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

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

Confab Steel (Private) Limited,
No. 5-9, East Tower,
5th Floor, World Trade Centre,
Echelon Square,
Colombo 01.

APPELLANT

CA No. CA/TAX/02/2012
Tax Appeals Commission
No. TAC/IT/009/2011

v.

Commissioner General of Inland Revenue,
Department of Inland Revenue,
Sir Chittampalam A, Gardiner Mawatha,
Colombo 2.

RESPONDENT

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

COUNSEL : Faiz Musthapha, P.C., with Riad Ameen and Rushitha Rodrigo for the Appellant.

Suranga Wimalasena, DSG., for the Respondent.

WRITTEN SUBMISSIONS : 09.10.2018 (by the Appellant)
08.08.2022 & 10.09.2018 (by the Respondent)

ARGUED ON : 07.06.2022

DECIDED ON : 08.09.2022

M. Sampath K. B. Wijeratne J.

Introduction

The Appellant Confab Steel (Private) Limited is a limited liability company incorporated in Sri Lanka engaged in the business of manufacture and marketing of rolled steel products. The Appellant entered into agreement No. 28 dated 18th March 2004 with the Board of Investment (hereinafter referred to as the 'BOI') in terms of Section 17 of the Board of Investment of Sri Lanka Act[1] (hereinafter referred to as the 'BOI Act').

The Appellant submitted its return of income for the year of assessment 2007/2008 claiming that '*interest income*' earned by the Appellant forms part and parcel of its business profits, and therefore qualified for the income tax exemption granted to the enterprise under the terms of the agreement entered into with the BOI. The Assessor by letter dated 22nd September 2009, issued under Section 163 (3) of the Inland Revenue Act No. 10 of 2006 (hereinafter referred to as the 'IR Act') rejected the Appellant's return of income for the year of assessment 2007/2008, on the ground, *inter alia,* that the interest income was subject to income tax. According to the Appellant, the Appellant received the Notice of Assessment dated 30th September 2009 subsequently. Thereafter, the Appellant appealed to the Commissioner General of Inland Revenue (hereinafter referred to as the 'CGIR') against the said assessment by letter dated 09th October 2009. The

[1] As amended by Greater Colombo Economic Commission (Amendment) Act No. 43 of 1980, 21 of 1983, 49 of 1992 and Board of Investment of Sri Lanka (Amendment) Act No. 9 of 2002, 36 of 2009 and 3 of 2012.
The words 'Greater Colombo Economic Commission' in the Long Title to the Greater Colombo Economic Commission Law No. 4 of 1978 was amended by Greater Colombo Economic Commission (Amendment) Act No. 49 of 1992 to read as 'Board of Investment of Sri Lanka'.

CGIR heard the appeal and confirmed the assessment made by the Assessor by his determination dated 5th October 2011.

The Appellant appealed to the Tax Appeals Commission (hereinafter referred to as the 'TAC') against the determination of the CGIR. The TAC confirmed the determination made by the CGIR and dismissed the appeal by determination dated 23rd August 2012. The Appellant aggrieved by the TAC's determination moved to state a case to the Court of Appeal. Accordingly, the TAC stated a case to this Court on four questions of law.

The four questions of law in the case stated to the Court of Appeal are as follows;

1. **Is the interest of Rs. 28,951,842/= received by the Appellant during the year of Assessment 2007/2008 immune from liability to pay income tax chargeable under the provisions of the Inland Revenue Act No. 10 of 2006, due to the operation of clause 10(1) of the Agreement dated 18th march 2004 between the Appellant and the Board of Investment of Sri Lanka?**

2. **Did the Tax Appeal Commission err in law in arriving at a conclusion of fact without legal evidence, the conclusion of fact being that the deposits the appellant held with banks were investments made with the intention of receiving interest?**

