JUDGMENT

As the issue involved in both these writ petitions is the same, they are taken up together for consideration and disposed by this common judgment.

2. The petitioner in W.P.(C).No.5348/2015 is an online service provider, registered as such under the Finance Act, 1994, as amended, governing the levy of Service Tax. In the writ petition, the petitioner is aggrieved by orders of penalty that have been passed against it by the authorities under the Kerala Value Added Tax Act [hereinafter referred to as the 'KVAT Act']. The said orders have been passed under Section 67 of the KVAT Act, *inter alia* on the finding that the petitioner has breached the provisions of Sections 20 and 40 of the KVAT Act in not getting itself registered as a dealer under the KVAT Act and further, not filing returns and maintaining true and correct accounts as mandated under the said Act.

3. The main contention of the petitioner in the writ petition is that it is a service provider who is not engaged in the business of sale or purchase of goods. It is pointed out that it merely facilitates transactions of sale and purchase through its online portal and, after an online customer identifies a product of his choice, the seller of the particular product is notified of the choice of the customer and he, in turn, raises an invoice on the customer and makes arrangements for the delivery of the product to the customer. Further, depending on the nature of the sale transaction, whether intra-state or inter-state, the seller of the product pays tax either under the local VAT Act or under the CST Act, and the fact of payment of tax is indicated in the invoice issued to the customer. The petitioner contends that it has absolutely no role to play in the transaction of sale and purchase and hence it could not have been proceeded against under the penal provisions of the KVAT Act. It is its further contention that even if the respondent authorities were of the view that it ought to have filed returns and paid tax under the Act, an opportunity ought to have been first afforded to it in terms of Section 22 of the KVAT Act before proceeding to issue a notice under Section 67 of the KVAT Act. Referring to the orders impugned in the writ petition, it is also contended that the findings therein, that the petitioner had effected sales within the State of

Kerala, was factually incorrect, and the transactions were, in fact, sales effected by WS Retail and other sellers, who were registered sellers on its web site. According to the petitioner, the said sales were all inter-state sales as the sale transactions occasioned a movement of the respective goods from outside the State to various locations within the State of Kerala.

4. As far as the petitioner in W.P.(C).No.6916/2015 is concerned, while the orders imposing penalty, impugned in its writ petition, proceed on similar lines as the orders impugned in W.P. (C).No.5348/2015, the only difference in the facts is that the petitioner herein is a person who actually engages in the business of sale and purchase through an online portal – myntra.com. The petitioner, however, maintains that during the relevant period, it was a registered dealer under the Karnataka Value Added Tax Act and was paying tax in respect of the local sales and inter-state sales effected from its business premises in the State of Karnataka. The orders of penalty, impugned in the writ petition, find that all the sales effected to its customers in Kerala are local sales and it is on the said premise that the petitioner has been proceeded against under the penal provisions of the KVAT Act and Rules.

5. I have heard Sri. Joseph Vellapally and Sri. Joseph Kodianthara, the learned Senior Counsel appearing for the petitioners in both the writ petitions and Sri Liju V Stephen, the learned Government Pleader appearing for the respondents in both the writ petitions.

6. On a consideration of the facts and circumstances of the case and the submissions made across the bar, I am of the view that the challenge in the writ petitions, against the impugned orders of penalty imposed on the petitioners, must necessarily succeed. It is relevant to note that the proposal for imposition of penalty in both the cases was premised on the contention that the petitioners had occasioned a breach of the provisions of Section 20 and Section 40 of the KVAT Act dealing with the filing of necessary returns and maintenance of true and correct accounts.

7. In the notices issued to the petitioners, proposing the imposition of a penalty, the stand of the respondents briefly stated is as follows:

- Through the action of a customer in Kerala choosing a product of his choice on the online portal of the petitioners herein, an agreement for sale came into existence whereby the petitioners agreed to sell the

product in question to the customer in Kerala for a consideration.

- The sale in question was a local sale insofar as the product was delivered to the customer in Kerala and from an online portal whose situs could be traced to Kerala. The contention of the petitioners that the sales in question were inter-state sales could not, therefore, be accepted.

