# 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/030/2016 by the Tax Appeals Commission under Section 170 of the Inland Revenue Act, No. 10 of 2006, as amended read together with Section 11(A) of the Tax Appeals Commission Act, No. 23 of 2011 (as amended).

**People's Leasing and Finance PLC,**
No. 1161, Maradana Road,
Colombo 08.

**APPELLANT**

**Case No. CA/TAX/0021/2019**
**Tax Appeals Commission No. TAC/VAT/011/2016**

**Vs.**

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

**RESPONDENT**

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|---|---|---|
| **BEFORE** | **:** | Dr. Ruwan Fernando J. & |
| | | M. Sampath K.B. Wijeratne J. |
| **COUNSEL** | : | F.N.Goonewardena for the Appellant |
| | | Manohara Jayasinghe, S.S.C. for the Respondent |
| **ARGUED ON** | : | 01.03.2021 |
| **WRITTEN SUBMISSIONS FILED** | : | 08.09.2020 & 20.04.2021 (by the Appellant) |
| | | 23.02.2021 (by the Respondent) |
| **DECIDED ON** | : | 20.07.2021 |

**Dr. Ruwan Fernando, J.**

## Introduction

[1] This is an appeal by way of Stated Case by the Appellant against the determination made by the Tax Appeals Commission dated 18.06.2019 confirming the determination made by the Respondent dated 09.05.2016 and dismissing the appeal of the Appellant. The taxable periods related to this Appeal are from April 1, 2010 to March 31, 2011.

## Factual Background

[2] The Appellant is a Public Limited Liability Company and was registered for Value Added Tax "(VAT") and VAT on Financial Services ("VAT on FS") under the Value Added Tax Act, No. 14 of 2002 as amended. The Appellant submitted monthly VAT returns for the above-mentioned taxable periods from April 1, 2010 to March 31, 2011 on the due dates and its annual adjustment on 28.06.2013. The assessor by letter dated 21.03.2014 refused to accept the same for the following reasons:

1. Incorrect Net profit for the purpose of calculating Value Added Tax on the supply of financial services in terms of section 25 (1) of the Value Added Act, No. 14 of 2002 as amended, has been taken into account by the Appellant for the calculation of Value addition in the annual adjustment;

2. Incorrect emoluments payable for the purpose of section 25C (1) of the VAT Act, have been taken into account for the calculation of Value addition in the annual adjustment;

3. Computation of the value addition attributable to financial services has not been made in terms of section 25C (5) of the Value Added Tax Act, No. 14 of 2002 as amended by the VAT (Amendment) Act, No. 17 of 2003.

[3] Accordingly, the assessor on 21.03.2014 assessed the VAT on financial services payable by the Appellant for the periods from 01.04.2010 to 31.12.2010 (9 months) and 01.01.2011 to 31.03.2011 (3 months) separately, breaking up of the turnover for the taxable periods from 01.04.2010 to 31.12.2010 (9 months) and 01.01.2011 to 31.03.2011 (3 months) (pages 94-97) and issued two separate notices of assessment on 27.03.2014 (pages 98 and 99).

## Appeal to the Commissioner-General of the Inland Revenue and the Tax Appeals Commission

[4] The Appellant appealed to the Respondent against the said assessments and the Respondent by its determination dated 09.05.2016 confirmed the assessments issued by the assessor (p. 1). Being dissatisfied with the said determination of the Respondent, the Appellant appealed to the Tax Appeals

Commission and the Tax Appeals Commission by its determination dated 18.06.2019 confirmed the determination of the Respondent and dismissed the appeal for the following reasons: .

1. The appeal was made on 29.04.2014 and it was acknowledged on 27.05.2014 and thus, the appeal was acknowledged within thirty days of its receipt in terms of Section 34 (8) of the VAT Act, No. 14 of 2002. The determination of the Respondent was made on 09.05.2016 and thus, the appeal has been determined by the Respondent within the two year period specified therein;
2. The Appellant has failed to submit the annual adjustment, which is a statutory requirement together with the audited financial statement of accounts and all the material information necessary to calculate the VAT liability within the time limit and thus, the Appellant cannot be allowed to avoid tax liability under the guise of the statutory time bar;
3. The Appellant is a finance company registered under the Finance Companies Act, No. 78 of 1988 and the Appellant is engaged in the business of supplying financial services as a "specified institution" and thus, in terms of Section 25C (1) of the VAT Act, No. 14 of 2012, the Appellant is liable to pay VAT on financial services;
4. The income received by the Appellant as a "specified institution" from dividends, sale of shares of listed companies and the income received from bank deposits and government securities referred to in section 25F of the VAT Act, cannot be excluded from the value addition on the supply of financial services as a Zero rated supply in terms of section 25 (5) (f), 25 (5) (gg) and 25 (5) (e) of the VAT Act;

**Appeal to the Court of Appeal**

[5] Being aggrieved by the decision of the Tax Appeals Commission, the Appellant appealed to the Court of Appeal and formulated Eight Questions of Law in the case Stated for the opinion of the Court of Appeal. At the hearing of the appeal, Mr. F.N. Goonawardena, the learned Counsel for the Appellant and the learned Senior State Counsel, Mr. Manohara Jayasinghe made extensive oral submissions on the Eight Questions of Law submitted to Court.

**Question of Law 1**

**Has the Tax Appeals Commission erred in determining that the assessment made under Charge No. VATFS/BFSU/2014/579 dated 27.03.2014 in terms of the Value Added Tax Act, No. 14 of 2002 (as amended) ('VAT ACT') was valid in law notwithstanding the said assessment having aggregated value added tax payable for the 9 taxable periods ending 30.04.2010, 31.05.2010, 30.06.2010, 31.07.2010, 31.08.2010, 30.09.2010, 31.10.2010, 30.11.2010 and 31.12.2010?**

**Question of Law No. 2**

**Has the Tax Appeals Commission erred in determining that the Assessments made under Charge No. VATFS/BFSU/2014/580 dated 27.03.2014 in terms of the Value Added Tax Act, No. 14 of 2002 (as amended) ('VAT ACT') was valid in law notwithstanding the said Assessment having aggregated value added tax payable for the 3 taxable periods ending 31st January 2011, 28th February 2011 and 31st March 2011?**

[6] The Question of Law, No. 1 relates to the validity of the assessment under Charge No. VATFS/BFSU/2014/579 dated 27.03.2014 by aggregating 9 taxable periods from April 01, 2010 to December 31, 2010 into a single taxable period in violation of the provisions of the VAT Act. The Question of Law, No. 2 also relates to the validity of the assessment under Charge No. No. VATFS/BFSU/2014/580 dated 27.03.2014 by aggregating 3 taxable periods from January 1, 2011 to March 31, 2011 into a single taxable period in violation of the provisions of the VAT Act.

[7] At the hearing, Mr. F. N. Goonewardena submitted that the taxable period prior to January 1, 2011 for the Appellant, in terms of Section 25B of the VAT Act was one month and that the Appellant submitted separate VAT returns for monthly taxable periods from April 01, 2010 to December 31, 2010 under Section 21 of the VAT Act. There is no dispute that the Appellant has submitted the VAT returns for the monthly taxable periods from April 01, 2010 to December 31, 2010 on 20.05.2010, 17.06.2010, 20.07.2010, 20.08.2010, 20.09.2010, 20.10.2010, 18.11.2010, 17.12.2010 and 20.01.2010 respectively (X2-X10).

[8] He submitted that as Section 25B of the VAT Act specifically stipulates that for the period prior to 01.01.2011, a taxable period shall be considered to be one month, for the periods from 01.04.2010 to 31.12.2010, there were nine separate taxable periods. His contention was that while the last sentence of Section 33 (2) specifically permits a single notice of assessment to refer to one or more separate taxable periods, the VAT Act does not make provisions for the aggregation of multiple taxable periods into a single amalgamated taxable period without assessing the amount of tax for each taxable period separately. In short, his contention was that no aggregation of taxable periods into one assessment can be made without assessing the amount of tax due for each taxable period separately.

[9] The last sentence of Section 33 (2) clearly states that any notice of assessment may refer to one or more taxable periods. It reads as follows:

> *"For the purposes of this Chapter* ***any notice of assessment may refer to one or more taxable periods".***

[10] The learned Senior State Counsel attached great importance to the last sentence of Section 33 (2) of the VAT Act and contended that an aggregation of

multiple taxable periods in a single notice of assessment is not prohibited by the VAT Act. He argued that the Parliament introduced the said provision by way of the VAT (Amendment) Act, No. 9 of 2011 to deal with a situation where the assessor is not in a position to determine the respective income for each taxable period and invited us to consider the contents of the assessor's intimation letter dated 21.03.2014 (p. 97). He contended that the assessor had aggregated taxable periods and assessed the total amount of tax for nine months and three months separately to the best of his judgment due to the inability to determine the respective income for each taxable period on the basis of the information provided by the Appellant in time as required by the VAT Act.

[11] The sole question for determination is one of law, namely, whether it is competent to the assessor under the VAT Act to aggregate several taxable periods from April 1, 2010 to December 31, 2010 and January 01, 2011 to March 31, 2011 in one assessment without the assessment being made for each nine taxable periods separately or calculating the amount of tax due on each taxable period separately. In order to determine the question raised, it is necessary to have a survey of the relevant provisions of the VAT Act.

**Tax Returns & Taxable Period**

[12] The system of VAT assessment is the self-assessment procedure where the assessee is expected to assess his taxable income and furnish particulars of his income and pay tax as per the prescribed procedure. The assessor is expected to check and scrutinise the returns of income to find out whether the income has been correctly shown in the returns. A VAT return is a form filed with the Commissioner-General, that reports income and expenses and other pertinent tax information and, such tax returns allow the taxpayer to calculate its tax liability or request refunds for the overpayment of taxes.

**Taxable Period-**

[13] Section 83 of the VAT Act generally defines a "taxable period" as follows:

> "A taxable period" means-
>
> *"(a)* ***a period of one month****-*
>
> *(i) where a person makes zero rated supplies;*
>
> *..*
>
> *(b)* ***a period of three months*** *commencing respectively on the first day of January, the first day of April, the first day of July and the first day of October of each year in respect of a registered person whom is not referred to in paragraph (a) or who opts to submit quarterly returns on the approval by the Commissioner-General.*

**Returns in respect of Taxable Period**

[14] Section 21 of the VAT Act, as amended, relates to returns and the manner in which returns are furnished to the Commissioner-General. It reads as follows:

> *"21(1) Every registered person shall furnish to the Commissioner-General-*
>
> *(a) for any taxable period ending prior to January 1, 2013, not later than the twentieth day of the month after the expiry of each taxable period;*
>
> *(b) for any taxable period commencing on or after January 1, 2013 not later than the* ***last day of the month after the expiry of each taxable period***
>
> *a return either in writing or by electronic means of his supplies during that taxable period. Every such return shall be in the specified form and shall contain all such particulars as may be required to be set out in such form".*

[15] Section 25B of the VAT Act as amended by VAT (Amendment) Act, No. 9 of 2011 specifically relates to a taxable period for levying VAT on the **supply of financial services** from every "registered specified institution" or "other person" and identifies a taxable period of such registered specified institution or other person. It provides:

> *"(1) The taxable period of every registered specified institution or other person shall be:-*
>
> *(a)* ***one month*** *for any taxable period prior to* ***January 1, 2011*** *and*
>
> *(b)* ***six months*** *for any taxable period commencing on or* ***after January 1, 2011:***
>
> *(2) Every* ***registered specified institution*** *or other person shall furnish a return in the Form specified, in respect of* ***each taxable period*** *before the end of the following month of the taxable period."*

[16] It is true that that the system for the assessment and collection of VAT by means of returns are dealt with by reference to a taxable period as a return is furnished under Section 21 (1) of the VAT Act, for **any taxable period**, not later than the twentieth day of the month after the expiry of each taxable period, which can be any taxable period. The taxable period may be a period of one month (s. 83 or s. 25B (1) (a)) or three months (s. 83) or six months (s. 25B (1) (b) etc., which depends on the categories of registered persons referred to in the definition of "taxable period" in Section 83 or Section 25B (1) of the VAT Act.

[17] Section 25B provides that the taxable period of every **registered specified institution or other person** shall be **one month** and such institution or person shall furnish a return in respect of each taxable period before the end of the following month of the taxable period. It seems to me that the returns of any registered specified institution or other person shall furnish on the supply of financial services, a return for the monthly taxable period under Section 25B in the Form specified in respect of each such monthly taxable period before the end of the following month of such taxable period.

[18] The Taxable periods in question of the Appellant relate to the period prior to **01.01.2011** and the VAT returns on supply of financial services have been furnished on the basis that the taxable period is one month, claiming zero rated supplies under Section 25 (5) (Vide- VAT Returns). The Appellant's argument is that as the taxable period is one month, for the period from 01.04.2010 to 31.12.2010, there were nine taxable periods and thus, the amalgamation is not permissible unless, the assessment is made for each taxable period separately.

**Aggregation of Multiple Taxable Periods in One Assessment**

[19] I will now turn to the period in respect of which the assessment shall be made as set out in the VAT Act. Section 28 (1) relates to the power of the assessor to make assessment and reads as follows:

> *"28 (1) Where-*
>
> *(a) any registered person who is in the opinion of the Assessor is chargeable with tax, fails to furnish a return **for any taxable period**; or*
>
> *(b) any registered person, who is chargeable with tax, furnishes a return in respect of any taxable period but fails to pay the tax for that taxable period;or*
>
> *(c) any person requests the Commissioner-General in writing to make any alteration or addition to any return furnished by such person for any taxable period,*
>
> *the Assessor shall assess the amount of the tax, which such person, in the judgment of the Assessor, ought to have paid for that taxable period and shall, by notice in writing, require such person to pay such amount forthwith. The amount so assessed in respect of any person for a taxable period shall be deemed to be the amount of the tax payable by him for that taxable period".*

[20] For an assessment of VAT under Section 28 (1) of the 2012 Act to be valid, it must be of an amount due for '**any taxable period'** and the amount due from a person who has failed to make one or more returns for '**any taxable period'** or who furnishes a return in respect of any taxable period, but fails to pay the tax for that taxable period. Thus, the assessor is free to make an assessment, to the best of his judgment for that taxable period. Section 33 (1) which relates to the limitation period for assessment or additional assessment provides that a limitation period of 3 years applies "where any registered person has furnished a return under Subsection (1) of Section 21 in respect of a taxable period **or such person has been assessed for tax in respect of any period".** It reads as follows:

> *"33 (1) Where any registered person has furnished a return under subsection (1) of section 21, in respect of a taxable period **or has been assessed for tax***

***in respect of any period,*** *it shall not be lawful for the Assessor where an assessment-*

*(a) has not been made, to make an assessment; or*

*(b) has been made, to make an additional assessment, after the expiration of three years from the end of the taxable period* ***in respect of which the return is furnished or the assessment was made*** *as the case may be".*

[21] There is nothing to indicate in Section 28 (1) or Section 33 (1) of the VAT Act that an assessment is to be confined to a single prescribed taxable period, since Section 28 (1) and Section 33 (1) of the Act refer to "**any taxable period**" and such period can relate to any taxable period ***in respect of which the return is furnished or the assessment was made.*** This could, in my view, be construed as referring to 'any taxable period' included in a single notice of assessment. This permits the assessor to calculate the amount due from a taxpayer in regard to 'any taxable period' and when this option applies, the notice of assessment may relate to one or more taxable periods, which can be either one month or 3 months or 6 months as set out in the Act.

[22] However, the present question of law relates to the taxable period of a "specified institution or other person" referred to in Section 25B (1) (a), which is one month for any taxable period prior to January 1, 2011 and thus, every such person shall furnish a return in respect of each taxable period before the end of the following month of the taxable period. The force of Mr. Goonewardena's argument is based on the 'one month taxable period' referred to in Section 25B (1) (a), so that, the notice of assessment must relate to each nine taxable periods separately because the amount of tax due for each taxable period can only be calculated accurately when the assessment relates to each taxable period separately.

