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).

Unilever Sri Lanka Limited,
No. 258, M. Vincent Perera Mawatha,
Colombo 14.

APPELLANT

CA No. CA/TAX/0019/2018
Tax Appeals Commission
No. TAC/VAT/001/2014

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 : Dr. Kanag-Isvaran, P.C., with Dr. Shivaji Felix and Shivaan Kanag-Isvaran for the Appellant.

F. Jameel, ASG, P.C., with Suranga Wimalasena, DSG for the Respondent.

WRITTEN SUBMISSIONS : 03.05.2019, 06.09.2019 & 02.06.2022 (by the Appellant)

29.07.2019 (by the Respondent)

ARGUED ON : 21.03.2022

DECIDED ON : 04.11.2022

M. Sampath K. B. Wijeratne J.

Introduction

The Appellant, Unilever Sri Lanka Limited (hereinafter referred to as 'USL') is a limited liability company incorporated in Sri Lanka, engaged in the manufacture, production, marketing and distribution of a variety of household goods and consumer products such as soaps, detergents, toiletries and food products under the trademarks/brand names of Unilever PLC in the United Kingdom. The Appellant furnished the Value Added Tax (hereinafter referred to as 'VAT') returns for the taxable quarters of the year 2010 and the Assessor rejected the returns for eight taxable periods ending on 31.01.2010 (10031), 31.03.2010 (10033), 30.06.2010 (10063), 31.07.2010 (10091), 31.08.2010 (10092), 30.09.210 (10093), 31.10.2010 (10121) and 30.09.2010 (10122) by his letter dated 8th June 2011 issued under Section 29 of the VAT Act. By the same letter, the Assessor communicated the reasons for not accepting the returns namely, the Appellant's failure to declare the value of supply of two products: *Vim* dish bars and the *Signal* toothbrushes made by the Appellant[1]. Thereafter, the Assessor proceeded to issue Notice of Assessment.

Being aggrieved by the assessment, the Appellant appealed to the Commissioner General of Inland Revenue (hereinafter referred to as 'the CGIR') pursuant to Section 34 of the VAT Act. The CGIR made his determination on the 19th December 2013 confirming the Assessor's assessment. The Appellant was informed of the reasons for the determination by letter dated 23rd January 2013.

[1] *Vide* CGIR's determination at page 9 of the appeal brief.

The Appellant appealed to the Tax Appeals Commission (hereinafter referred to as 'the TAC') under Section 7 of Tax Appeals Commission Act No. 23 of 2011, as amended (hereinafter referred to as 'the TAC Act'), against the determination of the CGIR.

The TAC made its determination on the 22nd April 2014 confirming the determination of the CGIR and dismissed the appeal. The Appellant, aggrieved by the determination, moved the TAC to state a case to this Court on the following five questions of law.

1. ***Is the determination of the Tax Appeals Commission time barred?***

2. ***Did the Tax Appeals commission err in law in coming into the conclusion that the Appellant was a manufacturer within the contemplation of the Value Added Tax Act, No. 14 of 2002 (as amended)?***

3. ***Is the determination of the Tax Appeals Commission against the weight of the evidence?***

4. ***Is the amount of Value Added Tax and penalty payable, as confirmed by the tax Appeals Commission, excessive, arbitrary and unreasonable?***

5. ***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?***

Factual background

The Appellant USL has a Trademark License Agreement with Unilever PLC of the United Kingdom. The agreement authorized the Appellant, as the sole licensee, to use the trademarks relating to the products defined in the list including *Vim* scourer bars and *Signal* toothbrushes. in connection with manufacture, packaging, advertising and sale of these articles in Sri Lanka[2]. Accordingly, the Appellant entered into two manufacturing agreements with two companies named R M Chemical Ceylon (Pvt) Limited[3] (hereinafter referred as 'RMCC') to manufacture *Vim* scourer

[2] At page 96 of the appeal brief.
[3] Agreement dated 25th June 2002, at p. 319 of the appeal brief.

bars and Polypak Secco Limited[4] (hereinafter referred to as 'PSL') to manufacture *Signal* toothbrushes[5]. These facts are unchallenged.

Analysis

Is the determination of the Tax Appeals Commission time barred?

The learned President's Counsel for the Appellant submitted that the TAC made its determination beyond the prescribed time limit resulting the appeal being abated. It was also submitted that this has the practical effect of allowing the appeal[6]. This brings up the first question of law.

In my view, the above question is twofold: Did the TAC make its determination within the deadline and is the deadline mandatory? It does not appear necessary to restate the sequence of events to determine whether the determination of the TAC was within the timeframe. This allegation was not contested by the learned Additional Solicitor General and the Court is satisfied that the TAC in fact exceeded the time limit. The Respondent argued that the period specified for determination by the TAC merely directory.

This leads me directly to the question of whether compliance with the timeline is mandatory, or merely directory.

The learned President's Counsel for the Appellant argued that the Legislature, by amending the above provision, not only once but twice with retrospective effect and having an avoidance of doubt clause in Section 15, clearly manifested its intention of enacting the time frame provided for the conclusion of an appeal to be mandatory[7].

However, I am not inclined to accept the submission of the learned President's Counsel for the Appellant. The Legislature, at first having extended the one-hundred-and-eighty-day period from the **commencement of the hearing,** up to two hundred and seventy days, later reduced the said period by enacting that the time should take effect from the **commencement of sittings for the hearing**, which would precede the hearing itself.

