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

In the matter of an Appeal by way of a 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).

Johnson and Johnson (Private) Limited,
Renuka Building,
41, Janadipathi Mawatha,
Colombo 01.

Appellant

Case No. CA/TAX/0002/2018
Tax Appeals Commission
No. TAC/IT/039/2015

Vs.

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

Respondent

Before : Dr. Ruwan Fernando J. &

M. Sampath K.B. Wijeratne J.

: Dr. Shivaji Felix with Nivantha Satharasinghe for the Appellant

Milinda Gunatilake, Additional Solicitor General, P.C. for the Respondent.

Argued on : 18.02.2021, 12.03.2021, 28.04.2021 & 15.12.2021

Written Submissions filed on

: 29.06.2018, 31.01.2020 & 17.02.2022 (by the Appellant)

29.06.2018 & 24.03.2022 (by the Respondent)

Decided on : 27.05. 2022

Dr. Ruwan Fernando, J.

Introduction

[1] This is an appeal by way of a case stated against the determination made by the Tax Appeals Commission dated 07.11.2017 confirming the determination made by the Respondent on 14.10.2015 and dismissing the Appeal of the Appellant. The period relates to the year of assessment 2010/2011.

Factual Background

[2] According to the case stated (p. 189 of the Tax Appeals Commission brief) and the Certificate of Approved Accountant under Section 107(2)(a) of the Inland Revenue Act (p. 158 of the Tax Appeals Commission brief), the Appellant (Johnson & Johnson Pvt. Ltd) is a company incorporated in India, having a branch office in Sri Lanka, and the company is engaged in the export of medical equipment, import and wholesale business of cosmetics and baby care items. The Appellant submitted the return of income for the above year of assessment and deducted an amount of Rs. 37,522,673/- as exempt profit from offshore trading and claimed a tax exemption under Section 13 (b) (ii) of the Inland Revenue Act, No. 10 of 2006. The Assessor refused to accept the return of income submitted by the Appellant and

refused to grant the exemption under Section 13 (b) (ii) of the Inland Revenue Act, No. 10 of 2006 for the following reason:

1. Johnson & Johnson Ltd (Sri Lanka Branch) is a non-resident company;
2. Even though the goods are purchased and sold out of Sri Lanka by Johnson & Johnson Ltd (Sri Lanka Branch), the business has been carried out in Sri Lanka.

[3] Accordingly, the Assessor assessed the assessable income as follows:

Y/A 2010/2011	
Trade Profit	
On local sales	132,260,570
On Enter port sales	39,080,710
On sales outside Sri Lanka	37,522,673
	208,863,953
Less	
Loss of income for the year	(17,610,339)
	191,253,614
Tax on income taxable at special rate	
39,080,710 X 10%	3,908,071
Tax on balance taxable income	
152,172,904 X 35%	53,260,516
Tax payable	57,168,587
Social Responsibility levy payable	857,529

[4] Accordingly, the notice of assessment was issued by the Assessor, and being dissatisfied with the said assessments, the Appellant appealed to the Commissioner-General of Inland Revenue (hereinafter referred to as the Respondent). The Respondent by its determination dated 14.10.2015 confirmed the assessment and dismissed the appeal (Vide- reasons for the determination at pp. 26-30 of the Tax Appeals Commission brief).

Appeal to the Tax Appeals Commission & the Court of Appeal

[5] Being dissatisfied with the determination of the Respondent, the Appellant appealed to the Tax Appeals Commission. The Tax Appeals

Commission by its determination dated 07.11.2017 confirmed the determination made by the Respondent and dismissed the appeal. The Tax Appeals Commission held in its determination that:

1. The tax exemption under section 13 (b)(ii) of the IRA 2006 is given to a resident company and the Appellant does not satisfy the requirement of a resident company;
2. The Appellant is not involved in offshore business specified in Section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006 and the business has been carried out in Sri Lanka;
3. The circumstances or the activities of the resident company and the non-resident company are different and therefore, there is no discrimination on the ground of nationality or residency. Therefore, Article 25 (1) and 25 (2) of the Double Taxation Avoidance Agreement cannot be equally applied to a non-resident company under Section 13 (b)(ii) of the IRA, 2006;
4. The concessionary tax rate claimed by the Appellant under section 51 or section 52 of the IRA, 2006 applies to any specified undertaking and the taxable income of such company includes any qualified export profits and income from such specified undertaking. The Appellant who claims to have earned profits and income from offshore business cannot claim the concessionary tax rate under section 51 or 52 on the basis that it earned profits or income from exports.

Appeal to the Court of Appeal

[6] Being dissatisfied with the said determination of the Tax Appeals Commission, the Appellant appealed to the Tax Appeals Commission by way of case stated and formulated the following questions of law in the case stated for the opinion of the Court of Appeal:

1. Is the determination of the Tax Appeals Commission time barred?
2. Did the Tax Appeals Commission err in law when it came to the conclusion that the Appellant was not lawfully entitled to the income tax exemption conferred under and in terms of Section 13

(b) (ii) of the Inland Revenue Act, No. 10 of 2006 (as amended) (read with Article 25 of the Double Taxation Avoidance Treaty between the Governments of Sri Lanka and India?

3. In the event that the Appellant is not entitled to the income tax exemption conferred by Section 13 (b) (ii), did the Tax Appeals Commission err in law when it concluded that the Appellant was not entitled to be taxed at the concessionary tax rate contemplated by Section 51 of the Inland Revenue Act, No. 10 of 2006?

4. In view of the facts and circumstances of the case, did the Tax Appeals Commission err in law when it came to the conclusion that it did?

[7] At the hearing of the appeal, Dr. Shivaji Felix, the learned Counsel for the Appellant and Mr. Milinda Gunatilake, Additional Solicitor General for the Respondent made extensive oral submissions and further filed written submissions on the four questions of law submitted for the opinion of the Court.

Analysis

Question of Law, No. 1

Is the determination of the Tax Appeals Commission time barred?

[8] At the hearing, Dr. Shivaji Felix submitted that the first date of the hearing of the appeal before the Tax Appeals Commission commenced on 09.06.2016 but the determination was made by the Commission on 07.11.2017, which is clearly beyond the time period of 270 specified by the Tax Appeals Commission Act. He submitted that the statutory requirement in making the determination within a period of 270 days from the commencement of the oral hearing is mandatory and accordingly, the determination of the appeal by the Tax Appeals Commission was time barred by operation of law. He relied on the decision of the Court of Appeal in *Mohideen v. Commissioner-General of Inland Revenue* ((CA 2/2007 (20-15) Vol. XXI. BASL Law Journal, page 170) in support of his contention.

[9] He submitted that in terms of Section 10 of the Tax Appeals Commission Act, No. 23 of 2011, the Tax Appeals Commission was required to decide such appeals within a period of 180 days from the date of such transfer of cases to the Tax Appeals Commission but in terms of the Tax Appeals Commission (Amendment) Act, No. 04 of 2012, this period was extended to 12 months from the date on which the Commission shall commence its sittings. He further submitted that this period was further extended by the Tax Appeals Commission (Amendment) Act, No. 20 of 2013 to 24 months from the date on which the Commission shall commence its sittings for the hearing of each such appeal. He submitted therefore, that this makes it very clear that the intention of Parliament is that Section 10 (as amended), is a mandatory provision of law which requires strict compliance.

[10] The learned Additional Solicitor General, however, submitted that the time limit specified in Section 10 of the Tax Appeals Commission Act (as amended) is not mandatory, but rather directory and the failure to adhere to the time limit specified in the Tax Appeals Commission Act (as amended) cannot render the Tax Appeals Commission *functus officio* to hear and determine the appeal. He relied on the decisions of this Court in *Stafford Motor Company Limited v. The Commissioner General of Inland Revenue* (CA /Tax/17/2017, decided on 15.03.2019), *Kegalle Plantations PLC v. Commissioner General of Inland Revenue* (CA/Tax/09/2010) decided on 04.09.2018, *S.P. Muttiah v. Commissioner General of Inland Revenue* (CA/Tax/46/2019) decided on 30.07.2021, *Visuwalingam v. Liyanage* (1983) (1) Sri L.R. 203 and *Amadeus Lanka (Private) Limited v. Commissioner General of Inland Revenue*, CA/Tax/04/2019 decided on 30. 07. 2021in support of his contention.

[11] Section 10 of the Tax Appeals Commission Act, No. 23 of 2011, stipulated that the Tax Appeals Commission shall make the determination within a period of one hundred and eighty days from the date of the commencement of the hearing of the appeal. It reads as follows:

> *"The Commission shall hear all appeals received by it and make its decision in respect thereof, within* ***one hundred and eighty days*** *from the date of the commencement of the hearing of the appeal".*

[12] Section 10 of the Tax Appeals Commission Act was amended by Section 7 of the Tax Appeals Commission (Amendment) Act, No. 4 of 2012, which stipulated that the determination of the Commission shall be made within two hundred and seventy days. Section 10 of the Tax Appeals Commission Act was further amended by Section 7 of the Tax Appeals Commission (Amendment) Act, No. 4 of 2012 by the substitution of the words "within hundred and eighty days from the date of such transfer" of the words "within twelve months of the date on which the Commission shall commence its sittings". This Amendment came into effect on 15.02.2012 and pending appeals were transferred to the Tax Appeals Commission from the Board of Review. In terms of Section 13 of the said Act, the amendment was to have retrospective effect and was deemed to have come into force from the date of the Principal Act (i.e. 31.01.2011).

[13] Section 10 of the Tax Appeals Commission Act, No. 23 of 2011 was further amended by Section 7 of the Tax Appeals Commission (Amendment) Act, No. 20 of 2013 by the substitution for all the words commencing from "two hundred and seventy days" to the end of that Section, of the following: -

> ***"Two hundred and seventy days from the date of the commencement of its sittings for the hearing of each such appeal***
>
> *Provided that, all appeals pending before the respective Board or Boards of Review in terms of the provisions of the respective enactments specified in Column I of Schedule I, or Schedule II to this Act, notwithstanding the fact that such provisions are applicable to different taxable periods as specified therein shall with effect from the date of coming into operation of the provision of this Act be deemed to stand transferred to the Commission, and the Commission shall, notwithstanding anything contained in any other written law make its determination in respect thereof, within twenty four months from the date on which the Commission shall commence its sittings for the hearing of each such appeal.".*

[14] In terms of Section 14 of the Tax Appeals Commission (Amendment) Act, No. 20 of 2013, the amendment was to have retrospective effect and was deemed to have come into force with effect from 01.04.2011. Section 15 of the Tax Appeals Commission (Amendment) Act, No. 20 of 2013 further provides an avoidance of doubt clause as follows:

"For the avoidance of doubts, it is hereby declared, that the Commission shall have the power in accordance with the provisions of the principal enactment as amended by this Act, to hear and determine any appeal that was deemed transferred to the Commission under section 10 of the principal enactment, notwithstanding the expiry of the twelve months granted for its determination by that section prior to its amendment by this Act."

[15] Accordingly, Section 10 of the Tax Appeals Commission Act, No. 23 of 2011 as last amended by the Tax Appeals Commission (Amendment) Act, No. 20 of 2013 now provides as follows:

*"The Commission **shall** hear all appeals received by it and make its determination in respect thereof, within **two hundred and seventy days from the date of the commencement of its sittings for the hearing of each such appeal**:*

Provided that, all appeals pending before the respective Board or Boards of Review in terms of the provisions of the respective enactments specified in Column I of Schedule I, or Schedule II to this Act, notwithstanding the fact that such provisions are applicable to different taxable periods as specified therein shall with effect from the date of coming into operation of the provision of this Act be deemed to stand transferred to the Commission, and the Commission shall, notwithstanding anything contained in any other written law, make its determination in respect thereof, within twenty four months from the date on which the Commission shall commence its sittings for the hearing of each such appeal".

Mandatory vs. Directory

[16] Section 10 of the Tax Appeals Commission Act stipulates that the Tax Appeals Commission shall make its determination within 270 days from the date of the commencement of its sittings for the hearing of the appeal. Superficially, the effects of non-compliance of a provision are dealt with in terms of the mandatory-directory classification. Generally, in the case of a mandatory provision, the act done in breach thereof is void, whereas, in the case of a directory provision, the act does not become void, although some other consequences may follow (P.M. Bakshi, Interpretation of Statutes, First Ed, 2008422).

