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

In the matter of an appeal on a question of law by way of a case stated for the opinion of the Court of Appeal of the Democratic Socialist Republic of Sri Lanka under and in terms of Section 170(2) of the Inland Revenue Act No. 10 of 2006 (s amended) read with Section 11A of the Tax Appeals Commission Act No. 23 of 2011 (as amended)

Uni-Grand Lanka (Pvt) Ltd.,

No. 34, Park Road,

Colombo 05.

APPELLANT

Case No. CA/TAX/09/2015

Tax Appeal Commission Case No.

TAC/OLD/ESC/001

Vs.

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:

Saliya Pieris P.C. with Upendra Walgampaya for the Appellant

Chaya Sri Nammuni State Counsel for the Respondent

Written Submissions tendered on:

Appellant on 05.12.2017 and 31.05.2018

Respondent on 17.05.2018

Argued on: 15.05.2018

Decided on: 23.01.2019

Janak De Silva J.

The Tax Appeals Commission (TAC) has acting under section 170 of the Inland Revenue Act No. 10 of 2006 referred the following questions of law for the opinion of this Court:

(1) Whether the FOB (Free on Board) prices prepared and used for export purposes can be treated as turnover as provided in sub section 3 of section 2 of the Finance Act No. 11 of 2004 imposed for Economic Service Charge purposes, if the business was transacted outside Sri Lanka?

(2) Transactions entered into in Sri Lanka by non-resident persons are taxed through their respective agents as provided in the interpretation given for the 'Agent' in the section 217 of the Inland Revenue Act, No. 10 of 2006, read with sub section (1) and (2) of the Section 2 of the same act. The interpretation given in the said Inland Revenue Act for 'Agent' applies to ESC purposes as per Section 12 of the Finance Act, No. 11 of 2004.
Uni Eastern Sportswear Manufacturing Ltd. is a non-resident company and separate legal entity registered and domiciled in Taiwan. The Uni Grand (Lanka) Pvt. Ltd., the appellant company, is a BOI approved registered resident company in Sri Lanka and it is not the

agent of the Uni Eastern Sportswear Manufacturing Ltd. The Uni Eastern Sportswear Manufacturing Pvt. is the parent company of the Uni Grand (Lanka) Pvt. Ltd. Can the Revenue issue an assessment in the name of resident company to cover the purported liability of the non-resident company?

Before addressing the questions that arise for determination in this case stated I am compelled to make certain observations on the procedure adopted by the TAC in referring the case stated to this Court. The record indicates that the Appellant had by letter dated 28.01.2015 addressed to the TAC requested it to state a case for the opinion of the Court of Appeal on the above questions of law. It appears that the TAC has adopted the proposed questions of law without any consideration thereby abdicating its statutory responsibilities.

In terms of section 11A (1) of the TAC Act, either the person who preferred an appeal to the Tax Appeals Commission (TAC) under paragraph (a) of subsection (1) of section 7 of the TAC Act or the Commissioner-General may make an application requiring the TAC to state a case on a question of law for the opinion of the Court of Appeal. It is the TAC that must state a case on a question of law for the opinion of this Court. This is clear upon a consideration of section 11A (2) of the TAC Act which states that "**the case stated by the Commission"**.

In *Rajapakse v. Commissioner of Income Tax* (Reports of Ceylon Tax Cases, Vol. I, page 27 at 33) Drieberg J. held that "A 'case stated' should, I think, contain in addition to a statement of the facts the matter of law submitted for decision formulated as a question". Accordingly, in my view the obligation to frame the questions of law is initially placed on the TAC and not the Appellant. In fact, Basnayake C.J. in *R.M. Fernando v. Commissioner of Income Tax* (Reports of Ceylon Tax Cases, Vol. I, page 571 at 577) specifically stated that "it is not for the appellant to state the questions of law arising on a case stated".

Of course, a party preferring an appeal may in the application propose certain questions of law for consideration by the TAC to be referred to this Court as part of the case stated. But the TAC cannot blindly adopt the proposed questions of law without giving its mind to them. Such a course of action will amount to an abdication of its statutory responsibilities.

