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

In the matter of a Case Stated under Reference No. TAC/VAT/014/2014 by the Tax Appeals Commission under Section 36 of the Value Added Tax Act No. 14 of 2002 as amended

Lalan Rubber (Pvt) Ltd.,

No. 95B, Zone A,

Biyagama, Malwana.

APPELLANT

Case No. CA/TAX/05/2017

Vs.

Tax Appeals Commission Case No.

TAC/VAT/014/2014

The Commissioner General of Inland Revenue,

Department of Inland Revenue,

Sir Chittampalam A. Gardiner Mawatha,

Colombo 02.

RESPONDENT

Before: Janak De Silva J.

Achala Wengappuli J.

Counsel:

F.N. Goonewardena for the Appellant

Sumathi Dharmawardena Senior D.S.G. for the Respondent

Written Submissions tendered on:

Appellant on 11.05.2018

Respondent on 11.05.2018

Argued on: 03.07.2018

Decided on: 04.09.2018

Janak De Silva J.

This is a Case Stated submitted for the opinion of this Court by the Tax Appeals Commission (TAC) under section 36 of the Value Added Tax Act No. 14 of 2002 as amended (VAT Act). Although neither party raised this issue, we note that the VAT Act was amended by the Tax Appeals Commission Act No. 23 of 2011 as amended (TAC Act) by the repeal of section 36 therein. Hence the TAC has made a reference to this Court under a repealed provision.

However, it is well-settled that an exercise of power will be referable to a jurisdiction which confers validity upon it and not to a jurisdiction under which it will be nugatory. This principle has been applied even to cases where a Statute which confers no power has been quoted as authority for a particular act, and there was in force another Statute which conferred that power. [*Pieris v. The Commissioner General of Inland Revenue* (65 N.L.R. 457), *Kumaratunga v. Samarasinghe, Additional Secretary, Ministry of Defence and Others* (1983) 2 Sri.L.R. 63]. Section 11A of the TAC Act enables the TAC to refer for the opinion of this Court a Case Stated. Accordingly, we are of the opinion there is a valid reference and make our determination accordingly.

The questions of law raised by the Appellant for consideration by Court are as follows:

1. Is the assessment for the taxable period ending 31st March 2009 invalid in terms of Section 33(1)(a) of the VAT Act as it has been dated 8 June 2012 and received by the Appellant on 24 July 2012 and is therefore time barred?
2. Has there been a "taxable supply of goods" by the Appellant in relation to rubber trees under the aforesaid agreements, in terms of the VAT Act?

3. Has the TAC erred in concluding that the agreements entered into by the Appellant with contractors titled "Agreement for Uprooting Old Rubber Trees and clearing the Land" were in fact contracts for the supply of rubber logs or timber?
4. Would the supply of Rubber trees in terms of the aforesaid agreements be an exempt supply in terms of the VAT Act by reasons of it being:
    a. "Unprocessed agricultural products produced in Sri Lanka" within the meaning of item (b) (xxiii) of Part II of the First Schedule of the VAT Act;

       or
    b. "Agricultural plants" in terms of item (a)(xi) of Part II of the First Schedule of the VAT Act?

The first question relates to a procedural issue while the other questions deals with substantive issues.

Time Bar

The appeal relates to two (2) monthly taxable periods of March 2009 and March 2010. The learned Counsel for the Appellant contends that the assessment for the taxable period ending 31st March 2009 is invalid in terms of Section 33(1)(a) of the VAT Act as it has been dated 8 June 2012 and received by the Appellant on 24 July 2012 and is therefore time barred.

There is no dispute that the Appellant is a registered person under the VAT Act. Section 21(1)(a) of the VAT Act requires every registered person to furnish a return not later than the 20th day of the month after the expiry of the taxable period. The Appellant filed his VAT return for the taxable period ending 31st March 2009 on 21st April 2009, which is one day later than the due date.

Section 33(1) of the VAT Act imposes a limitation of time for making an Assessment. It must be done within three years from the end of the taxable period. Hence the time bar period for the taxable period ending 31st March 2009 commences on 1st April 2012.

