MP-RB-GP

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY**

**CIVIL APPELLATE JURISDICTION**

**WRIT PETITION NO. 9175 OF 2015**

**MAHYCO MONSANTO BIOTECH (INDIA) PVT. LTD.,**
(formerly known as Mahyco Monsanto Biotech (India) Ltd), a company duly registered under the Companies Act, 1956 having its registered office at 5th Floor, Ahura Centre, 96, Mahakali Caves Road, Andheri (East), Mumbai 400 093. …Petitioner

*versus*

1. **THE UNION OF INDIA**
through the Secretary, Ministry of Finance, Department of Revenue, North Block, New Delhi 110 001

2. **THE STATE OF MAHARASHTRA**
Through the Government Pleader, High Court, Mumbai

3. **THE PRINCIPAL COMMISSIONER OF SERVICE TAX,**
Mumbai IV, 4th Floor, New Central Excise Building, 115, Maharshi Karve Road, Churchgate, Mumbai 400 020.

4. **THE COMMISSIONER OF SALES TAX,**
8th Floor, Vikrikar Bhavan, Mazgaon, Mumbai 400 010 …Respondents

**ALONG WITH**

**ORDINARY ORIGINAL CIVIL JURISDICTION**

**WRIT PETITION NO. 497 OF 2015**

1. **SUBWAY SYSTEMS INDIA PVT LTD**
Having its registered office at Level 2, Elegance, Mathura Road, Jasola, New Delhi 110 025.

2. **JAGANATH RAO**,
Director, having his office at Level 2, Elegance, Mathura Road, Jasola, New Delhi 110 025.

3. **RAVINDRA PAL SINGH**,
Partner, Suresh Surana & Associates LLP, having his office at 3rd Floor, Tower-B, Sector-1, Noida, 201 301, New Delhi NCR …Petitioners

*versus*

1. **THE STATE OF MAHARASHTRA**
Through the Government Pleader, pwd Building, High Court, Mumbai

2. **UNION OF INDIA**
Aaykar Bhavan, Maharshi Karve Road, Churchgate, Mumbai 400 021.

3. **COMMISSIONER OF SERVICE TAX**,
Division-II, Range-XI, New Delhi

4. **ASSISTANT COMMISSIONER OF SALES TAX**,
MUM-INV-D-039, INV-B, having her office at Cabin No. D-8, 2nd Floor, Old Building, Vikrikar Bhavan, Mazgaon, Mumbai 400 010 …Respondents

## APPEARANCES

**IN WRIT PETITION NO. 9175 OF 2015 | MAHYCO MONSANTO BIOTECH (INDIA) PVT LTD V UNION OF INDIA & ORS.**

| | |
|---|---|
| **FOR THE PETITIONER** (*Monsanto*) | **Mr. N. Venkatraman, Senior Counsel**, *with Mr. Arun Jain, Mr. Jas Sanghvi and Ms. Shilip Jain, i/b M/s. PDS Legal.* |
| **FOR RESPONDENTS NOS. 2 AND 4** (*State of Maharashtra & Commrr of Sales Tax*) | **Mr. V. A. Sonpal**, *Special Counsel.* |
| **FOR RESPONDENTS NOS. 1 & 3** (*Union Of India &Principal Commr Of Service Tax*) | **Mr. Pradeep S. Jetly,** *with Mr. Jitendra B. Mishra.* |

**IN OS WRIT PETITION NO. 497 OF 2015 | SUBWAY SYSTEMS (INDIA) PVT LTD V STATE OF MAHARASHTRA & ORS.**

| | |
|---|---|
| **FOR THE PETITIONER** (*Subway Systems*) | **Mr. D. B. Shroff, Senior Counsel,** *with Mr. Hormazd Daruwalla, i/b M/s. Khaitan & Co.* |
| **FOR RESPONDENTS NOS. 1 AND 4** (*State of Maharashtra & Asst Commr of Sales Tax*) | **Mr. V.A. Sonpal,** *Special Counsel, with Ms. Anjali Helekar, AGP.* |
| **FOR RESPONDENTS NOS. 2 AND 3** (*Union of India & Commr of Service Tax*) | **Mr. Pradeep S. Jetly,** *with Mr. Jitendra B. Mishra.* |

**CORAM : S.C. Dharmadhikari & G.S.Patel, J.J.**

**JUDGMENT RESERVED ON : 4th March 2016**

**JUDGMENT PRONOUNCED ON : 11th August 2016**

**JUDGMENT (per G.S. Patel J):**

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## I. INTRODUCTION

**1.** These two Writ Petitions came to be tagged together presumably because they both raise issues of whether, in respect of the transactions that arise in each, the Petitioners are liable to a levy of service tax or sales tax. As it turns out, the facts are materially distinct; and as the following judgment shows, the two cases seem to us to be mirror images of each other: if one fails, on a parity of reasoning, the other must succeed.

**2.** We have heard Mr. Venkatraman for the Petitioners, Mr. Sonpal for Respondents Nos. 2 and 4, and Mr. Jetly for Respondent Nos. 1 and 3 in Writ Petition No. 9175 of 2015 ("**the Monsanto Petition**"). In Writ Petition No. 497 of 2015 ("**the Subway Petition**"), we have heard Mr. Shroff for the Petitioners, Mr. Jetly for Respondents Nos. 2 and 3 and Mr. Sonpal for Respondent Nos. 1 and 4. We have carefully considered the submissions of all the counsels and the material they have placed before us. Mr. Jetly has broadly adopted the arguments of Mr. Venkatraman and Mr. Shroff.

**3.** Mr. Venkatraman's submissions are intricately structured. We will turn to these presently. It seems to us necessary, however, to at least attempt to distill the essence of the arguments in his Petition and, therefore, in the companion Petition. In doing so, we leave aside for the present all questions of legislative competence.

**(a)** If we may be permitted a small latitude, the kernel (or 'seed', as it were) of Mr. Venkatraman's case is this: Mahyco Monsanto Biotech (India) Pvt. Ltd. ("**Monsanto India**") supplies to third parties a certain type of hybrid cotton seed. This seed is impregnated with a proprietary technology that protects it against the boll-weevil, a known menace to cotton crops. From those hybrid seeds, these third parties then generate large quantities of sowable seeds, which they then sell to cotton farmers. Monsanto India itself sells nothing to the end-user. These end-product seeds have the benefit of the boll-weevil protection technology; and the third party purchasers from Monsanto India are thus able to commercialize the technology to produce hybrid seeds for sale to cotton growers. From a small seed do mighty cotton plantations grow. Monsanto India says that what it provides when it gives the third party purchasers the parent, impregnated seed is a service, and this is liable to be taxed under the relevant provisions of the Finance Act as amended, read with the Rules that pertain to service tax. This is a central levy. The transaction between Monsanto India and the third party with whom it deals is not, and cannot be, a sale assessable under the Maharashtra Value Added Tax Act, 2002 ("**the MVAT Act**"). Mr. Venkatraman insists that the transaction in question involves no transfer of a chattel *qua* chattel; no transfer of the right to use; and therefore, by necessary elimination, it must be a service and must be construed as such. He says that what is being offered is the technology; the container, receptacle or form in which it is transmitted is entirely irrelevant. What the third party pays for is the technology, not the container; and since this has none of the qualities that define a sale or a deemed sale (viz., a transfer of the right to use), it must be held to be a service. Central to this argument is the aspect of non-exclusivity: Monsanto India passes no 'property' or 'estate' in the technology itself to the third party developer. It merely licenses it. Monsanto India may issue innumerable such technology licenses to various third party developers. Those developers in turn cannot further sub-license the technology. They can only use it to produce a hybrid, sowable seed. Therefore, the third party developers obtain only a right to use the technology; and there is no transfer of that right. The argument against this seems to us to be straightforward: that the only way for Monsanto India to effect this so-called technology transfer is by selling to the developer a seed duly imbued or impregnated with the protective technology. In other words, it is simply not possible for Monsanto India to divorce the container from the technology; without the seed container, the technology is in itself useless. Once this is seen, it becomes apparent that all the qualities that Monsanto India describes as applicable to a sale apply exactly to the third party developers' acquisition of that impregnated seed. That third party developer may further sell it as is or do what he wishes with it. There is clearly not only a transfer of a right to use (as there would be in a deemed sale), but there is in fact a direct sale of the impregnated seed; this is in no way a service.

**(b)** The Subway Petition is, as we have said, an almost exact mirror image. Here, the transaction is a franchise agreement. Subway holds considerable intellectual property in the form of trade marks, copyright and so on. The franchisee in question is in Mumbai, though the agreement is stated to have been executed in Delhi. The situs argument is subsidiary. What Subway says is that the franchise agreement is purely a service. Its franchisee has a mere right to display Subway's marks. It cannot sub-license the intellectual property further downstream to sub-franchisees; it cannot sell or alienate that intellectual property; it enjoys no estate or title in any of the marks. This is, therefore, not a sale or even a deemed sale; it is purely a service. The State Government argues that these submissions are irrelevant. The franchisee has acquired a right to use the marks, and there is, therefore, a transfer of the right to use those marks. In any case, certain amendments to the MVAT Act make all this moot: trade mark assignments and franchise agreements are both now brought into the sweep of the local sales tax law.

**4.** Having closely considered the submissions, we are of the view that the Monsanto Petition must fail, and the Subway Petition must succeed. Our reasons follow.

## II. CONSTITUTIONAL AND LEGISLATIVE FRAMEWORK

**5.** Article 366(29A) reads as follows:

> **"366. In this Constitution, unless the context otherwise requires, the following expressions have the meanings hereby respectively assigned to them, that is to say—**
>
> **(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;"

**6.** The incidence of tax in sub-clause (a) is on the transfer of property in goods; in sub-clause (b), too, it is on the transfer of property in goods, but in the context of a works contract; in sub-clause (c), it is on the delivery of goods; in sub-clause (d), it is on the transfer of a right to use any goods; in sub-clause (e), it is on the supply of goods as part of a service; and in sub-clause (f), it is on the supply of services. It is sub-clause (d) that falls for consideration in these Writ Petitions.

**7.** The relevant provisions of The Maharashtra Value Added Tax, 2002 read thus:

> "**2. Definitions.— In this Act, unless the context otherwise requires,-**
>
> (24) "sale" means a sale of goods made within the State for cash or deferred payment or other valuable consideration but does not include a mortgage, hypothecation, charge or pledge; and the words "sell", "buy" and "purchase", with all their grammatical variations and cognate expressions, shall be construed accordingly;
>
> Explanation.— For the purposes of this clause,—

(a) ...