3. **Did the Commissioner err in law in not annulling the assessment under appeal on the basis of its own correct formulation of the applicable law which it stated as follows; clause (10) (1) of the BOI Agreement has granted tax exemption for a period of three years in relation to the business of the enterprise namely manufacturing and marketing of rolled steel products, so that the provisions of the Inland Revenue Act relating to the imposition payment and recovery of income tax should not apply to the profits and income of the Enterprise? (Emphasis added – please see page 7 of the determination)**

4. **Did the Commissioner err in law in dismissing the appeal of the appellant (in disregard of the law as correctly formulated by the Commission itself) on the basis of the conclusion that any tax exemption granted under a BOI Agreement would necessarily**

have to be confined to certain specific types of income and profits earned by an Enterprise as identified in the Agreement, which conclusion is based on the policy consideration (which is a matter properly considered by the legislature) that the grant of 'blanket' tax exemption to an Enterprise encompassing all its earnings cannot be considered as a step taken to "foster and generate economic development of the Republic" ? (Emphasis added- please see page 7 of the Determination.

Relevant facts

The Appellant's contention is that in terms of clause 10 (i) of the agreement with the BOI, the profits and income of the Appellant company are exempt from tax for a period of three years. The BOI determined the three-year period to reckon from the year of assessment 2005/2006.

The aforesaid clause has been included in the agreement pursuant to the Regulations made under Section 17 of the BOI Act and published in the Extra Ordinary Gazette No. 8/2 dated October 31, 1978.

The year of assessment relevant to the case at hand is 2007/2008, which falls within the three-year tax holiday. The Appellant submitted its return of income for the above year of assessment and the Assessor rejected the return in his aforementioned letter dated 22nd September 2009. The Assessor proceeded to issue an assessment on the basis that the Appellant's interest income from fixed deposits, call deposits and savings accounts is a separate source of income subject to income tax.

The Appellant submitted that these amounts were received on short term deposits made by the Appellant with commercial banks in the course of its business and therefore, the interest is an integral part of its business profits. The Appellant argued that this interest should not be subject to taxation under the provisions of the above-mentioned BOI agreement. According to the Appellant, written agreements with each bank set out the terms and conditions under which the credit facilities are provided by the banks. The Appellant submitted that the foreign suppliers from whom the goods are imported provide the Appellant with a 180-day credit period, subject to *libo* interest. The Appellant imports the goods by means of such credit facilities and the goods are dispatched in the name of the bank, in accordance with the agreement between the bank and the Appellant. When the goods arrive, they are stored in the Appellant's premises, but under the control and supervision of the bank's security personnel. The goods will be

released to the Appellant for production only on payment of the value of the goods released and the payment is held in a special account in the name of the Appellant. The money held in the aforementioned account is used by the bank to make payment to foreign suppliers at the end of the credit period. Until then, the bank pays interest to the Appellant for the monies in the special account. The Appellant submits that the interest at issue is generated by the special account referred to above.

The Appellant has received Rs. 28,951,842/= as interest income in the year of assessment 2007/2008. The Appellant's position is that the above interest income is part of its business profits under Section 3 (a) of the IR Act. The Respondent contended that the interest income of the Appellant is a separate source of income which falls under Section 3 (e) of the IR Act.

Analysis

The Section 3 of the IR Act reads as follows;

> '***3.*** *for the purpose of this Act, "profits and income" or "profits" or "income" means-*
>
> *(a) the profits from any trade, business, profession or vocation for however short a period carried on or exercised;*
> *(b) (...)*
> *(c) (...)*
> *(d) (...)*
> *(e) dividends, interest or discount;*
> *(f) (...)'*

Section 217 of the IR Act defines the term '*profits*' or '*income*' to mean "*the net profits or income from any source for any period calculated in accordance with the provisions of the act*".

The Appellant claims that the interest income is earned from its business.

The term '*business*' is defined in Section 217 as follows;

"*includes an agricultural undertaking, the racing of horses, the letting or leasing of any premises, including any land by a company and the forestry*".

It appears that the Appellant's business does not fall under any of these categories in the IR Act.

Be that as it may, in the case of *Grainger and son v. Gough*,[2] Lord Morris observed that the phrases 'exercising a trade' and 'carrying on a business' are synonyms:

> *"There can be no definition of* ***the words 'exercising a trade'. It is only another mode of expressing 'carrying on a business****'…."*.

