IN THE COURT OF APPEAL OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

In the matter of a Case Stated under Reference No. TAC/IT/022/2015 by the Tax Appeals Commission under Section 170 of the Inland Revenue Act No. 10 of 2006 as amended.

Unimo Enterprises Limited
No. 100, Hyde Park Corner, Colombo 02.

Appellant

Case No. CA(TAX) 15/2018
TAC No. TAC/IT/022/2015

Vs.

The Commissioner General of Inland Revenue
Department of Inland Revenue,
Sir Chittampalam A. Gardiner Mawatha,
Colombo 02.

Respondent

Before: Janak De Silva J.

N. Bandula Karunarathna J.

Counsel:

F.N. Gunawardena for the Appellant

Nayomi Kahawita SSC for the Respondent

Argued On: 29.05.2019

Written Submissions tendered on:

Appellant on 02.05.2019

Respondent on 27.05.2019 and 21.08.2019

Decided on: 29.05.2020

Janak De Silva J.

The Appellant is a limited liability company incorporated in terms the provisions of the Companies Act No. 17 of 1982. The principal activity of the Appellant is importation and selling of vehicles, tractors and other agricultural equipment.

The Appellant submitted the return of income for the year of assessment 2009/2010 on 29.11.2010. The Assessor rejected the return as the Appellant had not made adjustments in respect of Nation Building Tax (NBT) paid on imports in ascertaining the profit and income for the year and issued an assessment.

The Appellant appealed to the Respondent against the assessment issued by the Assessor who confirmed it. Then the Appellant appealed to the Tax Appeals Commission (TAC) which was dismissed.

In this Case Stated the following questions of law have been referred by the TAC to this Court:

(1) Was the assessment for the year of assessment 2009/2010 dated 30.11.2012 issued against the Appellant time barred in terms of Section 163(5)(a) of the Inland Revenue Act No. 10 of 2006 as amended (IRA) as applicable to such year of assessment?

(2) In terms of the IRA read together with the provision of the Extraordinary Gazette No. 1606/31 dated 19th June 2009,

   a. Is the Nation Building Tax (NBT) paid at the time of importation of goods a "prescribed tax or levy" for the purpose of Section 26(1)(l)(iii) of the IRA or

   b. Is the NBT which is expensed in the financial statements of any accounting principles a "prescribed tax or levy" for the purposes of Section 26(1)(l)(iii) of the IRA for a different year of assessment?

Question 1

The Appellant filed its income tax return for the year of assessment 2009/2010 on 29.11.2010. The Inland Revenue Department issued an assessment on the Appellant for the relevant year on 30.11.2012. There is no dispute between the parties on this position.

The dispute is whether the assessment was made within the time period specified in section 163(5) (a) of the IRA which prohibits the making of an assessment after the specified period.

The original position was that no assessment can be made after the expiry of 18 months from the end of the year of assessment. This was amended in 2009 by Act No. 19 of 2009 by which no assessment can be made after the expiry of two years from the end of the year of assessment.

This was the legal position when the Appellant filed its return on 29.11.2010. If there was no change in the legal regime no assessment could have been made after 31.03.2012 provided the tax return was filed on time which was done. However, the assessment in this case was made on 30.11.2012.

The Appellant submits that the assessment is time barred as it had a vested right to have got the assessment made on or before 31.03.2012. However, the Respondent submits that in view of the amendment made to section 163(5) (a) of the IRA by Act No. 41 of 2011, the assessment in this case was validly made.

A vested right is a certain or assured right contrasted with a contingent right which is conditional on the happening of an event. When the word 'vested' is used in this sense, Austin (Jurisprudence vol. 2, lect. 53) points out that in reality a right of one class is not being distinguished from a right of another class but that a right is being distinguished from a chance or possibility of a right, but it is convenient to use the well-known expressions vested right and conditional or contingent right.

