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

In the matter of an appeal on a question of law in terms of Economic Service Charge Act No. 13 of 2006 read together with the Inland Revenue Act No. 10 of 2006.

C.A. Case No. Tax 05/2010

Board of Review Case No. BRA/ESC-01

Senvec Lanka (Pvt) Limited,
No. 28, Ramakrishna Road,
Colombo 6.
APPELLANT

-Vs-

Commissioner General of Inland Revenue,
Department of Inland Revenue,
Sir Chittampalam A. Gardiner Mawatha,
Colombo 2. 22.11.2016 (For the Appellant)
RESPONDENT

BEFORE : **Vijith K. Malalgoda, P.C. J, (P/CA) &**
A.H.M.D. Nawaz, J.

COUNSEL : Nihal Fernando, PC with Johann Corera for the Appellant.
Anusha Samaranayake, DSG for the Respondent.

Argued on : 17.11.2014; 11.12.2014; 28.07.2016
Written Submissions on: 10.02.2015 and 24.11.2016 (For the Appellant)
09.02.2015 (For the Respondent)

Decided on : 07.04.2017

A.H.M.D. NAWAZ, J.

This appeal raises the question of whether the Appellant in the case-Senvec Lanka (Pvt) Ltd "imported" Colour Sorting Machines and is sold them to use domestic customers. This question assumes importance in the case as the imposition of taxes known as Economic Service Charge relates to an ascertainment of the issue whether the Appellant, if at all, passed any title of the Colour Sorting Machines to the local customers. As is apparent, the appeal relates to two assessments issued by the Commissioner General of Inland Revenue (the Respondent to the appeal) seeking to charge the aforesaid Economic Service Charge tax which was brought into operation by virtue of the provisions of the Finance Act No. 11 of 2004. The Appellant has preferred this appeal on the following questions of law:-

(1) Did the Board of Review fail to consider the provisions of the agency agreement between the Appellant and the principal particularly clauses 2(b), 2(d), 2(f), 3(a), 3(b) and 3(c) of the agreement?

(2) Did the Board of Review err in determining that the Appellant imported and sold Senvec Colour Sorting Machines in Sri Lanka?

(3) Has the Board of Review failed to consider the 'turnover' as stated in the audited accounts of the Appellant which were accepted for the purpose of income tax?

(4) Did the Board of Review and the Commissioner General of Inland Revenue err in determining that the Appellant failed to submit ESC returns for the year of assessment 2005/2006?

(5) Has the Board of Review and/or the Commissioner General of Inland Revenue failed to consider the Appellant's submission/explanation relating to the filing of erroneous VAT returns?

(6) Did the Board of Review and/or the Commissioner General of Inland Revenue fail to consider the definition of turnover applicable for the purposes of imposing ESC?

The Finance Act No. 11 of 2004 imposed an "Economic Service Charge" for the years of assessment

(i) 1st April 2004 to 31st March 2005, and

(ii) 1st April 2005 to 31st March 2006.

Subsequently in 2006 the legislature enacted a specific statute to provide for the imposition of tax known as 'the Economic Service Charge." The new Economic Service Charge (ESC) is imposed from 01.04.2006 by Economic Service Charge Act No. 13 of 2006, as amended by Economic Service Charge (Amendment) Act No. 15 of 2007. The ESC Amendment operates from 01.04.2007.

Be that as it may, it is the predecessor legislation namely Finance Act No. 11 of 2004 that would apply to the case at bar since the disputed assessments relate to the tax periods/years of assessment that are prior to the Economic Service Charge Act.

In the circumstances it is pertinent to briefly survey the provisions of the Finance Act No. 11 of 2004 that are engaged in the case.