(b)(i) the transfer of property in any goods, otherwise than in pursuance of a contract, for cash, deferred payment or other valuable consideration;

(ii) the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract including, an agreement for carrying out for cash, deferred payment or other valuable consideration, the building, construction, manufacture, processing, fabrication, erection, installation, fitting out, improvement, modification, repair or commissioning of any movable or immovable property;

(iii) a delivery of goods on hire-purchase or any system of payment by instalments;

**(iv) 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;**

(v) the supply of goods by any association or body of persons incorporated or not, to a member thereof for cash, deferred payment or other valuable consideration;

(vi) 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 made or given for cash, deferred payment or other valuable consideration;

**shall be deemed to be a sale**."

"**Schedule C**

| **Sr. No.** | **Name of Commodity** | **Conditions and exceptions** | **Rate of Tax** | **Date of Effect** |
|---|---|---|---|---|
| 39 | Goods of intangible or incorporeal nature as may be notified from time to time by the State Government in the Official Gazette. | | 4% | 1-4-2005 to 31-2-2010 |
| 39 | Goods of intangible or incorporeal nature as may be notified from time to time by the State Government in the Official Gazette. | | 5% | 1-4-2010 to date |

**8.** The relevant provisions of the Finance Act, 1994 are set out below.

**65. Definitions.— In this Chapter, unless the context otherwise requires,**

> "(55a) "intellectual property right" means any right to intangible property, namely, trade marks, designs, patents or any other similar intangible property, under any law for the time being in force, but does not include copyright;"
>
> "(55b) "intellectual property service" means, — (a) transferring, temporarily; or (b) permitting the use or enjoyment of any intellectual property right;"
>
> "(105) "taxable service" means any service provided or to be provided,-
>
> > (zzr) to any person, by the holder of intellectual property right, in relation to intellectual property service;"

**66E. Declared Services:**- The following shall constitute declared services, namely:—

> (c) temporary transfer or permitting the use or enjoyment of any intellectual property right;

(*Emphasis added throughout*)

**9.** Mr. Venkatraman relies on a number of judgments to elucidate the meaning and requirements of Article 366(29A)(d). These, he says, must always be present for a transaction to fall within the ambit of this Article. Mr. Shroff too has adopted his formulation of the law. Although these are considered in detail later in this judgment, a summary of these legal submissions on this aspect would be helpful. Briefly, Mr. Venkatraman's argument is that for a transaction to qualify as a transfer of the right to use goods — a deemed sale — the following requirements must be met : (a) there must be a transfer goods; (b) 'transfer' requires divesting in one and vesting in another of the same rights or goods; (c) the effective control over the goods must pass to the transferee; (d) the original owner must be temporarily excluded from using the right himself and, besides the conveyance of title, every other right should accrue absolutely in the hands of the transferee — the right cannot exist simultaneously in the hands of both the transferor and the transferee; (e) the original owner must not be able to effect a further transfer of the same rights to others, during the period they are vested in the transferee; and (f) the concept of transfer is the same for both tangible and intangible goods.

**10.** We have not found this summation of the law to be entirely accurate. We do not think that points (c), (d) and (e) must always be satisfied. The judgments cited in support were in a certain factual background and, in our opinion, were given not as a general proposition of law, but within the confines of their respective factual matrices. In any case, even on Mr. Venkatraman's formulation of the law we have found against him. For precisely the reasons we rule against Monsanto India, we find for Subway.

## III. FACTS IN THE MONSANTO PETITION

**11.** The Petitioner in Writ Petition No. 9175 of 2015, Monsanto India, is a joint venture company of Monsanto Investment India

Private Limited ("**MIIPL**") and the Maharashtra Hybrid Seeds Co. Monsanto India develops and commercializes insect-resistant hybrid cottonseeds using a proprietary "Bollgard technology", one that is licensed to Monsanto India by Monsanto USA through its wholly-owned subsidiary, Monsanto Holdings Private Limited ("**MHPL**"). This technology is further sub-licensed by Monsanto India to various seed companies on a non-exclusive and non-transferable basis to use, test, produce and sell genetically modified hybrid cotton planting seeds. In return for this technology, Monsanto India receives trait fees based on the number of packets of seeds sold by the sub-licensees. These sub-licensing agreements, with almost 40 seed companies, are the transactions in question. Respondent Nos.1 and 2 in the Monsanto Writ Petition are the Union of India and the State of Maharashtra respectively. Respondent No.3 is the Principal Commissioner of Service Tax. Respondent No. 4 is the Commissioner of Sales Tax.

**12.** The Monsanto Petition, filed under Article 226 of the Constitution of India, brings a challenge to Entry 39 of Schedule C to the Maharashtra Value Added Tax Act, 2002 ("**the MVAT Act**"); the definitions under Sections 65(105)(zzr), 65(55a) and 65(55b) of the Finance Act, 1994; and sub-clause (c) of Section 66E of the Finance Act, 1994. The challenge is on two grounds. First, that these are *ultra vires* Articles 14, 19(1)(g) and 265 of the Constitution of India. Second, that the exercise of power of the Respondent No.1 under Entry 54 in List II of the Constitution is *ultra vires*; it encroaches on the power vested exclusively in the Union under Entry 97 in List I.

**13.** The principal question of this dispute is whether these agreements whereby the 'Monsanto technology' is granted by the Petitioner to the seed companies amounts to mere permissive use and, therefore, a service under Section 65(B)(44) of the Finance Act, 1994 ( "**Finance Act**") read with Entry 97 List I of the Constitution, or whether it is a "deemed sale" in the nature of "transfer of right to use goods" under clause (b)(iv) of the Explanation to Section 2(24) of the MVAT Act read with Article 366(29A)(d) and Entry 54 List II of the Constitution.

**14.** A brief background of the Monsanto technology and business structure is necessary. *Bacillus Thuringlensis* ("**BT**") is a naturally occurring bacterium that produces proteins that kill specific insects. Using biotechnology, Monsanto USA introduces a specific BT gene into the cotton genome. This produces a toxin protein in the cottonseed sufficient to kill specific insects, viz., boll weevils or bollworms. These 'Bollgard' cottonseeds, called the 'donor seeds', containing the BT gene were initially imported by MHPL in India from Monsanto USA. MHPL also uses these seeds to produce more donor seeds in its facilities, and licenses the technology to Monsanto India in return for a 16.5% royalty on the latter's turnover. The process thereafter is as follows. Monsanto India enters into sub-licensing agreements with other seed companies through which it claims to grant permissive use of the technology via donor seeds. A sample of such sub-licensing agreement is annexed.[1] Monsanto India delivers fifty sample BT 'donor seeds' to the seed companies for BT cotton hybrid production, along with the standard operating

1. Monsanto Petition, Exhibit "D", *pp.* 44–69.

procedure (SOP) manual prepared by Monsanto USA. The seed companies produce or generate additional donor seeds from these given seeds. Monsanto India provides initial training to the seed companies to assist them in using the donor seeds and developing foundation seeds, which will enable them to eventually produce BT cotton hybrids. Monsanto India thereafter provides training to the seed companies to carry out the zygosity test, which tests the execution of the breeding plan. The sub-licensees, at the end of this process, are required to undertake regulatory trials to obtain the relevant approvals from the various institutes such as the Institutional Biosafety Committee of the Department of Biotechnology, Ministry of Science and Technology, Ministry of Environment, Genetic Engineering Advisory Committee (GEAC) and others responsible. These approvals need certificates of validation and test reports, which are provided by Monsanto India. Once such approval is obtained from the GEAC, each sub-licensee can produce BT cotton hybrid seeds. These BT cotton hybrid seeds are then sold to farmers.

**15.** At present, the technologies licensed are Bollgard I ("**BG I**") and Bollgard II ("**BG II**"). The agreement provides for a few restrictions on the seed companies: the technology is non-transferable, non-exclusive, and cannot be assigned except in the manner provided in the agreement. The seed companies cannot grant further sub-licenses, and the sub-licensee is not permitted to reverse engineer, modify or use the BT gene without the prior consent of Monsanto India. Under the agreement, Monsanto India has also to provide training to produce hybrids at various stages, apart from assisting the seed companies in obtaining the required approvals and conducting zygosity tests. This training includes classroom training and sharing of protocols. Under the sub-licensing agreement, Monsanto India receives consideration from the seed companies in the form of a one-time fixed fee and a recurring variable based on the sale of the genetically modified seeds; in essence, a trait fee.

**16.** Prior to the introduction of the VAT system in Maharashtra, tax on transfer of right to use goods was governed by the Maharashtra Sales Tax on Transfer of Right to Use any Goods Act, 1985 ("**Lease Tax Act**"). Under this legislation, Monsanto India was not liable to pay any sales tax because the exhaustive entry concerning intangible goods did not cover technical know-how. *Vide* an application of Determination of Disputed Question ("**DDQ**"), Monsanto India applied to the Commissioner of Sales Tax to determine the applicability of the Lease Tax Act.[2] The order provided that Monsanto India would be expected to pay a 4% sales tax on the sub-licensing transaction.[3] Aggrieved by this order, Monsanto India appealed to the Maharashtra Sales Tax Tribunal. The appeal succeeded.[4]

**17.** From 1st April 2005, the VAT regime replaced the sales tax regime, and this covers lease transactions, attracting a tax of 4% (increased to 5% since April, 2010) on the basis of the rate specified under the Schedule. This entry expressly includes technical know-

2. Monsanto Petition, Exhibit "F", *pp.* 71-78.
3 Monsanto Petition, Exhibit "G", *pp.* 79–91.
4. Monsanto Petition, Exhibit "H", *pp.* 92—110.

how. However, Section 96(1)(f) of the MVAT Act provides that this would only apply to transactions after April 1st 2005; prior transactions were covered by the Lease Tax Act and, therefore, attracted no tax. So even under the VAT regime, no tax was paid on the trait fees. However, all amended agreements attracted VAT. In order to determine the applicability of the Supreme Court judgment in the case of *Bharat Sanchar Nigam Ltd v Union of India*,[5] Monsanto India made another DDQ application.[6] However, there is no order against this DDQ application. By its letter dated 4th February, Monsanto India requested the Commissioner of Sales Tax, Maharashtra to pass an order against this application.[7] There, too, no order has been passed till date.

**18.** Monsanto India is a registered Service Tax assessee with the registration certificate no. AABCM0176BST001, and is also listed with the Principal Commissioner of Service Tax.[8] Monsanto India's agreement also came within the ambit of the definition of 'service', provided in the Finance Act, and was liable be taxed in the category of "Intellectual Property Services". Several show cause notices were issued by the Service Tax Commissioner demanding service tax under the category of "Franchisee Service" for the trait fees received for BG I. One of these is annexed.[9] Monsanto India was initially engaged in licensing the BG I technology, but this did not come under the ambit of "Intellectual Property Services" because it

5. 2006 (2) STR 161 (SC).
6. Monsanto Petition, Exhibit "K", *pp.* 116–123.
7. Monsanto Petition, Exhibit "L", *p.* 124
8. Monsanto Petition, Exhibit "C", *pp.* 42–43.
9. Monsanto Petition, Exhibit "N", *pp.* 131–142.

was not patented. Monsanto India, in 2007, started to license the technology in BG II, which, being patented, required it to remit service tax. Monsanto India has been paying service tax since 2007.

