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

In the matter of a Case Stated under Section 170 of the Inland Revenue Act No. 10 of 2006 (as amended).

CA Case No: CA/TAX/47/2023
Tax Appeals Commission No. TAC/VAT/024/2017

Senkadagala Finance PLC,
Of No. 267,
Galle Road,
Colombo 03.

Appellant

Vs.

The Commissioner General of Inland Revenue,
Department of Inland Revenue,
Sir Chittampalam A. Gardiner Mawatha,
Colombo 02.

Respondent

Before: **M.C.B.S. Morais J.**
&
Annalingam Premashanker J.

Counsel: Riad Ameen with Rushitha Rodrigo instructed by Arime Legal for the Appellant.

N. Kahawita, SSC for the Respondent.

Written Submissions: By the Appellant – on 09.08.2024, 28.04.2026

By the Respondent – on 27.05.2024

Argued on: 20.02.2026

Decided On: **18.06.2026**

JUDGMENT

M.C.B.S. Morais J.

This is an appeal by way of case stated against the determination of the Tax Appeals Commission (TAC) dated 24th of January 2023, in the case of TAC/VAT/024/2017.

This appeal is filed under section 170 of the Inland Revenue Act No. 10 of 2006 (hereinafter will be referred to as 'IRA 2006').

The tax in dispute is against the assessment for the year of assessment 2012/2013 and the taxable amount in issue is Rs. 19,591,670.00.

FACTUAL BACKGROUND

The Senkadagala Finance PLC (hereinafter will be referred to as the Appellant) is a listed company in the Colombo Stock Exchange as a Finance Company under the Finance Business Act No.22 of 2011. The Appellant being a Finance Company mainly engages in the business of mobilizing deposits and providing them for hire purchase, leasing, and other loan facilities for customers. The Appellant has registered for VAT on financial services as well as normal VAT and files the respective VAT returns accordingly. The Appellant pays VAT on financial services on the taxable value addition arising from supply of financial services as defined

under section 25F of the Value Added Tax Act No. 14 of 2002 (VAT Act) under the required method.

The Appellant has filed the VAT returns in respect of supply of financial services for the periods 01.04.2012 – 30.06.2012, 01.07.2012 – 31.12.2012, and 01.01.2013 – 31.03.2013 respectively and has filed the annual adjustment report subsequently. The Assistant Commissioner of the Inland Revenue has rejected the said assessment and has issued the letter of intimation dated 21st of September 2015 and the Notice of Assessment dated 4th of September 2015. The Appellant being aggrieved by the said assessment, made an appeal to the Commissioner General of Inland Revenue (hereinafter will be referred to as the Respondent). The Respondent after hearing the said appeal confirmed the assessment made by the Assistant Commissioner of the Inland Revenue by the determination dated 31st of October 2017. Being dissatisfied with the said determination, the Appellant had made an appeal to the Tax Appeals Commission. The TAC after hearing both parties, agreed with the determination of the Respondent, for the reasons set out in the determination dated 24th of January 2023.

On this basis, the Appellant has requested the TAC to cause a Case Stated to the Court of Appeal on the following Questions of Law.

I. *"Has the Tax Appeals Commission erred in law in determining that the appellant failed to submit documentary evidence to prove that the appellant has acted in compliance with section 25C(1) of the Value Added Tax Act?*

II. *Has the Tax Appeals Commission erred in law when the Tax Appeals Commission failed to determine whether the Commissioner General refusing to give effect to his own directive is lawful?"*

ANALYSIS

It is the Appellant's position that the Sri Lanka Financial Reporting Standards (SLFRS) was introduced in the year 2012/2013 and it is the first year of adoption of the said standard by the Appellant.

Due to the significant tax implication of these adjustment, the Department of Inland Revenue has issued a directive requesting the taxpayers to make the required adjustments for the specified year accordingly (Annexure B_1 and Annexure B_2). The required adjustment has been communicated to the Appellant by way of the letter dated 28th of January 2014, which includes the following.

