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IN THE SUPREME COURT OF INDIA
CIVIL APPELLATE JURISDICTION
ARAVIND KUMAR; J., PRASANNA B. VARALE; J.
JULY 13th, 2026.

CIVIL APPEAL NO. 48 OF 2009
ASIA SUGAR & CHEMICAL CO., DEVANGERE *versus* THE STATE OF KARNATAKA & ORS.
SLP(C) NO. 25469 OF 2009
M/S INDIAN SUGAR AND GENERAL EXPORTS IMPORT CORPORATION LTD.
versus
STATE OF KARNATAKA AND OTHERS

Karnataka Sales Tax Act, 1957; Section 8, Fifth Schedule (Entry 31-B / Entry 51) – Exemption on Sugar – Scope of pre-2001 entry – Retrospective withdrawal of exemption via Karnataka Act No. 5 of 2001 – Reassessment, Penalty and Interest - Scope of Pre-2001 Exemption Entry: Prior to Karnataka Act No. 5 of 2001, imported sugar fell within the exemption entry relating to “sugar” under the Fifth Schedule to the KST Act - The reference in the entry to the Additional Duties of Excise (Goods of Special Importance) Act, 1957 was incorporated solely for identifying and describing the commodity and did not introduce an origin-based or territorial limitation excluding imported goods - Strict construction requires interpreting the entry according to its text without reading in words of limitation such as “produced or manufactured in India” before they were expressly enacted. [Relied on *State of Kerala v. State Trading Corporation of India Ltd.*, (1999) 9 SCC 102; *Govind Saran Ganga Saran v. Commissioner of Sales Tax*, 1985 Supp SCC 205; *Mathuram Agrawal v. State of Madhya Pradesh*, (1999) 8 SCC 667; Paras 16–18, 40–44, 53, 56–88]

Validity of Retrospective Amendment (Karnataka Act No. 5 of 2001): The insertion of the words “produced or manufactured in India” with retrospective effect via a deeming clause is substantively a withdrawal/restriction of an exemption and not merely clarificatory - The State Legislature possesses plenary competence under Entry 54 of List II to enact retrospective fiscal legislation, grant exemptions, and subsequently withdraw or restrict them in public interest - Retrospective withdrawal of a fiscal exemption is not unconstitutional *per se*. [Relied on *Rai Ramkrishna v. State of Bihar*, AIR 1963 SC 1667; *Epari Chinna Krishna Moorthy v. State of Orissa*, AIR 1964 SC 1581; *M/s. Hiralal Rattanlal v. State of U.P.*, (1973) 1 SCC 216; *Shri Prithvi Cotton Mills Ltd. v. Broach Borough Municipality*, (1969) 2 SCC 283; *P. Kannadasan v. State of Tamil Nadu*, (1996) 5 SCC 670; *Kasinka Trading v. Union of India*, (1995) 1 SCC 274; *Shrijee Sales Corporation v. Union of India*, (1997) 3 SCC 398; *Empire Industries Ltd. v. Union of India*, (1985) 3 SCC 314; *R.C. Tobacco (P) Ltd. v. Union of India*, (2005) 7 SCC 725; *CIT v. Vatika Township (P) Ltd.*, (2015) 1 SCC 1; Paras 64–71, 80–88]

Limits on Enforcement of Retrospective Levy – Penalty and Interest - Retrospectivity cannot be enforced in a penal or oppressive manner against dealers who acted strictly under the earlier exemption regime, whose original assessments were completed as exempt by the department, and who did not collect indirect tax from purchasers - While the State is entitled to determine and recover the principal tax liability upon lawful reassessment, no penalty can be imposed for past periods since penalty presupposes contumacious conduct, culpable failure, or deliberate breach of an existing obligation - interest cannot be levied retrospectively from the date of the original transactions or assessment periods, as doing so would operate punitively; interest shall run only from the date of a fresh lawful demand raised pursuant to reassessment. [Paras 72–84, 88– 91]

Central Sales Tax Act, 1956; Section 8(2) – Inter-State Sales Reassessment - Retrospective amendments under State law do not dispense with the statutory rate and conditions mandated under the Central Sales Tax Act - Reassessment of tax on inter-State sales must be strictly recomputed in terms of the applicable provisions of the CST Act, including Section 8(2), after providing a hearing to the assesseees.

[Paras 85–87, 88(ix), 91(d)]

For Appellant(s): Mr. Kiran Kumar Patra, AOR Mr. Preetish Sahu, Adv. Ms. Abhilasa Pathak, Adv. M/S. Parekh & Co., AOR Mr. S.K. Bagaria, Sr. Adv. Mr. E.R. Kumar, Adv. Ms. Pratyusha Priyadarshini, Adv. Mr. Dilpreet Singh Dardi, Adv.