[23] I am not inclined to agree with the submission of Mr. Goonewardena that it is a rule that an assessment that covers multiple taxable periods to be valid under Section 28 (1), must necessarily specify what tax is due from the taxpayer in respect of each taxable period separately when the assessor is unable to split the income due and determine the tax due from the taxpayer in respect of each taxable period. I do think that the intention of the legislature in introducing the last sentence of Section 33 (2) is to remedy a situation where the assessor is unable to spilt the income for each taxable period accurately to the best of his judgment due to the failure of the taxpayer to disclose fully and truly all the material facts necessary to determine the amount of tax for each taxable period.

[24] It seems to me that the legislature introduced this provision to empower the assessor to make one assessment in respect of multiple taxable periods setting out a proportionate rate covering one aggregate period where it is impossible for

the assessor to spilt up and determine the tax due from the taxpayer in respect of each taxable period to which the assessment relates.

[25] In this context, it is significant to look for guidance from some jurisdictions which have interpreted the question whether it is possible for an assessor to spilt the assessment into several taxable periods without assessing the amount of tax due for each period of time separately. There is some support for this proposition from decisions made by the UK Courts in recent times and hence, I shall refer to them in this judgment. In the United Kingdom, at one time, gave rise to a proposition that it was not possible for Customs to make an assessment other than in relation to a prescribed accounting period, which normally is one of three months. It is to be noted that Subsection (4) of Section 73 of the UK VAT Act, 1994 (previously, the Finance Act 1972) states that "the assessment may relate to one or more periods and the assessment can be combined and notified to him as one assessment." The only difference in the last sentence of Section 33 (2) of the VAT Act of Sri Lanka in comparison with the UK VAT Act, 1994 is that the words "combination of assessment" are missing.

[26] That proposition was dispelled by a decision of the Court of Appeal in the case of *S.J. Grange Ltd v. Customs and Excise Commissioners* (1979) STC 183, a VAT case, wherein a single notice of assessment was issued for a period of 21 months from 15.04.1973 to 31.12.1974 showing a single amount of tax due and payable by the company for the said 21 months periods on the basis that the trader's returns were incomplete and incorrect. The prescribed accounting period for VAT liability under Section 31 (2) of the UK Finance Act, 1972 was a period of 3 months. The company challenged the notice stating that, for an assessment made under Section 31 (1) to be valid, it has to be restricted to a prescribed accounting period of three months and it ought to have been split up to three monthly periods and accordingly, the assessment in question was invalid since it related to a continuous period of 21 months.

[27] The company alleged, as Mr. Goonewardena argued in the present case, that the amount due for any prescribed accounting period can only be calculated sensibly in regard to each accounting period and thus, the notice of assessment must relate to each accounting period separately, and as it was not spilt up, the notice was bad in law. The Tribunal dismissed the company's appeal and an appeal against the said decision was allowed by the Judge upholding the company's argument. The Commissioners appealed to the Court of Appeal.

[28] It is to be noted that Section 31 of the Finance Act 1972 (now VAT Act, s. 73) which relates to the assessment of VAT reads as follows:

> *"(1) Where a taxable person has failed to make any returns required under this Part of this Act or to keep any documents and afford the facilities*

*necessary to verify such returns or where it appears to the Commissioners that such returns are incomplete or incorrect that may assess the amount of tax due from him to the best of their judgment and notify it to him"*

[29] The Court of Appeal consisting of Lord Denning MR, Bridge LJ and Templeman LJ reversed the said proposition and held that:

(a) there was nothing in Section 31, sub-section 1 of the 1972 Finance Act (now VAT Act 1994, s. 73) to indicate that an assessment was to be confined to a single prescribed period, and since S. 31 (2) and (4), which referred to "any prescribed accounting period", could be constituted as referring to any prescribed accounting period included in the notice of assessment; and

(b) the construction of Section 31 (1) on the basis that under S. 31 (1), an assessment could only be made in respect of a single prescribed accounting period would produce an unworkable and unreasonable result.

[30] It is apt to refer to the following observations made by Lord Denning in the above-mentioned case at page 7:

*"Stopping there is nothing to prevent the Commissioners making an assessment for any period, whether it be three months, 12 months or longer. But the trader says that an assessment can only be made for a prescribed accounting period, and that is three months. In support, he relies on s. 31 (2), which says:*

*"An assessment under subsection (1) of this section of an amount of tax due for any prescribed accounting period shall not be made after the later of the following (a) two years after the end of the prescribed accounting period; or (b) one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge.....*

*The trader said that the amount due for any prescribed accounting period can only be calculated sensibly in regard to each accounting period. So they submitted that the notice of assessment must relate to each accounting period separately.*

*The judge accepted that argument. I can see the force of it. It is literally correct. But it leads to such impracticable results that it is necessary to do a little adjustment so as to make the section workable. This can be done by reading in a few words, such as Bridge LJ suggested in the course of the argument. This is, after 'for any prescribed accounting period' read in these words, 'which is included in the notice of assessment'. Making this interpolation, it means that the two years in sub s. 2(a) runs from the end of the first three months included in the assessment".*

**Applicable Test**

[31] Having dispelled the proposition and taken the view that such a restricted meaning is impracticable and unworkable, Lord Denning proceeded to set down the test to be applied when deviating from the earlier proposition at page 7 as follows:

> *"So read, it means that, in all cases it is impossible for the commissioners to spilt the assessment up into three-monthly periods, they can assess the amount of tax for any period of time which they specify (be it six, 12, 15 or 21 months) and such assessment will be good. They must do it within one year after they get evidence of the facts sufficient to justify the nature of the assessment: see s. 31 (2)(b)."*

[32] Mr. Goonewardena's argument that the assessor was required to identify and determine the amount of tax due for each nine taxable periods and issue the assessment separately, as the amount due for all nine months cannot be determined on the proportionate basis in one single taxable period leads obviously to unworkable and unreasonable results. The fallacy of this argument is that where it is impossible for the assessor to spilt the assessment up into a monthly period in the absence of sufficient information provided by the taxpayer, yet, the assessor will be obliged to make a speculative assessment or make further inquiries over and over again for a long period of time. By this time, obviously, the period of limitation would have expired.

[33] The following observations of Lord Denning in *S.J. Grange Ltd v. Customs and Excise Commissioners* (supra), at page 9 clearly provide the appropriate answer to the argument and accordingly, that argument cannot be sustained:

> *"I may add that, if the trader's argument were right, it would open the door to avoidance of value added tax. It would mean that, for every three months, the commissioners would have to make a speculative assessment to make a guess as to what sales the trader made in those three months. He might then evade it by saying: 'I did not sell anything in that time, so you are wrong as regards that accounting period. you must try another'. There would have to be further enquiries, and these would take so long that the period of limitation would have expired. Many other practical difficulties would arise in making assessments if they had to be made for every accounting period separately. In my opinion, therefore, a notice of assessment can be made for a period such as 21 months. This notice of assessment was good. The preliminary point fails...."*

**The Concept of 'Global Assessment' covering several Taxable Periods as opposed to Separate Assessments**

[34] The only other case to which I need to refer to this point is the decision of the Court of Appeal in *Customs and Excise Commissioners v. Le Rififi Ltd* [1995] BVC 55 & [1995] STC 103. The case concerned an assessment in prescribed form covering a number of periods, including a period which was out of time. The

Commissioners issued the assessment which referred to different accounting methods for different accounting periods. The taxpayer argued that one of the assessments was made more than 6 years after the end of the first prescribed accounting period included in **a global assessment** of pounds 132,303.68. One of the issues was whether the notice of 8 August 1989 was a **single global assessment** and if so, it was out of time. Balcombe J. stated at p. 59B:

> *"It is undoubtedly permissible for the Commissioner to make a single or 'global assessment' which covers more than one accounting period. In practice, this may be necessary when it is impossible or impracticable for Customs to identify the specific accounting period or periods for which the tax claimed is due".*

[35] Balcombe J., was, however, of the view that the power of the customs to make a global assessment is not confined to those cases where it is impossible or impracticable to identify the specific accounting period or periods for which the tax claimed is due (p. 59B). In the said case, however, it was found that the notice of assessment of 8 August 1989 could not be interpreted as constituting a single global assessment as it clearly refers to **24 separate assessments** for each of the accounting periods and thus, only the first assessment was out of time.

[36] An assessment in a case thus, constitutes what is called in the common tax parlance, a '**global assessment'** in that it does not make separate assessments of tax for each of the prescribed accounting period (in Sri Lanka, a taxable period) referred to in the notice of assessment, but one total amount is specified, where it is not possible to make separate assessments for each prescribed accounting period (See- judgment of Balcombe J. in *House (t/a P & J Autos) v. Customs and Excise Commissioners* (1996) BVC 116, S.J. *Grange Ltd v. C & E Commissioners* (supra) and *Customs and Excise Commissioners v. Le Rififi Ltd* (supra). In *Rififi Ltd* (supra), the Court of Appeal, however, found from VAT Forms, that (i) the Commissioners had made the assessments of tax for the periods shown; (ii) the assessed VAT was identified into separate periods; (iii) the form was designed to notify either one or more than one assessment and the form's three pages had notified 24 separate assessments, rather than one global assessment. On that basis, the Court of Appeal held that it was a number of separate assessments and so, only the assessment which was made outside the time-limit was invalid and the other 23 assessments were upheld.

[37] I now turn to consider the subsequent case of *International Language Centres Ltd v C & E Commissioners* (1983) BVC 545 & (1983) S.T.C. 394). In this case, a global assessment was made in respect of amounts totalling 40,560 pounds as regards supplies of educational courses to foreign students. The Commissioners made an assessment and the said assessment was confirmed by the Tribunal. Meanwhile, the appellant deducted tax in respect of 'over-payments' by it for periods previous to those covered by the first assessment. After the first

assessment had been confirmed, the Commissioners issued a second assessment which was the 'global assessment' for an amount of 40,560 pounds. Woolf, J. *inter alia,* stated at pp. 547-548:

> *"It is apparent from the judgments of the Court of Appeal in the Grange case that the use of global assessments is to be confined to those cases where it is not possible to identify a specific period for which the tax claimed is due. Clearly, it is good practice for the commissioners when they can identify a specific period to make an assessment in respect of that period*."

[38] There is one final case to which I wish to refer, is the case of *House (t/a) & J Autos) v. Customs and Excise Commissioners* [1996] BVC 116], which in my view is directly relevant to the resolution of the argument advanced by Mr. Goonewardena. The notice of assessment contained a single global assessment made for more than one prescribed accounting period from November 29/84 to January 1990. The notice of assessment Form VAT, which stated a total amount for the whole period, was received by the taxpayer, but the form did not specify the prescribed accounting periods covered by the assessment and amounts of tax attributed to them.

[39] The taxpayer first argued that, since the formal notice of assessment on Form VAT did not state the prescribed accounting periods covered by the assessment with the amount of tax claimed to be due on each, the assessment had not been duly notified to the taxpayer within the VAT Act, 1983, Sch. 7, para. 4 (1) and was therefore invalid. The taxpayer's second argument was that the assessment was formally deficient as the identification of the relevant accounting periods was necessary to enable the taxpayer to know whether the assessment was made in time or not, or if he wished to appeal, whether one or more appeals should be lodged. Dismissing the taxpayer's appeal, Balcombe, J. stated that:

> *"the references in para 4(2) of Sch. 7 to tax due* ***for a prescribed accounting period,*** *and, in other parts of the 1983 Act, at one time gave rise to a belief that it was not possible for Customs to make an assessment other than in relation to a prescribed accounting period, which normally would be one of three months. That belief was dispelled by a decision of this Court in the case of SJ Grange Ltd v. C & E Commrs (1978) 1 BVC 210. I should say that the belief to which I have referred had, in fact, commended itself to Neill J, which heard the case at first instance but the Court of Appeal, consisting of Lord Denning MR and Bridge LJ and Templeman LJ reversed it. The headnote reads as follows ([1978] 1 BVC 191):*
>
> *'There is nothing in Section 31, sub-section 1of 1972 Act [and] I pause there to interpolate that that was, in terms, the same as para, 4 (1) of Sch. 7 of the 1983 Act to indicate that an assessment was to be confined to a prescribed accounting period".*

[40] Having said that, Balcombe, J. stated on the first argument that it was permissible for the Commissioners to make a single assessment which covers more than one accounting period to the best of their judgment, within the meaning of para. 4 (1) of Sch. 7 to the Value Added Act 1983, in one total amount even where they had necessary information to make separate assessments. On the second argument, Balcombe, J. stated that the schedules sent to the taxpayer with details shown on enclosed schedules, indicated how the sums assessed were made up so that the taxpayer was properly notified as required by para. 4 (1) of Sch. 7 to the 1983 Act.

[41] Although whatever possible, the VAT should, for good practice be allocated to individual periods and a single assessment should be issued covering one or multiple taxable periods by calculating the amount of tax due for each taxable period separately, there will be situations where the making of a single assessment covering a single taxable period or multiple taxable periods will lead to impossible and impracticable results. If a blanket proposition is made that the amount due for any taxable period can only be calculated accurately in regard to each taxable period, so that the assessment must relate to each taxable period separately, the scheme of assessment set out in the VAT Act may produce an unworkable and unreasonable result.

[42] I do not think that it would be necessary to produce a separate piece of paper showing a separate and distinct assessment for each taxable period where the assessor cannot split up and determine the income for each taxable period due to failure of the taxpayer to disclose all the material facts necessary to determine the amount of tax for each taxable period.

[43] The assessor is entitled in case where it is impossible and impracticable to determine and split the assessment up into several taxable periods and calculating the amount due on each period separately, to issue one notice of assessment aggregating several taxable periods, (be it 1, 6 or 12 months) and calculate one total amount of tax due for that particular single taxable period.

[44] I shall now proceed to consider whether the assessor was justified in issuing a single assessment covering several monthly taxable periods, what is generally known as a ‘global assessment’ covering nine taxable periods from 01.04.2010 to 31.12.2010 and another global assessment covering three taxable periods from 01.01.2011 to 31.03.2011 and calculating the total amount due for that whole period without making separate assessments for each of the taxable periods referred to in the notice.

[45] A perusal of the record reveals that the only material available to the assessor to make assessment was the VAT Returns submitted on the basis of estimated amounts and the annual adjustment submitted by the Appellant on **28.06.2013**,

after the lapse of the first and second statutory time bar periods and two days before the end of the third statutory time bar period, together with the turnover schedule and the summary of the audited statement of accounts. (p. 198, 199).

**Concept of Annual Adjustment**

[46] It is to be noted that the VAT Act has introduced the concept of the annual adjustment for the calculation of VAT payable only by "any registered specified institution" referred to in Section 25F of the VAT Act. Section 25C (1) of the VAT Act provides the manner of calculating VAT of any specified institution on the supply of financial institutions. The VAT of any specified institution shall be calculated by including the net profits or loss in accordance with accepted accounting standards, **subject, however, to an adjustment** for economic depreciation and the emoluments payable to all the employees of such institution.

[47] The proviso, however, states that though the amount of profits for each taxable period can be estimated on the basis of available information where it cannot be accurately ascertained, such estimated amounts shall be adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis. Section 25C (1) of the VAT Act as amended by the VAT (Amendment) Act, No. 17 of 2003 reads as follows:

> *"25C (1). Every registered specified institution under this Chapter shall be liable to tax for each taxable period on its total value addition of such institution which includes the new profits or loss, as the case may be, before payment of income tax on such profit computed in accordance with the accepted accounting standards, subject to an adjustment, for economic depreciation, determined by the Minister having regard to the interest of economy by order published in the Gazette, and the emoluments payable to all the employees of such institution:*
>
> *Provided however, where the amount of profits for each taxable period cannot be accurately ascertained, such amount may be estimated on the basis of available information. The estimated amounts shall be adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis and such adjustment shall be submitted within six months after the closing date of the relevant accounting period."*

[48] The Appellant has submitted its annual adjustment in terms of Section 25C (1) for the first nine months from 01.04.2010 to 31.12.2010 and last three months from 01.01.2011 to 31.03.2011 separately and included the figures for two separate periods for nine months and the balance three months. There is nothing to indicate in the annual adjustment that the figures set out in the monthly estimated VAT Returns have been compared with each monthly VAT Returns and the VAT Returns have been adjusted to reflect the actual amounts with the audited statement of accounts on an annual basis.

