

**CONSTITUTIONAL
PROVISIONS
FOR
INDIRECT TAXES.**

Prepared by:-

National Academy of Customs,
Excise and Narcotics,
Kanpur

CONSTITUTIONAL PROVISIONS FOR INDIRECT TAXES.

Article 265 of the Constitution of India says that "*No tax shall be levied or collected except by authority of law*".

2. The Article 13(3) says, "*law includes any ordinance, order, by-law, rule, regulation, notification, customs or usage having in the territory of India, the force of law*".

3. Further, Article 366(10) says that "*existing law*" means any law, any ordinance, order, by-law, rule or regulation passed or made (before the commencement of the Constitution) by any legislative authority or person having power to make such law, any ordinance, order, by-law, rule or regulation.

4. Article 245 enables the Parliament to make laws.

5. Article 246 sets out matters on which laws can be made by Parliament, State legislature or both, by enumerating various matters in three lists- namely, Union list, (ii) State List, and (iii) concurrent List. These lists are contained as List I (Union List), List II (State List) and List III (Concurrent List) in the Seventh Schedule 7 in this constitution.

6. Entries 41, 83, 84, 92C and 97 of List I in the Seventh Schedule are as under:-

Entry 41. Trade and commerce with foreign countries; import and export across customs frontiers; definition of customs frontiers.

Entry 83: Duties of Customs including export duties

Entry 84: Duties of Excise on tobacco and other goods manufactured or produced in India except, –

(a) alcoholic liquors for human consumption

(b) opium, Indian hemp and other narcotic drugs and narcotics,

but including medicinal and toilet preparations containing alcohol or any substance included in sub-para (b) of this entry.

Entry No.92C: Tax on Services [Entry Inserted in the Constitution of India *vide* 88th Constitutional Amendment Act, 2003 (with effect from 15.1.2004)]

[Note: Prior to 15.1.2004, the Service tax was levied by the Parliament under Entry No. 97 of the List I in the Seventh Schedule in the Constitution of India].

Entry No. 97. Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists.

7. State List: Entries relating to State Taxes are as under:-

Entry No. 51. Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India:—

(a) alcoholic liquors for human consumption;

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

Entry No. 54: Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of List I.

Entry No. 60: Taxes on professions, trades, callings and employments.

Entry No. 62. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.

8. **Article 112: This articles deals with Annual financial statement** and it provides as under:-

(1) The President shall in respect of every financial year cause to be laid before both the Houses of Parliament a statement of the estimated receipts and expenditure of the Government of India for that year, in this Part referred to as the "annual financial statement".

Budget is the Annual Financial Statement containing details of Govt's expenditure and estimated revenue receipts.

9. **Article 366-Definitions**

(29A) "tax on the sale or purchase of goods" includes—

- (a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;
- (b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;
- (c) a tax on the delivery of goods on hire-purchase or any system of payment by instalments;
- (d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;
- (e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;
- (f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration,

and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made;

This was introduced by 46th amendment of the Constitution of India.

Need for 46th Constitutional amendment

10. Hon'ble Supreme Court gave restricted meaning to the word "sale of goods" appearing in the State list. Therefore, Sales tax could not be levied in transactions like works contract wherein element of sale as well as service was involved- indivisible works contract, example - inter-state sale from head office to branch office. Therefore, need was felt for amending Constitution to include in article 366 a definition of "tax on the sale or purchase of goods" by inserting a new clause (29A). The definition considered the six types of transactions as deemed sales which were not being considered as sale.

11. The laws relating to collection of Customs duty, Central Excise duty, and Service Tax are as under:-

- a) The Customs Act, 1962 (No. 52 of 1962) commencing from 1st February, 1963 [vide Notification G.S. No. 155 dated 26.1.1963, Gazette of India, Extraordinary, Pt. II Sec. 3(1) of 73].
- b) The Central Excises Act, 1944 (No. 1 of 1944) dated 24th February, 1944, It came into force on 28th February, 1944 [vide Notification No. F.D.C.R.No. II.D. C.Ex. dated 26th February, 1944].
- c) The Chapter V of the Finance Act, 1994 [with effect from 1.7.1994].

12. Proposals for levy of duty of Customs/ Central Excise on new articles or changes in the rate of duty; or for bringing news services in tax net etc. are made by making proposals in the Finance Bill presented by the Finance Minister in the Parliament on the last working day of February when the "Budget" is presented.

13. The Budget derived from the French word "Baguette" (meaning a leather bag which bulges), is the annual financial statement laid before both Houses of the Parliament in accordance with the provisions of Article 112 of the Constitution. The statement is prepared under the major heads of account prescribed in consultation with the Comptroller and Auditor General of India and the heads fall either under the **consolidated fund of India (Article 266 of the Constitution)** or in the public account of the Government. In addition, the Government of India also maintains a **contingency fund set up under Article 267(1) of the Constitution**.

Legislative Journey of Tax on Services in India

14. In 1990, Tax Reforms committee headed by Dr. Raja J. Chelliah first time recommended levy of tax on selected services. Acting on the recommendation of Dr. Chelliah Committee, in 1994, in the budget speech, Dr. Man Mohan Singh, as a Finance Minister said that:

“Over the years, while attempts have been made to widen the base for domestic indirect taxes, the services sector has not been subjected to taxation. Yet this sector accounts for about 40% of our GDP and is showing strong growth. There is no sound reason for exempting services from taxation, when goods are taxed and many countries treat goods and services alike for tax purposes.