[4] Agreement dated 30th August 2005, at p. 307 of the appeal brief.
[5] At paragraph 11 of the Appellant's Written Submissions filed on the 3rd May 2019.
[6] *Ibid* at paragraph 73.
[7] *Ibid* at paragraphs 39, 60 and 72.

In the case of *D.M.S. Fernando and Another v. Mohideen Ismail*,[8] Neville Samarakoon C.J., citing *Maxwell on the Interpretation of Statutes*[9], introduced a three-limbed test that may assist in determining the intention of the Legislature:

'*Then again it is said that to discover the intention of the Legislature it is necessary to consider - (1) The Law as it stood before the Statute was passed. (2) The mischief if any under the old law which the Statute sought to remedy and (3) The remedy itself.*'

In applying this test to the present case, it appears that the law as it existed prior to the amendments was modified by extension and reduction, as the Legislature has deemed appropriate, the timeframe within which the TAC should decide. There does not seem to be any clear mischief that the amendments were meant to correct, and the remedy itself does not appear to be anything other than a modification of the time granted to the TAC to decide an appeal. Even if the mischief sought to be corrected was a delay in the appeal process, there is little support for the claim that the Legislature intended the said time limit to be mandatory, since it was initially extended, and then reduced.

Therefore, I am of the view that the intention of the Legislature in amending the aforementioned clause was merely to redefine. the time available to the TAC to adjudicate an appeal.

It is also important to note that while the Legislature has amended the relevant provision on two occasions, it did not specifically make the deadline mandatory. If the intention of the legislature was that the failure of the TAC to meet the time limit should entitle the Appellant to the relief sought, the legislature could have expressly enacted it.

In the case of *K. Nagalingam v. Lakshman de Mel*,[10] Sharvananda J. (as His Lordship then was) cited the following two excerpts from the academic literature, in determining whether a statutory time frame for the discharge of a duty was mandatory:

[8] [1982] 1 Sri.L.R. 222, at p.229.

[9] Twelfth edition.

[10] 78 N.L.R. 231, at pp.236-237.

'*The whole scope and purpose of the enactment must be considered, and one must of that provision* ***to the general object intended to be secured by the Act****' – Smith Judicial Review of Administrative Action (2nd Ed. at page 126)* (emphasis added).'

"*Where the prescriptions of a statute relate to the performance of a public duty, and where 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 yet not promote 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,* ***when 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****. (Maxwell-11th Ed. at page 369)* (emphasis added)."

Having reviewed the above legal literature, His Lordship concluded the following about the time limits prescribed by the Termination of Employment Act:

'*The object of the provision relating to time limit in section 2 (2) (c) is to discourage bureaucratic delay. That provision is an injunction on the Commissioner to give his decision within the 3 months and not to keep parties in suspense. Both the employer and the employee should, without undue delay, know the fate of the application made by the employer. But the delay should not render null and void the proceedings and prejudicially affect the parties, as the parties have no control over the proceedings. It could not have been intended that the delay should cause a loss of the jurisdiction that the Commissioner had, to give an effective order of approval or refuse. In my view, a failure to comply literally with the aforesaid provision does not affect the efficacy or finality of the Commissioner's order made thereunder.* ***Had it been the intention of Parliament to avoid such orders, nothing would have been simpler than to have so stipulated*** (emphasis added).'

His Lordship upheld this decision in the subsequent case of *Ramalingam v. Thangarajah*,[11] by deciding that the time limits prescribed by the Primary Courts Procedure Act were to be interpreted as directory, and not mandatory.

One cannot assume that there was any oversight by the Legislature when Section 10 of the TAC Act was drafted and amended by not specifying the consequences that result when the TAC does not strictly comply with the prescribed deadline. This is further supported by the fact that, as submitted by counsel for the Appellant himself, the relevant section has been amended twice. This means that the Legislature had the opportunity on two occasions to specify the consequences of non-compliance, even though it saw fit not to do so.

In the case of *Mohideen v. The Commissioner General of Inland Revenue*,[12] His Lordship Gooneratne J. (sitting in the Court of Appeal) made a similar observation when considering the intention of the Legislature regarding the time limit available for the Board of Review (which was the body that was replaced by the TAC) to reach its determination:

'*If it was the intention of the legislature that hearing* (sic) *should be concluded within 2 years from the date of filing the petition or that the time period of 2 years begins to run from the date of filing the petition,* ***there could not have been a difficulty to make express provision, in that regard*** (emphasis added).'

In light of certain tax statutes passed by our Parliament, I note that the Legislature, in its wisdom, has specifically enacted in Section 165 (6) of the Inland Revenue Act No. 10 of 2006 (hereinafter referred to as 'the IR Act'), as amended, that failure to acknowledge receipt of an appeal within thirty days of receipt should result the appeal being deemed to have been received on the day on which it is delivered to the CGIR. Furthermore, Section 165(14) of the IR Act provides that failure to dispose of an appeal within two years of its receipt should result in the appeal being allowed and tax charged accordingly. Similarly, Section 34 (8) of the VAT Act also

[11] [1982] 2 Sri.L.R. 693, at p.703.

