

ANALYSIS OF FREEDOM OF TRADE AND COMMERCE IN INDIA UNDER THE INDIAN CONSTITUTION

Written by *Aneri Shah*

Independent Researcher

INTRODUCTION

Part XIII of the Indian Constitution, discusses in detail about trade, commerce and intercourse within the territory of India. Trade, commerce and intercourse may be domestic or foreign or international. Articles 301 to 305 discuss the freedom of trade and commerce throughout the territory of India. There are two major types of trade and commerce governed in India:

1. Inter-state: trade and commerce confined within the country, i.e. it extends to two or more states as well; and
2. Intra-state: trade and commerce confined within the territory of the specific state.

Creation of trade barriers affect economic growth of the country and the same is against the national interest of the country. The free flow of trade, commerce and intercourse within a federal country has a two-tier polity which is helpful in the economic growth, stability and development of the country. Every country has its own laws pertaining to trade and commerce in the country. In India, this freedom is not absolute, but is subject to restrictions which are necessary and required to maintain the public interest of the people within the territory of India. Hence, the legitimate regulatory measures restricting the trade and commerce are not considered as restrictions to 'free trade and commerce'.¹ Thus, the courts have interpreted the term businesses and other activities such as gambling, illegal trade, etc. as not being a part of this Article.

“An attempt in all federations, through adopting of suitable constitutional formulae, to create and preserve a national economic fabric, transcending State boundaries, to minimise the

¹ Chapter XVIII, Trade, Commerce and Intercourse within the Territory of India, available at <<http://interstatecouncil.nic.in/wp-content/uploads/2015/06/CHAPTERXVIII.pdf>>

possibility of emergence of local economic barriers, to remove impediments in the way of inter-State trade and commerce and thus help in welding the whole country into single economic unit so that the economic resources of all the regions may be exploited, harnessed and pooled to the common advantage and prosperity of the country.”²

The present article discusses the status of trade, commerce and intercourse in India, and the approach of the court through various judicial pronouncements on the issue pertaining to compensatory tax, regulatory tax and entry tax.

ARTICLE 301 AND AUSTRALIAN CONSTITUTION

The Commonwealth of Australian Constitution Act, 1900 (“**Australian Act**”) was enacted during the British Parliament and it specified separate and only specific powers to the Centre and elaborated in detail the scheme of separation of powers. Section 51³ of the Australian Act entitles 40 matters on which the Central Government has the power to legislate. However, this section does not make the power exclusive on the Centre and the states also have an authorized power to legislate in the area.

The Centre has powers in the ‘inter-state commerce’ to regulate the economic affairs of the country, as gradually trade and commerce are becoming subjects of national importance as they are major source in contributing to the economy of the country and thereby less confining within the limits of only one state. There are several points of comparison and contrast between the Australian and Indian schemes of distribution of powers. Both in Australia and India, there are certain powers that have been given exclusively to the Centre through the List I of the Indian Constitution, and these powers are more exhaustive as compared to list under the Australian Act.⁴

The crucial position for the purpose of the Australian Act is Section 92 according to which the trade, commerce and intercourse among the States shall be absolutely free. The major difference between Indian Constitution and Australian Constitution is that the clause here

² M.P. Jain, *Indian Constitutional Law* (7th edn, LexisNexis 2016) 759

³ Legislative Powers of the Parliament

⁴ M.P. Jain, *Indian Constitutional Law* (7th edn, LexisNexis 2016) 595

applies only to inter-state and not intra-state commerce, and restricts both the States and the Centre from interfering with trade and commerce.⁵

Section 92 of the Australian Act can be read as: ‘*On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free. But notwithstanding anything in this Constitution, goods imported before the imposition of uniform duties of customs into any State, or into any Colony which, whilst the goods remain therein, becomes a State, shall, on thence passing into another State within two years after the imposition of such duties, be liable to any duty chargeable on the importation of such goods into the Commonwealth, less any duty paid in respect of the goods on their importation.*’

Section 92 guarantees both legislative as well as executive freedom and prohibits discrimination as well as fiscal burdens. In the case of *James v Commonwealth*⁶, Lord Wright stated that only ‘Section 92 declares right of trade or business.’ The Privy Council held that, “*the Commonwealth should be held to have failed in its attempt by the method adopted under the Act in question to control prices and establish a marketing system even though the commonwealth government is satisfied such a policy is in the best interests of the Australian people.*”

Thus, any attempt to interfere with the freedom of trade and commerce will act in violation to Section 92 of the Australian Act. This freedom is unlimited and unqualified but is not absolute. The court lays down criteria’s when the freedom will be restricted. The Privy Council held that: *the laws relating to trade and commerce amongst the states was compatible with the absolute freedom as mentioned and further mentioned that Section 92 gets violated only when the legislative or executive acts in a manner which is direct and immediate violation of trade, commerce or inter-course and not in circumstances when there is indirect or inconsequential impediment which may fairly be regarded as remote.*⁷

Thus, this Section of Australian Act may find some of its presence in the enactment and establishment of the Part XIII of the Indian Constitution.