[49] The assessor has obtained the details for the assessment from the annual adjustment, which does not include accurate figures at all to ascertain the actual amounts of the VAT due on financial services for each taxable period **separately** from 01.04.2010 to 31.12.2010 or from 01.01.2011 to 31.03.2011. There is no comparison or adjustment to the amount set out in the estimated monthly VAT Returns and thus, it was impossible and impractical for the assessor to spilt up and determine the amount of tax due on each nine taxable period from 01.04.2010 to 31.12.2010 and 01.01.2011 to 31.03.2011 **separately**.

[50] The next question is whether the Appellant had sufficient notice of the two assessments made by the assessor for the periods included in the two notices of assessments. A perusal of the two forms of notices of assessments reveals that each is an independent, freestanding notice of assessment that covers the periods from 01.04.2010 to 31.12.2010 and from 01.01.2011 to 31.03.2011. None of them refers to either of the others. Each of them contains figures which apply to the **whole stated periods** (i.e. first nine months and the next three months separately) and none of them is a continuation sheet. None of them contains an amount carried forward to or brought forward from the other one and thus, there is nothing to connect them with each other except for the fact that they cover one financial year from 01.04.2010 to 31.03.2011and the figures have been taken on the basis of the annual adjustment submitted by the Appellant.

[51] The assessor has stated in the intimation letter submitted to the Appellant on 21.03.2014 along with the two separate notices of assessment that the returns have not been accepted for the reasons set out therein. He has further stated that the proportionate rate for total turnover, emolument payable was taken as per the annual adjustment, which together with the turnover analysis schedule has been prepared by the Appellant himself by segregating the value addition for two different periods, for the first 9 months and the next 3 months.

[52] The assessor has calculated the net profit break up for the 1-9 months and the last 3 months separately on the basis of the amounts contained in the annual adjustment and the audited statement of accounts (Vide- page 96), emoluments payable for the purpose of Section 25C(1) (Vide- p. 96) and annual depreciation (p. 96). According to the notice of assessment for the taxable periods from 01.04.2010 to 31.12.2010, VAT assessed for the said periods is Rs, 349,258,339 and the balance payable is nil (Vide- p. 98). According to the notice of assessment for the taxable periods from 01.01.2011 to 31.03.2011, VAT on financial services was Rs. 86,769,980 and after deducting the tax paid and adding the penalty, the total VAT payable is Rs. 76,521,407 (Vide- p. 99).

[53] Notices of assessments have been accompanied by the intimation letter dated 21.03.2014 addreessed to the Appellant. There is no dispute that the Appellant has received both notices of assessments and the said intimation letter.

In the circumstances, the Appellant had sufficient notice of the effect of the two notices of assessments. In my view, the Appellant has been informed in reasonably clear terms of the effect of the assessments for the periods from 9 and 3 months, respectively together with the intimation letter which shows with complete clarity, how that sums were made up and how much the amount due on VAT was calculated under two different periods.

[54] Can the Appellant be prejudiced? No prejudice will be suffered by the Appellant when the assessor makes a single global assessment for a period which aggregates a number of taxable periods based on the annual adjustment submitted by the Appellant and where it is impossible for the assessor to make an assessment for each taxable period separately.

[55] Under such circumstances, I hold that subject to the limitation period, the assessor was justified, to the best of his judgment, in issuing one assessment comprising nine taxable periods from 01.04.2010 to 31.12.2010 and the second assessment, comprising three taxable periods from 01.01.2011 to 31.03.2011, without calculating the amount of tax due for each taxable period separately.

**Question of Law 3**

**Has the Tax Appeals Commission erred in determining that the assessment made under Charge number VATFS/BFSU/2014/579 was valid in law notwithstanding the said assessment which was issued on 27.03.2014 being time barred in terms of Section 33 (1)(a) of the VAT Act?**

**Question of Law 4**

**Has the Tax Appeals Commission erred in determining that the Assessment under Charge No. VATFS/BFSL/2014/580 was valid in law notwithstanding the said Assessment, which was issued on 27.03.2014 covering the taxable periods of January 2011 and February 2011, were time barred in terms of Section 33 (1) of the Vat Act?**

**Time Bar of Assessment**

[56] Section 33 (1) of the VAT Act provides the general rule that the assessment or additional assessment shall be made within 3 years from the end of the taxable period in respect of which the return is furnished or the assessment was made as the case may be. The three-year time bar is applicable in respect of assessment and additional assessments unless the exception under Setion 33 (2) applies. Section 33 (1) reads as follows:

> *"33 (1). Where any registered person has furnished a return under subsection (1) of section 21, in respect of a taxable period or has been assessed for tax*

*in respect of any period, it shall not be lawful for the Assessor where an assessment*

*(a) has not been made, to make an assessment; or*
*(b) has been made, to make an additional assessment, after the expiration of three years from the end of the taxable period in respect of which the return is furnished or the assessment was made as the case may be."*

**Exception**

[57] While the general rule is that the assessment shall be made within three years from the end of the taxable period, where the assessee has wilfully or fraudulently failed to make a full and true disclosure of all the material facts necessary to determine the amount of tax payable by him for any taxable period, an assessment or additional assessment can be made within a period of 5 years. Section 33 (2) reads as follows:

*"(2) notwithstanding the provisions of subsection (1) where the Assessor is of opinion that a person has wilfully or fraudulently failed to make a full and true disclosure of all the material facts necessary to determine the amount of tax payable by him for any taxable period, it shall be lawful for the Assessor where an assessment-*

*(a) has not been made, to make an assessment; or*
*(b) has been made, to make an additional assessment,*

*at any time within a period of five years from the end of the taxable period to which the assessment relates".*

[58] The general rule is that the time limits, which are measured from the end of a prescribed taxable period, run from the end of the first taxable period included in the assessment (*S.J. Grange Ltd v. C & E Commissioners* (supra). Mr. Goonewardena submitted that as the Returns for the taxable periods from 01.04.2010 to 31.12.2010 in accordance with Section 21 (1) quoted above, were furnished on or before the due dates in respect of each taxable periods, the statutory time bar period applicable for the taxable periods from April 01, 2010 to December 31, 2010 is as follows:

| **Taxable period** | **Date of statutory bar** |
|---|---|
| April 2010 | April 30,2013 |
| May 2010 | May 31, 2013 |
| June 2010 | June 30,2013 |
| July 2010 | July 31, 2010 |
| August 2010 | August 31, 2013 |
| September 2010 | September 30, 2013 |
| October 2010 | October 31,2013 |

| | |
|---|---|
| November 2010 | November 30,2010 |
| December 2010 | December 31,2013 |

[59] Mr. Goonewardena further submitted that as the notice was issued in relation to all nine taxable periods on 27.03.2014, the three year time bar was exceeded in respect of all nine taxable periods. He, however, submitted that the annual adjustment and Returns are two different documents. He submitted that where the annual adjustment was not submitted or other information required by the Respondent to accurately quantify the VAT on FS was required, the assessor could have requested same from the Appellant in terms of Section 21 (8) or issued an assessment in terms of Section 21 (8) within the time limit bar period with a penalty.

[60] It is not in dispute that the Parliament has given the assessor sufficient leeway empowering him to discover and obtain any information relevant for the assessment of tax payable by any person and request the taxpayer to produce the information relevant for the assessment. Section 21 (8) of the VAT Act empowers the assessor to notify the taxpayer to furnish to him within the time specified in such notice, fuller or further returns or any further information required for making the assessment. It reads as follows:

> *"8. An assessor may give notice in writing to any person where he thinks, it is necessary, requiring him to furnish within the time specified in such notice-*
>
> *(a) fuller or further returns; or*
> *(b) fuller or further information relating to any matter which in the opinion of the Assessor be necessary or relevant for the assessment to tax payable by such person".*

[61] There is nothing to indicate on the record that the assessor has notified the Appellant to submit the annual adjustment under Section 21 (8) of the VAT Act as submitted by Mr. Goonewardena. Mr. Goonewardena did not, however, dispute the assertion of the Respondent that the annual adjustment which is referred to in Section 25C (1) of the VAT Act was submitted by the Appellant only on **28.06.2013.** It is abundantly clear that the annual adjustment was submitted after the lapse of the statutory time bar period for the month of April, 2010 and May, 2010 and just two days before the end of the statutory time bar period for the month of June, 2010.

[62] The learned Senior State Counsel, however, submitted that the Appellant being a specified institution is liable to pay VAT on the total value addition, which includes the net profits or losses and the computation of such net profits, which is subject to the statutory requirement of annual adjustment. He further submitted that the annual adjustment shall be submitted to the assessor with supporting documents within the time to enable the assessor to make his assessment

accurately to the best of his judgment. He submitted that the non-submission of the annual adjustment on time, automatically entailes the logical consequences of the assessment being delayed. His argument was that where the Appellant has failed to provide the necessary information by way of the statutory annual adjustment within the time in compliance with the provisions of the VAT Act, the Appellant cannot rely on the time bar provision under Section 33 (1).

[63] It is not in dispute that the three year cap in Section 33 (1) is paramount and the assessment for the periods from 01.04.2010 to 31.12.2010 and from 01.01.2011 to 31.03.2011 must fall within the statutory time bar period specified in Section 33 (1). The exception applies where there is a wilful or fraudulent failure to make a full and true disclosure of all the material facts necessary to determine the amount of tax payable by the taxpayer as set out in Section 33 (2). The main points on which the case will be turned are:

1. whether the submission of the annual adjustment is a statutory requirement under Section 25C (1) of the VAT Act to be submitted by the taxpayer as a condition precedent to the assessment to be made by the assessor to the best of his judgment within the limitation period; and
2. If so, whether a taxpayer who fails to submit the annual adjustment in time, disclosing true and full information to determine the amount of tax payable by any specified institution, can seek the benefit of the statutory time bar in Section 33 (1) of the VAT Act.

**Annual Adjustments**

[64] It is significant now to consider the nature, relevance and mechanism provided by the VAT Act for the calculation of VAT payable by any "specified institution" under Section 25C (1) of the VAT Act, which applies only to any "registered specified institution". The provisional input tax claimed by a taxpayer in each tax period in the returns can be revised and adjusted with the provisional tax for each taxable period through a longer period of calculation covering the accounting period on an annual basis, in order to compare the actual input tax eligible to recover during the year, which is known as the "annual adjustment" (VAT Parlial Exemption Tookit, 2017 HM Revenue & Customs, http://assessts.publishing.service.gov.uk). Thus, the annual adjustment uses the values for the whole period in question, comparing the result to the cumulative result of the individual VAT return period calculations and also accounts for any changes in use or intended use during the annual adjustment period (Supra).

[65] The European Court of Justice (Seventh Chamber) in the case *Mydibel SA v. État belge (the Belgian State),* Case C-201/18 (2019) BVC 22, decided on 27.03.2019 concerning the adjustment of a deduction of VAT under Council Directive 2006/112/EC of 28.11.2006 [(OJ 2006 L 347, p. 1] that the VAT

adjustment mechanism provided for in Articles 184 to 186 of the VAT Directive is an integral part of the VAT deduction scheme established by that Directive. The Court observed at paragraph 27:

> *27. The adjustment mechanism provided for in Articles 184 to 186 of the VAT Directive is an integral part of the VAT deduction scheme established by that Directive. It is intended to enhance the precision of deductions so as to ensure the neutrality of VAT, so that transactions effected at an earlier stage continue to give rise to the right to deduct only to the extent that they are used to make supplies subject to VAT. That mechanism thus aims to establish a close and direct relationship between the right to deduct input VAT and the use of the goods or services concerned for taxable output transactions (judgment of 31 May 2018, Kollroß and Wirtl, C-660/16 and C-661/16, EU:C:2018:372, paragraph 55 and the case-law cited).*

[66] The principle behind the annual adjustment and the overall scheme thereof, and the accurate method of calculation were lucidly explained by Justice Mann in the High Court case of *The Commissioners of Her Majesty's Revenue and Customs v. Dunwood Travel Limited* [2007 BVC 406] at paragraphs 7,8 and 24:

> *"7. The principle behind the annual adjustment is to look at the year end calculation for the previous year, ascertain the aggregate of the sales which were subject to relevant rate VAT, and identify what percentage of the whole those constituent parts were. That calculation shows what percentage of total sales represented the relevant rated items (calculated by amount). That percentage is then applied to the total sales for each quarter, presumably on the footing that, from one year to the next, the proportion of relevant rated items in packages is overall likely to be roughly the same. VAT is then calculated and accounted for on that reduced percentage, quarter by quarter;*
>
> *8. Thus the overall scheme requires provisional payments during the course of a financial year, quarter by quarter, based on applying a percentage derived from the previous year's trading to relevant turnover, and charging VAT on that. The final figure for a year is ascertained at the end of the year by doing a more analytical calculation of the year's turnover. Any difference between the amounts provisionally paid and the amounts finally calculated is paid or repaid as the case may be.*
>
> *24 This means that the analysis of the Tribunal is wrong. It is not correct to say that there is an 'annual adjustment' despite the fact that that is a description appearing in the heading to section 8, and certainly not correct to say that- 'The annual adjustment is no more than a method of re-calculating the "prescribed accounting period, or even 're-calculating the amounts due in the previous "prescribed accounting periods" if that is what the Tribunal meant. The year end calculation produces the amount due, and is offset by the provisional figures. The year end calculation is carried out in the "first prescribed accounting period ending after the end of the financial year during*

*which the supplies were made" (TL5 para 4). It cannot be done before then (for obvious logical reasons) but has to be done in that particular period. It therefore becomes a liability calculated, and arising, in that period;*

*31.....What is required to be brought into the adjustment is "the amount of VAT* paid *on the provisional value of those supplies" (my emphasis). It is not the amount of VAT correctly calculated on that provisional value. The wording is clear. It also coincides with common sense".*

[67] What is necessary is that the amounts of tax calculated in the returns to be adjusted to reflect the actual amounts with the audited statement of accounts and sums paid, if any, be deducted from the year end figure or any amount not entered in the Returns to be adjusted to reflect such actual amounts with the audited statement of accounts. Unless the true figures are entered in the annual adjustment with supporting documents, there is no way of ascertaining whether the estimated amounts are accurately adjusted by the specified institution to reflect the actual amounts with the audited statement.

[68] In the first place, it should be examined whether an annual adjustment of the deduction of VAT is a statutory requirement and a condition precedent to the assessment as set out in Section 25C (1). It is to be noted that Section 25C (1) applies only to any specified institution and thus, the calculation of VAT on financial services shall be done in accordance with the statutory provisions set out in Section 25C (1) of the VAT Act. The concept of annual adjustment was not, however, found in the original VAT Act, No. 14 of 2002 and it was brought into effect by the VAT (Amendment) Act No. 7 of 2003. This reflects the purpose and context in which Section 25C (1) was introduced by Parliament to regulate the adjustment mechanism provided for in Section 25C (1) of the VAT Act as an integral part of the VAT calculation and deduction mechanism in relation to a registered specified institution.

[69] Section 25C (1) of the VAT Act refers to the annual adjustment to be submitted by any specified institution and provides that the total value addition of such an institution which includes the net profits or loss which is computed in accordance with accepted accounting standards is **subject to the annual adjustment, for economic depreciation and the emoluments payable to all the employees of such institution.** The matters that shall be taken into accounts and included in the emoluments paid to employees and documents that shall be maintained and taken into account in computing the value addition and the percentage are also included in Section 25C (1) of the Act.

[70] The proviso in the VAT Act as amended by the Value Added Tax (Amendment) Act, No. 9 of 2011 reads as follows:

> ***"Provided however where the amount of profits for each taxable period cannot be accurately ascertained, such amount may be estimated on the basis of available information. The estimated amounts shall be adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis*** and such adjustment shall be submitted within six months after the closing date of the relevant accounting period".