Thus, it is clear that the terms *'business'* and *'trade'* are synonyms.

The term '*trade'* is defined in Section 217 as follows;

"*includes every trade and manufacture and every adventure and concern in the nature of trade*".

Consequently, a trade under the IR Act need not be a trade alone. Any act in the nature of a trade as well as manufacturing is covered by the definition. This gives the terms '*business'* and '*trade'* a broad scope under the IR Act; one under which the Appellant's interest income could fell quite easily, provided that the interest is derived from its business.

As such, the important question is whether the Appellant's interest income is a profit from its business.

The Appellant heavily relied on the five-bench decision of the Supreme Court in the case of *Ceylon Financial Investments Limited v. Commissioner of Income Tax*[3] (hereinafter referred to as the 'CFI judgment') in support of the Appellant's contention. In the above case four judges have delivered separate judgments agreeing as well as differing on some of the points. De Kretser J., has agreed with Soertsz J., without writing a separate judgment. Howard C.J., and Keuneman J., in both their Lordship's judgments set out a test for determining whether interest was a source under Section 6 (1) (a) or 6 (1) (e) of the then Income Tax Ordinance[4] (which correspond to Section 3 (a) and 3 (e) of the Inland Revenue Act No. 10 of 2006).

The relevant passage of the judgment of Howard C.J., is as follows;

[2] 3 TC 462 at page 472

[3] 1 CTC 206/34 N.L.R. 1.

[4] No. 2 of 1932 as amended

'if the business of a company consists in the receipt of dividends, interest or discounts alone or if such a business can be clearly separated from the rest of the trade or business, then any special provisions applicable to dividends, interest or discounts must be applied. *Applying the principle laid down in the Egyptian case,* ***the appellant company is within source (e) and cannot get out of it.*** *To take such a view does not in any way disturb the scheme of the Ordinance. I agree, therefore, with Keuneman J. that the Commissioner was empowered to charge the appellant Company under section 6 (1) (e) in respect of the dividends and interest received from undertakings in which its capital was invested.'*

The relevant passage from Keuneman J.'s judgment reads thus;

'How then are we to treat income which comes under source (e) but can also be regarded as coming under source (a)? In my opinion it was the intention of the Ordinance to regard dividends, interest or discounts as a separate source. ***If then the business of an individual or a company consists in the receipt of dividends, interest or discounts alone, or if the business of receiving dividends, interest or discounts can be clearly separated from the rest of the trade or business, then any special provisions applicable to dividends, interest or discounts must be applied.*** *I do not think any question of opinion arises.* (Emphasis Added)

Regarding the difficulty in dividing the income into sources under Section 6 (1), His Lordship observed that;

> *'it is no doubt true that the divisions into "sources" under Section 6 (1) does not appear to be scientific and it is difficult to see on what grounds the division is made. But we must take the Ordinance as we find it'.*

From the above quotations of the CFI judgment, it is seen that both Howard C.J. and Keuneman J., have set out the same criteria i.e. (i) when the business consists solely of the receipt of interest or (ii) where the business of receiving interest can be clearly separated from the rest of the trade or business, such interest income falls under Section 6 (1) (e).

Although the assessee in the CFI case received only interest and dividends, in contrast, the Appellant's main source of income is manufacturing and marketing of rolled steel products. Therefore, the first criterion set out in the CFI judgment would not apply to the case in hand and that if a criterion applies, that is the second criterion.

Section 3 (a) applies to profits earned *from* any trade, business, profession or vocation. As I have already stated above in this judgment, the Appellant's contention is that in terms of the agreements entered into with the banks, material imported by the Appellant for its business is consigned to the banks. Once the goods are received those are kept in the premises of the Appellant but under the control and supervision of the banks. Once the Appellant needs the material for manufacturing, the Appellant make payment to the relevant bank an amount equivalent to the value of the goods to be released. According to the Appellant, the Appellant has at times borrowed money from the bank for this purpose.

