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

S.C. (SD) No. 19/2022 to S.C. (SD) No. 21/2022 and S.C. (SD) No. 23/2022 to S.C. (SD) No. 29/2022

SURCHARGE TAX BILL

BEFORE:

Buwaneka Aluwihare, PC - Judge of the Supreme Court
A. H. M. D. Nawaz - Judge of the Supreme Court
Arjuna Obeyesekere - Judge of the Supreme Court

S.C. (SD) No. 19/2022

Petitioner : Swisstek (Ceylon) PLC

Counsel : Uditha Egalahewa, PC, with Damitha Karunarathne, Vishva Vimukthi and Miyuru Egalahewa instructed by H. Chandrakumar de Silva

Respondents : 1. Hon. Mahinda Yapa Abeywardena
2. Hon. Attorney General

S.C. (SD) No. 20/2022

Petitioner : Manikkavasagar Thiyagaraja

Counsel : Uditha Egalahewa, PC, with Damitha Karunarathne, Vishva Vimukthi and Miyuru Egalahewa instructed by H. Chandrakumar de Silva

Respondents : 1. Hon. Mahinda Yapa Abeywardena
2. Hon. Attorney General

S.C. (SD) No. 21/2022

Petitioner : B. K. K. Ranasinghe

Counsel : Romesh De Silva, PC, with Niran Anketell instructed by Sanath Wijewardane

Respondent : Hon. Attorney General

S.C. (SD) No. 23/2022

Petitioner : Asela Sampath Mallawa Arachchi Gamage

Counsel : Sanjeeva Jayawardena, PC, with Lakmali Warusavithana and Dr. Milhan Mohamed instructed by Ashoka Niwunhella

Respondents : 1. Hon. Basil Rajapaksa
2. Hon. Attorney General

S.C. (SD) No. 24/2022

Petitioner : Roshan Pathirana

Counsel : Dushantha Kularathne with Anurangi Singh instructed by Nimmi Sanjeewani

Respondent : Hon. Attorney General

S.C. (SD) No. 25/2022

Petitioners : 1. Brendon Roche
2. Lanka Walltiles PLC

Counsel : Romesh De Silva, PC, with Niran Anketell instructed by Sanath Wijewardane

Respondent : Hon. Attorney General

S.C. (SD) No. 26/22

Petitioners : 1. Don Bannet Gamalath
2. Unidil Packaging Limited

Counsel : Harsha Amarasekera, PC, with Shahila Wijewardena and Aadhes Thureraja instructed by Paul Ratnayeke Associates

Respondents : 1. Hon. Mahinda Yapa Abeywardena
2. Hon. Attorney General

S.C. (SD) No. 27/22

Petitioner : Chandra Jayaratne

Counsel : Suren Gnanaraj with Dathika Wikramanayake, Rashmi Dias and Sakuni Weeraratne instructed by Vidanapathirana Associates

Respondent : Hon. Attorney General

S.C. (SD) No. 28/22

Petitioner : Kapukankanamalage Purnima Priyanthi Gnanasekara

Counsel : Palitha Kumarasinghe, PC, with Harith de Mel and Hasini Rupasinghe instructed by Sanath Wijewardane

Respondent : Hon. Attorney General

S.C. (SD) No. 29/2022

Petitioner : Piyadasa Guruge

Counsel : Naomal Goonewardena with Dilrukshi Paul instructed by Malin Rajapakse

Respondent : Hon. Attorney General

Counsel : Viveka Siriwardena, PC, Additional Solicitor General with Dr. Avanti Perera, Senior State Counsel and Medhaka Fernando, State Counsel for the Respondents

The Court assembled for hearings at 10.00 am on 2nd March 2022, 3rd March 2022, 4th March 2022 and 7th March 2022.

A Bill entitled "Surcharge Tax" [the Bill] was published as a Supplement in Part II of the Government Gazette of 3rd February 2022. It was presented in Parliament by the Hon. Minister of Finance and was placed on the Order Paper of the Parliament of 22nd February 2022.

Eleven applications numbered as above were filed in the Registry of the Supreme Court during the period 23rd February 2022 and 2nd March 2022. Although SC (SD) No. 29/2022 was filed only on 2nd March 2022, this Court allowed the Petitioner in that application to be heard on the basis that 1st March 2022, which was the last date for the filing of applications as provided for by Article 121(1) of the Constitution, was a Public holiday.

The Petitioners in the above applications have invoked the jurisdiction of this Court in terms of Article 121(1) of the Constitution and have prayed for determinations in terms of Article 123 thereof.

The Bill seeks to impose a tax referred to as the "Surcharge Tax" on:

(a) Any individual, partnership or company, whose taxable income for the year of assessment commencing 1st April 2020 exceeds Rupees Two Thousand million, at the rate of twenty-five per cent on the taxable income of such individual, partnership or company for that year:

(b) Each company of a group of companies, of which the aggregate of the taxable income of all subsidiaries and the holding company in that group of companies for the year of assessment commencing 1st April 2020 exceeds Rupees Two Thousand million, at the rate of twenty-five per cent on the taxable income of each such company, for that year.

The Bill contains provisions *inter alia* relating to (a) the furnishing of tax returns in respect of the Surcharge Tax on a form specified by the Commissioner General of Inland Revenue [the Commissioner General], (b) the dates on which the Surcharge Tax must be paid, (c) the application of the provisions of the Inland Revenue Act, No. 24 of 2017, ("the IRA Act, No 24 of 2017") relating to the issuance of assessments, and the challenge of such assessments by way of appeals to the Commissioner General, Tax Appeals Commission and as well as by way of an appeal to the Court of Appeal, and (d) the interpretation of the words, 'group of companies', 'holding company', 'subsidiary' and 'taxable income'.

Once hearing commenced, the learned Additional Solicitor General submitted that she has received instructions from the Ministry of Finance that certain amendments to the Bill will be moved at the Committee Stage of Parliament. While the amendments to the clauses that have been challenged by the Petitioners would be referred to where necessary, we would like to refer at the outset to the amendment sought to be effected to the definition of 'Company' which, as the Bill presently stands, was to have the same meaning as assigned to the said word in the Inland Revenue Act, and included pension funds and provident funds. The learned Additional Solicitor General submitted that the definition would be amended so that it would not include the following:

a) Any Employees Trust Fund, Provident Fund, Pension Fund, Pension Trust Fund, Gratuity or Termination Fund;

b) The Employees Provident Fund established under the Employees Provident Fund Act No. 15 of 1958;

c) The Employees Trust Fund established under the Employees Trust Fund Act No. 46 of 1980;

d) The Ceylon Electricity Board Provident Fund and the Ceylon Electricity Board Pension Fund established under the Ceylon Electricity Board Act No. 17 of 1969;

e) Universities Provident Fund established under the Universities Act No. 16 of 1978;

f) Mercantile Service Provident Society established under the Chamber of Commerce Ordinance;

g) Bank of Ceylon Provident Fund established under the Bank of Ceylon Ordinance;

h) Hatton National Bank Employees Provident Fund established by the Hatton National Bank;

i) People's Bank Pension Trust Fund established under the People's Bank Act No. 29 of 1961;

j) Sri Lanka Central Bank Employees Pension Fund established under the Monetary Law No. 58 of 1949;

k) Sri Lanka Telecom Provident Fund established by Sri Lanka Telecom PLC;

l) National Insurance Trust Fund established under the National Insurance Trust Fund Act No. 28 of 2006;

m) Bank of Ceylon Pension Trust Fund 2014 (POST 96) established under the Trust Ordinance;

n) Any provident fund or contributory pension scheme approved by the Commissioner General of Labour in terms of the Employees Provident Fund Act No. 15 of 1958.