The learned Counsel for the Appellant submitted that "the Assessment has been issued a little over two months subsequent to the date on which the time bar commences" and that "the Assessment was received by the Appellant on 24th July 2012, which is almost three months over the date on which the time bar commences".

In addressing this submission, it is important to note the distinction between an "Assessment" and "Notice of Assessment".

Section 28(1) of the VAT Act as amended deals with the making of an Assessment and Notice of Assessment. Accordingly, Assessment is a departmental computation of the amount of VAT payable by a person for the relevant taxable period. Notice of Assessment is the formal intimation to the person of the fact that such an Assessment has been made.

The distinction between the "making of an Assessment" and "Notice of Assessment" has been clearly recognized in *Commissioner of Income Tax v. Chettinad Corporation Ltd.* (55 N.L.R. 553) which was quoted with approval by the present Supreme Court in *Ismail v. Commissioner of Inland Revenue* [(1981) 2 Sri.L.R. 78]. In the English case of *Honig and Others v. Sarsfiled* [(Tax Cases Vol. 30 page 337), (1986) BTC 205] Fox LJ drew a distinction in the making of an assessment and the notice of assessment and held them to be different, the assessment being in no way dependent upon the service of notice. He held that giving of the notice was independent of the making of a valid and effective assessment.

The learned Counsel for the Appellant contended that the facts in *Honigs* case (supra) is different to the instant case as there was evidence in that case which indicated that the assessment itself had been done prior to the expiry of the time bar period which is not there in the instant case. We are unable to accept this submission.

Section 29 of the VAT Act states that where the Assessor does not accept a return furnished by any person under section 21 for any taxable period and makes an assessment or an additional assessment on such person for such taxable period under section 28 or under section 31, as the case may be, the Assessor shall communicate to such person by registered letter sent through the post why he is not accepting the return. The letter dated 26.01.2012 sent by the Assessor informs the Appellant to treat the said letter as an intimation under section 29 of the VAT Act.

Accordingly, we are of the view that the letter dated 26.01.2012 can be treated as notice of making an Assessment and therefore the assessment for the taxable period ending 31st March 2009 has been made within the time stipulated in Section 33(1) of the VAT Act.

The letter dated 08.06.2012 and received by the Appellant on 24.07.2012 is only the Notice of Assessment. The VAT Act does not specify a time limit within which the Assessor is required to give Notice of Assessment to the person assessed.

In any event, we are of the view that the time bar in section 33(1) of the VAT Act does not apply to the instant case. Section 33(1) of the VAT Act is qualified by the words "**Where any registered person has furnished a return under sub section (1) of section 21** in respect of a taxable period or has been assessed for tax in respect of any period...". (emphasis added) This in our view demonstrates that **a registered person obtains the time bar protection in section 33(1) of the Act, only where he performs the duty** he has **of furnishing a return not later than the 20th day of the month after the expiry of the taxable period.**

In the instant case, the Appellant has furnished the return one day later on 21st April 2009. The learned Counsel for the Appellant submits that there has been a delay of just one day which amount to substantial compliance. He relies on the decision of the Supreme Court in *Wickremesinghe v. Commissioner of Income Tax* (48 N.L.R. 481).

We are unable to accede with this submission. In *Wickremasinghe's* case (supra) the Court was interpreting the words "at or before the time" in section 74(3) of the Income Tax Ordinance. In the instant case the words "not later than the twentieth day of the month after the expiry of each taxable period" in section 21(1)(a) of the VAT Act clearly does not, in our view, give any latitude as to the time before which the return must be filed. The provisions in section 33(1) of the VAT Act are very clear and unambiguous and the question of substantial compliance does not arise in the circumstances. [per S.N. Silva C.J. in *Ediriweera, Returning Officer for Akuressa Pradeshiya Sabha v. Kapukotuwa, General Secretary, United National Party and Others* (2003) 1 Sri.L.R. 228 at 233].

More so, as the time within which the Assessment must be made, as set out in section 33(1) of the VAT Act, has already started running from the end of the taxable period. The revenue authorities must be given the full time contemplated by the legislature to make Assessments pertaining to the vast number of registered persons and recognizing a substantial compliance standard brings about uncertainty in practice. When will substantial compliance cease? Is it after a two day or a weeks or a month's delay?