- Even if the petitioner was not the seller of the product in question, the petitioner could nevertheless be held liable to tax in view of the provisions of Section 16 (13) of the KVAT Act, because the online portal could be seen as an intangible shop and the situs of the sale would be in Kerala where the agreement to sell was made.

- As the petitioners were liable to pay tax under the KVAT Act, and they had not complied with the provisions of Sub sections 20 and 40 of the KVAT by filing the necessary returns and maintaining true and correct accounts, they were liable to pay penalty quantified at twice the amount of tax that was payable.

8. It is relevant to note that, on receipt of the notice proposing penalty, the petitioner in W.P.(C).No.5348/2015 responded to the allegations raised therein by clarifying as follows:

- The petitioner had nothing to do, whatsoever, with the transactions of sale and purchase that took place over its online portal. The petitioner was not, therefore, a dealer for the purposes of the KVAT Act. When the customer in Kerala chose a product on its portal, the product was invoiced to the said customer by WS Retail, or some other seller that was registered on its portal, and the said seller subsequently raised an invoice on the customer and paid the applicable tax, under the CST Act, in the State where it had its place of business, and from where the movement of the goods originated for delivery to the customer in Kerala.

- Although there was a transaction of sale involved, the said sale was an inter-state sale effected by a seller located outside the State to a buyer located within the State of Kerala. The sale occasioned a movement of goods from outside the State to the customer within the State of Kerala and was therefore an inter-state sale on which tax was payable in the State where the movement of the goods originated.

- The online portal could not be seen as a premises within Kerala because the petitioner did not own any premises in Kerala where the sellers stored or stocked their products. The analogy that was sought to be drawn by the authorities with reference to Section 16 (13) was therefore wholly misplaced.

- As the petitioner is not a dealer for the purposes of the KVAT Act, there is no statutory obligation to file returns or maintain records or accounts and hence, the penal provisions under the Act could not have been invoked against the petitioner.

9. It is in the backdrop of the aforesaid stand adopted by the revenue authorities in the notices issued to the petitioner, and the explanation given in the reply submitted by the petitioner to the said notice, that I have to now consider the legality of the penalty orders that have been impugned in the writ petition. Before doing that, however, I must dwell a little on the notice that was issued to the petitioner in the instant case. A mere perusal of the said notice would indicate that rather than stating the reasons that prompted the revenue authorities to suspect an evasion of tax, and calling for the explanation of the assessee to those reasons, the notice proceeds to draw definite conclusions as regards the commission of an offence by the assessee. There is no indication in the notice as to why the revenue authorities considered the petitioner a dealer, or why the transactions in question had to be treated as local sales as against inter-state sales. The notice adopts the figure furnished by the petitioner, representing the total turnover in respect of sale transactions completed through its online portal to customers in

Kerala during the relevant period, as the total sales turnover of the petitioner for the purposes of quantifying the tax liability and penalty against the petitioner. The notice does not, however, spell out how the said figure could be taken as representing the sales turnover of the petitioner, or how the said sales could be seen as intra-state sales for the purposes of the KVAT Act. The tenor of the notices issued to the petitioner gives ample indication that the authority had, more or less, made up his mind to impose a penalty on the petitioner. It is by now well settled that show cause notices issued by statutory authorities, more so when they propose the imposition of penalty on an assessee, cannot pre-determine the guilt of an assessee. The notices issued cannot confront an assessee with definite conclusions as regards the commission of an offence by him as, otherwise, it would make a mockery of the process of quasi-judicial adjudication. In **Oryx Fisheries Private Limited v Union of India and Ors – [(2010) 13 SCC 427]**, the Supreme Court found that a show cause notice that was served on the appellant in that case was one that confronted him with definite conclusions of his alleged guilt and observed as follows:

> *"27. It is no doubt true that at the stage of show cause, the person proceeded against must be told the charges against him so that he can take his defence and prove his innocence. It is obvious that at that stage the authority issuing the charge-*

sheet, cannot, instead of telling him the charges, confront him with definite conclusions of his alleged guilt. If that is done, as has been done in this instant case, the entire proceeding initiated by the show-cause notice gets vitiated by unfairness and bias and the subsequent proceedings become an idle ceremony.

