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IN THE HIGH COURT OF KERALA AT ERNAKULAM

PRESENT

THE HONOURABLE MR.JUSTICE K.VINOD CHANDRAN

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THE HONOURABLE MR. JUSTICE T.R.RAVI

FRIDAY, THE 05TH DAY OF JUNE 2020 / 15TH JYAISHTA, 1942

WA.No.2318 OF 2017

AGAINST THE JUDGMENT IN WPC 11326/2017 DATED 17-07-2017 OF HIGH COURT OF KERALA

APPELLANTS:

1 THE ASSISTANT COMMISSIONER (KVAT)
COMMERCIAL TAXES, SPECIAL CIRCLE,KOTTAYAM.686 001.

2 THE COMMISSIONER OF COMMERCIAL TAXES
COMMERCIAL TAXES, SPECIAL CIRCLE,KOTTAYAM.686 001.

3 THE STATE OF KERALA
REPRESENTED BY ITS SECRETARY,TAXES DEPARTMENT,
GOVERNMENT SECRETARIAT,THIRUVANANTHAPURAM.695 001.

4 THE INSPECTING ASSISTANT COMMISSIONER
DEPARTMENT OF COMMERCIAL TAXES,KOTTAYAM.686 001.

BY GOVERNMENT PLEADER

RESPONDENT:

M/S.KUNNATHUKALATHIL JEWELLERS, CHANGANASSERY
KOTTAYAM, REPRESENTED BY ITS MANAGING
PARTNERK.V.VISWANATHAN.686 101.

OTHER PRESENT:

SRI HARISANKAR V MENON
SENIOR GOVERNMENT PLEADER SRI.V.K.SHAMSUDHEEN

THIS WRIT APPEAL HAVING BEEN FINALLY HEARD ON 25-05-2020, THE COURT ON 05-06-2020 DELIVERED THE FOLLOWING:

"C.R"

JUDGMENT

Dated, this the 5th day of June, 2020

Vinod Chandran, J.

The appeal by the State arises from the judgment of the learned Single Judge reducing the tax liability under Section 8(f) for the assessments years 2011-12 and 2012-13, on the finding that the Explanation added in the year 2014 is clarificatory in nature.

2. The brief facts to be noticed are that the assessee engaged in the business of jewelry had its Head Office at Changanacherry and three branches at Kottayam, Thiruvalla and Chengannoor. From the year 2006-2007 onward the assessee was paying tax under Section 8(f) of the Kerala Value Added Tax Act, 2003 (hereinafter "KVAT Act").The assessee on

31.03.2010 closed down the branch at Thiruvalla and from the next assessment year the business is carried on from the Head Office and two branches.

3. The assessee for the year 2010-11 applied for compounding and the issue is said to be pending before the Tribunal in appeal. The Department maintains that the compounded tax to be paid by the assessee is at the percentage prescribed of the tax paid in the previous year, ie, 2009-10 which included the Head Office and three branches. In the year 2011-12 and 2012-13 the assessee again applied for compounding and the same was permitted. The assessee had made an application excluding that portion of the tax paid, attributable to the Thiruvalla Branch for the year 2009-10; in the year 2010-11. The assessee was permitted to pay tax under the compounded provision by Exts.P1 and P1(a) orders dated 13.12.2011 and 04.08.2012. Later notice was issued under Section 25(1) of the KVAT Act and Exts. P4 and

P4(a) orders were passed for the two consecutive years including that portion which was excluded in the previous year, for the purpose of determining the tax payable under the compounding scheme for the years under option. The assessment orders were dated 12.10.2015 and 18.02.2017.

4. The assessee contended before the learned Single Judge that the only measure that could be adopted by the Assessing Officer to correct the mistake if at all occasioned, was the devise of rectification for which limitation is prescribed of four years. The impugned orders were beyond the said period. It was also contended that the relevant Explanation as available in the subject years only excluded the tax paid in respect of a branch that remained closed during the whole of the year 2009-10. This was absurd, unworkable, resulted in immense hardship and was aimed at helping vested interests; was the argument.