The learned President's Counsel appearing for the Petitioner in SC (SD) No. 22/2022 submitted that the above undertaking of the learned Additional Solicitor General addresses the concerns of the Petitioner represented by him, and in those circumstances, that he has received instructions not to proceed with the said application. Proceedings of the said Determination were accordingly terminated.

The learned Additional Solicitor General submitted that the Bill must be read and understood in its proper context and invited this Court to consider at the outset, the necessity for the imposition of the Surcharge Tax.

The learned Additional Solicitor General traced the roots of the issue that is sought to be addressed by the imposition of the Surcharge Tax to the Budget Speeches of 2020, 2021 and 2022. In the Budget Speech 2020 delivered on 17th November 2020, the Minister of Finance had referred to the World Economic Outlook [20th October 2020], where the International Monetary Fund (IMF) had forecast that due to the "Corona pandemic", almost all the major economies in the world have recorded negative growth rates and have seen a contraction of their economies.

While stating that Sri Lanka is also expected to record a negative growth of 4.3 percent, the Minister had stated that a monumental effort has been made towards the management of the Covid-19 pandemic with the Government spending around Rs. 70,000 million in that regard and the payment of an allowance of Rs.5,000/- to low-income families adversely affected by the Covid-19 pandemic.

The learned President's Counsel for the Petitioner in SC (SD) No. 26/2022 drew our attention to the Annual Report of the Central Bank for the year 2020. The following findings under the heading of "Fiscal policy and Government Finance" reflect the true picture of the economy at the time the said Report was published:

> *"At the turn of the year 2020, fiscal policy was focused on reviving a stagnant economy. However, with the economic fallout from the COVID-19 pandemic, the fiscal outcome deviated from expectations, as reflected in the decline of the government revenue and a rise in government recurrent expenditure, thereby widening the budget deficit and raising the outstanding central government debt. Heavy reliance on domestic sources in financing the budget deficit in 2020 reflected the impact of extremely challenging global market conditions that limited access to foreign financing, and the expressed preference of the Government to reduce the reliance on foreign financing.*
>
> *The Government implemented measures to lower the tax burden of businesses and individuals, thereby supporting the rebounding of economic activity and enhancing the income of people. Major tax revisions initiated since late 2019 included lowering the income tax rates and the Value Added Tax (VAT) rate, raising the VAT threshold, and abolishing the Nation Building Tax (NBT) and Economic Service Charge (ESC). These measures were expected to enable a strong rebound of economic activity in spite of their adverse impact on government revenue in the near term.*

The tax concessions introduced at the outset of the COVID-19 pandemic reinforced the fiscal stimulus measures implemented since late 2019, thereby minimizing the adverse impact of the pandemic on businesses and individuals in 2020. Further, small and medium scale enterprises (SMEs) were granted various tax relief measures in the form of waivers of income tax arrears, granting of a grace period to settle taxes in arrears/ default, extension on seizure notices and extended timelines for tax payments and filing tax returns.

Government revenue declined in 2020, both in nominal terms and as a percentage of GDP, reflecting the combined impact of subdued economic performance due to the COVID-19 pandemic, the tax revisions implemented from late 2019, and the tax concessions granted to businesses and individuals affected by the pandemic."

The first reference to the imposition of a surcharge tax had been made in the Budget Speech 2022 presented to Parliament in November 2021 when it was announced that:

a) *A one-time tax surcharge of 25 percent is proposed to be imposed on persons or companies with taxable income over Rupees 2,000 million for the year of assessment 2020/2021. Rupees 100 billion is expected to be earned through this tax.*

b) *VAT on banks and financial service providers under supply of financial services by specified institutions is proposed to be increased to 18 percent from 15 percent. Rupees 14 billion is expected to be earned through this tax.*

Prior to the said announcement, and during the course of the Budget Speech, the Minister of Finance had identified the economic situation that the Country is faced with in the following manner.

This Budget is presented at a time when the world is grappling with 5 major issues.... The fourth issue is that assistance from bi-lateral and multi-lateral institutions are severely limited as was never before in the history. This is mainly due to the developed countries also being beset with a number of internal issues *that they have given priority to resolve. The fifth issue is the challenge of adapting to the "new normal" that has emerged post the Corona pandemic. We are faced with the challenges that arises simultaneously from lockdowns, work from home, price increases, and disruption to global production networks. These conditions have had a varying impact on each country. The impact is worse on countries with trade focused economies, such as ours, compared to those economies dominated by the manufacturing sector.*

As a result, the loss of revenue to the country and the Treasury has been unlike any other year before. The loss to the Treasury according to our estimates is over Rs. 500 billion.

Our annual earnings from tourism amounting to almost USD 5 billion did not materialize during the last two years. Adequate foreign direct investments have not flowed into the country. The inflow of worker remittances have also been somewhat limited. Many avenues of earning revenue locally have also been affected. The gap between the export income and the import expenditure is not simply a national challenge during the past several decades, but it is an unsolved economic problem.

We acknowledge that public finances will be severely impacted with all sources of revenue contracting in the face of the Covid pandemic.

Government revenue reduced to 9.2 percent in 2020 owing to the impact of the Covid-19 pandemic. Despite the decline in the government revenue, government expenditure has increased. Government revenue has come to a level which is insufficient to cover the day-to-day recurrent expenditure. Therefore, deficit in the recurrent account, i.e. government revenue over recurrent expenditure, as a percentage of Gross Domestic Product has increased to 7.9 percent in 2020."

The learned Counsel for the Petitioner in SC (SD) No. 27/2022 has in fact submitted that, "*Sri Lanka is currently facing an unprecedented economic and financial crisis.*

Following the COVID-19 pandemic, Sri Lanka's foreign reserves have severely depleted in the wake of mounting foreign debt repayments, loss of foreign employment remittances and the lack of income from several sectors including tourism.

It is in the above circumstances that the learned Additional Solicitor General submitted that the policy rationale for the Bill is lucid, legitimate and clearly in the interests of meeting the just requirements of the general welfare of a democratic society.

The learned Additional Solicitor General handed over to this Court, a copy of the Cabinet Memorandum which (a) draws reference to the above Budget proposal *introduced to strengthen the fiscal position of the Country and help regain the economic activities that were affected by the Covid-19 pandemic,* and (b) outlines the salient features of the Bill. Approval to proceed with the Bill has been granted by the Cabinet of Ministers on 31st January 2022. The provisions of Article 152, which requires that a Bill for the imposition of any tax should have the approval of the Cabinet of Ministers has therefore been complied with.