- *"The Net profit or loss referred to in the Section 25C (1) of the Value Added Tax Act No 14 of 2002 (Act) is the profit from operation (before Income Tax Expenses) ascertained as per SLFRS.*

  Every person registered for payment of VAT on FS is required to make the following adjustments statements:

- *Calculation of Tax*

  - *The Net Profit or Loss*

    The Net Profit or loss referred to in the Section 25C(1) of the Value Added Tax Act No 14 of (Act) is the aggregate of the Total Comprehensive Income and Income Tax Expenses ascertained as per SLFRS.

  - *Emoluments paid to All Employees*

    Emoluments referred to in the Section 25C(1) of the Act mean the aggregate of both benefit in money and benefits not in money.

  - *Adjustments for Depreciations*

For the purpose of computation of Economic Depreciation referred to in the Section 25C(1) of the Act, the treatment of historical cost will continue.

In computing economic depreciations, on the basis of the Gazette Notification No. 1606/30 of 19.06.2009 published for that purpose, the classification of assets should be on the basis of SLFRS. However, in relation to any asset acquired prior to the adaptation of SLFRS, the earlier classification may be followed in calculating economic depreciations even after the adaptation of SLFRS.

- *Profit/Loss arising upon the transition*

> ***Profit or Loss arising upon the transition to the SLFRS should be treated as such, for the period in which the transition effected. Any additional tax arising thereon may be paid within one year. Where any refund arises, such refund may be set off against the VAT on Financial Services within one year from the date of such transition."***

Accordingly, the Appellant contends that the following three adjustments have been made to their financial statements, as a result of the first time adoption of SLFRS.

"(a) The originally recognized interest income (arising from loans and leases) under Sri Lanka Accounting Standards ("SLAS") based on Sum of Digit Method ("SDM") was adjusted to the Effective Interest Rate method ("EIR") under SLFRS.

(b) Prior to the adoption of SLFRS, loan interest expenses on account of bank borrowing were accounted on cash basis and with the implementation of SLFRS interest expenses were accounted on accrual basis.

(c) Prior to the SLFRS implementation, the Appellant has recognized the investment in associate at cost. Upon the implementation of SLFRS, investments had to be recognized under equity method. "

It is the Appellant's position that they have duly complied with the said directives, and has made adjustment to the annual adjustment which was already filed. However, the said

assessment has been rejected by the Assessor on the basis that the expenditure incurred in relation to the adoption of SLFRS as first adopter cannot be claimed from profit when computing VAT on Financial Services.

According to the journal entry dated 20th of February 2026, the parties in their oral submissions agreed that this court need not answer the question of law I. Hence, only the question of law II needs to be answered. Therefore, I shall only deal with the question of law II, in the following manner.

Question of Law II

Has the Tax Appeals Commission erred in law when the Tax Appeals Commission failed to determine whether the Commissioner General refusing to give effect to his own directive is lawful?"

The Appellant being dissatisfied with the assessment issued by the Assessor has made an appeal to the Respondent. Accordingly, the Respondent has determined confirming the assessment made by the Assessor. Being aggrieved by the said determination the Appellant has appealed to the TAC, which confirmed the decision of the Respondent.

It is the contention of the Appellant that the Appellant submitted the VAT return for the tax period 2012/2013 in accordance with SLAS (Sri Lanka Accounting Standards). However, subsequently, a new accounting standard was introduced, namely 'Sri Lanka Financial Reporting Standard' (SLFRS). Accordingly, following the directive issued by the Respondent, the Appellant has adjusted the said VAT return in accordance with the new accounting standard under SLFRS. On this basis, the Appellant contends that the Respondent, or TAC, cannot now renounce the application of the said directive in the present circumstances.

The TAC in its determination dated 24th of January 2023 has set out the following reasoning to uphold the assessment issued by the Assessor.