For Respondent(s): Mr. Muhammad Ali Khan, A.A.G. Mr. Sanchit Garga, AOR Mr. Omar Hoda, Adv. Mr. Kunal Rana, Adv. Mr. Shashwat Jaiswal, Adv. Ms. Patil Rekha Chandra Gouda, AOR

J U D G M E N T

ARAVIND KUMAR J.

1. Leave granted in SLP(C) No. 25469 of 2009.
2. These appeals raise a question concerning the true scope of an exemption granted to “sugar” under the Karnataka Sales Tax Act, 1957, and the legal effect of a subsequent legislative amendment by which such exemption was confined to sugar “produced or manufactured in India” with retrospective effect. The controversy is not merely whether a fiscal enactment can operate retrospectively. The larger issue is whether a commodity which stood exempted under the statutory entry as it then read, and which was so treated by the taxing authority itself, can thereafter be retrospectively excluded from the exemption and subjected to tax for past periods, together with the incidents of penalty and interest.
3. The appeals arise out of the common judgment dated 26.11.2007 passed by the Division Bench of the High Court of Karnataka, whereby the appeals preferred by the State were allowed, the orders passed by the Single Judge were set aside, and the retrospective amendment made to the exemption entry relating to “sugar” was upheld. The Single Judge had earlier struck down the retrospective operation of the amendment on the ground that it imposed an unreasonable burden on dealers who had not collected tax during the relevant assessment periods.
4. Since the statutory amendment, the relevant facts, the question of interpretation, and the constitutional challenge are common, both appeals are disposed of by this common judgment.

I. FACTUAL BACKGROUND

5. The Karnataka Sales Tax Act, 1957, hereinafter referred to as “the KST Act”, was enacted to provide for levy of tax on sale or purchase of goods in the State of Karnataka. Section 8 of the KST Act provided for exemption from tax in respect of goods specified in the Fifth Schedule. The provision, as relevant for the present controversy, reads as follows:

“8. Exemption of tax.

No tax shall be payable under this Act on the sale of goods specified in the Fifth Schedule subject to the conditions and exceptions, if any, set out therein.”

6. Sugar found place in the Fifth Schedule as an exempted commodity. The history of the entry assumes significance, for the answer to the present dispute turns largely upon the manner in which the Legislature described the commodity before Karnataka Act No. 5 of 2001 came into force.

7. Entry 31-B, as originally inserted in the Fifth Schedule, exempted:
“Sugar other than sugar candy, confectionery and the like.”
8. With effect from 01.04.1986, the entry was amended to read:
“Sugar including sugar candy but excluding confectionery and the like.”
9. With effect from 01.04.1992, the entry was further amended to read:
“Sugar as described from time to time in Column 3 of the First Schedule to the Additional Duties of Excise (Goods of Special Importance) Act, 1957, but excluding confectionery and the like.”
10. With effect from 01.04.1998, the entry stood renumbered as Entry 51 and continued, in substance, as:
“Sugar as described from time to time in Column 3 of the First Schedule to the Additional Duties of Excise (Goods of Special Importance) Act, 1957.”
11. It is thus clear that prior to the amendment brought about in 2001, the exemption entry used the expression “sugar”. It did not use the words “sugar produced in India”, “sugar manufactured in India”, “indigenous sugar”, or any equivalent expression which could, on its own terms, restrict the exemption by reference to the place of production or manufacture.
12. The appellant in Civil Appeal No. 48 of 2009, Asia Sugar & Chemical Co., was engaged in the business of trade in sugar and had imported substantial quantities of sugar during the period 1994 to 1996. The appellant in the connected appeal, M/s Indian Sugar and General Export Import Corporation Ltd., was registered under the KST Act and the Central Sales Tax Act, 1956, and was also dealing in imported sugar.
13. During the relevant assessment periods, the assessees imported sugar from outside the country and sold the same either within the State of Karnataka or in the course of interState trade. Their case is that they proceeded on the footing that sugar, including imported sugar, was exempt under the Fifth Schedule and that, acting on such understanding, they did not charge or collect sales tax from their purchasers.
14. This aspect is not a matter of mere equity. It has a direct bearing on the nature of the burden now sought to be imposed. Sales tax, in its ordinary commercial operation, is collected by the dealer from the purchaser and is thereafter paid to the State. Where the commodity is treated as exempt, the dealer does not collect tax. If, years later, the law is retrospectively amended and the dealer is called upon to pay tax for past transactions, the burden is not passed on in the ordinary manner. It rests upon the dealer himself.
15. The original assessments were completed by granting exemption on imported sugar. In the case of Asia Sugar & Chemical Co., the reassessment notice itself records that exemption had earlier been allowed on transactions of imported sugar by treating the goods as falling under Entry 31-B of the Fifth Schedule and by relying upon the judgment of this Court in ***State of Kerala and Another v. State Trading Corporation of India Ltd.***¹
16. The relevance of the said decision may be noticed at this stage. In ***State Trading Corporation of India Ltd. v. Assistant Commissioner (Assessment-I), Special Circle, Trivandrum***,² the Kerala High Court considered whether imported sugar was exempt from sales tax where the exemption entry adopted the definition of sugar from the Central

