

**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 questions 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).

**CA (Tax) No.56/2023,  
TAC Appeal No.TAC/VAT/32/2021  
CA (Tax) No. 90/2023  
TAC Appeal No.TAC/VAT/14/2019  
CA (Tax) No.91/2023,  
TAC Appeal No.TAC/VAT/007/2020  
CA (Tax) No. 97/2023,  
TAC Appeal No.TAC/VAT/004/2018**

Bank of Ceylon,  
Bank of Ceylon Square,  
No. 01, Bank of Ceylon Mawatha,  
Colombo 01.

**Appellant**

**Vs.**

The Commissioner General of Inland  
Revenue,  
14<sup>th</sup> Floor, Secretarial Branch,  
Department of Inland Revenue,  
Sir Chittampalam A. Gardiner Mawatha,  
Colombo 02.

**Respondent**

**Before: M.C.B.S. Morais J.**

**&**

**Annalingam Premashanker J.**

**Counsel:** Suren Fernando with K.Wikramanayake and Shiloma David for the Appellant.

Manohara Jayasinghe, DSG for the Respondent.

**Written Submissions:** By the Appellant – on 28.08.2025

By the Respondent – on 27.08.2025

**Argued on:** 16.06.2025

**Decided On:** 23.10.2025

### **Judgment**

**M.C.B.S. Morais J.**

This is an appeal by way of a case stated against the determination of the Tax Appeals Commission dated 19<sup>th</sup> of June 2023 in the case of CA/TAX/56/2023, determination dated 17<sup>th</sup> of July 2023 in the case of CA/TAX/90/2023, determination dated 17<sup>th</sup> of July 2023 in the case of CA/TAX/91/2023 and determination dated 19<sup>th</sup> June 2023 in the case of CA/TAX/97/2023.

This appeal is filed under and in terms of section 11A of the Tax Appeals Commission Act No. 23 of 2011 (as amended). Since the matters CA/TAX/56/2023, CA/TAX/90/2023, CA/TAX/91/2023, and CA/TAX/97/2023 primarily deal with the same substantial issue of Value Added Tax (VAT) on Financial Services (FS), these cases are addressed together. Even though, the observation is mainly based on case No. CA (Tax) No.56/2023, the matters in relation to the remaining cases has also been addressed under the question of law raised. If the parties wish to pursue the remaining questions of law undecided, they could do so separately under those cases.

The taxable period for the value addition on Financial Services is from 1<sup>st</sup> of January 2016 to 31<sup>st</sup> of December 2016.

### **Factual Background**

The Bank of Ceylon (sometimes will be referred to as the Appellant) is established under and in terms of the Bank of Ceylon Ordinance No. 53 of 1938 (as amended). The Appellant is challenging the determination of the Tax Appeals Commission (hereinafter will be referred to as TAC) dated 19<sup>th</sup> of June 2023 by the Commissioner General of Inland Revenue (hereinafter sometimes will be referred to as the CGIR/ Respondent) in case No. TAC/VAT/032/2021. The total Tax in Dispute is an amount of Rs.424,062,870.00 and a penalty of Rs.222,074,132.00.

The Appellant Company has filed the returns for VAT for the taxable period 1<sup>st</sup> of January 2016 to 31<sup>st</sup> of December 2016, which was rejected by the Deputy Commissioner, and an intimation letter dated 22<sup>nd</sup> of May 2019 was issued stating the reasons for refusal. Being aggrieved by the said assessment, the Appellant Company has made an appeal to the Respondent. After hearing the appeal, the Respondent has made a determination dated 11<sup>th</sup> of June 2021 confirming the assessment of the Deputy Commissioner. Being aggrieved by the said determination, the Appellant Company has preferred an appeal to the TAC.

The main issue arises from the loan provided by the Appellant to its employees on a concessionary rate which is less than the market rate. However, the Respondent has considered the market rate of those loans, which is higher than the concessionary rate provided by the Appellant in determining the VAT of the Appellant for the period mentioned above.