⁵ *Jindal Stainless Ltd. v State of Haryana* [2006] AIR SC 2550

⁶ [1936] AC 631

⁷ *Clark King v Australian Wheat Board* [1978] 21 ALR 1

INTER-RELATION BETWEEN ARTICLE 301 AND ARTICLE 19(1)(G) OF THE INDIAN CONSTITUTION

Article 19(1)(g) can be read as:

“All citizens shall have the right to:

(a)

.....

(g) to practise any profession, or to carry on any occupation, trade or business”

Article 301 can be read as:

“Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.”

Thus, the differences between the two articles are as follows:

Article 19(1)(g)	Article 301
<ul style="list-style-type: none"> Acts as a Fundamental Right and confers to the right of an individual. 	<ul style="list-style-type: none"> Safeguards the rights to carry on trade as a whole, and is distinguished from an individual’s right to trade.
<ul style="list-style-type: none"> Confers rights on individuals to practise any profession and carry on any occupation, trade or business, and subject to reasonable restrictions in public interest. 	<ul style="list-style-type: none"> This article aims at preventing restrictions on the amount of trade flowing within the states and territory of India, and hence the effect of law on individuals is irrelevant.
<ul style="list-style-type: none"> Deals with the right at rests. 	<ul style="list-style-type: none"> Deals with the right to trade in motion.
<ul style="list-style-type: none"> Can be invoked when an individual’s right to freedom to carry on any profession or business is being 	<ul style="list-style-type: none"> Can be invoked when an individual is restricted or prevented from sending his/her goods from one place to another,

hampered, irrespective of the movement of goods in existent or not.	within the same state or in relation to inter-state trade.
<ul style="list-style-type: none"> The advantage of this right being a Fundamental Right can be taken by merely citizens. This right is not available to a corporate person. 	<ul style="list-style-type: none"> This right being a general right, can be invoked by both citizens as well as non-citizens. This right can also be invoked by corporations.

ANALYSIS OF PART XIII OF THE INDIAN CONSTITUTION

The framers of the Indian Constitution were fully conscious about the need of freedom of trade and commerce within the territory of India, and were absolutely aware that the same was necessary for promoting economic growth, stability and progress of the federal policies in India. The framers were aware of the fact that during the course of years, different political parties with different mind-set and ideologies will form a party at the Centre and accordingly this may generate general and local pulls and pressures in the economic matters. The legislature of the States may take up measures to control regional trade and regional interest above national, thereby affecting the national economy. Hence the main object of Part XIII of the Indian Constitution with special reference to Article 301 was to remove any such possibility and ensure free movement of trade, commerce and inter-course throughout the territory of India.⁸

Article 301: “*Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.*”

The words ‘*trade*’, and ‘*commerce*’ have been broadly interpreted by the courts in different case laws in a different manner, keeping in mind the facts and circumstances of each case. The freedom granted under this Part XIII of the Indian Constitution is not an absolute freedom and is subject to reasonable restrictions as mentioned under Article 302 to 307 of the Indian Constitution. The freedom provided under this Article 301 as interpreted by courts in various

⁸ M.P. Jain, *Indian Constitutional Law* (7th edn, LexisNexis 2016) 765

case laws, does not include gambling, trafficking of child and women, prostitution or any other illegal acts, either falling against the ambit of the laws of India and in violation to Indian laws.

The freedom of trade and commerce cannot be infringed in any manner for the situations as provided within the regulatory and statutory measures. The restrictions as imposed may take form either in fiscal or non-fiscal measures. Thus, there exists violation of this freedom only in cases where the legislature or executive acts or operates in a manner restricting trade, commerce and intercourse either directly or immediately.⁹

In the landmark case of *Atiabari Tea Co.*¹⁰, the court emphasized on the fact that: “*whatever else the Article 301 may or may not include, it certainly includes movement of trade which is of the very essence of all trade and is its integral part.*” The court further held that, “*Art. 301 provides that trade shall be free throughout the territory of India, it means that the flow of trade shall run smoothly and shall be unhampered by any restriction either at the boundaries of the States or at any other points inside the States themselves. It is the free movement or the transport of goods from one part of the country to other that is intended to be saved, and if any Act imposes any direct restrictions on the very movement of such goods it attracts the provisions of Art. 301, and its validity can be sustained only if it satisfies the requirements of the Article.*”

