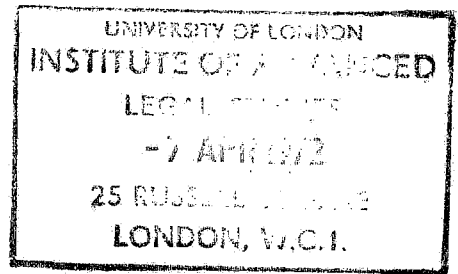


IN THE PRIVY COUNCIL

No. 7 of 1971

O N A P P E A L
FROM THE SUPREME COURT OF CEYLON



B E T W E E N :

THE COMMISSIONER OF INLAND REVENUE
Appellant

- and -

J.M. RAJARATNAM, Assessee
Respondent

CASE FOR THE RESPONDENT

Record

- 10 1. This is an appeal from the Judgment of the Supreme Court of Ceylon (G.T. Samarawickrema J. and C.G. Weeramantry, J.) dated 10th day of December 1969 on a Case Stated under the Income Tax Ordinance (Chapter 242) in respect of a decision of the Board of Review dated 23rd day of June 1967 by the Respondent (hereinafter referred to also as "the Assessee") against Assessments to Income Tax for the year 1958/59. The Supreme Court by its said Judgment set aside with costs the decision of the Board of Review dated 23rd day of June 1967. p.21, 1.17
- 20 2. The question for determination in this appeal is whether payments made under Deeds of Covenant (A1, A2) by the said Assessee are deductible in arriving at the assessable income for the year 1958/59 under the Income Tax Ordinance (Chapter 242), Section 15. p. 18
p. 11
p. 21
p. 11
- 3. The relevant portions of the Income Tax Ordinance (Chapter 242) are included in the Annexure hereto. p. 37
p. 38
- 30 4. The facts are as follows:-
Annexure

The Assessee was a Chartered Accountant having qualified in England and was employed as an audit

<u>Record</u>	assistant in a firm of Chartered Accountants in Ceylon.	
p.2, 1.4 p. 37	(a) On 1st of February 1958 the Assessee under a Deed of Covenant agreed to pay annually to his brother, Mr. Mailvaganam Paramanadan, for a period of seven years the sum of Rs. 1,500/- per annum - <u>marked A1.</u>	
p.2, 1.4 p. 38	(b) On the same date the Assessee under a Deed of Covenant agreed to pay annually to his brother, Mr. Mailvaganam Sathanandan, also for a period of seven years the sum of Rs. 1,500/- per annum - <u>marked A2.</u>	10
pp. 37, 38 Annexure F.12, 1.24	These two documents providing for the payment of annuities are recognized by Sections 26 and 44 of the Stamps Ordinance (Chapter 247) annexed. Stamp Duty recovered on the two Agreements A1, A2 as interest creating Annuity.	
p.1, 1.40 p.2, 1.3	5. The Assessee has paid these sums of Rs. 1,500/- referred to above under the said two Covenants for the year ending 31st March 1958. The two brothers have included such sums as income in their Tax Returns and have been taxed thereon and taxes paid.	20
pp. 37, 38	6. The Assessee in his Tax Returns for the year 1958/59 claimed the two sums paid in 1958 under the Deeds of Covenant (A1 and A2) as deductions as Annuities under Section 15(1) of the Income Tax Ordinance (Annexure) in arriving at his assessable income.	
Annexure pp. 1 - 9	The deduction of these two sums were disallowed whereupon the Assessee appealed to the Commissioner under the Income Tax Ordinance, <u>Section 73(1).</u>	30
	7. By an Order dated 1st December 1966 the Deputy Commissioner, who heard the appeal of the Assessee, confirmed the assessment.	
	8. The ground of appeal was that the two payments made by the Assessee under the Covenants A1 and A2 were annuities and ought to be deducted in arriving at the assessable income in terms of Section 15 of the Income Tax Ordinance.	
pp. 1 - 9	9. The Assessee, being dissatisfied with the said Order dated 1st December 1966 of the Deputy	40