### **Appeal to Tax Appeals Commission**

After considering the written submissions filed by both parties, the TAC has made a determination dated 19<sup>th</sup> of June 2023 by dismissing the appeal. Accordingly the Tax Appeals Commission determined as follows.

*“A. Emoluments payable to all employees in terms of Section 25C of the VAT Act should be the emoluments payable not only the amount payable in cash but the gross emoluments payable in cash and all other benefit as well, hence, the amortization of staff interest is correct as it is within the emoluments.*

*B. The gains from the sale of shares of Miraka Investment should be liable to VAT on FS”*

### **Appeal to the Court of Appeal & Questions of Law**

Being aggrieved by the determination of the TAC, the Appellant has appealed to the Court of Appeal, to have the case stated for the opinion of the Court. Accordingly, the following question of law has been raised by the Appellant;

#### **CA (Tax) No.56/2023**

*“1. Did the Assessor, the Commissioner - General, and the Tax Appeals Commission, err in law by failing to understand and properly apply the concept of "value addition" in computing the VAT liability on the supply of financial services?*

*2. Did the Assessor, the Commissioner Appeals Commission, err in law by failing to recognize that;*

*a. Section 25C (1) of the Value Added Tax Act applies only to transaction which result in value addition?*

*b. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of the grant of loans to employees, does not create a value addition equivalent to amounts reflected in such notional accounting entries?*

*c. There was no "value addition" as claimed by the Assessor by the grant of loans to employees?*

*d. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, had no impact on the profit of the Bank, in as much as inter alia the Bank only received interest based on the actual interest rate at which the loans were granted?*

*3. Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that:*

*a) Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*

*b) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be considered or deemed to be an "emolument" for the purpose of VAT?*

*c) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be deemed to be an emolument paid and / or payable to the employee?*

*4. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by:*

*a. Failing to appreciate that Appellant's primary function of being engaged in the "Banking Business" did not apply to the sale of shares (of Mireka Capital Land (Pvt) Limited), which was a distinct and isolated transaction?*

*b. Failing to recognize that the sale of the shares of Mireka Capital Land (Pvt) Limited was not performed in pursuit of providing financial services?*

*c. Failing to recognize that (in the case of the Mireka Capital Land (Pvt) Limited transaction) the mere transfer of equity will not make such transaction liable to VAT on financial service?*

*5. Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) contrary to law?*

*6. In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err in law in arriving at the conclusions set out in its Determination?"*

### **CA (Tax) No.90/2023**

*"1. Did the Tax Appeals Commissioner err in law by failing to recognize that the Inland Revenue Officer assigned to hear the Appeal (to the Commissioner-General) on the 21 February 2019 did not have the power to hear the Appeal?*

*2. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to understand and properly apply the concept of "value addition" in computing the VAT liability on the supply of financial services?*

*3. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to recognize that;*

*a. Section 25C (1) of the Value Added Tax Act applies only to transaction which result in value addition?*

*b. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of the grant of loans to employees, does not create a value addition equivalent to amounts reflected in such notional accounting entries?*

*c. There was no "value addition" as claimed by the Assessor by the grant of loans to employees?*

*d. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, had no impact on the profit of the Bank, in as much as inter alia the Bank only received interest based on the actual interest rate at which the loans were granted?*

*4. Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that;*

*a) Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*

*b) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be considered or deemed to be an "emolument" for the purpose of VAT?*

*c) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be deemed to be an emolument paid and/or payable to the employee?*

*5. Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) contrary to law?*

*6. In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err in law in arriving at the conclusions set out in its Determination?"*

## **CA (Tax) No.91/2023**

*"1. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to understand and properly apply the concept of "value addition" in computing the VAT liability on the supply of financial services?*

*2. Did the Assessor, the Commissioner Appeals Commission, err in law by failing to recognize that;*

*a. Section 25C (1) of the Value Added Tax Act applies only to transactions which result in value addition?*