[71] The provisio makes it clear that where the amount of profits for each taxable period cannot be accurately ascertained, such amount may be estimated on the basis of available information, but such estimated amounts **shall be adjusted** to reflect the actual amounts with the audited statement of accounts on yearly basis. This Section clearly provides for a simplified year end calculation by adjusting the estimated amounts with the audited statement of accounts, and it is only at the year end, as a result of the calculation carried out then, that the relevant value is "determined".

[72] Thus, it provides for a simplified year end calculation by adjusting the estimated amounts in the returns and as a result of the calculation carried out, the actual value, including deductions is determined on the basis of such adjustment. Until that is done, in the coming financial year, the provisional value is ascertained in accordance with the available information. The amount of VAT paid on the provisional value of those supplies, **shall be adjusted by the specified institution** on the VAT return for each taxable period ending after the end of the financial year during which the supplies were made.

[73] As the year end calculation will indicate the transactions and the "amount of VAT due", and the difference between the "amount of VAT paid", such difference has to be adjusted on a "return". This means that if a further payment or loss is made, it will have to be entered and adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis. It follows from Section 25C (1), that the initial estimated amount must be adjusted where it is higher or lower than that to which the taxable person was entitled. An adjustment must, in particular, be made where after the estimated VAT Returns are made, some change occurs in the factors used to determine the amount to be deducted. For example, where purchases are cancelled or price reductions are obtained, such deductions shall be adjuted on the estimated amounts in the VAT Returns to reflect the actual amounts with the audited statement of accounts on yearly basis. This is paramount because the tax period can be affected by factors such as the seasonal variations either in the value of the supplies, the taxpayer makes or in the amount of input tax the taxpayer incurs.

[74] I must add that the statutory scheme of the VAT Act in section 25C (1) does not make provisions to waive the requirement of annual adjustment merely because of the claim of a taxpayer that the transactions remain totally or partially unpaid or emempt or zero rated. The statutory requirement of annual adjustment

is not confined to such situations. The annual adjustment must, also be made where transactions remaining totally or partially unpaid, whether it is exempt or zero rated, unless exempt or zero rated is duly proved to the satisfaction of the assessor on facts or confirmed by the assessor.

[75] Section 67 of the VAT Act provides that any person who fails to furnish an annual adjustment under Subsection (1) of Section 25C shall be guilty of an offence under the VAT Act, which further confirms that though the annual adjustment is not part of the return, it is a statutory requirement and an integral part of the VAT calculation and deduction mechanism.

[76] The adjustment is to be done by applying the formula in Section 25C (1), that is to say, the formula which is applied in the year end calculation in the course of carrying out that calculation as specified in the first part of the said section and the proviso. Unlike in Section 28 (1), the manner of calculation of VAT in respect of a "**registered specified institution"** is set out in Section 25C (1) and, Section 25C (1) including its provisio is important because, it contains the obligation to adjust the estimated amounts with the audited statement of accounts on yearly basis and submit such adjusted annual adjustment to the assessor in the manner set out in the said Section.

[77] The Appellant is, however, a specified institution within the meaning of Section 25F of the VAT Act (see- the findings at paragraphs 124-142 of the judgment) and thus, the provisions in Section 25C (1) directly apply to the Appellant as a specified institution. It is manifest from the VAT calculation and adjustment scheme stipulated in Section 25C (1) of the VAT Act that though the annual adjustment is not part of the VAT Return, the Act has imposed a statutory obligation on any registered specified institution to submit the annual adjustment in time to determine the amount of tax payable by the taxpayer before issuing the assessment. The annual adjustment of any specified institution is an integral part of the VAT mechanism established by the VAT Act as amended and is a condition precedent to the assessment of a specified institution as it is intended to enhance the precision and determine the accuracy of the VAT liability of any specified institution, which is essentially a finance company registered under the Finance Companies Act.

[78] In those circumstances, Section 25C (1) of the VAT Act must be interpreted as imposing an obligation on the Appellant to submit the annual adjustment, which is an integral part of the VAT calculation mechanism in Sri Lanka of a specified institution, by adjusting VAT on financial services which was initially deducted incorrectly, where such services are subject to VAT in circumstances such as those described under the Questions of Law 6, 7 and 8.

[79] The learned Senior State Counsel submitted that without the annual adjustment, no assessment is possible and the non-submission of the annual adjustment automatically entailed the logical consequence of the assessment being delayed. The statutory limitation period for the month of April 2010 ended on 30.04.2013, the limitation period for the month of May 2010 ended on 31.05.2013 and the limitation period for the month of June ended on 30.06.2013. Like wise, the limitation periods from July 2010 to March 2011 ended after the expiration of three years from the end of the remaining taxable periods.

[80] The annual adjustment with attached documents in support thereof necessary to make the assessments for the taxable periods April 2010 and May 2010 were made available by the Appellant to the assessor only on **28.06.2013.** The annual adjustment necessary to make the assessment for the taxable period of June 2010 was made available to the assessor only on **28.06.2013**, just 2 days before the end of the limitation period. For the taxable period of July, the assessor had only one month and two days, for August, the asssessor had two months and two days.

[81] Unless the annual adjustment is submitted to the assessor in time with supportive documents, the assessor cannot determine the amount of proficts for each taxable period accurately with the estimated returns, which only relate to the zero rated attributable method whereas the Appellant as a specified institution must declare VAT on the supply of financial services, which is incomplete and incorrect. In my view, the Appellant has failed to fulfil its statutory obligation imposed by the VAT Act and defaulted in submitting the annual adjustment in time with the necessary documents. The natural consequence of such default was that the assessment was delayed as the Appellant had not disclosed all the material facts together with the annual adjustment in time, to enable the assessor to make proper assessment in his best judgment.

[82] Mr. Goonewardena complains about the failure of the assessor to give notice under Section 21(8) requesting the Appellant to submit the information relevant for the assessment. In my view, the annual adjustment is a document that shall be prepared by the Appellant according to the method of calculation and adjustment laid down in Section 25C (1). The assessor is not required to do the work of the taxpayer and the statutory obligation imposed on him under the provisions of the VAT Act. Any failure on the part of the assessor to give notice in writing to the Appellant under Section 21 (4) and require him to furnish the annual adjustment in time will not absolve the Appellant being a specified institution from fulfilling its statutory obligation of submitting its annual adjustment with the supportive documents in time as required by Section 25C (1) of the VAT Act.

[83] As regards the Question of Law No. 5, Mr. Goonewardene sought to argue that though the assessment for the periods from 01.01.2011 to 31.03.2011 has

been made by the assessor on the basis that such periods involve multiple tax periods, but the relevant taxable period from 01.01.2011 is a period of six months as specified in section 25B (1)(b) by virtue of the Value Added Tax (Amendment) Act, No. 09 of 2011. He submitted that the period from 01.01.2011 to 31.03.2011 is only part of a period which is not considered a taxable period and as such, the assessment issued for the periods from 01.01.2011 to 31.03.2011 is time barred under section 33 (1) of the VAT Act.

[84] I observe however, that the Appellant has never raised the time bar objection in respect of the notice of assessment made for the periods from 01.01.2011 to 31.12.2011 in its appeal filed before the Tax Appeals Commission under Charge No. VATFS/BFSL/2014/580. The Appellant has only raised the time bar objection in respect of the assessment made for the taxable periods from April 2010 to December 2010 under Charge No. VATFS/BFSL/2014/579 (Vide-the written submissions filed on behalf of the Appellant before the Tax Appeals Commission on 30.04.2019, paragraph 'b') and written submissions dated 06.06.2019, paragraph 3). The Tax Appeals Commission has thus, considered the time bar objection for the taxable periods from 01.04.2010 to 31.12.2010 and held that the assessment made in respect of that assessment is not out of time.

[85] The relevant taxable period from 01.01.2011 is a period of six months as specified in Section 25B (1)(b) by virtue of the Value Added Tax (Amendment) Act, No. 09 of 2011. The said Amendment Act however, came into effect only on 31.03.2011 and by that time, the Appellant had already furnished monthly returns under the provisions of the VAT (Amendment) Act, No. 2 of 2003, which refers to the taxable period as one month as specified in Section 25B. Accordingly, the Appellant could not have furnished its returns for a period of 6 months in terms of Section 25B (1) (b) of the VAT (Amendment) Act, No. 09 of 2011. The returns had been furnished only in respect of the period covering from January 2011 to March 2011 and a global assessment has been made for a period covering 3 months for the reasons described under Questions of Law Nos. 1 and 2. For those reasons, I hold that there is no substance in the argument that the assessment had been made for a part of the taxable period of 6 months as requried by the Value Added Tax (Amendment) Act, No. 09 of 2011.

[86] The only other question to be decided is whether such failure to submit the annual adjustment constitutes a wilful or fraudulent failure to make a full and true disclosure of all the material facts necessary to determine the amount of tax payable by the Appellnat as set out in Section 33 (2).

**Willful or fraudulent failure to make a full and true disclosure of all the material facts necessary to determine the amount of tax**

[87] The learned Senior State Counsel referred to the decision of this Court *in HSBC Entronic Data Processionf Lanka (Pvt) Ltd, v. The Commissioner General of Inland Revenue,* CA/Tax/17/2013, decided on 12.05.2021 and submitted that the 3 year cap will not apply where there has been a failure to provide necessary information. In *HSBC Entronic Data Processionf Lanka (Pvt) Ltd, v. The Commissioner General of Inland Revenue* (supra), the Court of Appeal held that the letter of intimation dated 21.02.2007 explains that the Appellant has failed to provide information on the time of supplies and thus, it was justifiable on the part of the assessor to invoke the amended Section 33 (2) of the VAT Act and make a singular assessment for the entire calender year 2004.

[88] Mr. Goonewardena submitted that the State has taken this new position for the first time in appeal and thus, the State is now prevented from relying on Section 33 (2) of the VAT Act at this stage of the appeal. I find however, that the Respondent has raised this issue in the written submissions filed in the appeal proceedings before the Commissioner General and stated that as the Appellant has failed to fulfil its legal obligation of filing the annual adjustment within time as required by Section 25C (1) after the closing of the relevant accounting period, the limitation of time for assessment as mentioned in Section 33 (1) is not applicable (p. 126 of the record). I further find that the Tax Appeals Commission has, taken the view that as the Appellant has not furnished the information necessary to calculate and assess the financial VAT in time as stipulated in the VAT Act, the Apppellant cannot seek the benefit of the statutory time bar:

> *"unless the taxpayer provides such information in time as stipulated in the statute, the officials of the Inland Revenue Department are not in a position to calculate the tax liability and issue the assessment within the time period stipulated in the statute. In this case it is clear in respect of certain VAT returns, the required documents have been submitted to the CGIR even after the statutory time bar period.....one should not be allowed to avoid tax liability under the guise of the statutory time bar, by not providing the necessary information in time to calculate the relevant tax liability. Therefore it is our view that the Apppellant cannot seek the benefit of the statutory time bar for the taxable periods from April to December 2010, as he has not furnished the information that were necessary to calculate and assess the financial VAT as stipulated in the VAT Act."*

[89] It is quite clear that even though no reference was made to section 33 (2), the Tax Appeals Commission has held that where the taxpayer failed to provide all material information in time necessary to calculate and assess the financial VAT, the limitation period in Section 33 (1) has no application and thus, we have to look at the applicability of Section 33 (2) of the VAT Act. I must emphasise however, that Section 33 (2) requires the assessor to form an opinion that the taxpayer has wilfully or fraudulently failed to make a full and true disclosure of all the material facts necessary to determine the amount of tax. The word "willful" has not been

defined under the VAT Act. In *Reg v. Senior* (1899) 1 QB 283, Lord Russell, explains “wilfully'” to mean:

> *“that the acts if done deliberately and intentionally not by accident or inadvertence, but so that the mind of the person who does the acts goes with it.*

[90] In *In re YOUNG AND HARS-TON'S CONTRACT'* (1886) 31 Ch D 168, Bowen, L.J., explained the word "wilful" which has been accepted and applied in subsequent cases, as follows:

> *“It (i.e., the word 'wilful') generally, as used In Courts of law, implies nothing blamable, but merely that the person of whose action or default the expression it used, is a free agent, and that what has been done arises from the spontaneous action of his will. It amounts to nothing more than this, that he knows what he is doing and intends to do what he is doing, and is free agent”.*

[91] In the Indian case of *E.I. Rly. Co. v. Ahmed Ali Mohammad AIR* (14) 1921 Nag 34, the question was whether a railway company was guilty of willful neglect. The learned Judge said.

> *“that the term willful neglect implies an intentional and purposeful omission to do a certain act and, it is an even more extreme term than gross and culpable negligence”.*

[92] In *Re: T.N.K. Govindarajulu v. Unknown*, 1951 1952 CriLJ 1063, Subba Rao, J. held at paragraph 10 in the context of tax evasion:

> *“In my view, this construction which leads to startling results should not be accepted unless the words in the statute are clear and unambiguous. Not only I do not see any such words but to my mind the word wilful used in the section was intended only to hit at intentional omissions of an assessee with full knowledge that the item omitted is a taxable one”.*

[93] In *Chellappah v. Commissioner of Income Tax* 52 NLR 416 at 418, Basnayake J. (as he was then) held that ordinarily, the word “wilfully” means deliberately or purposely without reference to bona fides but that in penal statutes, it is used in a sense denoting deliberatively or purposely and with an evil intention. In *HSBS Electronic Data Processing Lanka (Pvt) Ltd v. The Commissioner General of Inland Revenue* (supra), Janak Silva J. relying on the interpretation given by Basnayaka J. (as he was then) held that the VAT Act being a fiscal rather than a penal statute, the word “wilfully” in section 33 (2) means deliberately or purposlely without reference to bona fides.

[94] Mr. Goonewardena however, submited that for a valid assumption of jurisdiction under Section 33 (2), the assessor has to form an opinion that the

Appellant has wilfully or fraudulently failed to disclose fully and truly all material facts which were necessary for the assessment but not otherwise. There is nothing in section 33 (2) to indicate that the assessor shall indicate his opinion in specific language and in specific manner in writing. The formation of assessor's opinion can be gathered from the language used in any notice or any intimation letter sent by him to the taxpayer supported by the contents of the record maintained by the Respondent.

[95] On the other hand, the annual adjustment shall be submitted to the assessor with supporting documents, and unless all the necessary documents are submitted with the annual adjustment in time to enable the assessor to make an assessment within the limitation period, it would be impossible for the assessor to assess the taxpayer accurately. In the present case, the assessor has stated in the intimation letter that the annual adjustment contains incorrect figues such as (i) the net profits for the purpose of calculating VAT on the supply of financial services are not provided in the annual adjustment; (ii) incorrect emolument payments have been taken into account in the annual adjustment; and (iii) value addition to financial services has been wrongly computed in terms of Section 25C(5) on the supply of financial services.

[96] On the face of the annual adjustment, the figures in the annual adjustment contains incorrect figures and the figures in the estimated VAT retuns have not been adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis referring to each taxable period from 01.04.2010 to 31.03.2011. This has made it impposible for the assessor to spilt up the amount and determine the amount of tax payable by the Appellant for each taxable period. As noted, this has clearly resulted in the assessor issuing global assessments covering several taxable periods from 01.04.2010 to 31.12.2010 (9 months) and from 01.01.2011 to 31.03.2011 (3 months).

[97] It is not in dispute that the Appellant has submitted the annual adjustment only on **28.06.2013** and thus, the Appellant has delayed in submitting the annual adjustment together with the necessary documents. The natural consequence was that the assessments were also delayed. A perusal of the record reveals that the audited statement of accounts submitted by the Appellant marked 'B' contains notes of the financial statements (p. 198) with the turnover analysis marked 'A' only for **three months ended 31.03.2011** (p. 199).

[98] Apart from the VAT returns claiming only zero rated supplies, notes of the audited financial statement and a turnover for a period of only three months ended 31.03.2011 are provided with the adjustment, no other material documents were made available by the Appellant to the assessor to make a proper assessment. This position is further confirmed by the letter of the Appellant sent to the Respondent on 17.09.2014, after the appeal was lodged and the statutory time

bar period ended. The Appellant, in response to a written request made by the Respondent**,** has submitted the following documents to the Respondent for the settlement of the appeal:

1. Activity wise breakups for (a) bad debt recovered; (b) other gain and charges; (c) bad debt recovered; (d) bad debt write offs; (e) disposal losses; and bad debts provisions; and
2. Activity wise breakups for VAT declared representing liable and exempt activities.