Section 2 of the Finance Act No. 11 of 2004 authorises the imposition of a tax described as 'Economic Service Charge' (ESC) based on the '***liable turnover***' of every person or partnership. In Section 2(3) of the said Act, the expression '***liable turnover***' is defined to mean the 'turnover' of the *previous year of assessment.*

The cardinal portions of Section 2 of the Finance Act No. 11 of 2004 could now be looked at:

Section 2(1)

"An Economic Service Charge (hereinafter referred to as "the Service Charge") shall, subject to the provisions of this Act, be chargeable from every person and every partnership for each

year of assessment commencing on or after April, 1, 2004 (hereinafter in this Act referred to as "the relevant year of assessment") in respect of every part of the ***liable turnover*** *of such person or partnership for that relevant year of assessment, at the rate specified in the Schedule to this Act:*

Provided....."

Section 2(2)

"Notwithstanding the provisions of subsection (1), the Service Charge chargeable from any person or partnership for any relevant year of assessment shall be charged if and only if the liable turnover of such person or partnership for that relevant year of assessment exceeds rupees fifty million:

Provided that the Service Charge chargeable from any person or partnership for any relevant year of assessment shall in no case exceeds rupees fifty million."

Section 2(3)

*"****liable turnover****" in relation to any person or partnership and to any relevant year of assessment* ***means****, the aggregate turnover of every trade, business, profession or vocation other than any trade, business, profession or vocation the commercial operations of which commenced, whether by such person or partnership or by any other person or partnership, on a date which falls within the period of thirty-six months immediately preceding the first day of that relevant year of assessment, carried on or exercised by such person or partnership as the case may be, in Sri Lanka whether directly or through an agent or more than one agent, being the turnover for the year of assessment* ***immediately preceding*** *that relevant year of assessment; and"*

Therefore it is crystal clear that under Section 2(1) of the Finance Act No. 11 of 2004, a person is entitled to be charged with ESC, if and only if, the "***liable turnover***" of the immediately preceding year of assessment, exceeds **Rs fifty million**.

The Appellant's Liable Turnover

The Appellant's 'liable turnover' for the two years of assessment which is material to this appeal is given in the Appellant's audited Statement of Account at page 57 of the brief. Accordingly for:

Year of Assessment 2004/2005

a) The Appellant's 'liable turnover' for the year of assessment 2004/2005 = turnover for the 2003/2004 (i.e. the immediately preceding year) = Rs. 22,714,856/- (approximately rupees thirty three million). (*see* page 57 of the appeal brief). Therefore it is seen that the liable turnover for the year of assessment 2004/2005 is less than rupees fifty million.

   So the Appellant contends that it is NOT liable to pay Service Charge for 2004/2005 in terms of Section 2(2) of the Finance Act No. 11 of 2004.

It is worthy of note at this stage that the Income Tax Assessment relating to the year 2003/2004 was cancelled and the Appellant's Audited Statement of Accounts was accepted by the Respondent. (*vide*: Annexure A1 – seen at the unnumbered page above page 193 of the brief). **Therefore the Appellant contends that the Respondent could not be heard to dispute the 'liable turnover' for the year 2004/2005.**

Year of Assessment 2005/2006

b) The Appellant's 'liable turnover' for the year of assessment 2005/2006 = turnover of the immediately preceding year (2004/2005) = Rs. 37,890.851.11/- (approximately rupees thirty seven million). (*see* page 57 of the appeal brief). Therefore the liable turnover is less than Rupees Fifty Million and the argument accordingly is that the Appellant is NOT liable to pay Service Charge for the year of assessment 2005/2006 in terms of Section 2(2) of the Finance Act No. 11 of 2004.

If liable turnover is accepted as "**X**" for the year of assessment 2004/2005, can it lie in the mouth of the Respondent to assert that it is "**Y**" for ESC purposes? **It is a**

question that needs to be answered in this appeal. In the first instance this Court observes that the Respondent's argument that "liable turnover" must be increased to "Y" which is other than "X"-the accepted figure for income tax purposes, would attract the trite saying of Lord Kenyon, that a man shall not be permitted to "blow hot and cold" with reference to the same transaction.[1] I would presently set out my reasons as to why liable turnover for ESC cannot be an increased "Y" when the turnover is "X" for income tax purposes.