The Appellant's main business and/or other businesses is never a ***business*** of receiving dividends interest or discounts and that the Appellant's interest income cannot be separated from its rest of the ***business***. According to the Appellant's own analysis of Howard C.J.'s and Keuneman J.'s., judgments in the CFI case, where the ***business*** of receiving interest can be clearly separated from the rest of the trade or business, such interest income falls under Section 3 (e). Accordingly, it should be a ***business*** that receive dividends, interest or discounts that need to be clearly segregated and identified from the rest of the business. It is true that the account entries of the aggregate interest received are separately shown in the account statements of the Appellant. Yet, there isn't evidence whatsoever to establish that the Appellant is in the ***business*** of receiving dividends interest or discounts.

The Appellant alleged that the TAC failed to consider the relevant legal evidence in determining the purposes for which the Appellant maintained the deposit accounts for which interest was accrued. The Appellant argued that there is no legal evidence to support the TAC's inference that the Appellant made the deposits using surplus funds as an investment. I acknowledge that there was insufficient evidence for the TAC to reach this conclusion. The Appellant submitted that if the TAC had any doubt in its mind, it could and ought to have called evidence of the bank officials to ascertain how the bank accounts were operated in the context of the business. The Assessor or even the CGIR did not ask for such proof either. If the Assessor or the CGIR were not satisfied with the Appellant's claim, they could have verified the process by requesting additional evidence or even conducting an inspection.[5] Nevertheless, the CGIR has observed in

[5] Section 214 and 215 of the IR Act.

his determination that the Appellant did not adduce any evidence to the effect that investment is part of their principal activity, manufacturers and dealers of all types of steel rolled products. Yet, the Appellant has failed to submit those material evidence at least to the TAC. The Appellant submitted that the proper cause of action for this Court is to remit the case back to the TAC to ascertain evidence as to whether the funds in the accounts were indeed excess funds that were deposited to the bank accounts, as stated by the TAC.

In light of the above, the Appellant's submissions, I would first like to examine whether the onus is on the Appellant to establish that the Appellant is exempt from income tax or that the Respondent must establish that the Appellant is liable to tax. In the case of *Union of India v. (M/s). Wood Papers Limited*[6] it was observed that; *'Literally exemption is freedom from liability, tax or duty. Fiscally it may assume varying shapes, especially in a growing economy. For instance, tax holiday to new units, concessional rate of tax to goods or persons for limited period or with specific objective etc. That is why its construction, unlike charging provision, is like an exception and on normal principle of construction or interpretation of statutes, it is construed strictly either because of legislative intention or on economic justification of inequitable burden or progressive approach of fiscal provisions intended to augment State revenue*'.

It was also observed '*When the question is whether a subject falls in the notification or in the exemption clause then it being in the nature of exception is to construed strictly and against the subject; but once about ambiguity or doubt about applicability is lifted and the subject falls in the notification, then full play should be given to it and it calls for a wider and liberal construction*'.

In the case of *Madras Provincial Co-operative Bank Ltd. v. Commissioner of Income tax, Madras*,[7] the question was one of construction of a notification granting a tax exemption to a Co-operative society for the profits made in its turnover. The Court observed that '*If an assessee is under a section of taxing statute assessable to tax, it is for that person to show that he has been exempted*'.

[6] AIR 1991 SC 2049: 1991(1) JT 151: (1990) 4 SCC 256.
[7] AIR 1933 Mad 489(FB).

In the case of *Liquidators of Pursa Ltd v. Commissioner of Income Tax, Bihar*[8] the Court observed that '*In construing an Act which imposes a burden, doubts, should be resolved in favour of the tax-payer but this general rule cannot be applied when the taxing provision is clear and explicit or when a doubt arises in regard to a provision granting a deduction of an exemption from payment of tax.*'

It was the Appellant who asserted that the Appellant earned interest in terms of the agreements with the banks for the amounts deposited into the Appellant's accounts during the credit period offered by the consignee. Accordingly, in my view, it is the Appellant who should have produced these agreements and satisfied the authorities with his claim. I therefore find that there is no obligation on the Court to refer the matter back to the TAC to ascertain further evidence.