	Commissioner, appealed to the Board of Review under the Income Tax Ordinance, <u>Section 75(1)</u> .	<u>Record</u> p.10
	10. By its decision dated 23rd day of June 1967, the Board of Review dismissed the appeal of the Assessee.	p.11
	11. In arriving at its decision the Board expressed the following view:-	
10	"Section 15 allows the deduction of annuities ground rent and royalty which are not allowed to be deducted under Section 12. The word 'annuity' in Section 15 must be given the same meaning as in Section 12 and that is it must mean a payment made having the character of income expenditure The payments made under Agreements A1 and A2 are not attributable to a source of income and therefore did not come within the category of income expenditure."	p.15, 1.16
		p.16, 1.5
20	12. Dissatisfied with the decision of the Board of Review, the Assessee by his communication dated 5th day of July 1967 applied to the Board under Section 78 of the Ordinance to state a Case for the opinion of the Supreme Court on a question of law:-	p.11 p.17
	That the payments made under the Deeds of Covenant A1 and A2 being annuities are deductible in arriving at the assessable income in terms of Section 15(1) of the Income Tax Ordinance.	pp.37, 38
30	13. The Case was duly Stated for the opinion of the Supreme Court dated 31st day of August 1967 with the question of Law for the opinion of the Supreme Court.	p.18 p.20
	14. The Case came up for hearing in the Supreme Court before G.T. Samarawickrema J. and C.G. Weeramantry J. who, by their Judgment dated 10th day of December 1969, set aside the decision of the Board of Review dated 23rd day of June 1967.	p.21 p.21 to p.26, 1.22 p.11
40	15. The Supreme Court delivered Judgment setting aside the decision of the Board of Review and expressed its opinion (G.T. Samarawickrema J. with C.G. Weeramantry J. agreeing):	
	(a) the promise to pay, or agreement to pay was a binding agreement - <u>Public Trustee vs. Uduruwana</u> 51 N.L.R. 193	p.26, 1.1

Record

- p.26, 1.8 (b) the Covenants were accepted and the money due paid and declared as part of the income for income tax by the recipients.
- p.26, 1.13 (c) the payments were not voluntary but were made under a legal obligation.
- p.26, 1.22 (d) the amounts paid by the appellant (Assessee) satisfy the characteristics of an annuity and were deductible in ascertaining the assessable income and should have been allowed.
- p.23, 1.20 (e) 'Annuity' within the Income Tax Ordinance is not limited to an annuity purchased with a sum of money but extends to other annual payments. 10
- p.34 16. The Appellant was granted Final Leave to appeal to Her Majesty in Council dated 3rd May 1970.
17. The Assessee humbly submits that this Appeal of the Commissioner of Revenue should be dismissed with costs for the following among other

R E A S O N S

- (1) BECAUSE the Judgment of the Supreme Court is right for the reasons therein stated; 20
- (2) BECAUSE the sums paid under the Deeds of Covenant and the deductions claimed were annuities and deductible in ascertaining assessable income under Section 15;
- (3) BECAUSE the Deeds of Covenant were legally enforceable.
- (4) BECAUSE the payments made under the two Deeds of Covenant were not payments within the meaning of Section 12.
- (5) BECAUSE all annuities for a period of years or otherwise whether purchased, under Wills, settlements, order of Court or covenants are all equally deductible under Section 15. 30
18. The Assessee further humbly submits that this appeal of the Appellant is in the nature of a test case and therefore the Appellant be ordered to meet

5.

the costs of the Respondent in the Privy Council
in any event.

S. AMBALAVANER

HAMAVI HANIFFA

Advocates/Barristers-at-Law

A N N E X U R E

INCOME TAX ORDINANCE (Cap. 242)

CHAPTER I

PRELIMINARY

Interpretation S. 2. In this Ordinance, unless the context otherwise requires -

"assessable income" means the residue of the total statutory income of any person after deducting the amount of the deductions provided for in Chapter V;

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"taxable income" means the residue of assessable income after deducting the amount of the allowances provided for in Chapter VI;

CHAPTER II

IMPOSITION OF INCOME TAX

Income chargeable with tax

S. 6. (1) For the purposes of this Ordinance, "profits and income" or "profits" or "income" means

(f) any charge or annuity;

CHAPTER III

ASCERTAINMENT OF PROFITS OR INCOME

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Deductions not allowed

S. 12. For the purpose of ascertaining the profits or income of any person from any source no deduction shall be allowed in respect of -

(j) any annuity, ground rent, or royalty;

CHAPTER V

ASCERTAINMENT OF ASSESSABLE INCOME

Deductions from statutory income in arriving at assessable income.