**19.** Monsanto India submits that while under Section 66E of the Finance Act, a temporary transfer or permissive use or enjoyment of any intellectual property is considered to be a declared service, liable to service charge, the issuance of the Trade Circular also brought its sub-licensing agreement under the ambit of VAT. Currently, therefore, it is subject to a double levy, as both a service and a sale. This is impermissible in law.

## IV. SUBMISSIONS & FINDINGS IN MONSANTO

**20.** The crux of Mr. Venkatraman's case is that Monsanto India's agreements fall within the ambit of a permissive use rather than a transfer of a right to use. It is, therefore, a service and not a deemed sale within the meaning of Article 366(29A)(d) of the Constitution of India. The transaction, he says, is a single composite transaction and cannot be taxed as both a sale and a service. Sales tax and service tax are mutually exclusive and this, he says, is well-settled: *BSNL*,[10] *Imagic Creative Private Limited v CTO*[11] and *Association of Leasing and Finance Companies v UOI*.[12] Paragraph 28 of *Imagic Creative*, which followed the law in *BSNL*, reads:

**10**. 2006 (2) STR 161 (SC).
**11**. 2008 (9) STR 337.
**12**. 2010 (20) STR 417.

> "Payments of service tax as also the VAT are mutually exclusive. Therefore, they should be held to be applicable having regard to the respective parameters of service tax and the sales tax as envisaged in a composite contract as contradistinguished from an indivisible contract. It may consist of different elements providing for attracting different nature of levy. It is, therefore, difficult to hold that in a case of this nature, sales tax would be payable on the value of the entire contract; irrespective of the element of service provided. The approach of this assessing authority, to us, thus, appears to be correct."

**21.** The expression 'transfer of a right to use' under Article 366(29A) of the Constitution, Mr. Venkatraman says, was first considered by a Constitution Bench of the Supreme Court in *20th Century Finance Corporation Limited v State of Maharashtra*.[13] The Court held that the taxable event under Article 366(29A)(d) was the *transfer* of the right to use goods, and a distinction was set out between a transfer of a right to use goods and a mere permissive use of goods. Paragraphs 26 and 27 of the judgment read:

> "26. **Next question that arises for consideration is, where is the taxable event on the transfer of the right to use any goods.** Article 366(29A)(d) empowers the State legislature to enact law imposing sales tax on the transfer of the right to use goods. The various sub-clauses of Clause (29A) of Article 366 permit the imposition of tax thus: Sub-clause (a) on transfer of property in goods; Sub-clause (b) on transfer of property in goods; Sub-clause (c) on delivery of goods; Sub-

**13** (2000) 6 SCC 12

clause (d) on transfer of the right to use goods; Sub-clause (e) on supply of goods; and Sub-clause (f) on supply of services. The words "and such transfer, delivery or supply..." In the latter portion of Clause (29A), therefore, refer to the words transfer, delivery and supply, as applicable, used in the various sub-clauses. Thus, the transfer of goods will be a deemed sale in the cases of sub-clauses (a) and (b), the delivery of goods will be a deemed sale in case of Sub-clause (c), the supply of goods and services respectively will be deemed sales in the cases of sub-clauses (e) and (f) and the transfer of the right to use any goods will be a deemed sale in the case of Sub-clause (d). **Clause (29A) cannot, in our view, be read as implying that the tax under Sub-clause (d) is to be imposed not on the transfer of the right to use goods but on the delivery of the goods for use. Nor, in our view, can a transfer of the right to use goods in Sub-clause (d) of Clause (29A) be equated with the third sort of bailment referred to in "Bailment" by Palmer, 1979 edition, page 88. The third sort referred to there is when goods are left with the bailee to be used by him for hire, which implies the transfer of the goods to the bailee. In the case of Sub-clause (d), the goods are not required to be left with the transferee. All that is required is that there is a transfer of the right to use the goods. In our view, therefore, on a plain construction of Sub-clause (d) of Clause (29A), the taxable event is the transfer of the right to use the goods regardless of when or whether the goods are delivered for use.** What is required is that the goods should be in existence so that they may be used. And further contract in respect thereof is also required to be executed. Given that, the locus of the deemed sale is the place where the right to use the goods is transferred. Where the goods are when the right to use them is transferred is of no relevance to the locus of the deemed sale. Also of no relevance to the deemed sale is where the goods are delivered for use pursuant to the transfer of the right to use them, though it may be that in the case of an oral or implied transfer of the right to use goods, it is effected by the delivery of the goods.

27. **Article 366(29A)(d) further shows that levy of tax is not on use of goods but on the transfer of the right to use goods. The right to use goods accrues only on account of the transfer of right. In other words, right to use arises only on the transfer of such a right and unless there is transfer of right, the right to use does not arise. Therefore, it is the transfer which is sine qua non for the right to use any goods**."

(*Emphasis added*)

**22.** The expression 'transfer', Mr. Venkatraman says, is neither novel nor recent. It is jurisprudentially well-established. The essence of a 'transfer', he submits, is the acquisition of a right by the transferee, and the corresponding loss of it by the transferor. When applied to goods, it would mean the the passing of the goods from the hands of the transferor to the hands of the transferee. He relies on *Salmond on Jurisprudence, Corpus Juris Secundum* and the judgment of the Andhra Pradesh High Court in *Rashtriya Ispat Nigam Limited v Commercial Tax Officer*,[14] in support.

**23.** *Salmond* defines the expression 'transfer of a right' as follows:[15]

> The transfer of a right is an event which has a double aspect. It is the acquisition of a right by the transferee, and loss of it by the transferor. The vestitive fact, if considered with reference to the transferee is a derivative title, while from the point of view of the transferor it is an alienative fact.

**24.** *Corpus Juris Secundum* defines 'transfer' as follows:[16]

> "The common use of the word 'transfer' is to denote the passing of title in property, or an interest therein, from one person to another, and in this sense the term means that the owner of property delivers it to another person with the intent of passing the right which he had it to the later."

**25.** In *Rashtriya Ispat Nigam Limited v Commercial Tax Officer*,[17] the High Court of Andhra Pradesh, relying on *Salmond* and *Corpus Juris Secundum*, explained the expression 'transfer', in the context of the transfer of the right to use in paragraph 9 of its judgment in these words:

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**14**. (1990) 77 STC 182.
**15**. 12th Edition, *pp*. 332 and 333.
**16**. Volume 87, *p.* 892.
**17**. (1990) 77 STC 182.

> "the essence of transfer is passage of control over the economic benefits of property which results in terminating rights and other relations in one entity and creating them in another."

**26.** Mr. Venkatraman further states that the question of whether or not a particular transaction amounts to a transfer of the right to use goods depends on who, i.e., the transferor or transferee, has *effective* control over the goods. If the effective control over the goods is given to the transferee, then, he says, it would be a transfer of the right to use goods. If, on the other hand, the transferor retains effective control, then it would be a case of a mere permissive use or license to use. The term 'effective control' is used in contrast to mere physical control. It is the power to exercise those rights that arise out of ownership, as opposed to, say, a bailment. For this, he relies on the judgments of the Supreme Court in *Aggarwal Brothers v State of Haryana*[18] and *State of Andhra Pradesh v Rashtriya Ispat Nigam Limited*.[19]

**27.** Mr. Venkatraman concludes his summation of the law on the transfer of the right to use goods by relying on the Supreme Court decision in *Bharat Sanchar Nigam Limited v Union of India*.[20] In his separate but concurrent judgment, Lakshmanan J listed the five attributes that must be present for a transaction to qualify as a transfer of the right use goods. Most pertinent, Mr. Venkatraman

**18**. (1999) 9 SCC 182.
**19**. (2002) 3 SCC 314.
**20**. 2006 (2) STR 161 (SC).

says, are attributes 4 and 5. He refers to these two collectively as the '*BSNL twin test*'. Paragraph 91 lists these attributes as follows:

> **91.** To constitute a transaction for the transfer of the right to use the goods the transaction must have the following attributes:
>
> a. There must be goods available for delivery;
>
> b. There must be a consensus ad idem as to the identity of the goods;
>
> c. The transferee should have a legal right to use the goods — consequently all legal consequences of such use including any permissions or licenses required therefore should be available to the transferee;
>
> d. **For the period during which the transferee has such legal right, it has to be the exclusion to the transferor — this is the necessary concomitant of the plain language of the statute — viz. a "transfer of the right to use" and not merely a licence to use the goods;**
>
> **e. Having transferred the right to use the goods during the period for which it is to be transferred, the owner cannot again transfer the same rights to others.**"

(*Emphasis added*)

**28.** Mr. Venkatraman then submits that although the law on the concept of 'transfer' in the context of the transfer of the right to use goods, as seen above, has been laid down in the context of tangible goods, it applies equally to intangible goods as well. The reason, he says, is that the expression 'goods' includes both tangibles and intangibles. The Constitution of India, under Article 366(12), defines 'goods' to include all materials, commodities and articles. We have no difficulty in accepting this proposition. The Supreme Court, in a number of judgments, has held that the expression 'goods' includes both tangibles and intangibles. The Constitution Bench in *Tata Consultancy Services v State of Andhra Pradesh*[21] held that as long as intangible goods remained in an intangible form, they could be treated differently. However, once such intangibles are captured in some media, which is a tangible form, the intangibles, too, become goods. Similarly, in *Sunrise Associates v Government of NCT of Delhi*[22] and *Yasha Overseas v Commisioner of Sales Tax*[23] the Supreme Court held that a right, tangible or intangible, that is capable of being bought and sold independently for consideration becomes goods.

**29.** Therefore, Mr. Venkatraman says, there is no distinction in law between tangible and intangible goods. Neither Article 366(12) nor 366(29A)(d) of the Constitution prescribe separate parameters for a 'transfer' of tangible goods and a 'transfer' of intangible goods. Neither expression, i.e. 'goods' or 'transfer', has any artificial or deeming fictions for intangible goods. The expression 'transfer' in Article 366(29A)(d), therefore, has the same meaning with respect to both tangible goods and intangibles.

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**21**. (2005) 1 SCC 30.
**22**. (2006) 5 SCC 603.
**23**. (2008) 8 SCC 681.