It is said that the current practice is that the TAC forwards all the questions of law set out in the application preferred by an appellant to this Court as part of the case stated and clearly the present case is an example. In this respect, I reiterate the following statement of Basnayake C.J. in *R.M. Fernando v. Commissioner of Income Tax* (supra. at 578):

> "The responsibility for stating a case is vested by the statute in the Board of Review and although the statute provides for the appointment of a clerk and legal adviser to the Board it cannot delegate its functions to either of them. Though in the performance of its statutory duty it may make use of its ministerial officers the ultimate responsibility for the due and proper performance of its duty rests with the Board and the Board alone. If it is the practice to leave the preparation of the case entirely to one of its ministerial officers and for the Board merely to sign the case as stated by such officer that practice is not warranted by law and must cease forthwith."

The observations made above is particularly pertinent to question no. 2 submitted for the opinion of this Court. It essentially raises the question whether the revenue can issue an assessment in the name of a resident company to cover the purported Economic Service Charge (ESC) liability of the non-resident company. But it begins with a statement to the effect that the Appellant is not the agent of Uni Eastern Sportswear Manufacturing Ltd. Yet the TAC bases its decision on the finding that the Appellant is an agent of Uni Eastern Sportswear Manufacturing Ltd.

Therefore, I shall first address the issues raised in question no. 2. In doing so, it is important to state that it is open for this Court to consider questions of law other than what is set out in the case stated [*The Commissioner General of Inland Revenue vs Dr. S.S.L. Perera* (C.A. (Tax) 03/2017, C.A.M. 11.01.2019]. However, I wish to state that such a course of action is permissible only if the answers to the new questions of law may result in the confirmation, reduction, increasing or annulling the assessment determined by the Commission, or requires the remitting of the case to the TAC with the opinion of the Court.

Accordingly, I will not answer question 2 as submitted to this Court. Instead I will examine the question whether the Appellant was an agent of Uni Eastern Sportswear Manufacturing Ltd. as that is the basis on which the TAC made its determination.

Agent

In terms of section 12 of the Finance Act No. 11 of 2004 (Finance Act 2004), "agent" has the meaning assigned to it in the Inland Revenue Act. This is a reference to the Inland Revenue Act No. 38 of 2000 wherein section 186 defines "agent" to mean:

> "agent", in relation to a non-resident person or to a partnership in which any partner is a non-resident person, includes any person in Sri Lanka through whom such person or partnership is in receipt of ***any profits or income, arising in or derived from Sri Lanka*** (emphasis added)

The question is whether the Appellant is an "agent" of Uni Eastern Sportswear Manufacturing Ltd. registered and domiciled in Taiwan. The answer to this question must be found after ascertaining what is meant by "any profits or income, arising in or derived from Sri Lanka".

In addressing this issue, the Appellant relied on the decision in *Anglo-Persian Oil Co. Ltd. vs. Commissioner of Income Tax* (38 N.L.R. 348) where Akbar S.P.J. in construing the words in section 5 of Income Tax Ordinance No. 2 of 1938 held:

> "In my opinion these two words " arise" and " derive " were meant to include the case of the Ceylon company when it makes any profits or gets any income for anything done in Ceylon and the case of a non-resident owner deriving his income from an estate in Ceylon."

However, as Fernando A.J. held in *Chivers & Sons Ltd. v. Commissioner of Income Tax* (39 N.L.R. 342 at 347) the question considered in *Anglo-Persian Oil Co. Ltd. vs. Commissioner of Income Tax* (supra) and the English authorities relied upon therein is where a sale in fact takes place. But the question that arises in this case is whether any profits or income, arises in or is derived from Sri Lanka within the meaning of section 186 of the Inland Revenue Act No. 38 of 2000.

In *Commissioner of Inland Revenue v. Hang Seng Bank Limited* [(1990) UKPC 42, 8 October 1990] the Privy Council was called upon to interpret the words "profits arising in or derived from Hong Kong" and held as follows:

> "Their Lordships were referred in the course of the argument to many authorities on different taxing statutes in different common law jurisdictions raising a variety of questions as to the geographical source to which income or profits should be ascribed. But the question whether the gross profit resulting from a particular transaction arose or derived from one place or another is always in the last analysis a question of fact depending on the nature of the transaction. It is impossible to lay down precise rules of law by which the answer to that question is to be determined. ***The broad guiding principle, attested by many authorities, is that one looks to see what the tax payer has done to earn the profit in question. If he has rendered a service or engaged in an activity such as the manufacture of goods, the profit will have arisen or derived from the place where the service was rendered or the profit making activity carried on***. "(emphasis added)