¹ (1999) 9 SCC 102

² (1986) 61 STC 190 (Ker)

Excise law. The argument on behalf of the State of Kerala was that the description of sugar in the excise entry was confined to sugar produced in India. The Kerala High Court rejected the said argument. It held that the definition had been borrowed for the limited purpose of identifying the commodity and not for incorporating a territorial limitation.

17. The Kerala High Court reasoned that the phraseology in the excise statute could not be bodily lifted so as to add words such as “in India” after the word “factory” in the definition of sugar, when the sales tax statute itself did not so provide. The Court observed, in substance, that the expression had been borrowed only to define what sugar is for the purpose of the sales tax exemption. The decision was affirmed by this Court in **State of Kerala and Another v. State Trading Corporation of India Ltd.** (supra)

18. The position, therefore, prior to 2001, was that the exemption entry in Karnataka contained no origin-based limitation, and the prevailing judicial understanding in relation to similarly worded exemption provisions was that imported sugar was not excluded merely because it was imported.

19. Thereafter, Karnataka Act No. 5 of 2001 came to be enacted. The relevant amendment inserted the words “produced or manufactured in India” after the word “Sugar”. The amendment was given retrospective operation through a deeming clause. The material part reads thus:

“In the Karnataka Sales Tax Act, 1957, in the entries relating to Serial No. 51 as it exists from the first day of April, 1998, after the word ‘Sugar’, the words and brackets ‘produced or manufactured in India’ shall be and shall be deemed always to have been inserted.”

20. Simultaneously, a separate entry was introduced in respect of sugar imported from outside the country. The consequence of the amendment was that exemption came to be confined to sugar produced or manufactured in India. Imported sugar, which had earlier been treated as falling within the exempted commodity “sugar”, was retrospectively excluded from the exemption.

21. Pursuant to the amendment, reassessment proceedings were initiated. Notices were issued under Section 9(2) of the Central Sales Tax Act, 1956 read with Section 12-A of the KST Act. The basis of reassessment was that by virtue of the retrospective amendment, imported sugar was not entitled to the exemption earlier granted.

22. In the case of Asia Sugar & Chemical Co., notice dated 16.01.2003 was issued proposing reassessment for the period 03.12.1994 to 31.03.1995. The notice recorded that exemption had earlier been allowed on sales of sugar in the course of inter-State trade and on stock transfers outside the State aggregating to Rs.9,02,52,932. Reassessment order was thereafter passed imposing tax of Rs.90,25,293 for the period 03.12.1994 to 31.03.1995. Similar proceedings were initiated for the subsequent period.

23. In the case of M/s Indian Sugar and General Export Import Corporation Ltd., the authority imposed tax on sale of imported sugar at 4% for assessment years 1994-95 and 1995-96 under the KST Act. The assessee further contended that on inter-State sales, tax was imposed at 10%, ignoring Section 8(2) of the Central Sales Tax Act, 1956.

24. The assessees approached the High Court of Karnataka challenging the constitutional validity of the retrospective insertion of the words “produced or manufactured in India” and the consequential reassessment orders.

25. The Single Judge of the High Court, by common order dated 26.05.2003, struck down the retrospective operation of the amendment as violative of Article 19(1)(g) of the Constitution. The Single Judge reasoned that the amendment imposed an unexpected

and unreasonable burden on dealers who had acted under the exemption regime and had not collected tax from their purchasers. The reassessment and revision orders were accordingly set aside.

26. The State preferred writ appeals. The Division Bench of the High Court, by common judgment dated 26.11.2007, allowed the appeals, set aside the orders of the Single Judge, upheld the retrospective amendment, and restored the reassessment proceedings. The correctness of the said judgment is now before us.