[99] It is absolutely clear that the material documents including the activitiy wise breakups for VAT declared, representing liable and exempt activities for the determination of the VAT liability were in the custody of the Appellant but they were not disclosed to the assessor trully and fully in time to enable the assessor to determine the amount of tax payable by the Appellant with the annual adjustment. It is clear from the record that the assessor had no evidence of facts sufficient to make an early assessment as all the necessary information with all relevant documents had not been disclosed to the assessor in time to make the assessment in time. What is the explanation for the delay? No explanation was offered.

[100] Can the Appellant now complain that he provided all the information including the annual adjustment in time in compliance with his statutory obligation imposed by Section 25C (1) of the VAT Act, but the assessor having had all such information delayed in making the assessment, which is wholly unreasonable or perverse? In my view, the Appellant has wilfully (deliberately and purposely without reference to bona fides) failed to make a full and true disclosures of all the material facts necessary to determine the amount of tax payable by it for the relevant periods from 01.04.2010 to 31.03.2011.

[101] In my view, the taxpayer cannot invoke the time bar objection against his own wilful, deliberate and negligent act of failing to submit all the material facts, including the statutory annual adjustment in time, necessary to determine the amount of tax payable by him for the taxable periods in question, in compliance with his statutory obligation imposed by the VAT Act. In the result, the assessor was justified in invoking Section 33 (2) of the VAT Act in making one assessment for the periods from 01.04.2010 to 31.12.2010 and one assessment from 01.01.2011 to 31.03.2011. Accordingly, the assessments made in respect of the said two periods fall within the meaning of Section 33 (2) of the VAT Act. For those reasons, I hold that the assessments dated 27.03.2014 are not time barred.

**Question of Law 5**

**Should the Tax Appeals Commission have determined that the appeal which was made by the Commissioner-General of Inland Revenue under section 34 (1) in respect of the assessments under charge numbers VATFS/BFSU/2014/579 and VATFS/BFSU/2014/580 be deemed to have been allowed in terms of the second proviso to section 34 (8) of the VAT Act in view of it not having been determined by the Commissioner General within 2 year period specified therein?**

[102] Mr. F.N.Goonewardena next submitted that the Appellant filed two separate appeals on 29.04.2014 to the Commissioner-General of Inland Revenue in respect of both notices of assessments but the acknowledgement of the appeal was signed by the assessor without any authority of the Commissioner-General of Inland Revenue. It was urged by Mr. Goonewardena that the legislative intent reflected in Section 34 of the VAT Act is that once an appeal is made to the Commissioner-General, every action in relation to such appeal shall be taken by the Commissioner-General himself unless the authorisation to make such acknowledgement is specifically delegated by the Commissioner-General to the assessor.

[103] His contention was that as the appeal was not properly acknowledged under Section 34 of the VAT Act, it shall be deemed to have been received by the Commissioner-General on 29.04.2014 in terms of the statutory time bar provided in Section 34 (8) and as the appeal was determined by the Respondent on 14.05.2006, after the expiration of the two year period, the determination of the appeal was time barred under section 34 (8) of the VAT Act.

[104] On the other hand, the learned Senior State Counsel countered the submission of Mr. Goonewardene and submitted that as the two appeals had been made on 29.04.2014 and the Appellant has not disputed the fact that the acknowledgement was received on 27.05.2014, the appeals had been duly acknowledged by the Respondent under Section 34 (8) of the VAT Act. He submitted that it is not envisaged in 34 (8) of the VAT Act that the Commissioner-General himself should sign the acknowledgement of the appeal and the validity of the acknowledgement is not conditional upon the same being signed by the Commissioner-General. He strongly relied on the decision of this Court in *Lanka Ashok Leyland PLC v. The Commissioner of Inland Revenue,* CA Tax 14/2017, decided on 14.12.2018 in support of his contention that the Inland Revenue Act does not indicate expressly that the Commissioner-General himself should sign the acknowledgement of the appeal.

[105] In view of the rival submissions made by the parties pertaining to the acknowledgement of the appeal made to the Commissioner-General, the following issues arise for consideration under this question of law:

(a) Firstly, whether the Commissioner-General himself should sign the acknowledgment of the receipt of the appeal under the second proviso to Section 34 (8) of the VAT Act and if so, whether the acknowledgement of the appeal signed by the assessor is valid in law; and

(b) Secondly, even if the Commissioner-General himself need not sign the acknowledgement, whether the authority needs to be specifically delegated by the Commisssioner-General to the assessor for such acknowledgement to be valid in law; and

**Statutory Provisions on Acknowledgement of Appeal under the VAT Act**

[106] Section 34 (1) of the VAT Act confers on the assessee a right of appeal against any assessment or additional assessment made in respect of him or a penalty imposed under the VAT Act to the Commissioner-General of Inland Revenue within 30 days after the service of notice of such assessment or additional assessment or imposition of penalty. The relevant provisions of Section 34 relating to the appeals to the Commissioner-General are reproduced for clarity as follows:

> *"(1) Any registered person, may, if he is satisfied with any assessment or additional assessment made in respect of him by an Assessor, or a penalty imposed under this Act, appeal against such assessment, additional assessment or penalty, as the case may be, to the Commissioner-General within thirty days after the service of notice of such assessment, additional assessment or imposition of penalty as the case may be. Such person shall, notwithstanding the appeal, but subject to subsection (2) of section 26 pay the tax charged by such assessment or additional assessment together with any penalty imposed on him by this Act:*
>
> *Provided that, the Commissioner-General, upon being satisfied that, owing to absence from Sri Lanka, sickness or other reasonable cause, the appellant was prevented from appealing within such period, shall grant an extension of time for preferring the appeal.*
>
> *(2) Every appeal shall be preferred by a petition in writing addressed to the Commissioner-General and shall state precisely the grounds of such appeal.*
>
> *(6) On receipt of a valid petition of appeal, the Commissioner-General may cause further inquiry to be made by an Assessor, other than the Assessor who made such assessment against which the appeal is preferred and if in the course of such inquiry an agreement is reached as to the matters specified in the petition of appeal, the necessary adjustment of the assessment shall be made.*
> *(8).....*
>
> *Provided further, that every petition of appeal under this Chapter shall be agreed to or determined by the Commissioner-General within two years from*

*the date on which such petition of appeal is received by the Commissioner-General, unless the agreement or determination of such appeal depends on the furnishing of any document or the taking of any action by any person other than the appellant or the Commisioner-General or an Assessor. Where such appeal is not agreed to or determined within such period the appeal shall be deemed to have been allowed and the tax charged accordingly.* ***The receipt of every appeal shall be acknowledged (within thirty days of its receipt*** *and where so acknowledged, the date of the letter of acknowledgement shall for the purpose of this section, be deemed to be the date of receipt of such appeal).* ***Where however the receipt of any appeal is not so acknowledged, such appeal shall be deemed to have been received by the Commissioner-General on the day on which it is delivered to the Commissioner-General"*** [Emphasis added].

[107] In terms of the second proviso to Section 34 (8) of the VAT Act, the date of receipt of appeal by the Commissioner-General shall be regarded as follows:

(a) If the receipt of the appeal is acknowledged within 30 days of its receipt, the date of acknowledgement of the appeal shall be the date of receipt of appeal;
(b) If the receipt of the appeal is not so acknowledged, the appeal shall be deemed to have been received by the Commissioner-General on the date on which the appeal is delivered to the Commissioner-General.

**Date of Acknowledgement of Appeal**

[108] The determination of the Tax Appeals Commission in relation to this question of law is based on the scheme of Section 34 (8) of the VAT Act as amended in its context wherein it has held:

*"It is to be noted that according to section 34(8) of the VAT Act, the legislature has purposesly and intentionally used the passive form in stating that "receipt of every appeal shall be acknowledged instead of the person, whether the Assessor or the Commissioner-General who does it. There is no reference in this section, that the Commissioner-General should acknowledge the appeal. Further, section 34 (6) of the Revenue Act, states that on receipt of a valid petition of appeal, the Commissioner-General may cause further inquiry to be made by an Assessor, other than the Assessor who made such assessment against which the appeal is preferred.....(p. 3)*

*Further, the Assessor who signed the acknowledgement, will make further inquiry to settle the appeal. This procedure fulfils the requirements of the VAT Act and the said inquiry is made by an Assessor who is statutorily empowered by the Commissioner-General. Therefore, it would appear that, the intervention of the Commissioner-General is necessary only where a decision has to be made by the Commissioner-General and not in situations such as informing the Appellant with regard to the acknowledgement of the appeal...(page 4)... In the circumstances, we are of the view that the*

*determination of the Respondent is not time barred, since the appeal was acknowledged on 27.05.2014 and the determination was made on 09.05.2016" (p. 5).*

[109] There is no dispute that the Appellant has delivered the appeals to the Commissioner-General on 29.04.2014 and the Appellant received the acknowledgement of the appeals by letters dated 27.05.2014 (pages 24 and 25 of the brief). A perusal of the said letters of acknowledgement of the appeal dated 27.05.2014 reveals that they had been signed by the senior assessor Mr. R.D.M.S. Muhandiram and addressed to the Appellant. It reads *inter alia*, as follows:

*"1. I hereby acknowledge the receipt of your appeal made by the letter of 29.04.2014 against the assessment of Value Added Tax for the aforesaid taxable period.*

*2. Kindly note that in terms of section 34(8) of the Value Added Act, No. 14 of 2002 the date of the receipt of your appeal shall be the date of this letter of acknowledgement, which is 27.05.2014 and the period of two years within which your appeal shall be agreed or determined will end on 26.05.2016.*

*3. The Commissioner-General of Inland Revenue has in terms of section 34 (6) of the Value Added Act directed me to make further inquiry into your appeal.*

*4. Please be noted that as decided by the Commissioner-General in terms of section 34(6) of the Value Added Act:*

*(a)...*

*(b) A payment of Rs. 2,189,004 out of the tax assessed has been deferred and the balance of Rs. 43, 908,229 should be paid.*

*Yours faithfully,*

*Senior Assessor"*
*Sgd*

[110] It would be apt at this stage to consider the decision of this Court in *Lanka Ashok Leyland PLC v. The Commissioner-General of Inland Revenue* (Supra), which was relied on by the learned Senior State Counsel in support of his contention that it is not necessary for the Commissioner-General himself to sign the acknowledgement, which is only an administrative task. In *Lanka Asok Leyland PLC v. The Commissioner-General of Inland Revenue* (Supra), the identical issue arose whether the acknowledgement of the appeal should have been signed by the Commissioner-General of Inland Revenue himself and if the appeal is not so acknowledged, whether the appeal shall be deemed to have been received by the Commissioner-General on the day on which it is delivered to the Commissioner-General. The Court of Appeal held that although the appeal has to be submitted to the Commissioner-General, there is no requirement that the acknowledgement must be made by the Commissioner-General himself. His Lordship Janak de Silva, J. stated at page 6:

*"Court is of the view that there is no merit in the submission of the Appellant that the acknowledgement must be signed by the Respondent. The functions of the Inland Revenue Department are so multifarious that no Commissioner-General of Inland Revenue could ever personally attend to all of them. In particular, Court will be slow to impose such requirements unless there is unequivocal language in the IR Act. It is true that the appeal has to be submitted to the respondent. However, that does not mean that the acknowledgement to be made by the respondent. A similar approach has been taken by our Courts in applying the Carltona principle in relation to administrative functions to be performed by Ministers (M. S. Perera v. Forest Department and another [(1982) 1 Sri. L.R. 187] and Kuruppu v. Keerthi Rajapakse, Conservator of Forests [(1982) 1 Sri. L.R. 163]".*

[111] The question of acknowledgement falls entirely within the purview of Section 34 (8) of the VAT Act, which stipulates the period within which the receipt of the appeal shall be acknowledged and where so acknowledged or not acknowledged, as the case may be, the consequences thereof. On a careful reading of Section 34 (8), it is patently clear that it does not state in unequivocal language that the Commissioner-General himself should sign the acknowledgement and if it is not so acknowledged, the date of the letter of acknowledgement shall, for the purpose of Section 34 (8), be deemed to be the date of the receipt of such appeal.

[112] It is to be noted that an identical issue under the Inland Revenue Act, No. 10 of 2006 arose in the case of *Polycrome Electrical Industries (Pvt) Ltd, v. The Commissioner-General of Inland Revenue* (CA/TAX/0049/2019), decided on 26.03.2021 wherein I stated at paragraph 19:

*"In this modern-day administration, with expansion of powers and multifarious functions exercised by public officers, the Commissioner-General cannot be expected, as the head of the Inland Revenue Department to attend to all and perform each and every function himself. As there may be thousands of taxpayers in Sri Lanka, it cannot be expected that the Commissioner-General shall perform each and every task himself, unless the Inland Revenue Act itself has specifically empowered to him to exercise such function personally I do not see any such intention reflected in the language, scope or object of section 165 (6) of the Act. I do not think that the Parliament intended such a result".*

**Delegation of Power**

[113] In view of Mr. Goonewardena's second argument, the question arises for consideration whether there needs to be an explicit power to delegate or whether an implied power to delegate exists. The intention of the legislature in a taxation statute is to be gathered from the words or language used in the provision and accordingly, it is not possible to assume any intention or governing purpose of the statute, more than what is stated in the plain language (P. M. Bakshi, Interpretation of Statutes, 1st Ed. 2011, p. 512). The question of delegation of authority, however, arises where the Commissioner-General entrusts or delegates

another with authority by empowering such other person to act or do things which otherwise, he himself would have to do. In *Sidhartha Sarawagi v. Board of Trustees for the Port of Kolkata and others* [(2014) 16 SCC 248], the Indian Supreme Court, while dealing with the issue of delegation of authority, observed:

> *"2-Delegation is the act of making or commissioning a delegate. It generally means of powers by the person who grants the delegation and conferring of an authority to do things which otherwise that person would have to do himself. Delegation is defined in Blacks Law Dictionary as the act of entrusting another with authority by empowering another to act as an agent or representative. …Delegation generally means parting of powers by the person who grants the delegation, but it also means conferring of an authority to do things which otherwise that person would have to do himself."*

[114] Mathew J. in *Gwalior Rayon Silk Manufacturing (Wvg.) Co. Ltd. v. The Assistant Commissioner of Sales Tax and others,* 1974 AIR 1660, has succinctly discussed the concept of delegation at paragraph 37:

> *"37-Delegation may be defined as the entrusting, by a person to another person or body of persons, of the exercise of a power residing in that person or body of persons, to another person or body of persons, with complete power of revocation or amendment remaining in the grantor or delegator. ……It is important to grasp the implications of this, for, much confusion of thought has unfortunately resulted from assuming that delegation involves or may involve, the complete abdication or abrogation of a power. This is precluded by the definition.* ***Delegation often involves the granting of discretionary authority to another, but such authority is purely derivative****. The ultimate power always remains in the delegator and is never renounced"* [Emphasis added].

[115] A Statute will generally provide the answer as to whether a power must be performed personally by those to whom they have been given or whether such power can be delegated to another. As noted, there is no express provision in the VAT Act that authorises the Commissioner-General to sign the acknowledgement of the appeal personally or delegate his power to another officer of the department authorising him to sign the acknowledgement. In this context, the question of delegation will not arise, unless the Commissioner-General has been authorised by express words to sign the letter of acknowledgement himself. It is to be noted that the nature of the duty to be exercised here is merely to acknowledge the appeal and the character of the person involved is the Commissioner-General who is the head of the Department.