[17] The argument advanced by Dr. Felix was that the word "shall" used in Section 10 is normally to be interpreted as connoting a mandatory

provision, meaning that what is thereby enjoined is not merely desired (directory) to be done but must be done (mandatory). Thus, he submitted that the effect of such breach of a mandatory provision, which has the consequence of the determination of the Tax Appeals Commission rendering invalid. But, the use of the word “shall” does not always mean that the provision is obligatory or mandatory as it depends upon the context in which the word “shall” occurs, and the other circumstances as echoed by the Indian Supreme Court case of *The Collector of Monghyr v. Keshan Prasad Goenka,* AIR 1962 SC 1694 at p. 1701) in the following words:

> *“It is needless to add that the employment of the auxiliary verb " shall" is inconclusive and similarly the mere absence of the imperative is not conclusive either. The question whether any requirement is mandatory or directory has to be decided, not merely on the basis of any specific provision which, for instance, sets out the consequence of the omission to observe the requirement, but on the purpose for which the requirement has been enacted, particularly in the context of the (1) [1958] S.C.R. 533, other provisions of the Act and the general scheme thereof. It would, inter alia, depend on whether the requirement is insisted on as a protection for the safeguarding of the right of liberty of a person or of property which the action might involve”.*

[18] Thus, an enactment in form is mandatory might, in substance be directory and that the use of the word “shall” does not conclude the matter (*Hari Vishnu Kamath v. Ahmad Ishaque* AIR 1955 SC 233). It is not in dispute that Section 10 of the Tax Appeals Commission Act does not say what will happen if the Tax Appeals Commission fails to make the determination within the time limit specified in Section 10 of the Tax Appeals Commission Act, No. 23 of 2011 (as amended).

Legislative Intent

[19] The question as to whether a statute is mandatory or directory is a question which has to be adjudged in the light of the intention of the Legislature as disclosed by the object, purpose and scope of the statute. If the statute is mandatory, the act or thing done not in the manner or form prescribed can have no effect or validity and if it is a directory, a penalty may be incurred for non-compliance, but the act or thing done is regarded

as good (P.M. Bakshi, Interpretation of Statutes, p. 430 & *Mohanlal Ganpatram v. Shri Sayaji Jubliee Cotton and Jute Mills Co. Ltd* AIR 1966 Guj. 96). *In State of U.P., v. Baburam Upadhya*, reported in AIR 1961 SC 751, the Supreme Court of India said that when a statute uses the word "shall", prima facie, it is mandatory, but the Court may ascertain the real intention of the legislature by carefully attending to the whole scope of the statute.

[20] Crawford on "Statutory Construction" (Ed. 1940, Art. 261, p. 516) sets out the following passage from an American case approvingly as follows:

> *"The question as to whether a statute is mandatory or directory depends upon the intent of the legislature and not upon the language in which the intent is clothed. The meaning and intention of the legislature must govern, and these are to be ascertained, not only from the phraseology of the provision, but also by considering its nature, its design, and the consequences which would follow from construing it the one way or the other".*

[21] According to Sutherland, Statutory Construction, Third Ed. Vol. III, p. 77:

> *"The difference between mandatory and directory statutes is one of effect only. The question generally arises in a case involving a determination of rights as affected by the violation of, or omission to adhere to statutory directions. This determination involves a decision of whether or not the violation or omission is such as to render invalid Acts or proceedings to the statute, or the rights, powers, privileges claimed thereunder. If the violation or omission is invalidating, the statute is mandatory, if not, it is directory".*

[22] Then the question is this: What is the fundamental test that is to be applied in determining whether or not the failure to obey the time bar provision in Section 10 of the Tax Appeals Commission Act was intended by the legislature to be mandatory or directory? The question whether the non-compliance with a statutory provision can be classified as mandatory rendering the proceedings invalid or directory leaving it intact depends, on the consideration of whether the consequences of the non-compliance were intended by the legislature to be mandatory or directory. This proposition was echoed by Lord Woolf MR (as he then was) in *R v. Secretary of State for the Home Department, Ex p Jeyeanthan [2000] 1 WLR*

354, who stated that it is "much more important to focus on the consequences of the non-compliance". He elaborated this proposition in the following words at p. 360:

> *"In the majority of cases, whether the requirement is categorized as directory or mandatory, the tribunal before whom the defect is properly raised has the task of determining what are to be the consequences of failing to comply with the requirement in the context of all the facts and circumstances of the case in which the issue arises".*

[23] Here, it is also desirable to remember the words of Lord Hailsham of St. Marylebone L.C. in his speech in *London and Clydeside Estates Ltd. v. Aberdeen District Council* [1980] 1 W.L.R. *182* , 188–190. He stated at p. 36:

> *"The contention was that in the categorization of statutory requirements into 'mandatory' and 'directory,' there was a subdivision of the category 'directory' into two classes composed (I) of those directory requirements 'substantial compliance' with which satisfied the requirement to the point at which a minor defect of trivial irregularity could be ignored by the court and (ii) those requirements so purely regulatory in character that failure to comply could in no circumstances affect the validity of what was done. When Parliament lays down a statutory requirement for the exercise of legal authority it expects its authority to be obeyed down to the minutest detail. But what the courts have to decide in a particular case is the legal consequence of non-compliance on the rights of the subject viewed in the light of a concrete state of facts and a continuing chain of events".*

[24] In *Howard and Others v. Bodington* (1877) 2 PD 203, the Court of Arches considered the question of whether the consequences of a failure to comply with a statutory requirement are mandatory or directory. Lord Penzance stated at pp. 211-212:

> *"Now the distinction between matters that are directory and matters that are imperative is well known to us all in the common language of the courts at Westminster. I am not sure that it is the most fortunate language that could have been adopted to express the idea that it is intended to convey; but still, that is the recognized language, and I propose to adhere to it. The real question in all these cases is this:* ***A thing has been ordered by the legislature to be done. What is the consequence if it is not done?*** *In the case of statutes that are said to be imperative, the Courts have decided that if it is not done the whole*

thing fails, and the proceedings that follow upon it are all voids. On the other hand, when the Courts hold a provision to be mandatory or directory, they say that, although such provision may not have been complied with, the subsequent proceedings do not fail. Still, whatever the language, the idea is a perfectly distinct one. There may be many provisions in Acts of Parliament which, although they are not strictly obeyed, yet do not appear to the Court to be of that material importance to the subject-matter to which they refer, as that the legislature could have intended that the non-observance of them should be followed by a total failure of the whole proceedings. On the other hand, there are some provisions in respect of which the Court would take an opposite view, and would feel that they are matters which must be strictly obeyed, otherwise the whole proceedings that subsequently follow must come to an end".

[25] In the absence of any express provision, the intention of the legislature must be ascertained by weighing the consequences of holding a statute to be directory or mandatory and having regard to the importance of the provision in relation to the general object intended to be secured by the Act *(Caldow v. Pixcell* (1877) 1 CPD 52, 566) & *Dharendra Kriisna v. Nihar Ganguly* (AIR 1943 Cal. 266). As held in *Attorney General's Reference (No 3 of 1999),* the emphasis ought to be on the consequences of non-compliance, and asking the question of whether Parliament can fairly be taken to have intended total invalidity.

[26] Now the question is, to which category does Section 10 in this case belong? The question as to whether Section 10 is mandatory or directory depends on the intent of the legislature, and not upon its language, irrespective of the fact that Section 10 is couched in language which refers to the word "shall". The intention of the legislature must be ascertained not only from the phraseology of Section 10, but also by considering its purpose, its design and more importantly, the consequences which would follow from construing it one way of another.

[27] Again, the question is, what is the consequence of the failure to adhere to the time limit specified in Section 10 that has been intended by the legislature to be categorized as mandatory or directory. Accordingly, one has to identify the tests to be applied in deciding whether a provision that has been disregarded as mandatory or directory, and then applies them to the statute which stipulates the determination shall be made within the

time limit specified therein, but makes no reference to any penal consequences.

Avoidance of doubt clause

[28] Dr. Felix further relied on the avoidance of doubt clause in Section 15 of the Tax Appeals Commission Act to argue that Section 15 would be rendered nugatory if the provisions of Section 10 are considered to be directory. A perusal of Section 15 of the Tax Appeals Commission (Amendment) Act, No. 20 of 2013 reveals that it relates to appeals that have been transferred to the Commission from the Board of Review, and provides that the Tax Appeals Commission shall have the power to make a determination in respect thereof, beyond twelve months granted for its determination of appeals by the Inland Revenue (Amendment) Act No. 23 of 2011.

[29] It seems to me that the avoidance of doubt clause in Section 15 applies to appeals transferred from the Board of Review and not to new appeals directly filed before the Tax Appeals Commission. On the other hand, the intention of the legislature in Section 15 is to empower the Commission to hear an appeal transferred to it by the Board of Review under Section 10 of the Act, notwithstanding the expiry of the twelve months granted for its determination by the Tax Appeals (Amendment) Act, No. 4 of 2012. It seems to me that Section 15 manifests that the legislature never intended that the time period specified in the general scheme of the Tax Appeals Commission Act to be mandatory and holding otherwise, would not promote the main object of the legislature reflected in the Act.

Consequence of non-compliance with a statutory provision

[30] In considering a procedural requirement from this angle, a court is likely to construe it as mandatory if it seems to be of particular importance in the context of the enactment, or if it is one of a series of detailed steps, perhaps in legislation which has created a novel jurisdiction, (*Warwick v. White* (1722) Bunb. 106; 145 E.R. 612) or if non-compliance might have entailed penal consequences for one of the parties (*State of Jammu and Kashmir v. Abdul Ghani* (1979) Ker LJ 46). Where the disobedience of a provision is made penal, it can safely be said that such provision was

intended by the legislature to be mandatory (*Seth Banarsi Das v. The Cane Commissioner* & Another, AIR 1955 All 86).

[31] As noted, the fact that no penal consequence is stated in a statute, however, is only one factor to be considered towards a directory construction, and there are other factors to be considered in determining whether a provision of a Statute is mandatory or not. As noted, one of the factors in determining whether the consequence of non-compliance provision was intended by the legislature to be mandatory or directory is to consider the broad purpose and object of the statute as Lord Penzance stated in *Howard v. Bodington* (*supra*) at 211 as follows:

> *"I believe, as far as any rule is concerned, you cannot safely go further than that in each case you must look into the subject-matter: consider the importance of the provision that has been disregarded, and the relation of that provision to the general object intended to be secured by the Act; and upon a review of the case in that aspect decide whether the matter is what is called imperative or only directory."*

[32] The legislature is a purposive act, and judges should construe statutes to execute that legislative purpose, intent and context (Robert A. Katzmann, Judging Statutes 31 (2014) by focusing on the legislative process, taking into account the problem that the legislature was trying to solve (Henry M. Hart, Jr. & Albert M. Sacks, "The legal Process: Basic Problems in the Making and Application of Law" 1182 (William N. Eskridge, Jr. & Phillip P. Frickey Eds., (1994). We must thus, ascertain what the legislature was trying to achieve by amending the Tax Appeals Commission Act, twice as far as the time bar is concerned.

[33] A legislative intention to amend Section 10 twice by increasing the time periods for the determining of appeals does not necessarily or conclusively mean that the failure to make the determination of the Tax Appeals Commission within the time limit specified in Section 10 is mandatory. If such drastic consequence was really intended by the legislature, it would have made appropriate provisions in express terms in Section 10 to the effect that "the appeal shall be deemed to have been allowed where the Tax Appeals Commission fails to adhere to the time limit specified in Section 10 of the Tax Appeals Commission Act.

[34] There are guidelines in tax statutes which stipulate that the failure to observe any time limit provision would render the appeal null and void or that the appeal shall be deemed to have been allowed. For example, Section 165 (14) of the Inland Revenue Act, No. 10 of 2006 as amended, provides that "an appeal preferred to the Commissioner-General shall be agreed to or determined by the Commissioner-General within a period of two years from the date on which such petition of appeal is received…". The same section specifically stipulates that "where such appeal is not agreed to or determined within such period, the appeal shall be deemed to have been allowed and tax charged accordingly".

