IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

WRIT PETITION NO.1456 OF 2010

Maharashtra Chamber of Housing Industry and another ..Petitioners.

versus

Union of India and others ..Respondents.

WITH

WRIT PETITION NO.845 OF 2006

WITH

APPELLATE SIDE

WRIT PETITION NO.1486 OF 2006

Maharashtra Chamber of Housing Industry and Others ..Petitioners.

Vs.

Union of India and others ..Respondents.

WITH

WRIT PETITION NO.1230 OF 2010

D.B. Realty Limited ..Petitioner.

Vs.

Union of India and others ..Respondents.

WITH

WRIT PETITION NO.1407 OF 2010

M/s. Mayfair Housing Pvt. Ltd. and another ..Petitioners.

Vs.

Union of India and others ..Respondents.

WITH

WRIT PETITION NO.1473 OF 2010

Mighty Construction Private Ltd. ..Petitioner.

Vs.

Union of India and others ..Respondents.

WITH

WRIT PETITION NO.2674 OF 2010

Acme Complexes Private Ltd. and others ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.461 OF 2011

Siroya Developers Pvt. Ltd. and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.1795 OF 2011

Lok Housing and Constructions Ltd. and others ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.2088 OF 2011

Balaji Developers and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.2101 OF 2011

Pratik Construction ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.2436 OF 2011

Arkade Developers Pvt. Ltd. and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION NO.2441 OF 2011

Shubh Associates and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION NO.2442 OF 2011

Atul Property and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION (LODG.) NO.2584 OF 2011

Atul and Arkade Associates and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION (LODG.) NO.2585 OF 2011

Paras and Arkade Associates and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION (LODG.) NO.2586 OF 2011

Arkade Realty and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION (LODG.) NO.2876 OF 2011

Mayfair Maru Developers and others ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

APPELLATE SIDE

WRIT PETITION NO.8577 OF 2011

Maharashtra Chamber of Housing Industry ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.10159 OF 2010

Hiranandani Palace Gardens Pvt. Ltd. ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.10160 OF 2010

Sunny Vista Realtors Pvt. Ltd. ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.10161 OF 2010

Palace Gardens Chennai Sez Pvt. Ltd. ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.4969 OF 2011

The Promoters and Builders Association
of Poona and another ..Petitioners.
Vs.
Union of India and others ..Respondents.

WITH

WRIT PETITION NO.6741 OF 2011

Chamunda Builders and Developers ..Petitioner.
Vs.
Union of India and others ..Respondents.

WITH
WRIT PETITION NO.9357 OF 2011

Shobha Developers ..Petitioner.
Vs.
Union of India and others ..Respondents.

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Mr. J.J. Bhatt, Senior Advocate with Mr. Milind Sathe, Senior Advocate, Mr. P.K. Shroff, Mr. D.V. Deokar, Mr. Vismay Shroff, Mr. Medhavin Bhatt, Mr. Subodh Joshi, Ms. Shivani Bansal and Ms. Jay Gaud and Ms. Rashmi Jha i/b M/s. Parimal K. Shroff & Co. for the Petitioners in W.P. 1456/2010 and W.P.845/2006.

Mr. Y.E. Moomen –for the Petitioners in W.P. 1230/2010.

Mr. Vikram Nankani with Mr. Sushant Murthy and Mr. Monish Ponda, i/b Mr. Madhur R. Baya for the Petitioners in W.P.1407/2010 and ASWP 4969/2011.

Mr. Pralhad Paranjape i/b M/s. Thakore Jariwala & Associates for the Petitioners in W.P.2674/2010.

Mr. V.S. Kapse with Mr. Shailesh Chavan i/b Mr. Rakesh G. Jain for the Petitioners in W.P. 461/2011.

Mr. U.L. Shah with Mr. Sanjay Kotak for the Petitoiners in W.P. 1795/2011.

Mr. V. Sridharan, Senior Advocate with Ms. Beena Pillai for the Petitioners in W.P.2088/2011.

Mr. M.H. Patil with Ms. Aparna Hirandagi and Mr. Sachin Chitnis for the Petitioners in W.P.2101/2011, WPL2876/2011 and ASWP 8577/2011 and W.P.9357/2011.

Mr. Simil Purohit with Mr. Avikshit Moral i/b India Law Aliance for the Petitioners in W.P.2436/2011, W.P.2441/2011, W.P.2442/2011, WPL2584/2011, WPL2585/2011 and WPL 2586/2011.

Mr. Prakash Shah with Mr. Prasad Paranjape, Mr. Jas Sanghavi and Ms. Nehal Parekh i/b PDS Legal for the Petitioners in ASWP

10159/2010, W.P.10160/2010 and WP 10161/2010.

Mr. V. Sridharan, Senior Advocate with Mr. Prakash Shah, Mr. Bharat Raichandani, Mr. Jas Sanghavi, Ms. Nupur Agarwal and Ms. Neha Parekh i/b PDS Legal for the Petitioners in W.P.6741/2011.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Dr. G.R. Sharma, Special counsel, Mr. A.S. Rao, Mr. Rajinder Kumar and Mr. Anurag Gokhale for Respondent No.1 in W.P.1456/2010 and W.P.845/2006.