**30.** For a transaction to qualify as a transfer of the right to use goods, in Mr. Venkatraman's formulation, the following tests must be met: (a) there must be a transfer goods; (b) such a 'transfer' requires divesting in one and vesting in another of the same rights or goods; (c) the effective control over the goods must pass to the transferee; (d) the original owner must be temporarily excluded from using the right himself and besides the conveyance of title, every other right should accrue absolutely in the hands of the transferee —the right cannot exist simultaneously in the hands of both the transferor and the transferee; (e) the original owner must not be able to effect a further transfer of the same rights to others, during the period they are vested in the transferee; (f) the concept of transfer is the same for both tangible and intangible goods. If these criteria are not met, then, he says, the transaction does not constitute a 'deemed sale' within the meaning of Article 366(29A)(d). For this reason, he contends that the decisions of this Court in *Commissioner of Sales Tax v Duke and Sons*[24] and *Tata Sons Limited v State of Maharashtra*,[25] and that of the Andhra Pradesh High Court in *Nutrine Confectionary Company Private Limited v State of Andhra Pradesh*[26] do not represent the correct position in law.

**31.** Mr. Venkatraman urges us to hold the decision of this Court in *Duke & Sons* was *per incuriam* because substantially relevant law had not been considered; or, at any rate, it is no longer good law. At the time when *Duke & Sons* was decided, there was no judgment of the Supreme Court interpreting Article 366(29A)(d). According to

**24**. (1999) 1 Mah LJ 26

**25**. 2012 SCC OnLine Bom 697; (2015) 80 VST 173 (Bom).

**26**. (2011) 40 VST 327 (AP).

Mr. Venkatraman, *Duke & Sons* held that control and possession are not essential for a transfer of right to use, and that the mere authorization to use is sufficient for the transaction to qualify as a transfer. In fact, even without effective control, permissive use and license would fall within the meaning of transfer of right to use. However in 2000, the Supreme Court held in *20th Century Finance Corporation* that mere use would not constitute a deemed sale, and that transfer is the *sine qua non* of any sale. Even *Salmond on Jurisprudence* and *Corpus Juris Secundum* say that transfer is an acquisition of right on the part of the transferee and loss of that right by the transferor. The decisions of the Supreme Court in *Aggarwal Brothers* and in *Rashtriya Ispat Nigam Limited* also hold that effective control is a *sine qua non* for transfer of right to use. Mr. Venkatraman therefore submits that the finding in *Duke & Sons* that there is no need for effective control and that mere permission or license would be sufficient to constitute a deemed sale cannot be good law. This is especially so in light of the decision in *BSNL*, where the Supreme Court laid down a two-pronged test, viz., i) temporary exclusion of transferor and ii) loss of effective control, for a transaction to qualify as a transfer of the right to use making it a 'deemed sale'. Mr. Venkatraman submits that the holding in *Duke & Sons* that the decision of the Andhra Pradesh High Court in *Rashtriya Inspat Nigam Limited* does not apply to trade marks is not the correct position in law today. This is so, he submits, because the Supreme Court has clarified time and again, right from *20th Century* to *BSNL*, that there must be an vesting in the hands of the transferee and a concomittant divesting from the hands of the transferor. There is also nothing in the law, he submits, to distinguish between tangible and intangible goods. This, he says, also cannot be done in view of the judgment of the Constitutional Bench in *Tata Consultancy Service*, which held that goods include both tangible and intangible. Thus, the same considerations will apply to transactions regarding intangible goods as well.

**32.** He also contends that the judgment of this Court in *Tata Sons* was also decided *per incuriam* (or is incorrect) since certain crucial aspects directly affecting the issue in question were not brought to the Court's notice. To begin with, he says, *Tata Sons* followed the ratio in *Duke & Sons*, which, as stated earlier, is not the correct position in law in light of subsequent judgments of the Supreme Court. These were not placed before the Court. Further, during the period in question, i.e., 1998 to 2002, only the transfer of a right to use goods was taxable under Article 366(29A)(d), and a mere permissive or license to use was not liable to service tax under the Finance Act, 1994. Sections 65(55a) and 65(105)(zzr) of the Finance Act, 1994, under which permissive use of intellectual property is liable to service tax, came into force only on 10th September 2004. The service tax authorities were not parties to the proceedings. The Court, therefore, did not have the opportunity to consider rival submissions on the question of whether the transaction was a deemed sale under Article 366(29A)(d) or a mere permissive use. In fact, in paragraph 58 the Court expressly stated that it did not express any opinion as to the propriety of the Maharashtra Sales Tax Tribunal's decisions in *M/s. Smokin' Joe's Pizza Pvt. Ltd. v State of Maharashtra*[27] and *Diageo India Pvt. Ltd. v State of Maharashtra*,[28] as

**27**. (2009) 39 MTJ 266; Appeal No. 25 of 2004; decided on 25th November 2008.

separate proceedings in that regard were pending. These were cases where the issue of sale versus service had been raised, but on which the *Tata Sons* court expressed no opinion. Lastly, Mr. Venkatraman says that the Court placed reliance on three decisions of the Kerala High Court *in Kreem Foods Private Limited v State of Kerala*,[29] *Jojo Frozen Foods Private Limited v State of Kerala*[30] and *Mechanical Assembly Systems (India) Private Limited v State of Kerala*,[31] all of which had concurred with the view taken in *Duke and Sons*. These three decisions had subsequently been distinguished by the Kerala High Court itself in *Malabar Gold Private Limited v CTO*.[32] This was not pointed out to the Court.

**33.** Mr. Venkatraman submits that the decision of the Andhra Pradesh High Court in *Nutrine Confectionary Co Pvt Ltd v State of Andhra Pradesh*[33] does not correctly interpret the test laid down in *BSNL*. In *Nutrine*, the Court held that in *BSNL*, the goods in question were mobile telephone connections, which are anyway invariably limited to the licensee. This cannot be said to be true of a trade mark or logo. The fact that the appellant still continued to hold the mark **NUTRINE** for itself and transacted business in such name even after licensing it to others, the Court held, cannot be reason to exclude it from being a sale. This is because a trade mark is

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**28**. (2009) 40 MTJ 285; Second Appeal Nos. 1432 to 1438 of 2006 decided on 12th February 2009.

**29**. (2009) 24 VST 333.

**30**. (2009) 24 VST 327.

**31**. (2006) 144 STC 536.

**32**. (2013) 32 STR 3.

**33**. (2011) 40 VST 327 (AP).

inherently capable of being assigned for either an exclusive use or a limited use to multiple licensees. Mr. Venkatraman urges that the decision in *Nutrine* did not apply the *BSNL* "twin test" that was expressly laid down by the Supreme Court. Without appreciating that Nutrine Confectionary Company was not divesting effective control or retaining exclusivity, the Bench held it to be a transfer of right to use. This is contrary, Mr. Venkatraman says, to *BSNL*.

**34.** The Finance Act tells us that a service is a transaction without a sale. This means, Mr. Venkatraman says, that any transaction that is not a sale (or a deemed sale within the meaning of Article 366(29A) of the Constitution of India) is a service, barring of course, those transactions specifically excluded from the definition. Permissive use is one such transaction: it is a service. Therefore, he submits, the transaction in question is a service, and not amenable to any form of sales tax levy.

**35.** Mr. Venkatraman says that in the present case, the 'goods' in question is the 'Bollgard Technology'. This is a pure intangible. The seeds, he says, are merely the media. They are immaterial while considering the question of whether this transaction is a sale or a service, and should be ignored. The licensee is merely permitted to use the Bollgard Technology and nothing further. How it acquires that permission to use is of no consequence. Clause 2.1 of the sub-licence agreement explicitly states that the grant to the sub-licensee is of a non-exclusive and non-transferable sub-license to use the Bollgard technology. The expression "non-exclusive", he says, has important implications. First, Monsanto India can continue to use the technology during the period of the agreement; and second, it can further sub-license the same technology to as many others as it pleases. Therefore, this agreement fails the *BSNL* twin test. At no point is Monsanto India divested of the technology. The simultaneous availability of the same right in the hands of both the transferor and the transferee, Mr. Venkatraman argues, nullifies the presumption of a transfer. Effective control over the goods, i.e., the intangible technology, remains with Monsanto India. Therefore, this is a case of mere permissive use. Had the right to use the technology been granted *exclusively* to the sub-licensee, then, he says, it would have been a case of transfer of the right to use.

**36.** He explains this using the following illustrations:

**(a)** *A* is the owner of an intangible right. *A* transfers this right to use the intangibles to *B* temporarily, to *A*'s exclusion. This case, he says, would fall under Article 366(29A)(d) as the transfer is of a right to use goods, since the *BSNL* twin tests of exclusion of the right and incapability of further transfer are both satisfied.

**(b)** In the second scenario, *A* grants the right to use the intangibles to *B* in Maharashtra, to *C* in Karnataka and to *D* in Tamil Nadu. This agreement, he says, would reflect two aspects. First, the transfer is exclusive to the respective parties in their jurisdictions. It also excludes the transferor from using the intangible right in any of these States, thus rendering temporarily numb the transferor's right to use. In this case, too, he says, the

*BSNL* twin tests would apply. The question that arises here is whether the second aspect of the *BSNL* twin test (incapacity of the transferor to make further transfers) is satisfied, given that *A* has transferred the right to three different individuals. Had the goods in question been tangibles, the test of incapacity to make further transfers would mean that once the goods are transferred to *B*, the first transferor, *A* could not then transfer these to *C*, *D* and so on. The reason this is not so is because of the nature of intangible rights. A tangible right is limited to the physical property involved, but this is not the case with intangible rights. One can wheel out as many transactions as possible and simultaneously too, in terms of place, person, period etc. But the test of transfer must remain the same as seen above, i.e., an extinction of the right temporarily in the hands of the transferor and the inability to transfer it again to somebody else. When, therefore, *A* makes a temporary transfer to *B* in Maharashtra, he agrees that it is to his exclusion. This precludes *A* from further transferring it to *B2*, *B3* or *B4* in Maharashtra. This makes the transfer to *B* in Maharashtra, and likewise to *C* and *D* in Karnataka and Tamil Nadu respectively, exclusive *and* to the exclusion of *A*. Therefore, he says, the *BSNL* twin test is satisfied.

**(c)** Lastly, *A* grants a license to use the right to *B*, *C* and *D* either for the whole of India or specified territories to each party. The agreement does not exclude the right

> temporarily in the hands of *A*. He can grant the same rights to others, either for the whole of India or some specified territories. This transaction, he says, does not satisfy the *BSNL* twin test for two reasons: first, *A* is not temporarily excluded from the right, and second, he can further grant the same rights to others. Therefore, this is a case of permissive use or license to use goods but not a case of a transfer of the right to use. He submits that Monsanto India's case falls under this third scenario.