Thus Parliament's constitutional role in exercising full control over public finance has been initiated and as is provided for in Article 148 of the Constitution:

> *"Parliament shall have full control over public finance. No tax, rate or any other levy shall be imposed by any local authority or any other public authority, except by or under the authority of a law passed by Parliament of any existing law."*

As has been authoritatively laid down in **S.C.S.D. Nos 3 & 4/2008 Appropriation Bill {Decisions of the Supreme Court on Parliamentary Bills (2007-2009) at page 45}** the Supreme Court has observed that under Article 148 of the Constitution, there are three vital components that constitute Parliament's "full control" over public finance, namely:

i) Control over the sources of finance i.e. imposition of taxes, levies, rates and the like and the creation of any debt of the Republic;

ii) Control by way of allocation of public finance to the respective departments and agencies of Government and setting of limits of such expenditure;

iii) Control by way of continuous audit and check as to due diligence in performance in relation to (i) and (ii) above.

It is in this backdrop of legislative authority to have full control over finance that legitimacy is given to the rationale in the classification sought to be attained by a taxation Bill and it is axiomatic that Article 12(1) of the Constitution postulates that equals must be treated equally and unequals cannot be treated equally-**Perera v Building Materials Corporation (2007) BLR 59 and Dayawathie and Others v Dr. M.Fernando and Others (1988) 1 Sri LR 371.** It is ingrained in Article 12 (1) of the Constitution that the State is allowed to classify persons or things for legitimate purposes.

In light of the foregoing, we would consider the grounds on which some core clauses of the Bill are sought to be impugned.

Chargeable Clauses

The principal clauses charging the aforesaid objects of taxation as described are found in Clause 2 (1) (a) and (b) of the impugned bill. It is their constitutionality that is put in issue by all Counsel who appeared for the Petitioners. Along with it there are other grounds of challenge such as retrospectivity of the Bill that have been raised before this Court. In this succinct matrix the chargeable clauses could now be evaluated for their inconsistency or otherwise with the Constitution.

Clause 2(1) of the Bill reads as follows:

"(1) There shall be levied, subject to the succeeding provisions of this Act, a tax to be called Surcharge Tax (hereinafter referred to as "the tax") from –

(a) *any individual, partnership or company, whose taxable income calculated in accordance with the provisions of the Inland Revenue Act, No. 24 of 2017, exceeds rupees two thousand million, for the year of assessment commenced on April 1, 2020, at the rate of twenty five per centum on the taxable income of such individual, partnership or company, for such year of assessment: Provided however, the income of a partner derived from a partnership shall not be taken into account when calculating the taxable income of such partner as an individual under this paragraph, if the tax has been paid by the partnership on such taxable income; and*

(b) *each company of a group of companies, of which the aggregate of the taxable income of all subsidiaries and the holding company in that group of companies, calculated in accordance with the provisions of the Inland Revenue Act, No. 24 of 2017, exceeds rupees two thousand million, for the year of assessment commenced on April 1, 2020, at the rate of twenty five per centum, on the taxable income of each such company after deducting the gains and profits from dividends received from a subsidiary which is part of such taxable income of each such company, for such year of assessment, notwithstanding that the taxable income of any one of such companies does not exceed rupees two thousand million."*

The learned Additional Solicitor General submitted that she has received instructions from the Ministry of Finance that the Minister of Finance will be moving to insert the following proviso, after Clause 2(1)(b), during the Committee Stage:

"Provided however, if a company is liable to pay the tax in terms of paragraph (b), such company shall not be liable to pay the tax in terms of paragraph (a)."

Upon a reading of the aforesaid clauses it is apparent that corporate entities are bifurcated into two categories-viz companies which are not in a group but had as a distinct entity arrived at the taxable income of more than Rupees 2 billion and companies in a group whose aggregate of taxable income of all subsidiaries and the holding company in the group had exceeded Rupees 2 billion.

Clauses 2 (1) (a) and (b) eventuate in the above taxation and Clause 2 (2) of the Bill is emphatic that in calculating the aggregate income of the group of companies charged with liability under Clause 2 (1) (b), a loss making subsidiary or any holding company is left out. The interpretation section-Clause 2(8) of the Bill seeks to assimilate the taxable income of a BOI company to its tax before profit whilst the expression "taxable income" in regard to individuals, partnerships and other companies will have the same meaning assigned to it under section 3 of the IRA, No. 24 of 2017.

As could be clearly seen from a reading of the impugned clauses a threshold of over Rupees two thousand million (more than Rupees 2 billion) in taxable income in Clause 2 (1) (a) or an aggregate of upees more than 2 billion for a group of companies in Clause 2 (1) (b) has been unambiguously laid down. While an individual, partnership, or a company which is not part of a group has been chosen as the objects or persons of taxation in clause 2(1)(a), companies in a group whose aggregate of taxable income exceeds more than Rupees 2 billion is chosen for surcharge in Clause 2(1)(b).

In fact the word "surcharge" is not defined in the Bill but etymologically, inter alia, 'surcharge' stands for an additional or extra charge or payment. 'Surcharge' is thus superadded charge, a charge over and above the usual dues. In fact in the Indian cases of ***D.C.M. vs Rajasthan State Electricity Board***, AIR

1986 SC 1126; *M/s Bisra Stone Lime Co. Ltd and Orissa Textile Mills Ltd. v. Orissa State Electricity Board*, 1976 (2) SCR 307 the judicial consensus was that a surcharge is in substance an addition to the stipulated rates of tariff. Though this is called Surcharge Tax Bill, what it seeks to levy is indeed a surtax. Black's Law dictionary (10th Edition, p1688) defines surtax to mean an additional tax imposed on something being taxed or on the primary tax itself. Therefore, we are disinclined to accept the argument that the word "surcharge" used in the Act is a misnomer. After all, what is in a name, a rose by whatever name you call it will smell as sweet. That is of course in the esthetic sense of describing a rose and not a tax which is always perceived to be obnoxious and burdensome.

Both the President's Counsel in S.C. (S.D.) No. 19 & 20/2022 and S.C.(S.D.) No. 26/2022 contended that the taxable threshold of Rupees two thousand million (Rs. 2 billion), is arbitrary and irrational because the tax rate of 25% will not apply to any person, company, or partnership earning a taxable income of up to Rupees 1,999.99 million.

They both contrasted the above two clauses of the Bill 2 (1) a) and 2 (1) b) vis-à-vis the tax rates in the First Schedule to the IRA, which imposes an incremental tax rate. The exclusion of individuals, partnerships and companies that posted taxable incomes of less than Rupees 2 billion is even described as astonishing in the written submissions filed on behalf of the Petitioner in S.C.(S.D.) No. 26/2022. This Court does not find the imposition of the threshold of more than Rupees 2 billion astonishing or unusual.

Undoubtedly the progressivity of the tax rates in the First Schedule to both IRA No. 24 of 2017 and IR (Amendment) Act No. 10 of 2021 were drawn in aid to support the argument that a tax free allowance of Rs. 2 billion leaves an individual, partnership or company posting a taxable income of Rs. 1,999.99 million, uncharged. We pause to make the observation for the moment that equality can exist only among equals and not unequals. A partition of Rs 2 billion as the threshold is bound to leave intact anyone below the threshold and provided that the legislature enjoys the competence in fiscal legislation to create thresholds and tax rates, the fact that somebody falls short of even one rupee below the threshold does not make the law invalid.