[12] CA (BRA) 02/2007, decided on 16.01.2014, at p.18.

provides that the failure to determine an appeal within the specified time limit should result in the appeal being allowed and tax charged accordingly.

Inland Revenue Act No. 24 of 2017, which is in force as at now, also provides for an Administrative Review of an assessment by the CGIR. However, unlike in the previous Inland Revenue Act No. 10 of 2006, no time frame has been specified in Section 139 for the CGIR to deliver his decision. Nevertheless, Section 140 provides that within thirty days from the date of the decision or upon lapse of ninety days from the request being made for an administrative review, the tax payer is entitled to make an appeal to the TAC. Hence, it is clear that while the breach of certain time limits is accompanied by remedies or sanctions, the breach of others is not. It should be noted that, under Section 144 of the 2017 Act, if the TAC fails either to determine or to respond to an appeal filed by a person within ninety days from the appeal request, the Appellant has the right to appeal to the Court of Appeal.

From the preceding analysis, it is clear that in the new Inland Revenue Act No. 24 of 2017, the Legislature has removed the penal consequences previously imposed on the CGIR for failure to meet the statutory deadline. Nevertheless, in the event of non-compliance, the Appellant has been granted a remedy through a direct right of appeal to the TAC. In addition, upon the failure of the TAC to respond to an appeal request within the prescribed time frame, the Appellant has been granted a direct right of appeal to the Court of Appeal. Therefore, it can be seen that though the Legislature has in the case of the Inland Revenue Act No. 24 of 2017, introduced a remedy where the TAC fails to respond within the specified time limit; in the case of the TAC Act, despite twice availing itself of the opportunity to amend the law, the Legislature has not specified a remedy in case of non-compliance.

I am not unmindful of the fact that this particular question of law is on the TAC Act. Yet, I am of the view that consideration of the above provisions in the Inland Revenue Act are relevant, since those provisions manifest the intention of the Legislature regarding the time limits imposed on the TAC.

In light of the above, it is my considered view that the Legislature, although has amended Section 10 of the TAC Act twice, intentionally refrained from introducing a penal consequence and/or a remedy for the failure of the TAC

to comply with the specified time limit. Therefore, I am not in favour of the argument advanced by the learned President's Counsel for the Appellant, that the fact that the Legislature has amended Section 10 twice with retrospective effect means that it intended the time limit contained therein to be mandatory.

Furthermore, by Amendment Act No. 20 of 2013, the proviso to Section 10 of the TAC Act was amended by extending the time limit granted to the Commission to determine an appeal transferred from the Board of Review, up to twenty-four months; twice the time limit which existed previously.

In the same amendment, through the introduction of Section 15, the avoidance of doubt clause, the Legislature promulgated that the TAC has power to hear and determine any pending appeal that was deemed to have been transferred to the Commission from the Board of Review under Section 10 of the principal Act, notwithstanding the expiry of twelve months granted for its determination.

Since Section 10 was amended retrospectively, in any event, the 24-month period will apply to all appeals transferred from the Board of Review. As a result, the introduction of Section 15 of the amendment will not have any useful effect and appears redundant. Nevertheless, in my view, Section 15 demonstrates that the intention of the Legislature, by introducing Amending Act No. 20 of 2013, is not to make the time frames mandatory.

On the other hand, it is possible to argue that the application of Section 15 of the amendment is limited to the proviso in Section 10 and that therefore, the Legislature has expressed its intention that the time limit in the proviso to be merely directory, but that which is in the main part to be mandatory. Yet, this cannot be a valid argument since in the circumstances, the Legislature has extended the time frame in the proviso and reduced it in the main part, by the same Amendment. When the time limit is lowered, the question of going beyond the existing deadline will not arise, and therefore, a necessity to enact as above will also not arise.

Therefore, I am not willing to accept the assertion of the learned President's Counsel for the Appellant, that the fact that the Legislature gave retrospective effect to the amended provisions means that it intended the time limit contained in Section 10 to be mandatory.

Having argued extensively, as above, that the time limit specified for the TAC is mandatory, the learned President's Counsel for the Appellant submitted that when the two-hundred-and-seventy-day time limit is exceeded, the appeal stands abated. The practical effect would be that the appeal is as good as allowed[13].

In my view, the submission of the learned President's Counsel for the Appellant that if this Court were to hold that the TAC prevented from hearing an appeal after the two-hundred-and-seventy-day period has lapsed, the appeal should stand allowed is untenable. Should the State, and in general the people of this country, lose revenue or the taxpayers themselves lose the opportunity of getting the relief because of the fault of the TAC?

Samarakoon C.J.'s judgement in the case of *K. Visvalingam and Others v. Don John Francis Liyanage*,[14] addresses the above issue, in the context of the time limit applicable to a Fundamental Rights petition before the Supreme Court of Sri Lanka:

'*These provisions confer a right on the citizen and a duty on the Court. If that right was intended to be lost because the Court fails in its duty, the Constitution would have so provided. It has provided no sanction of any kind in case of such failure. To my mind, it was only an injunction to be respected and obeyed but, fell short of punishment if disobeyed. I am of the opinion that the provisions of Article 126 (5) are directory and not mandatory. **Any other construction would deprive a citizen of his fundamental right for no fault of his*** (emphasis added).'