Thus, it is a well settled principle that the concept of ‘trade, commerce and intercourse’ is wide and that the word alone in its narrow sense would include all the activities in relation to buying and selling or interchange or exchange of those commodities. In the case of *State of Bombay v RMDC*, the hon’ble Supreme Court held that: “the protection afforded by Article 301 is confined to activities as may be regarded as lawful trading activities and does not extend to activity which is *res extra commercium* and cannot be considered as trade”.¹¹

The Supreme Court in *B.R. Enterprises v State of Uttar Pradesh*¹², gave an assertion on the fact that lotteries act as merely a chance of luck and winning and is not a skill and thus fall within the ambit of gambling. Thus, sale of lottery tickets cannot be claimed under Article 301 as free trade commerce or inter-course. The court was of the view that: “... we have no hesitation to hold that sale of lottery tickets organized by the State could not construed as trade

⁹ Shodhganga, available at <http://shodhganga.inflibnet.ac.in/bitstream/10603/129409/10/10_chapter%203.pdf>

¹⁰ *Atiabari Tea Co. Ltd. v State of Assam* [1961] AIR SC 232

¹¹ [1957] SCR 874

¹² [1999] 9 SCC 700

and commerce and even if it can be, then it cannot be raised to status of 'Trade and Commerce' as used in common parlance". In *P.N. Kaushal v Union of India*¹³ an order restricting the sale of liquor for two 'dry days' after every 'wet week' was valid and that those involved in the liquor trade could not avail of the protection afforded under Article 301. This, and other rulings of the Supreme Court of a like nature, effectively meant that any restrictions imposed upon a trade like liquor would be valid even if the conditions of Article 304 (b) were not satisfied.

The issue of tax law and that Article 301 does not confer absolute freedom from taxation in matters of trade, commerce and intercourse have been decided by the courts in various cases. In one of the landmark case of *India Cement v State of Andhra Pradesh*¹⁴, the court was of the view that "there can be no dispute that taxation is a deterrent against free flow. As a result of favourable or unfavourable treatment by way of taxation, the course of flow of trade gets regulated either adversely or favourably. If the scheme which Part XIII guarantees has to be preserved in national interest, it is necessary that the provisions in the Article must be strictly complied with". The tax laws are not excluded from the scope of Article 301. The tax which affects the trade, commerce and intercourse either directly or immediately will fall within the purview of Article 301.

Regulatory measures as required for maintaining the law and order in the society, for following the established law of the land i.e. laws relating to filing of return, traffic regulations, etc., are not affected by Article 301. It is for the court to decide whether the provision is regulating the freedom of trade and commerce or restricting the freedom so provided under Article 301. The term 'regulation' does not have a defined and specific meaning or definition and it is for the courts to decide its meaning and interpretation on the basis of different facts and circumstances of each case placed before the court. In some cases, its meaning may be interconnected to prohibition whereas in some it is regulatory measures.¹⁵ The court in *Jindal Stainless Ltd. v State of Haryana*¹⁶, highlighted the distinction between regulating the freedom granted and interfering with the freedom. The former can be interpreted as the rules of proper conduct or other restraints directed to the due and orderly manner to carry out trade activities, whereas the latter would mean interfering with the freedom to carry out activities constraining the trade.

¹³ [1978] 3 SCC 558

¹⁴ [1988] 1 SCC 743

¹⁵ B. Shiva Rao, *The Framing of India's Constitution (Select Documents)* (3rd edn, Universal Law Publishing 2004)

¹⁶ [2006] 7 SCC 241

In accordance to the principles of Indian Constitution, no freedom is absolute and henceforth, this freedom of free trade, commerce and inter-course within the territory of India is also subject to reasonable restrictions as mentioned under the Articles 302- 307 in the Part XIII of the Indian Constitution.