As Mr.F.N.Goonewardene the learned Counsel in SC.SD 29/2022 aptly described in his oral submissions, equity and taxation are strange bedfellows. It is at the border or threshold that taxation looks unfair but in effect taxation is on all or nothing. Either one pays tax above the threshold or he does not if he is below the threshold. When one crosses the Rubicon, the tax is irreversible and liability is fixed and certainly a difference of one Rupee makes the difference. Even a man who has earned just one Rupee more than the threshold is obligated to pay just as much the man who has earned one Rupee less than the threshold is not liable to pay. Fiscal legislation is rife with similar examples and the existence of such thresholds has not resulted in the invalidity of those enactments. Neither will it do, in our view, in the case of this Bill. The partition or border or threshold by whatever name you call it makes the two classes of citizens dissimilar and as is demonstrably made clear by the jurisprudence on tax legislation, the legislative act of fixing a rate or threshold does not make the law invalid. The two classes of citizens are dissimilar as some rise above the threshold and some fall below the threshold.

We hasten to point out at the outset that a comparison with rates of taxation that prevail for individuals is totally misplaced. As would be evident, the individuals, be it resident or non-resident, who are charged at different rates as their income rises, are dissimilarly situated from those who are sought to be charged by this Bill. We would like to state that those who are sought to be charged with surcharge by this Bill are dissimilar not only to those below the threshold of Rupees 2 billion but also to individuals who pay normal taxes under the IRA. They may look alike but they are not doppelgängers in taxation. Only likes can be likened to likes.

Now that the learned Counsel for the Petitioners attempted a comparison with the individuals who pay normal taxes under the IRA, it becomes apposite to analyze that argument.

Progressive Taxation for Individuals

This requires an explanation of the incremental rates of taxation that prevails for individuals as the learned President's Counsel in SC.SD 19/2022, SC.SD 20/2022, SC.SD 23/2022 and SC.SD 26/2022 in unison juxtaposed the proposed imposition of the surcharge by the impugned Bill vis-à-vis the progressive system (slab scheme) prevalent under the Inland Revenue (Amendment) Act No. 10 of 2021 for payment of taxes by resident and non-resident individuals. They drew the attention of Court to the progressive system of taxation that is reflected in the First Schedule to the Inland Revenue Act, No. 24 of 2017 (IRA, No. 24 of 2017), as amended by the Inland Revenue (Amendment) Act No. 10 of 2021 (IR (Amendment) No. 10 of 2021). Consequent to the passage of IR (Amendment) No. 10 of 2021, the tax rate leviable on resident and non-resident individuals on or after January 1, 2020 is reflected in the following table.

Inland Revenue (Amendment)
Act No. 10 of 2021

Taxable Income for a year of assessment	Tax Payable
Not exceeding Rs. 3 million	6% of the amount in excess of Rs. 0
Exceeding Rs. 3 million but not exceeding Rs. 6 million	Rs. 180,000 plus 12% of the amount in excess of Rs. 3 million
Exceeding Rs. 6 million	Rs. 540,000 plus 18% of the amount in excess of Rs. 6 million

Item No. 1 in the First Schedule to IRA No. 24 of 2017, as amended by IR (Amendment) Act No. 10 of 2021 could thus be seen to create only 3 different tax rates for resident and non-resident individuals. With the coming into effect of IR (Amendment) Act No. 10 of 2021, normal tax rates for individuals were changed from those tax rates that prevailed under IRA No. 24 of 2017. At a glance the normal tax rates for individuals, be they residents or non-residents, that prevailed prior to the amendment and thereafter, could be graphically differentiated as follows:

NORMAL TAX RATES – INDIVIDUALS

Prior to January 1, 2020	On or After January 1, 2020
1st - 600,000- 4%	1st - 3,000,000 - 6%
2nd – 600,000- 8%	2nd - 3,000,000 -12%
3rd – 600,000- 12%	On balance - 18%
4th – 600,000 -16%	
5th – 600,000 - 20%	
On balance - 24%	

Both the tax rates under the two regimes show in contrast the legislative choice of progressivity (as opposed to proportionality or regressivity) as the most appropriate means of achieving vertical equity in the income tax (i.e., of differentiating the tax burdens imposed on tax payers with unequal incomes). Since the above two tables under IRA No. 24 of 2017 and the IR (Amendment) Act No. 10 of 2021 show progressive taxation, we will take the tax rates imposed by the IR (Amendment) Act No. 10 of 2021 to illustrate the concept of progressive taxation. As Joel. S. Newman states in his *Federal Income Taxation: Cases, Problems, and Materials* 18-19 (3d ed. 2005): "Progressive" income tax is one in which the tax rates rise as the income rises.

As the tax rates which have come into effect on or after January 1, 2020 show, any taxable income over rupees 3 million is taxed at 12 per cent, whilst a man below this taxable income of rupees 3 million will be paying tax only at 6 percent. As the income rises high, so does the tax rate. In other words, the normal income tax is progressive in the sense that the rates are graduated, that is, the rates increase from 6 per cent to 18 per cent-for those who have a taxable income after having exhausted their tax free allowance and other reliefs allowed under the Act-vide Fifth Schedule to the IR Act, No 24 of 2017 entitled "Qualifying Payments and Reliefs". As is evident the incremental tax rates reach the top rate of 18 per cent which applies only to taxpayers with taxable incomes of more than rupees 6 million. Put in a nutshell, in progressive taxation the percentage goes up as the income rises. It is to the contrary in proportional taxes-the percentage does not change as the income goes up. In contrast, a "proportional" income tax "is one in which all taxpayers pay the same percentage of their income."

A regressive income tax is one in which "higher-income taxpayers", would pay a lower rate of tax than lower-income taxpayers. For example, to take individual A and B, B would pay less than A under a regressive income tax even though B may have ten times as much income as A. We do not encounter regressivity in this case, and therefore it is irrelevant for a discussion but relevant for purposes of differentiating between the three types of taxation. Be that as it may, the impugned Bill displays progressivity in that those above a particular threshold of taxable income are sought to be taxed with a surcharge whilst anyone below that threshold would not be so taxed, regardless of the amount of its taxable income. However, a noticeable difference emerges in the progressivity that we see in the taxes imposed on individuals, and the progressivity that this Court observes in the case of this Bill. There are multi-slabs of taxation in the case of individuals, whereas in the case of the Bill, just one threshold separates those who are liable to tax from those who are not liable to taxation.

As we said, the striking feature of progressivity under normal taxation is that a person who earns a higher taxable income above a particular threshold is taxed at a specified rate whilst the citizens below the specified rate does not get taxed at that rate. For example, in the progressive system specified in the First Schedule, there are 6 per cent, 12 per cent, and 18 per cent at which thresholds are set. Up to a point namely the taxable income which exceeds Rs. 6 million, there are taxable rates which are common to both high-income earners and low-income earners. In other words, the tax rates of 6 per cent and 12 per cent are common to both high-income earners and low-income earners who fall within that range. But when the taxable income rises to more than Rs 6 million, a tax rate of 18 per cent applies to all those individuals who have earned more than Rs. 6 million.

We can thus see that in progressive taxation the percentage becomes different when the taxable income goes up. But the learned President's Counsel in the S.C.(S.D.) 26/2022 sought to compare the above slab system with the threshold that is sought to be achieved in the impugned Bill and argued that the commonality of tax rates found in the slab system is totally absent from the Bill. In the Bill, there is only one threshold namely those who earn more than Rupees 2 billion and those below that threshold. The three slabs prevalent in the tax rates for individuals are completely different from the threshold which simply partitions those earning over Rupees 2 billion and those who secure a taxable income of less than Rupees 2 billion.