Mr. R.V. Desai, Senior Advocate with Mr. R.B. Pardeshi for Respondent Nos.4 to 6 in W.P.1456/2010, for Respondents 2 and 3 in W.P. 1407/2010, for Respondents 2 to 4 in W.P.1473/2010, W.P.1230/2010, ASWP 10159/2010, ASW.P.10160/2010, ASW.P.10161/2010, W.P.6741/2011 and for Respondent Nos.2 to 6 in W.P461/2011.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Mr. A.S. Rao, and Mr. Anurag Gokhale for Respondent No.1 in W.P.1230/2010, W.P.1407/2010 and W.P.1473/2010.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Mr. Pradeep S. Jetly, Mr. A.S. Rao, Ms. Suchitra Kamble and Mr. Anurag Gokhale for Respondents in W.P.2674/2010, W.P.461/2011, W.P.1795/2011, W.P.2088/2011, W.P. 2436/2011, W.P.2441/2011, WPL 2585/2011, WPL2586/2011, WPL2876/2011, W.P.2442/2011 and WPL 2584/2011.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Mr. A.S. Rao, Mrs. V.S. Masurkar and Mr. S.P. Shinde for Respondents in W.P.2101/2011 and W.P. 9357/2011.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Mr. Pradeep S. Jetly, Mr. Jitendra B. Mishra and Mr. A.S. Rao, for Respondents in ASWP 8577/2011.

Mr. Darius J. Khambata, Additional Solicitor General with Mr. Afroz Shah, Mr. Aditya N. Mehta, Mr. Gautam Ankhad, Mr. A.S. Rao, Mr. R.

Ashokan and Mr. S.D. Bhosale for Respondents in ASW.P.4969/2011.

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CORAM : DR.D.Y.CHANDRACHUD &
A. A. SAYED, JJ.

19/20 January 2012

ORAL JUDGMENT (PER DR.D.Y.CHANDRACHUD, J.) :

1. The Finance Act 1994 was amended by the Finance Act 2010 to introduce an explanation to Section 65(105)(zzq) and Section 65(105)(zzzh). Besides a new provision was introduced in the form of clause (zzzzu) in Section 65(105). In these proceedings there is a challenge to the constitutional validity of those provisions.

2. Service tax as an economic concept is a value added tax. Parliament legislated in the Finance Act of 1994 to impose a service on taxable services. Section 65 provides for a list of taxable services in clause (105). Section 66 provides for the levy of a tax on the value of taxable services. Section 67 stipulates that the value of any taxable service shall be the gross amount charged by a service provider of such service provided or to be provided by him. Under sub-section (1) of Section 68 the obligation to pay service tax is cast on every person providing a taxable service.

3. In the Finance Act of 2004 clause (zzq) was introduced in Section 65(105) in order to bring within the fold of the expression 'taxable service' any service provided or to be provided to any person, by a commercial concern, in relation to construction service. The expression 'construction service' was defined in clause (30a) to

mean inter alia the construction of a new building or civil structure or repairs, alteration or restoration of a building or civil structure, used, occupied or engaged or to be used, occupied or engaged primarily in commerce or industry. By the Finance Act of 2005 clause (zzzh) was introduced into Section 65(105) so as to bring within the purview of the expression 'taxable service', a service provided or to be provided to any person by any other person "in relation to construction of complex". Simultaneously, clause (25b) was introduced to provide for a definition of the expression "commercial or industrial construction service". Clause (91a) provided for the definition of the expression 'residential complex'.

4. By the Finance Act of 2010 an explanation has been inserted into clause (zzq) and clause (zzzh) of Section 65(105). Clause (zzq) relates to a service provided or to be provided to any person by any other person in relation to commercial or industrial construction and clause (zzzh), a service in relation to the construction of a complex. Both bear the following explanation :

> "[Explanation – For the purposes of this sub-clause, the construction of a new building which is intended for sale, wholly or partly, by a builder or any person authorised by the builder before, during or after construction (except in cases for which no sum is received from or on behalf of the prospective buyer by the builder or the person authorised by the builder before grant of completion certificate by the authority competent to issue such certificate under any law for the time being in force) shall be deemed to be service provided by the builder to the buyer.]"

5. Clause (zzzzu) has been introduced in Section 65(105) as a result of which a service provided or to be provided of the following nature

is also brought in within the purview of a taxable service :

> "(zzzzu) to a buyer, by a builder of a residential complex, or a commercial complex, or any other person authorised by such builder, for providing preferential location or development of such complex but does not include services covered under sub-clauses (zzg), (zzq), (zzzh) and in relation to parking place.
>
> Explanation – For the purposes of this sub-clause, "preferential location" means any location having extra advantage which attracts extra payment over and above the basic sale price."

6. The expression 'commercial or industrial construction' is defined in clause (25b) as follows :

> "(25b) "commercial or industrial construction" means -
>
> (a) construction of a new building or a civil structure or a part thereof; or
> (b) construction of pipeline or conduit; or
> (c) completion and finishing services such as glazing, plastering, painting, floor and wall tiling, wall covering and wall papering, wood and metal joinery and carpentry, fencing and railing, construction of swimming pools, acoustic applications or fittings and other similar services, in relation to building or civil structure; or
> (d) repair, alteration, renovation or restoration of, or similar services in relation to, building or civil structure, pipeline or conduit, which is-
>
> (i) used, or to be used, primarily for; or
> (ii) occupied, or to be occupied, primarily with; or
> (iii) engaged, or to be engaged, primarily in,
>
> commerce or industry, or work intended for commerce or industry, but does not include such services provided in respect of roads, airports, railways, transport terminals, bridges, tunnels and dams."