Article 302: *“Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part of the territory of India as may be required in the public interest”.*

This Article empowers the parliament to establish reasonable restrictions on the freedom of trade, commerce and intercourse between one state and another within the boundaries of India, if the same necessary and required for public interest. Thus, Article 302 relaxes restrictions imposed by Article 301 in favour of the Parliament. The *prima facie* question of public interest underlying the Parliamentary law imposing restrictions on trade and commerce may not be justiciable, and hence, a person challenging the law will have to prove as to why the act is not required in the interest of the public at large.¹⁷

In the *State of Madras v Nataraja Mudalia*¹⁸, the question before the hon’ble Supreme Court was whether the higher amount of tax as paid by an unregistered dealer engaged in inter-state trade under section 8(2)(b) of the Central Sales Tax Act was in violation to Article 301 of the Indian Constitution. The court held that even where a restriction imposes a direct burden on the freedom of trade and commerce under Article 301, it would be constitutionally valid if it were deemed to be in public interest. The court here accepted the argument of the government that the same was applied to prevent tax evasion and for exercising supervision. The same principle was reiterated in *State of Tamil Nadu v Sitalakshmi Mills*¹⁹. Thus Article 302 as used as both a sword and a shield to put forward the presumption that there is always a strong chance that any Parliamentary law on taxes would be in public interest.

Article 303: *“(1) Notwithstanding anything in Article 302, neither Parliament nor the Legislature of a State shall have power to make any law giving, or authorising the giving of, any preference to one State over another, or making, or authorising the making of, any*

¹⁷ David P. Derham, ‘Some Constitutional Problems Arising under Part XIII of the Indian Constitution’ (1959) 1 Journal of Indian Institute of Law 523

¹⁸ [1969] AIR SC 147

¹⁹ [1974] AIR SC 1505

discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

(2) Nothing in clause (1) shall prevent Parliament from making any law giving, or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India.”

Article 303(1) acts as an exception to Article 302 if the Indian Constitution. Through this Article, the right of the Parliament to make laws to impose restrictions on freedom of trade and commerce is restricted, as the neither the Parliament nor the legislation of the state is allowed to make any such law which differentiates, discriminates or gives preference to any one state over another. However, Article 303(2) acts as an exception to Article 303(1). It permits the Parliament to make any law which may, if in discrimination or giving preference to another state is a valid law, if the same is required to be enacted as a result of any such circumstance or situation which has arisen from the scarcity of goods in that particular part of the territory of India. However, the same is permitted only for the Parliament to make law and not for the State Legislature.

Hence, when the Parliament is faced with a task of meeting an emergency situation that has been created as a result of scarcity of goods, in any particular part of India, it can make an enactment which though may be discriminatory or giving preference to any particular state, such declaration and act of the Parliament would be considered as conclusive and justiciable.

The *State of Madras v Nataraja Mudaliar*²⁰, several views were supported for deciding that the purpose of impeding tax collected and retained by the state does not amount to a law giving preference to one state over another or making any discrimination between the states. The views supporting these are²¹:

1. The flow of trade does not depend upon the rates of sales tax and there are other various factors as well necessary and relevant; and
2. The legislature has contemplated that the elasticity in the rates is in consistency with the economic forces.

²⁰ [1969] AIR SC 147

²¹ M.P. Jain, *Indian Constitutional Law* (7th edn, LexisNexis 2016) 782

Article 304: “*Notwithstanding anything in article 301 or article 303, the Legislature of a State may by law: (a) impose on goods imported from other States or the Union territories any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and (b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest: Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President.*”

Article 304 thus is a clause allowing imposing restrictions on trade, commerce and intercourse among the states. This article allows the State Legislature to impose any tax on the goods imported from the other states, to which similar goods have been manufactured and produced in India. Such act/legislature passed by the State is valid and permitted. However, clause (b) of the article allows such reasonable restrictions to be imposed by the state legislature on the ground of public interest only in circumstances where the bill/amendment shall be introduced or allowed only with the prior sanction of the President.

This provision is however limited to only one subject matter, i.e. the tax imposed on imported goods in the state from outside the state. This clause permits the levy on goods from sister States any tax which similar goods manufactured or produced in that State are subject to. In other words, goods imported from sister states are placed on par with similar goods manufactured or produced within the state in regard to state taxation within the state allotted field. A state cannot discriminate beyond its capacity between its own goods and imported goods. This is the demand of the concept of economic unity in India.²²

Article 304(a) thus ensures that state shall not discriminate and impose more tax than required on the imported goods as compared to that imposed on the similar state manufactured and produced goods. Thus the article places both the imported goods and state local goods at par with each other.

For the application under Article 304(b) the following applications and conditions need to be fulfilled:

²² Dr. Subhash C. Kashyap, *Constitutional Law of India* (2nd edn, Universal Law Publishing 2015)

- a. The Bill has to be introduced or moved in the State Legislature with the prior sanction of the President, or that the Bill has been assented to by the President.
- b. The tax in question constitutes reasonable restrictions.
- c. The tax has been levied in the public interest.

This mechanism thereby draws a balance between national and regional economic interests and it makes the legislature the arbitrator of what the restrictions may be allowed to be imposed.