Sharvananda J. (as His Lordship then was) made a similar observation in the previously cited case of *K. Nagalingam v. Lakshman de Mel*,[15] regarding an order made by the Commissioner of Labour after the expiry of a statutory time limit:

*'To hold that non-compliance with the time limit stipulated by section 2 (2) (c) renders the Commissioner's order of approval - or refusal void will cause grave hardship to innocent parties. **Parties who have done all that the statute requires of them should not lose the benefit of the order***

[13] At paragraph 57 of the Appellant's Written Submission filed on the 12th May 2020.
[14] Decisions on Fundamental Rights Cases, 452, at p.468.
[15] *Supra* note 8, at p.237.

because it was made after the final hour had struck with the passage of the 3 months (emphasis added).*'*

I find that the comments of Their Lordships are relevant to the present case, illustrating the injustice that either party could suffer if the TAC was to be determined to be *functus officio* at the expiration of the relevant period. In addition, when an appeal was made to the TAC, it necessarily follows that the Appellant would have done so with high confidence in a positive result. In such a case, it would not be necessary for the Appellant, upon expiry of the time limit, to require that the determination of the TAC be prescribed, since there would always be every possibility that their appeal would be successful, and no significant injustice would be caused owing to the delay. Even if some other significant rights were to be infringed upon, it would not weigh so heavily as to vitiate the right of either party to receive a considered determination from the TAC.

It is therefore the opinion of this Court that there is no statutory construction whereby either the appeal before the TAC being abated and/or being allowed, where the TAC has overrun its statutory time frame. It is therefore best left to the Legislature to specify in no uncertain terms what the effect, if any, of a time bar would be, in order to avoid any inequitable outcomes as illustrated above.

In the previously cited case of *Mohideen v. The Commissioner General of Inland Revenue* (hereinafter referred to as '*Mohideen*'),[16] it was stated that the time limit for determining the appeal by the Board of Review would be mandatory, if counted from the commencement of the hearing. The wording of Gooneratne J in the paragraph under consideration is as follows:[17]

'*I find that an area is left uncertain for interested parties to give different interpretation on time bar. Hearing need* (sic) *to be in camera and Section 140 subsection 7, 8 & 9 provide for adducing evidence. As such in the context of this case and by perusing the applicable provision, it seems to be that the hearing contemplated is nothing but 'oral hearing'. One has to give a practical and a meaningful interpretation to the usual day to day*

[16] *Supra* note 10.

[17] *Ibid.* at p.15.

functions or steps taken in a court of law or a statutory body involved in quasi-judicial functions, duty or obligation. If specific time limits are to be laid down the legislature need to say so in very clear 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. ***It would be different or invalid if the time period exceeded 2 years from the date of oral hearing. If that be so it is time barred*** (emphasis added).'

However, in the subsequent cases of *Kegalle Plantations PLC v. The Commissioner General of Inland Revenue*[18] (hereinafter referred to as *Kegalle* Plantations) and *Stafford Motor Company (Private) Limited v. The Commissioner General of Inland Revenue* (hereinafter referred to as '*Stafford Motors*'),[19] Their Lordships declined to follow the reasoning in *Mohideen* on the ground that it is *obiter dicta.*

Black's Law Dictionary provides the following definition for *obiter dictum*:[20]

'*[Latin "something said in passing"] A judicial comment made while delivering a judicial opinion, but one that is* ***unnecessary to the decision in the case*** *and therefore not precedential (although it may be considered persuasive). Often shortened to dictum or, less commonly, obiter* (emphasis added).'

The learned Counsel for the Appellant invited the Court to depart from the ruling in *Kegalle Plantations* and *Stafford Motors,* and argued that even though statement of Gooneratne J., regarding applicability of the time bar would not constitute part of the *ratio decidendi* for the decision it nevertheless constitutes relevant judicial dicta which sheds light on this issue[21].

[18] CA (TAX) 09/2017, decided on 04.09.2018.

[19] CA (TAX) 17/2017, decided on 15.03.2019. [This stance was further affirmed in the case of *CIC Agri Businesses (Private) Limited v. The Commissioner General of Inland Revenue* [CA (TAX) 42/2014, decided on 29.05.2020].

[20] B. A. Garner and H. C. Black, *Black's Law Dictionary*, Ninth Edition, 2009. at p.1177.

[21] At paragraph 59 of the Appellant's Written Submissions filed on the 12th May 2020.

However, it was observed by His Lordship Justice Soza (sitting in the Court of Appeal) in the case of *Ramanathan Chettiar v. Wickramarachchi and Others* that:[22]

'*The doctrine of stare decisis is no doubt an indispensable foundation upon which to decide what is the law and its application to individual cases. It provides at least some degree of certainty upon which individuals can rely in the conduct of their affairs as well as a basis for orderly development of legal rules. Certainty in the law is no doubt very desirable because there is always the danger of disturbing retrospectively the basis on which contracts, settlements of property and fiscal arrangements have been entered into. Further there is also the especial need for certainty as to the criminal law. While the greatest weight must be given to these considerations, certainty must not be achieved by perpetuating error or by insulating the law against the currents of social change*.'

If indeed this Court were to find that the said statement in *Mohideen* is *obiter*, then it would not set a binding precedent on the matter in issue in this case, under this particular question of law.

