘\textit{res-extra Commercium}’.\textsuperscript{98} In that case, the Court held that by banning State lotteries of other States, the question of violation of either Article 301 or Article 303 does not arise, since, dealing in lottery is not trade or business.

Online gaming and gambling laws in India are in a state of flux. Online \textit{rummy} and online \textit{poker} may still be illegal and punishable. The real trouble seems to be use of cash or stakes while conducting online \textit{rummy} and \textit{poker} competitions without following all the applicable laws of India. Madras High Court\textsuperscript{99} held that these games are illegal as these involved gambling. On appeal (pending) before the Supreme Court of India\textsuperscript{100} in which the Supreme Court is well aware of this situation and it has taken a stand that was very

\textsuperscript{95} A wager is a contract by which two or more persons agree that a certain sum of money or other thing of value shall be paid or delivered to one of them by the other or others upon the happening of an uncertain event.
\textsuperscript{96} Supra, note 16.
\textsuperscript{97} Ibid.
\textsuperscript{99} \url{http://perry4law.org/onlinegamingandgambling/?p=161}, retrieved on 12-12-2014, time-11.30 a.m.
\textsuperscript{100} Ibid.
much required. The Court has asked the Central Government for its legal stand regarding games like online *rummy* and online *poker*. The Supreme Court issued a notice to the Central Government asking it to spell out its position on the legality or otherwise of the online game of *rummy* and *card* games involving stakes. The Court also extended its stay on Madras High Court judgment that had held these games illegal as these involved gambling. Perhaps, the stay is applicable only to the petitioners before the Court. This means other are vulnerable to legal risks and they cannot take the protection of this stay. It is submitted that online gaming entrepreneurs must ensure techno-legal compliance in order to stay on the right side of the law till legal position is made clear in this regard.

Gambling activities from their very nature and in essence are ‘*extra Commercium*’, although the external forms, formalities and instruments of trade may be employed, they are neither protected by Article 301 or 19(1)(g) of the Constitution. This entry will cover ‘only’ gambling prize competition.\(^{101}\)

5.4. **Taxing Power of Parliament and State Legislature on Freedom of Trade**

The taxing powers are divided between the Centre and the States under the various Lists in the Seventh Schedule to the Constitution. The taxes enumerated in the Union List are leviable by the Centre exclusively while

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those mentioned in the State List are leviable by the State exclusively. The Constitution of India does not permit the levy of any tax outside the tax entries. Yet, the residuary taxing power is vested with the Union.

5.4.1. Taxing power of Parliament on freedom of trade

The Parliament’s power to levy inter-State tax is subject to the limitations set-out in Article 301 and Article 303. However, Article 302 empowers Parliament to restrict inter-State and intra-State trade and commerce if public interest requires the same, subject to Article 303 that no preference be given to one State over another or discrimination be made between States.

The following tax entries are mentioned in the Union List of the Seventh Schedule and taxes on trade and commerce leviable exclusively by the Parliament.

5.4.1. Excise duties

The Constitution of India makes a clear demarcation of excise powers. Entry 84 of List I confers powers on Parliament to levy duties of excise and

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102 Article 265 read as: No tax shall be levied or collected except by authority of law.
103 Entry 97 of List I- Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists.
104 Article 303 speaks of “any entry relating to trade and commerce” includes “all those entries in the lists of the Seventh Schedule which deal with the power to legislate, directly or indirectly in respect of activities, in the nature of trade and commerce”. If the tax provided under a law made under any such entry operates on trade and commerce will be covered by Article 303. Once it is held that Article 301 covers tax law also, it is more logical to take the position that the Constitution intended to prohibit not only non-tax legislation giving preference to one State over another but also tax laws, whose effects on the economy of the country may be more far-reaching.
105 Duties of excise 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,
State Legislature under entry 51 of List II is given the power to impose excise duties.\textsuperscript{106}

A duty of excise is primarily levied upon a manufacturer or producer in respect of the commodity manufactured or produced,\textsuperscript{107} even though it may be levied at a stage subsequent to the manufacture.\textsuperscript{108} It is a tax upon goods, not upon sales or the proceeds of sale of goods\textsuperscript{109} and sale is not a necessary condition for charging excise duty.\textsuperscript{110}

Excise duty has nothing to do with movement of trade, so it will not come within the inhibition of the ‘Free Trade Clause’. Under the Constitution of India the Supreme Court has evolved the test of ‘\textit{extra commercium}’\textsuperscript{111} As a result, the protection in Article 301 would not be available where the goods are ‘\textit{extra- Commercium}.’ In this respect, excise does not affect the free flow of trade contemplated in Article 301.