There is also a jurisprudential basis for rejecting the substantial compliance proposition. Hohfeld[1] argued that there needs to be an understanding of the true nature of legal conceptions and relations to obviate the difficulties posed by artificial dichotomies and constructs. He pointed out that "right", "duty", "liberty "and "no-right" are connected in a fundamental way with each other. The existence of one brings about the existence of the other. Hofeld identified only jural correlatives and opposites whereas Glanville Williams identified a third set of jural relations which he referred to as jural contradictories. In this situation, the presence of one conception in one party means the absence of the contradictory in the other party. The registered person must perform the duty of submitting his return within the time stipulated in section 21(1) of the VAT Act in order to ensure that the Assessor has no right to breach the time bar in section 33(1) of the Act. Where the duty is not performed the no right does not come into existence.

For the foregoing reasons, we are of the opinion that the assessment for the taxable period ending 31st March 2009 is not time barred.

[1] *Some fundamental legal conceptions as applied in judicial reasoning*, Volumes 23(1913) and 26(1917) of the Yale Law Journal

Taxable Supply of Goods

In terms of section 2(1) of the VAT Act, one condition for the imposition of Value Added Tax (VAT) is that there must be a "taxable supply of goods and services". The Appellant contends that this condition is not met in the circumstances of the instant case.

The Appellant is a limited liability company having as its principal business activity the manufacture and sale of rubber gloves primarily for the export market. Under the rubber re-planting program of the Appellant, existing old rubber trees are uprooted for the preparation of the land in accordance with the requirements of the relevant authorities. The Appellant entered into several contracts with contractors for the uprooting and removal of rubber trees.

The contention of the learned counsel for the Appellant is that the contracts are in effect contracts for the sale of rubber trees *in situ* (i.e. live rubber trees in the natural form) and the successful bidder has paid the full sale consideration when the trees are in live form and live trees are "unprocessed agricultural product", which is an exempt supply within the contemplation of item (b)(xxiii) of Part II of the First Schedule to the VAT Act. In the alternative the Appellant contends that it sold agricultural plants which is an exempt supply within the contemplation of item (a)(xi) of Part II of the First Schedule to the VAT Act.

In this context it is important to determine the true nature of the contracts entered into by the Appellant. The substance test has been used by courts to determine whether a contract is a contract for the sale of goods or contract for the supply of services [per Greer L.J. in *Robinson v. Graves* [(1935) 1 KB 579 at 587; Atiyah, Adams and Macqueen, *The Sale of Goods* (11th Ed.; page 27)]. We are of the view that the same test is appropriate in determining the true nature of a contract.

The true nature of the contracts entered into by the Appellant can be discerned only after scrutinizing its terms and conditions. The Appellant called for public tenders for "Uprooting Old Rubber Trees". The agreement states that it is for the "uprooting and removal of trees". It lays down several conditions which regulate the manner in which the contractors must perform their part of the bargain. It requires the contractor to uproot and clear old rubber trees. The contractor has to pay the Appellant a sum of Rs. 2100/= per tree. Furthermore, the contractor is required to

deposit a sum of Rs. 100/= per tree as a security deposit to ensure the due uprooting and removal of the tree. Where the contractor fails to duly clean the land, the security deposit is forfeited. Some of the agreements even specify the dimensions of the pieces to which the tree must be cut. More importantly, the Notes to the Financial Statements of the Appellant for the year ended 31st March 2008 identify the profits of these transactions as "Sales of firewood, logs and chips". This, although not decisive, is important in understanding the true nature of the contracts under consideration as the intention of the parties is paramount in a contract. The intention as well as the understanding of the Appellant is quite clear when it describes the profits of the contracts as "Sales of firewood, logs and chips".

However, the learned counsel for the Appellant submitted that in terms of section 2(1)(a) of the VAT Act, VAT is chargeable **at the time of supply** and that in terms of section 4(1) of the VAT Act the time of supply is deemed to be the earlier of payment or delivery.