*b. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of the grant of loans to employees, does not create a value addition equivalent to amounts reflected in such notional accounting entries?*

*c. There was no "value addition" as claimed by the Assessor by the grant of loans to employees?*

*d. Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, had no impact on the profit of the Bank, in as much as inter alia the Bank only received interest based on the actual interest rate at which the loans were granted?*

*3. Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that;*

*a) Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*

*b) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be considered or deemed to be an emolument for the purpose of VAT?*

*c) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be deemed to be an emolument paid and / or payable to the employee?*

*4. Has the Commissioner General, and the Tax Appeals Commission erred in law in failing to recognize that and/or failing to consider the evidence produced demonstrating that expenses for tours abroad for board members and staff constitute business expenses and do not constitute an employment benefit?*

*5. Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) contrary to law?*

*6. In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err in law in arriving at the conclusions set out in its Determination?"*

### **CA (Tax) No.97/2023**

*“1. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to understand and properly apply the concept of "value addition" in computing the VAT liability on the supply of financial services?*

*2. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to recognize that;*

*(a) Section 25C (1) of the Value Added Tax applies only to transactions which result in value addition?*

*(b) Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of the grant of loans to employees, does not create a value addition equivalent to amounts reflected in such notional accounting entries?*

*(c) There was no "value addition" as claimed by the Assessor by the grant of loans to employees?*

*(d) Notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, had no impact on the profit of the Bank, in as much as inter alia the Bank only received interest based on the actual interest rate at which the loans were granted?*

*3. Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that;*

*(a) Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*

*(b) Notional interest based on notional accounting entries (recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be considered or deemed to be an "emolument" for the purpose of VAT?.*

*(c) Notional interest based on notional accounting entries ((recorded for the purpose of Sri Lanka Accounting Standards) in respect of loans granted to staff, cannot be deemed to be an emolument paid and/or payable to the employee?*

*4. Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) Contrary to law?*

*5. In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err, in law in arriving at the conclusions set out in its Determination?"*

Accordingly, the court shall deal with the following questions of law, which would basically cover all the question of law raised.

*"1. Did the Assessor, the Commissioner General, and the Tax Appeals Commission, err in law by failing to understand and properly apply the concept of "value addition" in computing the VAT liability on the supply of financial services?*



- 2. Did the Assessor, the Commissioner - General, and the Tax Appeals Commission, err in law by failing to recognize that; Section 25C (1) of the Value Added Tax Act applies only to transaction which results in value addition?*
- 3. Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that; Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*
- 4. Did the Assessor, the Commissioner - General, and the Tax Appeals Commission, err in law by; failing to appreciate that Appellant's primary function of being engaged in the "Banking Business" did not apply to the sale of shares (of Mireka Capital Land (Pvt) Limited), which was a distinct and isolated transaction?*
- 5. Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) contrary to law?*
- 6. In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err in law in arriving at the conclusions set out in its Determination?"*

As above, there are six main questions of Law raised by the Appellant, which I will be dealing in the following manner.

The first and second Questions of Law relate to the concept of “value addition” and its relevance to the computation of Value Added Tax on “financial services” will be considered together. The third and fourth Questions of Law, which pertain to the issues of “emoluments” and the sale of shares, will be considered separately. The fifth and sixth Questions of Law are consequential issues which will be addressed finally.

### **Questions of Law I and II**

#### **Question of Law I**

*Did the Assessor, the Commissioner General, and the Tax Appeals Commission err in law by*

*failing to understand and properly apply the concept of “value addition” in computing the VAT liability on the supply of financial services?*

## **Question of Law II**

*Did the Assessor, the Commissioner General, and the Tax Appeals Commission err in law by failing to recognize that Section 25C(1) of the Value Added Tax Act applies only to transactions which result in value addition?*

The questions of law I and II are similar in nature and therefore I shall discuss them together.

It is the contention of the Appellant that the Respondent has failed to appreciate the principle of value addition, hence that there is no value addition by the Appellant to be taxed.