\textbf{5.4.1.2. Central sales tax}

The general sales tax falls in the State List.\textsuperscript{112} Perhaps, to protect the newspapers which have an intimate connection with the freedom of speech and expression guaranteed as a fundamental right by the Constitution, sales

\textsuperscript{106} Infra, pp.211-212.
\textsuperscript{107} Supra, note 22, p.11927.
\textsuperscript{109} C.C.E. v. Acer India Limited, AIR 2004 SC 4805.
\textsuperscript{110} Medley Pharmaceuticals Limited v. C.C.E., (2011)2 SCC 601.
\textsuperscript{111} Supra, note 16.
\textsuperscript{112} Entries 53 and 54 of List II of Seventh Schedule.
tax on newspapers has been made a Central subject.\textsuperscript{113} It also avoids indiscriminate taxation.\textsuperscript{114}

In entry 92A of List I provides “Taxes on the sale or purchase of goods\textsuperscript{115} other than newspaper where such sale or purchase takes place in the course of inter-State trade or commerce.” This entry was inserted by the Constitution (Sixth Amendment) Act, 1956, on the recommendations of the Taxation Enquiry Commission appointed in 1953. The Commission held that the sales tax must continue to be a State tax and as a source of revenue, it must wholly belong to the States; and as a tax to be levied and administered, it must substantially pertain to the State governments. Perhaps, the sphere of power and responsibility of the State, might be said to end and that of the Union to begin, when the sales tax of one State impinged administratively on the dealers and fiscally on the consumers of another State. Broadly speaking

\textsuperscript{113} Entry 92 of List I- Taxes on the sale or purchase of newspapers and on advertisements published therein.
\textsuperscript{114} Supra, note 1, p.203.
\textsuperscript{115} In Article 366(29A) which was inserted by the Constitution Amendment (Forty-Sixth Amendment) Act, 1982 defines “tax on the sale or purchase of goods” includes-
\textsuperscript{(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;
\textsuperscript{(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;
\textsuperscript{(c)} a tax on the delivery of goods on hire-purchase or any system of payment by instalments;
\textsuperscript{(d)} a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;
\textsuperscript{(e)} a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;
\textsuperscript{(f)} a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration,
and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made.
the Commission recommended that inter-State sale should be the concern of the Union.\(^{116}\)

Though the taxes under this entry are levied and collected by the Centre but the net proceeds thereof in their entirety, are made over to the States in whose territory the tax is levied and collected.\(^ {117}\)

Sales tax legislation \textit{per se} does not violate Article 301. Impact of the operation of the law in such as to impede free flow of trade, it comes within the mischief of freedom of trade under Article 301. Article 302 is not concerned with taxation laws. It will not be proper to read tax within the word ‘restriction’ in Article 302 or Article 304(b).\(^ {118}\)

It is submitted that a Central sales tax is imposed on inter-State transaction and movement of goods generally restrict freedom of trade provided under Article 301 of the Constitution of India. Perhaps, Indian judiciary adopts a mere tolerant attitude towards a tax law.

\textbf{5.4.2. Taxing power of the States Legislature on freedom of trade}

The power to levy taxes by the States is subject to the foregoing provisions. The States cannot impose discriminatory taxes upon imported


\(^{117}\) Article 269(1)(g).

goods, because of the specific limitation in Article 304(a).\textsuperscript{119} Consequently no State may discriminate or give preference to one State over another in imposing taxes on goods going out of the State, either because of the specific limitation in Article 303(1)\textsuperscript{120} or by reason of the fact that such taxes may amount to unreasonable restriction on trade and commerce under Article 304(b).\textsuperscript{121}

The State List contains the following taxes on trade and commerce which are leviable exclusively by the States:-

5.4.2.1. Excise duties

Entry 51 List II of Seventh Schedule of the Constitution of India provides that 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.