**37.** We have considered most carefully this submission. It is indeed sophisticated in its construction, and, at first blush, appears most appealing. On reflection and a closer examination, we find ourselves unable to subscribe to the interpretation Mr. Venkatraman so eloquently commends, viz., that his transaction is one of a merely permissive use. We find this interpretation not to be supported by law, and we have the most serious reservations about the universal applicability of his propositions, which seem to us to be overbroad and to cast the net too widely. The first question is whether there is a 'transfer' within the meaning of Article 366(29A)(d). We believe there is. It is true that the essence of a 'transfer' is the divesting of a right or goods from transferor and the investing of the same in the transferee, and this is what *Salmond on Jurisprudence* and *Corpus Juris Secundum* both say. In our opinion, the seeds embedded with the technology are, in fact, transferred. Monsanto India is divested of that portion of the technology embedded in these fifty seeds and these are fully vested in the sub-licensee. Mr. Venkatraman is not correct when he says that the effective control of the 'goods' is with

Monsanto India. In *RINL*, the Supreme Court concluded that the contractor (transferee) did not have effective control over the machinery, despite the fact that he was using it, since he could not make such use of it as he liked. He could not use the machinery for any project other than that of the transferor's, nor could he move it out during the period of the project. We do not see how we can draw a parallel from that case to the one at hand. The effective control over the seeds, and, therefore that portion of the technology that is embedded in the seeds, *is entirely* with the sub-licensee. That sub-licensee is not bound to use the seeds (and the embedded technology) in accordance with Monsanto India's wishes. Monsanto India cannot further dictate to the sub-licensee what he or it may do with these technology-infused seeds. The sub-licensee can do as it wishes with them. It may not use them at all. It may even destroy the seeds. Once the transaction is complete, i.e., once possession of the technology-imbued seeds is effected, and those seeds are delivered, Monsanto India has nothing at all to do with the technology embedded in those fifty seeds given to the sub-licensee. At no point does Monsanto India have access to this portion of the technology. In other words, the transfer is to the exclusion of Monsanto India. This clearly satisfies the so-called *BSNL* "twin test" that Mr. Venkatraman is at pains to propound. Mr. Venkatraman's argument that the seeds are "merely the media" and therefore irrelevant is, in our opinion, erroneous. They are relevant for the simple reason that the technology could not have been given to the sub-licensee without them; and there is no other method demonstrated anywhere of effecting any such transfer.

**38.** We must note that Mr. Venkatraman's submission that the *BSNL* test must always be present in each and every case for a transaction to be considered a transfer of the right to use goods is overbroad. We do not think that in *BSNL* the Supreme Court intended to prescribe a test of global or universal application without regard to individual circumstances. The judgment of the Supreme Court (in paragraph 90) notes the factual aspects. There, the entire infrastructure, instruments, appliances and exchange remained in the physical control and possession of the petitioner at all times and there was neither any physical transfer of such goods nor any transfer of the right to use such equipment or apparatuses. One of the issues that arose for consideration was whether there was any transfer of the right to use goods by providing access or a telephone connection by the telephone service provider to a subscriber. This *BSNL* test, was, therefore, set out in these circumstances. The Court had no occasion to consider its applicability to intangible property like intellectual property. This is how *BSNL* has been interpreted by us in *Tata Sons*. We think that this interpretation is correct. In any case, it binds us. The Kerala High Court in *Malabar Gold*, in paragraph 35, took a contrary view. It took the *BSNL* twin test to be applicable as a general proposition, i.e., one that admits of no variance. As discussed above, we do not think this can ever be the a correct reading of *BSNL*.

**39.** Similarly, we do not think the test of 'effective control' in the sense laid down in *RINL* was intended to be one that demanded satisfaction in every case. The goods in *RINL* were machinery. It is in that context that the Supreme Court, upholding the decision of the Andhra Pradesh High Court, held that for a transaction to qualify as a transfer of the right to use goods, 'effective control' must be transferred to the transferee. This Court, in *Duke and Sons*, held that this test would not be applicable in the case of trade marks. It was held that for the transfer of a trade mark it was not necessary to 'hand over' the trade mark to the transferee or give control or possession of trade mark such transferee. We think that this represents the correct position in law. Indeed, when it comes to trade and service marks, there are several intermediate positions that are possible: there may be a mere right to display the mark, for instance; or, there may be an assignment of the mark in its entirety; or there may be a limited or hybrid arrangement that lies in between. Many examples abound: large retail stores routinely carry goods of various brands, i.e., goods with marks that identify their source. A fabric or textile retailer, for instance, or one dealing in electronics, may have multiple brands on sale. This is not a case of a transfer; the right to the retailer is a mere right to display, and there is no transfer of the right to use those marks. There is a mere permission to display goods bearing the mark. An agreement that allows for a mere right to display would be purely a service, and never a sale. At the end of the agreement, the retailer would have to cease all display of the mark; any continued use would be an infringement. The fact that the retailer vends goods bearing those marks does not in any sense confer on him ownership of those marks, nor does it divest the proprietor of those marks of any of the incidents of proprietorship.

**40.** We are, therefore, in complete agreement with Mr. Sonpal when he says that this is a case of a transfer of the right to use goods. He points out certain clauses in the Monsanto India's sub-license agreement which, in our opinion, further substantiate this. Clause

1.1 defines "Cotton Proprietary Germplasm" to mean proprietary hybrid cotton parent lines developed or *owned* by the sub-licensee during the term of the agreement. The word 'owned' implies that a sale has taken place. The term of the agreement, as provided under clause 9.1, is for an initial period of ten years and is further renewable in increments of five years by mutual consent of both parties, unless it is otherwise terminated earlier. What happens after the expiry or termination of the agreement is most interesting. Under clause 9.4, the sub-licensee is not bound to return to Monsanto India any portion of the initial fifty seeds given under the agreement, nor any additional donor seeds the sub-licensee may have produced. The control (and ownership) of the Bollgard Technology contained in those initial fifty donor seeds, as also in the additional donor seeds produced by the sub-licensee is with the sub-licensee. Monsanto India has nothing whatsoever to do with this portion of the technology. The only restriction appears to be on the sale of the GMO cotton planting seeds. The sub-licensee is given a two-year window to sell or otherwise dispose of any remaining GMO planting seeds. After this period, Monsanto India has the option of requiring the sub-licensee to *sell* these planting seeds to Monsanto India itself or to dispose them for non-planting purposes. This clause makes it evident that the ownership of even the planting seeds is with the sub-licensee. Clause 2.5(d) then provides that Monsanto India can further sublicense the Bollgard Technology to a maximum of three other companies in the same territory as that the of the original sub-licensee. For additional transfers, Monsanto India would have to first consult the sub-licensee. Mr. Sonpal rightly states that this suggests that a transfer of the right has, in fact, taken place; and, even on Mr. Venkatraman's own illustrations, this case would not fall within the third illustration, but within the second and perhaps even the first. The degree of territorial exclusion is surely irrelevant; the question is whether or not there is any exclusivity. If it were mere permissive use, there would be no question of the Monsato India having to first consult the sub-licensee before effecting further transfers. Further, under clause 7.1 the sub-licensee can assign the agreement and its rights and obligations under it to its wholly-owned subsidiaries without Monsanto India's permission. Mr. Sonpal rightly says that this can never happen in a case of a permissive use. In law, a wholly-owned subsidiary is a distinct legal entity. In a case of service or permissive use, a person can never assign the goods or rights to a third person.

**41.** At this stage, we find that a parallel to practical, every-day examples would be useful. Take, for instance, the example of when one buys a book from Amazon for their Kindle device. In this case, Amazon can transfer the intellectual property of the book to multiple other users simultaneously, but each single transaction would still be a sale. This would also be true of the example of a music CD. The CD is the 'medium' by which the intellectual property, viz. the songs, passes to the buyer. The manufacturer can sell it to an end-user or to an intermediate retailer. The same song can be put on countless CDs. This too is a sale. When one buys a car, one buys the technology that is contained in the body of the car; the body is just the medium. On ITunes, when one buys a song, the song is transferred into a format which is accessible to the buyer, a proprietory format that needs a special device or software. Yet it is a sale. Limitless ITunes users can buy the song simultaneously. This is a sale to each of them. In the case of CD containing software, say for example Microsoft Word, the medium would again be the CD holding the intellectual property, which would be the software technology. This would also be a sale, despite the fact that this same software technology could be put on unlimited number of CDs and sold to multiple users simultaneously. Effective control of that particular software on that one CD is passed to the buyer. The buyer could use it, alienate it, destroy it, and do anything at all that he likes with it. If he made illicit copies of it, this would constitute infringement; and that in itself would not make the transfer of the software on a CD a service. Even if the buyer transferred this non-transferable software, it would amount to a breach of contract provided in the CD package, just as it would under Monsanto India's sub-licensing agreement. However, this does not do anything to disqualify the transaction itself from being a sale. These are all sales.

**42.** In our opinion, the most fundamental aspect of permissive use of goods is that at the end of the period for which the use is granted, the goods must be returned to the transferor. Let us consider this in the context of a car hire service, a book library service, Amazon Kindle Unlimited and ITunes Radio. When a car is taken on hire, a fee is paid and the car can be used for a certain period of time. During this time, the person renting the car can only use it. He cannot part with it and certainly cannot destroy it. Once the period of hire comes to an end, the car must be returned to the transferor. Therefore, the effective control over the car remains with the transferor. Likewise, in the case of a book library, the books must be returned to the library. With the Kindle Unlimited, one must pay a subscription fee to gain access to an unlimited number of books in the proprietory AZW format. When the subscription expires, all the books are repossessed. ITunes Radio too is a similar concept. A subscription fee is paid, which allows access to music. Once this expires, access to the music is denied. These, in our opinion, are cases of permissive use. The Monsanto India sub-licensing transaction could only be a service in one circumstance, i.e., if the seed companies gave Monsanto India a bag of seeds to mutate and improve with the Bollgard Technology which would, thereafter, be returned to the seed companies. That might perhaps be a service.

**43.** Mr. Sonpal relies on a great many authorities, not all of them apposite. In a case like this, we will not be detained by his submission that Monsanto India's petition is not maintainable because it is a company and therefore disentitled to a high prerogative discretionary remedy under Article 226 of the Constitution of India for a violation of Article 14.[34] The questions raised cannot be countered in so facile a manner. In any case, the Petition was admitted on 15th December 2015, and we do not understand how we can now, at this late stage, dismiss the Petitions on this ground. Similarly, Mr. Sonpal's invocation of the well-settled principle that every precedent must be considered in its factual context is one we cannot appreciate. This does not mean that no judgment has any precedential weight, or that a judgment is a precedent only if the facts are an exact match. This is against every canon of the principle of *stare decisis*. Besides, in making such a submission, Mr. Sonpal might well be, as the Bard famously put it,

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**34**. *State Trading Corporation of India v Commercial Tax Officer*, AIR 1963 SC 1811.

hoist by his own petard; for then the very judgments he cites[35] would have to be held to be restricted to the facts in each. It is also, in our view, not only incorrect but also improper to trivialize Mr. Venkatraman's submissions, the product of much industry and ingenuity, by saying that they are based on nothing more than 'stray' observations of this or that Court. We perhaps lack Mr. Sonpal's dauntlessness, but we are not prepared to agree with him when he says that observations of the Supreme Court do not bind us. They do.