[35] The legislature in its wisdom has placed a time limit for the speedy disposal of appeals filed before the Commissioner-General and the overall legislative intention sought to be attained by the Inland Revenue Act in Section 165 (14) was to ensure that an appeal before the Commissioner-General of Inland Revenue is disposed of within a period of 2 years from the date on which the Petition of Appeal is received. As the Commissioner-General is an interested party against another interested party (tax payer) in the tax collection, it shall determine the appeal within 2 years from the receipt of the Petition of Appeal and if not, the appeal shall be deemed to have been allowed, and tax charged accordingly, so as to safeguard the rights of the taxpayer

[36] Although the Tax Appeals Commission Act was amended by Parliament twice and increased the period within which the appeal is to be determined by the Commission from 200 days to 270 days with retrospective effect, the legislature in its wisdom did not specify any penal consequence or any other consequence of non-compliance of the time bar specified in Section 10 of the Tax Appeals Commission Act. Had the legislature intended that the non-compliance with Section 10 to be mandatory, it could have easily included a provision with negative words requiring that an act shall be done in no other manner or at no other time than that designated in the Section or a provision for a penal consequence or other consequence of non-compliance. This proposition was echoed by FOTH, C. J. in *Paul v. The city of Manhattan* (1973) 212 Kan 381 as follows:

> *"The language of the enactment itself may provide some guidance. Thus, we said in Shriver v. Board of County Commissioners, 189 Kan.*

548, 370 P. 2d 124, "Generally speaking, statutory provisions directing the mode of proceeding by public officers and intended to secure order, system and dispatch in proceedings, and by a disregard of which the rights of parties cannot be injuriously affected, are not regarded as mandatory, unless accompanied by negative words importing that the acts required shall not be done in any other manner or time than that designated". (p. 556. Emphasis added). A critical feature of mandatory legislation is often a provision for the consequences of non-compliance. This element was noticed by early legal commentators, for in Bank v. Lyman, supra, we find this observation (p. 413)."

[37] Bindra's Interpretation of Statutes, 10th Ed. referring to the decision of *Paul v. The city of Manhattan* (supra), states that factors which would indicate that the provisions of a Statute or Ordinance are mandatory are: (1) the presence of negative words requiring that an act shall be done in no other manner or at no other time than that designated; or (2) a provision for a penalty or other consequence of non-compliance (p. 433).

[38] The object sought to be attained by Section 10 of the Tax Appeals Commission Act has been designed primarily to expedite the appeal process filed before the Tax Appeals Commission, which was established by an Act of Parliament comprising retired Judges of the Supreme Court or the Court of Appeal and those who have gained wide knowledge and eminence in the field of Taxation.

[39] It is settled law that the Courts cannot usurp legislative function under the disguise of interpretation and rewrite, recast, reframe and redesign the Tax Appeals Commission Act, because this is exclusively in the domain of the legislature. This proposition was lucidly explained by Lord Simonds in *Magor and St Mellons Rural District Council v. Newport Corporation* [1951] 2 All ER 839, HL. Referring to the speech of Lord Denning MR, Lord Simonds said at page 841: "It appears to me to be a naked usurpation of the legislative function under the thin disguise of interpretation", Lord Simonds further stated at 841:

"The duty of the court is to interpret the words that the legislature has used; those words may be ambiguous, but, even if they are, the power and the duty of the court to travel outside them on a voyage of discovery are strictly limited. If a gap is disclosed, the remedy lies in an amending Act and not in a usurpation of the legislative function under the thin disguise of interpretation".

[40] The same proposition was echoed by Arijit Pasayat, J. in the Indian Supreme Court case of *Padmasundara Rao and Ors. v. State of Tamil Nadu and Ors.* AIR (2002) SC 1334, at paragraph 14, as follows:

> *"14. While interpreting a provision the Court only interprets the law and cannot legislate it. If a provision of law is misused and subjected to the abuse of process of law, it is for the legislature to amend, modify or repeal it, if deemed necessary".*

[41] Section 10 of the Tax Appeals Commission Act, No. 23 of 2011 granted time to the Tax Appeals Commission to hear all appeals within one hundred and eighty days from the date of the commencement of the hearing of the appeal. The Tax Appeals Commission (Amendment) Act, No. 4 of 2012 extended the said time period from one hundred and eighty days to two hundred and seventy days from the date of the commencement of the hearing of the appeal. The Tax Appeals Commission (Amendment) Act, No. 20 of 2013 however, reduced the time limit granted to the Tax Appeals Commission to conclude the appeal by enacting that the time specified in Section 10 shall commence from the date of the commencement of its sittings for hearing the appeal.

[42] The legislature has, from time to time, extended and reduced the time period within which the appeal shall be determined by the Tax Appeals Commission, but it intentionally and purposely refrained from imposing any consequence for the failure on the part of the Tax Appeals Commission to adhere to the time limit specified in Section 10.

[43] The legislature amended the Tax Appeals Commission Act, twice with retrospective effect and provided time frames to conclude appeals quickly as possible within the time limit of 270 days from the date of the commencement of its sittings for the hearing of such appeal. It is true that the legislature has amended Section 10 with the retrospective operation but if it intended to take away the jurisdiction of the Tax Appeals Commission and render its determination made outside the time limit specified in section 10 invalid, it could have easily made, with retrospective effect, appropriate provision in express terms that the appeal shall be deemed to have been allowed or other consequence of non-compliance.

[44] On the other hand, the proviso to Section 10 of the Tax Appeals Commission Act, No. 23 of 2011 granted time for the Commission to make its determination in respect of appeal transferred to the Commission from the Board of Review within hundred and eighty days (180) from the date of such transfer, notwithstanding anything contained in any other written law. The Tax Appeals Commission (Amendment) Act, No. 4 of 2012 extended the said time period from hundred and eighty days to twelve months of the date on which the Commission shall commence its sittings. (Vide-Section 7 of the Act, No. 4 of 2012). The Tax Appeals Commission (Amendment) Act, No. 20 of 2013 extended the said time period to twenty-four months from the date on which the Commission shall commence its sittings for the hearing of each such appeal.

[45] It is crystal clear that these procedural time limit rules in respect of appeals received by the Tax Appeals Commission or appeals transferred from the Board of Review to the Commission have been devised by the legislature to facilitate the appeal process by increasing and reducing the time period within which such appeals shall be concluded. The provision for the determination of an appeal by the Tax Appeals Commission within a period of 270 days from the commencement of its sittings for the hearing of an appeal has been designed with a view to regulating the duties of the Tax Appeals Commission by specifying a time limit for its performance as specified in Section 10 of the Act.

[46] So that the legislature, in its wisdom has made provision in Section 10 to the effect that the appeal shall be disposed of speedily within a period of 270 days from the date of the commencement of the sittings for the hearing of the appeal. But the legislature imposed no drastic and painful penal consequence or other consequence of non-compliance, including prohibitory or negative words in Section 10, rendering the determination of the appeal null and void for non-compliance of the time limit specified in Section 10. In my view, they are not intended to make the parties suffer from the failure of the Commission to make the determination within the time limit specified in Section 10 of the Tax Appeals Commission Act.

[47] Any procedural retrospective operation of a provision, in my view, cannot take away the rights of parties who have no control over those entrusted with the duty of making determinations within the time limit

specified in Section 10. The retrospective operation of Section 10 without any penal or other consequence of non-compliance, by itself, cannot be treated as a factor in determining that the legislature intended that the failure to adhere to the time limit specified in Section 10 is mandatory.

Consequences of non-compliance with statute by those entrusted with public duty

[48] One factor that is necessary for determining whether a provision is mandatory or directory is to find as to who breached the time limit specified in Section 10-whether it was breached by one of the parties to the action or by those entrusted with the performance of a public duty. Also coming under this head are cases where the Court will take into account the practical inconveniences or impossibilities of holding a time limit requirement to be mandatory where the public duty is performed by a public body. If the statutory provision relates to the performance of a public duty, the Court is obliged to consider whether any consequence of such breach would work serious public inconvenience, or injustice to the parties who have no control over those entrusted with such public duty.

[49] It is true that the Tax Appeals Commission Act has imposed a duty on the Tax Appeals Commission to make the determination within the time limit specified in Section 10 but the parties had no control over those entrusted with the task of making the determination within the time limit specified in Section 10. Should the parties who have no control over those entrusted with the task of making the determination be made to suffer for any failure or delay on the part of the Tax Appeals Commission in not making its determination within the time limit specified in Section 10? I do not think that the legislature intended that the time limit specified in Section 10 is mandatory where it is impossible for the Commission to make its determination within such period due to practical reasons or where the parties had no control over those entrusted with the task of making the determination within the time limit specified in Section 10. I held the same view in our decision in *S.P. Muttiah v Commissioner General of Inland Revenue* (CA Tax 46/2019).

[50] Maxwell, Interpretation of Statute, 11th Ed. at page 369 referring to the ascertaining the intention of the legislature in relation to the interpretation of limitation provision states:

> *"On the other hand, where the prescriptions of a statute relate to the performance of a public duty and where the invalidation of acts done in neglect of them would work serious general inconvenience or injustice to persons who have no control over those entrusted with the duty without promoting the essential aims of the Legislature, such prescriptions seem to be generally understood as mere instructions for the guidance and government of those on whom the duty is imposed, or, in other words, as directory only. The neglect of them may be penal, indeed, but it does not affect the validity of the act done in disregard of them. It has often been held, for instance, where an Act ordered a thing to be done by a public body or public officers and pointed out the specific time when it was to be done, then the Act was directory only and might be complied with after the prescribed time" [emphasis added.]*

[51] Where the statute imposes a public duty on persons and to treat, as void, acts done without compliance with the statute would cause serious inconvenience to persons who have no control over those entrusted with this duty, then the practice is to hold the provision to be directory only so as not to affect the validity of such action taken in breach of such duty (*Montreal Street Rly. Co. v. Normandin* (1917) AC 170, 175). Lord Sir Arthur Channell echoed this proposition in that case at p. 176 as follows:

> *"When the provisions of a statute relate to the performance of a public duty and the case is such that to hold null and void acts done in neglect of this duty would work serious general inconvenience, or injustice to persons who have no control over those entrusted with the duty, and at the same time would not promote the main object of the Legislature, it has been the practice to hold such provisions to be directory only, the neglect of them, though punishable, not affecting the validity of the acts done. This principle has been applied to provisions for holding sessions at particular times and places (2 Hale, P. C., p. 50, Rex v. Leicester Justices (1827) 7 B & C. 6 and Parke B. in Gwynne v. Burnell (1835) 2 Bing. N.C. 7);….".*

[52] This proposition is further confirmed by Sutherland's Statutory Construction, Third Ed. Vol. 3. at p. 102 as follows:

> *"A statute specifying a time within which a public officer is to perform an official act regarding the rights and duties of others is directory unless the nature of the act to be performed, or the phraseology of the statute, is such that the designation of time must be considered a limitation of the power of the Officer". At p. 107 it is pointed out that a statutory direction to private individuals should generally be considered as mandatory and that the rule is just the opposite to that which obtains with respect to public officers. Again, at p. 109, it is pointed out that often the question as to whether a mandatory may be directory construction should be given to a statutory provision may be determined by an expression in the statute itself of the result that shall follow the non-compliance with the provision...."*

[53] If we hold that the literal compliance with the time limit specified in Section 10 is mandatory, disregarding the fact that neglect was performed by those who are entrusted with the duty, we will be disregarding the practical impossibility of the Commission and inconvenience of holding proceedings and making a determination strictly within the time limit specified in Section 10. In the present case, the duty to make the determination within the time limit specified in Section 10 is statutorily entrusted to the members of the Tax Appeals Commission in terms of the provisions of the Tax Appeals Commission Act, No. 23 of 2011 as amended, and the parties had no control whatsoever, over the Tax Appeals Commission.

[54] As Lord Sir Arthur Channell put it correctly, it would cause the greatest injustice to both parties who had no control over those entrusted with the duty of making the determination, if we hold that neglect to observe the time limit specified in Section 10 of the statute renders the determination made by the Commission *ipso facto* null and void. In my view, every limitation period within which an act must be done, is not necessarily a prescription of the period of limitation with painful and drastic consequences and the parties who have no control of those entrusted with a statutory duty and no fault of them should not be made to suffer and lose their rights for the failure to adhere to the time limitation specified in a provision.