\textsuperscript{119} Legislature of a State may by law impose on goods imported from other States [or the Union territories] any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced.

\textsuperscript{120} No State Legislature shall have power to make any law giving, or authorising the giving of, any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

\textsuperscript{121} Supra, note 54.
The nature of an ‘excise duty’ has already been discussed, perhaps, this entry gives power to the State Legislature to levy countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India. Such duties can only be levied on goods entering the State from outside if similar goods being manufactured within the State are subjected to excise duty. The duties are meant to equalize the tax burden on home production and imports so that the local manufacturer is not to be at a disadvantage. Further, the duty is levied on the entry of goods and not on goods being taken out.

5.4.2.2. Octroi duty

Entry 52 List II of Seventh Schedule of the Constitution of India provides ‘taxes on the entry of goods into a local area for consumption, use or sale therein. The tax levied under this entry is commonly known as Octroi duty. The words ‘consumption’ and ‘use’ does not mean that the goods must be destroyed or used up in the process.

The imposition of entry tax levied in terms of entry 52, List II of Seventh Schedule is violative of the freedom of trade, commerce and intercourse guaranteed by Article 301 of the Constitution of India, perhaps,

122 Supra, pp. 207-208.
124 Ibid, p. 207.
125 Ibid/ for example, wheat imported into the municipal limits by flour mills for converting it into flour, is taxed under this Entry as conversion into flour by grinding involves an user of wheat. It is not essential that the flour shall be consumed in the State itself.
such levy of the tax is compensatory in character. The yardsticks to be applied in determining the compensatory character of the entry tax would be the same as applied by the Supreme Court of India in Automobile Transport Limited\textsuperscript{126} and reiterated in Jindal Stainless Limited\textsuperscript{127}. The levy of entry tax will have to satisfy the principle of proportionality which implies that its quantum should be approximately equal to the benefit conferred on trade as a result of the tax. The Court observed,\textsuperscript{128} that the primary purpose of a taxing statute is the collection of revenue. On the other hand, regulation extends to administrative act which produce regulative effects on trade and commerce.

The Court has also observed\textsuperscript{129} that when the tax is imposed as a part of regulation or as part of regulatory measure, its basis shifts from the concept of “burden” to the concept of measurable/quantifiable benefit and then it becomes a “compensatory tax” and its payment is then not for revenue but as reimbursement or recompense to the service or facility provider. The burden is always on the State to prove that the payment of compensatory tax is a reimbursement or recompense for the quantifiable or measurable benefit provided or to be provided to its payers. A compensatory tax may incidentally bring in net revenue to the government but that circumstance is not an essential ingredient of compensatory tax. It is clear that even if entry 52, List

\footnotesize{
\begin{itemize}
\item Supra, note 72.
\item Supra, note 53.
\item Id.
\item Id.
\end{itemize}
}
II of Seventh Schedule does not specifically requires the State to spend the money collected in that local area, still any compensatory tax cannot be a device of revenue collection for the State and it has to necessarily provide some quantifiable or measurable benefit to its payers.

The Court$^{130}$ has clearly elaborated the conceptual distinction between a compensatory tax and a fee. Despite the fact that principle of burden (capacity to pay) governs a tax, fee is governed by the principle of equivalence (exaction should approximate the benefit flowing from the exaction). The Supreme Court in *International Tourist Corporation v. State of Haryana*$^{131}$ had stated that a compensatory tax need not provide approximate benefit as it would render it indistinguishable from a fee. The Court in *Jindal Steel Ltd.$^{132}$* has corrected this proposition and has considered that compensatory tax is a species of fee with the difference that a compensatory tax is levied on an individual as a member of class, while a fee is levied on an individual as such. V. Niranjan, in an insightful analysis of the decision of the Supreme Court in *Jindal Steel Ltd.,* has observed:$^{133}$

“A fee is ‘compensatory’ if that particular fee improves the flow of trade, and if so, it will be outside the purview of Article 301. But that does not make it a compensatory tax, because a fee is not a tax in the first place. In other words, equivalence is a necessary but not sufficient condition for a levy to be considered a fee. A tax is generally not

$^{130}$ Id.