In *Mohammed Bhoy et al. v. Lebbe Maricar* (15 N. L. R. 466) it was held that the interests of a fideicommissaries cannot be sold in execution during the lifetime of the fiduciaries as it is a contingent interest within the meaning of section 216 (k) of the Civil Procedure Code where such an interest was created by will and contained the condition that, on the death of the fiduciaries, the property should pass to the fideicommissaries. The interest of the fideicommissaries, in this case, was "expectant on his surviving his father".

In *Silva v. Silva* (29 N. L. R. 373) a deed of gift created a fideicommissum in which the fideicommissary succeeded to the property after the death of the fiduciary. It was held that the former acquired "an assured and certain interest" which was liable to be seized and sold under section 218 (k) of the Civil Procedure Code.

When the amendment was made in 2011, the time period for the making of assessment had not lapsed. This amendment extended the time for making of an assessment to the thirtieth day of November of the immediately succeeding year of assessment. In the light of these facts I reject the submission that the Appellant had a vested right to have got the assessment made on or before 31.03.2012.

The time bar in section 163(5) (a) of the IRA is procedural. In *A.G. v. Vernazza* [(1960) 3 All.E.R. 97 at 100] it was held that if the new Act effects matter of procedure only, then prima facie, it applies to all actions, pending as well as future. This was reiterated in *Blyth v. Blyth* [(1966) 1 All.E.R. 524 at 535] where Lord Denning held that the rule that an Act of Parliament is not to be given retrospective effect does not apply to statutes which only alters the form of procedure.
A similar issue arose in *Seylan Bank PLC. v. The Commissioner General of Inland Revenue* [CA(Tax) 23/2013, C.A.M. 23.05.2015]. In that case this Court held that irrespective of whether the assessee had to submit the tax return on or before the 30th September or 30th November 2009, the assessor can send the assessment to the assessee within two years immediately succeeding that year of assessment. The Court further considered the amendments made to section 163 of the Act by Act Nos. 22 of 2011, 18 of 2013 and 8 of 2014. The Court also held that section 163(5) of the IRA is a procedural law and that even if the amendment has retrospective effect, it applies.

Accordingly, I hold that the assessment for the year of assessment 2009/2010 dated 30.11.2012 issued against the Appellant is not time barred in terms of section 163(5) (a) of the IRA.

Question 2

The main issue here is whether NBT paid at the point of importation falls under "prescribed levy" for the purpose of section 26(1)(l)(iii) of the IRA.
Section 25 of the IRA states that there shall be deducted for the purpose of ascertaining the profits and income of any person from any source, all outgoings and expenses incurred by such person in the production thereof. Section 26 of the IRA provides for certain specific items which are not prohibited deductions.
NBT is not specifically identified in section 26 of the IRA as a non-deductible. In the absence of any other provision, the Appellant is then entitled to deduct the NBT paid by it at the time of importation. However, section 26(1)(l)(iii) of the IRAstates that for the purposes of ascertaining the profits or income of any person from any sources no deduction shall be allowed in respect of "any prescribed tax or levy".

The prohibition in section 26(1)(l)(iii) of the IRA in effect acts as an exemption when a person is not caught up within it as then the person can deduct all the expenses and outgoings of his business before calculating the taxable income. Exemption notifications must be interpreted strictly and, in its entirety, and not in parts [*Grasim Industries Ltd. & Anvor v. State of Madhya*

Pradesh & Anvor and Gwalior Sugar Co. Ltd. v. Madhya Pradesh Electricity Board &Ors (1999) 8 SCC 547].