Although I note that Their Lordships in *Mohideen* observed the foregoing in answering a specific question of law raised by the Appellant, closer scrutiny of the final two sentences of that paragraph reveal that they are not essential to the finding of the Court. The finding of the Court was that the Board of Review had not erred in law as regards the time available for it to arrive at its determination. The matter in issue in deciding that particular question of law was whether or not the two-year time limit applicable to the Board of Review was to be counted from the date of receipt of the Petition of Appeal by the Board, or whether it was to be counted from the date of commencement of the hearing of the appeal. That matter was decided in favour of the Respondent, with the Court holding the latter to be the case.

In the above context, the final two sentences, '*It would be different or invalid if the time period exceeded 2 years from the date of oral hearing. If that be so it is time barred*.', constitute a conditional observation by Their Lordships. Its nature is hypothetical, and does not reflect the facts of the

[22] [1978-79] 2 Sri.L.R. 395, at p.410.

case, as the time period did not exceed two years from the date of oral hearing. In other words, if these two sentences were taken out of the judgement, there would be no change whatsoever either to the line of reasoning in *Mohideen*, or to the outcome. I therefore consider that the hypothetical conclusion arrived at by Their Lordships in *Mohideen* is indeed 'unnecessary to the decision in the case'. I am of the view that the aforementioned final two sentences do not form part of the *ratio* in *Mohideen.* Therefore, in keeping with the definition I have provided above, and following the dicta in *Stafford Motors*, it is my view that the particular statement in *Mohideen* (as reproduced and emphasised on above) is indeed *obiter dictum*.

The doctrine of stare decisis also requires the court to follow the judgment in *Stafford Motors* and the line of cases it is part of,[23] to avoid disturbing the certainty established by such cases.

Thus, for the reasons enunciated above in this judgement, I would prefer to follow the judgement in the case of *Stafford Motors*, and I hold that the time limit prescribed in Section 10 of the TAC Act is merely directory.

In concluding my reasoning on the first question of law, I am indeed mindful of the contention by the learned Counsel for the Appellant that the two-hundred-and-seventy-day time frame cannot be devoid of meaning. I am aware that a lack of substantial compliance with the said time frame may inconvenience the taxpayer, especially where the time frame is overrun by many years. In the case of *Wickremaratne v. Samarawickrema and Others*,[24] Silva J. (as His Lordship then was) stated that:

'*In statutory interpretation there is a presumption that the Legislature did not intend what is inconvenient or unreasonable. The rule is that the construction most agreeable to justice and reason should be given.*'

I am of the opinion that a ruling to the effect that the time frame contained in Section 10 of the TAC Act is mandatory, would be inconvenient to the TAC, since delays must be countenanced owing to a variety of circumstances. Furthermore, to declare that the TAC is *functus officio* upon expiry of the time frame would be unreasonable to both parties for the

[23] *Supra* note 17.

[24] [1995] 2 Sri.L.R. 212, at p.218.

reasons enunciated above. However, that is not to say that this Court endorses significant delays on the part of the TAC, rather, it is merely acknowledging that the construction most agreeable to justice and reason is that the time frame prescribed in Section 10 of the TAC Act is merely directory. The duty of this Court is not to legislate, but to interpret legislation. Legislation is the prerogative of the Legislature. It is therefore the duty of the Legislature to specify what penal consequence or remedy, if any, must follow a lack of substantial compliance by the TAC with the time frame specified in Section 10 of the TAC Act, so that the parties are not inconvenienced.

Accordingly, having given due consideration to all of the learned President's Counsel's submissions on this question of law, I hold that the determination of the TAC is not time barred.

As a result, I answer the first question of law in the negative, in favour of the Respondent.

Whether the Appellant is a *manufacturer* pursuant to the VAT Act?

The principal issue in this appeal is whether the Appellant (USL), or RMCC and PSL are the manufacturers of *Vim* scourer bars and *Signal* toothbrushes within the meaning of the provisions of the VAT Act.

The scope for the imposition of VAT is provided in Section 2 of the VAT Act. Which reads thus;

> '***2.*** *(1) Subject to the provisions of this Act, a tax, to be known as the Value Added Tax (hereinafter referred to as "the tax") shall be charged –*
>
> > *(a) at the time of supply, on every* ***taxable supply*** *of* ***goods or services****, made in a taxable period, by a registered person in the course of the carrying on, or carrying out, of a* ***taxable activity*** *by such person in Sri Lanka;*
> >
> > *(b) (…)*
>
> *(2) (…)*
>
> *(3) (…)*'

The words *taxable activity* is defined in Section 83 as follows;

*'**83**. "**taxable activity**" means –*

(a) any activity carried on as a business, trade, profession or vocation other than in the course of employment or every adventure or concern in the nature of a trade;

(b) the provision of facilities to its members or others for a consideration and the payment of subscription in the case of a club, association or organization;

(c) anything done in connection with the commencement or cessation of any activity or provision of facilities referred to in (a) or (b);

(d) the hiring, or leasing of any movable property or the renting or leasing of immovable property or the administration of any property;

(e) the exploitation of any intangible property such as patents, copyrights or other similar assets where such asset is registered in Sri Lanka or the owner of such asset is domiciled in Sri Lanka;'

It is obvious that, of the five categories mentioned above, the issue under consideration could only fall under (a) or (e). Nevertheless, in my view, the exploitation of intangible property by the Appellant, being the licensee of the Trademarks, occurs when they get their goods to be produced by the RMCC and PSL. However, as the assessment issued by the Assessor is not with regards to the exploitation of intangible property but with regards to the supply of goods by the Appellant to its customers, the application of item (e) above is not relevant here. Nevertheless, it is beyond doubt that the Appellant carries on a business in respect of *Vim* scourer bars and *Signal* toothbrushes, falling under Section 3 (a) of the VAT Act.