28. *Justice is rooted in confidence and justice is the goal of the quasi-judicial proceeding also. If the functioning of a quasi-judicial authority has to inspire confidence in the minds of those subjected to its jurisdiction, such authority must act with utmost fairness. Its fairness is obviously to be manifested by the language in which charges are couched and conveyed to the person proceeded against.*

29. .....
30. .....

31. *It is of course true that the show-cause notice cannot be read hypertechnically and it is well settled that it is to be read reasonably. But one thing is clear that while reading a show-cause notice the person who is subject to it must get an impression that he will get an effective opportunity to rebut the allegations contained in the show-cause notice and prove his innocence. If on a reasonable reading of a show-cause notice a person of ordinary prudence gets the feeling that his reply to the show-cause notice will be an empty ceremony and he will merely knock his head against the impenetrable wall of prejudged opinion, such a show-cause notice does not commence a fair procedure especially when it is issued in a quasi-judicial proceeding under a statutory regulation which promises to give the person proceeded against a reasonable opportunity of defence.*

> ***32.*** *Therefore, while issuing a show-cause notice, the authorities must take care to manifestly keep an open mind as they are to act fairly in adjudging the guilt or otherwise of the person proceeded against and specially when he has the power to take a punitive step against the person after giving him a show-cause notice.*
>
> ***33.*** *The principle that justice must not only be done but it must eminently appear to be done as well is equally applicable to quasi-judicial proceeding if such a proceeding has to inspire confidence in the mind of those who are subject to it."*

10. Turning now to the orders impugned in the writ petitions, I find that the said orders are more or less verbatim reproductions of the notices issued to the petitioner. While this would fortify my observations as regards the manner in which the notices themselves were issued, I find that in the impugned orders, the authority concerned does not enter a specific finding, supported by reasons, as to whether there was any sale effected by the petitioner at all. The impugned orders only find that there were transactions of sale that resulted in goods being delivered to customers in Kerala, but do not go further and find that it was the petitioner who effected those sales. Further, there is no consideration of the specific contention of the petitioner that the sales in question were

effected by sellers who were registered on its online portal, and that all the said sales were inter-state sales on which the respective sellers had paid applicable tax under the CST Act. A specific finding on the above issues, in my view, was necessary to clothe the authority concerned with the jurisdiction to proceed against the petitioner under the penal provisions of the KVAT Act, and the absence of a finding on these issues, denudes the authority concerned of such a jurisdiction. Although the learned Government Pleader sought to justify the orders impugned on various other grounds, I do not propose to deal with those grounds in this judgment since it is trite that the legality of the orders impugned can be sustained only on the reasons to be found in the said orders and not through reasons that are sought to be supplied later through a counter affidavit of the respondents in the writ petitions. **[See: Mohinder Singh Gill v. Chief Election Commissioner, New Delhi [(1978) 1 SCC 405]].**

As regards the finding in the impugned orders, that the situs of the virtual shop can be traced to Kerala on an analogy with the decision of the Karnataka High Court in **Antrix Corporation Limited v Assistant Commissioner of Commercial Taxes and Ors – [2011 (19) KTR 182 (Kar)]**, the said finding is legally

flawed because, it is well settled that the situs of a sale is wholly irrelevant to a determination of the issue of whether a sale is an inter-state sale or not **[See: Union of India v K.G.Khosla & Co. Ltd – [(1979) 2 SCC 242]; Oil India Limited v Superintendent of Taxes & Ors – [(1975) 1 SCC 733]; English Electric Company of India Ltd v DCT & Ors – [(1976) 4 SCC 460]]**. The most perplexing aspect of the instant case, however, is that WS Retail, the seller responsible for effecting majority of the sales to customers in Kerala, through the online portal of the petitioner, is registered as a dealer under the KVAT Act and, in the returns submitted by the said dealer for the relevant period, they had conceded NIL taxable turnover under the KVAT Act, on the contention that their entire sales turnover pertained to inter-state sales effected by them. Under the said circumstances and, in the absence of any material to suggest that the returns filed by the said seller were rejected by the revenue authorities, one fails to understand how the revenue authorities could proceed to levy tax, or impose penalty, on the petitioner in respect of the same turnover. The findings in the impugned orders reflect a patent non-application of mind by the authority concerned and also smack of arbitrariness. I therefore quash Exts.P11 and P12 orders, Exts.P13 and P14 Demand Notices as also Exts.P8 and P9 show cause