Based on the foregoing analysis, it is my considered view that the Appellant has failed to satisfy that the Appellant meets the second test set out by Howard C.J., and Keuneman J. In my view, interest on the Appellant's deposits in this case does not flow from transactions entered into to carry on its business and does not correspond to income exempt under Clause 10 (i) of the agreement with the BOI, read along with Section 3 (a) of the IR Act.

In the judgment of Wijeyewardene J., in the CFI case, His Lordship concluded that the CGIR has an option to decide under which source the income should fall. However, this view was not endorsed by any other judge. Keuneman J., expressly repudiated the view expressed by Wijeyewardene J., and observed that the same view expressed by Akbar J., in the previous case of the *Commissioner of Income Tax v. Arunachalam Chettiar*[9] was only an additional reasoning which could be reviewed in the case at hand. On the above point, Soertsz J., also agreed with Keuneman J. Howard C.J., was of the view that the statement of Wijeyewardene J., was merely *obiter*. Therefore, it is clear that the view expressed by Wijeyewardene J., regarding the option available to the CGIR does not form part of the majority judgement.

The Appellant also cited the following passage from the judgment of Soertsz J., (with whom de Kretser J., agreed)

[8] (1954) SCJ 294, AIR 1954 SC.
[9] 37 N.L.R. 145.

'*The view I have reached is that the categories enumerated in Section 6 (1) are mutually exclusive, and that the question whether 6 (1) (a) or 6 (1) (e) applies in a particular case, depends on whether we are dealing with the* ***profits of a business or the income of an individual. If it is a case of dividends, interests, or discounts appertaining to a business****, they fall within the words "profits of any business" and* ***section (6) (1) (a)*** *applies. If, however, it is a case of dividends, interest or discounts accruing to* ***an individual not, in the course of a business****, but as a part of his income from simple investments, then* ***section 6 (1) (e)*** *is the relevant section, and so far as interest is concerned, section 9 (3) modifies section 9 (1).'* (Emphasis added)

Relying on the aforementioned view expressed by Soertsz J., the Appellant submitted that if the interest appertains to a business, the interest falls under Section 6 (1) (a) and if the interest accruing to an individual, then Section 6 (1) (e) applies. Accordingly, the Appellant argued that the Appellant not being an individual, the income of the Appellant should anyway fall under Section 6 (1) (a) of the IR Act.

However, it is important to observe that in Section 217 of the IR Act, the interpretation Section, the word *person* is defined to include a company as well. Moreover, I am of the view that the language in Section 3 of the IR Act does not suggest an interpretation as to if interest accrues to an individual, not in the course of a business, it is not profit of a business but, is part of his income and if the interest appertains to a company, it is profits of the business. The reason being, Section 3 (a) of the IR Act is not limited to the profits from any trade or business but includes the profits from any profession or vocation as well. A profession or vocation is obviously related to an individual. Therefore, it is obvious that application of Section 3 (a) of the IR Act cannot be limited to a business. Similarly, the dividends interest or discounts are not limited to an individual but could be in relation to a company as well. Accordingly, Section 3 (e) also could not be limited to an individual and should apply to a company as well. Hence, in my view the above submission of the Appellant is devoid of merit.

As a result, although the Appellant suggested that the TAC erred in failing to apply the test suggested by Soertsz J., with whom de Kretser J., agreed, in my view, the TAC has not.

The learned Counsel for the Appellant also submitted that the TAC incorrectly comprehended the CFI judgement by the following statement

made in the TAC determination[10] '*The Ceylon Financial Investment Limited v. Commissioner of Income tax was a case relating to an investment company, and therefore, the interest income and dividends received were treated as part of trading profits, whereas the appellant company, in this case is not an investment company, but a company engaged in the business of manufacturing and making rolled steel products.'* However, in my view, the TAC has made the above distinction between the CFI judgment and this case, only for the purpose of distinguishing the facts and the TAC has not arrived at its determination on the basis that the Appellant is not entitled to the tax exemption as it is not an investment company.