[116] ] In view of the submission made by Mr. Goonewardena, I shall now consider the question whether a delegation of power can be implied from the scheme and objects of the VAT Act. In *Polycrome Electrical Industries (Pvt) Ltd, v. The Commissioner-General of Inland Revenue* (supra), *this Court considered the question whether* a delegation of power can be implied from the scheme and

objects of the Inland Revenue Act, which has identical provision to the VAT Act, and the character of the power to be delegated and the circumstances, when the power is able to be exercised. In *Polycrome Electrical Industries (Pvt) Ltd, v. The Commissioner-General of Inland Revenue* (supra), at paragraph 24, I stated:

> *"[24] As there may be thousands of taxpayers in Sri Lanka, the head of the Department of Income tax cannot be expected to discharge personally all the duties of administrative nature which can be performed by the officials of the Department in the exercise of statutory powers referred to in section 165 (6). I do not think that the acknowledgement signed by the officials of the Department acting under authorisation of their superior officers in the exercise of the statutory duty conferred by section 165 (6) is invalid where no express or implied delegation of authority authorising the officials to sign the acknowledgement is reflected in the scheme of the Inland Revenue Act. I do not think that the Parliament intended such a result".*

[117] Mr. Goonewardena drew our attention to a case reported in *Carltona Ltd. v. Commissioners of Works,* (1943) 2 All E R 560 and while seeking to distinguish the principle established in *Carltona Ltd. v. Commissioner of Works* (supra) from the facts of the present case, referred to the following statement made by Lord Green, M.R. in the said case:

> *"The duties imposed upon ministers and the powers given to ministers are normally exercised under the authority of the ministers by responsible officials...Constitutionally, the decision of such officials is, of course, the decision of the Minister".*

[118] Mr. Goonewardena's submission was that the official in *Carltona Ltd. v. Commissioner of Works* (supra) signed *"for and on behalf of the Commissioner of Works*" and therefore, the actions of the official are the actions of the Commissioner of Works himself. He submitted, however, that assessor could have only signed *'for and on behalf of the Commissioner-General'*-"*Qui facit per alium facit per se"* which means "He who acts through another does the act himself". He contended that unlike in the case of *Carltona Ltd. v. Commissioner of Works* (supra), the assessor in the present case had signed on his own behalf when exercising the authority of the Commissioner-General of Inland Revenue and consequently, for the acknowledgement of the appeal to have been valid, the assessor should have signed it "*for and on behalf of the Commissioner-General of Inland Revenue".*

[119] Greene, M.R. in *Carltona Ltd. v. Commissioners of Works,* (supra) explained broadly the principle at page 560 as follows:

> *"In the administration of government in this country, the functions which are given to ministers (and constitutionally properly given to ministers, because they are constitutionally responsible) are functions so multifarious that no minister could ever personally attend to them. To make the example of the*

*present case, no doubt there have been thousands of requisitions in this country by individual ministries. It cannot be supposed that this regulation meant that in each case, the minister in person should direct his mind to the matter.* ***The duties imposed upon ministers and the powers given to ministers are normally exercised under the authority of the ministers by responsible officials of the department. Public business could not be carried on if that were not the case.*** *Constitutionally, the decision of such an official is, of course, the decision of the minister. The minister is responsible. It is he who must answer before Parliament for anything that his officials have done under his authority, and, if for an important matter, he selected an official of such junior standing that he could not be expected competently to perform the work, the minister would have to answer for that in Parliament. The whole system of departmental organisation and administration is based on the view that ministers, being responsible to Parliament, will see that important duties are committed to experienced officials. If they do not do that, Parliament is the place where complaint must be made against them"*.[Emphasis added].

[120] In interpreting the Carltona doctrine, this Court in *Polycrome Electrical Industries (Pvt) Ltd, v. The Commissioner-General of Inland Revenue* (supra) referring to *Kuruppu v. Keerthi Rajapaksha, Conservator of Forests* (supra), *Commissioners of Customs and Excise v. Cure & Deeley Ltd.* (1962) 1 QB 340, 371*, In Re University of Sydney* [1963] S.R. N.S.W. 723, 733, *Minister for Aboriginal Affairs v. Peko-Wallsend (1986)* 162 and *Re Golden Chemical Products Ltd*. (1976) Ch. 300*CLR 24* and stated in paragraphs 28, 29, 31, 32,33 and 34 as follows:

*"[28] The Carltona doctrine applies where a statute has conferred a power on a Minister, and it is practically impossible for the Minister to exercise such power personally, he may, in general, act through a duly authorised officer of his department without having a formal delegation to do so. It recognises the principle that the functions of a Minister are so multifarious that the business of government could not be carried on if he was required to exercise all his powers personally. Thus, the official is treated as the minister's alter ego, and to that extent, his decision is regarded as those of the Minister".*

*"[29] The same principle was applied in Kuruppu v. Keerthi Rajapaksha, Conservator of Forests* (supra). *The question arose inter alia, as to whether it was competent for the Conservator of Forests to specify the area within into or out of which no timber of any species could be transported without a permit from an authorised officer. Rodrigo, J. who quoted the following passage from De Smith's Judicial Review of Admistrative Action, 2nd Ed. Pp. 290 & 291 at pages 168 and 169:*

*"Special considerations arise where a statutory power vested in a Minister or department of State is exercised by a departmental official. The official is the alter ego of the Minister or the Department and since he is subject of as to the fullest control by his superior he is not usually spoken of as a*

*delegate…..The Courts have recognized that duties imposed on Ministers and the powers given to Ministers are normally exercised under the authority of the Ministers by responsible officials of the department…….In general, therefore, a Minister is not obliged to bring his own mind to bear upon a matter entrusted to him by statutes, but may act through a duly authorized officer of his department".*

*[31] It is to be noted that the Carltona principle does not confine to Ministers and it has been judicially recognised in Commissioners of Customs and Excise v. Cure & Deeley Ltd. (1962) 1 QB 340 at p 371 that the Commissioners of Customs and Excise were in a position parallel to that of Ministers:*

*"The Commissioners are in a position parallel to that of the Ministers referred to in the judgment of Lord Greene in the Carltona case [1943] 2 All ER 560 at 563, in that their functions are so multifarious that they could never personally attend to them all, and the powers given to them are normally exercised under their authority by responsible officials of the department.[45]".*

*[32] In Re University of Sydney [1963] S.R. N.S.W. 723, at p 733, the Senate of a University was regarded as being in a similar situation. The Carltona principle may, in my view apply in appropriate circumstances where the Government officials or bodies are authorised by their superior officers to carry out certain administrative or routine tasks without having a formal delegation to do so. Because, it is almost impossible for the head of a department in the Public Service to discharge personally all the duties which are conferred by a Statute otherwise than his officers responsible to him unless it is stated in the Act in unequivocal language that such duties shall be exercised by the head of the department personally. As Mason, J. referring to the Carltona principle observed in Minister for Aboriginal Affairs v. Peko-Wallsend (1986) 162 CLR 24 at paragraph 12:*

*"The cases in which the principle has been applied are cases in which the nature, scope and purpose of the function vested in the repository made it unlikely that Parliament intended that it was to be exercised by the repository personally because administrative necessity indicated that it was impractical for him to act otherwise than through his officers or officers responsible to him".*

*[33] In Re Golden Chemical Products Ltd*. (1976) Ch. 300 at p. 20, it was observed:

*"Yet I find the logic of the principle equally persuasive in its application to the head of any large government department, and, a fortiori, to a Deputy Commissioner of Taxation responsible within a State for the implementation of the Commonwealth's laws with respect to taxation. No permanent head of a department in the Public Service is expected to discharge personally all the duties which are performed in his name and for which he is accountable to the responsible Minister".*

*[34] Those authorities established that when a Minister is entrusted with administrative functions he may, in general, act through a duly authorised officer of his department. The same principle applies to the Commissioner-General of Inland Revenue, who as the head of a department, is not expected to discharge personally all the duties otherwise through his responsible officers where the relevant power, duty or function is of an administrative nature or routine.".*

**Acting under authorisation of the Superior Officers**

[121] The acknowledgement letters dated 27.05.2014 further indicate that the Commissioner-General of Inland Revenue has, in terms of Section 34 (6) of the VAT Act, has directed the senior assessor, Mr. R.D.M. S. Muhandiram to make further inquiry into the appeal. The senior assessor who had been nominated to make a further inquiry into the appeal, has signed and acknowledged the receipt of the appeals made by the Appellant under Section 34 (8) of the VAT Act.

[122] The definition of "Commissioner-General" in section 83 of the VAT Act means "the Commissioner-General of the Inland Revenue appointed under the Inland Revenue Act, No. 38 of 2000, and includes a Commissioner, and a Deputy Commissioner specifically authorised by the Commissioner-General either generally or for a specific purpose to act on behalf of the Commissioner-General". The definition of "Assessor" in Section 83 of the VAT Act means an Assessor or a Senior Assessor appointed under the Inland Revenue Act, No. 38 of 2000. By the VAT (Amendment) Act, No. 7 of 2014, the word "Assessor" was substituted with the words "Assessor or Assistant Commissioner".

[123] It is patently clear that the senior assessor who is appointed under the Inland Revenue Act, has performed an administrative function conferred by Section 34 (8) of the Act and signed the acknowledgement letter, acting under the authorisation of his Superior Officers rather than performing any discretionary power in terms of the provisions of the VAT Act. In the result, the absence of any reference in the acknowledgement letter that the senior assessor signed the acknowledgement "*for and on behalf of the Commissioner-General"* will not make the acknowledgement of the appeal invalid.

[124] I am of the view that the appeals dated 29.04.2014 have been validly acknowledged within 30 days of their receipt by letters dated 27.05.2014 (pp. 24 & 25) as required by section 34 (8) of the VAT Act and accordingly, the date of the acknowledgement viz. 27.05.2014 shall, for the purpose of Section 34 (8) of the VAT Act, be deemed to be the date of the receipt of the appeal made to the Commissioner-General. The date of acknowledgement was 27.05.2014 and the date of the time bar was 26.05.2016. The Respondent has determined the appeals on 09.05.2016 (p.105) and accordingly, the determination of the appeal

by the Commissioner-General is not time barred under Section 34 (8) of the VAT Act.

**Question of Law No. 6**

**Has the Tax Appeals Commission erred in determining that the income from share trading of the Appellant was liable for Financial Services VAT under section 25 of the VAT Act?**

[125] The main substantive question that was raised by Mr. Goonewardena was that the three types of income generated by the Appellant, namely (i) income from the sale of shares (question of Law No. 6), (ii) dividend income (Question of Law No. 7) and (iii) interest income (Question of Law No. 8) are not liable for Value Added Tax on Financial Services.

[126] It was the contention of Mr. Goonewardena that the Appellant is not a "specified institution" within the meaning of Section 25F of the VAT Act, during the period in question and that the Appellant is not an unregistered financial services provider within the meaning of Section 25C (5) of the VAT Act and thus, the income assessed by the assessor does not fall within the definition of "supply of financial services" in Section 25F of the VAT Act. Mr. Goonewardena further submitted that (i) the Appellant was, during the taxable period assessed from 01.04.2010 to 31.03.2011, functioning only as a registered leasing company and was not engaged in supplying or providing services similar to the services provided by a finance company by conducing finance business; (ii) the Appellant, as a registered leasing business establishment only received a license to conduct financial business under the Finance Business Act, No. 42 of 2011 in November 2012.

[127] He argued that as the Appellant does not fall into any of the two categories and thus, the Appellant is entitled to the zero rating available in relation to profits and income arising from the sale of company shares and thus, the Appellant's income arising from the sale of such shares is not liable to VAT on financial services.

[128] The learned Senior State Counsel, however, disputed the argument advanced by Mr. Goonewardena and submitted that the Appellant has described itself as a registered finance company as indicated in the written submissions filed by the Appellant before the Tax Appeals Commission. He further submitted that no issue was raised by the Appellant either before the Commissioner-General of Inland Revenue or the Tax Appeals Commission that the Appellant was not a specified institution and thus, the Appellant is now precluded from challenging the determination of the Tax Appeals Commission that it was not a "specified institution".

[129] The assessor, Respondent and the Tax Appeals Commission have made the determination on the basis that the Appellant, being a finance company is engaged in the supply of a financial services similar to services provided by a finance company and thus, the transfer of ownership of equity security is listed as a financial service within the meaning of section 25F of the VAT Act.

**Categories of Persons liable to pay VAT on Financial Services**

[130] At the outset, it is necessary to examine the statutory provisions of the VAT Act to the extent relevant to the imposition of VAT on the supply of financial services and identify the categories of persons liable to pay VAT on financial services. Section 25A of the VAT Act, as amended, deals with the charge of VAT on the supply of financial services by specified institutions or by any person. Section 25A (1) provides:

> *"(1) notwithstanding the provisions of Chapter I, II, III and item (xi) of the First Schedule to this Act, a Value Added Tax (hereinafter in this Chapter referred to as "the Tax") shall be charged in accordance with the provisions of this Chapter on the supply of financial services in Sri Lanka-*
>
> *(i) by any **specified institution** during the period commencing January 1, 2003 and ending on June 30, 2003; and*
> *(ii) by **any person** on or after July 1, 2003 but prior to December 31, 2007;*
> *(iii) by any person other than a Co-operative Society registered under the Co-operative Society Law, No. 5 of 1972, on or after January, 1, 2008 but prior to January, 2009; and*
> (iv) *by any person other than a **Co-operative Society** registered under the Co-operative Societies Law No. 5 of 1972 or **Lady Lochore Loan Fund** established under the Act No. 38 of 1951, commencing on or after January 1. 2009, or the **Central Bank** of Sri Lanka established by the Monetary Law Act (Chapter 422) (with effect from Julay 1, 2003).* [Emphasis Added].
>
> *Where **such specified institution** or **person carries on the business of supplying such financial services.***

[131] It is manifest that for the time period relevant to this case, and subject to the aforesaid three exceptions, namely, Co-operative Societies, the Lady Lochore Loan Fund and the Central Bank, all persons including any specified institution, are liable to pay VAT on FS. The twofold elements to be satisfied for the application of section 25F of the VAT Act for the charge of VAT on FS are the following:

1. The Appellant can be a specified institution within the meaning of section 25A of the VAT Act carrying on the business of supplying of any financial service in Sri Lanka; or

2. The Appellant can be any person within the meaning of section 25A of the VAT Act carrying on the business of supplying of any financial service in Sri Lanka.

**What is a specified institution?**

[132] Now, the next question is whether or not, the Appellant is a "specified institution" who carries on the business of supplying financial services within the meaning of Section 25F of the VAT Act, to be liable to pay VAT on FS. Section 25F defines a "specified institution" which includes a finance company registered under the Finance Companies Act, No. 78 of 1988. In terms of Section 25F, a "specified institution" broadly means-

(a) a licensed commercial bank within the meaning of the Banking Act, No. 30 of 1988;
**(b) a finance company registered under the Finance Companies Act, No. 78 of 1988;**
(c) a licensed specialized bank within the meaning of the Banking Act, No. 30 of 1988.