The concept of “value addition” is not expressly defined in the Act or in any other written law. However, Section 25A of the Act lays down the imposition of VAT on “supply of financial services on specified institutions or any other persons”. In the context of the application of VAT on financial services, the relevant provision is Section 25A(1) of the Act, which stipulates as follows;

*“Notwithstanding the provisions of Chapters I, II, III and item (x) of paragraph (b) of PART II of the First Schedule to this Act, a Value Added Tax (hereinafter in this Chapter referred to as ‘the tax’) shall be charged in accordance with the provisions of this Chapter on the supply of financial services in Sri Lanka.*

- (i) By any specified institution during the period commencing January 1, 2003 and ending on June 30, 2003; and*
- (ii) By any person on or after July 1, 2003 but prior to December 31, 2007; and*
- (iii) By any person other than a co-operative Society registered under the Co-operative Societies Law, No.5 of 1972, on or after January 1, 2008.*
- (iv) By any person other than a Co-operative Society registered under the Co-operative Society Law, No. 5 of 1972, or Lady Lochore Loan Fund established under the Act, No. 38 of 1951, commencing on or after January 1, 2009, or the*

*Central Bank of Sri Lanka established by the Monetary Law Act, (Chapter 422) (with effect from July 1, 2003), or the Sri Lanka Deposit Insurance Scheme established by regulation made under the said Act, (with effect from April 1, 2018) where such specified institution or person carried on the business of supplying such financial services.*

*Provided however, the supply of financial services by a Unit Trust or a Mutual Fund shall not be treated as a financial service for the purpose of this section.”*

Therefore, irrespective of the interpretation that could be given to the concept of “value addition,” under the law—specifically under Section 25A(1) a person is liable to pay VAT on the supply of financial services. However, the calculation of the VAT on Financial Services are done in accordance with Section 25C, unless such person falls outside the ambit of Section 25(f), which defines the supply of financial services. In essence, where a person supplies financial services as contemplated under Section 25(f), such person becomes liable to pay VAT as computed under Section 25C of the same Act, irrespective of any definition that can be given to the phrase “value addition”.

Accordingly, irrespective of the concept of “value addition,” the determining factor in this instance would be the above criteria as for Section 25A of the Act. Therefore, I will not consider it necessary to define the concept of Value Addition to answer to the above first and second Questions of Law stated.

Hence, I do not find that the Respondent has erred in law, and answer the first and second question of law in the negative.

### **Question of Law III**

*Has the Assessor, the Commissioner General, and the Tax Appeals Commission, erred in law by failing to recognize that; Loans granted to employees did not constitute "emoluments" within the meaning of section 25C of the Value Added Tax Act?*

The primary issue is whether the emoluments, specifically the loans granted to the employees subject to VAT under Section 25A should be calculated based on the market value or the actual/ concessional rate provided to employees. This question arises on the basis that the assessors of the Respondent has calculated the VAT adding the emoluments using the market rate, which exceeds by far the actual concessional rate extended by the Appellant to their employees. The dispute centers on which valuation method accurately reflects the taxable value for VAT purposes.

The Respondent contends that when an employee receives a loan from the employer at a subsidized interest rate, this constitutes a benefit to the employee. This is because the employee would not have access to such favorable terms if obtaining a loan from a third-party financial institution at the prevailing market interest rate. Consequently, the difference between the market interest rate and the subsidized rate represents a benefit accruing to the employee arising from the employer-employee relationship.

In terms of section 4 of the Inland Revenue Act, it is evident that the market value of any benefits received or derived by the employee forms part of the profits from employment and is considered as remuneration. Therefore, the Respondent has considered that the emoluments payable to all employees in terms of Section 25C of the VAT Act include not only cash payments but also gross emoluments payable in cash and all other benefits derived from the employer. On this basis, the Respondent has determined that the amortization of staff interest should be considered as emoluments payable in computing the value addition for VAT on financial services.