Therefore, the individuals on the progressive taxation (the slabs in the First Schedule) are not identical to those who are sought to be charged with surtax in this Bill. It is only likes who could be compared with likes. Incomparables cannot be compared as they are different as chalk and cheese. The individuals on the system of graduated tax rates found on the First Schedule to the Inland Revenue Act stand apart from the class of individuals, partnerships and companies who are sought to be taxed in this Bill.

It is only similarly situated tax payers who could be compared for discrimination and not those who are dissimilarly situated. The attempted comparison is flawed because one cannot look at only common features which happen to be the same up to some point on the progressive system and argue that they have to be transposed on this Bill for it to become valid or constitutional. Up to a point such as where the taxable income becomes Rs 3 million the taxable rate remains at 6% under the IRA. Between the range of Rs 3 million and Rs 6 million, a tax rate of 12% remains the same for those who fall within the range. These tax rates are certainly common for both low-income earners and those who earn higher income within the range, but this commonality does not make them alike nor could it be said that everything is equal between the two income tax payers. As the taxable income soars beyond Rs three million, the higher income earner is asked to pay the higher rate. The percentage becomes different as the income goes up. In the last slab which applies to those earning more than Rs 6 million, a heightened 18 per cent applies and it does not apply to those who rake in a taxable income below Rs 6 million. In the circumstances, even in the slab system that is available for individuals, one cannot find equality. In other words, the taxable income does not stop at Rs. 3 million or 6 million on the system of progressive taxation. What if the taxable income rises to Rs 100 million? Can it be said in such a situation that a person who earns a sum of Rs 3 million can be equated to a person whose income is Rs 100 million?

Therefore, it is crystal clear that in the case of individual taxpayers in the country, we deal with differently situated persons as item 1 to the First Schedule quite unambiguously shows. They are differently situated not only among themselves but they are also distinct and apart from those individuals, partnerships and entities who are sought to be taxed via this Bill. But both President's Counsel in S.C. (S.D.) No. 19 & 20/2022 and S.C.(S.D.) No. 26/2022 sought to transpose the above system of progressive taxation on the legislative scheme in the proposed bill which aims, in the view of this Court, at similarly situated persons who stands as a class because of the threshold of Rs 2 billion.

The sameness or similarity is brought about by the creation of an identical tax base for the individuals, partnerships and entities namely, a taxable income of more than Rupees 2 billion in the year of assessment commencing on April 1st 2020.

Upon a close scrutiny of Clauses 2(1)(a) and (b) of the Bill, it is clear that the following objects have been chosen for surcharge.

1. Any individual whose taxable income exceeded Rupees two thousand million (Rs. 2 billion) in the year of assessment 2020/2021.
2. Any partnership whose taxable income exceeded Rupees two thousand million (Rs. 2 billion) in the year of assessment 2020/2021.
3. A company which is not part of a group but had a taxable income of Rupees two thousand million (Rs.2 billion)
4. A group of companies whose aggregate of the taxable income of all subsidiaries and holding companies exceeded Rupees two thousand million (Rs.2 billion). The aggregate is arrived at by the computation of taxable income of all subsidiaries and the holding companies. No reference is made to the losses incurred by the companies of the group which are in the red.

Once the taxable income exceeds Rs 2 billion in the case of individuals, partnership and companies, they become liable to be charged at 25 per centum on their taxable income. The companies in this category are single economic units that are not part of a group. The companies in a group are dealt with in Clause 2 (1) (b) of the Bill and for purposes of liability it is the aggregate of the taxable income of subsidiaries and the holding company, that are taken into account in the computation of the threshold namely Rs. 2 billion. Once it is found that the taxable income of the group exceeded Rupees 2 billion, a flat rate of 25 per centum is imposed on the taxable income of each subsidiary and the holding company. It has to be remembered that in the computation of the aggregate of the taxable income of the group, loss making companies are left out. This provision clause 2 (1) (b) was attacked as unconstitutional and invalid.

We have already stated that the fact of fixing a threshold or tax rate does not make the tax law invalid. The legislative choice of companies in a group for taxation because of the economic superiority of the companies aggregated together would not offend Article 12 of the Constitution as authorities demonstrate. It was strenuously contended that the concept of group taxation is unknown to Sri Lanka and the notional selection of a group is arbitrary and unfair. Section 60 of the IR Act, No. 24 of 2017 was cited to this court as embodying the principle of separate legal personality echoing the everlasting values of the *Saloman principle.*

Several Counsel cried foul of what they called "targeting" of these companies who had appreciably done well because of the prudent management of these companies by their Boards of efficient directors in the seat. The budget speech made by the Minister in charge of the subject of finance was also called in aid as indicative of the so-called selective capture of these persons and entities within the tax net. It was also argued by Counsel all-round that, by way of this selective targeting, some companies face the risk of tax liability by virtue of the fact that 51% of the equity in those companies is held by a holding company. The Counsel in unison pointed out that the taxable income of a company in a group runs the risk of being taxed at 25% regardless of the size of the taxable income merely because such a subsidiary belongs to a group.

Some counsel went to the extent of classifying the process of aggregation of taxable incomes of all the companies in a group as veil lifting. All these arguments coalesce into one strand of incompatibility with Article 12 of the Constitution. Mr. Romesh De Silva PC who called the surcharge as a masquerade for a tax also challenged the proposed legislation on the ground of inconsistency with Art.13 (6) of the Constitution which prescribes the prohibition against retroactive legislation to penalize acts or omissions that did not constitute an offence at the time of the act or omission. There was also the argument proffered that the surcharge was a penalty.

In the circumstances, the question before this Court is whether this Bill falls foul of Articles 12, 13, and 14 of the Constitution. The majority of Counsel argued that the infringement of these constitutional provisions renders the proposed imposition of the surcharge offensive of Art.4 (d) of the Constitution and as such, the infringement of Art.4 will result in inconsistency with Art.3 leading to the imperative requirement of this Bill to be passed by a special majority of Parliament, and later approved at a referendum.

A determination of the Supreme Court on the **Special Goods and Service Tax Bill,** S.C (S.D.) 01 - 09/2022 was put forward for the proposition that the infringement of these fundamental rights will result in the Bill requiring the imprimatur of a 2/3rds majority and a referendum. The question arises therefore, whether the Bill or any provision thereof is inconsistent with the Constitution and if so, which provisions of the Constitution. This Court will now proceed to assay the provisions of this impugned Bill vis-a-vis the Constitutional provisions in question.

<u>Article 12</u>

Article 12 (1) and (2) of the Constitution go as follows:

(1) All persons are equal before the law and are entitled to the equal protection of the law.

(2) No citizen shall be discriminated against on the grounds of race, religion, language, caste, sex, political opinion, place of birth or any one of such grounds:

As we have said before, the selection of the four categories of individuals and entities who are liable to pay has been called into question as discriminatory and unfair. But it has to be remembered that the legislature need not tax everyone in order to tax someone. As the Supreme Court of India has aptly observed "It is well settled that a statute does not have to tax everything in order to tax something. It is allowed to pick and choose districts, objects, persons, methods and even tax rates for taxation if it acts reasonably" per Hedge J in **S.K. Dutta v Lawrence I.T.R** (1968) 68 ITR 272.

These core principles in regard to fiscal legislation have been repeatedly emphasized in Sri Lankan jurisprudence. Before we turn to the Sri Lankan cases, an excursus on these principles vis-a-vis Art.12 of the Constitution demands consideration.