7. The expression 'construction of complex' is defined in clause (30a) as follows :

"(30a) "construction of complex" means -

(a) construction of a new residential complex or a part thereof; or
(b) completion and finishing services in relation to residential complex such as glazing, plastering, painting, floor and wall tiling, wall covering and wall papering, wood and metal joinery and carpentry, fencing and railing, construction of swimming pools, acoustic applications or fittings and other similar services; or
(c) repair, alteration, renovation or restoration of, or similar services in relation to, residential complex."

8. The expression 'residential complex' is defined in clause (91a) as follows :

"(91a) "residential complex" means any complex comprising of-

(i) a building or buildings, having more than twelve residential units;
(ii) a common area; and
(iii) any one or more of facilities or services such as park, lift, parking space, community hall, common water supply or effluent treatment system,

located within a premises and the layout of such premises is approved by any authority under law for the time being in force, but does not include a complex which is constructed by a person directly engaging any other person for designing or planning of the layout, and the construction of such complex is intended for personal use as residence by such person."

9. The constitutional validity of the explanation which was inserted into clauses (zzq) and (zzzh) of Section 65(105) and of clause (zzzzu) is assailed on behalf of the Petitioners on the following grounds which were urged before the Court :-

i) The amendment is beyond the legislative competence of Parliament since the subject matter of the tax falls within the legislative power of the States under Entry 49 of List II to the Seventh Schedule of the Constitution. The explanation would indicate that it is a transaction of sale or an agreement to sell an immovable property yet to be constructed or under construction and not certified to be complete by the appropriate authority which is sought to be taxed. Unless there is a transaction which involves a transfer of immovable property or a contemplated transfer and a receipt of money, no charge would arise. Hence, the tax is directly one on the transfer of land or buildings and would fall within the legislative competence of the State legislatures under Article 246(3) read with Entry 49 of List II;

ii) By the explanation to clauses (zzq) and (zzzh), the construction of a new building or complex is by a deeming fiction treated to be a service when – (i) The construction is intended for sale; and (ii) Some receipt is envisaged before the grant of a completion certificate by the appropriate authority. According to the Petitioners the tax in pith and substance is not on construction, but on the sale of land and the element of sale is essential to fasten the charge. The sale of immovable property before, during or after construction, but before a completion is granted can by no stretch of imagination be regarded as a service. Once a completion certificate is received, there would be a sale pure and simple. In substance, the tax is on the transfer of land and buildings and therefore a tax on land and buildings within the meaning of Entry 49 of List II;

iii) The provisions of Section 65(105)(zzzzu) are unconstitutional because – (a) No element of service is involved whatsoever since the advantage that is sought to be brought to tax attaches to the preferential location or development of the property; (b)There is no voluntary act of rendering service; (c) The tax must be regarded as a tax on land per se, because it is a tax on location; and (d) What is the preferential location or an extra advantage or a payment over and above the basic sale price is not defined. The provision is therefore vague and suffers from the vice of an excessive delegation of legislative power since the enforcement of the provision is left to the unguided discretion of the administrative authority;

iv) Between a builder and a contractor who constructs a building, there may be a service element involving a service provider and receiver. Between the builder and a buyer there is no provision of service. The title to the building which is under construction vests in the builder. After construction is complete and a final transfer of title takes place, there can in any event be no provision of service;

v) The explanation has brought in two fictions of a deemed service and a deemed service provider which will fall foul of the provisions of Sections 67 and 68 of the Finance Act.

10. On the other hand, the learned Additional Solicitor General of India appearing for the Union of India has urged that -

i) The explanation to clauses (zzq) and (zzzh) does not tax a transfer of property at all. The subject matter of the tax is the service rendered during the course of construction.

Construction is an activity on land or a user of land which does not fall within the ambit of Entry 49 of List II;

ii) The explanation to clauses (zzq) and (zzzh) was enacted to plug a loop hole and to obviate a seepage from the value added net of agreements which intrinsically involved service during the course of construction. Prior to the enactment of the explanation where an agreement to sell was entered into with the builder since the title to the property vested in the builder, the activity of construction was liable to be regarded as a service rendered by the builder or developer to himself. As a result the timing of the execution of the agreement under which a transfer of title took place became crucial, resulting in a loss of revenue. This was sought to be obviated by introducing an explanation. The explanation creates a deeming fiction under which a service is deemed to be provided by the builder to the buyer where (i) There is a intention to sell; and (ii) Atleast some payment has been received from the flat purchaser. These, however, are incidents on the happening of which tax may be charged, but do not form the subject matter of the tax. The tax has not been imposed on the transfer or sale of immovable property. The tax is on a construction service, but is triggered when there is an intent to sell and some payment is received;

iii) In the alternate even if the explanation was to be construed to bring within the ambit of the tax a transfer of property, it is a settled principle of law that a tax on the transfer of property does not fall under Entry 49 of List II;

iv) Construction reasonably construed does involve an element of

service. Even if arguably it were to be suggested that no element of service was involved, that would not impinge on the power of parliament as long as it does not trench upon a subject reserved to the States in the state list of the Seventh Schedule. The affidavit in reply contains a sufficient elaboration of the nature of the service that is provided during the course of construction, to which there is no traverse on the part of the Petitioners;

v) Clause (zzzzu) was introduced to cover diverse services which builders provide under different heads for which charges are levied separately. Parliament has intervened in order to ensure that they do not slip out of the value added tax net. If no charge is levied for a service, no liability would arise. Builders do charge for providing preferential locational and other development amenities which form part of service rendered. There is no vagueness or arbitrariness in the provision.