However, it is the contention of the Appellant that the VAT on financial services can only be made in respect of the emoluments payable to the employees, which is the actual amount payable and not the notional sums. The Appellant further contends that the gross remuneration paid or payable to employees is reflected in the pay sheet, but the notional sums are not included in the employee remuneration. Therefore, the Appellant argues that the reduced interest rate loans are accounted for financial accounting and income tax purposes by the Appellant and hence do not constitute a taxable benefit to the employees.

Section 25C(1) of the VAT Act refers to the exact point on which the VAT is imposed. It is prior to the payment of income tax and emoluments. Hence, emoluments and payable taxes are to be added to the Net Profit, subject to an allowance for depreciation. Therefore, the VAT is imposed on an actual gross profit as stated above.

Accordingly, section 25C of the VAT Act No. 14 of 2002 (as amended) reads as follows;

*“(1) Every registered specified institution under this Chapter shall be liable to tax for each taxable period on its total value addition of such institution which includes the net profits or loss, as the case may be, before payment of income tax on such profit computed in accordance with accepted accounting standards, subject to an adjustment for economic depreciation, determined by the Minister having regard to the interest of economy by order published in the Gazette, and the **emoluments payable to all the employees of such institution** :*

*Provided however where the amount of profits for each taxable period cannot be accurately ascertained, such amount may be estimated on the basis of available information. The estimated amounts shall be adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis and such adjustment shall be submitted within six months after the closing date of the relevant accounting period.*

***Emoluments paid to all the employees shall include—***

*(a) in the case of specified employees under Chapter XIV of the Inland Revenue Act, No. 10 of 2006, the gross remuneration payable to such employees and reflected in the pay sheet maintained under section 119 of the Inland Revenue Act, No.10 of 2006;” and*

*(b) in the case of an employee other than a “specified employee” the gross remuneration paid to such employee reflected in the pay sheet maintained under subsection*

*(2) Calculation of Tax [s 14 (1) (a) of 17 of 2013] [s 14 (1) (b) of 17 of 2013] for the purpose of this Chapter the value addition of such specified institution shall be computed :-*

*(i) for any taxable period commencing prior to January 1, 2011, based on the net profit or loss prior to the deduction of the tax payable under this Chapter; and*

*(ii) for any taxable period commencing on or after January 1, 2011, based on the net profit or loss after the deduction of the tax payable under this Chapter”*

The VAT on value addition of a “specified institution” is calculated under section 25C(1)(ii). Accordingly, for any taxable period commencing on or after 1<sup>st</sup> of January 2011, the calculation is based on the net profit or loss after the deduction of tax payable and the economic depreciation, under Chapter XIV of the Act. On this basis, the VAT on specified institution is calculated on the taxable amount for VAT, before the deduction of the income tax and the “*emoluments payable to all the employees of such institution*”.

In determining the point of VAT taxation, the question arises as to the rate of interest on which the loans granted to the employees should be considered to be added to the calculation of the VAT in accordance with the aforementioned provision.

When calculating the profit of an entity for income tax purposes, the emoluments should be deductible at the rate of the staff loan given on a concessionary basis, as the Inland Revenue Commissioner (IRC) will not permit any deduction based on the market rate where loans were granted at a lower concessionary rate. Therefore, the deductible emoluments are those corresponding to the staff loan provided at the concessional rate. In absence of an interpretation given in the VAT Act the Respondent has correctly referred to the interpretation given in the Inland Revenue Act (IR Act) No. 10 of 2006 where “official emoluments” are interpreted in Section 132(4) of the said act. In there a reference is made to the section 04(1) of the IR Act where the emoluments are interpreted as profits from employment as for paragraph 4(a) excluding the pension. Since there is no alternative interpretation of the term “emoluments” other than that could be gathered by Section 4 of the Inland Revenue Act, no other interpretation of “emolument” can be applied.