But it is implied in the argument of the Respondent that the turnover of the Appellant exceeds Rs fifty million if one looks at the supplies declared in VAT Returns. It is the contention of the Appellant though that it would be wrong and illegal to issue ESC assessments based on Letters of Credit values reflected in VAT Returns. The fact that the letters of credit were opened by the Appellant Company on behalf of buyers for a Japanese seller does not make the Appellant the importer. This was the argument put forward by the Appellant. This will be gone into at a later stage.

The Appellant contends that the ESC Assessment should necessarily be based on the Audited Financial Accounts of the immediately preceding year and it cannot be linked to VAT Returns. In addition it has been contended that the Letter of Credit values were erroneously entered in the VAT returns even though they were not *de facto* suppliers of the machines.

The Respondent's document **R5** (at page 120 of the appeal brief) demonstrates that the Assessor has sought permission of the higher officers of the Department of Inland Revenue to "***estimate the ESC liability as per the supplies declared in the VAT Returns.***" According to the last paragraph of **R5**, the Assessor has sought instructions to estimate the Appellant's Service Charge liability based on VAT returns: ***"May I estimate the ESC liability as per the supplies declared in the VAT returns. Your instructions please"*** (Sic).

[1] See *Cave v Mills* 7 H & N where the maxim was applied.

It would appear that the Assessor has been instructed to issue the ESC Assessments based on the VAT Returns-this is evident from the Respondent's letter to the Appellant dated 30.05.2006 marked **R3** (at page 132 of the Appeal brief) which states: "*.....Therefore your liable turnover for ESC has been calculated, according the VAT Returns furnished for the above taxable period*".

In my view this goes contrary to reason. Why VAT returns should be looked at in order to issue ESC assessments is not borne out by cogent reasoning. If the VAT returns were erroneous in that they contained the LC values as supplies, the error or otherwise of this entry must have been considered having regard to the scheme of the Finance Act No. 11 of 2004. Does the Appellant have to incur additional liability because he has made a mistake? If there is evidence to show that VAT declarations are wrong, it should have been brought home to the Appellant. One cannot accept the VAT Return at face value merely because the Appellant has included the LC values as supplies in the VAT Returns. The question before the Respondent was whether there was in fact an error for VAT purposes. In fact I would sum up the crux of the issue thus. The Respondent accepted the income tax return showing a particular turnover. VAT Return showed another turnover. Both cannot be right for ESC purposes. What is then the Return that should be taken into account for purposes of ESC assessments?

The following reasoning is compelling enough to impel this Court to take the view that the Respondent acted outside the four corners of his powers to base ESC assessments on VAT Returns.

ESC Paid only to be set off from Relevant Income Tax

Section 3 of the Finance Act No. 11 of 2004 provides that the Service Charge paid by any person or partnership for any relevant year of assessment may be deducted from the relevant income tax payable for that relevant year of assessment. The balance (un-deducted) Service Charge, if any may be deducted from the next year of assessment.

Similarly, Section 11 of the Finance Act No. 11 of 2004 by reference provides that certain Chapters of the Inland Revenue Act specifically identified in Section 11 of the said Act, shall *mutatis mutandis* apply to matters under the Finance Act No. 11 of 2004. Therefore, the provisions of Section 3 and 11 of the Finance Act No. 11 of 2004 also demonstrate that the 'Service Charge' imposed under the Finance Act No. 11 of 2004 is, if at all, connected or linked to the Income Tax Act and not to the Value Added Tax Act.

In other words the closest approximation of turnover is between income tax and Economic Service Charge. There is no nexus or logical basis to use VAT returns to determine turnover for ESC assessments. Having accepted the turnover for income tax purposes, the Respondent cannot blow hot and cold. It does not lie in the mouth of the Respondent to contend that the turnover for ESC is something else. If set off is to be made from a common pool namely 'turnover' shown in the audited statement of accounts, it is logical that the turnover for ESC assessments must also flow from the said audited statement of accounts.