"According to the "Directive" issued by the Department of Inland Revenue, in regard to the adoption of SLFRS, profit or loss arising upon the transition to the SLFRS should be (applicable on), for the period in which the transition is effected. Any additional tax arising thereon may be paid within one year. Where any refund arises, such refund may be set off against the VAT on financial services within one year from the date of such transition. ***The Appellant's argument is that the Assistant Commissioner's decision to disregard the directive issued by his own department is ultra vires and arbitrary.*** *Hence, the adjustment is not valid in law, the Appellant contends.*

The Senior Commissioner who has given reasons for the determination on behalf of the Respondent, states that the computation of the total value addition in terms of Section 25, (1) of the VAT Act is the total value addition of the overall business for a particular period. ***Even though the Appellant Company has mentioned that such interest income/expenses which is already taxed in prior periods there is no provision to eliminate such from the current year's value addition."***

According to the reasons provided by the TAC in its determination, it is apparent that the Appellant has already paid the required VAT for the specified taxable period. The sole reason for the TAC's failure to deduct such VAT payment is the absence of a provision permitting the exclusion of such payment from the current valuation. I find this position untenable, since failure to deduct such payment shall only lead the Appellant to double taxation, which contravenes the legislature's intention in taxation matters.

Further, it is the view of the TAC that section 25C(1) of the VAT Act is subject only to adjustments for economic depreciation and emoluments payable to employees.

"*According to Section No. 25C (1) every registered specified institution shall be liable to tax for each taxable period on its total value addition of such institution which include the net profits or loss, as the case may be, before the payment of income tax on such profit computed in accordance with accepted accounting standards subject to an adjustment for economic depreciation as determined by the Minister having regard to the interest of the economy by an Order published in the Gazette and the emoluments payable to all the employees of such institution. Respondent's contention*

is that Sec. ***25C (1) shall not allow to make any adjustment in the net profit or loss computed in accordance with accepted accounting standards other than depreciation and emoluments payable.***"

However, it needs to be noted that section 25C(1) is not exhaustive as to the manner of calculating tax.

The section 25C(1) of the VAT Act, which deals with the calculation of tax on financial services, reads as follows;

"25C. (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 and maintaining the uniformity of allowable depreciation by Order published in the Gazette, and the emoluments payable to all the employees of such institution:"

………………….

(8) Every specified institution or any other person shall for the purpose of the calculation of tax, submission of returns and information to be furnished relating to such return, payments of tax, issue of assessments, imposition of penalty for non-submission of the returns or the information required for the purpose of this Chapter, follow –

(a) the guidelines specified by the Commissioner-General; and

(b) the relevant guidelines specified in the Order published in the Gazette,

having considered the uniform application of the calculation of the liability and any other matter specified in the guideline provisions of this Chapter."

Section 25C(1) of the VAT Act imposes VAT liability on every registered specified financial institution for each taxable period, calculated on its total value addition. This comprises the institution's net profit or loss (computed in accordance with accepted accounting standards, prior to the deduction of income tax), subject to two statutory adjustments: (i) economic depreciation, and (ii) emoluments payable to all employees.

Further, Section 25C(8) of the VAT Act expressly prescribes the guidelines that shall be issued for the purpose of calculating taxes payable under the said section. This provision demonstrates that the calculation of tax to be governed not solely by the terms of section 25C(1), but also by the supplementary guidelines to be issued pursuant to section 25C(8).

Accordingly, it can be reasonably construed that section 25C(1), which deals with the calculation of tax on financial services, is not exhaustive in its scope. The very structure of section 25C indicates that subsection (1) operates in conjunction with subsection (8), as the former gives effect to the guidelines promulgated under the latter for the same purpose.

Furthermore, the TAC in its determination has clearly mentioned that;

> "***Though the Appellant repeatedly argues that the Respondent has not considered his own directive issued by a Deputy Commissioner to clarify the way of adoption of SLFRS, it has failed in convincing submitting any documentary evidence to convince either the Respondent or the Commission that it has acted in compliance with the Section 25C (1) of the VAT Act.*** *The Commission, therefore, is of the opinion that there is no reason to interfere with the determination of the Respondent.*"

It must be observed that the Respondent has not alleged that the Appellant has failed to produce documentary evidence in support of its position. Moreover, had the Respondent asserted non-compliance with section 25C(1) of the Value Added Tax Act, the burden of proving such non-compliance would lie upon the Respondent itself. On the contrary, it is the Respondent who has failed to adduce any evidence to establish that the directives relied upon by the Appellant was not in fact issued by the Respondent. In the absence of such proof, the Respondent cannot seek to impugn the Appellant's position on the basis of alleged non-compliance.