In other words, in calculating the income tax, the emoluments are a deductible expense, however when loans granted to the employees are considered, they would only be deductible at the actual rate which is the concessionary rate. Therefore, the word of “emoluments” interpreted in relation to section 4 of the Inland Revenue Act No. 10 of 2006 (as amended) gives a clear impression that

emoluments should be considered at actual rate, and therefore its quite impossible to give a different interpretation to the term “emolument” as under the Inland Revenue Act No. 10 of 2006 (as amended) as for the purpose of VAT under section 25A of the VAT Act No. 14 of 2002.

This clearly indicates that the legislature intended VAT to be imposed on the actual gross profit of the institution, prior to the deduction of income tax and employee emoluments, and subject to the allowance for economic depreciation. Consequently, artificially expanding the said gross profit by artificially introducing an excessive interest rate would result in calculating a hypothetical gross profit rather than the actual one, which contradicts the legislative intent.

Therefore, the underlying important principal should be, “if the said emoluments are deductible for the income tax purposes, then it should similarly be capable of being added to the net profit of the entity in calculating the VAT.”

On the same line, regarding VAT on financial services payable in respect of official travel abroad of employees, if such expenses qualify as deductible emoluments for income tax purposes, then they must similarly qualify and be added back as emoluments when calculating VAT. The word ‘Emoluments’ cannot bear two different or inconsistent meanings in tax computations.

Therefore, the question of law III is hereby answered in the affirmative.

#### **Question of Law IV**

*Did the Assessor, the Commissioner - General, and the Tax Appeals Commission, err in law by; failing to appreciate that Appellant's primary function of being engaged in the "Banking Business" did not apply to the sale of shares (of Mireka Capital Land (Pvt) Limited), which was a distinct and isolated transaction?*

The main question that arises is, does the sale of shares of Mireka Capital Land is a Financial service which falls within the meaning of “banking business”? It is admitted by both parties that the Appellant is a “specified institution” which engages in financial services and falls under section 25C(1) of the VAT Act.

The Appellant contends that the gains made from the sale of shares which the Appellant held in Mireka Capital Lands (Pvt) Limited were not carried out as part of the business activities of the Appellant Bank and therefore must be excluded from the calculation of VAT on financial services. The Appellant held a 40% stake in Mireka Capital Lands (Pvt) Limited and, by the sale of those shares, reported a gain of Rs. 3,130,000,000.

In the case of ***Boehm+Leckner Multi Moulds (Private) Limited V. The Commissioner General of Inland Revenue***, case No. CA (TAX) 34/2014, Justice Janak De Silva held that;

*“The purpose of accounting is usually to provide information to interested parties relevant to stewardship, control and decision-making. The requirements of a tax system can be quite different. The profits and income shown in the accounts prepared in accordance with accounting standards differ from profits and income computed in accordance with the provisions of the Inland Revenue Act No. 10 of 2006 as amended.*

*In fact, the Supreme Court in Rodrigo v. The Commissioner General of Inland Revenue [(2002) 1 SrLL.R. 384 at 387J held that to arrive at the taxable income consideration should be given only to the permissible deductions provided by the Act and the Court cannot take into consideration any other means of computing the deductible amounts. In doing so, it quoted with approval the decision in Sub Nigel Ltd., v. CLR [(1948) 4 SA 580, 15 S.A.T.c. 381J where Centiliversc.J. held that the Court is not concerned with deductions which may be considered proper from an accountant's point of view or from the point of view of a prudent trader, but merely with the deductions which are permissible according to the language of the Act.”*

Therefore, it needs to be noted that the accounting standards prescribed by law is only for the accounting purpose. Even though the Appellant has shown the market rate of the loan given to their employees in their accounts, its only for the accountancy and it would not be relevant for taxation purposes.

Moreover, in considering Section 25C, it is important to pinpoint the exact basis on which VAT is imposed. According to this section, VAT is levied on the gross profit before the deduction of income tax and after allowing for the permitted economic depreciation, with the emoluments paid to employees being added back.