The State government suggested that the proviso to Article 304(b) be omitted as it imposes unreasonable fetters and unjustifiable restrictions on the legislative autonomy of the state. The Article mentions that the restrictions imposed should be reasonable in nature, and if the same does not satisfy the criteria's, these restrictions are subject to the decision of the court and thus could be set aside and be considered unconstitutional. Thus, there arises a broader question as to whether the inclusion of trade, commerce and intercourse within a State in Article 302 and the requirement of previous sanction of the President in the proviso to Article 302(b) is against the basic principle of federalism and amounts to 'unjust restrictions on the legislative autonomy of the state'.²³

The Sarkaria Commission when was established, it was argued that the proviso to Article 304(b) imposing control of the Centre over the State laws may be deleted, however the same was rejected by the committee. It stated the following remarks: "*State laws though purporting to regulate intra-State trade, may have implications for Inter-State trade and commerce. These may impose discriminatory taxes or unreasonable restrictions, impeding the freedom of inter-State trade and commerce. If clause (b) of Article 304 is deleted, the commercial and economic unity of the country may be broken up by State laws setting up barriers to free flow of trade and inter-course through parochial or discriminatory use of their powers.*"

It presumably draws inspiration from the antiquated and obsolete theory of federalism, according to which two levels of government were supposed to function in water-tight compartments in isolation from each other. The scheme of the Articles in Part XIII considered as a whole, however is well-balanced. It reconciles the imperative of economic unity of the

²³ Report of Sarkaria Commission, Chapter XVIII, Trade, Commerce and Intercourse within the Territory of India, Available at <<http://interstatecouncil.nic.in/wp-content/uploads/2015/06/CHAPTERXVIII.pdf>>

Nation with interests of State autonomy by carving out in clauses (a) and (b) of Article 304, two exceptions in favour of State legislatures to the freedom guaranteed under Article 301.²⁴

Article 305: “Nothing in articles 301 and 303 shall affect the provisions of any existing law except in so far as the President may by order otherwise direct; and nothing in article 301 shall affect the operation of any law made before the commencement of the Constitution (Fourth Amendment) Act, 1955, in so far as it relates to, or prevent Parliament or the Legislature of a State from making any law relating to, any such matter as is referred to in sub-clause (ii) of clause (6) of Article 19.”

Thus, this article protects the laws that were enacted before the commencement of the Indian Constitution, except so far in cases where the President may have given any other directions. The Article 305 protects the law and not any executive action which is unsupported by law. A monopoly in favour of the State or the Centre cannot be created by a mere administrative order. Moreover, Article 305 does not in any manner protect monopoly so created which is neither owned nor controlled by state created corporation.²⁵

Article 307: “Parliament may by law appoint such authority as it considers appropriate for carrying out the purposes of articles 301, 302, 303 and 304, and confer on the authority so appointed such powers and such duties as it thinks necessary.”

The problems arising out of trade, commerce and inter-course often keeps on increasing with the changes in the economic and fiscal federations and governance in India. In such circumstances, a body or a legal entity consisting of experts and people having special knowledge and training in the field of law, economics etc. could help bring sustainable solutions. This idea was incorporated in the Indian Constitution through the language as mentioned under the Article 307.

Under the Sarkaria Commission report, the commission argued in favour of establishing such a body and stated that: “The whole field of freedom of trade, commerce and intercourse bristles with complex questions not only in regard to constitutional aspects but also in respect of working arrangements on account of impact of the legislation of the Union on the powers of the States and the effect of legislation of both the Union and States on free conduct of trade,

²⁴ Report of Sarkaria Commission, Chapter XVIII, Trade, Commerce and Intercourse within the Territory of India, Available at <<http://interstatecouncil.nic.in/wp-content/uploads/2015/06/CHAPTERXVIII.pdf>>

²⁵ *Dist. Collector, Hyderabad v Ibrahim* [1970] AIR SC 1275

*commerce and intercourse. Trade, Commerce and intercourse cover a multitude of activities. Actions of the Union and State Governments have wide-ranging impact on them. Legislative and executive actions in the field of licencing, tariffs, taxation, marketing regulations, price controls, procurement of essential goods, channelisation of trade, and controls over supply and distribution, all have a direct and immediate bearing on trade and commerce. Innumerable laws and executive orders occupy the field today. This has led to an immensely complex structure. Many issues of conflict of interests arise everyday”.*²⁶

Such a body being free would be able to perform its administrative functions in an effective and an efficient manner. The body would be able to tackle the various problems pertaining to trade, commerce and intercourse. It would also help inspire confidence among various states and other interests. The ambit of this article is wide enough to include all the laws and provisions relating to inter-state trade, commerce and intercourse.