In the instant case, according to the Appellant it carries on a business of an export trading house for the export of apparel/garments after processing in Sri Lanka. The raw material (fabric & accessories) required to manufacture apparel/garments were owned and provided by Uni Eastern Sportswear Manufacturing Ltd. based in Taiwan. The raw material (fabric & accessories) were sent to the Appellant by the Taiwanese company on a No-Foreign Exchange (NFE) basis. The Appellants task is to cut, make and package (CMP) the material (fabric & accessories) into a final product (apparel/garments) from Sri Lanka directly to the buyers in U.S.A., Canada and Mexico for the Taiwanese company. The contracts for the sale of the said final products have been entered into by and between the Taiwanese company and overseas buyers. According to the Appellant, it plays no role in the sale of the said final product. The payments for the final product are made by foreign buyers directly to the Taiwanese company.

I have set out above the activities the Appellant states it carries out as set out in its written submissions. The question is whether these facts results in Uni Eastern Sportswear Manufacturing Ltd. receiving ***any profits or income, arising in or derived from Sri Lanka***. The answer to this question determines whether the Appellant was an "agent" of Uni Eastern Sportswear Manufacturing Ltd. within the meaning of "agent" in Finance Act 2004.

The subject matter of the sale of goods transaction between Uni Eastern Sportswear Manufacturing Ltd. and the buyers in U.S.A., Canada and Mexico is the finished product whereas what the Appellant is sent by Uni Eastern Sportswear Manufacturing Ltd. is the raw material. The subject matter of the sale of goods transaction is the final product after the Appellant performs the CMP services on the raw material (fabric and accessories). Clearly the service was rendered or the profit-making activity was carried on in Sri Lanka. Accordingly, I hold that the profits or income, in relation to the said sale of goods transactions arose in or was derived from Sri Lanka. Hence the Appellant is an "agent "of Uni Eastern Sportswear Manufacturing Ltd. within the meaning of the Finance Act 2004.

Turnover

Section 2(3) of Finance Act 2004 (Finance Act 2004) defines "liable turnover" as follows:

> "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.

In terms of the above definition the liable turnover for the purposes of the Finance Act 2004 is the aggregate turnover which includes trade carried on or exercised through an agent. In view of my findings above, the Appellant as the agent of Uni Eastern Sportswear Manufacturing Ltd. has to include all costs of the transaction in determining the aggregate turnover which in these cases will be the total Free on Board (FOB) value.

Accordingly, I answer the questions posed as follows:

(1) Whether the FOB (Free on Board) prices prepared and used for export purposes can be treated as turnover as provided in sub section 3 of section 2 of the Finance Act No. 11 of 2004 imposed for Economic Service Charge purposes, if the business was transacted outside Sri Lanka? **Yes, as the Appellant is an agent of Uni Eastern Sportswear Manufacturing Ltd.**

(2) Transactions entered into in Sri Lanka by non-resident persons are taxed through their respective agents as provided in the interpretation given for the 'Agent' in the section 217 of the Inland Revenue Act, No. 10 of 2006, read with sub section (1) and (2) of the Section 2 of the same act. The interpretation given in the said Inland Revenue Act for 'Agent' applies to ESC purposes as per Section 12 of the Finance Act, No. 11 of 2004.
Uni Eastern Sportswear Manufacturing Ltd. is a non-resident company and separate legal entity registered and domiciled in Taiwan. The Uni Grand (Lanka) Pvt. Ltd., the appellant company, is a BOI approved registered resident company in Sri Lanka and it is not the agent of the Uni Eastern Sportswear Manufacturing Ltd. The Uni Eastern Sportswear Manufacturing Pvt. is the parent company of the Uni Grand (Lanka) Pvt. Ltd. Can the Revenue issue an assessment in the name of resident company to cover the purported liability of the non-resident company? **The Appellant is an agent of Uni Eastern Sportswear Manufacturing Ltd.**

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

Achala Wengappuli J.

I agree.

Judge of the Court of Appeal