Therefore, in the present circumstances, there is no burden on the Appellant to prove, by documentary evidence, that it has acted in compliance with section 25C(1). Accordingly, I find the position of the TAC is wholly untenable.

Furthermore, the TAC in the latter part of the determination has provided that;

> '*As the provisions of law supersede a mere direction. As such, the Commission affirms the determination of the Respondent, namely the Commissioner General of Inland Revenue and dismiss the Appeal.*'

It is trite law that a provision of law shall supersede a direction. However, it needs to be noted that a directive issued by the Respondent and subsequently gazetted to provide tax calculation guidelines by the Commissioner-General of Inland Revenue becomes part of the law. This applies, provided the directive is not contrary to the legislature's intention in the Act.

Furthermore, the VAT Act, under section 25C(8), has clearly established that any person or institution may follow the guidelines specified by the Commissioner-General regarding tax calculation. Therefore, it is my view that the TAC has not considered the above provisions of law in arriving at its determination.

It should also be noted that the required adjustment was communicated to the Appellant by the letter dated 28th January 2014 (Annexure B1 and B2). Therefore, it is apparent that a guideline has been issued by the Respondent to the Appellant. Further, the Deputy Commissioner clearly states in the said communication that any person who has furnished returns not in conformity with the said format is permitted to make the necessary adjustment and payment on that basis and to inform the Deputy Commissioner accordingly. Therefore, the Appellant contends that it adjusted the returns for the 2012/2013 tax period solely on this basis.

Further, section 67(m) of the VAT Act, which contains the penal provisions relating to returns and related matters, reads as follows:

"67. Every person who –

(m) fails to comply with the requirements specified by order published in the Gazette or the guidelines issued by the Commissioner General under sections 2 or 25C, as the case may be ; or

(n) fails to furnish an annual adjustment under subsection (1) of section 25C

shall be guilty of an offence under this Act, and shall be liable, on conviction after summary trail before a Magistrate, to a fine not exceeding twenty five thousand rupees, or to imprisonment of either description for a term not exceeding six months or both such fine and imprisonment."

According to section 67(m) of the VAT Act, a taxpayer who fails to comply with the guidelines issued by the Commissioner-General of Inland Revenue under sections 2 and 25C of the Act is liable to the penalties prescribed therein. Thereby, adherence to the guidelines issued pursuant to the aforesaid provision is not merely procedural in nature but constitutes a statutory obligation imposed upon taxpayers.

Therefore, if the Appellant has failed to adhere to the directives issued by the Respondent, such failure would only attract the penal consequences prescribed under section 67(m) of the VAT Act.

The paramount issue in this appeal is that the Respondent has failed to provide the refund claimed by the Appellant. Having submitted the VAT returns for the year 2012/2013 under SLAS format, the Appellant also submitted the annual adjustment for the same period on 30th of September 2013 in the required SLFRS format. Subsequently, by letter dated 21st of November 2013, the Appellant has also submitted the amended annual adjustment claiming the refund arising from the incorporation of the annual adjustment under SLFRS, which has been denied by the Respondent.