The freedom as mentioned under Part XIII of the Indian Constitution is not an absolute freedom and is governed by the several entries as mentioned under the three lists of Schedule 7, where both the Parliament and the State Legislature has been given the power to legislate in the matters relating to trade, commerce and intercourse. Within the purview of Indian Constitution, Entry 42 in List I deals with Inter-state trade and commerce; Entry 26 in List II deals with trade and commerce subject to provisions of Entry 33 in List III; and Entry 33 in List III deals with specified matters pertaining to trade, commerce and intercourse. In case of conflict between the two, the doctrine of pith and substance can be invoked in order to determine the true nature and character of the legislation in question.

The power and authority on the states and centre to impose taxes comes through these Articles and Entries as mentioned under the various lists. The courts have interpreted the taxes imposed on the goods being transported (either inter-state or intra-state through trade and commerce) depending upon the facts and circumstances of each case. The arguments provided by the state include that these types of taxes act as compensatory and regulatory in nature by saying that the imposition of tax is for facilitating the trade and commerce and for providing facilities like maintenance of roads, traffic lights, etc. The main argument on behalf of the State is that,

²⁶ Report of Sarkaria Commission, Chapter XVIII, Trade, Commerce and Intercourse within the Territory of India, Available at <<http://interstatecouncil.nic.in/wp-content/uploads/2015/06/CHAPTERXVIII.pdf>>

compensatory and regulatory measures facilitate rather than hampering free flow of trade and commerce.²⁷

It is the tax thus realized that makes it feasible for opening new means of communication or for improving old ones. It cannot therefore, be said that taxation in every case must mean an impediment or restraint against free flow of trade and commerce.²⁸ A tax does not cease to be compensatory because the precise or specific amount collected is not actually used in providing facilities.

CASE ANALYSIS

In *Atiabari Tea Co. Ltd. v State of Assam*²⁹, the question before the court was whether the Assam Taxation (on goods carried by Road or Inland Waterways) Act, 1950 is constitutionally valid piece of legislation or not. In the present case, the appellants grew tea in West Bengal and Assam, and their tea was carried in the markets of Calcutta from where the tea was exported within and outside the territory of India. The Assam Legislature passed an Act after the assent of Governor of Assam was received. The main objective and purpose of the legislature was to levy taxes on the goods carried by road or inland waterways in Assam. The appellant before the court challenged the constitutional validity of the said Act. The five judge bench in this case, struck down the enactment holding it ultra-virus to the genesis and Part XIII of Indian Constitution. The court held that: *“The taxes and levies can and do amount to restriction on freedom of trade and the working test for determining this was that whether the tax or levy in question directly and immediately amounts to restriction on free flow of trade.”*

In *Automobile Transport (Rajasthan) Ltd. v State of Rajasthan Ors.*³⁰, the Rajasthan Motor Vehicles Taxation Act, 1951 was challenged on similar grounds as that of *Atiabari Tea Co.* case. In this case, the government of Rajasthan levied a tax on the motor vehicles (a tax of the amount of Rs. 60 on motor car and that of Rs. 2000 of the vehicle carrying goods per year) used within the State in any public place or kept for use in the State. The validity of the said

²⁷ Juhi Bansal, ‘Entry Tax: Is it Constitutional?’, available at <<http://www.servicetaxindia.co.in/forms/entrytax.pdf>>

²⁸ Report of The Commission on Centre-State Relations, *Evolution of the Centre-State Relations in India*, Vol. 1, (March 2010) available at <<http://interstatecouncil.nic.in/volume1.pdf>>

²⁹ [1961] AIR SC 232

³⁰ [1962] AIR 1406

act was challenged. The seven judge bench upheld the validity of the tax and held that the freedom as provided under Article 301 should not be interfering in an unduly manner with the power and autonomy given to the state, and should be in consistency with the laws of India. The Supreme Court in the present case held the tax to be not in violation to Article 301, and the same is compensatory in nature, thus does not amount to restriction or impediment on freedom of trade, commerce and intercourse and thereby facilitating the same. The collection of toll or tax for the development or repairing the road etc., does not create hindrance to anybody's freedom so long as they remain reasonable and does not hamper anybody's freedom of trade or commerce. If any law has repercussions on tariffs, licensing, price control etc. such law should if passed be subject to President's approval, and should not under any circumstances be in violation to Part XIII of the Indian Constitution. "A working test for deciding whether a tax is a compensatory or not is to enquire whether the trade is having the use of certain facilities for the better conduct of its business and paying not patently much more than what is required for providing the facilities". Thus, the freedom granted under Article 301 does not mean absolute freedom, free from taxation as taxation is not restriction within the meaning of the meaning of relevant articles in Part XIII.