The learned counsel for the Appellant then referred to clauses 2, 4 and 5 of one agreement and contended that they evidence that (i) at the time of signing the agreement the contractor is required to make a deposit of Rs. 100/= per tree which is to prevent him from defaulting on the agreement; and the contractor is required to pay the full sum payable in respect of the number of trees he intends to remove, and he would only be entitled to remove the trees after he has paid for the full value of the trees. Accordingly, he contended that the supply for the purpose of the VAT Act in the instant case was complete whilst the tree was *in situ* and therefore the contract must be construed as being one for the supply of live trees in their natural form which is an exempt supply.

We are of the view that this proposition is not tenable in law. The Appellant called for tenders to uproot and remove **non-harvesting rubber trees**. Hence, the trees sold have ceased to be productive in their natural form. Furthermore, section 4(1) of the VAT Act reads:

> "The supply of goods shall be deemed to have taken place at the time of occurrence of any of the following whichever, occurs earlier; (a) the issue of an invoice by the supplier in respect of the goods; or (b) a payment for the goods including any advance payment received by the supplier; or (c) a payment for the goods is due to the supplier in respect of such supply; or (d) the delivery of the goods have been effected."

The meaning of the word "deemed" was considered and explained by Ranasinghe, J. (as he then was) in *Jinawathie v. Emalin Perera* [(1986) 2 Sri.L.R. 121 at 130,131] in the following words:

> "In statutes, the expression deemed is commonly used for the purpose of creating a statutory function so that a meaning of a term is extended to a subject-matter which it properly does not designate. . . Thus, where a person is deemed to be something it only means that whereas he is not in reality that something, the Act of Parliament requires him to be treated as if he were".

Section 4(1) of the VAT Act is a deeming provision to determine the time of supply for the purposes of section 2(1) of the VAT Act. VAT is charged at the time of supply and as such it is important to clearly identify the time at which the taxable supply of goods or services takes place. Section 4(1) of the VAT Act seeks to facilitate the identification of this point of time. The deeming effect is in our view restricted to ascertaining the time of supply for the purpose of charging VAT.

It cannot be used to establish that the supply of goods did in fact take place at that point of time. In terms of section 83 of the VAT Act "supply of goods" means the passing of exclusive ownership of goods to another as the owner of such goods. Hence for there to be a "supply of goods" there must be a passing of "exclusive ownership of goods". That in our view must be ascertained upon a consideration of the provisions in the Sale of Goods Ordinance dealing with the passing of property.

The learned counsel for the Appellant concedes this point in submitting that the Sale of Goods Ordinance applies to the relevant contracts in relation to when the property or title to the underlying goods passes. However, he contends that the goods forming the subject matter of the contracts are specific or ascertained goods and that in terms of section 18 of the Sale of Goods Ordinance, the property is transferred to the buyer at such time the parties to the contract intend it to be transferred.

We are of the view that the goods forming the subject matter of the contracts between the Appellant and his contractors are not specific or ascertained goods but unascertained goods. The contracts do not identify the particular trees to be cut. It refers only to the number of trees. The contracts require the contractor to take over the trees that are identified by the field officer. Hence the goods remain unascertained as at the date of payment and passing of "exclusive ownership of goods" did not for the purposes of the Sale of Goods Ordinance take place at the date of payment as submitted by the learned counsel for the Appellant.

Section 19 of the Sale of Goods Ordinance sets out different rules for ascertaining the intention of the parties as to the time at which the property in the goods pass to the buyer unless a different intention appears from the terms of the contract, conduct of the parties and the circumstances of the case. Rule 5 thereunder specifies that where there is a contract for the sale of unascertained or future goods by description, and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer. In *Kursell v. Timber Operators & Contractors Ltd.* [(1927) 1 K.B. 298] the plaintiff sold to the defendants all the trees in a Latvian forest which conformed to certain measurements on a particular date, the buyer to have 15 years in which to cut and remove the timber. The English Court of Appeal held that the property in the trees had not passed to the defendants as the goods were not sufficiently identified, since not all the trees were to pass but only those conforming to the stipulated measurements.

In the instant case, exclusive ownership of the trees is not passed when the payment was made by the contractor as the goods remain unascertained. The property in the trees can be passed if at all only after the trees are ascertained by the field officer as stated above.