5. The learned Single Judge found that the impugned orders were within the limitation period for reason of they being assessment orders passed under Section 25(1) which has a limitation prescribed of five years from the close of the year of assessment. As to the other contentions, the learned Single Judge found that an Explanation introduced in the year 2014 worked to the advantage of dealers and has to be treated as a clarificatory measure; especially following the judgment in Allied Motors Private Limited v. Commissioner of *Income Tax [(1997) 224 ITR 677 (SC)]*.

6. We need not labour much on the question of whether the impugned orders are in the nature of a rectification or an assessment; since there is no appeal by the assessee. The issue also stands covered by another Division Bench of this Court in *Commercial Tax Officer v. Hotel Breezeland Ltd.[2019(2) KLT 432]* (authored by one of us, KVC(J)). The Division Bench

categorically held that though there is a bilateral agreement between the assessee and the department, insofar as application for compounding being accepted and orders issued by the assessing authority; it could not be said that an assessment under Section 25(1) as such cannot be carried out. Often times the provision for compounding determines the tax payable in the year under option on the basis of the tax paid in the previous year or years. The assessments of the previous years may not be completed even by the close of the year under option and hence there is always a possibility of the tax effect in the year under option being more than that provisionally accepted at the time of grant of permission to compound by the assessing authority. Looking at the rules as also the provisions of the Act, it was categorically held that even if the assessee is permitted to pay tax under the compounding provision, there could necessarily be an assessment determining the actual amounts payable

under the compounding provision. This would not detract from the principle of there being a binding contract between the assessee and the department; which is on the aspect of compounding, from which neither can resile from. The binding nature of the agreement between the assessee and the department is insofar as neither being permitted to resile from the compounding provision so as to attempt a regular assessment adopting the complicated process of examination of books of accounts and records.

7. The learned counsel for the assessee Sri.Harisankar V Menon while accepting the said position however, draws a caveat insofar as the compounding provision not intending to tax an assessee more than that, what would necessarily and legally follow from Section 6 which is the charging section. An alternate mode of assessment would not enable the State to levy more tax than that due under the charging provision. It is argued that if the

payment under Section 6 was adopted there would be no liability for the assessee insofar as the branch closed in the previous assessment year. Under the compounding provision hence that portion which could not have been assessed in the year under option could not have been included even for the purpose of determining the compounded tax payable. The learned Counsel would rely on the decisions of the Hon'ble Supreme Court in *State of Kerala v. Builders Association of India [(1997) 104 STC 134]* and a learned Single Judge of this Court in *Kairali Jewelery v. Assistant Commissioner-III [2019(4) KLT 593]*.

8. Learned Senior Government Pleader Sri. Mohammed Rafiq, appearing for the Revenue relies on the decision of yet another Division Bench on the very same facts and provisions; *Fashion Jewellery v. Commercial Tax Officer [2013(4) KHC 78]*. It is argued by Sri.Rafiq that no issue arises as to the

exigibility of tax under Section 6 since the compounding provision is an alternate method requiring determination of tax payable for the year under option on the basis of the tax paid in the previous year or years. The assessee had exercised option quite aware of such determination and cannot challenge the same on the ground of closure of the branch in the previous year; which has no effect by the clear words employed in the statutory provision for compounding. The Explanation added in the year 2014 cannot be said to be clarificatory especially since the entire provision under Section 8(f) was substituted.

9. Section 8(f)as available in the subject assessment year and as amended in the year 2014 have been extracted by the learned Single Judge which we need not repeat. Suffice it to find that the entire provision itself was substituted, on amendment, but however, sub-clause (i) in its effect remained the

same. The tax payable under the year of option was dependent upon the turnover of the previous year and had to be at the rate of 115% of the tax paid or payable, if the turnover for the preceding year was Rs.10 lakhs or below, 120%, if it were above Rs.10 lakhs and up to Rs.40 lakhs, 135%, above Rs.40 lakhs and up to Rupees one crore and 150% above Rupees one crore. The percentage being determined on the highest tax conceded or paid in the three consecutive years preceding the year under option.