II. SUBMISSIONS

A. SUBMISSIONS ON BEHALF OF THE ASSESSEES

27. Learned Senior Counsel appearing for the assesseees submitted that the entire case must be tested on the language of the exemption entry as it stood prior to the amendment of 2001. It was urged that the entry exempted “sugar” simpliciter. Neither Entry 31-B nor the later renumbered Entry 51 contained any words restricting exemption to sugar produced or manufactured in India.

28. Learned Senior Counsel submitted that the Legislature amended the entry on more than one occasion, including in 1986 and 1992. On neither occasion did it restrict exemption to domestic sugar. It was urged that when the Legislature consciously used the expression “sugar” and did not add any words of limitation, the Court cannot supply such words by implication.

29. It was further submitted that the reference to the Additional Duties of Excise (Goods of Special Importance) Act, 1957 was for the limited purpose of identifying the commodity. It was not an incorporation of the entire excise scheme. According to learned Senior Counsel, the State seeks to convert a description of goods into a condition of origin, which the text of the entry does not permit.

30. It was further submitted that this understanding was not confined to the assesseees. The Department itself granted exemption in the original assessments. The reassessment notice in the case of Asia Sugar & Chemical Co. records that exemption was allowed in reliance on ***State of Kerala and Another v. State Trading Corporation of India Ltd.*** (supra)

31. Learned Senior Counsel submitted that Karnataka Act No. 5 of 2001 was not clarificatory. It introduced, for the first time, a source-based distinction by inserting the words “produced or manufactured in India”. The amendment, therefore, was a substantive withdrawal of exemption.

32. It was further submitted that though retrospective fiscal legislation is not unknown to law, the retrospective operation in the present case is unconstitutional to the extent it imposes a burden on completed transactions. The assesseees had not collected tax. The assessments had been completed. The transactions had attained finality. To compel payment years later would convert what is ordinarily an indirect tax into a direct burden on the dealer.

33. Learned Senior Counsel submitted that the Single Judge correctly appreciated the factual and constitutional dimension of the case. According to him, the Division Bench confined itself to legislative competence and failed to examine the manner in which the retrospective levy operated upon the assesseees.

34. On the Central Sales Tax aspect, it was submitted that the authorities had applied the rate of 10% on inter-State sales without proper regard to Section 8(2) of the Central

Sales Tax Act, 1956. It was urged that the reassessment orders, in any event, require interference on this ground.

B. SUBMISSIONS ON BEHALF OF THE STATE

35. Learned counsel appearing for the State submitted that the Legislature was competent to amend the KST Act and to withdraw or restrict an exemption. It was urged that exemption is a matter of fiscal policy and no dealer can claim a vested right that an exemption must continue either prospectively or retrospectively.

36. It was submitted that the exemption entry relating to sugar had always to be understood in the context of the Additional Duties of Excise regime. The exemption, according to the State, was intended for sugar produced or manufactured in India and not for imported sugar which did not stand on the same footing for the purposes of additional duties of excise.

37. Learned counsel further submitted that the Legislature, having noticed the unintended consequence of the earlier wording, inserted the words “produced or manufactured in India” with a deeming clause. Once the Legislature has expressly declared that the words shall be deemed always to have been inserted, the Court must give full effect to the legal fiction.

38. It was further submitted that retrospective fiscal legislation is valid if the Legislature has competence. According to the State, hardship to an assessee is not a ground to strike down a taxing statute. The Division Bench, it was urged, correctly restored the reassessment proceedings.

39. With regard to computation under the Central Sales Tax Act, it was submitted that if any limited arithmetical or raterelated grievance survives, the same may be examined by the assessing authority in accordance with law. Such grievance, however, cannot affect the validity of the amendment.

III. QUESTIONS FOR CONSIDERATION

40. On the rival submissions and the statutory scheme noticed above, the following questions arise for consideration:

- i. Whether imported sugar was covered by the exemption entry relating to “sugar” in the Fifth Schedule to the Karnataka Sales Tax Act, 1957 prior to Karnataka Act No. 5 of 2001?
- ii. Whether Karnataka Act No. 5 of 2001, inserting the words “produced or manufactured in India” with retrospective effect, is within the legislative competence of the State and constitutionally valid?
- iii. Whether the retrospective operation of the amendment can be enforced without qualification against dealers who had acted under the earlier exemption regime, whose assessments had been completed, and who had not collected tax from purchasers?
- iv. What consequential relief should follow in respect of reassessment, penalty, interest, and computation under the Central Sales Tax Act, 1956?