S. 15. (1) The assessable income of a person for any year of assessment shall be his total statutory income for that year subject to the following deductions:-

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- (a) sums payable by him for the year preceding the year of assessment by way of interest not allowable under section 11(1)(g), annuity, ground rent, or royalty;

Provided that -

- 10 (i) where under section 13 the statutory income arising from any source has been computed by reference to the profits or income of any period other than the year preceding the year of assessment, the interest, annuity, ground rent, or royalty payable in respect of such source shall be computed on the like basis;
- (ii) no deduction shall be allowed in respect of any sum payable by way of interest, annuity, ground rent, or royalty by a person out of Ceylon to another person out of Ceylon;
- 20 (iv) where, at the time of making any assessment, it appears to an Assessor that any of the said sums has not been paid, he may refuse to allow any deduction in respect of that sum; and
- 30 (v) where it appears to an Assessor that any sum in respect of which a deduction has been refused under paragraph (iv) has subsequently been paid, he shall, on application made in writing within twelve months of such payment and supported by such proof as he may require, make an amended assessment allowing such deduction, notwithstanding the provisions of section 79; and any tax found to have been paid in excess as a result of such amended assessment shall be refunded notwithstanding that the claim for such refund may be made after the expiry of the period of three years prescribed by section 89.

CHAPTER VIII

PROVISIONS RELATING TO SPECIAL CASES

(C) PARTNERSHIPS

Assessment of
partnership
income

S. 30. (2) An Assessor may give notice in writing to the precedent partner of the partnership requiring him to furnish within the time limited by such notice a return showing the profits or losses of the partnership from such trade, business, profession, vocation, or employment during the period of twelve months immediately preceding the year of assessment or during any other period in respect of which statutory income may be computed under section 13, ascertained in accordance with the provisions of this Ordinance relating to the ascertainment of profits and income of a person, and showing also any interest, annuity, ground rent, or royalty payable by the partnership in respect of such trade, business, profession, vocation, or employment for the said period. The amount of such interest, annuity, ground rent, or royalty (except where it is payable by a person out of Ceylon to another person out of Ceylon) shall be deducted from the profits or added to the losses ascertained as above, and the figure thus arrived at shall be known as the divisible profit or loss for that period. The precedent partner shall further in such return declare any other income of the partnership for the said period together with the names and addresses of all the partners, and shall apportion among them the whole of the divisible profit or loss and other income in accordance with their shares in the partnership during the period in which the said profit or loss or income arose.

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Where no active partner is resident in Ceylon, the return shall be furnished by the agent of the partnership in Ceylon.

(J) INTEREST, &C., PAYABLE TO
PERSONS OUT OF CEYLON

Deduction of
tax from
interest, &c.

S. 45. (1) Where any person in Ceylon pays or credits to any person or partnership out of Ceylon any sum falling due after the 31st day of March, 1932, but before the 1st day of April, 1951, being -

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(b) rent, ground rent, royalty, or annuity, which is payable either in respect of property in Ceylon or out of income arising in Ceylon,

whether such sum is due from him or from another person, or from a partnership, he shall be entitled notwithstanding any agreement to the contrary whether made before or after the passing of this Ordinance, to deduct tax therefrom.

CHAPTER XI

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APPEALS

APPEALS TO THE COMMISSIONER

S. 73. (1) Any person aggrieved by the amount of an assessment made under this Ordinance may within twenty-one days from the date of the notice of such assessment appeal to the Commissioner by notice of objection in writing to review and revise such assessment. Any person so appealing (hereinafter referred to as "the appellant") shall state precisely in his notice the grounds of his objection and the notice shall not be valid unless it contains such grounds and is made within the period above mentioned:

Procedure on appeals to the Commissioner

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Provided that the Commissioner, upon being satisfied that owing to absence from Ceylon, sickness, or other reasonable cause the appellant was prevented from giving notice of objection within such period, shall grant an extension thereof;

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Provided further that, where the assessment appealed against has been made in the absence of a return of income by the appellant, no notice of objection shall be valid unless and until such return has been duly made.

APPEALS TO THE BOARD OF REVIEW

S. 74. (1) For the purpose of hearing appeals in the manner hereinafter provided, there shall be a board of review (hereinafter referred to as "the board") consisting of not more than twenty members who shall be appointed from time to time by the

Constitution of the board of review

Minister. The members of the board shall hold office for a term of three years but shall be eligible for reappointment.