Though taxing laws are not outside Article 12, however, having regard to the wide variety of diverse economic criteria that go into the formulation of a fiscal policy, the legislature enjoys a wide latitude in the matter of selection of persons, subject-matter, events, etc., for taxation. The tests of the vice of discrimination in a taxing law are, accordingly, less rigorous. In examining the allegations of a hostile, discriminatory treatment, what is looked into is not its phraseology, but the real effect of its provisions. If there is equality and uniformity within each group, the law would not be discriminatory.

We observe that the previous determinations of this court on the matter have permitted the legislatures to exercise an extremely wide discretion in classifying items for tax purposes, so long as it refrains from clear and hostile discrimination against particular persons or classes. But, with all this latitude, certain irreducible desiderata of equality shall govern classifications for differential treatment in taxation laws as well. The classification must be rational and based on some qualities and characteristics which are to be found in all the persons grouped together and absent in the others left out of the class. But this alone is not sufficient. Differentia must have a rational nexus with the object sought to be achieved by the law.

The State, in the exercise of its Governmental power, has, of necessity, to make laws operating differently in relation to different groups or class of persons to attain certain ends and must, therefore, possess the power to distinguish and classify persons or things. It is also recognized that no precise or set formulae or doctrinaire tests or precise scientific principles of exclusion or inclusion are to be applied. The test could only be one of palpable arbitrariness applied in the context of the felt needs of the times and societal exigencies informed by experience. The pressing needs of the time have already been brought home to this Court by reference to the speech of the Minister of Finance. In fact the learned President's Counsel Mr.Uditha Egalahewa adverted to the case of ***Pepper v Hart*** (1992) 3 WLR 1032; (1993) 1 All ER 42 and invited this Court to infer the selective targeting of 62 companies attempted by this proposed Bill. Undoubtedly the House of Lords in 1992 by a 6:1 decision decided to allow references to be made to Hansard in limited circumstances. Reference to Parliamentary materials would be allowed where:

i) legislation is ambiguous or obscure or leads to absurdity;

ii) the material relied upon consists of one or more statements by Minister or of the promoter of the Bill, together if necessary with such other Parliamentary material as is necessary to understand such statements and their effect;

iii) the statements relied upon are clear;

The statement of Lord Bridge is worth noting at page 1039H, WLR.

> *It should be only be permitted in rare cases where the very issue of interpretation which the courts are called on to resolve has been addressed in Parliament debate and where the promoter of the legislation has made a clear statement directed at that very issue that reference to Hansard should permitted.*

In *Pepper v. Hart* (supra) the House of Lords was not dealing with a speech made by a Minister on an appropriation bill but rather it was a provision in a law that came up for interpretation. The statement sought to be relied upon was in the introduction of the bill and in such a situation there is no such convergence between the appropriation bill and this bill which has just been placed on the order paper. Assuming without conceding that ***Pepper v. Hart*** applies to this situation, and the invitation by counsel is for the purpose of gathering the purpose for which this bill has been introduced, it is crystal clear that the pressing need for the legislation in order to meet the economic needs of the country has been amply articulated in the Hansard materials.

Erskine May in his tome *Parliamentary Practice* refers to the fundamental rules of financial procedure which reserve the right of initiative to the Crown and require that new charging proposals be authorized by resolution of the House apply to the business of **Ways and Means ('charges upon the people')** as they do to proposals for new expenditure ('charges upon the public revenue'). So the Ways and Means as Erskine May points out, are based largely on the established practice of the House and it can be moved only by a Minister and, once moved, it has the same limiting effect upon amendments relating to taxation as a Money resolution recommended by the Crown has upon amendments relating to expenditure, whether such amendments are offered by private Members or by Ministers.

So we would conclude that the speech on appropriation bill sets out the ways and means of raising revenue and it serves notice to the public on whom the charge is sought to be made and how the revenue is sought to be raised with a view to meeting the pressing needs of revenue. That practice sanctioned by Parliamentary convention may indicate targeting as counsel put it but law has it, as we discussed, that the State enjoys the democratic legitimacy under Article 148 of the Constitution to cherry pick its objects of taxation.

Some other Indian cases also lend credence to the concept of democratic legitimacy.

In the Indian case of ***Jaipur Hosiery Mills (P.) Ltd. v. State of Rajasthan*** [1970] 2 SCC 27 ; [1970] 26 STC 341 (SC), a notification under the Rajasthan Sales Tax Act, 1950, exempting from tax the sale of garments which did not exceed Rs. 4 per piece was assailed. The court found the classification permissible. It was held (at p. 343 of 26 STC)

> "*. . . it has to be borne in mind that in matters of taxation, the Legislature possesses a large freedom in the matter of classification. Thus wide discretion can be exercised in selecting persons or objects which will be taxed and the statute is not open to attack on the mere ground that it taxes some persons or objects and not others. It is only when within the range of its selection the law operates unequally and cannot be justified on the basis of a valid classification that there would be a violation of article 14.*

In ***State of Gujarat v. Shri Ambica Mills Ltd.*** [1974] 3 SCR 760 , 784 ; AIR 1974 SC 1300 , 1314, Mathew J. said

> "*Statutes are directed to less than universal situations. Law reflects distinctions that exist in fact or at least appear to exist in the judgment of legislators those who have the responsibility for making law fit fact. Legislation is essentially empiric. It addresses itself to the more or less*

outside world and not to the neat, logical models of the mind. Classification is inherent in legislation. To recognize marked differences that exist in fact is living law ; to disregard practical differences and concentrate on some abstract identities is lifeless logic."

"In the utilities, tax and economic regulation cases, there are good reasons for judicial self-restraint if not judicial deference to legislative judgment. The Legislature, after all, has the affirmative responsibility. The courts have only the power to destroy, not to reconstruct. When these are added to the complexity of economic regulation, the uncertainty, tile liability to error, the bewildering conflict of the experts, and the number of times the judges have been overruled by events-self-limitation can be seen to be the path to judicial wisdom and institutional prestige and stability."

In ***G. K. Krishnan v. State of Tamil Nadu*** [1975] AIR 1975 SC 583 [1975] 2 SCR 715 , 729, Mathew J. referred to the following observations of the Supreme Court of U. S. A. in ***San Antonio School District v. Rodrigues*** [1973] 411 US I (at p. 592 of AIR 1975 SC)

"Thus we stand on familiar ground when we continue to acknowledge that the Justices of this court lack both the expertise and the familiarity with local problems so necessary to the making of wise decisions with respect to the raising and disposition of public revenues. Yet, we are urged to direct the States either to alter drastically the present system or to throw out the property tax altogether in favour of some other form of taxation. No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods and services, has yet been devised which is free of all discriminatory impact. In such a complex arena in which no perfect alternatives exist, the court does well not to impose too rigorous standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection Clause."