In *Zebra Technologies Corporation v. Judy Baar Topinka, as Treasurer of the State of Illinois, and The Department of Revenue* [799 N.E.2d 725 (2003), 344 Ill. App.3d 474, 278 Ill.Dec. 860] the Appellate Court of Illinois, First District, First Division held:

> "We are mindful that taxation is the rule and tax exemption is the exception. *Chicago Bar Ass'n v. Department of Revenue*, 163 Ill.2d 290, 301, 206 Ill.Dec. 113, 644 N.E.2d 1166 (1994). Here, taxpayer is claiming an exemption from tax on income that would otherwise be assessed but for the 80/20 rule. Thus, taxpayer has the burden of proving clearly that it comes within the statutory exemption. *United Air Lines, Inc. v. Johnson*, 84 Ill.2d 446, 455-56, 50 Ill.Dec. 631, 419 N.E.2d 899 (1981). Such exemptions are to be strictly construed, and doubts concerning the applicability of the exemptions will be resolved in favor of taxation. *United Air Lines*, 84 Ill.2d at 455, 50 Ill.Dec. 631, 419 N.E.2d 899."

Regulations made by the Minister under section 212 of the IRAread with section 26 therein and published in Gazette Notification No. 1606/31 dated 19.06.2009 (Regulation) reads:

> *"Two thirds of the Nation Building Tax charged by the Nation Building Tax Act, No. 9 of 2009 payable for the period commencing on May 1, 2009 and ending on June 30, 2009, and for every quarter commencing on or after July 1, 2009, shall for the purposes of sub-paragraph (iii) of paragraph (l) of sub-section (1) of section 26 of the Inland Revenue Act No. 10 of 2006 be a prescribed levy".*

Hence, a portion of the NBT has been made a prescribed levy for the purposes of section 26(1)(l)(iii) of the IRA. However, the Appellant contends that it has been made a prescribed levy only for the persons who pay NBT quarterly whereas the Appellant pays NBT at the point of importation on each article and therefore is not caught within the prohibition.

The Respondent on the other hand submits that the prohibition on deduction in terms of section 26(1)(l)(iii) of the IRAcovers all three persons referred to in section 2 of the IRAincluding the Appellant and therefore the Appellant is not entitled to deduct the NBT paid by it on its imports.

In order to have a better understanding of the competing positions, it is important to examine certain other provisions of the NBT Act. Section 3(1) of the NBT Act reads:

> "3. (1) A tax to be called the "Nation Building Tax" (hereinafter referred to as "the Tax") shall, subject to the provisions of this Act, be charged from every person to whom this Act applies calculated at the appropriate rate specified in the Second Schedule to this Act, in the following manner: -
>
> (i) in the case of a person referred to in paragraph (a) of subsection (1) of section 2, who imports any article into Sri Lanka on or after January 1, 2009 the tax shall be chargeable in respect of the liable turnover of such person arising from the importation into Sri Lanka of such article; and
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> (ii) in the case of a person referred to in paragraph (b) (c) or (d) of subsection (1) of section 2, for every quarter commencing on or after January1, 2009 (hereinafter referred to as "relevant quarter", the tax shall be chargeable in respect of the liable turnover of such person for such relevant quarter."

Section 3(1) of the NBT Act deals with two separate and distinct incidents of the taxing regime. The first part is the charging section by which NBT is charged on every person to whom the Act applies, namely the persons referred to in section 2 of the NBT Act. The second part deals with the calculation of the NBT. Accordingly, NBT is calculated at the appropriate rate specified in the Second Schedule thereto in the case of importersof any article on the liable turnover of such person arising from the importation into Sri Lanka of such article and in the case of a person referred to in paragraph (b) (c) or (d) of subsection (1) of section 2, the NBTis calculated on the liable turnover of such person for such relevant quarter.

The Appellant has based its argument on the reference to "quarter" in the Regulation and submits that as an importer it does not pay NBT quarterly but only in respect of the liable turnover of such person arising from the importation into Sri Lanka of such article and as such the NBT it pays on every import is not a "prescribed tax or levy".

I am unable to accede to this submission. The Regulation covers both the charging section as well as the calculation part referred to above. That is why the Regulation reads "***Two thirds of the Nation Building Tax charged by the Nation Building Tax Act, No. 9 of 2009*** *payable for the period commencing on May 1, 2009 and ending on June 30, 2009, and for every quarter commencing on or after July 1, 2009...".* If one were to accept the submission of the Appellant it would amount to excluding part of the Regulation in its interpretation.