Section 83 of the Act defines the terms *taxable supply, supply of goods* and *supply of services* as follows;

*'**83**. '"**taxable supply**" means any supply of goods or services made or deemed to be made in Sri Lanka which is chargeable*

with tax under this Act and includes a supply charged at the rate of zero percent other than an exempt supply.'

*'"**supply of goods**" means the passing of exclusive ownership of goods to another as the owner of such goods or under the authority of any written law and includes the sale of goods by public auction, the transfer of goods under a hire purchase agreement, the sale of goods in satisfaction of a debt and the transfer of goods from a taxable activity to a non-taxable activity;'*

*'"**supply of services**" means any supply which is not a supply of goods but includes any loss incurred in a taxable activity for which an indemnity is due;'*

Accordingly, a *taxable supply* of *goods or services* made by a registered person in the course of carrying on, or carrying out, of a *taxable activity* is subject to VAT.

However, Section 3 of the VAT Act sets out that the *wholesale and retail supply of goods* are exempted from VAT unless the supply was made by a manufacturer or by other categories of persons specified in the Section.

***'3**. (1) Notwithstanding the provisions of section 2, the tax shall not be charged on the wholesale or retail supply of goods, other than on the wholesale or retail supply of goods, by-*

(a) a manufacturer of such goods; or

(b) – (f) (...)

(2) (...)'

The word *manufacturer* is not defined in the VAT Act, but the word *manufacture* is defined in Section 83, the interpretation Section, which reads thus.

'**83**. *"**manufacture**" means the making of an article, the assembling or joining of an article by whatever process, adapting for sale any article, packaging, bottling, putting into boxes, cutting, cleaning, polishing, wrapping, labelling or in any other way preparing an article for sale other than in a wholesale or retail activity;'*

The Appellant submitted that it is abundantly clear from the commercial agreements between RMCC and PSL that the Appellant is not in any way engaged in any of the activities within the term *manufacture* defined in the VAT Act. On the contrary it was submitted that each and every activity within the definition of the term *manufacture* of *Vim* scourer bars and *Signal* toothbrushes are carried out by RMCC and PSL.

The Appellant contended that the question as to whether the Appellant is a manufacturer for the purpose of the VAT Act must be determined solely by reference to the definition in the VAT Act[25]. I do concede that the above matter has to be decided within the scope of the VAT Act itself. Yet, as I have already stated above in this judgement, although the word *manufacture* is defined in the VAT Act the word *manufacturer* is not. However, notably, besides the words *supply of goods* and *supply of services* the word *supplier* is also defined separately. In my view, the Legislature, in its wisdom, did so deliberately, allowing the word *manufacturer* to be interpreted in light of the facts of each case.

The Appellant cited the following observations made by Hoffmann J., in the case of *Charter House Investment Trust v. Tempest Diesels Ltd*[26] . in support of the above-mentioned argument, which reads as follows;

'one must examine the commercial realities of the transaction and decide whether it can properly be described as the going of financial assistance by the company, bearing in mind that the section is a penal one and should not be strained to cover transactions which are not fairly within it.'

Accordingly, it was submitted that when looking at transactions challenged under a law, the Court must look to the commercial realities of what had taken place.

It was also cited the following comment made by Peter Smith J., in *Anglo Petroleum Limited and Paul Sutton v. TFB (Mortgages) Limited*[27] regarding the aforementioned dictum of Hoffmann J.;

'In effect what he is saying is that if a transaction has a lawful and bona fide purpose the court should not strain the section to render the transactions illegal.'

[25] At paragraph 25 of the Appellant's Written Submissions filed on the 3rd May 2019.
[26] (1986) BCLC 1, at p. 10.
[27] (2007) AWCA Civ 456 at paragraph 126/127.

At this point, it is appropriate to examine the terms of the agreements USL has entered with RMCC and PSL to verify their commercial reality.

In the South African case of *Rumbles v. Kwa BAT Marketing (Pty) Ltd* it was observed that contractual terms were not definitive of the nature of any legal relationship that may exist.[28] The Court will have regard to the realities of the relationship between the parties in order to determine the true nature of the relationship between them.

Although, this was a case on labour law, in the Sri Lankan case of *Free Lanka Trading Co. Ltd. v. De Mel, Commissioner of Labour and Others*[29] the Supreme Court held that the description of a relationship in a written agreement between parties was not determinative of the status of parties and that the nature of actual work done and the extent of control exercised were decisive factors.

Therefore, I will now examine the status of parties as reflected in the terms and conditions of the agreement.

The agreement between the Appellant and RMCC is at page 319 of the appeal brief. According to the agreement it is between Unilever Ceylon Limited and RMCC. However, the Appellant conceded that this was an agreement between the Appellant, Unilever Sri Lanka Limited and RMCC[30].