11. When the validity of a law which imposes tax is called into question, it is necessary for the Court, while interpreting the provisions of the statute to distinguish between the subject matter or the object of the tax, the incidence of the tax and the machinery for collection. The taxing event, as it called in this branch of jurisprudence, determines the object or the event of taxation. The object of the tax or its subject matter determines the character of the tax. The incidence of the tax is distinct from the taxable event. The incidence of the tax identifies, as it were, the person on whom the burden of the tax would fall. The incidence of the tax, it is well settled is not relevant to construing the subject matter of the tax.

The principle that the incidence of the tax does not determine the competence of the legislature which seeks to impose the tax was enunciated by a Constitution bench of the Supreme Court in **Chhotabhai Jethabhai Patel v. Union of India**[1]. The Supreme Court observed that "Under the Indian Constitution the scheme of division of the taxing powers between the Union and the States is not based on any criterion dependent on the incidence of the tax". This distinction was elaborated upon by holding that while an excise duty is a duty on manufacture or production, there is no reason why in theory it cannot be imposed even on a retail sale of the article if the taxing act so provides. Subject to the legislative competence of the taxing authority, the duty can be imposed at the stage which the authority finds to be the most convenient and the most lucrative, but that would be the matter of the machinery of collection and would not affect the essential nature of the tax. The ultimate incidence of the excise duty would be on the consumer who pays as he consumes or expends, but it continues to be a duty of excise levied on production or manufacture of goods, no matter at what stage it is levied. This principle was followed by the Supreme Court in the Constitution Bench decision in **Godfrey Phillips India Limited v. State of Uttar Pradesh**[2]. In the judgment of the Court, delivered by Justice Ruma Pal, the principle was stated to be thus :

> "Classically, a tax is seen as composed of two elements: the person, thing or activity on which the tax is imposed and the incidence of tax. Thus every tax may be levied on an object or an event of taxation. The distinction between the two may not, ultimately, be material in the context of the Indian Constitution as we will find later. But for the time being we may note that

1 AIR 1962 SC 1006.
2 (2005) 2 SCC 515.

> both these elements are distinct from the incidence of taxation. For example the tax may be imposed on goods on the event of their manufacture, sales, import etc. The law imposing the tax may also prescribe the incidence or the manner in which the burden of the tax would fall on any person and would take within itself the amount and measure of tax. The importance of this distinction lies in the fact that in India, the first two have been given a Constitutional status, whereas the incidence of tax would be a matter of statutory detail. The incidence of tax would be relevant in construing whether a tax is a direct or an indirect one. But it would be irrelevant in determining the subject matter of the tax. [See: M/s. Chhotabhai Jethabhai Patel & Co. vs. Union of India & Another[1]]"

12. In **Gujarat Ambuja Cements Ltd. v. Union of India**[3] the Supreme Court emphasized that there is a distinction between the object of tax, the incidence of tax and the machinery for the collection of tax. Legislative competence is to be determined with reference to the object of the levy and not with reference to its incidence or machinery.

13. This principle must be borne in mind by the Court in determining the issue of constitutional validity which arises in the present case. The incidence of the tax, the stage at which it is collected and the machinery which has been laid down by the legislature for the process of collection do not have a bearing on the constitutional validity of the tax imposed. A determination of whether the tax in its true nature is a tax on land and buildings must therefore depend upon the object of taxation or the taxable event on which the charge of tax arises.

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1 AIR 1962 Sc 1006.
3 AIR 2005 SC 3020.

14. The Finance Act of 2004 brought within the fold of taxable services, a service provided or to be provided to any person by a commercial concern in relation to construction service by introducing clause (zzq) in Section 65(105). By the Finance Act of 2005 clause (zzzh) was introduced to bring "the construction of complex" within the ambit of taxable services. Simultaneously, definitions were provided of the expressions 'commercial or industrial construction service' in clause (25b), of the expression 'construction of complex' in clause (30a) and of 'residential complex' in clause (91a).

15. The rationale for the introduction of a service tax on these taxable services found elaboration in circulars of the Central Board of Excise and Customs. On 17 September 2004 the Board issued a circular, when clause (zzq) was on the statute clarifying that services provided by a commercial concern in relation to construction, repair, alteration or restoration of buildings, civil structures, or parts thereof occupied or engaged for the purposes of commerce and industry were covered by the new levy. In this case, the circular noted, the service is essentially provided to a person who gets such construction done by a building or civil contractor. Hence, estate builders who construct buildings or civil structures for themselves (for their own use, for renting out or selling subsequently) were not regarded as taxable service providers. However, if a real estate owner were to hire a contractor, the payment made to a contractor would be subjected to service tax under the head. The circular clarified that the gross value charged by a building contractor would include the cost of materials. The service provider would be eligible to take credit of the excise duty paid on inputs under the Cenvat Credit Rules 2004. Since the

inputs were normally procured from the market and were therefore not covered by duty paying documents, a general exemption was available to goods sold during the course of providing a service, but the exemption was subject to the condition of availability of documentary proof indicating the value of the goods sold. Since in the case of a composite contract, a bifurcation of the value of the goods sold is often difficult, an abatement of 67% was provided in case of composite contracts where the gross amount charged included the value of the material cost.