**44.** Mr. Sonpal's reliance on the decision of the Andhra Pradesh High Court in *G.S. Lamba & Sons v State of Andhra Pradesh*[36] is, however, well-founded. The facts of that case are that one *G* manufactured ready mix concrete to its customers' specifications. Dealers entered into contracts with *G* to provide a transportation service for ready-made concrete by hiring transit mixers. *G* was given access to a dedicated fleet of such mixers, coloured and sized to its specifications, and could decide the delivery schedule of these mixers. The Additional Commissioner levied sales tax. The dealers contended that this was a contract of transportation service. A Division Bench set out the essential requirements of transfer of right to use, taking into account all the previous decisions in the field. It held that the essentials are: (i) not a transfer of property in goods, but the right to use property in goods; (ii) Article 366(29A)(d) read with the latter part of the clause (29A) would show that the tax is

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**35.** *Deepak Bhandari v Himachal Pradesh State Industrial Development Corporation Ltd*, AIR 2014 SC 961; *Jitendra Nath Singh v Official Liquidator*, (2013) 1 SCC 462.

**36.** (2011) 43 VST 323.

not on the delivery of goods used, but on the transfer of the right to use goods regardless of when or whether the goods are delivered for use, subject to the condition that the goods should be in use forever; (iii) in a transaction for the transfer of right to use, the delivery of goods is not a condition precedent but one of the elements of the transaction; (iv) the effective or general control does not always mean physical control and even if the manner, method, modalities and the time of the use of goods is decided by the lessee or the customer, it would be under the effective or general control over the goods; (v) the approvals, concessions, licenses and permits in relation to the goods would also be available to the user of the goods even if such licenses or permits are in the name of the owner or transferor of the goods; and (vi) during the period of contract, exclusive right to use the goods along with permits, licenses, etc., vests in the lessee. The Court also reiterated the well-settled principle of law that a document or transaction must be taken as a whole and then scrutinized. This is essential to understand the very nature of the transaction and to understand the intention of the parties while contracting. Courts cannot rely only on the wording of the transaction. This is often of no help and could suggest an entirely different nature. After testing the transaction with the facts of the case, the Bench held that the transaction between *G* and the dealers was a transfer of right to use.

**45.** Requirement (iv) of the decision in *Lamba* is vital to Mr. Sonpal's argument on effective control. This is especially so because Mr. Venkataraman has extensively argued that effective control is essential to transfer of right to use. On testing Monsanto India's sub-licensing agreement against the requirements laid down in decision, we believe this decision sufficiently supports Mr. Sonpal in his argument that the sub-licensing actually amounts to passage of effective control as well of the Bollgard Technology embedded in the seeds.

**46.** In fact, we believe that this sub-licensing of the Bollgard technology may possibly even be an outright sale. For a transaction to qualify for a sale, there must be a transfer of the property in the goods. In legal usage, the word "property" is a generic term, of broad and extensive application; perhaps, the most comprehensive of all terms which can be used.[37] Property embraces everything which is or which may be subject to ownership of any kind at all, and is legally understood to include every class of acquisitions that a man can own or in which he can have an interest. The rights that transfer of property cover are the right of acquisition, possession, use, enjoyment and disposition.

**47.** We pause here momentarily to consider the nature of these intangible goods. We believe this is necessary, because this is perhaps a case where the law is yet evolving to keep abreast of technology. If what Mr. Venkatraman suggests is correct, then every sale of software as we currently know it is never a sale but only a service. In his formulation, the 'medium' (CD, pen drive, etc) is irrelevant. Surely this cannot be correct. Software may be downloaded too, without any 'physical medium' intervening — the medium is as intangible as the goods. It is impossible, we think, and does not stand to reason to suggest that unless, say, Microsoft or

**37**. *Corpus Juris Secundum*, Volume 73, *p.* 135.

Adobe wholly cede all control over their software products there is no sale, and when they allow a user to download and use their software they are only providing a service. Indeed, this is demonstrably incorrect. Microsoft and Adobe both have alternative distributions models. One may 'purchase' a license to Microsoft Office or Adobe Photoshop. This may be a one-off, standalone product, delivered either by download or on physical media. That is for the user to keep and do with it what he wishes (except, of course, attempting to decompile it). He does not have to use it all; he can destroy the media and all personal copies of it. The same software is also available nowadays for a subscription — for an annual or monthly fee, the software can be downloaded and used; if the subscription ends, at the very least updates end and very possibly the software will not function optimally. The latter may be a service, very like car rental or book borrowing from a library. The former is clearly a sale. The difficulty with Mr. Venkatraman's argument is that it tries to draw a completely unnecessary distinction between the technology and the medium in which it is delivered. Neither is the subject of the levy. The subject of the levy is not the technology nor the medium. It is the license; and the terms of that license are determinative. Where a license is *purchased*, it is still a sale, although what the user has 'purchased' is the right to use the software. Every license has a unique key and every sale is therefore uniquely identified. The purchase is therefore a transfer of the right to use that particular, identified software. The proprietary rights to the software do not have to be 'sold' or 'transferred'. Microsoft and Adobe retain all those rights, and all intellectual property continues to vest in them. This is, therefore, a transfer of the right to use that software, and to that extent, the intangible (the software) is sold; but the terms of that license allow the software vendor to retain complete seizin and dominion over all intellectual property rights. The transfer is not of those intellectual property rights, but of the right to use an identified and identifiable version of that software. In the subscription distribution model, where the software usage is dependent on payment of a periodic fee, there is no such transfer, and there is a mere right to use, without any transfer of that right to use even that particular download. So long as the fee is paid, the software may be used; when the fee payment stops, so does the right to use. This exactly parallels car or book rentals. The determinant in such a case must, therefore, be whether the license is such that the licensed intangible is with the licensee in perpetuity or whether the licensor has the right to terminate and repossess and deny further access to that intangible. In a software sale, there is no question of termination or repossession. It is for the licensee to use forever. This is clearly a sale or a deemed sale and it is in respect of not the medium or the intellectual property (the marks, copyright, patents, etc), but is the transfer of the right to use that software *subject* to those marks, patents, copyright, etc. Monsanto India's case is no different. Its sub-licensee do not acquire any proprietory intellectual property rights over the Bollard Technology; Monsanto India's and its parents' patents, copyright, marks and other intellectual property rights are preserved intact, unaffected by the sub-licensing. But the identified technology, the one infused in the fifty seeds given to the sub-licensee, is for the sub-licensee to use as he wishes. Viewed from this perspective, Mr. Venkatraman's clients' underlying fears are, we believe, unfounded.

**48.** Mr. Venkatraman, in the alternative and without prejudice, argues that the seeds themselves are exempt from being taxed under Entry 41 of Schedule A of the MVAT Act, 2002, even if the transaction in question is held to be a sale. Entry 41 of Schedule A reads thus:

> **"SCHEDULE A**
>
> **LIST OF GOODS FOR WHICH THE RATE OF TAX IS NIL%**
>
> **41. Seeds of all types excluding oil seeds and seeds to which any other entry of this Schedule or of Schedule C applies."**

The donor seeds are coker seeds in nature and therefore he argues that they do not fall under the category of oil seeds. To support this contention he relies on the definitions of 'oil seeds' from several dictionaries.

**49.** Since the seeds in question are purely donor seeds, the question of the scope of the entry relating to seeds, Mr. Venkatraman submits, does not arise. Trade Circular 12 T of 2005 bearing No. VAT-2005/Act/VD-1 dated 7th July 2005 has clarified this.[38] Para 2 of the Circular reads as follows:-

> **"Queries have been raised about the scope and limits of this entry. It is accordingly clarified that all types of sowing seeds are covered by the scope of the entry A-41 and such sowing seeds will accordingly stand exempted from tax. This would**

**38.** Monsanto's Compilation, Volume II, *p.* 445.

> **include sowing seeds for cereals, pulses as well as sowing seeds for oil seeds. In addition to sowing seeds, which includes certified seeds and truthfully labeled seeds, nuclear seeds, foundation seeds and breeder seeds, of all types would also be covered by the scope of this entry."**

**50.** Mr. Venkatraman submits that this circular applies to all sowing seeds: donor, breeding, foundation and nuclear seeds. Therefore, Monsanto India's donor seeds would not be liable to VAT.

**51.** Mr. Venkatraman goes a step further. He submits that even if cotton seeds are considered to be oil seeds, Entry 68 of Schedule C of the MVAT Act provides that these oil seeds would be liable to pay a rate of only 5%. Therefore, even in the worst-case scenario, Monsanto India is not liable to pay more than 5% sales tax.

**52.** Given our previous discussion, we do not think it is necessary to go into this question at all, for what is being taxed is not the seed itself but the license that transfers a right to use the seed. Therefore, in our opinion, it makes no difference if the seeds are coker seeds or oil seeds.

**53.** Mr. Venkatraman makes one more without prejudice argument, in case neither of his previous arguments succeed. He submits that even if the agreement in question is held to be a transfer of the right to use (deemed sale) and that it does not fall under the exemption for seeds in the MVAT Act, then the levy and collection of Service Tax by the Union of India would be without the authority of law since VAT can only be levied and collected by the States. As argued earlier, the same transaction cannot be taxed as both a sale and a service. Monsanto India has already paid service tax for the entire period at a rate significantly higher than what is provided under the MVAT Act and therefore he says that it is not liable to pay further tax. For the period between May 2007 and February 2009, it has paid service tax at a rate of 12.36%, for March 2009 to March 2012 at a rate of 10.3%, for April 2012 to May 2015 at 12.36%, and for the period beginning June 2015 at a rate of 14%. Under Entry 39 of Schedule C of the MVAT Act, the applicable rate of sales tax is only 5% since April 2010, prior to which it was 4%. He therefore seeks a Writ of Mandamus directing Union of India to transfer the amount paid as service tax from the Consolidated Fund of India to the Consolidated Fund of State of Maharashtra. He argues that such a transfer would not amount to unjust enrichment. We decline to enter into this debate. We leave it to Monsanto India to adopt suitable proceedings in this behalf, and leave their contentions open to the necessary extent.