Therefore, I am compelled to conclude that, with respect to Section 25 of the VAT Act, the amount to be added back in calculating the gross profit on which VAT is imposed should be based on the actual rate, which is the concessionary rate.

The Appellant asserts that the special circumstances under which the shares was owned, including the Government's involvement in requiring the Appellant to continue holding the investment and the appointment of three directors to the Joint Venture in connection with the acquisition of such shares, establish that the disposition of these shares was not part of the conventional course of business of the Appellant Bank. Therefore, the Appellant contends that the transfer of shares it is a unique transaction carried out outside routine business activities, and is not liable for VAT on financial services. Therefore, the Appellant asserts that their principal activity is not trading, and the shares in Mireka Capital Lands (Pvt) Limited were an isolated occurrence that did not form part of the principal business of the company under section 25G of the VAT Act.

However, the Respondent contends that the Appellant is liable to VAT on Financial Services under Section 25F(e) of the VAT Act, which specifies the items that can be considered as "Financial Services."

*"(e) the issue, allotment, transfer of ownership of any equity security or a participatory security ;"*

The primary issue that arises is whether the sale of shares of Mireka Capital Land falls within the definition of "banking business." According to Section 86 (Interpretation section) of the Banking Act No. 30 of 1998, "banking business" is defined as:

*"Banking business means the business of receiving funds from the public through the acceptance of money deposits payable on demand by cheque, draft, order, or otherwise, and the use of such funds, either in whole or in part, for advances, investments, or any other operations either authorized by law or by customary banking practices."*

This provision establishes that a registered bank under the Banking Act is authorized to engage only in the activities encompassed within the above definition. Furthermore, a bank is prohibited from engaging in any business activities other than those specified in its license.

Section 6 of the Banking Act No. 30 of 1988 provides that:

*“Subject to the provisions of section 17, no licensed commercial bank shall— (a) carry on any banking business other than the business specified in the license; or (b) carry on any other form of business other than those specified in Schedule II of this Act.”*

According to the financial statements submitted by the Appellant, the Commissioner General of Inland Revenue (CGIR) has considered investment activities as part of the bank’s business operations, thus regarding any gains derived from such investments as part of the bank’s business income. Additionally, the Respondent asserts that the paragraph (ii) of Schedule 3 of Gazette Notification 1868/10 dated 23<sup>rd</sup> June 2014 mandates that non-financial value addition must be calculated on a separate basis. Consequently, no income stream can be excluded from the total value addition calculation. Therefore, considering these facts and circumstances of the case, the Commissioner General of Inland Revenue has considered the profits gained from the sales of Mireka Capital Ltd by the Appellant as a Business Transaction within the scope of Banking Business.

It is noteworthy that the possession of Mireka Capital Ltd by the Appellant has occurred under special circumstances, and there is no evidence to demonstrate that the Appellant is engaged in the business of financing or trading shares beyond this instance. Although the Respondent has stated in their post argument written submissions that the Appellant is involved in purchasing shares in multiple companies, this claim was neither raised during oral arguments nor referenced in prior submissions, hence the Appellant had no opportunity to respond to the said claim of the Respondent. Furthermore, I do not find any materials to substantiate the claim that the Appellant holds shares in other companies or conducts business related to trading shares. Therefore, this contention by the Respondent is not sustainable and cannot be accepted.

Furthermore, section 25A(1) of the VAT Act No. 14 of 2002 as amended by Act No.13 of 2004, clearly implies the applicability of VAT on specified institution for Financial services where,

*“where such specified institution or person carries on the business of supplying **such** Financial services.”*

Therefore, it is established that section 25A can only be applied to an institution which carries on the business of supplying **“such”** Financial Services. The TAC has held that the Appellant provides Financial Services and trading in shares is also a Financial Service. Hence, the Appellant is liable to pay VAT on this occasion.

