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

In the matter of An Application of a case stated under section 11A of the Tax Appeals Commission Act No. 23 of 2011 as amended by Act No. 20 of 2013.

THE COMMISSIONER GENERAL OF INLAND REVENUE,
Department of Inland Revenue,
Inland Revenue Building,
Sir Chittampalam A. Gardiner Mawatha,
Colombo 2.

APPELLANT

Case No.: CA/TAX/12/2021
TAC/VAT/021/2015

-Vs-

LANKA ORIX LEASING COMPANY PLC,
No. 100/1,
Sri Jayawardenapura Mawatha,
Rajagiriya.

RESPONDENT

Before :	**JUSTICE M.CHAMATH.B.S. MORAIS**
	JUSTICE ANNALINGAM PREMASHANKER

Counsel: **Chaya Sri Nammuni, Deputy Solicitor General for the APPELLANT**

Maithri Wickramasinghe, President's Counsel with Rakitha Jayatunge, Attorney- at- Law instructed by Sithumini Wijeyrathne, Attorney - at -Law for the RESPONDENT.

Written Submissions of the Appellant :- 22.05.2023, 14.07.2026
Written Submissions of the Respondent :- 19.05.2023, 04.05.2026
Argued on :- 27.02.2026
Judgment on :- 06.08.2026

JUDGEMENT

ANNALINGAM PREMASHANKER, J.

A. INTRODUCTION

A1. APPEAL

This is an appeal by **The Commissioner General of Inland Revenue** (**Hereinafter sometimes referred to as CGIR/ Appellant**) from the determination of the Tax Appeals Commission dated 07.12.2020 made in TAC appeal No. TAC/NBT/021/2015. The Respondent is **LANKA ORIX**

LEASING COMPANY PLC (Hereinafter sometimes referred to as The Respondent/Tax Payer).

A2. REQUEST

The Appellant being dissatisfied with the Determination of Tax Appeals Commission (**Hereinafter sometimes referred to as TAC**) requested for an appeal by a case stated for the opinion of the Court of Appeal by their communication dated 24.03.2021.

B. ARGUMENT

On 27th February 2026, both parties concluded the argument. It is found that the Appellant has furnished written submissions on 22.05.2023 and 14.07.2026. The Respondent has furnished the written submissions on 19.05.2023 and 04.05.2026.

C. ANALYSIS

C1. QUESTION OF LAW

In the case stated dated 05.05.2021 following question was raised for the opinion of the Court of Appeal:-

1. **Has the TAC erred in interpreting the "gain from disposal of the shares of the subsidiary" in computing the Value Added Tax on Financial Services?**

C2. TAX RETURN

When the tax payer submitted their return for the taxable period 2011/2012, the claim was rejected by the Assessor on the basis that that the Tax Payer was not entitled for exemption from Value Added Tax returns for the relevant taxable periods. The return is not accepted and issued an assessment.

C3. FIRST APPEAL

Having aggrieved by the said Assessment, the tax payer made an appeal to the CGIR. The Tax Payer made the same agitation before the CGIR. CGIR by his determination dated 04.08.2015 determined the appeal by confirming the assessment.

C4. SECOND APPEAL

The tax payer being dissatisfied with the determination of the CGIR, made an appeal to the TAC. In the appeal before the TAC the tax payer raised the same issues. TAC by its determination dated 10.03.2022, upheld the decision of the Inland Revenue Department and dismissed the appeal subject to the adjustment with regard to the profit on sale of shares of the subsidiary company. Thereafter, the CGIR being dissatisfied with the said determination of the TAC requested TAC by his communication dated 24.03.2021 to have a case stated for the opinion of the Court of Appeal.

C5. SUBTANTIAL ISSUE

The substantial dispute relates to the liability of the Value Added Tax on the supply of financial services regard to the dividend income, interests received on profit on sale of shares for the taxable period from 01.04.2011 to 31.03.2012. The assessor did not accept the returns and assessment issued on the ground that certain calculations made by the taxpayer in ascertaining the value addition attributable to the financial services were not inconformity with the Value Added Tax act.

C6. PROVISIONS OF LAW

Section 25A of the Value Added Tax Act is the gateway for the imposition of Value Added Tax on the supply of Financial Services.

Section 25A (1) is as follows:

> ***"1) notwithstanding the provisions of Chapter I, II, III and item (xi) of the First Schedule to this Act, a Value Added 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;

III. by any person other than a Co-operative Society registered under the Co-operative Society Law, No. 5 of 1972, on or after January, 1, 2008 but prior to January, 2009; and

IV. by any person other than a Co-operative Society registered under the Co-operative Societies 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).

Where such specified institutions or persons caries on the Business of supplying of any Financial Services. Provided however, the supply of Financial Services by a unit of Trust or a mutual fund shall not be treated as a Financial Services for the purpose of this section.

C7. REAL VALUE ADDITION

Levy of Tax for value additions for financial services only, income from other sources which are not financial services have to be identified, in order to calculate and attribute the value addition only to the financial services. However, these value additions cannot simply be removed from the equation or deducted from the net profit.

Value addition for the financial services is calculated as per the section 25C(1) of the Value Added Tax Act, in accordance with acceptable accounting standards. For the purpose of calculating the percentage of value addition attributable to financial services, total turnover is adjusted as per the section 25C(5). The ratio of the turnover obtained for financial services is applied to the total value addition and then the value addition attributable for financial services is obtained.