In *ITO v. N. Takin Roy Rymbai* [1976] 103 ITR 82 , 89 (SC) [1976] 3 SCR 413 it was held:

> "*Given legislative competence, the Legislature has ample freedom to select and classify persons, districts, goods, properties, incomes and objects which it would tax, and which it would not tax. So long as the classification made within this wide and flexible range by a taxing statute does not transgress the fundamental principles underlying the doctrine of equality, it is not vulnerable on the ground of discrimination merely because it taxes or exempts from tax some incomes or objects and not others. Nor the mere fact that tax falls more heavily on some in the same category, is by itself ground to render the law invalid. It is only when within the range of its selection, the law operates unequally and cannot be justified on the basis of a valid classification, that there would be a violation of Article 14.*"

We would venture to state that the dicta in all these cases re-iterate the legislative competence to select objects for taxation, and rates pertinent to the thresholds and as we would presently see, several determinations of our Supreme Court have succinctly echoed these principles

Concept of Group in Clause 2 (1) (b)

It was pointed out by several counsel that in terms of section 60(1) of the IRA, No 24 of 2017 a Company is treated as a separate entity for purposes of taxation and therefore the notion of a group taxation is alien in Sri Lanka. It has to be remembered that a group is not sought to be charged with surcharge by this Bill. It is only the aggregate of a group that is looked at for the purpose of ascertaining the liability of each company. A group is only used to find out whether a Company in the group is liable for taxation. Once the aggregate of the taxable income works up to Rupees more than 2 billion, the taxable income of each company is charged at a flat rate of 25 per centum. When each company in the group is taxed separately at 25 per centum of its taxable income after having identified the taxable income of the holding company at more than rupees 2 billion, section 60 is fully complied with and there is no subversion of the doctrine of separate legal personality nor does any veil lifting take place.

Another argument that was raised is that in the computation of the aggregate the loss making companies are left out. The argument was that it is unfair not to take into account the minuses. It is unambiguously settled that the legislature can pick and choose objects of taxation. If it is a policy decision not to take into account loss making companies which do not have plusses, this Court is incompetent to call in question such a policy decision. Even the IRA is rife with provisions which do not take into account losses in certain circumstances. For instance section 19 of the IRA, No 24 of 2017 makes it clear that unrelieved losses cannot be carried over for more than 6 years. Even certain expenses are not allowed under the legislation. Section 10 (b) (ii) of the IRA, No 24 of 2017 makes it clear that tax payable under the Act cannot be deducted in calculating a person's income. The concept of allowable and disallowable expenses pervades the IRA and therefore the exclusion of loss making companies in a group cannot be condemned as unconstitutional. In the circumstances it cannot be argued that the exclusion of loss making companies in the computation of the taxable income is unfair.

In the present case, the bases of classification cannot be said to be arbitrary or unintelligible nor as being without a rational nexus with the object of the law. Apart from the impugnment of the Bill, on the taint of retrospectivity to which we will advert presently, a class of individuals and entities, whose taxable income exceeded more than Rupees two billion in the specified year of assessment is, in the legislative wisdom, a class apart by virtue of the economic superiority of those who compose the class. This legislative assumption cannot be assailed as irrational. Taxable turnover of more than Rupees two billion, whether it arose out of the fruits of labour and business activity of the individual, partnership, companies in the group or companies outside the group constitutes the intelligible differentia that distinguishes this class from the others. It is equally well recognized that judicial veto is to be exercised only in cases that leave no room for reasonable doubt. Constitutionality is presumed. The words of James Bradley Thayer may be recalled:

> *"This rule recognizes that, having regard to the great, complex ever-unfolding exigencies of government, much which will seem unconstitutional to one man, or body of men, may reasonably not seem so to another ; that the Constitution often admits of different interpretations ; that there is often a range of choice and judgment ; that in such cases the Constitution does not impose upon the Legislature any one specific opinion, but leaves open this range of choice ; and that whatever choice is rational is Constitutional.* " (emphasis supplied)

[***Supreme Court Statecraft; The Rule of Law and Men Wallace Mendelson :*** p. 41]

Thayer also referred to the words of a Chief Justice of Pennsylvania way back in 1811.

> *"For weighty reasons, it has been assumed as a principle in constitutional construction by the Supreme Court of the United States, by this Court, and every other court of reputation in the United States, that an Act of the legislature is not to be declared void unless the violation of the constitution is so manifest as to leave no room for reasonable doubt."*

In ***Secretary of Agriculture v. Central Roig Refining Co.*** [1949] 338 I.T. s. 604, the Supreme Court of USA said

> "... *This court is not a Tribunal for relief for crudities and inequities of complicated experimental economic legislation....*"

In **Hoechst Pharmaceuticals Ltd. v. State of Bihar** [1985] 154 ITR 64 (SC) ; AIR 1983 SC 1019 , 1046, it was observed

"On questions of economic regulations and related matters, the court must defer to the legislative judgment. When the power to tax exists, the extent of the burden is a matter for the discretion of the law-makers. It is not the function of the court to consider the propriety or justness of the tax, or to enter upon the realm of the legislative policy. If the evident intent and general operation of the tax legislation is to adjust the burden with fair and reasonable degree of equality, the constitutional requirement is satisfied."

There is a slew of Sri Lankan cases that fortify our conclusions.

Sri Lankan cases

Most of our determinations involved the question whether the proposed legislation violated the principle embodied in Article 12 (1) of the Constitution that "all persons are equal before the law and are entitled to the equal protection of the law". The Supreme Court has applied the principle of "classification" in such cases. For example, one of the matters that arose in the case relating to the ***Finance Bill*** **S.C (S.D)** No. 28/2004 was whether diplomats may be legitimately exempted from the tax sought to be imposed by that Bill on every person using a cellular mobile telephone. In making an affirmative determination, the Supreme Court noted that although "by the special consideration given by excepting them from the payment of tax referred to in Clause 14, a special category has been formed, such group has been recognized on an intelligible differentia which distinguishes the persons that are grouped together as they come within the Diplomatic Privileges Act No. 9 of 1966."

In the same case the question also arose as to whether an amendment to Section 11 of the Finance Act No. 25 of 2003 intended to exclude General Sales Agents licenced under the Tourist Development Act. No. 14 of 1968 as Travel Agents from the levy of one per centum on the turnover of every institution licenced under the Tourist Development Act violated the equality provision of the Constitution. The Supreme Court decided in the negative and observed –

> *"It is well settled law that equal protection of the laws is an injunction issued by the framers to the legislature against enactment of laws, which are discriminatory. However, this does not mean that all enactments should be universal in their application. The State has the power in making distinctions and classification of individuals, persons or things for the mere purpose of legislation thereby accepting the principle that every differentiation is not discrimination; However, such classification cannot be arbitrary and should only be based on intelligible criteria having a reasonable nexus to the object of the legislation."*

Having made reference to Article 15 (7) of the Constitution which specifically provides that certain provisions of the Constitution including Article 12 shall be subject to such restrictions as may be prescribed by law in the interest of *inter alia* "the just requirements of the general welfare of a democratic society", the Court went on to hold that

> *"The proposed amended is to relieve the General Sales Agents licensed under the Tourist Development Act, No. 14 of 1968 as a Travel Agent from the Tourism Development Levy. This is a category, which directly deals with the tourism development and the object being the general development of such industry, there is reasonableness we well as intelligible differentia in having such kind of a group to be treated differently. Furthermore, this too, relates to fiscal legislation which as pointed out earlier is a matter for the Legislature to decide."*

As pointed out by the Constitutional Court in the course of its determination in the case of the Finance (Amendment Bill, (1978) 5 Decisions of the Constitutional Court of Sri Lanka page 1 –

> *"In taxation matters even more than in other fields, it is well established that the legislature has the greatest freedom in classification. In deciding whether a taxing law is discriminatory or not it is necessary to bear in*

mind that the State has a wide discretion in selecting the persons or objects it will tax and that a stature is not open to attack on the ground that it taxes some persons or objects and not others. It is only when within the range of its selection the law operates unequally that it cannot be justified on the basis of any valid classification."