[55] In *S.P. Muttiah v. Commissioner General of Inland Revenue* (supra), this Court held at page 77 and 78;

'If we interpret the legislative intent of Section 10 from its mere phraseology, without considering the nature, purpose, the design, the absence of consequences of non-compliance and practical impossibility, which would follow from construing it one way or the other, it will tend to defeat the overall object, design, the purpose and spirit of the Tax Appeals Commission Act"

[56] If we hold that the determination of the Commission is null and void, it will cause serious injustice to parties who have no control over those entrusted with the duty of discharging functions under the Tax Appeals Commission Act. In *Stafford Motor Company Limited v. The Commissioner General of Inland Revenue (supra),* Janak de Silva, J. held that the time limits granted to the Tax Appeals Commission to make a determination is not mandatory as the Tax Appeals Commission Act, No. 23 of 2011 (as amended) does not spell out any sanction for the failure on the part of the Tax Appeals Commission to comply with the time limit set out in Section 10 of the Tax Appeals Commission Act.

[57] In the same case, Janak de Silva, J. having specifically considered the implication of the Court of Appeal decision in *Mohideen v. Commissioner-General of Inland Revenue* ((CA 2/2007 (20-15) Vol. XXI. BASL Law Journal, page 170), held at page 6 that the statement made by His Lordship Gooneratne J. referring to the statutory time bar applicable to the Board of Review in making its determination under the Inland Revenue Act, No. 38 of 2000 to the effect that

"*If specific time limits are to be laid down, the legislature needs to say so in very clear and unambiguous terms instead of leaving it to be interpreted in various ways. To give a restricted interpretation would be to impose unnecessary sanctions on the Board of Review. <u>It would be different or invalid if the time period exceeded two years from the date of oral hearing. If that be so, it is time barred.</u>" was an obiter dicta statement (*emphasis added).

[58] The principle laid down by Gooneratne J. in *Mohideen v. Commissioner General Inland Revenue* (supra) was that the hearing for the purpose of time limit of 2 years specified in the second proviso to Section 140 (10) of the Inland Revenue (Amendment) Act, No. 37 of 2003 commences from the date of the oral hearing and no more. That was the

principle upon which the case was decided by His Lordship Gooneratne J. which represents the reason and spirit of the decision, and that part alone is the principle which forms the only authoritative element of a precedent in *Mohideen v. Commissioner General Inland Revenue* (supra).

[59] In *Mohideen v. Commissioner General Inland Revenue* (supra), after having fully endorsed the proposition of law that the hearing contemplated in the said time bar provision is nothing but the oral hearing, His Lordship as a passing remark stated "It would be different or invalid if the time period exceeded 2 years from the date of the oral hearing. If that be so, it is time barred" (p. 176). That part of the statement enunciated by His Lordship Gooneratne J. is manifestly an obiter and not the ratio having a binding authority. Justice Jank de Silva, in *Staford Motors v. Commissioner-General of Inland Revenue (supra)*, *Kegalle Plantations PLC v. The Commissioner-General of Inland Revenue* (CA/Tax 09/2017 decided on 04.09.2014) and *CIC Agri Business (Private) Limited v. The Commissioner-General of Inland Revenue* (CA/Tax 42/2014 decided on 29.05.2021), arrived at a similar conclusion.

[60] We took the same view in our judgments in *Mr. S.P. Muttiah v. The Commissioner General of Inland Revenue, CA*/TAX/46/2019, decided on 26.06.2021 and *Amadeus Lanka (Pvt) Ltd v. CGIR (*C.A Tax 4/19 decided on 30.07.2021. In *Mr. S.P. Muttiah v. The Commissioner General of Inland Revenue*, we further held that the directory interpretation of Section 10 is consistent with the object, purpose and design of the Tax Appeals Commission Act, which is reflected in the intention of the legislature and that if a gap is disclosed in the Legislature, the remedy lies is an amending Act and not in a usurpation of the legislative function under the thin disguise of interpretation.

[61] I hold that having considered the facts and he circumstances and legal principles, the failure to adhere to the time limit specified in Section 10 was not intended by the legislature to be mandatory with painful and drastic consequences of rendering such determination null and void.

[62] For those reasons, I hold that the determination of the Tax Appeals Commission in the present case is not time barred and thus, I answer the Question of Law No. 1 in favour of the Respondent.

Question of Law No. 2

Exemption conferred under and in terms of Section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006 read with Article 25 of the Double Taxation Avoidance Agreement between the Government of India and Sri Lanka?

[63] At the hearing, Dr. Shivaji Felix submitted that the activity undertaken by the Appellant constitutes an offshore business within the contemplation of Section 13 (b) (ii) of the IRA, 2006 and that the Tax Appeals Commission erred in holding that as sales of goods take place in Sri Lanka, and therefore the Appellant has not fulfilled the requirement of offshore business specified in Section 13 (b)(ii) of the Inland Revenue Act. He further submitted that the Appellant has a fiscal domicile in India and as such, it has duly paid income tax in respect of all profits earned in India in respect of profits earned in India and further, the Appellant has a permanent establishment (PE) in Sri Lanka within the meaning of Article 25 of the Double Taxation Avoidance Agreement between India and Sri Lanka (hereinafter referred to as the "DTAA").

[64] He submitted, therefore that the Appellant is subject to the Sri Lankan tax laws in respect of profits attributable to its permanent establishment (PE) in Sri Lanka subject to the stipulations of relevant laws in Sri Lanka. His argument was that the non-discrimination clause under Article 25 of the DTAA requires that a non-resident company must be treated in the same way as a resident company and that the Appellant being a non-resident company is entitled to the income tax exemption granted to a resident company under Section 13 (b)(ii) of the IRA 2006.

[65] On the other hand, the learned Additional Solicitor General submitted that the Appellant is not a resident company within the meaning of Section 79(1) of the Inland Revenue Act and therefore, the Appellant falls outside the scope of Section 13 (b)(ii) of the Inland Revenue Act. He further submitted that the Appellant does not satisfy a separate and independent condition in Section 13(b)(ii) by remitting through a bank in Sri Lanka its profits or income less amount expended outside Sri Lanka.

[66] In my view the three vital questions that arise for consideration under this question of law No. 2 are:

1. Whether the Appellant being a resident company in India is entitled to income tax exemption conferred under Section 13 (b)(ii) of the Inland Revenue Act No. 10 of 2006 (as amended);
2. If not, whether the Appellant being a non-resident company in Sri Lanka carries on business through a permanent establishment in Sri Lanka by virtue of the Article 5 of the DTAA between India and Sri Lanka;
3. If so, whether the Appellant, comparatively placed with a resident company in similar circumstances and under similar conditions carries on similar activities in Sri Lanka through a permanent establishment under the provisions of the DTAA between India and Sri Lanka;
4. If so, whether the Appellant is entitled to the exemption under Section 13 (b)(ii) of the IRA, 2006 by virtue of the application of the non-discrimination clause under Article 25 of the DTAA between India and Sri Lanka;
5. If not, whether the Appellant is entitled to exempt the amount of Rs. 37,522,673/- earned by the Appellant on sales in question under Section 13 (b)(ii) of the IRA 2006, read with Article 25 of the DTAA between India and Sri Lanka.

Applicability of Section 13 (b)(ii) of the Inland Revenue Act.

[67] The Appellant has, in the returns of income deducted the profits of Rs. 37,522,673/- on account of sales outside Sri Lanka from its offshore business and claimed the tax exemption under Section 13 (b)(ii) of the Inland Revenue Act. Section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006 reads as follows:

"There shall be exempt from income tax-

(a)...

(b) the profits and income earned in foreign currency by a resident company or partnership carrying on or exercising any trade, business or vocation, in any year of assessment-

(i)...

*(ii) in respect of any **offshore business** which does not in any way involve any **goods manufactured or produced in Sri Lanka** or any **goods imported into Sri Lanka**; and....*

in the course of carrying on or exercising such trade, business or vocation, if such ***profits and income*** *(less any such amount expended by that company or partnership outside Sri Lanka as is considered by the Commissioner General to be reasonable expenses)* ***are remitted to Sri Lanka through a bank".***

[68] For profit and income earned to be exempt from income tax under Section 13 (b)(ii) of the IRA, 2006 must satisfy the following requirements:

1. The profits and income must be earned by a **resident company**;
2. The profits and income earned by such resident company must be engaged in **offshore business**;
3. The offshore business does not involve any **goods manufactured or produced in Sri Lanka or any goods imported into Sri Lanka**;
4. The profits and income should be earned in **foreign currency**;
5. The **profits and income of such offshore business** (less the deduction of expenses expended outside Sri Lanka as considered to be reasonable by the Commissioner General) must be **remitted to Sri Lanka through a bank.**

[69] I shall now consider the first issue identified in paragraph 68 above. The Assessor, the Respondent and the Tax Appeals Commissioner have denied the exemption claimed by the Appellant on the ground that the Appellant is a non-resident company and therefore, the Appellant is not entitled to the exemption as specified in Section 13 (b)(ii) of the IRA, 2006. What constitutes a residence is defined in Section 79 (i) of the Inland Revenue Act, No. 10 of 2006. It reads as follows:

"(1) Where a company or a body of persons has its registered or principal office in Sri Lanka, or where the control and management of its business are exercised in Sri Lanka, such company or body of persons shall be deemed to be resident in Sri Lanka for the purposes of this Act".

[70] In order that a company should be resident, it is necessary to satisfy the following two requirements under Section 79 (1) of the IRA, 2006:

1. The company has its registered or principal office in Sri Lanka; or

2. The control and management of its business are exercised in Sri Lanka.

[71] According to the Appellant's own document dated 20.10.2016 (at page 32 of the brief), "Johnson & Johnson Private Limited is a company that is **incorporated in India and maintains a branch office in Sri Lanka"** and the Corporate Office, Arena Space, Off, JVLR, Behind Majas Depot, Jogeshwari (E) Mumbai, 400 060, India. Its Registered Office is, L.B.S. Marg., Mulund (W), Mumbai 400 080", India. The Appellant company (Johnson & Johnson Pvt Limited) is a company incorporated and registered in India, a place outside Sri Lanka and having a branch office in Sri Lanka. The Appellant is not a resident company within the meaning of section 79(1) of the Inland Revenue Act, No. 10 of 2006. Accordingly, the Appellant is not a resident company within the meaning of Section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006.

Applicability of the Double Taxation Avoidance Agreement (DTAA)

[72] The matter did not rest there. The Appellant, claims that it is nevertheless entitled to the benefit of Section 13 (b)(ii) of the IRA, 2006 on the basis that the Appellant being a non-resident company should be treated in the same way as a resident company for the purpose Section 13 (b)(ii), by virtue of the permanent establishment clause under Article 5 and non-discrimination clause under Article 25 of the DTAA between India and Sri Lanka.

[73] The Government of Sri Lanka entered into a Double Taxation Avoidance Agreement (DTAA) with the Government of India on 27.01.1982 for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital and the text of the Agreement was published in Gazette Extraordinary No. 210/17 of 17.09.1982. Thereafter, the Government of Sri Lanka entered into a new Double Taxation Avoidance Agreement with the Government of India on 22.01.2013 and the new Agreement was published in Gazette Extraordinary No. 1828/9 of 17.09.2013 and the previous Agreement ceased to have effect (Article 30.4 of the new Agreement) when the provision of this new Agreement becomes effective in accordance with the provisions of paragraph Article 30.3 of the new Agreement. As the present appeal relates to the year of assessment 2011/2012, the provisions of the DTAA entered on 27.01.1982 will apply to the said year of assessment.

[74] It is relevant to note that the benefit of the DTAA between India and Sri Lanka applies to residents of one or both of the contracting states and therefore, a person who is not a resident of one of the contracting states, is outside the scope of the DTAA between India and Sri Lanka. The DTAA applies to taxes on income and capital imposed on behalf of each contracting state, irrespective of the manner in which they are levied (Article 2.2) and the existing taxes to which this Convention shall apply in Sri Lanka are (i) the income-tax, including the income-tax based on the turnover of enterprises licensed by the Greater Colombo Economic Commission; and (ii) the wealth-tax (Article 2.3). Article 2 (4) of the Double Taxation Avoidance Agreement (DTAA) between Sri Lanka and India states:

> *"This Convention shall also apply to any identical or substantially similar taxes which are imposed after the date of signature of this Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of any important changes which have been made in their respective taxation laws".*

[75] The term "competent authority" referred to in Article 2 (4) means: (i) in India: The Finance Minister, Government of India, or his authorized representative; and (ii) In Sri Lanka: The Commissioner General of Inland Revenue (Article 3 (g).