In *State of M.P. v Bhailal Bhai*³¹, a tax was imposed under the Madhya Bharat Sales Tax Act, 1950 as a result of which, tax was imposed on tobacco leaves, manufactured tobacco and the tobacco used for manufacturing bidi. The petitioners contended the tax to be unconstitutional as the same was violating Article 301. Justice Das Gupta, in the present case held the imposition of tax to be in violation to the Articles of Part XIII of the Indian Constitution, as the same was directly impeding freedom of trade and commerce. This case was not considered as an exception under the Article 304(a) as the similar goods manufactured under the state were not subject to the same tax ratio, as the traded goods. Thus, the case was in favour of the petitioners.

In *Bhagatram Rajiv Kumar v Commissioner of Sales Tax, Madhya Pradesh*³², the decision of the Madhya Pradesh High Court was challenged before the Supreme Court. The question before the court involved the validity of entry tax under section 3(1)(a) of Madhya Pradesh Sthaniya Kshetra Me Mal Ke Pravesh Par Kar Adhiniyaro, 1976. The question was whether the entry tax on goods such as sugar on which no sales tax is leviable, is subject to section

³¹ [1964] AIR SC 1006

³² [1995] 96 STC 645

3(1)(a). The court was of the view that tax on sugar would be payable and would not be beyond the taxing income, and the court thereby dismissed the appeal.

In *State of Bihar v. Bihar Chamber of Commerce*³³, entry tax was imposed on goods in the local area for the consumption, sale or use and the rate was not exceeding 5% as may be specified by the government. The state had the legislative competency on the basis of Entry 52 of the List II of the 7th Schedule. The issue raised before the Supreme Court was whether the tax was in violation to Article 301, as it imposed tax on entry of goods into local area, hence whether the same would fall under the category of compensatory tax or not. The court held the same to be compensatory in nature. The state in this case produced no specific material to ascertain that the levy was of compensatory and regulatory in nature. However, the court held that ‘*the situation as being of “no consequence” for the reason that the Court can take “notice” of the fact that the State does make available several facilities to the trade including maintenance of roads, water-ways and markets, etc.*’

Post decisional hearings from 1995 state that even if the imposition of tax is not of compensatory nature, or does not confer any special advantage to the traders but is in the general interest of the public, such levy of tax can also be considered compensatory in nature. Accordingly, any indirect or incidental benefit to the traders as a result of stepping up the developmental activities in the various local areas of the State can be brought within the concept of compensatory tax, and the nexus between the tax known as compensatory tax and the trading facilities not being necessarily either direct or specific.³⁴

In *Jindal Stainless Ltd. & Anr. v State of Haryana*³⁵, the Haryana Local Area Development Tax Act, 2000 was established to transport raw materials required by Haryana industries. The act was challenged on the grounds of violation of Article 301 of the Indian Constitution. A division bench questioned the decisions of *Bhagatram*³⁶ and *Bihar Chamber*³⁷ case. The petitioners argued that if the court accepted the decision of *Bhagatram* case, then as a result of the test, the distinction between compensatory tax and tax for general revenue would be eliminated. The two arguments on behalf of the respondents was that a compensatory tax does not have to be

³³ [1996] AIR SC 2344

³⁴ *Jindal Stainless Ltd. & Anr. v State of Haryana* [2006] AIR SC 2550

³⁵ [2006] AIR SC 2550

³⁶ *Bhagatram Rajeev Kumar v Commissioner of Sales Tax* [1995] 96 STC 645

³⁷ *State of Bihar v Bihar Chamber of Commerce* [1996] AIR SC 2344

in proportion to benefit, because that would make it impossible to differentiate from a fee, and their second argument was that in any event, the factor on which a tax is considered as compensatory cannot be the nature of the levy, but the nature of the legislative entry under which the relevant law is passed. The Entries 56, 57 and 59 of List II indicate the link with roadways, waterways and are in direct connection with fees and tax and thus are compensatory in nature. The case has in detail analysed the difference between 'tax' and 'fees'. Thus, the divisional bench held the applicability of the tax to be compensatory and regulatory in nature and the tax was used to improve the trade facilities, building infrastructure etc., and was thus outside the ambit of Article 301 of the Indian Constitution. Hence, the case overruled decisions held in landmark judgments of *Bhagatram* and *Bihar Chambers of Commerce* case.