Another argument advanced by the Appellant was that the TAC has wrongly applied the judgment in the English case of *Nuclear Electric Plc v. Bradley*[11] (hereinafter referred to as the *Nuclear Electric* case). Both CGIR and TAC relied on the *Nuclear Electric* case in arriving at their determination. It is a case where the tax payer whose business was generating electricity has set aside part of his business proceeds as an investment to be utilized later as expenditure in the same business. The Court held that this course is not within the meaning of '*trading income*' and, '*investment income*' cannot be converted into '*trading income*' by simply setting up a segregated fund. It was further held that the test is to see whether the investment form an integral part of the business. The Appellant's contention was that the English Courts have considered a different provision of the English statue which is not comparative to Section 3 of the IR Act. It is true that the provision considered in the *Nuclear Electric* case is Section 393 of the Income and Corporation Taxes Act, 1988 of the United Kingdom where the term trading income was interpreted in Section 393 (8) itself. In the said case the issue was whether the income from the investments fell within the scope of that section to be considered as trading income.

Therefore, I agree with the submission of the Appellant that the judgment in the case of *Nuclear Electric* is not conclusive in the application of Section 3 of the IR Act. Yet, the principle set out in the *Nuclear Electric* case that '*investment income*' cannot be converted into '*trading income*' by simply creating up a segregated fund is to some extent equivalent to the procedure adopted by the Appellant by remitting the payment in advance

[10] At page 6 of the TAC determination.
[11] [1995] STC 11 25 (HL).

to a special account in the name of the Appellant. Be that as it may, *Nuclear Electric* case is only one of the authorities considered by the TAC, and therefore, that case has not significantly influenced the decision of the TAC.

Lanka Ventures Limited v. Commissioner General of Inland Revenue (hereinafter referred to as *Lanka Ventures* case) is another case relied upon by the TAC in arriving at its determination. The TAC observed that in the said case this Court has held that the interest income was not earned from venture activities of the company, and therefore did not qualify for the tax exemption. Accordingly, the TAC held that in the instant case too, the disputed interest income cannot be considered as part of the profits and income of the business that were exempted under the BOI agreement. However, the learned Counsel for the Appellant submitted that the Section which was considered by this Court in the *Lanka Ventures* case is Section 22 DDD (2) of the Inland Revenue Act No. 28 of 1979 which reads thus;

'*The provisions of sub section (1), shall apply to any company which commenced to carry on business on or after January 1, 1990 and which is approved for the purposes of this section by the Minister by notice published in the Gazette, before April 1, 1993 and which is engaged* ***solely*** *in carrying on an undertaking of providing venture capital to any undertaking engaged in the manufacture of goods, export of goods, or the provision of any such service as may be approved by the Minister.*' (Emphasis added)

As it was argued by the learned Counsel for the Appellant the word ***solely*** in Section 22 DDD (2) clearly manifest that only income from providing venture capital should be considered and the incidental source of income should be excluded.

Similarly, the interest income of the Appellant in the instant case would fall under Section 3 (a) of the IR Act, only if such income is earned from trade, business, profession or vocation.

Therefore, although the two Sections are different, I am of the view that the principle set out in *Lanka Ventures* judgement is relevant to the instant case as well.

The next argument advanced by the Appellant is that even if the Appellant's income falls under Section 3 (e) of the IR Act, that income is also exempted under Clause 10 (i) of the agreement with the BOI. The

Appellant submitted that Section 17 (1) of the BOI Act confers on the BOI the authority to adopt one of the two methods specified in the Section for the purpose of granting an immunity, exemption, benefits or privileges in respect of income tax. Section 17 (1) reads as follows;

> *'17 (1) the Commission shall have the power to enter into agreements with any enterprise in or outside the area of authority and to grant exemption from any law referred in schedule B here to, or to modify or vary the application of any such laws, to such enterprises in accordance with such regulations as may be made by the Minister'*
>
> *(2) (...)*

Accordingly, the two methods are;

i. To grant exemption from any law referred in schedule B *or*
ii. To modify or vary the application of any laws referred in schedule B.