$^{132}$ Supra, note 53.

compensatory. However, that does not mean that a tax which is compensatory becomes a fee. It continues to be a compensatory tax, and is outside the purview of Article 301 for that reason. A fee, on the other hand, usually has elements of quid pro quo, but will not be ‘compensatory’ unless it improves trade.”

While a compensatory tax could be species of fee but conceptually they are very different from each other. First, a fee would be compensatory if it improves the flow of trade but that does not make it a compensatory tax. Second, a tax which is compensatory does not become a fee. The device of compensatory tax enables the State to override the freedom guaranteed under Article 301 of the Constitution. Hence, when there is no bar to the entry of goods at the State border, then the entry tax cannot be termed as a tax on the movement of goods, but it cannot be extended to mean that no entry tax could be levied when the goods pass through a local area within which they are not sold, used or consumed.134

Any tax on goods within the State which directly impedes the trade, by being excessive in nature, and thus violates Article 301 of the Constitution can be saved by reference to Article 304(b) of the Constitution. If any Act invades freedom of trade, it is necessary to enquire whether the State has proved that the restrictions imposed by it by way of taxation are reasonable and in public interest within the meaning of Article 304(b).135

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134 Vijaylakshmi Rice Mill v. CTO, AIR 2006 SC 2987.
5.4.2.3. State sales tax

Entry 54 List II provides that “taxes on the sale or purchase of goods other than newspapers, subject to the provision of entry 92A of List I”\(^\text{136}\) The power of the State Legislature to tax under the present entry can be availed of only where there has in fact been ‘sale’ as recognised by the general law.\(^\text{137}\) To constitute a sale, there should be an agreement between the parties for transforming title to goods, support by money consideration, and as a result of the transaction, property must actually pass in the goods.\(^\text{138}\)

A State would have the power to impose sales tax, if two conditions are fulfilled; firstly, the goods must have been actually delivered within that State as a direct result of contract of sale; and secondly, such delivery had to be for the purpose of consumption of such goods within the State. Perhaps, these two conditions were not satisfied and the goods were not actually delivered or the purpose was not consumption within the State, the State could not exercise its power under entry 54 of List II.\(^\text{139}\)

\(^{136}\) This entry was substituted by the Constitution (6th Amendment) Act, 1956. The original entry read as “taxes on the sale or purchase of goods other than newspaper.” The substitution was done along with the insertion of entry 92A in List I. the result of the amendment was that inter-State sale would be a Union subject and it is under that entry that the Central Sales Tax Act, 1956 was enacted.

\(^{137}\) Supra, note 22, p.12078./ The term sale has been defined under Section 4 of Sale of Goods Act, 1930 as ‘A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. And Section 2(g) of the Central Sales Tax Act, 1956 also defines sale as- “Any transfer of property in goods by one person to another for cash or for deferred payment or for any other valuable consideration and include a transfer of goods on the hire-purchase or other system of payment by installment, but does not include a mortgage or hypothecation of or a charge or pledge on goods”.

\(^{138}\) Ibid, p. 12079.

\(^{139}\) Himmatlal v. State of Madhya Pradesh, AIR 1954 SC 403.
Since a sales tax is imposed on the transaction of sale of goods and not on their movement, normally it does not directly impede the free movement of goods and would not offend against Article 301.\textsuperscript{140} It is submitted that this view is incorrect because State sales tax is imposed on the transaction of goods and on their movement within the State, normally it directly impede the freedom of intra-State of trade and offend against Article 301. Perhaps, Indian judiciary adopts a mere tolerant attitude towards a tax law for the protection of government revenue.

