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

In the matter of an appeal by way of Stated Case on a question of law for the opinion of the Court of Appeal under and in terms of Section 11A of the Tax Appeals Commission Act, No. 23 of 2011 (as amended).

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

APPELLANT

CA No. CA/TAX/0031/2019
Tax Appeals Commission
No. TAC/IT /003/2016

v.

Aitken Spence Travels (Pvt.) Ltd.,
No. 305,
Vauxhall Tower, Vauxhall Street,
Colombo 02.

RESPONDENT

BEFORE : Dr. Ruwan Fernando J. &
M. Sampath K. B. Wijeratne J.

COUNSEL : Chaya Sri Nammuni, SSC for the Appellant.

		K. Kanag –Isvaran, P.C. with Shivaan Kanag-Isvaran for the Respondent.
WRITTEN SUBMISSIONS	:	Not tendered by the Appellant 01.04.2021 (by the Respondent)
ARGUED ON	:	07.03.2022
DECIDED ON	:	26.05.2022

M. Sampath K. B. Wijeratne J.

Introduction

The Respondent Aitken Spence Travels (Private) Limited (hereinafter referred to as the 'Respondent' and/or 'ASTL') is a limited liability company incorporated in Sri Lanka. The principal activity of the Respondent company is providing all travel related services to their clients, including Foreign Tour Operators (hereinafter referred to as 'FTOs') who organize tours for tourists visiting Sri Lanka.

The Respondent submitted its income tax returns for the year of assessment 2010/2011 claiming a tax exemption for a portion of its income, under Section 13 (dddd) of the Inland Revenue Act No. 10 of 2006, as amended (hereinafter referred to as the 'IR Act'). The assessor rejected the return on the ground that the Respondent did not fulfil the *'service rendered to a person outside Sri Lanka'* requirement laid down in Section 13 (dddd) of the IR Act. Accordingly, an assessment was issued.

The Respondent appealed to the Commissioner General of Inland Revenue (hereinafter referred to as the 'CGIR') against the said assessment and the CGIR by his determination dated 23rd November 2015, confirmed the assessment.

Being aggrieved by the said determination, the Respondent appealed to the Tax Appeals Commission (hereinafter referred to as the 'TAC') in accordance with Section 7 of the TAC Act No. 23 of 2011, as amended (hereinafter referred to as 'the TAC Act').

The TAC, on the 13th June 2019, determined that the services provided by the Respondent are to a person outside Sri Lanka and annulled the assessment, acting under Section 9 (10) of the TAC Act.

The Appellant, CGIR then moved the TAC to state a case on the following two questions of law for the opinion of this Court, in accordance with Section 7 of the TAC Act.

1. ***Has the TAC erred in interpreting Section 13 (dddd) of Inland Revenue (Amendment) Act, No. 9 of 2009 as the Foreign Tour Operators were the recipient of the services rendered by the Appellant Company (Aitken Spence Travels (Pvt) Ltd.) not the Foreign Tourists who were physically present in Sri Lanka?***

   Section 13 (dddd) of IR Act: "notwithstanding the provisions of paragraph (ddd) of this Section, the profit and income for the period commencing from April 1, 2009 and ending on March 31, 2011, earned in foreign currency by any resident company, any resident individual or any partnership in Sri Lanka, from any service rendered in or outside Sri Lanka, to any person or partnership outside Sri Lanka, if such profits and income (less such amount, if any, expended outside Sri Lanka as is considered by the Commissioner General to be reasonable expenses) are remitted to Sri Lanka, through a Bank;"

2. ***Whether the TAC has erred in determining that the Appellant company can treat income received from foreign tour operators for the purpose of income tax as a foreign receipt and as a local receipt for the purpose of VAT.***

The substantive issue in this case is whether the supply of services made by the Respondent is exempt from income tax in terms of Section 13 (dddd) of the IR Act.

In accordance with section 13 (dddd) of the IR Act, profit and income will be exempt from income tax, if the following requirements are satisfied;

(i) service rendered in or outside Sri Lanka
(ii) to any person or partnership outside Sri Lanka
(iii) for the period of 01.04.2009 to 31.03.2011
(iv) earned in foreign currency
(v) remitted to Sri Lanka through a bank

I will now advert to the facts of this case in so far as they are material to the instant appeal.