10. We need extract only the relevant explanations as it existed in the subject assessment years and that available in the amended section 8(f)(i) in 2014.

<u>As it existed in the subject assessment years:</u>

Explanation 8:- Where a dealer who had opted and paid tax under this clause during previous years with respect to a branch that had remained closed during the whole of the

year 2009-10, for the purpose of determining the compounded tax payable for 2010-2011, the tax paid in respect of that branch shall not be reckoned.

Explanation relied on as it existed after the amendment in the year 2014

Explanation 3. Where a dealer paying tax under this clause, closes a branch duringthe year under option, proportionate reduction considering the number of business places, in the payment shall be granted in the next monthly instalment onwards, for the remaining months of the year".

11. We are unable to agree with the learned Single Judge that Explanation 3 as available in the amended Section 8(f) is clarificatory, for more than one reason. The Hon'ble Supreme Court in *Allied Motors* (supra) was concerned with a proviso inserted to remedy unintended consequences and make the provision workable which also was held to be

supplying an omission in the provision. Section 43B of the Income Tax Act provided that certain deductions of statutory dues allowable in computing the income tax, would only be permitted in the previous year in which such sum is actually paid. This was to ensure that the taxpayers following mercantile system of accounting, having such statutory obligation, do not claim such expenditure without actual payment. Many instances were noticed where the taxpayer had challenged the statutory dues and not made such payments for long years; while claiming the expenditure as a deduction in the year in which the liability is purportedly incurred. However, the language in which the provision was worded caused hardship to some taxpayers like the appellant therein. The appellant had incurred the liability of sales tax in the last quarter of the assessment year, but however paid it only in the next quarter, as permissible under the sales tax

enactment. In the year 1987, with effect from 01.04.1988, a proviso was added making such payments made prior to the date of furnishing of the return of income, allowable deduction in the previous year. In 1989 a further proviso was added in which Explanation 2 also stipulated that the sum payable as found in Section 43B(a) includes any sum the liability for which was incurred in the previous year, though the payment is not made within that year as provided under the relevant law (in that case the sales tax enactment). The second proviso was granted retrospective effect from April 1984 but the first proviso was expressly prospective. The Hon'ble Supreme Court found that the original Section 43B did not intend such hardship to be visited on the taxpayers and the amendments brought in as the first proviso and the second proviso were curative in nature. It was held that the first proviso though prospective in nature cannot be isolated from

Explanation 2 in the second proviso or the main body of Section 43B. Without the first proviso, Explanation 2 alone would not obviate the hardship or unintended consequences of Section 43B and it supplies an obvious omission, was the finding. It was held that but for this proviso the ambit of Section 43B becomes unduly wide bringing within it scope those payments, which were not intended to be prohibited from the category of permissible deductions.

12. In the present case we find no such curative exercise having been carried out by the amendment of 2014. Clause (f) of Section 8 was substituted in its entirety with six explanations where as the original clause (f) had eight explanations. If Explanation 3 in the new clause (f), as introduced in 2014, is found to be clarificatory, it has to be bodily taken out of the amended provision and placed in the un-amended clause (f)

which is not a permissible exercise. The Explanation in the amended clause(f) applies to that provision and not to the earlier one. Clause (f) as amended in 2014 can only apply prospectively and the Explanations therein are intended at explaining the meaning and intendment of the section itself, to clarify any obscurity or vagueness thereat, to make meaningful and workable the dominant object of that particular provision and not do any or all of these with respect to the un-amended provision, which had all-together different explanations [*S.Sundaram Pillai v. V.R.Pattabiraman (1985 1 SCC 591)*].