The regulations made by the Minister under Section 17 (1) of the BOI Act and published in Gazette Extra Ordinary No. 8/2 dated 31/10/1978 also confer authority on the BOI to grant exemptions from any laws referred to in schedule B. Consequently, clause 10 (i) of the BOI agreement is based on the first method and clause 10 (ii) is based on the second method. The relevant clause for the case at hand is clause 10 (i) of the BOI agreement.

Clause 10 (i) of the BOI agreement reads thus;

'10 (i) For a period of three (03) years reckoned from the year of assessment as may be determined by the Board (hereinafter referred to as "the tax exemption period") the provisions of the Inland Revenue Act No. 38 of 2000 relating to the ***imposition, payment and recovery of income tax in respect of the profits and income of the Enterprise shall not apply to the profits and income of the Enterprise****'* (Emphasis added)

The Appellant submitted that according to clause 22 of the BOI agreement enterprise shall mean Confab Steel Private Limited and also in the preamble of the BOI agreement Confab Steel Private Limited is referred to as the enterprise. Consequently, the Appellant argued that all of the profits and income of the Appellant would be exempted from the application of IR Act.

It was also submitted by the Appellant that although the term profits and income is not defined in the BOI agreement, the term profits and income is defined in Section 217 of the IR Act to mean '*the net profits or income from any source for any period calculated in accordance with the provisions of this act.'* Accordingly, it was argued that the relevant clause grants the relief to the income of the Appellant from all sources and the entirety of the IR Act has no application to the profits and income of the enterprise.

However, it is important to observe that clause 10 (i) is followed by the opening paragraph of clause 10 which reads as follows;

'*In accordance with and subject to the powers conferred on the Board under Section 17 of the said law No. 04 of 1978 and regulations that may be applicable there to the following benefit and/or exemptions and/or privileges are hereby granted to the enterprise* ***in connection with and/or in relation to the business*****'** (Emphasis added)

Clause 10 (i) cannot be read in isolation from the opening paragraph of clause 10. Therefore, it is clear that clause 10 (i) is restricted by the opening paragraph in clause 10 and any exemption granted to the Appellant pursuant to clause 10 should be in connection with and/or in relation to the business.

However, the Appellant's argument was that clause 10 (i) should not be controlled by the opening words in clause 10 and should be independent of it.

I am not inclined to accept the submission of the Appellant as it is contrary to the accepted rules of interpretation. In addition, the agreement with the BOI is entered into under the aforementioned regulations made under Section 17 (1) of the BOI Act. Accordingly, any agreement cannot supersede the rules set out in the Gazette Notification.

The Regulation No. 6 of the Gazette Notification reads thus;

> *'**6.** The exemption and modification of the laws set out in these regulations may be granted to an enterprise* ***only in respect of or in relation to a business*** *carried on by the enterprise under and in terms of the agreement entered into under section 17 of the Greater Colombo Economic Commission Law, No. 4 of 1978.'* (Emphasis added)

Accordingly, any agreement entered into under the Gazette Notification must be consistent with the provisions of the Gazette Notification. The aforementioned Regulation 6 of the Gazette Notification specifically provides that the exemptions and modifications of the laws provided for in the regulations are granted to an enterprise *only* in respect of or in relation to business carried on by the enterprise.

Furthermore, the BOI agreement states categorically that the approval is granted to the Appellant to set up/conduct and operate an industry/business to set up steel re-rolling mill to manufacture of steel products which is referred to in the agreement as '*the business*'. Therefore, it is clear that the Appellant's business is the manufacture of steel products, not other.

As such, I am not inclined to accept the argument advanced by the learned Counsel for the Appellant that the exemption should apply to the entire profits and income of the Appellant, including the interest income. If such an interpretation is accepted, the words '*in connection with and/or in relation to the business',* found in clause 10 of the agreement becomes redundant.