IV. GOVERNING PRINCIPLES

41. Since the questions raised lie at the intersection of statutory interpretation, exemption, legislative validation and constitutional limits on retrospective taxation, it would be apposite to first notice the governing principles.

42. A taxing statute has to be construed on the strength of its own language. In **Govind Saran Ganga Saran v. Commissioner of Sales Tax**³, this Court emphasized that the components of a tax must be clear. The subject of tax, the person liable, the rate and the measure must all be ascertainable. If any of these elements is uncertain, the levy cannot be sustained by intendment.

43. In **Mathuram Agrawal v. State of Madhya Pradesh**⁴, this Court reiterated that in a taxing statute one has to look merely at what is clearly said. There is no room for intendment. Nothing is to be read in and nothing is to be implied. The Court is not entitled to fill gaps in a charging or taxing provision on considerations of supposed legislative policy.

44. The same discipline applies while construing an exemption entry. It is no doubt true that a person claiming exemption must bring himself within the exemption. But where the entry describes a commodity in clear terms, the Court cannot curtail that description by adding words which the Legislature did not employ. Strict construction does not mean strained construction. It means construction according to the text.

45. The second set of principles concerns retrospective fiscal legislation. In **Rai Ramkrishna and Others Etc. v. State of Bihar**⁵, this Court held that a taxing statute is not unconstitutional merely because it operates retrospectively. The power of the Legislature to enact retrospective fiscal laws is well recognized. In **Epari Chinna Krishna Moorthy v. State of Orissa and Others**⁶, and **M/s. Hiralal Rattanlal Etc. Etc. v. State of U.P. and Another Etc. Etc.**,⁷ this Court upheld retrospective sales tax legislation and validation laws, subject to legislative competence and constitutional limitations.

46. The leading authority on validation laws is **Shri Prithvi Cotton Mills Ltd. and Another v. Broach Borough Municipality and Others**⁸. The principle stated therein is that where a tax has been invalidly imposed for want of power or on account of some defect, the Legislature may remove the defect and validate the levy retrospectively, provided it has competence to do so. The Court explained that the Legislature does not overrule a judgment merely by saying so. It must remove the basis of the judgment by enacting a valid law.

47. In **P. Kannadasan and Others v. State of Tamil Nadu and Others**⁹, the same principle was reiterated. A Legislature may change the law retrospectively and thereby alter the legal foundation on which a judgment rests. It cannot, however, exercise judicial power by merely declaring a judgment to be incorrect.

48. The third principle concerns exemption as a matter of fiscal policy. In **Kasinka Trading and Another v. Union of India and Another**¹⁰, this Court held that an exemption granted in public interest can be withdrawn in public interest. In **Shrijee Sales Corporation and Another v. Union of India**¹¹, this Court reiterated that public interest may justify withdrawal of an exemption and that no assessee can insist on continuation of a concession contrary to policy.

³ 1985 Supp SCC 205

⁴ (1999) 8 SCC 667

⁵ AIR 1963 SC 1667

⁶ AIR 1964 SC 1581

⁷ (1973) 1 SCC 216

⁸ (1969) 2 SCC 283

⁹ (1996) 5 SCC 670

¹⁰ (1995) 1 SCC 274

¹¹ (1997) 3 SCC 398

49. The fourth principle is equally important. Retrospectivity, though permissible, is not immune from constitutional scrutiny. In ***Empire Industries Limited and Others v. Union of India and Others***¹², this Court upheld retrospective fiscal legislation, but made it clear that the question in such cases is whether the retrospective operation is unreasonable. In ***R.C. Tobacco (P) Ltd. and Another v. Union of India and Another***¹³, this Court upheld retrospective withdrawal of an exemption, but observed that the unreasonableness of retrospectivity must be founded on the facts of the particular case.

50. In ***D. Cawasji & Co. v. State of Mysore***¹⁴, this Court was concerned with a retrospective amendment imposing a heavy burden after a long lapse of time. The decision is not an authority for the proposition that retrospective fiscal legislation is per se invalid. It is an authority for the more measured proposition that the duration, purpose and impact of retrospectivity are relevant in testing constitutional reasonableness.

51. In ***Commissioner of Income Tax (Central)-I, New Delhi v. Vatika Township Private Limited***¹⁵, this Court restated the general principle that legislation which imposes a new burden or attaches a new disability is ordinarily presumed to be prospective unless the language clearly indicates otherwise. Where the language is clear, the presumption yields. However, clarity of language answers only the interpretive question. It does not altogether exclude constitutional scrutiny where the burden imposed is said to be unreasonable.