13. The fact that in the year 2014 the provision was substituted also would not have the effect of it being retrospective. A Division Bench of this Court in *2018(3) KLT 877 [Commercial Tax Officer v. Najeem]* held that it is not an irrefutable rule that a substitution is invariably retrospective. We extract paragraph 16 of the aforesaid judgment:

"16. The power of the legislature to make an amendment, with retrospective effect, is undisputed but the requirement is that unless the same is expressed in clear language or implied, without any scope for doubt, then the amendment would only be prospective. We are of the opinion that when there is a substitution, unless the same is expressed to be prospective the Courts could always interpret it to be retrospective, looking at the scheme of the enactment, the purpose and object of the amendment, especially when the amendment by substitution, was intended at removing an obvious anomaly or correcting a blatant error or obliterating an absurdity or bringing it in consonance with any other law or the Constitution; as was the case in Hassan Co-operative Union. On the other hand an amendment other than by substitution would be retrospective only if it is so expressed or it follows from necessary intendment, as is implicit from the language employed. Otherwise there is no requirement for the legislature to express the retrospectivity; it could very well make a substitution, which would operate from the inception of enactment."

The above reasoning squarely applies. We find that the provision is not clarificatory nor has it any retrospective effect by virtue only of the Finance Act of 2014 having substituted the provision under Section 8(f); which is amended in its entirety.

14. We also pertinently observe that the Explanation relied on by the learned Single Judge does not permit exclusion of the turnover of a closed branch in a previous year for the determination of tax liability under the compounded provision in the year under option. Explanation 3 is specifically with respect to the closing of a branch during the year under option upon which proportionate reduction in the number of business places can be allowed for the purpose of payment from the next monthly installment. To illustrate, if in the year 2011-12 an assessee has business of one Head Office

and three branches which were continued from the earlier year and he applies under the compounding provision the tax liability would be the specified percentage of the highest of the previous three years liability. However, if during the course of the year under option, 2011-12, say in September, one of the branches is closed. The liability from October would be reduced insofar as that portion being excluded. If in the subsequent year 2012-13, the very same provision existed, there could be no reduction claimed insofar as the tax liability for the previous year with respect to the closed branch up to September, 2010; though that branch is not functioned in that subsequent year; which then becomes the year under option.

15. Explanation 3, of the amended Section 8(f) if available in the year 2011-12 and 2012-13 would not enable a reduction insofar as the determination of the quantum of the tax payable under

the compounding provision for the year under option merely for reason of the closure of the business in the previous year, which in the present case is on the last date of closure, ie, 31st of March. Explanations, of the year 2014, speak only of a closure in the year of option and does not reckon a closure in the previous year.

16. We also have to take into account the argument of the learned Counsel that under a compounding provision what is not exigible under regular assessment cannot be taken into account. If a regular assessment had been resorted to definitely there would have been no liability with respect to the closed branch. Explanation 8 as it existed in Section 8(f), in the relevant years, only granted exclusion of the turnover in any previous year of a branch which remained closed for the whole of the year 2009-10. The one out of the three branches of the assessee was closed down on 31.03.2010. There

could have been no exclusion of the turnover of that particular branch since the determination of compounded tax for the year under option, ie, 2010-11 reckoned the tax liability for the previous year at an increased percentage as specified under Section 8(f)(i). This definitely took in the liability of the closed branch also. The assessee definitely could have chosen regular assessment, in which event the assessee would have been assessed only with respect to the Head Office and two branches.