Effect of DTAA & Relief from Income Tax under the DTAA

[76] The DTAA is a contract between two Sovereign Governments of India and Sri Lanka and the contract has been signed by the two sovereign governments with full knowledge, understanding and free consent of both the governments. Relief by way of an exemption shall be considered in case of a DTAA in terms of Section 97 of the Inland Revenue Act, No. 10 of 2006. Section 97 reads as follows:

> *"97 (1) (a) Where Parliament by resolution approves any agreement entered into between the Government of Sri Lanka and the Government of any other territory or any agreement by the Government of Sri Lanka with the Governments of any other territories, for the purpose of affording relief from double taxation in relation to income tax under Sri Lanka law and any taxes of a similar character imposed by the laws of that territory, the agreement shall, notwithstanding anything in any other written law, have the force of law in Sri Lanka, in so far as it provides for–*

(i) *relief from income tax;*

(ii) *determining the profits or income to be attributed in Sri Lanka to persons not resident in Sri Lanka, or determining the profits or income to be attributed to such persons and their agencies, branches or establishments in Sri Lanka;*

(iii) *determining the profits or income to be attributed to persons resident in Sri Lanka who have special relationships with persons not so resident*

(iv) *exchange of information; or*

(v) *assistance in the recovery of tax payable.*

[77] There are two situations under which the relief can be achieved in Sri Lanka under the DTAA between India and Sri Lanka:

(a) Where income tax has been paid under the Income-tax Act of Sri Lanka and the corresponding Indian Income Act or income tax remains taxable in both countries (whether at a full or reduced rate), as the country of residence, Sri Lanka will give a tax credit for the purpose of Sri Lankan taxation; or

(b) Where exemption from taxation exists, Sri Lanka may grant the exemption from income tax in respect of the agreed source of income under the DTAA subject to conditions laid down in the domestic law or the DTAA.

[78] As per the Inland Revenue Act (S. 97), where the government has entered into a DTAA, then in relation to the assessee to whom such Agreement applies, the provisions of the DTAA, with respect to cases to which they would apply, would operate even if inconsistent with the provisions of the Inland Revenue Act. As a consequence, if a tax liability is imposed by the provisions of the IRA, the DTAA may be referred to and relief may be granted either by deducting or reducing the tax liability and the Treaty provisions would prevail, and are liable to be enforced in Sri Lanka and India.

Was the Appellant having a "permanent establishment" in Sri Lanka?

[79] The next point that arises is whether the Appellant company being a non-resident company carried on business in Sri Lanka through a "permanent establishment" (PE) which can be taxed in Sri Lanka by virtue of the application of Article 5 of the DTAA between India and Sri Lanka. It was the submission of Dr. Felix that the Appellant has a permanent

establishment (PE) in Sri Lanka in terms of Article 5 (2)(b) of the DTAA, and therefore, the Appellant is taxable in respect of profits earned in India and further, the Appellant is subject to the provisions of the Inland Revenue Act in respect of profits or income attributable to its permanent establishment (PE) in Sri Lanka, irrespective of whether the Appellant is non-resident company in Sri Lanka.

[80] By virtue of Article 7 (1) of the DTAA, the profits of an enterprise of a Contracting State shall be taxable only in that Contracting State unless the enterprise carries on business in the other Contracting State through a permanent establishment (PE) situated therein. It further provides *inter alia,* that if the enterprise carries on business through a PE, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that PE. in Sri Lanka. Thus, where a company incorporated in India carries on business through PE in Sri Lanka, its business income may be taxable in Sri Lanka to the extent to which it is attributable to such PE in Sri Lanka. The same principle applies where a company incorporated in Sri Lanka carries on business through PE in India, its business income may be taxable in India to the extent to which it is attributable to such PE in India on the basis of parity of status.

Permanent Establishment (PE)

[81] The word "permanent establishment" is, of course, a concept created by the DTAA for tax purposes and it can be described as a taxable entity which is commonly used in all international Double Taxation Avoidance Agreements, based on standard O.E.C.D or UN Model and their commentaries. Article 5 (1) defines the term “permanent establishment” as a “fixed place of business of an enterprise is wholly or partly carried on”. It reads as follows”

> *“1. For the purposes of this Convention, the term “permanent establishment” means a fixed place of business through which the business of the enterprise is wholly or partly carried on”.*

[82] Article 5 (2) describes what permanent establishment includes. It reads as follows:

> *“2. The term “permanent establishment” shall include especially:*
>
> *(a) a place of management;*
>
> ***(b) a branch;***

(c) an office;

(d) a factory;

(e) a workshop;

(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources; (g) an agricultural or farming estate or plantation;

(h) a building site or construction or assembly project which exists for more than 183 days;

(i) the furnishing of services, including consultancy services, by an enterprise through employees or other personnel, where activities of that nature continue within the country for a period or periods aggregating more than 183 days within any twelve-month period".

[83] Article 5 (3) describes what permanent establishment does not include. It reads as follows:

"3. Notwithstanding the preceding provisions of this article, the term "permanent establishment" shall be deemed not to include:

(a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;

(b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;

(c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; and

(e) the maintenance of a fixed place of business solely for the purpose of advertising for the supply of information or for scientific research, being activities solely of a preparatory or auxiliary character in the trade or business of the enterprise.

4. A person acting in a Contracting State on behalf of an enterprise of the other Contracting State - other than an agent of an independent status to whom paragraph (6) of this article applies - shall be deemed to be a permanent establishment in the first-mentioned State if he has, and habitually exercises in that State, an authority to conclude

contracts in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise.

5. Notwithstanding the preceding provisions of this article, an insurance enterprise of a Contracting State shall, except in regard to reinsurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person other than an agent of independent status to whom paragraph (6) of this article applies.

6. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that Sate through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph.

7. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise) shall not of itself constitute either company a permanent establishment of the other.

[84] The fundamental principle of the DTAA is that for the application of the DTAA, a person, whether an individual or company from one country (Country "A") will be taxable in the other country (Country "B") only if he has a permanent establishment (PE) in Country "B". Thus, if there is a PE, only the income attributable to such PE in Country "B" will be subject to tax in Country "B". Accordingly, a non-resident company will be liable to income tax in Sri Lanka if it carries on a trade in Sri Lanka through a permanent establishment (i.e., a branch or agency) and where a DTAA applies, a similar principle applies with an additional concept of non-discrimination. Section 97 of the Inland Revenue Act, No. 10 of 2006 however, does not speak of the concept of the permanent establishment (PE). The Inland Revenue Act, No. 24 of 2017 as amended by the Inland Revenue (Amendment) Act, No. 21 of 2021 however, defines the term "permanent establishment" (Vide-Section 76 [(2)(b)].

[85] There are three distinct ways in which a permanent establishment (PE) can be established in terms of Article 5 of the DTAA between India and Sri Lanka.

1. Fixed place PE;
2. Consultancy PE;
3. Agency PE

Fixed place-positive list-Article 5 (2)

[86] In the case of fixed place PE, there must be a fixed place of business, through which business is carried on by the enterprise wholly or partly and in this fixed place PE, the PE shall be an establishment referred to in Article 5 (2) through which the business of an enterprise is wholly or partly carried on. The profits of any non-resident foreign company that is registered in Sri Lanka as an overseas company in terms of the provisions of the Companies Act, 07 0f 2007, are taxable only where the said company carries on its business through a permanent establishment in Sri Lanka.

Negative list-Article 5(3)

[87] A treaty also provides a negative list–i.e., certain activities of a preparatory or auxiliary character will not constitute a PE as set out in Article 5(3). Thus, the mere maintenance of a fixed place of business solely for the purposes referred to in Article 5 (3) including the mere preparation or auxiliary character in the business would be insufficient to create a PE.

Consultancy PE

[88] In the case of consultancy PE, a person in one country (India) may work in the other country (Sri Lanka) for a particular period without having a fixed place such as a branch office or factory or workshop in Sri Lanka. But such person in another country (India) comes to work in Sri Lanka in a project of any construction company, which continues for more than 183 days, such a project may be considered a PE in Sri Lanka.

Agency PE

[89] In the case of agency PE, the enterprise (India) in the other country, (Sri Lanka) can be a person, without a fixed place, who is appointed as an agent in Sri Lanka and is vested with authority to regularly act or habitually exercise the authority on its behalf and to conduct business and conclude contracts in the name of the enterprise.

[90] As far as this case is concerned, the relevant PE is the fixed place of business and Article 5 of the DTAA provides a list of positive examples of fixed base PE, including a place of management, **a branch,** an office, a factory or a workshop etc. It is not in dispute that the Appellant company is a non-resident company, but has a **branch in Sri Lanka** (Johnson & Johnson Ltd (Sri Lanka Branch), No. 11, Castle Lane, Colombo 04 and it has been registered as a company in Sri Lanka (pp. 1-2,5, 10, 32, 74). According to the Company Registrar's Certificate as indicated in the Respondents reasons for the determination (p. 10), the Appellant company's branch has been registered under Section 3 (2) of the Companies (Special Provisions) Act, No. 19 of 1974 and its principal place of business in Sri Lanka is at No. 41, Janadhiipathi Mawatha, Colombo 01 (as per its Memorandum of Association and Articles of Association).

[91] Accordingly, I am of the view that the Appellant is a non-resident foreign company having a branch office in Sri Lanka and it is earning its profits and income from its business in Sri Lanka through a permanent establishment. Accordingly, the Appellant company can be treated as a permanent establishment (PE) with a registered branch office in Sri Lanka within the meaning of Article 5 of the DTAA between India and Sri Lanka. Accordingly, the Appellant company is subject to taxation in Sri Lanka on the profits of a business carried on in Sri Lanka, through a permanent establishment located in Sri Lanka.

Non-discrimination clause in the DTAA

[92] The next question is whether the Appellant who carried on its business through a permanent establishment in Sri Lanka can also fall within the non-discrimination clause under the DTAA so as to qualify for the treaty benefits subject to the stipulations of the other provisions of the DTAA read with the provisions of the Inland Revenue Act, No. 10 of 2006.

[93] It was the contention of Dr. Felix that the Appellant is taxable in India in respect of profits earned in India and the Appellant has duly paid income tax in India in respect of all profits earned in India. Then, he submitted that the Appellant is also taxable in Sri Lanka in respect of profits attributable to its permanent establishment in Sri Lanka subject to the tax laws of Sri Lanka by virtue of the non-discrimination clause in Article 25 of the DTTA.

[94] The learned Additional Solicitor General, however, submitted that the question of applicability of the exemption to a non-resident has to be tested on the "same conditions' as it applies to a resident and "in the same

circumstances" both in fact and law as it applies to a resident. He further submitted that the appropriate step is to examine whether the exemption would have been allowed to a non-resident carrying on the same activities under the "same conditions" and "same circumstances" as set out in Article 25 of the DTAA.

[95] The Indo-Sri Lanka DTAA, has a non-discrimination clause in the form of Article 25 which prohibits taxation which discriminates against the nationals or individuals of the other treaty country. It permits a permanent establishment of a non-resident company to claim equal treatment with a domestic enterprise of the country in which it is situated and receive a treatment no different from a resident company in that country. It means that the national treatment obligation applies if the nationals or residents of the two States are comparably placed or that two persons similarly situated must be treated similarly (Taxmann's Indian Double Taxation Agreements & Tax Laws, Vol. 1, 2004, para 30.3). The principal object is to forbid discrimination or unequal treatment in situations which are identical or comparable, and the principle requires that similar situations shall not be treated differently unless differentiation is objectively justified (supra).

[96] Article 25 of the DTAA between India and Sri Lanka also deals with the elimination of tax discrimination in certain precise circumstances and it reads as follows:

"ARTICLE 25 - Non-discrimination–

1. *Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the* ***taxation*** *and connected requirements to which nationals of that other State* ***in the same circumstances*** *are or may be subjected. This provision shall, notwithstanding the provisions of article 1, also apply to persons who are not residents of one or both of the Contracting States.*
2. *The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the* ***taxation*** *levied on enterprises of that other State* ***carrying on the same activities****. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account*

of civil status or family responsibilities which it grants to its own residents.