The agreement states that the appellant invited RMCC India to establish a manufacturing unit in Sri Lanka and to this end, RMCC has established a wholly owned subsidiary in Sri Lanka to produce *Vim* scourer bars. The duration of the agreement between the two parties was initially for a period of five years. The parties have agreed to ensure a stipulated return on investment (ROI) to RMCC on its invested funds and the cost of the plant would be reimbursed in five years[31]. However, in the event the agreement is terminated by either party under the termination clauses of the agreement, RMCC will be the sole owner of the plant and machinery[32]. Therefore, in an early termination of the agreement RMCC will be entitled to the plant and machinery which they have setup. The Appellant is required to repay the RMCC's investment within five years. RMCC has

[28] (D1055/2001) [2003] ZALC 57 (21st May 2003).
[29] 79 (II) N.L.R. 158.
[30] At paragraph 11 of the Appellant's Written Submissions filed on the 12th May 2020.
[31] Clause 7.1 of the agreement.
[32] Clause 10.4 of the agreement.

agreed not to enter into any agreements with other parties for the supply of products out of the premises and plant without the consent of the Appellant. From the aforementioned clauses it is clear that RMCC has setup the manufacturing unit in Sri Lanka on the invitation of the Appellant exclusively for the manufacture of *Vim* scourer bars for the Appellant. In fact, the Appellant is required to repay the RMCC's investment within five years.

By focusing on the clauses relating to the manufacture of *Vim* scourer bars, the Appellant representing the brand name *Vim* has permitted RMCC to use the said trademark[33]. The Appellant will communicate the quantity and supply schedule of the product to RMCC and RMCC will manufacture and supply the finished products in accordance with the specifications and quantities communicated by the Appellant. The raw materials, packing materials, bags, wrappers, pouches, labels and other inputs for the manufacture of the finished goods will be arranged by USL, for RMCC to purchase and procured on its own[34]. RMCC has expressly agreed not to claim any right or ownership or goodwill in any of the trademarks or material used by them in the manufacture of finished products[35].

RMCC has agreed not to enter into any agreements with other parties for the supply of products out of the premises and plant without the consent of the Appellant. This condition makes it clear that the plant is setup in the premises, exclusively for manufacturing the Appellant products.

The Appellant has retained the right to reject finished products which are not in conformity with the quality specifications of the Appellant[36].

Upon a careful consideration of the aforementioned clauses, it is my considered view that RMCC has setup a plant exclusively for making *Vim* scourer bars for an on behalf of the Appellant. Although the plant is setup at the cost of RMCC the Appellant has agreed to return the investment within a period of five years. RMCC has further agreed not to produce any other product in the plant without the consent of the Appellant. The plant exclusively produces *Vim* scourer bars of which the trademark rights are assigned to the Appellant by the owner, Unilever PLC, United Kingdom. RMCC has to manufacture the goods according to the specifications and quantities communicated by the Appellant. It is true that the Appellant has

[33] *Ibid* clause 3.2.
[34] *Ibid* clauses 4.1 and 4.3.
[35] *Ibid* clause 8.3.
[36] *Ibid* clause 5.2.

retained the right to reject the finished products which are not in conformity with the quality specifications setup by the Appellant. However, in my view, it cannot be considered as a risk factor associated with the production. It is a condition imposed upon RMCC to meet the quality specifications setup by the Appellant. In fact, the risk of a lower yield is not with RMCC and it has been taken over by the Appellant by agreeing to make minimum payments quarterly to RMCC in order that the fixed costs incurred are covered in case of sales falling below the forecast volume[37].

The agreement between USL and PSL is at page 307 of the appeal brief. In the agreement both parties state that they are in the business of manufacture. PSL agrees to manufacture, sell, and supply toothbrushes to USL bearing the brand names of which USL is the licensee, made to the technical/quality specifications and quantities specified by USL. However, PSL has to ensure the supply of raw and packaging materials through the standard suppliers recommended by USL and those materials meet the quality specifications laid down by the USL.

I am aware that the statutory provisions of the Indian laws considered in the cases cited in this judgment are different from the provisions of Sri Lanka. Yet, the general views expressed in these cases, although not binding can be a guideline.

In the Indian Supreme Court judgement of *Commissioner of Sales Tax, U.O vs. Dr. Sukh Deo*[38], Shah, J.C defined a manufacturer as *'a person by whom or under whose direction and control the articles or materials are made.'*

In the case of *Commissioner of Income Tax vs. Neo Pharma Private Ltd.*[39] High Court of Bombay held that it is not necessary for the manufacturing company to manufacture the goods from its own plant and machinery as its own factory, if, in essence, the manufacturing company employed another company to procure the goods manufactured by it under its own supervision and control.

[37] Clause 7.2 of the agreement.
[38] 1969 AIR 499, 1969 SCR (1) 710.
[39] (1982) 28 CTR (Bom.) 223, 1982 137 ITR 879 Bom.

Hence, it is clear, that although the PSL would purchase the raw and packaging material, the USL has retained the control by setting up the quality specifications and recommending the standard suppliers.

Further, PSL has to make the goods using the plastic moulding tools supplied by USL at their own cost. Those tools will remain USL's exclusive property and even the insurance cover for moulding tools will be taken by USL. Any product which does not meet the standards setup by USL will be destroyed by PSL at their own cost. USL has agreed to pay the price of the products based on an agreed cost model. PSL has agreed to maintain the secrecy/ confidentiality regarding shared information. PSL has agreed that any intellectual property right in relation to information provided by USL to PSL should remain owned by USL. Further, PSL has agreed that the conditions in the agreement do not imply or create any licence in respect of any patent, designs, copyright, or confidential information or know how.