notices that are impugned in W.P.(C).No.5348/2015 and allow the said writ petition.

W.P.(C).No.6916/2015:

As regards W.P.(C).No.6916/2015, I find that the notices and orders issued to the petitioner in this writ petition are more or less identical to those in W.P.(C).No.5348/2015 discussed above. The only difference in the instant case is that the petitioner herein is a person who actually engages in the business of sale and purchase through an online portal – myntra.com. The petitioner, however, was a registered dealer under the Karnataka Value Added Tax Act during the relevant period, and was paying tax in respect of the local sales and inter-state sales effected from its business premises in the State of Karnataka. There is no material relied upon by the respondents to suggest that the petitioner had effected local sales in Kerala for which he was to register himself as a dealer under the KVAT Act and comply with the other provisions under the said Act that were applicable to dealers. Thus, for the same reasons as already spelt out in this judgment while dealing with W.P.(C). No.5348/2015, I allow W.P.(C).No.6916/2015 by quashing Exts.P11 and P13 orders, P12 and P14 Demand notices, as also Exts.P8 and

P9 show cause notices.

Before parting with these writ petitions and taking note of the growing tendency among Intelligence Officers under the KVAT Act to invoke penal proceedings against assessees without first having ascertained whether they would come under the coverage of the Act in respect of the activities carried on by them, it would be relevant to remind the authorities of the dictum laid down in a Division Bench judgment of this Court in **U.K.Monu Timbers (M/s.) v. State of Kerala [2012 (3) KHC 111],** wherein, it was observed as follows as paras 10 & 12:

> "10. In penalty proceedings the offences indicated under Section 67 should be evidenced by the materials recovered on inspection or otherwise and the enquiry is pointedly against any actual suppression or omission in the course of the business transactions, which would lead to the definite conclusion of evasion or attempt to evade. On detection of such offences; in the event of the tax evaded or sought to be evaded being determinable, the officer initiating penalty proceedings is perfectly justified in imposing penalty at the maximum rate or twice the rate of tax actually evaded or sought to be evaded. Such officer conducting penalty proceedings cannot exceed this jurisdiction by finding out as to whether the evasion detected would in fact lead to an inference of earlier or subsequent evasion. Nor can such inferences regarding the earlier or subsequent conduct be reflected in the penalty proceedings by way of estimation of turnover based on such inferences. This, going by the clear words of estimation of turnover based on such inferences. This, going by the clear words employed in the Statute, is within

the realm of the assessment proceedings.

> 12. Section 67 does not confer power to make a reasonable estimate. The suppression or omission must be clearly disclosed from the materials available and there should be evidence of the amounts sought to be suppressed from the turnover. In cases where the same is not discernible, the only option is to make an order of imposition of fine not exceeding Rs.10,000/-. Any suppression detected or rather any file generated on a crime so detected and penalised necessarily gives the assessing authority the power to make estimations to compensate the State against probable omissions and suppressions. Such exercise, as is mandated by the Statute, has to be regulated by the best judgment of the individual officer which definitely is subject to the principles of reasonableness, proportionality and of course natural justice. Such estimation on best judgment would definitely have to be done with due notice and after affording a personal hearing. Such estimation should be reasonable and should have a nexus with the gravity and frequency of the commission of offences as also the quantum of loss suffered by the state. This exercise, in our opinion, cannot be under taken by the officer empowered with me power to impose penalty under Section 67 of the Act. Section 67 contemplates imposition of penalty on proof of commission of offences as a measure of deterrence; best judgment assessments are made to compensate the loss caused to the State."