3. *Except where the provisions of paragraph (1) of article 9, paragraph (7) of article 11 or paragraph (6) of article 12 apply, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first mentioned State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of such enterprise, be deductible* ***under the same conditions*** *as if they had been contracted to a resident of the first-mentioned State.*

4. *Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first mentioned State to any* ***taxation*** *or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of the first mentioned State are or may be subjected.*

5. *The provisions of this article shall, notwithstanding the provisions of article 2, apply to taxes of every kind and description.*

[97] It is significant to highlight the six basic principles contained in Article 24 of the OECD Model on non-discrimination which are more or less identical to the provisions on non-discrimination set out in the DTAA between India and Sri Lanka. Those six basic principles in Article 24 of the OECD Model on non-discrimination are as follows:

1. *Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State* ***in the same circumstances****, are or may be subjected. This provision shall, notwithstanding the fact that the persons who are not residents of one or both of the Contracting States.*

2. *Stateless persons who are residents of a Contracting State shall not be subjected in either Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of the State*

*concerned **in the same circumstances,** in particular with respect to residence, are or may be subjected.*

3. *The taxation on a permanent establishment in a Contracting State shall not be less favourably levied in that other State than the **taxation l**evied on enterprises of that other State carrying **on the same activities;***
4. *Deductions for expenditure made by a resident of one contracting state to a resident of the other shall be deductible **under the same conditions** as if they had been contracted to a resident of the first-mentioned State;*
5. *Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected;*
6. *The provisions of this Article shall, notwithstanding the provisions of Article 2, apply to taxes of every kind and description.*

[98] What is relevant is the legal situation, i.e., liability to taxation and not the fiscal fact of actual payment of tax as the expression "taxation" referred to in the DTAA, means "the entire process of imposing charge, assessment of tax as well as collection of charge" (Taxmann's Indian Double Taxation Agreements & Tax Laws, para, 306). The expression "taxation" does not mean rate of tax and it is different from levy of tax itself (supra). What the DTAA provides is that the nationals of one Contracting State shall not be subjected, in another Contracting State to any taxation, which is more burdensome than nationals of other Contracting State in the same circumstances and under the same conditions.

[99] Jonathan Schwarz in Schwarz on Tax Treaties (London: Wolters Kluwer, 2011, referring to Article 23 (2) of the UK-Switzerland Treaty, which is identical to Article 24 (3) of the OECD Model on-discrimination against permanent establishments notes that a permanent establishment shall not be less favourably levied in the other state than the taxation levied on other State carrying on the same activities. It states at p. 291:

> *"The purpose of this provision is to end all discrimination in the treatment of permanent establishments as compared with resident enterprises belonging to the same sector of activity. The form of a particular provision may be examined to ascertain whether it constitutes discrimination. It is also permissible to look at the results,*

but, a higher tax burden in a given year than that would have fallen in the branch if it had been a UK resident enterprise, is not necessarily a breach of the principle if the domestic rules accord with the principles in art. 7. The criteria for differentiation in relation to permanent establishments, is that taxation must not be less favourably levied…".

Features of non-discrimination clause in Article 25

[100] The question, however, arises to what extent the provisions of Article 25 can be interpreted to determine the non-discrimination and as to how to identify factors of discriminative treatment in specific circumstances. The provisions of Article 25 that appear to be designed in negative form, do not address all forms of possible discrimination, but seek to prevent **unjustified discrimination** and cover certain specific situations where a non-resident with a permanent establishment placed in similar situations, is impossible to meet the conditions for a specific tax treatment under the domestic law of that other State. What are these similar situations or circumstances-carrying on the same activities under the same conditions with that of the resident in another State?

[101] Article 25 assures nationals of a Contrasting State a non-discriminatory treatment by providing national treatment (paragraph 1) and residents of a Contracting State (paragraph 2) will not be subjected to discriminatory treatment in the other Contracting State. Article 25 thus, relates to the following key words:

1. Nationality & in the same circumstances -Article 25 (1);
2. In the same circumstances- Article 25 (2);
3. Carrying on the same activities- Article 5 (2)
4. Under the same conditions-Article 25 (3);
5. Similar enterprises-Article 25 (4).

[102] Article 25 deals with the elimination of tax discrimination that are based on certain grounds or in certain precise circumstances. Article 25 does not seek to ensure most-favoured nation treatment to non-nationals or non-residents, or it does not provide foreign nationals or non-residents with a tax treatment that is better than that of nationals or resident persons in enterprises (OECD, Application and Interpretation of Article 24 (non-discrimination) public discussion draft 3 may 2007, p.5).

[103] This principle in Article 25 requires that similar situations, namely, similar circumstances, carrying on same activities and same conditions

shall not be treated differently or obliges the State to accord the same treatment to a non-resident as that is accorded to its nationals placed in such similar situations (similar circumstances, carrying on similar activities under similar conditions). Reference to Article 24 of the OECD and the UN Model Convention, and their Commentaries were made by the learned Senior State Counsel during the oral hearing, which also contain identical terms as Article 25 of the DTAA between India and Sri Lanka.

[104] It is necessary to consider as to what are the relevant factors in determining whether a taxpayer is carrying on the same activities in the same circumstances in similar conditions for purposes of Article 25 (1). It is apt to consider the meanings of the expressions "similar circumstances", "similar activities" and "similar conditions" in Article 25 of the DTAA in the context of the Commentaries on the OECD Model/UN Convention and in judicial authorities.

The interpretation of the expression "in the same circumstances"

[105] The expression "in the same circumstances" refers to taxpayers (individuals, legal persons, partnerships and associations) placed, from the point of view of the application of the ordinary taxation laws and regulations, in substantially similar circumstances both in law and in fact. (OECD commentaries on the articles of the Model Tax Convention, p. 333). The expression "in the same circumstances" can in some cases refer to a person's tax situation. This would be the case, for example, where a country would subject its nationals, or some of them, to a more comprehensive tax liability than non-nationals (supra).

[106] Article 25 (1) establishes that for taxation purposes, discrimination on the basis of nationality is forbidden, i.e., nationals of one country cannot be subjected to additional taxation compared to the nationals of the source country subject, however, to both the nationals being in the same circumstances in the source country. To illustrate this further, 'A', an Indian national earning an income in Sri Lanka should not be treated differently in Sri Lanka vis-à-vis Sri Lankan nationals, while other circumstances remaining the same. Accordingly, the Sri Lankan tax law shall not be more burdensome on an Indian resident and shall not place a disadvantageous position than a similarly circumstanced Sri Lanka resident person.

The interpretation of the expression "carrying on the same activities"

[107] The expression "carrying on the same activities" is referable to the nature of the activities that happen to be the same and the income arising to a permanent establishment from such activities-meaning the same type of business (Taxmann's Indian Double Taxation Agreements & Tax Laws, para. 3010-3). It also refers to taxation levied on a resident person for carrying on activities shall not be favourably levied under the domestic law than the same activities carried on by a non-resident person in that State.

[108] The requirement of same activities means that the resident company has a market maker and the comparison between the same activities of a permanent establishment and a resident company that carries on market maker business (*UBS AG v. Revenue and Customs Commissioners* [(2006) BTC 232]. The principle in Article 25 (3) applies to the taxation of the permanent establishment's own activities and thus, it is restricted to a comparison between the rules governing the taxation of the permanent establishment's own activities and those applicable to similar business activities carried on by an independent resident enterprise.

The interpretation of the expression "under the same conditions'

[109] The expression "under the same conditions" refers to the allowance or disallowance of expenses or exemption or deductibility from income tax under the domestic law made to residents or non-residents had to be the same. In the Indian High Court of Delhi case of *Commissioner of Income Tax v. Herbalife International India Pvt. Ltd.* Decided On: 13.05.2016, it was stated that:

> *"The expression under the same conditions in DTAA clarifies the nature of the* ***receipt and conditions of its deductibility****. It was relatable, not merely to the compliance requirement of deduction of the tax at source. The lack of parity in the allowing of the payment as a deduction is what brings about the discrimination".*

Comparison Test for the application of the non-discrimination provision

[110] For the application of the non-discrimination provision to a permanent establishment, the test is that the comparison must be made between a hypothetical resident person in Sri Lanka and a permanent establishment (non-resident person-Indian Company-Appellant). Under this test, both the resident and the non-resident must be engaged in the same business activities and operate in the same circumstances (by the

application of the ordinary tax laws, regulations, both in law and fact) under the same conditions (imposition-receipt) and exemptions/deductions from income tax under the domestic law of the source State.

[111] This principle requires that the permanent establishments' business activities shall be compared with the similar business activities (same type of business) of the hypothetical resident person, and if both are involved in similar business activities, the non-resident shall not be treated differently or both resident and non-resident shall be treated in the same way. Secondly, by the application of the ordinary tax laws and regulations, both law and fact, the comparison must be made between the permanent establishment and the hypothetical resident company to ascertain whether they are in the same circumstances. If the domestic tax law/regulations subject a permanent establishment to additional taxation compared to a hypothetical resident placed under the same circumstances in the source country, the non-discrimination provision in Article 25 may be attracted.

[112] Thirdly, the test also requires a comparison to be made between a permanent establishment and a hypothetical resident company with regard to the imposition and exemptions of the tax liability to ascertain whether the two can be placed under the same conditions. If both are placed under the same conditions, a permanent establishment, shall not be treated differently as both hypothetical resident and permanent establishment (non-residents) shall be treated in the same way.

Comparison between the permanent establishment and the hypothetical resident company

[113] The comparison between the permanent establishment and the hypothetical resident company for the purpose of affording relief from the non-discrimination clause of the DTAA, shall be thus, made subject to the imposition and limitations laid down in the domestic law of the source country subject further, to the extent of inconsistency with Treaty terms. This also means that where the provisions of the domestic tax law are inconsistent with the provisions of the DTAA, the provisions of the DTAA will prevail.

[114] All what is required is that the provisions of the domestic tax law, shall be interpreted subject to the provisions of the DTAA, otherwise, the domestic tax law would be rendered meaningless and redundant. This is based on the principle that a DTAA exists to avoid double taxation, not to impose taxes as it is not an exercise in tax avoidance but avoidance of

double taxation. The DTTA rules merely alter the legal consequences derived from the tax laws of the Contracting States, either by excluding the application of the provisions of the domestic tax law where DTAA rules apply or by obliging one or both of the Contracting States to allow a credit against their domestic tax for taxes paid in other States.

[115] As noted, the Appellant being a non-resident company has registered its branch in Sri Lanka and has created a permanent establishment in Sri Lanka in terms of Article 5 of the DTAA and thus, such permanent establishment subject to the non-discrimination clause is liable to income tax in Sri Lanka similar to a resident company subject to permitted exemptions laid down in the domestic law read with the DTAA. One important qualification, however is that the differentiation in treatment has to be unreasonable, arbitrary or irrelevant to the object sought to be achieved by the DTAA. In the Indian Case of *Automated Securities v. ACIT* 118 TTJ 618 (ITAT Pune), this principle was recognized as follows:

> *"(i) In order to attract the non-discrimination clause in Article 26, mere differential treatment is not enough. The assessee has to show that not only has it been subjected to differential treatment vis-à-vis others, but also that the ground for this differentiation in treatment is unreasonable, arbitrary or irrelevant and that the basis of differentiation lacks any coherent relationship with the object sought to be achieved by that provision".*

[116] Thus, the mere differentiation between a resident company and non-resident company is insufficient for the invocation of the non-discrimination clause under Article 25 of the DTAA unless it can be shown that the differentiation in treatment of a permanent establishment of a non-resident enterprise comparatively placed in the same circumstances is unreasonable, arbitrary or irrelevant with the object sought to be achieved by Article 25 of the DTAA.

Requirements for the application of the Exemption read with the DTAA

[117] To enjoy the tax exemption on the offshore business claimed by the Appellant under Section 13 (b)(ii) read with the DTAA, the Appellant must present documentary evidence to the Assessor or the Commissioner-General and satisfy that the non-resident Appellant, comparatively placed in same circumstances with a hypothetical resident company in Sri Lanka involved in offshore business. In order to apply the non-discrimination

clause, the Appellant when comparatively placed in similar circumstances with a hypothetical resident company, must satisfy the following three conditions as laid down in Section 13 (b)(ii) of the Inland Revenue Act:

1. The Appellant is involved in any offshore business;
2. The Appellant is not involved in manufacturing or producing goods in Sri Lanka or importing goods into Sri Lanka;
3. The profits and income of such offshore business earned in foreign currency should be remitted to Sri Lanka through a bank (less expenses expended outside Sri Lanka, which are considered by the Commissioner General to be reasonable expenses).