According to the Respondent, FTOs market tourism destinations all over the world. They compile brochures with tourist attractions around the world, including Sri Lanka. The tour packages include air travel, hotel accommodation, transport, excursions etc. The tourists approach the FTO and purchase a package to their desired destination and the FTO enters into a contract with the tourist to deliver the said services. FTO obtains the services of ASTL to fulfil their contractual obligation towards their customers, the tourists. Accordingly, FTO enters into an agreement with ASTL to provide the aforesaid services to the tourists, in Sri Lanka. FTO pays ASTL for the services provided by ASTL to the foreign tourist, keeping a profit margin. The Appellant did not challenge the above position of the Respondent. The Appellant, in point 2, paragraph 2 of his reasons for the determination, concedes that FTO arrange vacations for tourists, collect a total cost of the tour with a profit margin and issue invoices to the tourists. It was also admitted that the profit margin is agreed between FTO and ASTL, beforehand. The Appellant also stated in point 2, paragraph 3 that ASTL issue invoices to FTO for the costs incurred by ASTL for the tourist with the profit margin and receive the total amount in foreign currency through banks.

Accordingly, it is admitted that the Respondent met the aforementioned third, fourth and fifth conditions of section 13 (dddd) in order to qualify for the tax exemption.

In terms of the first condition above, the service could be rendered in or outside Sri Lanka. Then the only issue the parties at variance is whether the service is rendered to a person outside Sri Lanka or to a person within Sri Lanka.

The Respondent's contention is that ASTL only facilitates FTO to provide the services agreed by the FTO to the tourists. However, the Appellant disputed the above contention by submitting that ASTL provides its services directly to the foreign tourist who are physically present in Sri Lanka. However, Section 13 (dddd) does not require services to be rendered in Sri Lanka. It could be in or outside Sri Lanka.

Upon a careful consideration of the aforementioned facts, I observe that it is the FTO who enters into a contract with the foreign tourists to provide agreed services in Sri Lanka. For the purpose of fulfilling the contractual obligations towards the foreign tourists, FTO enters into a contract with ASTL, the Respondent. As a result, ASTL provides the services agreed by FTO to the tourists in Sri Lanka.

Hence, in my view, although on the face of the sequence of events and also, in fact, ASTL provides certain services to foreign tourists in Sri Lanka, it is done under and in terms of the contractual obligation towards the FTO.

C*ommissioners of Customs and Excise v Plantiflor Limited*[1], is a case where Lord Millett observed the nature of the contractual obligations between three parties who entered into two separate but related bilateral contracts. In this case, Plantiflor carried on a business of selling plants and garden products, and delivered such goods to its customers through Parcelforce, an agency of the Post Office. One contract was between Plantiflor and its customer by which Plantiflor sold their goods to the customer and the other contract was between Plantiflor and Parcelforce by which Plantiflor made the necessary arrangements to have its customers' goods delivered. There was no third contract between Parcelforce and the customer. The customer's agreement to pay postal charges was made with Plantiflor and not with Parcelforce. Thus, in here, Parcelforce made two different supplies. One was the supply to Plantiflor's customer of the service of delivering his goods to his order, and the other was the supply to Plantiflor of the service of delivering its customer's goods to the addressee. It was held that Parcelforce does not deliver the goods pursuant to any contract with the customer and it makes delivery pursuant to its contract with Plantiflor, which both parties entered into as principals.

In the case in hand, ASTL provides two different types of services, firstly to FTO of the right to have the services agreed between the FTO and ASTL rendered to the foreign tourists in Sri Lanka and secondly, the provision of agreed services to the foreign tourists in Sri Lanka. ASTL earns an income by providing their services to FTO who are outside of Sri Lanka. On the other hand, even though ASTL provides agreed services to foreign tourists, ASTL does not earn an income from them. Since the exemption under section 13(dddd) only applies to profits and income earned in foreign currency by providing a service to a person outside Sri Lanka, and that it

[1] [2002] UKHL 33

does not apply to a service provided to a person in Sri Lanka where no income has generated, ASTL is entitled to claim the exemption under section 13(dddd) for the income they received by providing the services to FTOs. Thus, any service provided by ASTL to foreign tourists through which no income was generated is of no relevance to the application of exemption under Section 13(dddd). Nevertheless, on the other hand, if ASTL did provide a service to foreign tourists independent to the contract with FTOs through which ASTL generated an income, then the exemption under Section 13(dddd) cannot be claimed. However, this is not the matter in issue here.

The Assessor, in the reasons communicated to the Respondent on the 11th November 2013, in terms of Section 29 of the VAT Act, for rejecting the return, stated that the tour packages are arranged by ASTL and sold to the tourists through the FTO and ASTL provided services agreed in the tour package to the tourists in Sri Lanka. However, the CGIR took a contradictory view in his determination. The Appellant, CGIR, stated in his reasons for the determination that it is the FTO who arranges vacation for the tourists, raise the invoices and collect the total cost of the tour with a profit margin[2]. However, this finding is also self-contradictory. The CGIR stated in the same determination that the FTO acts as an agent on behalf of ASTL in collecting the expenses incurred by ASTL for the foreign tourists[3].

In my view, aforementioned set of affairs corresponds to a situation where one principal provides his services through another principal. The law does not expect that every act should be performed by the principal himself. It should also be the case for taxation.