[133] Now the question is whether the Appellant is a finance company registered under the Finance Companies Act, No. 78 of 1988 to be considered a "specified institution" within the meaning of Section 25F of the VAT Act. Mr. Goonewardena invited our attention to the definition of "finance company" and "finance business" in section 46 of the Finance Companies Act, No. 78 of 1988 and contended that the Respondent was wrong in holding that the Appellant was engaged in supplying financial services similar to a finance company by conducting finance business. Section 46 of the Finance Companies Act, No. 78 of 1988 defined a "finance company" as follows:

*"Finance Company means a company as defined in the Companies Act No. 17 of 1982, registered under this Act for carrying on finance business."*

*"Finance business" under the said Act means the business of acceptance of money by way of deposit the payment of interest thereon and*

*(a) the lending of money on interest; or*

*(b) the investment of money in any manner whatsoever; or*

*(c) the lending of money on interest and the investment of money in any manner whatsoever...."*

[134] The definition of "finance company" in Section 46 of the Finance Companies Act, No. 78 of 1982 was amended by the Finance Companies (Amendment) Act No. 23 of 1991 by the substitution for the definition of the expression "finance company", and "finance business" which read as follows:

*"finance company" means company as defined in the Companies Act No. 17 of 1982, registered under this Act for the carrying on finance business and shall be deemed to include for the purpose of any action that, may be taken by the Board or the Directors under this Act. Any institution within the meaning of the Control of Finance Companies Act No. 27 of 1979. Notwithstanding that such institution has ceased to carry on finance, business on the day preceding the date of commencement of this Act".*

*"finance business" means the business of acceptance of deposits, and*

*(a) the lending of money; or*

*(b) the investment of money in any manner whatsoever; or*

*(c) the lending of money and the investment of money in any manner whatsoever".*

[135] It is to be noted that the expression "institution" is defined in section 22 of the Control of Finance Companies Act, No. 27 of 1979 and its business is identical to the finance business as defined in Section 46 of the Finance Companies Act, No. 78 of 1988. The expression "institution" in section 22 of the Control of Finance Companies Act, No. 27 of 1979 is as follows:

*"Institution" means any person or body of persons, corporate or unincorporated, whose business or part of whose* ***business consists in the acceptance of money by way of deposit, the payment of interest thereon and-***

*(a) the lending of money on interest; or*

*(b) the investment of money in any manner whatsoever; or*

*(c) the lending of money on interest and the investment of money in any manner whatsoever".*

[136] Any specified institution for the purpose of section 25A of the VAT Act and relevant to the periods in question is any finance company, which is defined in the Companies Act, No. 17 of 1982 and registered under the Finance Companies Act, No. 78 of 1988 as amended, for carrying on finance business, namely, the business of acceptance of money by way of deposit, the payment of interest thereon and

*(d) the lending of money on interest; or*

*(e) the investment of money in any manner whatsoever; or*

*(f) the lending of money on interest and the investment of money in any manner whatsoever".*

[137] It is to be noted that the Finance Companies Act, No. 78 of 1988 was repealed by section 71 (1) of the Finance Business Act, No. 42 of 2011 and the said Act came into operation on **09th November, 2011** after the taxable periods assessed in question.

**Burden of Proof that the Assessment is Excessive or Erroneous**

[138] It is to be noted that the burden of proving that an assessment is excessive or erroneous is on the assessee who is objecting to the assessment and, thus, if the person assessed fails to prove that the assessment is excessive or wrong, the assessment will be affirmed in appeal. In the case of *Tynewydd Labour Working Men's Club and Institute v. Customs and Excise Commissioners* (1979) STC 570, this proposition was confirmed:

> *"any tax payer who appealed to the tribunal takes upon himself the burden of proving the assertion he makes. Namely that the assessment is wrong because unless he proves this there is nothing on which the tribunal can find an error in the assessment. There should be no difficulty in the way of the appellant assuming this burden. The facts and figures are known to him, and if he does not understand the commissioners' case, the rules provide for the commissioners to give a proper explanation".*

[139] A perusal of the record reveals, as correctly submitted by the learned Senior State Counsel that the Appellant has never taken up the position either before the Commissioner-General or the Tax Appeals Commission that it was not a registered finance company under the Finance Companies Act, No. 78 of 1988 or that the Appellant became a registered finance company to carry on finance business with effect from 08.11.2012. On the contrary, the Appellant has clearly admitted in the written submissions filed before the Commissioner-General on **30.03.2016,** (p. 31 of the record) that the Appellant is a **finance company registered with the Central Bank**. The last paragraph of page 31 of the written submissions reads as follows:

> *"Further, as you are aware,* ***the company is a finance company registered with the Central Bank of Sri Lanka to engage in business of finance company to accept mobilizing deposits and lending money to its customers by way of loans and other facilities.*** *Hence, investing in listed shares and realizing profit thereon is not a business carried on as a part of finance company's operation. As such, the gain on share trading is not liable for VAT on Finance Service".*

[140] The Appellant's Deputy Chairman/Director in its Petition of Appeal addressed to the Tax Appeals Commission dated 18.08.2016 (p. 81) has admitted in paragraph 3.0 that the Appellant **is a finance company licensed by the Central Bank of Sri Lanka engaging in the finance business** It reads as follows:

> *"3.0. The Company is a listed company in the Colombo Stock Exchange.* ***The Company being a finance company licensed by the Central Bank of Sri Lanka is mainly engaged in the business of mobilizing deposits and providing hire purchase, leasing and other loan facilities to the customers".***

[141] The Appellant in its written submissions filed before the Tax Appeals Commission at page 178, paragraph 4.6.2 has further admitted that the **Appellant company is a registered finance company**. It reads:

> "4.6.2. *The Hon. Tax Appeals Commission may appreciate the fact that the* ***company being the registered finance company*** *is not engaged in the business of issue of shares, allotment and transfer of ownership of any securities".*

[142] The Appellant never challenged the determination of the assessor or the Commissioner-General before the Tax Appeals Commission on the basis that the Appellant was not a finance company registered with the Central Bank of Sri Lanka under the Finance Companies Act, No. 78 of 1988 and thus, the Appellant could not be categorised as a specified institution under Section 25F of the VAT Act. There was no issue before the Tax Appeals Commission to the effect that the Appellant was not a finance company registered with the Central Bank of Sri Lanka and thus, it was outside the definition of a "specified institution". Mr. Goonewardena however, submitted for the first time, during the course of the argument that the Appellant was not a finance company registered with the Central Bank at the relevant time. Can the Appellant, after having clearly admitted before the Commissioner-General and the Tax Appeals Commission that it was a finance company registered with the Central Bank at the relevant time, now deny such admitted fact.?

[143] It is an elementary rule that a party litigant cannot be permitted to assume inconsistent positions in Court, to play fast and loose, to blow hot and cold, to approbate and reprobate to the detriment of his opponent-*quod approbo non reprobo* (*Lissenden v. C. A. V. Bosch Limited*, HL (1940) 412 & 417-419, *Banque des Marchands de Moscou v. Kindersley* (1951) Ch, 112). I hold that the Appellant has admitted that it was a finance company registered with the Central Bank and therefore, the Appellant cannot now take up any inconsistent positions, blow hot and cold, approbate and reprobate and contend now, that it was not a finance company registered with the Central Bank. The Tax Appeals Commission was fully justified in proceeding, upon the Appellant's own admission that the Appellant was a finance company registered with the Central Bank and thus, could be categorised as a "specified institution".

**Income arising from the supply of financial services**

[144] The next point is to consider whether the income assessed by the assessor falls within the definition of "supply of financial services" and if not, whether it is outside the ambit of the VAT on Financial Services. In terms of the charging section (s. 25A (1)), VAT shall be charged only on the "supply of financial services" and the following conditions should prevail to be chargeable with VAT on FS:

1. Such income shall be from the supply of financial services;
2. Such income shall be received by any specified institution or any person who carries on the business of supplying such financial services.

**Supply of Financial Services**

[145] Now, the question is whether the Appellant was engaged in the supply of financial services in Sri Lanka within the meaning of section 25F of the VAT Act. Section 25F of the VAT Act exclusively defines the transactions or activities that fall within the meaning of "supply of financial services". It reads as follows:

*"25F. For the purposes of this Chapter-*

*supply of financial services means-*

*(a) the operation of any current, deposit or savings account;*
*(b) the exchange of currency;*
*(c) the issue, payment, collection or transfer of ownership of any note, order for payment, cheque or letter of credit ;*
*(d) the issue, allotment, transfer of ownership, drawing, acceptance, or endorsement of any debt, security, being any interest in or right to be paid money owing by any person other than the transfer of nonperforming loans of a licensed Commercial Bank to any other person in terms of a re-structuring scheme of such bank as approved by the Central Bank of Sri Lanka with the concurrence of the Minister;*
*(e) the issue, allotment, transfer of ownership of any equity security or a participatory security;*
*(f) issue, underwriting, sub-underwriting or subscribing of any equity security, debt security or participatory security;*
*(g) the provision of any loan, advance or credit;*
*(h) the provision-*

*(a) of the facility of instalment credit finance in a hire purchase conditional sale or credit sale agreement for which facility a separate charge is made and disclosed to the person to whom the supply is made;*
*(b) goods under any hire purchase agreement or conditional sale or hire purchase agreement while have been used in Sri Lanka for a period not less than twelve months as at the date of such agreement".*

[146] The other important element of the charging section is that the supply of financial services made by any specified institution or any person should carry on

the business of supplying such financial services. As noted, the Appellant is a finance company registered with the Central Bank for carrying on finance business in terms of the definition of "finance company" in the Finance Companies Act, No. 78 of 1988 as amended. In terms of the definition of "finance business", finance business is acceptance of deposits, which includes (a) the lending of money; or (b) the investment of money in any manner whatsoever; or (c) the lending of money and the investment of money in any manner whatsoever.

[147] The remaining question is whether the income received by the Appellant from the sale of shares of the Appellant, being a specified institution falls within the definition of "supply financial services" under Section 25F. Section 25F (e) refers to the "***issue, allotment, transfer of ownership of any equity security or participatory security".*** This would encompass the sale of shares.

[148] The Appellant has stated that the company has made profits from sale and purchase of shares and the aim of purchase or sale of shares on the share market was to finance its business activities and raise capital, and therefore, such purchase and sale of shares on the stock market was only an investment, which was not a "supply of financial services" for consideration within the meaning of Section 25F (p. 31). The Appellant has further taken up the position that in case of a supply of financial services, there must be a service provider as well as a service receiver of such services and the activity of investing in shares and making profit thereon do not relate to supply of financial services. In short, the Appellant's argument is that the purpose of the purchase and sale of shares was not to provide a service, but to increase of its capital or finance its business activities, which is not a payment of consideration, but an investment or an employment of capital, which does not fall within the ambit of Section 25F.

[149] The definition of "supply" in the context of a supply of services is defined very lightly in Section 83 of the VAT Act. "Supply of services" means any supply which is not a supply of goods, but includes any loss incurred in a taxable activity for which an indemnity is due (s. 83). The issue is whether the sale of shares of the Appellant company constitutes a "supply of financial services" within the meaning of Section 25F of the VAT Act.

[150] The concept of "business" referred to in Section 25A (1), must, however, amount to a "continuing activity which is predominantly concerned with the supply of financial services to others for a consideration over a period of time" (see-*The National Society for the Prevention of Cruelty to Children v. Customs and Excise Commissioners* (1992) VATIR 417, 422). As "supply" is only subject to VAT if it is made for consideration or is deemed to be made for consideration, to be taxable, a supply must be one that adds value, which satisfies the requirement of an economic one (Davies: Principles Tax Law, Sweet & Maxwell, 2008, p. 430). This

means that a supply of financial services is not taxable unless the supply is for consideration and second, there must be a direct link between the supply of services provided and consideration [(*Kretztechnik AG v. Finanzamt Linz* Case C-465/03 (2005) ECR 1-435, ECJ , paragraph 36)].

[151] It is not in dispute that the Appellant had received income from sale of shares in the share market and the taxability of a share issue depends on whether any supply of service provided constitutes a business of supplying of financial services for consideration within the meaning of Section 25A.

[152] The question whether the issuance of new shares to finance the business of a company was "supply for consideration" within the meaning of Article 2 (1) of the EU, VAT Sixth Directive was considered by the ECJ in the case of *Kretztechnik AG v. Finanzamt Linz* Case C-465/03 (2005) ECR 1-435, ECJ. The first question that was considered by the ECJ was whether the issuance of new shares in connection with Kretxtechnik's entry to the stock market, in order to finance its business activities was a supply for consideration within the meaning of Article 2 (1) of the Sixth Directive. The ECJ. held that the issuance of new shares in the stock market was to **finance its business activities** and was not a part of a commercial activity of dealing in securities and thus, it was not a supply for consideration within the scope of Article 2 (1) of the Sixth Directive.

[153] It is noted that Article 2 (1) of the Sixth VAT Council Directive that defines the scope of VAT within a Member State provides that the supply of goods or services effected for consideration and importation of goods by a taxable person for an economic activity are subject to VAT. The ECJ. held that the **mere acquisition and holding of shares and sale of such holdings** does not, by itself constitute an economic activity and thus, was not a supply for consideration, but the transactions that consist of obtaining income on continuous basis from activities that go beyond the simple acquisition and sale of shares, will constitute a supply for consideration within the meaning of Article 2 (1) of the Directive. Paragraphs 19 and 20 of the decision read:

> *"19. It is settled law that the mere acquisition and holding of shares is not to be regarded as an economic activity within the meaning of the Sixth Directive. The mere acquisition of financial holdings in other undertakings does not amount to the exploitation of property of obtaining income therefrom on a continuous basis because any dividend yielded by that holding is merely the result of ownership of the property and is not the product of any economic activity within the meaning of that directive…… If, therefore, the acquisition of financial holdings in other undertakings does not in itself constitute an economic activity within the meaning of that directive, the same must be true of activities consisting in the sale of such holdings…*
>
> *20. On the other hand, transactions that consist in obtaining income on a* ***continuous basis from activities which go beyond the compass of the simple acquisition and sale of securities, such as transactions carried out in the course of a business trading in securities****, do fall within the*

*scope of the Sixth Directive but are exempted from VAT under Article 13B (d) (5) of that directive…"* [emphasis added].

[154] The *ratio* of the judgment, to my understanding is that when a company issued new shares, the assets of the company is increased by acquiring additional capital whilst granting new shareholders a right of ownership of part of the capital. The aim of such company that issued new shares was to raise capital and not to provide services. Thus, the payment of the sums necessary for the increase of capital is not a payment of consideration, but an investment or an employment of capital only, and thus, such a share issue does not constitute a supply of goods or services for consideration within the meaning of Article 2 (1).

[155] The situation is different where the company has received income on a continuous basis from the transactions carried out in the course of the business of trading in securities (i.e., sale or purchase of shares in the share market, which goes beyond the activity of a simple acquisition or sale of shares). Such transactions would be a supply of services provided for consideration as part of continuous commercial activities of such company.

[156] I shall now turn to the UK Court of Appeal decision in *Trinity Mirror Plc v. Commissioners of Customs and Excise, [2001] STC 192.* The question for the Tribunal was whether the Commissioners of Customs and Excise were correct in their view that the issue in the United Kingdom by a taxable person of its own shares for the purpose of financing the expansion of its business constitutes a "supply of services" for the purposes of the Value Added Tax Act, 1994. The Tribunal answered that question in the affirmative. The judge upheld that decision holding at paragraph 10 as follows:

*"The borrowing of a loan lacks this characteristic and does not constitute a supply by the borrower, but the reason why the borrower does not make a supply is that, far from making a supply to the lender, and far from receiving consideration capable of being expressed in monetary terms from the lender, he is providing such consideration (namely interest) . To hold that the borrower makes a supply would be to turn the Community concept of supply on its head. On the other hand to recognise an issue of shares as a supply is to treat the issue of shares the same as the sale of shares from which it is for the purposes of Community VAT legislation indistinguishable: they share the same essential ingredient, namely the vesting by the "vendor" in the "purchaser" for monetary consideration of like intangible property. As the Tribunal aptly put it:*

*'If the purchasers of shares in BLP were consumers, I can see no logical reason for distinguishing the subscribers in the present case'."*

[157] The Court of Appeal held that a company's issuance of its own shares is a supply of services for consideration. Chadwick LJ., in affirming the decision, stated at paragraph 46

*"46. In this Court, the appellant criticises the judge's explanation, in the words which I have emphasised in the passage cited, for the reason why the borrower does not make a supply of services to the lender. It is said that the judge failed to appreciate that a borrower does create rights in favour of the lender — the right to receive interest, rights over security and the right to receive repayment-for which the lender provides consideration capable of being valued in monetary terms, "namely putting the principal of the loan at the borrower's disposal for the period of the loan" (see paragraph 6 of the appellant's skeleton argument in this Court). In my view that criticism is misconceived. The judge was not addressing a case where the borrower provides security; nor was he addressing a case where the borrower issues loan or debenture stock. He was addressing the simple case where money is borrowed at interest. In such a case, as the judge pointed out, the payment of interest is the consideration for the use of the money lent. On a proper analysis the borrower is paying for a service (the grant of credit) which is provided by the lender. That is the analysis which found favour with the Advocate General in the* BLP *case, when he said, in the passage which I have cited:*

*"If, by contrast, he takes up a loan, he does not himself thereby effect a transaction within the meaning of those rules Instead he is the recipient of a service, which is the subject of a* transaction by a third party*".*

[158] The Court of Appeal in *Trinity Mirror Plc v. Customs and Excise Commissioners* (supra), after having surveyed a number of decisions, identified the following essential characteristics of "supply of services" for the purposes of Value Added Tax:

1. supply of service must be something done for a consideration (paragraph 15);
2. it must be something done which is not a supply of goods (paragraph 15);
3. supply of services to an identifiable consumer in return for a price paid by a customer (*Mohr v. Finanzamt Bad Segeberg* (Case C-215/94) (1996) STC328) (paragraphs 17);
4. supply of service to an identifiable consumer must provide any benefit which would enable them to be considered to be consumers of a service; *(Landboden-Agrardienste GmbH & Co KG v. Finanzamt Calau* (Case C-384/95 1998) STC 171) (paragraph 18);
5. supply of services provided must be capable of being used by and for the benefit of an identified recipient (paragraph 19); and
6. Benefit provided must be capable of being regarded as a cost component of the activity of another person in the commercial chain (paragraph 19).