In fact in a determination of the Supreme Court in relation to the *Inland Revenue* (Amendment) Bill S.C. No. 27/2004, the Supreme Court concluded that –

> *"It is clear from the observations made consistently by the Constitutional Court and this Court that in revenue matters, in making classifications for the purpose of granting concessions or imposing liability there is a wide discretion. These measures are taken not only to raise resources necessary for the State but also to direct economic activity projected to the general welfare of the society. Such measures would be considered as inconsistent with Article 12 of the Constitution only if they are manifestly unreasonable or discriminatory."*

The reasoning in this case has been consistently followed in Sri Lanka. In fact the Supreme Court in the determination involving the Value Added Tax (Amendment) Bill S.C. (S.D) No.29/2004 has observed as follows :-

> *"It is settled law that law dealing with tax matters and otherwise valid, creates no unreasonable restriction and would even be retrospective. Such retrospective taxation cannot be regarded as unreasonable. The general notion is that the Legislature is empowered to enact laws, which could be applicable with retrospective effect. (Government of Andra Pradesh v H.M.J [1975] SC 2037). This would include the tax laws (Jawahaumal V State of Rajasthan 1966) SC 764) and retrospective taxation cannot be regarded as unreasonable unless it is clearly prohibitive. More importantly, Parliament is empowered to enact laws having retrospective effect.*

So in effect we conclude that clauses 2 (1) (a) and (b) are not affected by any taint of unconstitutionality and these clauses do not infringe any of the provisions of the Constitution, in particular Article 12 of the Constitution.

Retrospection

The argument of a retrospective legislation that imposes penal consequences was put forward as a frontal impugnment of the Bill. The learned President's Counsel for the Petitioner in SC/SD/21/2022 contended that the Bill entails a retrospective effect in that it creates an offence that did not exist in the year of assessment in which the taxable income was earned and as such the Bill is offensive of Article 13 (6) of the Constitution. Mr.Romesh de Silva, PC drew in aid the decision of the Privy Council in ***Liyanage and Others v The Queen*** 68 N.L.R 265 where the enactment of laws that would amount to legislative judgments was considered. The Privy Council went on to hold in the case that under the Soulbury Constitution, such legislative judgments would be violative of the separation of the judicial power and therefore unconstitutional. But it has to be observed that the Supreme Court in ***Queen v Liyanage*** (1963) 65 N.L.R 74 at 82-84 held that the Parliament of Ceylon had the power to enact retroactive legislation and the court were bound to enforce such legislation. In fact it was while affirming the power of Parliament to pass retrospective legislation that the Privy Council held in ***Liyanage v The Queen*** (supra) that the legislation in question namely the Criminal Law (Special Provisions) Act 5 of 1962, as amended by Act No. 31 of the same year would be invalid if it was directed against particular individuals. It is worth mentioning that the impugned Acts were attacked before the Supreme Court on the basis that the Parliament of Ceylon could not pass *ex post facto* laws. This was unacceptable to the Court. Neither did the Privy Council think it fit to hold otherwise. The Parliament could pass a law not only with retrospective effect, it could also pass ad hoc or ad hominem laws, the Privy Council observed-(1965) 68 N.L.R. 265 at p. 284; (1966) 1 All E.R. 650, at p. 659. Though the Supreme Court and the Privy Council both did not disavow the competence of Parliament to pass ex post facto laws, the Privy Council ventured to put forward a principle which prohibited what was termed *'legislative judgments'.*

The words of Chase., J in the US case of ***Calder v Bull*** (1789) 3 Dallas U.S.C.C 386 gave vent to the expression legislative judgments. We have to say that the provisions of this Bill are not of the same force and effect as the two impugned Acts in that case regarding which the Privy Council said at page 284:

> *"The pith and substance of both Acts was a legislative plan ex post facto to secure the conviction and enhance the punishment of particular individuals. It legalised their imprisonment while they were awaiting trial. It made admissible their statements obtained during that period. It altered the fundamental law of evidence so as to facilitate their conviction and finally it altered ex post facto the punishment to be imposed on them"*

No such legislative judgment has been pronounced in the Bill and much water has flowed down under the bridge since the Liyanage case and the legislative competence to enact retrospective legislation is clearly entrenched in article 75 of the Constitution and the question of retrospection has itself received consideration in the Supreme Court of this country.

The question as to whether tax liability may be imposed with retrospective effect was raised in the case relating to the ***Finance Amendment Bill*** (1978) vol.(vi) Decisions of the Constitutional Court of Sri Lanka p 1 in the context of a Bill to amend Section 120 of the Finance Act No. 11 of 1963, which imposed a liability to pay BTT from 1st January 1964. The business of export of any manufactured or processed article including gems was exempted from the payment of the tax under Section 120 (3) of the Act. By the Bill that was considered by the Constitutional Court in this case it was proposed to remove the exemption in respect of the export of gems with effect from 1st January 1976. The Bill was objected to on the ground that this violated the equality clause of the Constitution. The Court observed as follows –

> *"The fact that some persons in the class are being taxed on transaction which have already been completed whilst they and the others will also be taxed on transactions in the future does not in our view affect the basis of the classification.*
>
> *It is well recognized that taxes cant be imposed with retrospective effect. In the instant case, these clauses select a class, namely, all exporters who had exported gems during the relevant past period, for the imposition of the tax retrospectively. It does not discriminate between the member of this class. The law applies to all of them equally and does not operate unequally amongst them. The fact that future exporters, into which the aforementioned class, namely, exporters who had exported gems during the relevant past period may or may not fall, can pass on the tax on the purchaser, in no way affects this classification as this fact does not make the clauses apply unequally between members of the selected class."*

On a parity of reasoning though this bill was attacked on the ground of prohibition against retrospective criminal law contained in Article 13 (6) of the Constitution, we take the view that this legislation is not retrospective at all, even if one assumes without conceding that this Bill creates retrospective liability. The above determination will absolve the Bill even if it is retrospective. Merely because the tax base has been taken to be a past event namely the taxable income in the year of assessment 2020/2021 it does not make the law a retrospective criminal law. The tax to be paid itself is prospective and it becomes payable in 2 installments on future dates. The failure to pay this tax in the past year has not been made an offence and the liability to pay is in the future. In the circumstances we take the view that Article 13 (6) is not engaged. The IR legislation in the country has been rife with cases where the tax base has been taken from a past event. For instance, in the case of capital gains brought in by the IRA Act, No 24 of 2017 the tax base may originate from a transaction in the past.

On an overall consideration of the provisions of the Bill, we arrive at the conclusion that neither the Bill nor any of its provision is inconsistent with Article 12 or Article 13 or any provisions of the Constitution. In the circumstances this bill can be validly passed by a simple majority of the legislature.

In conclusion, we wish to place on record our deep appreciation of the assistance rendered by the learned Additional Solicitor General and the learned Counsel for the Petitioners.

Buwaneka Aluwihare PC
Judge of the Supreme Court

A. H. M. D. Nawaz
Judge of the Supreme Court

Arjuna Obeyesekere
Judge of the Supreme Court