16. On 29 January 2009, a circular was issued by the Central Board of Excise and Customs recording that once an agreement of sale is entered into with a buyer for a unit in a residential complex, he becomes the owner of the unit and the activity provided by the builder of constructing the unit is a service to the customer on which service tax would be applicable. The contrary view which was expressed was that where a buyer makes a construction linked payment after entering into an agreement to sell, the nature of the transaction is not a service but a sale. Where an agreement to sell is entered into by a buyer with the builder, the property belongs to the builder till the completion of the transaction and any service provided towards construction would be in the nature of 'self service'. The circular of the Board noted that the matter was examined. The Board was of the view that in the case of a mere agreement to sell an interest in the property is not created under the Transfer of Property Act and the property continues to remain in the ownership of the seller. The ownership of the property gets transferred to the ultimate owner only upon the completion of construction. The Board

therefore opined that a service provided by a seller in connection with the construction of a residential complex till the execution of a sale deed would be in the nature of 'self service' and would not attract a liability to pay service tax. However, if the services of a person such as a contractor, designer or a similar service provider were received, then such a person would be liable to pay service tax.

17. The Finance Act of 2010 sought to bring within the field of service tax such cases which may have passed out of the net of value added tax merely on account of the timing of the execution of the agreement. By the amendment, an explanation came to be inserted in clause (zzq) and clause (zzzh) of Section 65(105). The explanation creates a legal fiction. The effect of the fiction is to provide a deeming definition of what constitutes a service provided by the builder to a buyer. The explanation stipulates two pre-requisites before the construction of a new building or a complex is deemed to be a service provided by the builder to a buyer. The first condition is that the construction of a new building or, as the case may be, of a complex must be intended for sale wholly or partly by a builder or a person authorized by him whether before, during or after construction. The second requirement is that a sum must be received from or on behalf of the prospective buyer by the builder before the grant of a completion certificate by the authority competent to issue such a certificate under any law for the time being in force. Intent to sell whether before, during or after construction is therefore made the touchstone of the deeming definition of a service provided by the builder to the buyer. The exception is where no sum has been received by the builder from the

prospective buyer before the grant of a completion certificate, in which case the deeming definition will not apply.

18. The rationale for the introduction of the explanation is contained in a circular issued by the Central Board of Excise and Customs on 26 February 2010. The circular explains that in the definition of 'taxable service' in clauses (zzq) and (zzzh) it is provided that unless the entire consideration for the property is paid after the issuance of a completion certificate, the activity of construction would be deemed to be a taxable service provided by the builder or developer to the prospective buyer and service tax would be charged accordingly. The reason for the explanation emerges from the following extract from the circular :

> "Service tax on construction services
>
> 8.1 The service tax on construction of commercial or industrial construction services was introduced in 2004 and that on construction of complex was introduced in 2005.
>
> 8.2. As regards payment made by the prospective buyers/ flat owners, in few cases the entire consideration is paid after the residential complex has been fully developed. This is in the nature of outright sale of the immovable property and admittedly no Service tax is chargeable on such transfer. However, in most cases, the prospective buyer books a flat before its construction commencement / completion, pays the consideration in installments and takes possession of the property when the entire consideration is paid and the construction is over.
>
> 8.3 In some cases the initial transaction between the buyer and the builder is done through an instrument called 'Agreement to Sell'. At that stage neither the full consideration is paid nor is there any transfer in ownership of the property although an agreement to ultimately sell the property under

settled terms is signed. In other words, the builder continues to remain the legal owner of the property. At the conclusion of the contract and completion of the payments relating thereto, another instrument called 'Sale Deed' is executed on payment of appropriate stamp duty. This instrument represents the legal transfer of property from the promoter to the buyer.

8.4 In other places a different pattern is followed. At the initial stage, instruments are created between the promoter and all the prospective buyers (which may include a person who has provided the vacant land for the construction), known as 'Sale of Undivided Portion of The Land'. This instrument transfers the property right to the buyers though it does not demarcate a part of land, which can be associated with a particular buyer. Since the vacant land has lower value, this system of legal instrumentation has been devised to pay lesser stamp duty. In many cases, an instrument called 'Construction Agreement' is parrallely executed under which the obligations of the promoter to get property constructed and that of the buyer to pay the required consideration are incorporated.

8.5 These different patterns of execution, terms of payment and legal formalities have given rise to confusion, disputes and discrimination in terms of Service tax payment.

8.6. In order to achieve the legislative intent and bring in parity in tax treatment, an Explanation is being inserted to provide that unless the entire payment for the property is paid by the prospective buyer or on his behalf after the completion of construction (including its certification by the local authorities), the activity of construction would be deemed to be a taxable service provided by the builder/ promoter/ developer to the prospective buyer and the Service tax would be charged accordingly. This would only expand the scope of the existing service, which otherwise remain unchanged."

19. The notes on clauses annexed to the Finance Bill of 2010 would indicate that Section 65 was sought to be amended to modify the scope inter alia of certain taxable services by amending, among

others, clauses (zzq) and (zzzh). From the circular issued by the Central Board of Excise and Customs it is evident that in different parts of the country agreements involving the transfer of residential and commercial properties followed various patterns. In certain cases, agreements to sell were entered into, at which stage the full consideration is not paid. The transfer of title to the property would take place on the conclusion of the contract and the completion of payments when a sale deed would be executed with appropriate stamp duty. The sale deed would transfer title from the builder to the buyer. In other parts of the country initially an instrument for the sale of an undivided portion of the land would be executed by which an un- demarcated interest in a portion of the land would be transferred to the buyer. This was a device adopted to reduce the incidence of stamp duty since the vacant land in which an undivided interest was created would have a lower value. Simultaneously a construction agreement would be executed incorporating the obligation of the builder to build and of the buyer to pay the consideration. The legislative intent underlying the explanation was to bring about a parity in tax treatment by stipulating that unless the entire consideration for the property is paid by the prospective buyer after the completion of construction as certified by the local authority, the activity of construction would be deemed to be a taxable service provided by the builder to the prospective buyer. The scope of the existing service was consequently sought to be expanded. The ambit of the expression 'taxable service' in relation to construction service or, as the case may be, the construction of a complex has thus undergone a material change by bringing within the fold of service tax construction services provided by builders to buyers.