## V. FACTS IN THE SUBWAY PETITION

**54.** In Writ Petition No. 497 of 2015, Subway is a private limited company of which Petitioner No. 2 is a full time director. Subway operates and franchises sandwich shops in India. It is part of an international chain. Petitioner No.3 is an executive of the outsourced agency that maintains Subway's account books. Respondent Nos. 1 and 2 are the State of Maharashtra and the

Union of India respectively. Respondent No. 3 is the Commissioner of Service Tax, an officer of Respondent No. 2, while Respondent No. 4 is the Assistant Commissioner of Sales Tax, an officer of Respondent No. 1. This Writ Petition under Article 226 of the Constitution of India, challenges Item (12) under the Notification No. VAT-1505/CR-114/Taxation-1 dated 1st June 2005 as being *ultra vires* Section 6 of the MVAT Act and Article 246 of the Constitution.

**55.** A brief description of Subway's business is this. Subway was granted a non-exclusive sub-license by Subway International B.V. ("**SIBV**"), a Dutch limited liability corporation to establish, operate and franchise others to operate SUBWAY-branded restaurants in India. This non-exclusive license was granted to SIBV itself by Subway Systems International Ansalt, which in turn was granted such a license by Doctor's Associates Inc., an entity that owns the proprietary system for setting up and operating these restaurants. These restaurants serve sandwiches and salads under the service mark **SUBWAY**. The agreement includes not only the trade mark **SUBWAY**, but also associated confidential information and goodwill, such as policies, forms, recipes, trade secrets and the like. Typically, Subway enters into franchise agreements with third parties, under which it provides specified services to the franchisee. In return, the franchisee undertakes to carry on the business of operating sandwich shops in Subway's name. The agreement only provides for a very limited representational or display right, and the franchisee cannot transfer or assign these exclusive rights to any third person. Subway also reserves the right to compete with these franchisees in the agreement. Under this agreement, Subway receives two kinds of consideration, one being a one-time franchisee fee which is paid when the agreement is signed; and the second is a royalty fee paid weekly by the franchisee on the basis of its weekly turnover. A sample franchise agreement is annexed.[39] Under these agreements, the franchisees have no more than a right to display Subway's intellectual property in the form of marks and logos, and a mere right to use such confidential information as Subway discloses and as prescribed by the franchise agreement.

**56.** Since September 2003, Subway has been paying service tax to the Union of India on the consideration received by it from the franchisees. In November 2014, Respondent No. 4 sought information from Subway under the MVAT Act, which Subway provided. Respondent No. 4 took the view that this consideration should be subject to VAT; on 21st November 2014, Respondent No. 4 issued a notice to this effect.[40] Subway received several notices asking it to show cause why the consideration it received should not be assessed to sales tax, and why no penalty should be imposed on the whole time director and the executive of the agency that maintained Subway's books of accounts.[41] The cumulative penalty for the period between 2006 and 2009 amounted to approximately Rs. 5.3 crores. The interest under Section 30(1) of the MVAT Act for same period amounted to approximately Rs.19 lakhs. There was much correspondence exchanged between Subway and Respondent No.4. Each side cited judgments. On 26th March 2015, Subway wrote to the 4th Respondent requesting it not assess tax till a

**39**. Subway Petition, Exhibit "A", *pp.* 30–49.
**40**. Subway Petition, Exhibit "D", *pp.* 59–70.
**41**. Subway Petition, Exhibit "G", *pp.* 92–98; Exhibit "H", *p.* 99.

decision was arrived at in the present writ proceedings, which it had by then already filed.[42] Respondent No. 4 did not accept this request but passed an *ex parte* assessment order, including interest and penalties Rs.17,98,988/-[43] in view of the decision of this Court in *Tata Sons Limited v State of Maharashtra*.[44] On 31st March 2015, the 4th Respondent issued a Notice of Demand in this amount.[45]

## VI. SUBMISSIONS AND FINDINGS IN SUBWAY

**57.** Mr. Shroff's argument on behalf of Subway is that the franchise agreement is not one for sale or transfer of right to use but merely permits the franchisee to display certain marks and to use certain technologies and methods in preparing the salads and sandwiches for sale. Therefore, he submits, it is liable to be taxed as a service, which Subway has been paying in any case. He adopts virtually all of Mr. Venkatraman's arguments. Mr. Shroff also refers to the cases of *Tata Sons*. He relies on these cases to urge that in Subway's case, all that is granted is a permissive use. The franchisee under the agreement obtains a mere permission to display the name 'Subway' in a particular fashion, along with other services.

**58.** Mr. Shroff formulates his case on several distinct grounds. First, the franchisee is entitled to display the name 'Subway' only for a limited period of time as stipulated in the agreement. After the

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**42**. Subway Petition, Exhibit "I", *pp.* 100–102; Exhibit "J", *pp.* 103–107.
**43**. Subway Petition, Exhibit "L", *p.* 109–118.
**44**. 2012 SCC OnLine Bom 697.
**45**. Subway Petition, Exhibit "M", *p.* 119.

expiry of this period of time, as provided in Clauses 8 and 8(g) of the Franchise Agreement, Mr. Shroff submits, and we agree with him, all the rights of the franchisee are terminated. A breach of the agreement also results in potential termination at the option of Subway. Second, Mr. Shroff argues that the franchisee cannot sub-franchise the mere permission it obtains under the agreement on account of the prohibition in Clause 9(a) of the agreement. Third, there is no territorial restriction or competition restriction of any kind placed on Subway. It is entitled to enter into as many or as few franchisee agreements as it wants, even simultaneously, and it can on its own directly compete with its franchisees too.

**59.** Mr. Shroff submits that in light of the decisions of the Supreme Court on various composite contracts, Article 366(29A) was amended in 1983 to introduce a legal fiction by which six instances of transactions, enlisted as the clauses of the Article, were to be considered as deemed sales. The Amendment allows certain specific composite contracts to be divisible; those in which the sale component could be isolated and separately taxed — for instance works contracts,[46] hire-purchase contracts[47] and catering contracts.[48] Works contracts and catering contracts can be split under sub-clauses (b) and (f) of clause (29A) of Article 366. Besides these, no other composite contracts can be split under Article 366(29A) itself. The State would not have any power to separate the agreement to sell from the agreement to render service and therefore would not be permitted to impose a tax on the sale component. This, Mr.

**46**. Article 366(29A) (b).
**47**. Article 366(29A) (c).
**48**. Article 366(29A)(d).

Shroff submits, is of course subject to the exception that the transaction does not represent two distinct contracts. He contends that Subway's agreement comes within the ambit of sub-clause (d) and therefore cannot be split in light of the Constitutional provisions. Here, the transaction does not involve two distinct agreements. There is no intention of separate agreements and the sale is not distinctly discernible. Mr. Shroff says that even if this were true of Subway's agreement, though it is not, the State would not have the power to encroach upon the Union's List and levy a sales tax on the service component as well.

**60.** In furtherance of his argument, Mr. Shroff relies on the decision in *Asian Oilfield Services v State of Tripura*[49] and *BSNL*.[50] He also cites the decision of the Supreme Court in *Imagic Creative*,[51] which follows *BSNL*. The thrust of these decisions is that it is not permissible for the State to tax composite contracts comprising of both sale and service components. The contracts cannot be artificially split to enable the sale element to be taxed, and neither can the whole agreement be taxed as a sale. The State in doing this would be entrenching on the legislative power of the Union.

**61.** Mr. Shroff, in the alternative and without prejudice to the preceding argument, submits that even if the transaction does amount to a transfer of right to use, the *situs* of such sales tax payable, if any, would be in Delhi and not Maharashtra. Subway is

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**49**. 2015 SCC OnLine Tri 483.

**50**. *Supra*.

**51**. *Supra*.

located in Delhi and has no place of business in Mumbai. Merely because its franchisees are in Mumbai, the *situs* cannot be said to be in Maharashtra. Subway is operating its business in Delhi, with no office at all in Mumbai. The franchise agreements are all signed in Delhi. Mr. Shroff contends that given the nature of the intangible goods, there is no physical transfer at all. The limited license, he says, is embodied in an agreement from Subway to its franchisees in Delhi. Therefore, Mr. Shroff contends, to determine the *situs*, the movement of goods, location of the goods, the place where the license is made available, and the place where such agreement is executed will be considered as the key factors. He submits that in this case, that place is Delhi. Therefore, even if the transaction were considered to be a sale, the State of Mahrashtra would have no right to impose a levy of sales tax. It would be the authorities in Delhi who would be entitled to levy sales tax.

**62.** For the most part, Mr. Sonpal adopts his arguments in Monsanto for this Writ as well. But, he argues, there is a vital difference between the two. He urges that "franchises" and "trade marks", are expressly covered under the MVAT Act since 2005. The Government of Maharashtra, under the powers conferred by Entry 39 of Schedule C of the MVAT Act, issued a Notification (No. VAT-1505/CR-114/Taxation-1), dated 1st June 2005, in which trade marks and franchises were included as "goods" for the purpose of Entry 39. In light of this express provision of law, Mr. Sonpal submits that Subway's franchise agreements are liable to be assessed to VAT. The Notification reads:

| Serial No. (1) | Name of the goods of intangible or incorporeal nature (2) |
|---|---|
| 1 | Patents |
| 2 | Trade marks |
| 3 | Import licenses including exim scrips, special import licenses and duty free advance licenses. |
| 4 | Export Permit or license or quota |
| 5 | Software packages |
| 6 | Credit of Duty Entitlement Pass Book |
| 7 | Technical know-how |
| 8 | Goodwill |
| 9 | Copyright |
| 10 | Designs registered under the Designs Act, 1911. |
| 11 | SIM cards used in Mobile Phones. |
| **12** | **Franchise, that is to say, an agreement by which the franchisee is granted representational right to sell or manufacture goods or to provide service or undertake any process identified or associated with the franchisor, whether or not a trade mark, service mark, trade name or logo or any symbol, as the case maybe, is involved.** |

(*Emphasis added*)

**63.** Mr. Sonpal relies on the decision of the Supreme Court in *Vikas Sales Corporation v Commissioner of Commercial Taxes*[52] and *Tata Consultancy Services v State of Andhra Pradesh*[53] in support of his argument that incorporeal rights can also be considered as goods for the purpose of sales tax. Therefore, he says, that purely because

**52**. (1996) 102 STC 106.
**53**. (2004) 24 PHT 581.

the agreement involves incorporeal rights, it cannot be exempted from sales tax. He refutes Mr. Shroff's argument on exclusivity and says that it is irrelevant that Subway can enter into multiple such agreements by giving franchises to multiple users. There is no such exception carved out in law, especially when the subject is a bundle of rights.

**64.** With regard to *situs*, Mr. Sonpal argues that merely because the agreements are executed in Delhi, the State of Mahrashtra would not be precluded from imposing VAT. Being an incorporeal right and not a tangible one, it exists at the place where it is being used. Therefore, he urges, despite the execution being Delhi, the use is in Maharashtra and this entitles the State of Maharashtra to levy VAT on the transaction.