It is submitted that by reason of Article 303(1) and 304(a), a sales tax, whether imposed by the Union or by a State, cannot discriminate between one State and another.\textsuperscript{141} A sales tax imposed by a State shall offend against Article 301, if it imposes a tax on the sale of a commodity only if it is imported from another ‘State, or if the rate of tax imposed on the sale of a commodity, when imported, is higher than the rate of tax imposed on the sale of the same commodity when the sale takes place within the taxing State.\textsuperscript{142}

\subsection*{5.4.2.4. Value added tax}

The power of the States to enact Value Added Tax is derived under entry 54 List II of the Seventh Schedule to the Constitution of India.\textsuperscript{143}

\begin{footnotesize}
\begin{enumerate}
\item Supra, note 22, Vol. 8, p.9768.
\item Id.
\item Id.
\item Id.
\item Supra, note 136.
\end{enumerate}
\end{footnotesize}
Sales tax which was introduced in India for the first time in early forties, occupies an important position in revenue structure. The importance of sales tax can be judged from the fact that more than sixty percent of the tax revenue of majority States used to come from this source alone. Sales tax laws in India have become unpopular because of its complicated provisions relating to administration and enforcement, cascading effect of taxation and diversion of trades. It is easier if all the taxes are replaced by one single system and this would reduced the compliance difficulties of complicated provisions of different statutes besides cascading effects of taxation and trade diversion.\textsuperscript{144}

As a measure to reform and stop trade diversion due to different rates of tax in different States the first step was adoption of uniform rate of tax in the General Sales Tax laws of all the States in India. The major initiative taken by the Central Government towards introduction of Value Added Tax in India was publication of draft model of Value Added Tax prepared by National Institute of Public Finance and Policy and direction by the Central Government to all the States to come out with an Act based on the model submitted by National Institute of Public Finance and Policy. In the year 1995 a committee was formed with the Finance Ministers of different State to reform Sales Tax. The Ministry of Finance, Government of India on the basis

of resolution adopted in the Conference of the Chief Ministers held on 16th
November, 1999 constituted the Empowered Committee of State Finance
Ministers with Sri Asim Kumar Dasgupta, Finance Minister, Government of
West Bengal, as its convenor. The Empowered Committee has published a
White Paper on State level Value Added Tax. The committee initially set
2001 as dead line for all the States to switch over to Value Added Tax.
Although the States failed to switch over, as such the dead line extended to 1st
April, 2003 and ultimately to 1st April, 2005.145

The State of Maharashtra adopted Value Added Tax in the year 1995
apart from General Sales Tax on experimental basis, had subsequently
withdrawn the Value Added Tax system and again adopted from 1st April,
2005. The main reason for withdrawal earlier being problem faced due to
significant drop in the growth of revenue from Sales Tax system after
introduction of Value Added Tax.146

Haryana became the first State in the country that had adopted the
Value Added Tax system on 1st April, 2003. As of now, Value Added Tax
system has been implemented in all the States and Union Territories of
India.147

145 Id.
146 Id.
147 http://en.wikipedia.org/wiki/Value_added_taxation_in_India, retrieved on 10-12-2014, time 10.00
p.m.
It is submitted that the levy of tax at every stage in the series of the sales of goods made with the provision of credit of input tax paid at the point of the previous purchases by a registered dealer to the other was the main phenomenon of the VAT system. Perhaps, VAT imposed on the transaction or movements of goods generally impaired freedom of trade under Article 301 and the consumers are to bear the burden of heavy price rise owing to such multiple levy of VAT, beset with, other allied elements.

5.4.2.5. Taxes on movement of goods and passengers

Taxes on goods and passengers are those taxes which are levied on the goods and passengers carried by means of transport. Such taxes may be levied, on the basis of fares, freights or distance travelled. The transport or carriage tax on goods and passengers is levied as a consideration for the use of means of communication provided by the State.

The State Legislature under entry 56 of List II, is authorised to levy ‘taxes on goods and passengers carried by road or on inland waterways,”and not extend to taxes on passengers carried by railway, sea or air.