Nature of offshore business

[118] The Tax Appeals Commission has, however, decided first, that the Appellant is involved in local sales of goods in Sri Lanka and therefore, the Appellant is not involved in offshore business as specified in Section 13 (b)(ii) of the Inland Revenue Act. Second, the Tax Appeals Commission appears to have treated an offshore company as a non-resident company for tax purposes, and such an offshore company is not liable to tax liability in Sri Lanka, if no sales are done in Sri Lanka. The findings are as follows:

> *"Besides, it would appear that the Appellant company is not involved in offshore business as specified in Section 13 (b)(ii) of the Inland Revenue Act. In the case of an offshore company which is treated for tax purposes as a non-resident company, the business of which consists solely of the purchase and sale of goods, there would be no tax liability to income tax in Sri Lanka, if no sales are affected in Sri Lanka. However, in the case of the Appellant Company, it is clear that the sale of some of the items takes place in Sri Lanka. Therefore, it is clear that the Appellant Company has not fulfilled the offshore business condition specified in the Section".*

[119] It is necessary, however, to consider these two different factual findings and the statement of law made by the Tax Appeals Commission separately. Dr. Felix argued at the hearing that the Appellant is an overseas company and not an offshore company and therefore, the Tax Appeals Commission has confused the notion of an offshore company with an overseas company which can also do offshore business. He further argued that the exemption under Section 13 (b)(ii) is not confined to an offshore

company but is available to an overseas company such as the Appellant doing any offshore business.

Offshore Company & Overseas Company

[120] In view of this argument, it is necessary first to understand the distinction between an offshore company and an overseas company. The term “offshore” refers to any activity that takes place outside an entity's home base (off the coast) or any location outside of one's home country and therefore, the term “offshore business” ” refers to any business that takes place in another country-off the coast (Investopedia, Offshore Definition, https://www.investopedia.com).

Offshore Company

[121] An offshore company is not defined in the Companies Act No. 7 of 2007. In terms of Section 261 of the Companies Act, any company incorporated outside Sri Lanka may make an application for the registration of an offshore company in accordance with Part XI under the provisions of the Companies Act, No. 07 of 2007. An offshore company shall have the power to carry on any business outside Sri Lanka, but shall not be entitled to carry on any trading business within Sri Lanka (s. 264). Thus, no tax consequence may arise depending on the place where the offshore activity takes place and the nature of the offshore activity. In the present case, however, the question of whether the Appellant is an offshore company or its tax liability does not arise for consideration.

Overseas company

[122] On the other hand, an overseas company is defined in Section 488 of the Companies Act No. 7 of 2007, to mean any company or body corporate incorporated outside Sri Lanka which- (a) after the appointed date (viz: 3rd May 2007) establishes a place of business within Sri Lanka; or (b) had, before the said appointed date, established a place of business within Sri Lanka and continues to have an established place of business within Sri Lanka on the appointed date. “Registered Overseas Company” is defined to mean an overseas company which has delivered or is deemed to have delivered to the Registrar the documents and particulars required under Section 489. Any overseas company in the form of the branch office or project office is generally treated as a non-resident company.

[123] The Companies Act, No. 7 of 2007 obliges every overseas company to apply for registration in Sri Lanka within one month from the date of establishment of the place of business in terms of the provisions of the Companies Act with relevant documents and particulars to be delivered to Registrar by such company as set out in S. 489 (1) of the Companies Act. The Appellant has, however, not produced any registration as an overseas company under Section 489 (1) of the Companies Act or its renewal of the registration under the Companies Act, No. 7 of 2007. The Respondent referring to the Registration Certificate of the Appellant however, states that the Appellant has registered its **branch office** under and in terms of Section 3 (2) of the Companies (Special Provisions) Law, No. 19 of 1974 (page 74 of the TAC brief). It is crystal clear that the Appellant company being a company incorporated outside Sri Lanka has registered **its branch** in Sri Lanka under Section 3 (2) of the Companies (Special Provisions) Act, No. 19 of 1974 (now repealed by Section 533 (2) of the Companies Act, No. 07 of 2007) together with the documents specified in Section 395 (1) of the Companies Act, No. 17 of 1982.

[124] It is to be noted, however, that in terms of Section 489 (7) of the Companies Act, No. 07 of 2007, a company incorporated outside Sri Lanka shall not establish a place of business within Sri Lanka or be registered as an overseas company where the business being carried on by that company does not conform to the stipulations made by the or under the Exchange Control Act.

[125] "Branch Office" is defined in the Companies Act No. 7 of 2007 to mean any establishment described as a branch of a foreign company or establishment carrying on the same business or substantially the same business as that carried on by the parent or Head Office. It is significant to remember that a company registered under the Companies Act as an overseas company is very different from an offshore company. An offshore company is not an overseas company, but it is a company incorporated outside Sri Lanka and registered in Sri Lanka under Part XI of the Companies Act, No. 07 of 2007. For those reasons, I hold that a company with offshore activities is very different from an offshore company but the crucial question that arises in the present case is whether or not the Appellant being a non-resident company is involved in offshore business to qualify for the tax exemption under Section 13 (b)(ii) of the Inland Revenue Act. No. 10 of 2006 read with DTAA between India and Sri Lanka.

Offshore business

[126] The Inland Revenue Act, No. 10 of 2006 does not define what is meant by an offshore business or offshore sale. Section 53 (7)(iii) (III b) of the Inland Revenue (Amendment) Act, No. 10 of 2021, which amends the Third Schedule to the Inland Revenue Act, No. 24 of 2017, by including the following new item (oo), in the list of exemptions as follows:

> *(iiib) offshore business where goods can be procured from one country or manufactured in one country and shipped to another country without bringing the same into Sri Lanka"*

[127] In order to qualify as offshore business, the business activity taking place must be based entirely in a country other than the person's or company's home base and offshore business must involve goods procured from one country or manufactured in one country and shipped to another country without bringing the same into Sri Lanka. Accordingly, a company incorporated in Sri Lanka (a resident company) with offshore business activities may be eligible for offshore business tax exemption subject to the fulfilment of other conditions specified in Section 13 (b)(ii) irrespective of whether it is registered as an offshore company under the Companies Act, No. 07 of 2007.

Application of the domestic tax laws subject to DTAA

[128] The Appellant, however, claims that it is entitled to the same tax exemption on the basis that as it is carried on offshore business activities through a permanent establishment in Sri Lanka within the meaning of Article 5 of the DTAA and in terms of the non-discrimination clause under Article 25 of the DTAA between India and Sri Lanka. It is not in dispute that the benefit under double taxation avoidance treaty can be claimed only by any person or company resident in any of the Contracting States. Under the domestic tax law of Sri Lanka, the test is whether the non-resident company is carrying on business in Sri Lanka through a branch or agency, and if so, the Sri Lankan tax will apply. Where a double taxation treaty applies, the test is replaced by the "permanent establishment' criterion-i.e., does the foreign trader has sufficient presence in Sri Lanka to constitute a permanent establishment. The test then is whether the branch is a permanent establishment of the non-resident company (*Firestone Tyre Rubber Co. v. Lewellin* [(1957) 1 All E.R. 561].

[129] In this regard, it is significant to remember that the DTAA does not in any way confine the powers of the Assessor under the Inland Revenue Act, with regard to any assessment of assessee covered by the permission of Indo-Sri Lanka DTAA. A DTAA does not create a separate taxation. Accordingly, a DTAA cannot be used to impose any new tax on a person or company when the domestic law imposes no tax. In short, any DTAA acts only as a shield against double taxation, and not as a sword to impose tax, which is not imposed under such domestic law (Maralynne A. Monteith, INBOUND INVESTMENT – CROSS BORDER ISSUES, National Tax Law CLE Program, 2011,p.2,http//www.cba.org/cha/cle/PDF/TAX11_Monteith_Paper.pdf).

[130] The object of the agreement is "for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital. The resulting position is that the Assessor or the Commissioner General in Sri Lanka on its own cannot lawfully impose or waive or exempt or reduce any tax imposed by Parliament except to the extent and in the manner permitted by the Inland Revenue Act itself.

[131] As the Commentary points out, the provision covering permanent establishment is based on situs and not on nationality, so that the benefit of the non-discrimination clause applies to all residents of a treaty country who, regardless of nationality, have a permanent establishment (e.g., branch) in the other country (Commentary on OECD Model, Article 24).

Proof of offshore business

[132] The Appellant's contention is that the Appellant, comparatively placed in the same circumstances, with a hypothetical resident company is engaged in the same activities and therefore, the Appellant being a permanent establishment, shall not be discriminated and treated less favourably than any other resident company. It was the contention of Dr. Felix that the commercial invoices produced by the Appellant as indicated in the Appeal Report establish that the goods were purchased and sold outside Sri Lanka and this matter is not disputed by the Respondent. He referred to the observations made by the Assistant Commissioner in the Appeal Report (pp.109-113).

[133] Now the question is whether the Appellant, comparatively being placed in similar circumstances with a hypothetical non-resident having a permanent establishment under the DTAA is entirely engaged in offshore business for the purpose of the exemption under Section 13 (b)(ii).

[134] Offshore business generally takes place, by securing offshore buyers, suppliers and manufacturers and shipping or airfreight agencies that transport goods to offshore buyers. Accordingly, documents relating to the involvement of offshore buyers, manufacturers, suppliers, shipping or air freight agencies are crucial to prove that goods were procured from one country or manufactured in one country and shipped to another country without bringing into Sri Lanka.

[135] A perusal of the observations made by the Assistant Commissioner, pp. 109-113 of the TAC brief reveals that at a discussion with him, the Appellant's representative has produced **some copies of commercial invoices** and copy of the business registration. Those documents include; purchase order, delivery advice, goods delivered to the buyer, payments received and payment of the cost of goods. The Appellant has further produced a diagram to explain the offshore business of the Appellant and the Assistant Commissioner after having examined the said diagram and the documents (p.111) has stated:

> *"As per the above diagram only the **goods are transferred (purchased and sold) outside of Sri Lanka** by Johnson & Johnson Ltd (Sri Lanka Branch) and **all other activities in relation to this business transaction have been done in Sri Lanka**...."*

[136] The Appellant solely relies on some commercial documents produced before the Assistant Commissioner to establish that it is involved in purchasing and selling goods outside Sri Lanka. The documents referred to in the Appeal Report only indicate that the goods are purchased and sold outside Sri Lanka. However, the entirety of the commercial documents that should correspond with the profits or income referred to in the statement of accounts have not been produced by the Appellant. While documents relating to purchases and sales outside Sri Lanka are relevant to support the offshore business, offshore business status cannot be conclusively determined by reason of the mere purchases and sales of goods outside Sri Lanka by the Appellant.

[137] The proper approach is to identify the locality of the entire business presence or operations overseas, which produced the relevant profits, identify the overseas business partners such as manufactures, suppliers, buyers the locality of the negotiations, contracts and execution of the terms of the contracts outside Sri Lanka.

[138] In my view, to enjoy the tax exemption on the offshore business under Section 13 (b)(ii) read with the DTAA, the Appellant must submit credible documents to the Assessor or the Commissioner-General. The question whether or not the business is transacted outside Sri Lanka would depend on the actual activities carried out by the company. Examples of activities that would qualify for offshore business tax exemption include:

1. The Company has no customers or suppliers for its business in Sri Lanka;
2. The employees or agents or representatives of the Company operate their business solely outside of Sri Lanka;
3. Customers, manufacturers, suppliers, shipping agencies are located outside Sri Lanka;
4. Email or other electronic correspondence with offshore customers, manufactures, suppliers and transport and shipping agencies;
5. Contracts signed with the manufactures or suppliers or shipping companies outside Sri Lanka;
6. Company products and goods are not manufactured or supplied or produced in Sri Lanka or not imported into Sri Lanka either for sale or any profit-making business;
7. Shipping documents show that goods ordered by customers were shipped from one country to another country without bringing the same into Sri Lanka;
8. Having no warehouses in Sri Lanka to store goods purchased outside Sri Lanka;
9. Invoices, purchase orders, delivery orders, payment receipts, bank facilities relate to offshore business activities and all purchases, suppliers, customers, investment takes place outside Sri Lanka;
10. Payments made by manufacturers, suppliers and shipping agencies outside Sri Lanka;
11. Travel documents of the company representatives for any foreign visits to manufactures, producers and suppliers outside Sri Lanka;
12. Profits and income earned in foreign currency from offshore business and income/profits and income remitted into Sri Lanka through a bank (excluding reasonable expenses expended).