Right of appeal to the board of review

S. 75. (1) Any appellant, or the authorised representative of any appellant, who is dissatisfied with the determination by the Commissioner of an appeal under section 73, may declare his dissatisfaction with that determination. Such declaration shall be made orally immediately after the announcement by the Commissioner of his determination or shall be communicated in writing to the Commissioner within one week from the date of such announcement.

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(2) Where the appellant has declared or communicated his dissatisfaction in accordance with subsection (1), the Commissioner shall, within one month of the determination of the appeal, transmit in writing to the appellant or his authorized representative his determination and reasons therefor.

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(3) Within one month of the transmission of such written determination and reasons by the Commissioner, the appellant may give notice of appeal to the board. Such notice shall not be entertained unless it is given in writing to the clerk to the board and is accompanied by a copy of the Commissioner's written determination, together with a statement of the grounds of appeal therefrom.

(4) Save with the consent of the board and on such terms as the board may determine the appellant may not, at the hearing by the board, rely on any grounds of appeal other than the grounds stated in accordance with subsection (3), and may not adduce any evidence other than evidence adduced at the hearing of the appeal before the Commissioner.

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APPEALS TO THE SUPREME COURT

Appeal on a question of law to the Supreme Court

S. 78. (1) The decision of the board shall be final:

Provided that either the appellant or the Commissioner may make an application requiring the board to state a case on a question of law for the opinion of the Supreme Court. Such application

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shall not be entertained unless it is made in writing and delivered to the clerk to the board, together with a fee of fifty rupees, within one month of the date of the board's decision. If the decision of the board shall be notified to the Commissioner or to the appellant in writing, the date of the decision, for the purposes of determining the period within which either of such persons may require a case to be stated, shall be the date of the communication by which the decision is notified to him.

(6) Any two or more Judges of the Supreme Court shall hear and determine any question of law arising on the stated case and may in accordance with the decision of the court upon such question confirm, reduce, increase or annul the assessment determined by the board, or may remit the case to the board with the opinion of the court thereon. Where a case is so remitted by the court, the board shall revise the assessment as the opinion of the court may require.

(7) In any proceedings before the Supreme Court under this section, the court may make such order in regard to costs in the Supreme Court and in regard to the sum paid under subsection (1) as to the court may seem fit.

STAMPS ORDINANCE (CHAPTER 247)

LEGISLATIVE ENACTMENTS OF CEYLON, VOL. VIII

CHAPTER II

STAMP DUTIES

(D) PROVISIONS RELATING TO THE CHARGEABILITY OF INSTRUMENTS TO DUTY

S. 26. Any instrument for the creation or sale of any annuity or other right to a periodical payment not before in existence, whether created by actual grant or conveyance or only secured by bond, warrant of attorney, covenant, agreement or otherwise, shall be chargeable with the same duty as on a conveyance of movable property for the consideration

Instrument for the creation or sale of an annuity

set forth in such instrument. If no consideration is set forth, the consideration shall be deemed to be -

- (a) where the annuity or periodical payment is for a definite period not exceeding twenty years so that the total amount to be paid can be previously ascertained, such total amount;
- (b) where the annuity or periodical payment is for a definite period exceeding twenty years, or in perpetuity, or for any indefinite period not terminable with life, the total amount which according to the terms of such instrument will or may be payable during the period of twenty years calculated from the date on which the first payment becomes due; 10
- (c) where the annuity or periodical payment is for a period terminable with any life or lives, the amount which will or may according to the terms of such instrument be payable during the period of twelve years calculated from the date on which the first payment becomes due. 20

CHAPTER IV

INSTRUMENTS NOT DULY STAMPED

Instruments impounded how dealt with

S. 44. (1) When the person impounding an instrument under sections 38 and 39 has by law or consent of parties authority to receive evidence, and admits such instrument in evidence upon payment of a penalty as provided by section 41, he shall send to the Commissioner of Stamps an authenticated copy of such instrument, together with a certificate in writing, stating the amount of duty and penalty levied in respect thereof, and shall send such amount to the Commissioner of Stamps or to such person as he may appoint in this behalf. 30

(2) In every other case the person so impounding an instrument shall send it in original to the Commissioner of Stamps.

No. 7 of 1971

IN THE PRIVY COUNCIL

ON APPEAL FROM THE SUPREME
COURT OF CEYLON

B E T W E E N :

THE COMMISSIONER OF INLAND
REVENUE Appellant

- and -

J.M. RAJARATNAM, Assessee
Respondent

CASE FOR THE RESPONDENT

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Respondent.