Therefore I am in agreement with the argument of the Appellant that the Respondent could not be heard to disregard or ignore the Appellant's 'turnover' for income tax purposes. The Appellant's 'turnover' shown in the audited statement of accounts for 2003/2004 was accepted by the Respondent. Upon accepting the Appellant's 'turnover' for 2003/2004, the Respondent cancelled the income tax assessment issued for 2003/2004. The turnover of 2003/2004 is the 'liable turnover' for 2004/2005 under the Finance Act No. 11 of 2004. In the circumstances, this Court takes the view that the Respondent cannot not maintain its Service Charge assessment for the year 2004/2005, since the turnover for 2003/2004 does not exceed Rs. 50 million.

Constitutional and Statutory Prohibition from Importing VAT Regime

As I stated before, the Respondent/Assessor seems to have transposed the provisions of the Value Added Tax Act when such a course of action is not specifically provided for by the Finance Act No. 11 of 2004. The Respondent's attempt to refer to the

erroneous VAT declarations to issue assessments under the Finance Act No. 11 of 2004 (when such a course of action is not specifically permitted under the Finance Act No. 11 of 2004) is an egregious error. The Appellant premised this argument by reference to Article 148 of the Constitution which encapsulates the principle that **no tax shall be imposed except under the authority of a law passed by Parliament**

Article 148 of the Constitution provides:

> *"Parliament shall have full power over public finance. No tax, rate or any other levy shall be imposed by any local authority or any other public authority, except by or under the authority of a law passed by Parliament or of any existing law."*

Accordingly, the collocation of the words *'except by or under the authority of a law passed by Parliament'* makes it clear that tax could only be charged to the extent permitted by a law passed by Parliament.

It is in pursuance of the above constitutional norm that Parliament has enacted a slew of fiscal legislation from time to time to authorize the imposition of taxes: for instance, income tax authorized to be imposed under and in terms of the provisions of the Inland Revenue Act No. 10 of 2006; Value Added Tax which is legalized and imposed under the Value Added Tax Act No. 14 of 2012; and Economic Service Charge which was initially introduced under the Finance Act No. 11 of 2004 and subsequently re-enacted under the Economic Service Charge Act of 2006. It is axiomatic that the law engaged in this case is found in the Finance Act No. 11 of 2004.

In view of the provision in Article 148 of the Constitution cited above, Section 2(1) of the Finance Act No. 11 of 2004 expressly states that:

> *"An Economic Service Charge (hereinafter referred to as "the Service Charge") shall, **subject to the provisions of this Act**, be chargeable from every person and every partnership for each year of assessment commencing on or after April, 1, 2004.....in respect of every part of the liable turnover of such person or partnership for that relevant year of assessment,...." (Emphasis added)*

Therefore, upon a careful reading of the provisions of Article 148 read together with Section 2(1) of the Finance Act No. 11 of 2004, it is abundantly clear that the tax described as the 'Economic Service Charge' can be charged or collected or claimed (for the years of assessment relevant to this case) only in terms of the Finance Act No. 11 of 2004. This argument of the Appellant has to be accepted because an argument which appeals to reason and logic cannot be gainsaid.

In the circumstances any attempt by the Respondent to claim, charge or collect Economic Service Charge relying on the provisions of any other Act, particularly the Value Added Tax Act, is misconceived in fact and in law. We incline ourselves to this argument.