The Tax Reforms Committee has also recommended imposition of tax on services as a measure for broadening the base of indirect taxes. I, therefore, propose to make a modest effort in this direction by imposing a tax on services of telephones, non-life insurance and stock brokers.”

15. First time, service tax was imposed on three services i.e. Telephone services, insurance (other than life insurance) and stock brokers at the rate of 5% with effect from 1.7.1994. Later on, more and more services were brought into service tax net. The parliament imposed tax on services by exercising its power to legislate under Entry No. 97 of the Union list under Seventh Schedule, which is a residual entry. At times, the competency of Parliament to legislate on levy and collection of service tax under the Entry No. 97 was also questioned in the court of law.

16. In the year 2003, the Parliament decided to amend the Constitution of India to incorporate specific provisions in the Constitution in respect of legislative power to deal with tax on service. While presenting the Constitution 88th Amendment Bill, 2003, in the statement of objects and reasons, it was mentioned as under:-

“ At present, the item relating to "taxes on services" is not specifically mentioned in any entry either in the Union List or in the State List of the Seventh Schedule of the Constitution. Parliament has the exclusive power to make laws with respect to entry 97 of the Union List for any other matters not enumerated in List II or List III including any tax not mentioned in either of those Lists. In exercise of this power, the Central Government has periodically taxes certain services at the rate of five per cent. ad valorem.”

2. The States have taken a unanimous decision to replace their existing sales tax system with the system of Value Added Tax (VAT) from the 1st April, 2003. In this context, with a view to widening their tax base, the States have suggested that they should be enabled to collect and appropriate tax on services.

3. The "service" sector accounted for 48.5% of the country's Gross Domestic Product (GDP) in the financial year 2000-2001. The role of this sector in the economy is quite significant. Expert Committees set up by the Central Government have repeatedly recommended taxation of services. On the basis of the deliberations between the State Governments and the Central Government and in view of the recommendations of various Expert Committees, it is proposed to suitably amend the Constitution to provide, (i) tax on services as a specific entry in the Union List, (ii) insertion of a new article, namely, article 268A and (iii) consequential amendment to article 270, to enable Parliament to formulate by law principles for determining the modalities of levying the said tax by the Central Government and collection of the proceeds thereof by the Central Government and the States.

4. The proposed amendment would help in significant augmentation of revenues of the States in accordance with the proposed law, and pave the way for eventual inclusion of services within the purview of State level VAT.

5. The Bill seeks to achieve the above objects.”

17. The 88th Constitutional Amendment Act, 2003 (with effect from 15.1.2004) made following changes in the Constitution of India

- (i) Inserted new entry 92C: Tax on services in the List I to the Schedule 7 of the Constitution of India

(ii) It inserted new Article 268A, which reads as under:-

"268A. Service tax levied by Union and collected and appropriated by the Union and the States.-

(1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2).

(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be-

(a) collected by the Government of India and the States;

(b) appropriated by the Government of India and the States,

in accordance with such principles of collection and appropriation as may be formulated by Parliament by law.

18. With the passage of the 88th Constitutional Amendment Act, the issue of constitutional validity of the provision of the Finance Act, 1994 (Chapter V) relating to levy and collection of service tax, has been settled.

19. This process of imposition of service tax on selective basis continued till 30.6.2012. With effect from 1.7.2012, the concept of negative services was introduced and all services other than negative services were brought into the ambit of Service tax. Further, with effect from 1.7.2012, the term "service" was defined and service specific definition of taxable service, value of taxable services were dispensed with.

20. The legislative journey of service tax in India can be divided in four distinct phases:-

(a) **First Stage [from 1.7.1994 to 15.1.2004]** : Service tax was imposed first time in 1994 vide Finance Act, 1994. The Government of India followed selective approach and imposed service tax on three services to begin with. Later, more and more services were added every year in the list of taxable services. This selective approach continued till 30.6.2012, by which 119 specific services were brought

into the net of tax on services. In the year 2012, concept of negative services was introduced and all services except negative services were brought into service tax net.

Since 1994, the Central Government imposed service tax exercising power under Entry No. 97 (Residual entry) under Union List specified in Seventh Schedule. The Constitutional validity of levy of service tax by Central Government has been challenged on various grounds **such as:**

- (i) Non-competency of the Parliament to Levy tax on the activity within the domain of the state power;
- (ii) Discriminatory in nature, Violation of Article 14 of the constitution; etc.

(b) **Second phase [15.1.2004 till 31.6.2012]:** In the year 2003, the Parliament passed the 88th Constitution amendment Act, 2003 by inserting specific Entry 92C in the List I included in the Seventh Schedule. The entry 92c empowered the Parliament to legislate on subject of “tax on services”. Further, Article 268 A was also inserted enabling parliament to levy tax on services and also provided for collection of such taxes by States and Centre. It also settled the question of constitutional validity of legislative provisions dealing with levy and collection of tax on services.

(c) **Third Phase (from 1.7.2012 to till date):** This phase started with introduction of concept of negative services and comprehensive coverage of services under Service Tax net. Further, the service specific definition of taxable service and value of taxable services has been done away with. New concepts such as defining the term “service”, place of provision of services, declared services, bundled services etc. This phase will continue till introduction of GST (Goods and services Tax) merging Central Excise and Service tax with state VAT and other state taxes.

(d) **Fourth Phase:** This phase will commence with introduction of GST in India.