I arrived at a similar conclusion in *Lanka Ashok Leyland PLC v. Commissioner General of Inland Revenue* [CA (Tax) 14/2017; C.A.M. 14.12.2018] and the Supreme Court refused special leave to appeal in S.C.(SPL.) L.A. 42/2019; S.C.M. 21.01.2020.

In the alternative, the Appellant submits that the financial statements of the Appellant are prepared on an accrual's basis and not on a payment basis and accordingly, for income tax purposes as well this basis is considered to be acceptable. It was submitted that if the Appellant effects any imports and such imported items remain unsold at the end of the financial year, and are sold in subsequent financial year, the cost of such imports would get recorded as an expense only in the subsequent year. Accordingly, the Appellant contended that if the contention of the Respondent is accepted such add back would occur in the year in which the NBT was collected at customs point even though the financial statements itself for such year has not considered such NBT as part of the costs of the goods sold.

The purpose of accounting is usually to provide information to interested parties relevant to stewardship, control and decision-making. The requirements of a tax system can be quite different.

In *Thor Power Tools Company v. Commissioner of Internal Revenue* [58L Ed. 2d.785 at 802 (1979)] the US Supreme Court stated:

> "The primary goal of financial accounting is to provide useful information to management, shareholders, creditors, and others properly interested; the major responsibility of the accountant is to protect these parties from being misled. The primary goal of the income tax system, in contrast, is the equitable collection of revenue; the major responsibility of the Internal Revenue Service is to protect the public fisc. Consistently with its goals and responsibilities, financial accounting has as its foundation the principle of conservatism, with its corollary that 'possible errors in measurement [should] be in the direction of understatement rather than overstatement

of net income and net assets'. In view of the Treasury's markedly different goals and responsibilities, understatement of income is not destined to be its guiding light. Given this diversity, even contrariety of objectives, any presumptive equivalency between tax and financial accounting would be unacceptable".

In fact, the Supreme Court in *Rodrigo v. The Commissioner General of Inland Revenue* [(2002) 1 Sri.L.R. 384 at 387] held that to arrive at the taxable income, consideration should be given only to the permissible deductions provided by the Act and the Court cannot take into consideration any other means of computing the deductible amounts. In doing so, it quoted with approval the decision in *Sub Nigel Ltd., v. CIR* [(1948) 4 SA 580, 15 S.A.T.C. 381] where Centilivers C.J. held that the Court is not concerned with deductions which may be considered proper from an accountant's point of view or from the point of view of a prudent trader, but merely with the deductions which are permissible according to the language of the Act.

Accordingly, I reject the submission of the Appellant that any inconsistency between the financial accounting practices and taxing provisions must be avoided.

For the reasons aforesaid, Court answers the questions of law as follows:

(1) Was the assessment for the year of assessment 2009/2010 dated 30.11.2012 issued against the Appellant time barred in terms of Section 163(5)(a) of the Inland Revenue Act No. 10 of 2006 as amended (IRA) as applicable to such year of assessment? **No**

(2) In terms of the IRA read together with the provision of the Extraordinary Gazette No. 1606/31 dated 19th June 2009,

   a. Is the Nation Building Tax (NBT) paid at the time of importation of goods a "prescribed tax or levy" for the purpose of Section 26(1)(l)(iii) of the IRA? **Yes**
   b. Is the NBT which is expensed in the financial statements of any accounting principles a "prescribed tax or levy" for the purposes of Section 26(1)(l)(iii) of the IRA for a different year of assessment? **Yes**

For the reasons aforesaid, this Court confirms the Determination of the TAC.

The Registrar is directed to send a certified copy of this judgment to the TAC.

Judge of the Court of Appeal

N. Bandula Karunarathna J.

I agree.

Judge of the Court of Appeal