It is a well-established rule that the subject is not to be taxed without clear words for that purpose. (*vide:* the case ***In Re Micklethwait***[2] cited in INCOME TAX IN SRI LANKA by E. GOONERATNE, 2nd ed., 2009-p.553)

It has been stated that the subject is not to be taxed unless the words of the statute unambiguously impose the tax on him -Lord Simond, in ***Russel v. Scott***[3] Similarly, it has been stated that a subject is only to be taxed on clear words, not on intendment or on the equity of the Act-Lord Wilberforce in ***W.T. Ramsay Ltd., v. CIR.***[4]

In the course of the argument, the learned President's Counsel for the Appellant cited the Supreme Court precedent of ***Vallibel Lanka (Pvt) Ltd., v. Director General of Customs and 3 others***[5] wherein K. Sripavan, J (as he then was) declared, *inert alia*:

a) In carrying out its task of enforcing the law, the Court has to insist on powers being exercised truly for the purpose indicated by the Parliament and not for any ulterior purpose;

b) **It is the established rule in the interpretation of statues that levy taxes and duties, not to extend the provisions of the statute by implication**, beyond

[2] 1885 11 EX 452
[3] 30 TC 375
[4] 54 TC 101
[5] (2008) BALR 47

the clear import of the language used or to enlarge their operation in order to embrace matters not specifically pointed out. **In case of doubt, the provisions are construed most strongly against the State and in favour of the citizen.** *(Emphasis added)*

Thus that the provisions of the Value Added Tax Act cannot be construed to impose the tax claimed in this case is patently clear. Particularly since the Constitution clearly lays down in Article 148 that a tax can only be imposed by or under the authority of a law passed by Parliament. The Value Added Tax Act No. 14 of 2002 only authorizes the collection of a tax described as Value Added Tax. It certainly does not authorize or permit the collection of any tax described as the 'Economic Service Charge'. Hence this Court endorses the view that the provisions of the Value Added Tax Act are irrelevant to this case.

Value Added Tax is collected based on 'taxable supply' (as opposed to 'turnover'), whereas Economic Service Charge under the Finance Act No. 11 of 2004 is charged based on 'turnover'-more specifically 'liable turnover' as defined in Section 2(3) of thee said Finance Act No. 11 of 2004. The word 'turnover' is not found anywhere in the Value Added Tax Act, whereas in contrast, the expression 'liable turnover' is defined in the Finance Act No. 11 of 2004 and the chargeability of Economic Service Charge is based on 'liable turnover' as defined in the Finance Act No. 11 of 2004.

In recognized accounting parlance the turnover of a company is shown in the audited Financial Accounts of the Company, more particularly in the profit and loss account. I have already alluded to the fact that the Audited Financial Accounts were submitted by the Appellant along with its Returns for Income Tax and the Audited Financial Statements were accepted by the Inland Revenue Department. (First relevant year of assessment 2003/2004 there was a charge which was withdrawn and second relevant year 2004/2005 the accounts were accepted without any assessment.) In the circumstances the 'turnover' shown in the said Audited Financial Statements are deemed to have been accepted for all purposes. As I said before, there cannot be one

turnover for Income Tax purposes and another 'turnover' for Economic Service Charge purposes.

The Value Added Tax Act does not 'authorize' the Respondent to charge or claim a tax described as the Economic Service Charge. Thus the Respondent's consistent attempt to justify the imposition of the 'Economic Service Charge' under the provisions of another Act of Parliament (namely the VAT Act) would amount to an infringement of the provisions of Article 148 of the Constitution. In the circumstances, this Court proceeds to reject the Respondent's submissions based on VAT Returns.

At the outset I pointed out that the pivotal question that falls to be decided is whether the Appellant acted as an importer in this case. In other words did the Appellant Company derive title from the Japanese seller and supply the Colour Sorting Machines to domestic consumers? Was there a supply from the Appellant Company to the end users in Sri Lanka? If the Appellant was not an importer, then he would have no title to pass and there would be no supply *qua* owner. It is crystal clear that in such a situation there would be no liable turnover though there was an entry of a turnover in the VAT Return. One has to look at the overall transactions that also involved letters of credit and determine this issue upon a perusal of all other accompanying documents.

I would now turn to this issue of whether or not the Appellant was an importer.

Is the Appellant an Importer of Color Sorting Machines?