The section 58 of the VAT Act, which deals with the refund of tax, explains the procedure to obtain the refund in the following manner;

> *"58. (1) Where a registered person makes an application for a refund of any tax or any penalty paid by him in excess during a taxable period, within three years from the end of such taxable period and satisfies the Commissioner-General that such person has paid any tax or any penalty in excess, of any amount which he was liable to pay for that period, such person shall be entitled to a refund of the amount paid in excess, subject to the provisions of subsection (3):*
>
> *Provided however, that any such amount paid in excess by a registered person referred to in paragraphs (a), (b), (c), (d) or (e) of subsection (5) of section 22, shall be refunded to such person within forty- five days from the end of the taxable period or from the date of the receipt of the return for the taxable period in which the excess arose, whichever is later:"*

Under section 58 of the VAT Act, any person who seeks a refund of any tax or penalty paid in excess for a specified taxable period is required to file the claim within three years from the end of such taxable period. Furthermore, such person must satisfy the Commissioner-General of Inland Revenue that they are entitled to the refund. This statutory provision establishes the time limit for filing the claim to be three years from the end of such taxable period.

However, the directive issued by the Respondent provides a different framework, as it reads in the following manner:

> "*Profit or Loss arising upon the transition to the SLFRS should be treated as such, for the period in which the transition effected. Any additional tax arising thereon may be paid within one year.* ***Where any refund arises, such refund may be set off against the VAT on Financial Services within one year from the date of such transition*.**"

The directive issued by the Respondent clearly states that where a refund arises upon the transition to SLFRS, such refund may be set off against the VAT on Financial Services within one year from the date of such transition. This provision establishes a specific one-year timeframe for the set-off of refunds arising from the SLFRS transition.

Consequently, the Appellant submitted a refund claim by letter dated 21st of November 2013, which falls within the one-year timeframe specified in the directive. It therefore follows that the refund claim was made within the timeframe stipulated by law. Furthermore, the Respondent has not provided any reasonable justification for denying the refund to the Appellant. Therefore, I am of the view that it is unlawful for the Commissioner-General to reject such claim without providing any valid reason

In view of the foregoing, I find that the Tax Appeals Commission has erred in law by failing to hold that the Commissioner-General's refusal to give effect to its own directive was unlawful. Accordingly, I answer Question of Law II in the affirmative.

In concluding the question of law II in the above manner, I would like to discuss Section 59 of the VAT Act, which deals with interest on refunds and reads as follows:

> *"(1) Where any amount refundable under this Act to a registered person has not been refunded within a period of thirty days from the due date of such refund, there shall be paid by the Commissioner-General to such person interest on such amount for the period commencing on the thirtieth day from the due date up to the date of refund of the amount, at the rate prescribed by the Minister from time to time:*
>
> *Provided, however, that no such interest shall be payable where there was a delay on the part of the registered person in complying with any requirement made by the Assessor in respect of any records of the registered person."*

According to Section 59 of the VAT Act, where a refund is not paid to a taxpayer within the period prescribed by law, the Commissioner-General is liable to pay interest on the refundable amount for the period of delay. In the present case, the Assessor has rejected the refund claim made by the Appellant without providing a valid reason. Furthermore, the proviso to section 59(1) shall not be applicable in the present matter, since the Respondent has not challenged any delay on the part of the Appellant. Accordingly, it is my view that the Appellant is entitled to interest on the refund amount in terms of Section 59(1) of the VAT Act.

Therefore, this Court finds that the Appellant is entitled to the refund claimed, together with interest on that amount for the period commencing on the thirtieth day after the due date of the refund and continuing until the date on which the refund is paid, at the rate prescribed by the Minister in accordance with Section 59(1) of the VAT Act.

CONCLUSION

When considering the facts and the circumstances of the case, in line with the materials presented before this court, I am of the view that the question of law II raised by the Appellant should be answered in the Affirmative.

Accordingly, the appeal is allowed.

The determination of the TAC dated 24th of January 2023 and the determination of the Respondent dated 31st of October 2017 is overturned. Further, the Notice of assessment dated 4th of September 2015, issued by the Assistant Commissioner of the Department of Inland Revenue is hereby annulled.

The Appellant is entitled to the refund claimed, with the interest on that amount for the period commencing on the thirtieth day after the due date of the refund and continuing until the date on which the refund is paid in full.

The Registrar is directed to serve a copy of this judgment to the Secretary of the Tax Appeals Commission for necessary action.

Judge of the Court of Appeal

Annalingam Premashanker J.

I agree

Judge of the Court of Appeal