52. It is with these principles in mind that the questions arising in the present appeals must be answered.

V. ISSUE NO. I: WHETHER IMPORTED SUGAR WAS COVERED BY THE PRE-2001 EXEMPTION ENTRY

53. The first issue is one of interpretation of the exemption entry as it stood before Karnataka Act No. 5 of 2001. The entry exempted “sugar”. After 01.04.1992, it described sugar by reference to Column 3 of the First Schedule to the Additional Duties of Excise (Goods of Special Importance) Act, 1957. The question is whether such reference excluded imported sugar.

54. The contention of the State is that the reference to the Additional Duties of Excise Act necessarily confines the entry to sugar produced or manufactured in India. The contention of the assessee is that the reference was only to identify the commodity.

55. The submission of the assessee merits acceptance.

56. A statutory entry may incorporate a definition from another enactment for different purposes. It may incorporate the entire scheme of the other enactment, or it may merely borrow a description for identifying the commodity. The answer depends upon the text, context and purpose of incorporation. In the present case, the exemption entry did not refer to liability to additional duties of excise. It referred to “sugar as described” in the First Schedule to the Additional Duties of Excise Act. The expression “as described” is significant. It identifies the goods. It does not, without more, import an origin-based limitation.

57. The Kerala High Court in ***State Trading Corporation of India Ltd. v. Assistant Commissioner (Assessment-I), Special Circle, Trivandrum*** (supra), dealt with the very

¹² (1985) 3 SCC 314

¹³ (2005) 7 SCC 725

¹⁴ 1984 Supp SCC 490

¹⁵ (2015) 1 SCC 1

nature of this argument. The relevant entry in the Kerala statute exempted sugar by referring to the definition in the Central Excise law. The contention advanced by the State was that the excise description applied only to sugar produced in India. Repelling the contention, the High Court held that the definition of “sugar” had been borrowed for the purpose of the sales tax exemption only to identify what sugar is.

58. The Kerala High Court observed, in substance, that it would not be justified, in the absence of legislative indication, to give a strained interpretation to the definition of sugar by adding the words “in India” after the word “factory”. It further observed that the object of incorporation was only to define sugar for the purpose of the sales tax exemption and not to apply the provisions of the Excise Act to the Sales Tax Act.

59. The said view was affirmed by this Court in **State of Kerala and Another v. State Trading Corporation of India Ltd.** (supra). The said decision, though arising under the Kerala statute, is of considerable persuasive value because the nature of the commodity description and the argument of origin-based exclusion were substantially similar.

60. The conduct of the Karnataka Department itself is consistent with this understanding. The original assessments granted exemption on imported sugar. The reassessment notice issued to Asia Sugar & Chemical Co. expressly records that exemption had earlier been allowed on the basis of Entry 31-B and the judgment in **State of Kerala and Another v. State Trading Corporation of India Ltd.** (supra)

61. The State’s contention that imported sugar did not bear additional duties of excise in the same manner as domestic sugar may furnish a reason why the Legislature later chose to amend the entry. But such reason cannot be used to rewrite the earlier entry. If the exemption was intended to be confined to domestic sugar, the Legislature could have said so. It eventually did so in 2001. That later amendment is the best indication that words of limitation were introduced only thereafter.

62. To accept the State’s argument would be to read into the pre-2001 entry words which were not there. It would amount to saying that “sugar” meant “sugar produced or manufactured in India” even before the Legislature inserted those very words. Such an approach would offend the settled rule of strict construction in taxing statutes.

63. We therefore hold that prior to Karnataka Act No. 5 of 2001, imported sugar was covered by the exemption entry relating to sugar in the Fifth Schedule to the KST Act.

VI. ISSUE NO. II: VALIDITY OF KARNATAKA ACT NO. 5 OF 2001

64. The next question is whether Karnataka Act No. 5 of 2001, which inserted the words “produced or manufactured in India” with retrospective effect, is constitutionally valid.

65. At the outset, it must be stated that the amendment is not merely clarificatory. Once it is held that imported sugar was covered by the exemption before 2001, the amendment cannot be characterized as a mere explanation of an existing legal position. It altered the legal position. It withdrew the exemption from imported sugar retrospectively.

66. However, this conclusion does not by itself invalidate the amendment. The State Legislature, at the relevant time, had legislative competence under Entry 54 of List II to levy tax on sale or purchase of goods. The power to levy tax includes the power to grant exemption. The power to grant exemption includes the power to withdraw or restrict exemption.