Agency Agreement

The Agency agreement **(P2)** which is at pages 68-76 of the appeal brief is demonstrative of the functions carried on by the Appellant. It shows that the Appellant functioned as an Agent of Hattori Seisakusho Co. Ltd., Japan. The Appellant canvassed orders on behalf of the Principal for which the Principal agreed to "*remit to the Agent in Sri Lanka the mutually agreed Commission on the realization of the*

payment in Japan in respect of each machine and for any spare parts supplied directly to the Customer within the said territory". (*vide:* Paragraph 2(f) of the Agency Agreement marked **P2** at page 74 of the appeal brief)

Pro-forma Invoice

There is another document that demonstrates that the Color Sorting Machines were supplied directly to the Customer. The Document **P3A** identified as the "Pro-forma Invoice' issued by the Principal in Japan to Pussellawa Plantations Ltd., indicates that the contract of sale is between the Pussellawa Plantations Ltd., and the Japanese Exporter, Hattori Seisakusho Co. Ltd., Japan-vide the Pro-forma Invoice at page 67 of the appeal brief. In international trade a Pro-forma invoice is a preliminary bill of sale sent to buyers in advance of a shipment or delivery of goods. Typically, it gives a description of the purchased items and notes the cost along with other important information, such as shipping weight and transport charges. This document gives an indication as to the status of the Appellant. This document strengthens the position of the Appellant that he was not acting in any character otherwise than as an agent.

Opening of Letters of Credit

Another fact to be taken note of is the role played by the Appellant in opening letters of credit. Admittedly the Appellant was able to have letters of credit opened on nil margin and facilitate the import-(*vide:* **P4** at page 66 of the appeal brief). It bears emphasizing that the LC shows *ex facie* that the LC was applied for by the Appellant 'On Account' of the Customer, Pussellawa Plantations Ltd. Similarly the Invoice marked **P5** (at page 64 of the brief) and the Shipping documents marked **P6** and **P7** (at pages 63 and 65 of the brief) have also been issued in favour of the Appellant 'On Account' of the Customer. The acronym O/A represents 'On Account'. It has to be noted that in the opening of letters of credit the Appellant has held out the buyer by using the acronym "on account" and if the Appellant was importing the goods for sale, there was no necessity to use the notation O/A. Thus the Appellant has held himself

out only as an applicant to open the letter of credit and it is in no way an indication that the Appellant was the importer.

Invoice and Shipping Documents

If one looks at the invoice sent by the Japanese seller the goods are consigned to the Appellant but on account of Pussellawa Plantations Ltd., (*vide*: **P5** at page 64 of the brief). The Bill of Lading is, as is customary under an LC, is drawn to the order of the issuing bank-in this instance Hatton National Bank (HNB)-*vide* the Bill of Lading at page 63. But the ***notify party*** is designated as Senvec Lanka (Pvt) Ltd on account of Pussellawa Plantations Ltd. As does usually happen in import LC's, the issuing bank of the LC- Hatton National Bank would have indorsed the Bill of Lading and handed it over to the Appellant because it is the indorsement in favour of the Appellant that would have facilitated the clearance of goods from the customs. In fact it is only upon the debiting of the LC value from the Appellant's account at HNB that HNB would have indorsed and handed over the bill of lading to the Appellant.

Security Provided by the Bill of Lading

Does this indorsement of the bill of lading by the bank in favour of the Appellant pass title of the goods to the Appellant? Upon a careful scrutiny of the transactions that have taken place, I do not hold the view that the title to the goods passed to the Appellant upon the indorsement of the bill of lading in favor of the Appellant. It is undeniable that the Appellant has acted as a funding intermediary of the local customers in addition to its role as an agent of the Japanese exporter. It is quite clear that the local customers like the Pussellawa Plantations solicited the services of the Appellant in order to have the goods consigned to them from Japan under a documentary credit which was opened by the Appellant on a nil margin. The Agency agreement does not designate the Appellant as the buyer of Colour Sorting Machines from Japan. On the contrary the Appellant facilitated the cross border trade. The Appellant not only opened the LCs on behalf of the customers but also paid for the

goods by having their account debited. The LC value was dispatched to Japan through its funds.