**65.** Mr. Sonpal submits that the State cannot decide the eligibility of service tax of a transaction, but it can determine whether the transaction has to be taxed under the MVAT Act. This is, he urges, within its powers. The whole amount of the agreement can be liable to both sales and service tax as provided by Article 366 (29A) read with Item 54 of List II.

**66.** Mr. Sonpal's reliance on *Vikas Sales* and *Tata Consultancy* is of no avail to him. The fact that incorporeal rights are also considered to be "goods" is an undisputed proposition of law. These decisions do not assist him in showing that Subway's franchise agreement involves a transfer of right to use. This is what he needs to show. This he is unable to do.

**67.** We cannot accept Mr. Sonpal's argument that the eligibility of VAT is to be determined by the State, and therefore it could levy a sales tax on a transaction which already attracts service tax. The decisions in *BSNL*, *Imagic Creative*, and *Associated Lease Finance* are exactly on this; service and sales tax are mutually exclusive of each other.

**68.** We have the greatest difficulty in accepting Mr. Sonpal's argument that Article 366(29A) allows a split of even a single composite agreement, where this is not the intention of the parties to the agreement. In our opinion, Mr. Shroff's reliance on the cases of *Asian Oilfield* and *BSNL* in support of his argument that Subway's transaction cannot be split into two distinct or severable components is correct. The State cannot tax the entire transaction as a sale either. This is well-settled law, and if a State was to be permitted to tax the whole transaction, it would amount to nothing less than entrenching upon the powers exclusively available to the Centre under the Union List. As has been repeatedly held by this Court, this just cannot be done.

**69.** We believe that Mr. Shroff is correct when he says that the agreement between Subway and its franchisees is not a sale, but is in fact a bare permission to use. It is, therefore, subject only to service tax. In our opinion, the fact that the agreement between Subway and its franchisee is limited to the precise period of time stipulated in the agreement is vital to Subway's case. At the end of the period of the agreement, or before in case there was any breach of its terms, the right of the franchisee to display the mark 'Subway' and its trade dress, and all other permissions would also end. This is what sets this agreement apart from the case of Monsanto and its sub-licensee. There, the seed companies could do as they pleased with the seeds; they could alienate or even destroy them. In Subway's case, there are set terms provided by the agreement which have to be followed. A breach of these would result in termination of the agreement. We believe that there is no passage of any kind of control or exclusivity to the franchisees. In fact, this agreement is a classic example of permissive use. It can be nothing else. For all the reasons in law and fact that the sub-licensing of technology in Monsanto is held to be a transfer of right to use, this franchising agreement must be held to be permissive use.

**70.** We do not mean to suggest that every franchise agreement will necessarily fall outside the purview of the amended MVAT Act. There is conceivably a class of franchise agreements that would have all the incidents of a 'sale' or a 'deemed sale' (i.e., a transfer of the right to use). Black's Law Dictionary defines a franchise, in the context of a commercial transaction as:[54]

> The sole right granted by the owner of a trade mark or a trade name to engage in business or to sell a good or service in a certain area.

**71.** Chambers' Dictionary[55] too describes it as a

> a commercial concession by which a retailer is granted by a company the exclusive right of retailing its goods in a specified area ...

54. Black's Law Dictionary, 8th Ed.
55. Chambers' Dictionary, 1983 Ed.

**72.** We find, on facts, that the Subway franchise does not meet these tests. There is no such exclusivity. The agreement itself says that Subway may itself open and operate its own outlets in direct competition with the franchisee.[56] The agreements themselves expressly contemplate that Subway may create further franchisees in the very area in which these franchisees operate.[57] The franchisee cannot unilaterally sub-franchise;[58] if it could do without Subway's prior permission or leave, then the consideration might be wholly different and it may then be possible to say that there is a transfer of the right to use. We find that the right of transferrability is extremely restricted and is impossible without Subway control throughout. Similarly, if there is no requirement of having to cease display and use,[59] or return the intangible property at the end of the franchise agreement's term,[60] then the transaction might arguably be a sale. Exercises in co-branding or sub-branding, where one party franchises its mark on a territorially-restricted basis and allows the franchisee to combine it with its own or other marks may also well have an element of sale. Similarly, where a dealership for, say, automobiles, has a territorial exclusivity, then it may amount to a franchise. The Subway franchise model has none of these elements. The so-called 'system' is controlled by Subway and it is exclusive to Subway. At the end of the franchise term, it cannot be used. Some (though not all) of the ingredients — breads, salad dressings and other 'key' items — are to be sourced from Subway or Subway-

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**56**. Subway Petition, Clause 11(l) of the Agreement, *p.* 46.

**57**. Subway Petition, Clause 11(l) of the Agreement, *p.* 46.

**58**. Subway Petition, Clause 9 of the Agreement, *p.* 42.

**59**. Subway Petition, Clause 8(e) of the Agreement, *p.* 41.

**60**. Subway Petition, Clauses 8(e) and (j) of the Agreement, *p.* 41.

authorised vendors and nowhere else. This gives Subway deep and pervasive control and dominion over the franchisee's daily operations, without, at the same time, ceding to the franchisee the slightest hint or latitude in what it may do with the permitted marks and technology. This is, therefore, diametrically opposed to the Monsanto model, for Monsanto India has no control whatever in what its licensee does with the BT-infused donor seeds; that licensee may choose not to use them at all. There is also no question of any 'return' or 'cessation' to Monsanto India. Thus, viewed from any perspective, and on the facts of the case, we are unable to hold that the Subway franchise agreements have any of the necessary elements of a sale or a deemed sale.

**73.** We clarify that we limit ourselves to the franchise agreements in question and we express no opinion on any other form of franchise agreement or on any broader question of whether all franchise agreements falls outside the MVAT despite the amendment. We only say that this franchise agreement does not, on the facts of this case, constitute a sale to bring it within the purview of that Act. Equally, we reject any general proposition to the effect that anything that is nothing but a service can be artificially converted into or treated as a sale merely by the insertion of an omnibus clause in a state-level taxing statute. To accept this argument, we would have to accept that the State Legislature can encroach upon the legislative powers of the Union in respect of items in the Union List simply by inserting such amendments that would by some process of fiscal and legal alchemy convert a pure service into a sale. The introduction of the word 'franchise' in the amended MVAT by notification will have to be read to mean those franchises that can reasonably and plausibly be construed to have the effect of a sale; it cannot be widened to include agreements styled as 'franchise' agreements simply because of the nomenclature. Indeed, it seems to us clear that if we accept that a franchise agreement is, by definition, one that requires territorial exclusivity, then the Subway agreements are not franchise agreements at all, but purely licensing agreements.

**74.** In our opinion, the mere inclusion of 'franchises' under the MVAT Act would not automatically make all franchise agreements liable to sales tax. What must be looked at is the real nature of the transaction and the actual intention of the parties. The agreement must be considered holistically, and effect must be given to the contracting parties' intentions. The label or description of the document is irrelevant. An agreement styled as a franchise might, on a proper examination, turn out to be nothing more than a mere license (as in Subway's case). On the other hand, an agreement that calls itself a license might actually be a franchise. If, in a given case, a franchise agreement is effectively nothing more than a mere permissive use, it cannot be made liable to VAT. It would be a service, and hence liable to service tax. When interpreting a taxing statute, or for that matter any statute, full effect must be given to the words used by the Legislature. This, however, does not mean that this principle must be stretched to a point which leads to an absurd result, or one that was not contemplated by the Legislature. The Legislature is presumed to know the law and to have acted in accordance with it. We, therefore, do not think that the Legislature intended for this Notification to have such a sweeping effect as to bring all franchise agreements within the ambit of the MVAT Act.

Presumably, what the Legislature intended was to included only those franchise agreements that involved a transfer of the right to use or some other aspect of a deemed sale as defined under Article 366(29A) of the Constitution. As discussed above, we find that Subway's franchise agreement grants to the franchisee nothing more than mere permissive use of defined intangible rights. It is therefore a service, and is not amenable to VAT. We also hasten to clarify that we are not determining whether any particular kind of arrangement is or is not a franchise. Any examples we have given are merely illustrative, and not binding or final findings.

**75.** Once we arrive at this conclusion, then the argument on situs, which is really one of jurisdiction, is entirely irrelevant. If the franchise agreement is not liable to sales tax, then it is not liable to sales tax by any state agency anywhere, irrespective of location. Sales tax is under the purview of the State List, while service tax comes under the ambit of the Central List. Since this transaction is held to be a service, the service tax levied will be assessed and payable to the Central Government. Therefore, a detailed discussion of *situs* is unnecessary. In any event, had it fallen for decision, we would have been inclined to accept Mr. Shroff's submission that the *situs* for such agreements executed in Delhi would not be in Maharashtra, but in Delhi. While considering tangible assets, there is no doubt as to where their *situs* is. It is where the goods are physically located. But, an intangible asset does not have any physical form or existence in any physical location. The legislature could have, by some appropriate deeming fiction, expressly provided for the *situs* of an intangible asset. This it has not done, so far as intellectual property is concerned. It has, however, specifically so provided for shares.[61] Therefore, where the legislature thought it necessary to make express provisions for intangible assets, it has done so. In this legislative vacuum, the internationally accepted principle of *mobilia sequuntur personam* would apply, i.e., the *situs* of the owner of an intangible asset would be the closest approximation of the *situs* of his intangible asset. This is the principle widely used, unless there is a local legislation to the contrary; there is not. This is also the thrust of the Delhi High Court's decision in *Cub Pty Limited v Union of India & Others.*[62] Therefore, the *situs* of Subway's agreement, as Mr. Shroff rightly says, would be Delhi.

## VII. CONCLUSION

**76.** For the reasons set out above, Rule is discharged in Writ Petition 9175 of 2015, but with no order as to costs.

**77.** In Writ Petition 497 of 2015, Rule is made absolute in terms of prayer clauses (b) and (c). These are as follows:

> **"(b) for a declaration that the provisions of the MVAT Act are not applicable in respect of the franchisee given by the 1st Petitioner or in respect of the franchise fee or royalty received by it from the franchisees.**

**61**. Explanation 5, Section 9(1)(i) of the Income Tax Act, 1961.

**62**. Writ Petition(Civil) 6902 of 2008, judgment delivered on 25th July 2016.

> **(c) for a writ of certiorari or a writ in the nature of certiorari or any other writ direction or order under Article 226 of the Constitution of India, calling pertaining to the show cause Notices dated 21 November, 2014 and 20 March 2015 (Exhibits D, G and H hereto) as also the assessment order dated 30 March 2015 and the notice of demand dated 31 March 2015 (Exhibits L and M hereto) and after considering the same quashing and/or setting aside the same."**

**78.** Both petitions are disposed of in these terms. It only remains for us to thank appearing Counsel for their assistance and considerable industry in these matters.

**(S.C. DHARMADHIKARI, J.)**

**(G.S. PATEL, J.)**