20. Explanations to statutory provisions can be of different genres. An explanation may in certain situations provide no more than a clarification of legislative intent by providing a legislative understanding of the meaning of the main provision. But all explanations to statutory provisions need not be clarificatory. There is nothing to prevent the legislature to enact an explanation which is not clarificatory but expansive. As a matter of constitutional principle, there is no fetter on the power of the legislature to enact an explanation which while expounding the content of the main provision actually expands the purview and ambit of the provision. The question is not one of constitutional fetter, but purely one of statutory interpretation. This is, however, subject to the limitation on the legislative competence of the legislature which enacts the law.

21. At this stage, a brief reference may be made to two decisions of the Supreme Court. In **Dattatraya Govind Mahajan v. The State of Maharashtra**[4], the Supreme Court emphasised that while a traditional function of an explanation is to expound the meaning and effect of the provision which it explains, ultimately it is the intention of the legislature which matters :

> "It is true that the orthodox function of an explanation is to explain the meaning and effect of the main provision to which it is an explanation and to clear up any doubt or ambiguity in it. But ultimately it is the intention of the legislature which is paramount and mere use of a label cannot control or deflect such intention. It must be remembered that the legislature has different ways of expressing itself and in the last analysis the words used by the legislature alone are the true repository of the intent of the legislature

4 AIR 1977 SC 915.

> and they must be construed having regard to the context and setting in which they occur. Therefore, even though the provision in question has been called an Explanation, we must construe it according to its plain language and not on any a priori considerations."

22. In an earlier decision in **Hiralal Ratan Lal v. The Sales Tax Officer**[5] the Supreme Court held that if on a true reading of an expression it appears to have widened the scope of the main section, effect must be given to the legislative intent notwithstanding the fact that the legislature labelled it as an explanation. In other words, the nomenclature of a provision in a statute as an explanation is not determinative of its scope. The explanation may in a certain situation do no more than clarify the intent or remove an ambiguity by explaining the provision. In another situation the explanation may widen the ambit of the main provision. In either case the duty of the Court is to determine the true intent of the legislature by construing the words which have been used.

23. The explanation which was inserted by the Finance Act of **2010** clearly brings within the fold of taxable service a construction service provided by the builder to a buyer where there is an intended sale between the parties whether before, during or after construction. No taxable service, however, is to be regarded as having been provided in a situation where no payment whatsoever has been made by the buyer to the builder until receipt of a completion certificate by the competent authority. The explanation was specifically legislated upon to expand the concept of taxable service. Prior to the explanation, the view taken was that since a mere agreement to sell does not

5 AIR 1973 SC 1034.

create any interest in the property and the title to the property continues to remain with the builder, no service was provided to the buyer and the service, if any, would be in the nature of a service rendered by the builder to himself ('self service', to use an inartistic term). Where, however, a builder engages a contractor, the service provided by the contractor to the builder would be within the fold of taxation. The revenue regarded this situation as resulting in slipping out of the net of value added services rendered by builders to buyers. Though under the Transfer of Property Act, 1882 property does not get transferred merely on an agreement to sell, Parliament could while enacting fiscal legislation take account of ground realities. Contracts involving diverse agreements between builders and buyers across the country where the legislature regarded that the transaction did involve an element of service, were sought to be taxed. The element of service evidently according to the legislature remains the same notwithstanding the timing at which a formal document conveying title from the builder to the buyer is executed. The explanation thus reaches out to service provided by builders to buyers in pursuance of an intended sale of immovable property before, during or after construction.

24. Now it is in this background that it is necessary for the Court to address itself to the challenge on the grounds of legislative competence. The submission of the Petitioners is that the tax in question is a tax on land and buildings within the meaning of Entry 49 of List II to the Seventh Schedule and would therefore fall within the exclusive legislative competence of the State legislatures under Article 246(3) of the Constitution.

25. The Supreme Court has dealt with the ambit of Entry **49** of List II in the context of diverse challenges to laws enacted by Parliament. The judgment of the Constitution Bench in **Sudhir Chandra Nawn v. Wealth Tax Officer**[6] negatived a challenge to the constitutional validity of the Wealth Tax Act of **1957** on the ground that Entry **49** of List II contemplates the levy of a tax on land and buildings as units and is a tax which is directly imposed on land and buildings. A tax on the capital value of assets was held not to bear a definable relationship to lands and buildings which may form a component of the total assets of an assessee. In **Second Gift Tax Officer v. D.H. Nazareth**[7] a challenge to the constitutional validity of the Gift Tax Act **1958** was similarly dismissed, overruling an objection that it trenched upon Entry **49** of List II. The principles in these decisions were reiterated by a Bench of seven judges of the Supreme Court in **Union of India v. H.S. Dhillon**[8]. In **India Cement Limited v. State of Tamil Nadu**[9] the Supreme Court once again reiterated the principles which were laid down in the earlier cases and observed that Entry **49** of List II is confined to a tax that is directly levied on land as a unit. A tax which is imposed not directly on land but on a particular user would not fall within the ambit of Entry **49** of List II.