However, as long as the trees are *in situ* on land owned by the State property in them cannot be transferred to the contractor. The property in them can be transferred only after uprooting them. In those circumstances, the true nature of the contracts in substance is that they are for the uprooting and removal of trees for the supply of rubber logs. The consideration for these contracts was the timber value of the trees uprooted, removed and taken into the possession of the contractor.

Accordingly, we reject the argument made by the learned counsel for the Appellant that the contracts are in effect contracts for the sale of rubber trees *in situ*.

We conclude that there has been a "taxable supply of goods" by the Appellant in terms of the VAT Act in relation to rubber trees under the aforesaid agreements.

Unprocessed Agricultural Product/Agricultural Plant

The learned counsel for the Appellant submitted that even if the Respondents argument was to be accepted that the supply could only take place after the trees were uprooted and cut, whether the mere uprooting and cutting of the tree for removal from the estate could be considered to be "processing" which would disentitle the Appellant to the exemptions referred to in section 7 of the VAT Act which are available for an "unprocessed agricultural product" or "agricultural plant".

In addressing this contention Court is called upon to interpret the provisions of the VAT Act to ascertain whether the activity of the Appellant under consideration is subject to VAT. In *Perera & Silva ltd., v. Commissioner General of Inland Revenue* [79(II) N.L.R. 164 at 167] Thamotheram J. quoted with approval the following statement in C. N. Beatie- Elements of the Law of Income and Capital Gains Taxation at page 2;

> "It has frequently been said that, there is no equity in a taxing statute. This means that tax being the creature of statute, liability cannot be implied under any principle of equity

but must be found in the express language of some statutory provision. The ordinary canons of construction apply in ascertaining the meaning of a taxing statute: "the only safe rule is to look at the words of the enactments and see what is the intention expressed by these words." **If in so construing the statute the language is found to be so ambiguous that it is in doubt whether tax is attracted or not, the doubt must be resolved in favour of the taxpayer, because it is not possible to fall back on any principle of common law or equity to fill a gap in a taxing statute.** " The subject is not to be taxed unless the words of the taxing statute unambiguously impose the tax upon him ". However, this does not prevent the court from construing a taxing statute against the subject, where that appears to be the correct interpretation of a provision the meaning of which it may be difficult to understand. **Difficulty does not absolve the court from the duty of construing a statute; it is only when ambiguity remains after the statute has been properly construed that the court is entitled to decide in favour of the taxpayer**". (Emphasis added)

The Appellant contends that the mere act of cutting or felling trees would not amount to "processing". The learned counsel for the Appellant contended that the term "processed" connotes the performance of a series of mechanical or chemical operations on an object in order to change or preserve its original form and the mere act of cutting the tree would not change or modify the essential character of the tree and therefore cannot be construed as "processing". Reliance was placed on the term "unprocessed agricultural product" and the opposing term "processed agricultural product" used in Title 7 of the U.S. Code, European Union Regulation No. 510/2014 and United Kingdom Consumer Protection Act of 1978 and it was submitted that in all such contexts the envisaged processing would not cover the mere act of cutting down or felling an agricultural product such as a live tree.

We note that even these legislative instruments do not support the proposition advanced by the Appellant and do not have a common meaning attributed to the word "unprocessed agricultural products". While in Title 7 of the U.S. Code "processing" appears to imply doing an act which makes the product retail ready, the European Union Regulation No. 510/2014 appears to require steps such as adding chemicals or breaking down or otherwise changing the character of the agricultural product.

Hence the legal meaning of a word changes from jurisdiction to jurisdiction depending on its context and the intention of the legislature. We are of the view that it is unsafe to define a word used in the domestic legislation merely by reference to the same word and its meaning in different foreign legislative instruments.

The learned counsel for the Appellant referred to the Guide to the Value Added Tax in Sri Lanka and submitted that the directions issued by the Respondent defines "unprocessed agricultural produce" to include live trees, and other plants, roots, branches, leaves, flowers, tubes, seeds, fruits and nuts of trees and other plants in natural form not otherwise processed. He contended that manifestly live trees are caught up within the definition of unprocessed agricultural produce and that the Respondent is estopped from taking up a contrary position.