[159] While the mere acquisition, holding and sale of shares does not by itself constitute "supply of services" within the meaning of Section 25F of the VAT Act as supply of financial services, if the purpose of consideration of payment provided was to finance its business activities only and raise capital for its

activities, such activities will not constitute a supply of services for consideration within the meaning of Section 25F. It is totally different where the sale of shares was to obtain income on a continuing basis that goes beyond the compass of the simple acquisition and sale of shares in the course of a business or trading in securities. Such transactions, would constitute a supply of a financial services within the meaning of section 25F of the VAT Act.

[160] In the present case, the income received by the Appellant from the sale of shares in the course of the business of supplying financial services was a staggering Rs. 229,816,064 [(Rs. 259313874 (dividend & share trading-p. 37) – Rs, 29479810 (dividend-p. 227)]. Apart from the mere statement that the income for the sale of shares was only to raise capital, the Appellant has failed to prove that the large income in a sum of Rs. 229,816,064/- was received by the Appellant for the mere purpose of financing its business activities and that it was not received on a continuous basis in the course of a business of share trading, which did not go beyond the compass of mere sale of shares to raise finance of its capital. Unless such proof is forthcoming from the Appellant, the Appellant, being a specified institution, cannot invite us to hold that such sale of shares was not a supply of financial service for consideration under Section 25F of the VAT Act.

[161] In my view, the issue of shares was done for an identified consumer (recipient) in the share market for consideration and for his benefit in the commercial chain and thus, the characteristics identified in *Trinity Mirror Plc v. Customs and Excise Commissioners* (supra) are met as a supply of financial services.

**Zero Ratted Supplies under s. 25C (5)**

[162] Although the sale of shares is proved to be a supply of financial services under Section 25F, for the calculating the tax, the income from the sale of shares can be excluded from VAT on Financial Services under Section 25C (5) as zero rated supplies. A zero-rated supply is however, a taxable supply, subject to tax at zero rate. The profits and income arising from the sale of shares at zero rate is set out in subparagraph (gg) as follows:

> *"gg. for the taxable period commencing on or after January 1, 2005, the profits or income arising to any person from the sale of company shares owned by such person or to any person who is instrumental in the purchase and sale of such shares by other persons, other than such profits and income arising to any "specified institution" within the meaning of this Chapter or a person not registered with the Central Bank of Sri Lanka, but provising services similar to such services provided by a finance company".*

[163] As noted, the Appellant is admittedly a finance company registered with the Central Bank and thus, the Appellant shall be regarded as a specified institution within the meaning of Section 25F of the VAT Act. The zero rating set out in

Section 25C(5) (gg) has no application to the Appellant and thus, the income received by the Appellant from sale of shares shall be considered as supply of financial services within the meaning of Section 25F of the VAT Act. For those reasons, I hold that the Appellant's income arising from the sale of shares is liable to VAT on financial services as correctly decided by the Tax Appeals Commission.

**Question of Law 7**

**Has the Tax Appeals Commission erred in determining that the dividend income of the Appellant was liable for Financial Services VAT under section 25 of the VAT Act?**

[164] The term "dividend" has not been defined in the VAT Act. However, Section 60 (1) of the Companies Act, 2007 defines the term "dividend" as follows:

> "A dividend means *a distribution out of profits of the company other than an acquisition by the company of its own shares or a redemption of shares by the company".* It is an inclusive and not an exhaustive definition. *The word "distribution" means*
>
> *(a) the direct or indirect transfer of money or property other than the shares of a company, to or for the benefit of a shareholder; or*
>
> *(b) the incurring of a debt to or for the benefit of a shareholder,*
>
> *in relation to a share or shares held by that shareholder, whether by means of a payment of a dividend, a redemption or other acquisition of the share or shares, a distribution of indebtedness or otherwise".*

[165] The Appellant has purchased shares from the share market and gained dividends from the share market (p. 29) but, taken up the position that the purchase of shares is not a subscription arrangement (pp. 29, 176), and thus, there is no consideration involved in the payment of dividends as it was only an investment. Generally, a shareholder does not supply any goods or services in order to receive a dividend and on that basis, the Appellant has argued that as the dividends do not represent consideration for any supply of service by the holder of security and accordingly, the dividends paid to shareholders are outside the scope of VAT.

[166] The question to be asked is whether the payment of dividends to the Appellant's company by any other company whose shares were purchased by the Appellant constitutes a "supply of financial services" by the Appellant for a consideration. The question whether or not dividend income is taxable as a "supply of financial service" depends on whether the nature of the characteristics of the transaction between the company and the shareholders and whether the dividends are qualified or unqualified, such as the ascertainment of the service provider, service recipient, occurance of service and the consideration.

[167] Subparagraph (f) of Section 25F (f) of the VAT refers to dividend income as follows:

> *"(f) issue, underwriting, sub-underwriting or subscribing of any equity security, debt security or participatory security".*

[168] An equity security represents the ownership interest held by shareholders in an entity (a company, partnership, or trust), realized in the form of shares of capital stock, which includes shares of both common and preferred stock and the holders (Investopedia, Security Definition (*investopedia.com*)). Such securities entitle the holder to some control of the company on a *pro rata* basis, *via* voting rights and often, do pay out dividends, but they are able to profit from capital gains when they sell the securities (supra).

[169] The issue is whether underwriting, sub-underwriting or subscribing of any equity security, debt security or participatory security is deemed to be a supply of financial services for the VAT purposes. A dividend, being a return for subscribing and contributing to any equity share capital, pursuant to an offer for subscription and purchasing of shares in the course of carrying on business of financial business, by financial companies, can be classified as a "supply of financial services".

[170] In the present case, Appellant, being a finance company registered with the Central Bank has admittedly purchased shares from another company in the share market and in return, such company having issued shares, has paid dividends to the Appellant. Thus, this is not an ordinary distribution of shares by a company to its shareholders for no consideration. I must emphasise that the word "consideration" which is very important in the VAT world. As noted, the expression "consideration" is to be defined widely to bring within the tax, everything a taxable person receives as consideration for the goods or services supplied in the course of the business of supplying financial services (U.K's HMRC's supply Manual & Policy Note VATSC30500).

[171] The mere acquisition and holding of shares by a company in other entities does not *ipso facto*, constitute a taxable supply, as dividends derived from such share holdings are deemed to arise solely through the ownership of shares for increasing finances, rather than from a form of carrying on business activity with the aim of generating income. There is no dispute that the share trading in question was between connected persons in the share market. If the Appellant being the holding company goes beyond the mere acquisition and holding of shares and becomes actively involved in carrying on financial business of trading in securities for generating income, the dividend payment regularly received as a consideration in the trading of shares may constitute a supply of financial service.

[172] The Appellant's annual income from dividend arising out of the business of a financial service was over 26 Million, which confirms that the Appellant has

received a sum of Rs. 26 Million from purchasing shares from the share market in the course of its financial business and generated a regular annual business income from the share market as part and parcel of its share trading business.

[173] The share trading business in question is obviously beyond the mere holding of shares as a shareholder to increase or expand its business activities. No material was presented by the Appellant to prove that the purpose of dividend income was to finance its business activities or apply it to deal with any possible collapse of business or reduce its expenses. The Appellant as an institutional subscriber has made a supply of service to the connected company by purchasing its shares in carrying on the business of generating income in stocks and the company that sold shares had paid dividend to the Appellant as the service receiver and such payment is the consideration in return for the share purchase arrangement between two connected companies. Thus, the characteristics identified in *Trinity Mirror Plc (formerly Mirror-Group Newspapers Ltd) v. Customs and Excise Commissioners* (supra) are met in respect of the dividend income received by the Appellant as a supply of financial services.

**Zero Ratted Supplies under s. 25C (5)**

[174] Although the dividend income is a supply of financial services under Section 25F, for the calculating the tax, the income from dividend can be excluded from VAT on financial services under Section 25C (5) as zero rated supplies subject to the qualified categories of persons. The dividend income as a zero rated supply is set out in subparagraph (f) of Section 25C (5) as follows:

> *" f. the dividend income (not being profit from a business) arising to any person, other than such income arising to any "specified institution" within the meaning of this Chapter or to a person not registered with the Central Bank of Sri Lanka, but providing services similar to the services provided by a finance company""*

[175] This section reflects the intention of the legislature that the dividend income is liable to tax as supply of financial services, subject to zero rate and, the zero rating for dividend income received is applicable to any category of persons other than such income arising to any "specified institution" or to any person not registered with the Central Bank, but providing services similar to services provided by a finance company.

[176] As noted, the Appellant is admittedly a finance company registered with the Central Bank and thus, the Appellant shall be regarded as a "specified institution" within the meaning of Section 25F of the VAT Act. The zero rating set out in Section 25C (5) (f) has no application to the Appellant and thus, the dividend income received by the Appellant shall be considered as supply of financial services within the meaning of Section 25F of the VAT Act. For those reasons, I

hold that the Appellant's income arising from dividends is liable to VAT on Financial Services as correctly decided by the Tax Appeals Commission.

**Question of Law 8**

**Has the Tax Appeals Commission erred in determining that the interest received from interest bearing government securities, fixed deposits and other deposits of the Appellant was liable to Financial Services VAT under section 25 of the VAT Act?**

[177] The Appellant has received interest income from bank fixed deposits and government securities (REPOS) in a sum of Rs. 44 Million (see-page 48 & 50 of the record). The Appellant has, however, stated that such income received from investment of surplus funds cannot be interpreted as equivalent to loan or advance within the meaning of subparagraph (e) of Section 25F of the VAT Act. The Appellant has, however, received Interest from bank deposits and REPOS that fall under the charging section of VAT on financial services in terms of Section 25F (g) of the VAT Act. It reads as follows:

*"g. the provision of any loan, advance or credit."*

[178] According to Merriam-Webster online Dictionary, the term "credit" in the financial world includes the balance in a person's favour in an account, an amount or sum placed at a person's disposal by a bank, the provision of money, goods or services with the expectation of future payment, and also money, goods or services so provided. As noted, the core activity of finance companies is carrying on finance business, which means the business of acceptance of money by way of deposit, the payment of interest thereon, and the lending or investment of money or the lending of money on interest and the investment of money in any manner whatsoever (see – the definition of "finance business" in the Finance Companies Act). Such financial activities also include trade in securities and investment of money in whatsoever, which includes bank deposits for the purpose of earning interest from their investment in banks.

[179] The Appellant being a financial institution had invested and provided money (credit) to the Bank with the expectation of future interest payment, by way of bank deposits in the course of carrying on its finance business for the purpose of generating further income. The Bank has relied on the credit supplied by the finance institution for borrowing and other banking activities and paid interest in return for the deposits made by the Appellant. The funds (deposits) that flow from the depositor to the Bank in expectation of interest and the interest paid by the Bank to the depositor in the return of the credit is the consideration. This constitutes a supply of financial services within the meaning of Section 25F of the VAT Act. Thus, the characteristics identified in *Trinity Mirror Plc (formerly Mirror-Group Newspapers Ltd) v. Customs and Excise Commissioners* (supra) are met in respect of the income received from bank deposits as a supply of financial services

[180] On the other hand, a sale and repurchase agreement (REPO) is an agreement in which an owner of shares (a borrower of government securities or original owner) sells them to a lender (interim holder) at an agreed price on the understanding that he will repurchase them at an agreed price at some future date. The difference between the amount received by the seller or original owner (sale price) and the amount he pays to repurchase the shares is treated as interest (consideration) paid by one party and received by the other (U.K. Income Tax Act, 2007, s. 607 (2) & Financial Instruments, Central Bank, Sri Lanka, www.cbsl.gov.lk).

[181] In the REPO agreement, the Appellant as a larger finance company sells government securities to the buyer at an agreed price and repurchases them at an agreed price, usually a higher price from the buyer and the Appellant receives the difference between the sale price and the repurchase price as interest (consideration). The seller (supplier of shares) and the buyer (recipient of shares) are both benefited from the agreement as the buyer receives the difference between the sale and repurchase price (interest) as the consideration and the buyer also earns an interest from the transaction.

[182] It is manifest that the REPO agreement is not a mere agreement between a borrower and a money lender for a borrowing of a loan or a mere stock lending agreement between a lender and a borrower under which the lender transfers stock to the borrower otherwise than by way of sale and the borrower agrees to transfer them to the lender otherwise than by way of sale. The transaction in question is between two connected persons in the share market for generating more income for a consideration from government securities in the course of carrying on the business of supplying a financial service

[183] The interest income received by the Appellant from fixed deposits and government securities was not an activity of increasing its mere capital or mere acquisition and holding of government securities. The Appellant as a finance company is engaged in the business of supplying of financial services for the purpose of generating interest income from bank deposits and government securities. The characteristics identified in *Trinity Mirror Plc (formerly Mirror-Group Newspapers Ltd) v. Customs and Excise Commissioners* (supra) are met in respect of the said interest income received by the Appellant from bank deposits and government securities as a supply of financial services within the meaning of section 25F of the VAT Act.

**Interest from bank deposits and government securities (REPOS) Zero Rated Supplies under s. 25C (5)**

[184] It is also manifest from section 25C (5) that while the interest income received from bank deposits and government securities is a supply of financial services under section 25F, for the calculating the tax, but such interest income

may be excluded from VAT on Financial Services as zero rated supplies subject to the qualified categories of persons. The interest income arising to any person other than a specified institution or unregistered finance institution is, however, considered as zero rated as set out in subparagraph (e) of section 25C (5) of the VAT Act. It reads as follows:

> *"(e). the profits or income on interest arising or accrued to any approved provided funds, including the Employees Trust Fund or a Pension Fund or any thrift, savings or building society or welfare fund to which contributions are made by employees only or any approved gratuity fund, or the interest income (not being profits from a business) arising or accruing to any person other than a "specified institution" within the meaning of this Chapter or a person not registered within the Central Bank of Sri Lanka, but providing services similar to the services provided by a finance company".*

[185] The zero rating set out in Section 25C (5)(e) has no application to the Appellant, being a specified institution and thus, the interest income received by the Appellant from bank deposits and government securities shall be considered as supply of financial services within the meaning of Section 25F of the VAT Act. For those reasons, I hold that the Appellant's interest income arising from bank deposits and government securities is liable to VAT on financial services as correctly decided by the Tax Appeals Commission.

**Conclusion**

[186] For those reasons, the opinion of the Courtt on Eight Questions of Law is as follows:

Question of Law 1
No.
Question of Law No. 2
No
Question of Law No. 3
No
Question of Law No. 4
No
Question of Law No. 5

No. The Respondent has complied with section 34 (8) of the VAT Act and determined the Appeal within the 2 year period specified therein.

Question of Law No. 6
No
Question of Law No. 7
No
Question of Law No. 8
No

[187] For those reasons, the determination of the Tax Appeals Commission is confirmed and the Appeal is dismissed.

[188] The Registrar is directed to send a certified copy of this judgment to the Tax Appeals Commission.

**JUDGE OF THE COURT OF APPEAL**

**M. Sampath K.B. Wijeratne, J.**

I agree.

**JUDGE OF THE COURT OF APPEAL**