26. The principles which emerge from the decisions of the Supreme Court expounding Entry **49** of List II are as follows :

6 AIR 1969 SC 59.
7 AIR 1970 SC 999.
8 AIR 1972 SC 1061.
9 AIR 1990 SC 85

i) A tax on land and buildings is a tax which is imposed on land and buildings as units;

ii) In order to be a tax on land and buildings, the tax must be directly imposed on land and buildings;

iii) A tax on a particular use of land or of a building or an activity in connection with land or buildings is not a tax on land and buildings;

iv) A tax on a contract or arrangement in relation to land or buildings is not a tax on land and buildings;

v) A tax on income which arises from land or buildings is not a tax on land and buildings; and

vi) A tax on a transaction involving a transmission of title to or a transfer of land and buildings is not a tax on land and buildings under Entry 49 List II.

27. A precise elaboration of these principles is contained in the judgment of the Constitution bench in **D.H. Nazareh** (supra) :

> "The pith and 'substance of Gift Tax Act is to place the tax on the gift of property which may include land and buildings. It is not a tax imposed directly upon lands and buildings but is a tax upon the value of the total gifts made, in a year which is above the exempted limit. There is no tax upon lands or buildings as units of taxation. Indeed the lands and buildings are valued to find out the total amount of the gift and what is taxed is the gift. The value of the lands and buildings is only the measure of the value of the gift. A gift-tax is thus not a tax on lands and buildings as such (which is a tax resting upon general ownership of lands and buildings) but is a levy upon a particular use, which is transmission of title by gift. The two are not the same thing and the incidence of the tax is not the same. Since entry 49 of the State List contemplates a tax directly levied by reason of the general ownership of lands and

> buildings, it cannot include the gift tax as levied by Parliament. "

28. The principles which have been enunciated in the judgments of the Constitution bench of the Supreme Court in **Sudhir Chandra Nawn and Nazareth** and subsequently have been consistently followed. Reference may be made in this context to paragraph **23** of the judgment of the Supreme Court in **India Cement.** In the decision in **State of Bihar v. Indian Aluminium Company**[10] the Supreme Court held that a tax which was levied on the activity of the removal or excavation of land was not a tax on land itself and would therefore fall outside the ambit of Entry **49** of List II. Reliance has also been placed by the Learned Additional Solicitor General on the judgment of a Division Bench of the Gujarat High Court in **Ambalal Maganlal v. Union of India**[11] and on a judgment of a Division Bench of this Court **Manubhai A. Sheth v. N.D. Nirgudkar, 2nd Income Tax Officer**[12] in support of the proposition that a tax on capital gains has been held to be a tax which arises from gains from the transfer of a capital asset and is therefore not a tax within the meaning of Entry **49** of List II. The decision in **Godfrey Phillips** does not mark any departure from the earlier decisions. **Godfrey Phillips** as a matter of fact did not construe Entry **49** of List II.

29. The charge of tax under Section **66** of the Finance Act is on the taxable services defined in clause **(105)** of Section **65.** The charge of tax is on the rendering of a taxable service. The taxable event is the rendering of a service which falls within the description set out

10 AIR 1997 SC 3592.
11 1975 ITR 237,
12 1981 (128) ITR 87.

in sub-clauses (zzq), (zzzh) and (zzzzu). The object of the tax is a levy on services which are made taxable. The fact that a taxable service is rendered in relation to an activity which occurs on land does not render the charging provision as imposing a tax on land and buildings. The charge continues to be a charge on taxable services. The charge is not a charge on land or buildings as a unit. The tax is not on the general ownership of land. The tax is not a tax which is directly imposed on land and buildings. The fact that land is subject to an activity involving construction of a building or a complex does not determine the legislative competence of Parliament. The fact that the activity in question is an activity which is rendered on land does not make the tax a tax on land. The charge is on rendering a taxable service and the fact that the service is rendered in relation to land does not alter the nature or character of the levy. The legislature has expanded the notion of taxable service by incorporating within the ambit of clause (zzq) and clause (zzzh) services rendered by a builder to the buyer in the course of an intended sale whether before, during or after construction. There is a legislative assessment underlying the imposition of the tax which is that during the course of a construction related activity, a service is rendered by the builder to the buyer. Whether that assessment can be challenged in assailing constitutional validity is a separate issue which would be considered a little later. At this stage, what merits emphasis is that the charge which has been imposed by the legislature is on the activity involving the provision of a service by a builder to the buyer in the course of the execution of a contract involving the intended sale of immovable property.

30. Parliament, in bringing about the amendment in question has made a legislative assessment to the effect that a service is rendered by builders to buyers during the course of construction activities. In our view, that legislative assessment does not impinge upon the constitutional validity of the tax once, the true nature and character of the tax is held not to fall within the scope of Entry 49 of List II. So long as the tax does not fall within any head of legislative power reserved to the States, the tax must of necessity fall within the legislative competence of Parliament. This is a settled principle of law, since the residuary power to legislate on a field of legislation which does not fall within the exclusive domain of the States is vested in Parliament under Article 248 read with Entry 97 of List I. However, it would be necessary for the Court to advert to the reply which has been filed on behalf of the Union of India in these proceedings. In paragraph 4 of the affidavit in reply it has been stated that service tax has been levied on account of the activity involving a value addition such as activities undertaken by an architect in designing a building, by civil contractors and engineers in constructing the building and in the provision of other utility services. A sample flat on site is normally made to enable prospective purchasers to envisage the final product. Choices are offered to buyers in respect of flat designs, internal shifting of walls, flooring patterns, wall colours, types of materials used for interior decoration, electrical and plumbing etc. These are also modified and personalized to suit the requirements of the buyer. Value additions and services are provided by developers to buyers when a prospective purchaser purchases a flat or unit before a completion