In terms of Article 23(1) of the Constitution, all laws are enacted and published in the Sinhala and Tamil, together with a translation thereof in English. Any interpretation of the VAT Act must be therefore be done by reference to the Sinhala Act as section 84 therein states that the Sinhala text shall prevail where there is any inconsistency between the Sinhala and Tamil texts and as the English text is only a translation.

The term used in the Sinhala text for "unprocessed" is "සැකසුම් නොකළ". We are of the view that the term "සැකසුම් නොකළ" is not a term of art as used in the VAT Act and must be given a literal meaning. In ගුණසේන මහා සිංහල ශබ්දකෝෂය compiled by Harischandra Wijetunge (2005, 1st Ed.) the word "සැකසීම්" is defined as නාප්‍ර සකසනවා යන්නෙහි භා නා පිළියෙල කිරීම, විශේෂ ක්‍රමයකට පිළියෙල කිරීම, සුදුසු සේ ගලපා සකස් කිරීම, සැකැස්ම.

The subject matter of the contracts between the Appellant and his contractors are not in our view live trees. The true nature of the contracts in substance is that they are for the uprooting and removal of trees for the supply of rubber logs. The consideration for these contracts was the timber value of the trees uprooted, removed and taken into the possession of the contractor. The exemption from VAT given to "unprocessed agricultural product" does not cover the instant case where non-harvesting rubber trees are uprooted and removed. That involves a process which changes the subject from a rubber tree to firewood, logs and chips. The Appellant in the Notes to the Financial Statements for the year ended 31st March 2008 identify the profits of these

transactions as "Sales of firewood, logs and chips". Accordingly, the subject matter of the contracts between the Appellant and its contractors are not live trees within the meaning of the Guide to the Value Added Tax in Sri Lanka. It is also not "unprocessed agricultural product" within the meaning of item (b) (xxiii) of Part II of the First Schedule of the VAT Act.

The remaining question is whether the subject matter of the contracts between the Appellant and the contractors are "Agricultural plants" in terms of item (a)(xi) of Part II of the First Schedule of the VAT Act.

In the Sinhala text of the VAT Act, the word used in item (a)(xi) of Part II of the First Schedule is "කෘෂිකාර්මික පැල". In ගුණසේන මහා සිංහල ශබ්දකෝෂය compiled by Harischandra Wijetunge (2005, 1st Ed.) the word "පැල" is defined to mean "පැළ නාපුංග 1 කුඩා ශාකය , ළපටි ගස, ළදරු ගස 2 බස්නාහිර දිසාව 3 පිටි පස්ස 4 පීඩාව, පෙළීම. වි. ළපටි, ළදරු". Non-harvesting rubber trees of around 25 feet which according to the Appellant were sold and profits derived as "Sales of firewood, logs and chips" are not in our view "කෘෂිකාර්මික පැල" within the meaning item (a)(xi) of Part II of the First Schedule of the VAT Act.

Accordingly, we answer the questions of law arising in the Case Stated as follows:

1. Is the assessment for the taxable period ending 31st March 2009 invalid in terms of Section 33(1)(a) of the VAT Act as it has been dated 8 June 2012 and received by the Appellant on 24 July 2012 and is therefore time barred? **No.**
2. Has there been a "taxable supply of goods" by the Appellant in relation to rubber trees under the aforesaid agreements, in terms of the VAT Act? **Yes.**
3. Has the TAC erred in concluding that the agreements entered into by the Appellant with contractors titled "Agreement for Uprooting Old Rubber Trees and clearing the Land" were in fact contracts for the supply of rubber logs or timber? **No.**

4. Would the supply of Rubber trees in terms of the aforesaid agreements be an exempt supply in terms of the VAT Act by reasons of it being:
    a. "Unprocessed agricultural products produced in Sri Lanka" within the meaning of item (b) (xxiii) of Part II of the First Schedule of the VAT Act? **No**

       or

    b. "Agricultural plants" in terms of item (a)(xi) of Part II of the First Schedule of the VAT Act? **No**

Accordingly, acting in terms of section 11A (6) of the VAT Act, we confirm the assessment determined by the TAC and dismiss this appeal with costs.

Judge of the Court of Appeal

Achala Wengappuli J.

I agree.

Judge of the Court of Appeal