C8. A SALE OF SHARES

The Appellant's contention is that the Respondent is engaging in the sale of inter company shares as part of its business activity and transfer of shares is in fact defined as a financial activity as per section 25F. Even if the Respondent's claim that this was a mandated disposal is accepted, it is the fact of the disposal that attracts the Value Added Tax liability. This is done as a business by the Respondent, will fall within the scope and ambit of financial services, since this sort of transaction is part of their regular business which is a Financial Service.

C9. REGULAR BUSINESS

The CGIR has acknowledged in the reasons for Determination of the CGIR provided in terms of section 7(3) of the TAC Act that the principal activities of the Company comprised of leasing, hire purchase, loans, operating leases and factoring." The TAC has also held that the principal activities of the Company comprised of leasing, hire purchase. loans, operating leases and factoring. <u>The Respondent is not in the business of selling shares and this is conceded by the CGIR and the TAC.</u>

C10. CHARGING SECTION

The charging section relating to Value Added Tax on the supply of Financial Services is section 25A(I). Value Added Tax on the supply of Financial Services is imposed in terms of Section 25A(1) of the Act. Liability for Value Added Tax on the supply of Financial Services can only arise in terms of Section 25A(1) of the Act. Section 25A(I) of the Act, as it applied at the time relevant to this assessment, provided as follows.

"Notwithstanding the provisions of Chapters I, II, III and item (xi) 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** - …

(iv) by any person other than a Co-operative Society registered under the Cooperative Society Law No. 5 of 1972 or Lady Lochore Loan Fund established under Act No. 38 of 1959 commencing on or after January 1, 2009".

where such specified institution or person carries on the business of supplying such financial services.

C11. BANK OF CEYLON CASE

In ***Bank of Ceylon v CGIR***, the TAC had upheld the imposition of Value Added Tax on the supply of Financial Services on the Bank of Ceylon, a bank not in the business of trading in shares. This Court has held that the Bank of Ceylon had no liability for Value Added Tax on the supply of Financial Services as it was not in the business of trading in shares.

*"Therefore, it is established that section 25A can only be applied to an institution which carried on the business 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. In my view both the regular business and one - off transaction simply being Financial Service is insufficient to hold that the bank as dispose of shares in the course of its regular business."

C12. VALUE ADDED TAX ON FINANCIAL SERVICE

This Court has held, Section 25A(1) of the Value Added Tax Act provides that in order that a transaction be liable to Value Added Tax on the supply of Financial Services, all of the following conditions must be satisfied.

1. The transaction must be a supply of financial services.
2. The supply of that financial service should take place in Sri Lanka.

3. The person must be in the business of supplying **<u>such</u>** financial service on which Value Added Tax is to be imposed.

<u>If any of these conditions are not present, then the person is not liable to Value Added Tax on the supply of Financial Services.</u> Accordingly, if a person is not in the <u>business</u> of supplying such type of financial service, no Value Added Tax on the supply of Financial Services can be imposed on such transaction. A one-off transaction does not constitute a business. Particularly so when the CGIR has specifically determined that the business of the entity is several other types of businesses in this case, principal activities of the Company comprised of leasing, hire purchase, loans, operating leases and factoring.

C13. BUSINESS OF SALE OF SHARES

In the present case, the Respondent is not in the business of sale of shares. The CGIR has come to a specific finding in the reasons for Determination that the businesses of the Respondent are "comprised of leasing, hire purchase, loans, operating leases and factoring." There is not even an allegation that the Respondent is in the business of sale of shares.

Moreover, in the case of the Respondent, the sale of shares was a result of a Direction of the Central Bank of Sri Lanka to its subsidiary and the requirements of the Rules of the Colombo Stock Exchange. A sale of shares in these circumstances cannot be a sale in pursuance of the business of sale of shares. The TAC held as follows.

> *"In this regard, it is to be noted that, shares of subsidiaries were disposed to comply with Colombo Stock Exchange (CSE) rules and on a directive given by the Central Bank of Sri Lanka (CBSL). Central Bank wanted Registered Finance Companies (RFC) to be listed in the CSE. To be eligible to become a listed company in the CSE, the Appellant had to dispose some of their shares to the public, to meet the minimum requirement of 10% of the shares. In the given situation, sale of shares owned by the Appellant to the public in a subsidiary, is a strategic decision taken by the Appellant to broad base the share ownership, by allowing the public to participate in equity ownership of the subsidiary.*

Therefore, we are of the view that gain from the sale of shares of the subsidiary as a result of a directive given by the CBSL cannot be considered as a transaction coming under the definition of "Supply of financial services" as envisaged under section 25(C) or 25(F) of the Value Added Tax Act."

Accordingly, there is no doubt that the Respondent is not in the business of selling shares. If the Respondent is not in the business of selling shares, then there can never be liability for Value Added Tax on the supply of Financial Services under the Value Added Tax Act on the sale of shares. To hold otherwise would be a violation of all known principles of statutory interpretation of taxing statutes. Additionally, in the present case, the sale of shares was consequent upon a directive of the CBSL, and such a sale cannot be construed as making the Respondent to be in the business of the sale of shares.

C14. ANSWER TO THE QUESTION OF LAW

For the reasons adumbrated above the Question of Law is answered as follows;

Q.N.1- NO

D. CONCLUSION

As analyzed above and as the one question of law raised in the case stated is answered in Negative, the determination of the TAC dated 07.12.2020 is affirmed, the appeal is dismissed.

The Registrar is directed to forward a copy of the judgment to the Tax appeal commission.

On this 6th day of August 2026

JUDGE OF THE COURT OF APPEAL

M. C. B. S. MORAIS

I agree.

JUDGE OF THE COURT OF APPEAL