Thus the Appellant advanced funds (a loan) to the end user like the Pussellawa Plantations. In order to secure this loan, the bank indorsed the bill of lading in favor of the Appellant and handed it over to the Appellant. In fact, though the Bill of Lading plays the role of a document of title to goods, in this instance it came into the hands of the indorsee-the Appellant as a security for its loan which it advanced to the domestic buyers of the Japanese seller. It is not unusual for a Bill of Lading to operate as a security for a loan.[6]

The Appellant as the Pledgee of the Goods in Exchange for the Loan

In fact a pledge of the goods is created in exchange for the funds advanced by the pledgee-the Appellant in this instance. A pledge is usually described as the transfer of the possession of goods by way of security whereby the ownership of the goods remains in the pledgor and the pledgee obtains a right to possession only. The pledgee has a 'special interest' in the goods, which includes a right to sell in the event the money advanced is not repaid. The goods must be transferred to the possession of the pledgee and actual possession is normally required. One of the exceptions to actual possession is the case where a bill of lading is transferred with the intention of pledging the goods to which the bill is title. Then the pledge is effective on the transfer of the bill alone.

The limited interest passed by the pledge of a bill of lading was considered by the House of Lords in ***James Sewell and Nephew v. James Burdick on behalf of himself and Others, The owners of the Steamship "ZOE"***,[7] in holding on the particular facts that bankers to whom bills of lading had been delivered as security for a loan

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[6] See: *The bill of lading for credit advances: deconstructing a misapplication of common law principles in Nigeria* by A. Olawoyin Adewale in (2003) 18 (2) *Journal of International Banking Law and Regulation* (J.I.B.L.R) at 61-68.

[7] (1884) 10 Appeal Cases 74 (House of Lords): see *Standard Chartered Bank v Dorchester LNG (2) Ltd* (2013) EWHC 808 (Comm) which makes a reference to *James Sewell v Burdick*.

were not liable for freight.[8] In the head note to the judgment which reflects substantially what has been decided the following passage occurs:

> *"The mere indorsement and delivery of a bill of lading by way of pledge for a loan does not pass "the property in the goods" to the indorsee, so as to transfer to him all liabilities in respect of the goods...."*[9]

The House of Lords declared so in the context of the position of a bank as a pledgee.

It is clear that in the classic situation where the bank receives bills of lading made out to the order of the shipper and blank indorsed it becomes a pledgee of them. Where the bills of lading are drawn to the order of the bank or are indorsed to the order of the bank, the bank will obtain a pledge in the same way as where the bills are drawn to order and blank indorsed. This is the case for an issuing bank as much as for the Appellant as we find it in the case. The bill of lading in the case is drawn to the order of the issuing bank Hatton National Bank but when the bank indorses it in blank and hands it over to the Appellant, by virtue of the advance provided to the buyer of the goods, a pledge is created in favor of the Appellant.

In such a situation the property in the goods would not pass to the Appellant but a security interest in the Appellant. The buyer is of course the end user like the Pussellawa Plantations and the rationale for such an interpretation merits recapitulation.

If the beneficiary in Japan has been paid through the funds of the Appellant, why should the Appellant be invested with title? His interest lies in obtaining reimbursement and the bill of lading signifies the pledge of the goods to the Appellant. When the documents are accepted by the Appellant, the property in the goods which has previously been retained by the seller has passed to the buyer and the Appellant looks to the promise of the buyer to reimburse him. The Appellant would hold the bill of lading as a security for the money it advanced. The bill of lading

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[8] *See* (1884) 10 Appeal Cases 74 at 92, 93 per Lord Blackburn.
[9] *See* Benjamin's Sale of Goods 9th Ed Chapter 18-Overseas Sales in General; Also Chapter 5-Passing of Property.

would constitute a symbolic possession of goods. Paull J. stated this proposition in the context of a bank in ***Sale Continuation Ltd v. Austin Taylor & Co Ltd***[10]

> *"The ownership of the goods passes to the buyer but the bank has the possessory title of a pledgee as against the buyer. He has that title until the buyer puts the bank in funds and discharges his liability....."*

In fact the local customer of the Japanese seller namely Pussellawa Plantations would have to liquidate the loan by reimbursing the Appellant and putting it in funds. If the pledgor doesn't do so the Appellant has the usual right of a pledgee to sell the goods in order to reimburse itself.