certificate is obtained. The attention of the Court has also been drawn to the United Nations classification of products and services in which construction services are specifically delineated in Section 5. There is no traverse on the part of the Petitioners of the statements which are contained in the affidavit in reply in which there is a reference to the nature of services rendered by builders to buyers. Be that as it may, we are firmly of the view that the legislative assessment on the basis of which a service tax is levied on the value addition which builders provide to buyers in the form of service rendered in the course of construction and construction related activities can by no stretch of imagination be regarded as so manifestly absurd so as to impinge on the constitutional validity of the provision. It would also be necessary to record that on 1 March 2006 a notification was issued by the Union Ministry of Finance in exercise of powers conferred by Section 93(1) of the Finance Act 1994 to provide for an exemption to the extent of 67% of the gross value of construction. By a subsequent notification dated 22 June 2010, the extent of the exemption has been enhanced to 75% of the gross value. What is taxed therefore is the value addition involved in the rendering of the service.

31. The submission that the explanation brings in two fictions and is ultra vires the provisions of Sections 67 and 68 of the Finance Act is completely lacking in substance. The levy under Section 66 is on the value of taxable services. Section 65(105) defines taxable services. The explanation cannot possibly be held to be ultra vires Sections 67 and 68.

32. The provisions of clause (zzzzu) which were introduced by the Finance Act of 2010 in the provisions of Section 65(105) are also sought to be challenged. The challenge is on the ground that firstly there is no element of service involved and the addition attaches to a location. Secondly, it has been submitted that there is no voluntary act of rendering a service. Thirdly, it has been urged that the tax is a tax on land per se, since it is a tax on location. Fourthly, it has been submitted that the provision is vague and therefore arbitrary since what constitutes a preferential location, an extra advantage or the basic sale price has not been defined.

33. Now what clause (zzzzu) of Section 65(105) brings in are services provided to a buyer by a builder of a residential complex or a commercial complex for providing a preferential location or development of such complex, but to the exclusion of services covered under sub clauses (zzg), (zzq) and (zzzh) and those in relation to parking places. A preferential location is defined to mean any location having extra advantages which attracts extra payment over and above the basic sale price. The circular which was issued by the Central Board of Excise and Customs on 26 February 2010 takes note of the fact that in addition to activities involving construction, completion and furnishing repair, alteration, renovation or restoration builders of residential or commercial complexes provide other facilities and charge separately for them. These charges do not form part of the taxable value for charging of tax. These facilities include – (i) Prime / preferential location charges for allotting a plot or commercial space according to the choice of the buyer; (ii) Internal or external development charges which are collected for developing and

maintaining parks, laying of sewage water pipelines, providing access roads and common lighting and other like charges. Since these charges are in the nature of service provided by the builder to the buyer over and above the construction service, they were brought within the purview of clause **(**zzzzu**)**. In the affidavit in reply that has been filed in these proceedings reference has been made to the fact that builders as a matter of fact charge separately under diverse heads. A special value addition service includes the provision of a flat on a preferred floor to a prospective buyer, a flat facing a particular direction or a particular room in a particular direction. This involves a locational choice of a prospective buyer having an extra advantage for which additional payment is made by the buyer to the builder over and above the basic sale price. These according to the Revenue involve value additions and services when the prospective purchaser purchases a flat or a unit before the completion certificate is obtained. We find merit in the contention which has been urged on behalf of the Revenue that if no charge is levied for a preferential location or development, no service tax would be attracted in the first place. Builders, however, follow the practice of levying charges under diverse heads including preferred development of the property intended to be sold or in terms of a preferred location which is made available to the buyer. Clause **(**zzzzu**)** only intends to obviate a leakage of revenue and plugs a loophole which would have otherwise resulted. To reiterate, if no separate charge is levied, the liability to pay service tax does not arise and it is only where a particular service is separately charged for that the liability to pay service tax arises. The fact that the service is rendered in the context of a location, does not make it a tax on land within the

meaning of Entry 49 of List II. The tax continues to be a tax on the rendering of a service by the builder to the buyer. There is no vagueness and uncertainty. The legislative prescription is clear. Hence, there is no excessive delegation.

34. Before concluding, we may also refer to the decision rendered by this Court in **Retailers Association of India v. Union of India** (Writ Petition 2238 of 2010 and connected petitions decided on 4 August 2011). A Division Bench of this Court rejected a challenge to the levy of service tax in connection with the provision of a service in relation to the renting of immovable property for use in the course of or furtherance of business or commerce. This Court construed the ambit of Entry 49 of List II of the Seventh Schedule in that context. A similar view has also been taken by a Full Bench of the Delhi High Court in **Home Solutions Retails (India) Ltd. v. Union of India** on 23 September 2011 in Writ Petition (Civil) 3398 of 2010 and connected matters.

35. For these reasons we do not find any merit in the constitutional challenges raised in the Petitions. No other submissions, other than those which we have recorded, were urged. The Petitions shall accordingly stand dismissed.

There shall be no order as to costs.

(Dr. D.Y. Chandrachud, J.)

(A. A. Sayed, J.)