I regret that I cannot agree with the above, as the Appellant is a banker and have not engaged in share trading other than on this occasion, and the law requires the entity to be engaged in **such** Financial Services, as a business. A banker engaging in a sale of shares as one-off transaction cannot be held to be in the business of share trading. In my view both the regular business and one-off transaction simply being Financial Service is insufficient to hold that the bank has disposed of shares in the course of its regular business.

Furthermore, in the case of *People’s Leasing and Finance PLC V. The Commissioner General of Inland Revenue, (2021)* CA (TAX) 21/2019, CA Minutes 20.07.2021, Dr. Ruwan Fernando, J held that;

*“While the mere acquisition, holding and sale of shares does not by itself constitute “supply of services” within the meaning of Section 25F of the VAT Act as supply of financial services, if the purpose of consideration of payment provided was to finance its business activities only and raise capital for its activities, such activities will not constitute a supply of services for consideration within the meaning of Section 25F. It is totally different where the sale of shares was to obtain income on a continuing basis that goes beyond the compass of the simple acquisition and sale of shares in the course of a business or trading in securities. Such transactions, would constitute a supply of a financial services within the meaning of section 25F of the VAT Act. ”.*

Therefore, the Respondent has failed to establish a continuation or a different instance where the Appellant has involved in share Transaction. On this basis, I would answer the question of law IV in the affirmative.

### **Question of Law V**

*Is the Assessment, (and the Determination of the Commissioner General, and the Determination of the Tax Appeals Commission, thereon) contrary to law?*

### **Question of Law VI**

*In view of the evidence and material before the Tax Appeals Commission, did the Tax Appeals Commission err in law in arriving at the conclusions set out in its Determination?*

When considering the question of Law V and VI, I would answer in affirmative for the reasons stated before.

Accordingly, I answer the questions of law raised by the Appellant in the following manner;

### **CA (Tax) No.56/2023**

Question of Law 1 – No

Question of Law 2 (a) - No

Question of Law 2 (b) - Yes

Question of Law 2 (c)– Not decided

Question of Law 2 (d) - Yes

Question of Law 3(a) –Yes

Question of Law 3 (b) -Yes

Question of Law 3 (c) – Yes

Question of Law 4 (a)– Yes

Question of Law 4 (b) - Yes

Question of Law 4 (c) - Yes

Question of Law 5- Yes

Question of Law 6 - Yes

**CA (Tax) No.90/2023**

Question of Law 1 – Not decided

Question of Law 2 – No (in absence of interpretation for value addition)

Question of Law 3(a) –No (in absence of interpretation for value addition)

Question of Law 3 (b) - Yes

Question of Law 3 (c) – Not decided

Question of Law 3 (d) - Yes

Question of Law 4 (a) – Yes

Question of Law 4 (b) - Yes

Question of Law 4 (c) - Yes

Question of Law 5- Yes

Question of Law 6 - Yes

**CA (Tax) No.91/2023**

Question of Law 1 –No (in absence of interpretation for value addition)

Question of Law 2 (a) - No (in absence of interpretation for value addition)

Question of Law 2 (b) - Yes

Question of Law 2 (c) - Not decided

Question of Law 2 (d) - Yes

Question of Law 3(a) – Yes

Question of Law 3 (b) - Yes

Question of Law 3 (c) - Yes

Question of Law 4 – Yes

Question of Law 5- Yes

Question of Law 6 - Yes

**CA (Tax) No.97/2023**

Question of Law 1 –No (in absence of interpretation for value addition)

Question of Law 2 (a) –Not decided

Question of Law 2 (b) - Yes

Question of Law 2 (c) – Not decided

Question of Law 2 (d) - Yes

Question of Law 3(a) – Yes

Question of Law 3 (b) -Yes

Question of Law 3 (c) - Yes

Question of Law 4 – Yes

Question of Law 5- Yes

No cost ordered.

The Registrar of this court is directed to forward a copy of this Judgment to the Tax Appeals Commission for the necessary action.

**Judge of the Court of Appeal**

**Annalingam Premashanker J.**

**I agree**

**Judge of the Court of Appeal**