So much for the passage of title which never vested in the Appellant. We take this view upon a review of all the accompanying documents and transactions. If there was no title in the Appellant it follows that it never sold these goods to the local customers and there was no supply. If the Appellant is not the importer it cannot sell something to which it has no title.

The Respondent's argument is on the premise that the Appellant is an importer and the Respondent has sought to add the CIF value of the machines (extracted from the erroneous VAT declarations) to the Appellant's turnover. From the foregoing analysis of the transactions and the applicable law it is quite clear that there is no import on the part of the Appellant. The document **P4** at page 61 shows that the Appellant charges a commission from the customer for facilitating the opening of the Letter of Credit (items **'B'** and **'C'** in **P4**), Clearing Charges (*vide*: **'D'**, **'F'**, **'G'**, **'H'**, **'I'** and **'J'** in P4 at page 61 of the brief). The Appellant also charges the Customer for transportation and installation (*vide*: Items **'K'** and **'L'** in **P4**). Installation takes place at a cost to the customer as under Clause 2(f) of the Agency Agreement the Appellant is entitled to a commission.

[10] (1968) 2 QB 849 at 861.

The breakdown of the Appellant's Turnover as shown in the Audited Statement of Accounts for both year 2004/2005 and 2005/2006 shows that the 'Commission' received by the Appellant from the Japanese Principal is distinct from the other income of the Appellant. The detailed description the Appellant's Turnover for the year 2004/2005 is shown in **P10** at page 48 of the appeal brief. The 'Commission' received from Sale of Machinery is Rs.11,092,221/-. Similarly the 'Commission' relating to the year 2005/2006 is shown in **P11** at page 30 of the appeal brief. The 'Commission' received from Sale of Machinery is Rs.13,174,430.53. In the circumstances, the Appellant's documents **P4**, **P5**, **P6**, **P7**, **P10** and **P11** clearly demonstrate that the Appellant has not engaged in importing the Color Sorting Machines as alleged by the Respondent.

Liable Turnover in a Nutshell

The Appellant's Statement of Accounts for year 2003/2004 shows a turnover of Rs.33,714,856/- for the financial year 2003/2004. (*vide*: the year on year comparison at page 57 of the brief) The Appellant's Accounts for 2003/2004 were accepted by the Respondent and the Respondent by Notice marked Annex **A1** cancelled the income tax assessment relating to 2003/2004. The accepted turnover in 2003/2004 is the 'liable turnover' for 2004/2005. Since it is less than rupees fifty million, this Court concludes that the Appellant is not liable to pay Economic Service Charge for the year of assessment 2004/2005.

The total 'Turnover' for the year 2004/2005 is shown at Rs.37,890,851 (*vide*: page 48 of the brief). Since Section 2 of the Finance Act No. 11 of 2004 provides that the 'turnover' in the immediately preceding year is the 'liable turnover' for any year of assessment, turnover for 20045/2005 is the 'liable turnover' for calculation of Economic Service Charge in the next year of assessment, namely for 2005/2006. Since the 'liable turnover' for 2005/2006 is less than Rupees Fifty Million, the Appellant would not be liable to pay ESC for 2005/2006.

In the circumstances we proceed to answer the questions of law in favor of the Appellant and allow the appeal.

JUDGE OF THE COURT OF APPEAL

Vijith K. Malalgoda, P.C. J. (P/CA)

I agree

PRESIDENT OF THE COURT OF APPEAL