In *Jindal Stainless Ltd. & Anr. v State of Haryana*³⁸, the question before the division bench on the State entry tax stood as a challenge. The issues involved whether the Clause (a) and (b) of Article 304 act independently to one another, and whether the impugned law if stood saved under Article 304(a), then it need not fulfil the test mentioned under Article 304(b). Accordingly the matter was been referred to a Constitutional Bench before the Hon'ble Supreme Court of India.

In the landmark judgment of the historic ruling in India in the *Jindal* case³⁹, a coram of 9 judges, upheld the validity of 'entry tax' imposed by the governments on the movement of goods entering their respective states. The questions to be considered before the court included:

1. Whether there occurred transgression of Article 301 of the Indian Constitution as a result of levy of non-discriminatory taxes?
2. If the answer to the above question stands affirmative, whether the tax would fall foul of Article 301 of the Indian Constitution?
3. What are the relevant steps to determine the compensatory nature of the taxes levied?
4. To determine the constitutional validity of the test relating to entry tax under Articles 304(a) and 304(b), and whether the entry tax levied is in violation to Article 301 of the Indian Constitution?

The decision held by a ratio of 7:2 stated the following terms⁴⁰:

³⁸ [2010] 4 SCC 595

³⁹ *Jindal Stainless Ltd. & Anr. v State of Haryana* [2017] 12 SCC 1

⁴⁰ *Jindal Stainless Ltd. & Anr. v State of Haryana* [2017] 12 SCC 1

1. Taxes simpliciter are not within the contemplation of Part XIII of the Constitution of India. The word 'Free' used in Article 301 does not mean "free from taxation".
2. Only such taxes as are discriminatory in nature are prohibited by Article 304(a). It follows that levy of a non-discriminatory tax would not constitute an infraction of Article 301.
3. Clauses (a) and (b) of Article 304 have to be read disjunctively.
4. A levy that violates 304(a) cannot be saved even if the procedure under Article 304(b) or the proviso thereunder is satisfied.
5. The compensatory tax theory evolved in Automobile Transport case and subsequently modified in Jindal's case has no juristic basis and is therefore rejected.
6. Decisions of this Court in Atiabari, Automobile Transport and Jindal cases and all other judgments that follow these pronouncements are to the extent of such reliance over-ruled.
7. A tax on entry of goods into a local area for use, sale or consumption therein is permissible although similar goods are not produced within the taxing state.
8. Article 304 (a) frowns upon discrimination (of a hostile nature in the protectionist sense) and not on mere differentiation. Therefore, incentives, set-offs etc. granted to a specified class of dealers for a limited period of time in a non-hostile fashion with a view to developing economically backward areas would not violate Article 304(a). The question whether the levies in the present case indeed satisfy this test is left to be determined by the regular benches hearing the matters.
9. States are well within their right to design their fiscal legislations to ensure that the tax burden on goods imported from other States and goods produced within the State fall equally. Such measures if taken would not contravene Article 304(a) of the Constitution. The question whether the levies in the present case indeed satisfy this test is left to be determined by the regular benches hearing the matters.
10. The questions whether the entire State can be notified as a local area and whether entry tax can be levied on goods entering the landmass of India from another country are left open to be determined in appropriate proceedings.

CONCLUSION

The tax powers as a result of which the Centre and States have been empowered are the Schedule 7 and the Article 265 of the Indian Constitution. The Lists I and II of the Schedule 7 show that the powers to tax under the Indian Constitution, are entrusted within the Centre and the State, and there are no powers which exist under the Concurrent List. Article 304(a) and 304(b) are distinct and disjunctive in nature. The main purpose of Article 304 and objective is to prevent discrimination against the goods imported and already being manufactured within the state. The views of the court specify that regulatory measures are actually ways which facilitate trade, though it appears to harm trade.⁴¹ Increase in globalization requires larger markets and for growth and development, every state is at a liberty to charge or levy entry tax. With the various Supreme Court judgments and case analysis, there has been certain clarity on the legality and status of entry tax within the states. Thus the freedom granted under the Article 301 is not an absolute freedom and is subject to obstructions and impediments to the free flow or movement of trade or non-commercial intercourses. The current regime of goods and service tax (GST) and the effect of trade and commerce on GST and vice versa is a situation which only time can answer.

⁴¹ V. Niranjan, 'Interstate Trade and Commerce: The Doctrine of Proportionality Reaffirmed', [2008] The Indian Journal of Constitutional Law available at <<http://www.indlaw.com/display.aspx?58B0AEB6-20B3-46BA-8CEF-21E8411C23EF>>