In cases such as the present where there is an uncertainty with regard to the real nature of the transaction in question, for instance, whether the transaction is an intra-state sale or an inter-state sale, the Intelligence Officers ought, ideally, to refer the matter to the assessing officers concerned to arrive at a finding

regarding liability to tax before taking recourse to the penal provisions of the Act. The assessing officers can then proceed sequentially as per the provisions of Sections 22 to 25 of the KVAT Act to determine the tax liability, if any, of the dealer concerned. Revenue authorities must realise that tax administration is not just about collecting revenue from citizens. They have to bear in mind the fundamental constitutional precept under Article 265 that no tax shall be levied or collected except by authority of law.

sd/-
A.K.JAYASANKARAN NAMBIAR
JUDGE

prp

WP(C).No. 5348 of 2015 (P)

APPENDIX

PETITIONER(S)' EXHIBITS :

EXT.P1: TRUE COPY OF THE SERVICE TAX REGISTRATION OF THE PETITIONER COMPANY DATED 07.01.2013.

EXT.P2: TRUE COPY OF THE TERMS OF USE OF THE ONLINE E-PLATFORM PROVIDED BY THE PETITIONER COMPANY.

EXT.P3: TRUE COPY OF THE AUDITED FINANCIALS OF THE PETITIONER COMPANY.

EXT.P4: TRUE SAMPLE COPIES OF CST SALE INVOICES RAISED BY THE SELLERS AND CORRESPONDING CST PAYMENT PROOF ON SUCH INVOICES.

EXT.P5: TRUE COPY OF THE NOTICE AND SUMMONS DATED 11.11.2013 ISSUED BY THE RESPONDENT NO.3.

EXT.P6: TRUE COPY OF THE LETTER DATED 02.12.2013 ISSUED BY THE RESPONDENT NO.3 TO THE 1ST PETITIONER.

EXT.P7: TRUE COPY OF THE 1ST PETITIONER'S LETTER DATED 23.12.2013.

EXT.P8: TRUE COPY OF THE SHOW CAUSE NOTICE DATED 04.11.2014 ISSUED BY THE RESPONDENT NO.2 FOR 2012-13.

EXT.P9: TRUE COPY OF THE SHOW CAUSE NOTICE DATED 04.11.2014 ISSUED BY THE RESPONDENT NO.2 FOR 2013-14.

EXT.P10: TRUE COPY OF THE 1ST PETITIONER'S LETTER DATED 25.11.2014.

EXT.P11: TRUE COPY OF THE IMPUGNED ORDER WITH CR NO.66/14-15 (2012-2013) DATED 31.12.2014 FOR THE PERIOD 2013-14 ISSUED BY THE 2ND RESPONDENT.

EXT.P12: TRUE COPY OF THE IMPUGNED ORDER WITH CR NO.67/14-15 (2013-2014) DATED 31.12.2014 FOR THE PERIOD 2013-14 ISSUED BY THE 2ND RESPONDENT.

EXT.P13: TRUE COPY OF THE NOTICE OF DEMAND OF RS.9,49,70,960/- FOR THE PERIOD 2012-13 ISSUED BY THE 2ND RESPONDENT.

EXT.P14: TRUE COPY OF THE NOTICE OF DEMAND OF RS.37,65,91,200/-FOR THE PERIOD 2013-14 ISSUED BY THE 2ND RESPONDENT.

EXT.P15: TRUE COPY OF THE PICTORIAL REPRESENTATION OF THE STEP-WISE TRANSACTION OF THE PETITIONER COMPANY.

WP(C).No. 5348 of 2015 (P)

EXT.P16: TRUE COPY OF THE PICTORIAL REPRESENTATION OF THE TRANSACTION STRUCTURE FOLLOWED BY THE PETITIONER COMPANY.

EXT.P17: TRUE COPY OF THE ADVERTISEMENTS IN TIMES OF INDIA.

RESPONDENT(S)' EXHIBITS :

NIL

//TRUE COPY//

P.S.TO JUDGE.

Msd.

TRUE COPY
Examiner