In *Khierbari Tea Co. v. State of Assam* the Supreme Court of India held that if the goods or passengers which come from outside and carried

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148 Supra, note 22, p.12084.
149 Ibid.
150 In the Union List, entry 30 confers power on Parliament to legislate on “carriage of passengers and goods by railway, sea or air or by national waterways”. It would seem that the State Legislature, under List II, entry 56, may levy taxes on goods or passengers carried on national highways or national waterways within the State.
within the State are liable to a special burden as compared with inside State passengers or goods, then the tax will not have the protection of Article 304(a), and will be struck down by Article 301.

5.4.2.6. Taxes on transport vehicles

Transport taxes are taxes levied on the means of conveyance and include taxes on vehicles, mechanically propelled or not. This tax is primarily levied to cover the expenses incurred by the State; a tax on a motor vehicle is levied so as to cover the cost of wear and tear of the roads.\textsuperscript{152}

The Constitution of India provides a clear demarcation between the Union and the State power to tax transport.\textsuperscript{153} In \textit{Automobile Transport Ltd. v. State of Rajasthan}, the Supreme Court of India held that motor vehicle taxes are compensatory taxes and could not hinder the freedom of trade.

5.4.3. Restriction on taxing powers

The Constitution of India imposes some restrictions on the taxing powers of the Parliament and State legislatures. Apart from the limitations imposed by the division of the taxing powers between the Centre and the

\textsuperscript{151} AIR 1964 SC 925, 941.
\textsuperscript{153} In entry 57 of List II the State Legislature is authorised to impose “taxes, on vehicles, whether mechanically propelled or not, suitable for use on roads, including tramcars subject to the provision of entry 35 of List III.” Under entry 35 of List III the States and the Parliament of India have concurrent power to legislate in respect of mechanically propelled vehicles including the principles on which taxes are to be levied.
\textsuperscript{154} AIR 1958 Raj. 114.
States by the relevant entries in the legislative Lists, those may be discussed under the following heads:

5.4.3.1. **No taxation save by authority of law.**

Article 265 of the Constitution of India lays down that “no tax shall be levied or collected except by authority of law.” The Article provides that not only the levy but also the collection of a tax must be under the authority of law. The term ‘Law’ in this Article means ‘statute law’, which means an Act of the Legislature.\(^\text{155}\) Accordingly, no levy can be imposed either by an executive action\(^\text{156}\) or by the resolutions of the Houses of the Legislature or by subordinate legislation in the absence of express statutory authority for the charge.\(^\text{157}\) In interpreting Article 265 the Supreme Court of India held that if tax has been paid in excess of the tax specified, excess tax realized must be refunded.\(^\text{158}\)

Further, the law must be a valid law, which means that-

1. The tax proposed to be levied must be within the legislative competence of the Legislature imposing tax.\(^\text{159}\)

\(^\text{155}\) Supra, note 22, Vol.8, p.9128.
\(^\text{156}\) Id.
\(^\text{157}\) Id.
\(^\text{158}\) Corporation Bank v. Saraswati Abharansala (2009)1 SCC 540
\(^\text{159}\) Supra, note 155, p.9131.
2. The law must be validly enacted, which means that, by the proper authority which has the legislative competence and in the manner required to give its acts the force of law.\footnote{Ibid.}

3. It must not contravene the specific provisions of the Constitution provided under Article 301, 303(1), 304(a) and 304(b) which provides limitation on legislative power.\footnote{Ibid, p.9132.}

4. The power of a State to levy tax on sale or purchase of goods is subject to Article 286.\footnote{Article 286 provides-Restrictions as to imposition of tax on the sale or purchase of goods- (1) No law of a State shall impose, or authorize the imposition of, a tax on the sale or purchase of goods where such sale or purchase take place- (a) outside the State; or (b) in the course of the import of the goods into, or export of the goods out of, the territory of India. (2) Parliament may by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1). (3) Any law of a State shall, in so far as it imposes, or authorises the imposition of- (a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or (b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b) sub-clause (c) or sub-clause (d) of clause (29A) of Article 366, be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify.}