67. The law in **Kasinka Trading and Another v. Union of India and Another** (supra), and **Shrijee Sales Corporation and Another v. Union of India** (supra), makes it clear

that exemption is a matter of fiscal policy. A concession granted by the State does not create an indefeasible right that it shall continue. Public interest and revenue considerations may justify withdrawal.

68. Nor can the amendment be invalidated merely because the withdrawal has been made retrospective. In ***Rai Ramkrishna and Others Etc. v. State of Bihar*** (supra), this Court recognized that retrospective taxation is within legislative power, subject to constitutional restraints. In ***Epari Chinna Krishna Moorthy v. State of Orissa and Others*** (supra), and ***M/s. Hiralal Rattanlal Etc. Etc. v. State of U.P. and Another Etc. Etc.*** (supra), retrospective validation of sales tax legislation was upheld. In ***P. Kannadasan and Others v. State of Tamil Nadu and Others*** (supra), this Court again recognized the power of the Legislature to retrospectively alter the law, provided it acts within its legislative field.

69. The amendment in the present case uses clear language. The words “produced or manufactured in India” are inserted with a declaration that they shall be deemed always to have been inserted. The intention to give retrospective effect is therefore manifest.

70. The contention that the amendment is beyond legislative competence is accordingly rejected. The contention that retrospectivity by itself renders the law unconstitutional is also rejected.

71. We hold that Karnataka Act No. 5 of 2001 is within legislative competence and is constitutionally valid.

VII. ISSUE NO. III: WHETHER THE RETROSPECTIVE LEVY CAN BE ENFORCED WITHOUT QUALIFICATION

72. The more difficult question is not whether the law is valid, but how far its retrospective consequences can be enforced against the assesseees.

73. The State contends that once the amendment is valid, all reassessments must stand in full. The assesseees contend that the retrospective levy must fail altogether. Neither extreme, in our view, does complete justice to the legal position.

74. Five facts must be kept in the forefront:

First, prior to the amendment of 2001, imported sugar was covered by the exemption entry.

Secondly, the Department itself completed the original assessments by granting exemption.

Thirdly, the assesseees did not collect tax from purchasers.

Fourthly, the transactions related to assessment years long prior to the amendment.

Fifthly, reassessment was initiated only because of the retrospective amendment.

75. These facts distinguish the present case from a simple case of validation of a defective levy. This is not a case where a levy always existed and a procedural defect alone was cured. This is a case where an exemption earlier available and acted upon has been retrospectively withdrawn.

76. The distinction is important. A validating law, in the classical sense explained in ***Shri Prithvi Cotton Mills Ltd. and Another v. Broach Borough Municipality and Others*** (supra), removes the defect on account of which the levy failed and validates what could otherwise have been lawfully levied. Here, the Legislature has certainly altered the law retrospectively. It had the competence to do so. But the Court must still examine whether the incidents attached to such retrospective levy, namely penalty and interest for the past period, can follow in the same manner as they would in an ordinary case of default.

77. In *R.C. Tobacco (P) Ltd. and Another v. Union of India and Another* (supra), this Court upheld retrospective withdrawal of exemption, but the judgment itself recognizes that reasonableness of retrospective operation has to be considered with reference to the facts. In *Empire Industries Limited and Others v. Union of India and Others* (supra) retrospective fiscal legislation was upheld, but not on the footing that retrospective operation can never be examined under constitutional standards.

78. In *D. Cawasji & Co. v. State of Mysore* (supra), this Court cautioned that retrospective taxation may become unreasonable where it imposes an oppressive burden after a long lapse of time. That decision turned on its own facts and does not control the present case in favour of striking down the law. Yet, it indicates that retrospectivity is not merely a matter of legislative draftsmanship. Its effect on past transactions remains relevant.

79. It is here that the nature of sales tax becomes material. A dealer who sells goods ordinarily collects sales tax from the purchaser when the law requires him to do so. If the goods are exempt, he does not collect tax. Where the assessment is completed by granting exemption, the dealer has no reason to retain or reserve any amount towards tax. Years later, when the law is amended retrospectively, he cannot go back to purchasers and recover the tax.

80. The validity of the principal tax liability is one thing. The imposition of penalty is another. Penalty presupposes culpability, default, deliberate breach or at least failure to comply with an existing obligation. It would be contrary to the basic notions of fairness to impose penalty on a dealer who did not collect tax because the statute, the judicial understanding and the Department's own assessment treated the commodity as exempt.

81. Interest also cannot be treated mechanically. Interest in fiscal law is often compensatory. It compensates the State for deprivation of money which ought to have been paid. But where the liability itself is created retrospectively by a subsequent amendment, and where the assessee could not have collected tax at the time of sale, the levy of interest from the date of the original transaction would, in substance, operate punitively.