The Appellant, citing the judgment of this Court in the case of *Ceyspence (Pvt) Ltd (under liquidation) v. The Commissioner General of Inland Revenue*[12] (hereinafter referred to as '*Ceyspence* case') argued that the words *'in relation to'* should be given a broad meaning in view of the Indian judgments cited in that case. However, it is important to note that in the *Ceyspence* case, this Court has distinguished the facts of those Indian cases from the facts of the *Ceyspence* case. Similarly, the facts of the Indian cases differ from those of the case at hand. Moreover, the *Ceyspence* case has not reached its finality and still in appeal before the Supreme Court.

Another argument advanced by the learned Counsel for the Appellant is that the observation made by the TAC to the effect that granting of a *blanket* tax exemption to an enterprise encompassing all its earnings from all its activities cannot be considered as a step taken *'to foster and generate economic development of the republic'* is a statement made in excess of the task of the TAC and it is a matter for the Legislature and the BOI.

The fourth question of law is formulated on the ground that the TAC, relying on the aforementioned policy consideration, dismissed the

[12] C.A. TAX 05/2013. C.A. Minutes dated 24.07.2015

Appellant's appeal on the basis that the tax exemption granted under the BOI agreement is confined to the types of income and profits specified in the agreement. I acknowledge that the TAC's task is not to determine policy matters but, to determine whether the assessment determined by the CGIR is excessive or erroneous. Yet, it is pertinent to note that one of the objectives of the Legislature in establishing the BOI is *'to foster and generate economic development of the republic'*[13]. Therefore, in my view, the TAC has rightly taken into account Section 3 (a) of the BOI Act in determining the scope of the exemption granted under paragraph 10 (i) of the agreement.

The first question of law is formulated on the assumption that the Appellant is immune from liability to pay income tax chargeable under the IR Act due to the clause 10 (i) of BOI agreement. It must be noted that the Appellant received the said interest income not from engaging in the business of manufacturing and marketing of rolled steel products, but from making short term deposits with commercial banks. If the Appellant did not make such deposits with banks, then the Appellant would not receive such an interest income. Thus, interest income received by the Appellant from making such deposits cannot be taken as an interest income received in connection with and/or in relation to the business of the enterprise to be treated as exempted under the BOI agreement. This interest income is separate from the trading income of the Appellant, and thus not immune from liability to pay tax.

The second question of law is formulated on the basis that the TAC erred in law in arriving at the conclusion that the Appellant's deposits in the banks were investments made with the intention of receiving interest. However, it is important to note that the TAC has not arrived at such a conclusion in its determination.

The third question of law is formulated on the following statement made by the TAC in its determination: *'Clause 10 (1) of the BOI agreement has granted a tax exemption for a period of 3 years in relation to the business of the enterprise namely manufacturing and marketing of rolled steel products, so that the provisions of the Inland Revenue Act No. 38 of 2000, relating to imposition payment and recovery of income tax should not apply to the profits and income of the Enterprise'.* The Appellant relied on the statement: '*the provisions of the Inland Revenue Act No. 38 of 2000,*

[13] Section 3 of the BOI Act.

relating to the imposition payment and recovery of income tax should not apply to the profits and income of the Enterprise' and claimed that the TAC has determined that the Appellant's entire income should be exempted from income tax. However, it is important to note that the aforementioned phrase is subject to the following qualification in the same paragraph: *'granted a tax exemption ……. in relation to the business of the enterprise namely manufacturing and marketing of rolled steel products'*

Therefore, as suggested in the third question of law, it is incorrect to state that the TAC has acknowledged that the entire income of the enterprise is exempted from income tax.

Conclusion

Thus, having considered all arguments presented to this Court, I hold that the TAC has not erred arriving at its determination.

Accordingly, I answer all four questions of law in the negative in favour of the Respondent.

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

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

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

JUDGE OF THE COURT OF APPEAL

Dr. Ruwan Fernando J.

I Agree.

JUDGE OF THE COURT OF APPEAL