Moreover, the Appellant stated[4], that the money remitted by FTO to ASTL consists only of the cost of serving the foreign tourists and the profit and includes no amount paid by FTO to ASTL. However, this assertion also contradicts one another. CGIR himself stated in his determination[5] that it is the FTO who collects the total amount from the tourists '*including'* the cost of ASTL. The word '*including*' itself establishes that the amount

[2] Point 2 paragraph 2
[3] Point 3 paragraph 3 (b)
[4] Point 2 Paragraph 3 (c)
[5] Point 2 paragraph 2

collected from the tourists is not only the cost of ASTL, but there is also an additional amount for the FTO.

Therefore, it seems to me that the Assessor and the CGIR both acted with great uncertainty in the assessment and its affirmation.

The Appellant further submitted that the Respondent, by paying VAT, acknowledged that the services are provided in Sri Lanka. This was one of the grounds upon which the CGIR confirmed the assessment[6] made by the assessor. However, the Respondent argued that VAT and income tax are profoundly different. It was submitted that the zero-rating criteria under Section 7 (c) of the VAT Act and the exemption criteria under Section 13 (dddd) of the IR Act are materially different and cannot be compared.

For clarity, I will reproduce Section 7 (c) of the VAT Act which read thus:

> *'7. (1) (...)*
>
> *(a) (...)*
>
> *(b) (...)*
>
> *(c) any other service, being a service not referred to in paragraph (b), provided by any person in Sri Lanka to another person outside Sri Lanka* ***to be consumed or utilized outside Sri Lanka*** *shall be zero rated provided that payment for such service in full has been received in foreign currency from outside Sri Lanka through a bank in Sri Lanka.* (emphasis added)
>
> *(2) (...)'*

It was submitted that the zero rating under Section 7 (c) of the VAT Act is based on the concept of service provided by any person in Sri Lanka to another person outside Sri Lanka to be '*consumed or utilized outside Sri Lanka*' and the exemption under 13 (dddd) of the IR Act is based on the concept of any service rendered in or outside Sri Lanka '*to any person or partnership outside Sri Lanka'*. As such, it is appropriate to note that, for the Respondent to be eligible for the zero rating under Section 7 (c) of the VAT Act, service must be consumed or utilized outside Sri Lanka. However, consumption and/or utilization of the service are not the criteria for the exemption from Income Tax under Section 13 (dddd) of the IR Act.

[6] At page 13 of the appeal brief

The criteria are whether the service is rendered to any person or partnership outside Sri Lanka. In the circumstances, I am in favour of the argument advanced by the learned President's Counsel for the Respondent that the two statutory provisions cannot be compared.

The Assessor, in his reasons for not accepting the return refers to a duplicity in the payment of Income Tax by ASTL. He observed that prior to the year of assessment 2010/2011 ASTL paid income tax at the concessionary rate of 15% in terms of Section 46 of the IR Act and thereafter, claimed exemption under Section 13 (dddd). In reply, the Respondent submitted that Section 13 (dddd) was introduced by amendment Act No. 19 of 2009 with effect from 31st of March 2009 and thereafter only ASTL could claim the exemption under Section 13 (dddd). I am inclined to accept the explanation offered by the Respondent and therefore, the Assessor's observation that there is a duplicity in tax treatment by ASTL has no merit.

CGIR v. Aitken Spence Travels Limited[7] is a case between the same parties and decided by a numerically equal bench of this Court on the 13th November 2018, on identical facts. His Lordship Justice Janak De Silva, (Achala Wengappuli J., agreeing) held that it is the FTO who provide services to the foreign tourists by organizing their tour in Sri Lanka. In order to fulfil the obligation undertaken by the foreign tour operator, it receives the service of the Respondent and in turn the foreign tourists receive the service from the Respondent.

Thus, for the reasons enunciated above in this judgement, I would prefer to follow the judgment of His Lordship Justice Janak De Silva in the aforementioned case of *CGIR v. Aitken Spence Travels Limited*[8].

For the reasons set out above, I hold that the TAC did not err in law when it arrived at the conclusion that it did.

Accordingly, I answer the questions of law stated for the opinion of this Court as follows:

1. ***No*. the TAC arrived at the correct conclusion.**
2. ***No.* the two statutory provisions cannot be compared since the two tax principles are distinct.**

[7] CA. TAX 04/2016 (the Supreme Court refused to grant special leave to appeal in respect of this case on 15/11/2019 in case No. SC.SPL.LA. No. 438/18)
[8] *Supra* Note 6

In light of the answers given the above two questions of law, acting under Section 11 A (6) of the TAC Act, I affirm the determination made by the TAC and dismiss this appeal.

The Registrar is directed to send a copy of this judgement to the Secretary of the TAC

JUDGE OF THE COURT OF APPEAL

Dr. Ruwan Fernando J.

I Agree.

JUDGE OF THE COURT OF APPEAL