82. The proper balance, therefore, is to uphold the validity of the amendment and permit determination of principal tax liability, but to prevent retrospective operation from assuming a punitive character.

83. Such an approach gives full effect to legislative will while preserving constitutional fairness. It does not rewrite the amendment. It merely ensures that consequences which presuppose default are not imposed on persons who acted in accordance with the law as it stood and as it was applied by the Department.

84. We therefore hold that the reassessment proceedings may continue for determination of principal tax liability in accordance with law. However, no penalty shall be imposed or recovered for the pre-amendment period. Interest, if otherwise leviable under the statute, shall run only from the date of lawful demand raised pursuant to reassessment after giving effect to this judgment and not from the date of the original transaction or the original assessment period.

VIII. CENTRAL SALES TAX ASPECT

85. The assessees have raised a specific grievance that, in respect of inter-State sales, tax was imposed at 10% ignoring Section 8(2) of the Central Sales Tax Act, 1956. This is a matter of rate and computation.

86. The validity of the retrospective amendment under the KST Act does not dispense with compliance with the Central Sales Tax Act. If tax is to be levied on inter-State sales, the assessing authority must apply the rate and conditions prescribed by the Central Sales Tax Act as applicable for the relevant period.

87. We do not consider it appropriate to finally compute the liability in these appeals. The assessing authority shall recompute the liability, if any, in respect of inter-State sales strictly in accordance with the Central Sales Tax Act, 1956, including Section 8(2), wherever applicable, after affording an opportunity of hearing to the assesseees.

IX. CONCLUSIONS

88. The conclusions reached by us are summarized as follows:

- i.** Prior to Karnataka Act No. 5 of 2001, imported sugar was covered by the exemption entry relating to “sugar” in the Fifth Schedule to the Karnataka Sales Tax Act, 1957.
- ii.** Karnataka Act No. 5 of 2001, inserting the words “produced or manufactured in India” after the word “Sugar” with retrospective deeming effect, is within the legislative competence of the State and is constitutionally valid.
- iii.** The amendment is not merely clarificatory. It substantively restricts an exemption which was earlier available to imported sugar. However, such retrospective restriction is not unconstitutional per se.
- iv.** The Single Judge was not correct in striking down the retrospective operation of the amendment in its entirety.
- v.** The Division Bench was correct in upholding the validity of the amendment, but erred in restoring the reassessment proceedings without protecting the assesseees from penal and oppressive consequences arising solely from retrospectivity.
- vi.** The State is entitled to determine and recover the principal tax liability, if any, upon lawful reassessment and recomputation.
- vii.** No penalty shall be imposed or recovered in respect of transactions effected prior to Karnataka Act No. 5 of 2001.
- viii.** Interest, if otherwise leviable under the statute, shall be computed only from the date of lawful demand pursuant to reassessment after giving effect to this judgment.
- ix.** Any reassessment relating to inter-State sales shall be recomputed strictly in accordance with the Central Sales Tax Act, 1956, including Section 8(2), wherever applicable.

X. OPERATIVE ORDER

89. In view of the foregoing discussion, the appeals are allowed in part.

90. The common judgment dated 26.11.2007 passed by the Division Bench of the High Court of Karnataka is affirmed insofar as it upholds the validity of Karnataka Act No. 5 of 2001 and reverses the declaration of invalidity made by the Single Judge.

91. The said judgment is modified in the following terms:

- a.** The reassessment proceedings may continue only for determination of principal tax liability in accordance with law.
- b.** No penalty shall be imposed or recovered from the assesseees in respect of transactions effected prior to Karnataka Act No. 5 of 2001.

- c.** Interest, if otherwise leviable under the statute, shall be computed only from the date of lawful demand pursuant to reassessment and not from the date of the original transaction or the original assessment period.
- d.** The assessing authority shall recompute the liability, including liability in respect of inter-State sales, strictly in accordance with the Central Sales Tax Act, 1956, including Section 8(2), wherever applicable.
- e.** If any amount has been recovered towards penalty or interest contrary to the above directions, the same shall be adjusted against lawful principal tax dues so determined, and if no such dues remain, the amounts collected and retained in excess of tax determined shall be refunded to the assessee/es in accordance with law.
- 92.** The assessing authority shall complete the consequential exercise after affording reasonable opportunity of hearing to the assessees.
- 93.** The appeals stand disposed of in the aforesaid terms.
- 94.** There shall be no order as to costs.

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