17. *Kairali Jewelery* was in a different context insofar as the liability of a new branch commenced in the course of the year under option. Therein the assessee was a partnership engaged in jewelery business who had also been paying tax on compounded basis. In the year 2012-13 the assessee applied for compounding and the same was permitted. In the course of the year on December 2012 a new branch was commenced. The Explanation under Section

8(f) provided that when a dealer opens a new branch the additional compounded tax payable with respect to that branch, will be average of the tax payable by him in respect of the principal place of business and all branches. The issue arose as to whether such compounded tax for the newly opened branch has to be paid for the entire year. The learned Single Judge found that from April to November since there was no branch functioning or business carried on there was no taxable event under Section 6. The taxable event, of a business being carried on, arose only from December 2012 and hence the average tax computed would have to be proportionally adjusted to the period in which the business was carried on. In the present case, the taxable event insofar as the year under option is with respect to the Head Office and two branches which alone would have been assessed if the assessee had gone under regular assessment. However, the assessee chose to apply for compounding

which alternate mode specifically provided for an enhanced percentage of the turnover for the previous year which took in the business of the 3rd branch also. The assessee had no escape from paying tax on the basis of the earlier turnover since that was an alternate mode available to the assessee for which the assessee had voluntarily opted with open eyes.

18. Now, we have to look at whether the Explanation as available in the relevant years under the un-amended Section 8(f) was absurd or unworkable. Explanation 8 as extracted herein above only provided for deduction of the business of a branch which had remained closed during the whole of the year 2009-10. There is no absurdity in the provision nor can it be found unworkable. Hardship, definitely could be pleaded but is no ground against the taxing statute especially one which provided an alternate mode from that of the rigour of a regular assessment which also was available as an alternative option. The assessee

had a choice not to opt under the compounding provision. Having so opted, he cannot plead hardship and seek modification of the very computation provided in the alternate mode.

19. The option available was very clear insofar as the tax payable under the compounding scheme to be at a percentage above the tax liability of the previous year. The assessee with open eyes applied under the scheme and obtained permission. There was no cause for any exclusion since the closed down branch had business in the previous year for which tax was also paid at the compounded rate. Coming to the relevant years, 2011-12 and 2012-13 again the assessee could not have claimed any deduction since the provision remained as such. If the assessee had closed the branch mid-year in 2009-10, then *Kairali Jewelery* would have applied and could have claimed proportionate reduction in that year of option, which would have reflected in

the subsequent years, if opted. The assessee however carried on that branch's business for the entire year.

20. *Builders Association (supra)* works against the assessee. The alternate method of compounding as held by the Hon'ble Supreme Court saves the assessee from the botheration of book keeping, assessment and appeals and all that it means. As found by the Hon'ble Supreme Court, there is no necessity to enquire and determine the extent or value of goods transferred or the rate applicable to them and so on. The compounding provision evolves a rough and ready method of assessment of tax and leaves it to the assessee to either opt to it or be governed by the normal method. It is merely an alternative method of ascertaining the tax payable which could be availed of by a dealer, if he feels the same advantageous to him. There is no compulsion on the assessee to opt under the compounding scheme.

We do not think that any exclusion of a liability for the previous year can be granted under the provisions under Section 8(f) as it existed in the year 2011-12 and 2012-13. The closure of branch on 31.03.2010 is irrelevant insofar as the tax liability determined in the years 2011-12 and 2012-13 on the basis of the tax conceded or paid in the three consecutive years preceding the year under option.

21. Before we part with the matter we have to notice the reference order of another Division Bench in *State of Kerala v. Raphel T. Joseph [2019(4) KLT 7]*. Therein a totally different question arise insofar as the permission granted under the compounding provision having been resiled from by the Department so as to proceed under Section 25 (1) of the KVAT Act, the regular mode of assessment. Such a question does not arise here and the Department has only computed the amounts given under the compounding provision for which permission was granted by the

department. The permission having been granted, it is a bilateral contract between the assessee and the department which neither can withdraw from. However, the actual amounts payable under the compounding provision could always be the subject of an assessment under Section 25(1) of the KVAT Act; the provisions of which are in pari materia with the KGST Act which is so held in *Hotel Breezeland Limited*.

We hence allow the appeal, setting aside the judgment of the learned Single Judge. No order as to costs.

Sd/-
K. Vinod Chandran,
Judge

Sd/-
T.R.Ravi,
Judge

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