The two agreements between USL and, RMCC and PSL appears to have been entered into so as to erect a facade under cover of which the parties could seek to avoid payment of taxes. In determining one acting for another, Court has to pierce the facade and see the true nature of the transaction between the parties. Upon a careful consideration of the aforementioned terms of the agreement between USL and PSL, I am of the view that, PSL has undertaken making of toothbrushes bearing the brand name assigned to USL by the owner and the manufacturing is done by PSL on behalf of USL and not on their own.

Admittedly, Unilever PLC of the United Kingdom, owner of the Trademarks *Vim* and *Signal* has authorized USL to use the Trademarks as the sole licensee in the manufacture, packaging, advertising, and sale of those products in Sri Lanka[40]. Therefore, it is the Appellant who is legally entitled to manufacture the above goods. Such goods can only be manufactured under the authority granted by the Appellant. If not, the manufacture of those goods would constitute an infringement of the Appellant's intellectual property rights. Hence, there cannot be a legally valid sale of goods to USL either by RMCC or PSL.

As I have already stated above in this judgment, *supply of goods* means the passing of exclusive ownership of goods to another as the owner of such

[40] *Vide* paragraph 12 of the Appellant's Written Submission filed on the 3rd May 2019 and Trademark License Agreement at p. 333 of the appeal brief.

goods or under the authority of any written law. Therefore, no valid sale of goods can take place in the transaction between RMCC and PSL, and USL. Since there is no passing of exclusive ownership of goods from RMCC and PSL to the USL, it amounts to a supply of services. The Appellant argued that RMCC and PSL are the sole parties engaged in all of the activities described in the definition of manufacturer of the *Vim* scourer bars and *Signal* toothbrushes, and therefore Appellant is not the manufacturer. However, it should be noted that section 3 of the VAT Act only applies to supply of goods. Contrastingly, RMCC and PSL are engaged in a supply of services. Thus, it is evident that the Appellant is the manufacturer of the supply of goods and not RMCC and PSL. Hence, the exemption claimed by the Appellant under section 3 of the VAT Act is not applicable here.

The Appellant's contention was that it has only engaged in buying and selling[41] of *Signal* toothbrushes and *Vim* scourer bars and does not manufacture and sell these goods.

In the Indian case of *Whirlpool of India Ltd. Bangalore vs. The Deputy Commissioner of Commercial Taxes, Bangalore*,[42] where the facts of the case were similar to the case at hand, Markandey Katju, J. stated that;

'*sales made by M/s. Applicomp to the Appellant are not sales to the exclusive marketing agent or distributor or wholesaler or any other dealer but are only sales of manufactured branded goods to the brand owner'.*

Applying the same line of argument, it can be seen that the sales by RMCC and PSL to the Appellant are not sales to a wholesaler or a retailer but sales to the brand owner. Hence, as the Appellant is neither a retailer nor a wholesale supplier but the manufacturer of the goods, the Appellant cannot claim the exemption under section 3 of the VAT Act.

In view of the foregoing analysis, I answer the third question of law in the negative, in favour of the Respondent.

Is the determination of the Tax Appals Commission against the weight of the evidence?

In light of the preceding analysis of facts related to this case, it is my considered view that the Tax Appeals Commission having analysed the

[41] At Paragraph 17 of the Appellant's synopsis of Written Submissions tendered on the 2nd June 2022.

[42] Appeal (civil) 5150 of 2006.

evidence properly and giving due weight to such evidence has arrived at the correct conclusion.

Hence, I answer the fourth question of law in the negative, in favour of the Respondent.

Is the amount of VAT and penalty payable, as confirmed by the TAC, excessive, arbitrary and unreasonable?

As I have already stated above in this judgement, the Appellant, USL is the real manufacturer of the *Vim* scourer bars and *Signal* toothbrushes and, consequently, the Appellant is liable to VAT. Although the Appellant raised the aforementioned question of law on the excessive, arbitrary and unreasonable assessment of VAT, the learned President's Counsel for the Appellant did not elaborate on this argument and no separate account statements or any other such evidence in support of the claim was tendered.

The burden is on the tax payer to disprove the correctness of an assessment and to establish a lower figure. Although the dispute may be on the reasons given by the Assessor for rejecting the return and making an assessment, yet, the onus of disproving the estimate lies on the tax payer.

Upon perusing the Appellant's written submissions, it appears that the Appellant has not set out material in support of fourth question of law. In these circumstances, I am unable to find that the assessment of VAT and penalty payable, as confirm by the TAC, are excessive, arbitrary and unseasonable.

Accordingly, I answer the fourth question of law in the negative, in favour of the Respondent.

Did the Tax Appeals Commission err in law when it came to the conclusion that it did?

For the reasons set out above and having considered the preceding four questions of law, I hold that the TAC did not err in law when it arrived at the conclusion that it did.

Accordingly, I answer the fifth question of law in the negative, in favour of the Respondent.

Conclusion

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

Therefore, I answer all five questions in the negative, in favour of the Respondent.

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

In light of the answers given to the above five 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