5.4.3.2. Restriction on the power of the State to impose tax on the sale or purchase of goods

The power to impose taxes on “sale or purchase of goods other than newspapers” belongs to the State.\footnote{Entry 54, List II.} Perhaps, taxes on “imports and exports”\footnote{Entry 83, List I.} and “inter-State trade and commerce”\footnote{Entry 42, List I.} and “taxes on sale or purchase of goods”
purchase of goods, other than news papers, in course of inter-State trade or commerce are exclusive Union subjects. The object of Article 286, under which the State’s power to levy ‘sales tax’ has been subjected to a few restrictions, is to ensure that sales taxes imposed by the States do not interfere with import and export and inter-State trade and commerce which are matters of national importance. It is to regulate taxation of inter-State sale or purchase lest an indiscriminate State taxation may hamper free flow of trade and commerce from one State to another and thus jeopardise the economic unity of the country. Article 286, hence, with a view to keep inter-State and international trade and commerce and trade in the goods and of special importance, free from haphazard State taxation, subjects the States’ power to levy sales tax to the following restrictions:

a) No State can tax a sale or purchase taking place outside the State.

b) No State can tax a sale or purchase taking place in the course of inter-State trade and commerce.

c) No State can tax a sale or purchase taking place in the course of import and export.

d) Restrictions could be imposed by Parliament on the powers of State Legislature with respect to the levy of tax on sale or purchase of goods

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166 Entry 92A, List I.
167 Supra, note 1, p.224.
168 Ibid.
169 Article 286(1)(a).
170 Ibid.
171 Article 286(1)(b).
within the State where the goods are declared by Parliament, to be of special importance in inter-State trade or commerce. ¹⁷²

5.5. Conclusion

It is seen from the foregoing discussion that there is no doubt on the capacity of a State to tax, together with its own products, goods produced in other States, when brought into it for sale or consumption. When the inter-State transit is over and they have become part of the mass of property within the State, any goods may be taxed, no matter from where they have come. But they must be taxed alike with all other such goods in the State. The tax is general, and laid equally on all goods of the kind to be taxed, whether their State of origin be the taxing State or another.

It is seen that excise duty has nothing to do with transaction or movement of goods therefore excise duty does not violate freedom of trade. While Central sales tax is imposed on inter-State transaction and movement of goods and a State sales tax is imposed on the transaction of goods and on their movement within the State, normally both the taxes directly impede the freedom of inter-State as well as intra-State trade and offend against Article 301. Perhaps, Indian judiciary adopts a mere tolerant attitude towards a sale tax for the protection of government revenue.

¹⁷² Article 286(3).
It is seen that the levy of tax at every stage in the series of the sales of goods made with the provision of credit of input tax paid at the point of the previous purchases by a registered dealer to the other was the main phenomenon of the VAT system. Perhaps, VAT imposed on the transaction or movements of goods generally impaired freedom of trade under Article 301 and the consumers are to bear the burden of heavy price rise owing to such multiple levy of VAT, beset with, other allied elements.

It is seen that the GST literature indicates that a series of Central and State laws will be unified and designed in a unique way to simplify the existing multiple levy of tax at the Centre and the States’ level. It is intended to consolidate and to design a single law at the behest of the Centre. The unified Central cum State laws will cover the Central excise duty, additional excise duty, excise duty levied under Medicinal and Toiletries Preparation Act, service tax, additional custom duty commonly known as countervailing duty, (CVD), special additional duty, surcharge and cess at the Centre while value added tax, sale tax, entertainment tax, luxury tax, taxes on lottery, betting and gambling, State cess and surcharges, entry tax not in lieu of octroi at the States’ level.

The item of goods, proposed to be excluded from the GST net are petroleum and petroleum products, namely; petroleum crude, high speed diesel, motor spirit, natural gas, aviation turbine fuel and alcoholic liquor for
human consumption besides tobacco. The nature, importance and comparative overview of GST is discussed in the next chapter to get a clear picture of proposed tax regime on trade and commerce in India.