[139] One of the factors that determines where a business is carried on outside a country is to ascertain the place where the contracts of purchase and sale with customers, suppliers, manufacturers or producers, shippers were made (see- *Grainger and Son v. Gough* [(1896). A.C. 325] where all

orders for French wine and champagne from U.K. customers were transmitted to France by the U.K. agents and were accepted by the French wine firm. It was held that because the contracts for the sale of wine and champagne were concluded in France, the French firm was only trading with and not within the U.K. The mere production of some documents which indicate that purchases and sales take place outside Sri Lanka will not be conclusive evidence that the business is transacted out of Sri Lanka unless the contracts or negotiations with the offshore suppliers, manufactures, producers or shippers take place outside Sri Lanka. In the present case, copies of contracts or negotiations with customers, manufactures, suppliers and shippers have not been provided by the Appellant to support the offshore activities.

[140] Another factor is that although the place where the contracts are made is significant, the test is where do the operations take place from which the profits in question arise (*Greenwood v. F.L. Smith and Co.,* 8 T.C. 193, p. 204). For example, in *Firestone Tyre and Rubber Co. v. Lewellin* [(1957) 1 All E.R. 561] where the US parent company (Akron) had a wholly-owned subsidiary company in the U.K. (Brentford) and Akron entered into agreements with its foreign distributors for the supply of Tires, which were manufactured and delivered direct from the U.K. by Brentford. It was held that although the main contract was located outside the U.K. Akron was trading in the U.K. through Brenford as its agent. The case highlights that the crucial factor was not the contract itself, but the dealings between Brentford and the foreign distributor and therefore, Akron's profits in the supply of Tyres by Brentford was subject to U.K. tax.

[141] I think that the crucial question thus is: where do the operations take place outside the country from which the profits in question arise? In order to answer that question, the Appellant must present credible documentary evidence to support its offshore operations by first filing the company's tax returns and then, by presenting all relevant documents during the assessment process.

[142] The guiding principle is that the Assessor or the Commissioner General must be satisfied where the Appellant has done business operations to earn the profits, how it has done its business operations which produced the profits and where its business partners and customers were located in the course of doing offshore business. In the present case, all 6 copies of commercial documents (pp. 11-18) indicate that although the goods were purchased and sold outside Sri Lanka, all the payments had

been made by the buyers directly to the HSBC Bank at, No. 24, Sir Baron Jayathilaka Mawatha, Colombo 01, Sri Lanka, which indicates that payments are not directly sent by the buyers to the Appellant's offshore agents or offshore banks, but direct to the HSBC Bank, in Sri Lanka. This is also suggestive of the fact that payments are not directly sent by the buyers to the Appellant's offshore agents or offshore banks, but direct to the Appellant's bank located in Sri Lanka.

[143] On the other hand, the entire turnover had been remitted to Sri Lanka by the buyers (p. 110 of the brief) and NOT by any employee, agent or representative of the Appellant located outside Sri Lanka. This is also suggestive of the fact that payments are not directly sent by the buyers to the Appellant's offshore agents or offshore bank, but direct to the Appellant's bank located in Sri Lanka.

[144] Another factor that determines the offshore business of a trading company is that goods are not manufactured or produced in Sri Lanka or imported into Sri Lanka for trading purposes. The Tax Appeals Commission has taken the view that the Appellant is also involved in local sales as sales of some of the items take place in Sri Lanka and therefore, the Appellant is not involved in offshore business as specified in Section 13(b)(ii) of the IRA (pp 179 of the TAC brief).

[145] The Appellant states that it is involved in both local sales and offshore sales (statement of account at page 94 of the TAC brief) and that the local sale component has been taxed in Sri Lanka. It was the contention of Dr. Felix that the tax exemption claimed only related to the offshore business and there is no prohibition for one entity to have a local business and an offshore business. His contention was that the Tax Appeals Commission has erred when it made a reference to the local sales taking place in Sri Lanka as admittedly there are no undeclared sales. The Assistant Commissioner having perused the commercial documents has found that only the goods are transferred (purchase and sale) outside Sri Lanka by the Appellant and all other activities in relation to this business transactions have been carried out in Sri Lanka (p. 110 of the TAC brief).

[146] Admittedly, the principal activities of the Appellant also include export of medical equipment, import and wholesale business of cosmetics and baby care items. It is not in dispute that the goods purchased and sold to customers by the Appellant outside Sri Lanka also related to those activities of the Appellant (medical equipment-Vide pp. 11-18). Under such

circumstances, it must be shown by producing, shipping or air freight documents that the goods purchased and sold outside Sri Lanka did not go through Sri Lanka and that they were procured or manufactured or supplied and transported outside Sri Lanka.

[147] As the Appellant's principal business also includes import of identical goods, it must also be shown that the goods involved in offshore sales were not imported into Sri Lanka for local sales, and how they were procured for local sales. The Appellant has failed to produce any credible document to exclude the possibility that the goods involved in offshore sales were not imported into Sri Lanka as part of local sales.

[148] The Appellant relies on the entire turnover that has been remitted to Sri Lanka through a bank in foreign currency in support of its offshore business activities. The Assistant Commissioner and the Respondent (pp. 49,110) have refused to consider the remittance as an offshore business on the basis that the amount remitted is not either profit or income, but entire turnover, which was remitted by the buyer to Sri Lanka without deducting the expenses incurred by the Appellant. Unless the Appellant is able to support its claim with credible documentary evidence that the profits (after deducting the expenses) were derived entirely from offshore business, the mere fact that the turnover was remitted to Sri Lanka through a bank in Sri Lanka is insufficient to qualify for offshore business exemption under Section 13 (b)(ii) of the IRA, 2006.

[149] There appears to be a consistent judicial view that a provision providing for an exemption, concession or exception, as the case may be, has to be construed strictly. In the case of Commissioner of Central Excise, New Delhi v. Hari Chand Shri Gopal, (2011) 1 SCC 236, the Supreme Court of India reiterated the law on the aspect of the interpretation of the exemption clause enunciated in *Hansraj Gordhandas v.H.H. Dave, Asst. Collector of Central Exercise & Customs, Surat and Others,* AIR 1970 SC 755 in para 29 as follows;

> *"The law is well settled that a person who claims an exemption or concession has to establish that he is entitled to that exemption or concession. A provision providing for an exemption, concession or exception, as the case may be, has to be construed strictly with certain exceptions depending upon the settings on which the provision has been placed in the statute and the object and purpose to be achieved. If the exemption is available on complying with certain conditions, the conditions have to be complied with...."*

[150] Recently, the Supreme Court of India was called up to consider in Commissioner of Income Tax (*Import), v. M/S. Dilip Kumar and Company* decided on 30 July, 2018, the appropriate interpretative rule to be applied while interpreting a tax exemption provision including any ambiguity as to its applicability with reference to the entitlement of the assessee or the rate of tax to be applied. After thoroughly examining the various precedents, The Supreme Court of India held at paragraph 52 that:

1. the exemption should be interpreted strictly and the burden of proving a tax exemption would be on the assessee to show that his case comes within the parameters of the exemption and the assessee cannot claim the benefit of any such ambiguity in the provisions;

2. When there is ambiguity in the exemption notification, which is subject to strict interpretation, the benefit of such ambiguity cannot be claimed by the subject/Assessee and it must be interpreted in favour of the revenue.

[151] The facts and circumstances of the case reveal that any hypothetical resident company, comparatively placed in the same circumstances, same activities and same conditions, with the Appellant would also not be entitled to the same exemption under Section 13 (b)(ii) of the Inland Revenue Act. The activities carried out by the Appellant do not fall as offshore transactions simply due to the facts that goods are purchased from one country and sold to another country. The fact remains that these are not offshore transactions, but transactions carried out on in Sri Lanka on which only the goods are transferred from one country to another country.

[152] In the absence of those crucial documents, the Appellant, comparatively placed in similar circumstances with a hypothetical resident company cannot complain that it was discriminated unreasonably, arbitrarily and unjustly against when affording a tax exemption granted to a hypothetical resident company under Section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006, read with Article 25 of the DTAA between India and Sri Lanka.

[153] For those reasons, I am of the view that the exemption in section 13 (b)(ii) of the Inland Revenue Act, No. 10 of 2006 (as amended) read with Article 25 of the DTAA does not apply to the Appellant.

Question of Law No. 3

Tax concession under Section 51 of the Inland Revenue Act

[154] Dr. Felix further submitted that that the Appellant is also entitled to the income tax concession conferred by Section 51 of the Inland Revenue Act, No. 10 of 2006 (as amended), as the Appellant can be regarded as an exporter within the meaning of Section 51 of the Inland Revenue Act, No. 10 of 2006 (as amended). His contention was that an exporter does not have to export only goods produced in Sri Lanka; and an exporter could be based in Sri Lanka and could ensure that the export is affected from one country to another. Section 51 of the Inland Revenue Act (as amended) refers to the concessionary rate of income tax on qualified export profits and income of a company which commenced to carry on any specified undertaking. It provides as follows:

> *"Where any company commences on or after November 10, 1993, to carry on* ***any specified undertaking*** *and the taxable income of that company for any year of assessment* ***includes any qualified export profits and income****, such part of the taxable income of that company for that year of assessment as consists of such qualified exports profits and income shall, notwithstanding anything to the contrary in this Act, be chargeable with income tax as the appropriate rate specified as the Fifth Schedule to this Act".*

[155] Section 52 of the Inland Revenue Act (as amended) refers to the concessionary rate of income tax on qualified export profits and income of a company which carries on any specified undertaking. It provides as follows:

> *52-Where any company commenced prior to November 10, 1993, to carry on any specified undertaking and the taxable income of that company for any year of assessment* ***includes any qualified export profits and income from such specified undertaking,*** *such part of such taxable income as consists of such qualified export profits and income, shall, notwithstanding anything to the contrary in this Act, be chargeable with income tax at the appropriate rate specified in the Fifth Schedule to this Act".*

[156] Section 60 of the Inland Revenue Act, No. 10 of 2006 interprets the terms "qualified export profits and income" and "specified undertaking" for the purpose Chapter IX as follows:

> "60. *For the purposes of this Chapter—*

(b) "qualified export profits and income" in relation to any person, means the sum which bears to the profits and income within the meaning of paragraph (a) of section 3, after excluding there from any profits and income from the sale of gems and jewelry and any profits and income from the sale of capital assets, for that year of assessment from any specified undertaking carried on by such person, ascertained in accordance with the provisions of this Act, the same proportion as the export turnover of that undertaking for that year of assessment bears to the total turnover of that undertaking for that year of assessment;
(c) "specified undertaking" means any undertaking which is engaged in–

*(i) the export of non-traditional goods manufactured, produced or **purchased by such undertaking;** or*

(ii) the performance of any service of ship repair, ship breaking repair and refurbishment of marine cargo containers, provision of computer software, computer programmes, computer systems or recording computer data, or such other services as may be specified by the Minister by Notice published in the Gazette, for payment in foreign currency;

[157] The question that arises for consideration is whether or not, the profits and income of the Appellant being a specified undertaking were derived from the export of goods to be treated as a "qualified export profits and income" within the meaning of Section 51 of the Inland Revenue Act, No. 10 of 2006 (as amended). It is not the Appellant's case that it is involved in exporting goods to any foreign destination from Sri Lanka. On the contrary, the Appellant's case is that it is involved in offshore business that does not involve goods manufactured or produced in Sri Lanka or any goods imported into Sri Lanka.

[158] Accordingly, the Appellant is not engaged in a specified undertaking within the meaning of Section 51 read with Section 60 (b) and (60 (c) of the Inland Revenue Act, No. 10 of 2006 (as amended). For those reasons, I am of the view that the Appellant is not entitled to be taxed at the concessionary rate of income contemplated by Section 51 of the Inland Revenue Act, No. 10 of 2006 (as amended).

Question of Law No. 4

[159] For the reasons, enumerated in this judgment, the Tax Appeals Commission was justified in confirming the determination made by the Respondent and dismissing the appeal of the Appellant.

Conclusion & Opinion of Court

[160] In these circumstances, I answer the questions of law in favour of the Respondent and against the Appellant as follows:

1. No
2. No
3. No
4. No

[161] For those reasons enumerated in this judgment and subject to our observations in paragraph 125 of this judgment, I confirm the determination made by the Tax Appeals Commission dated 07.11.2017 and the Registrar is directed to send a certified copy of this judgment to the Tax Appeals Commission.

JUDGE OF THE COURT OF APPEAL

<u>M. Sampath K.B. Wijeratne, J.</u>

I agree.

JUDGE OF THE COURT OF APPEAL