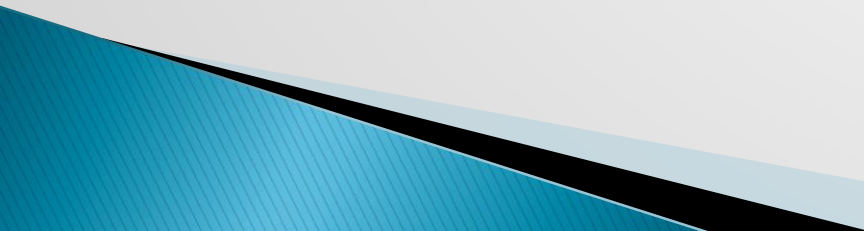


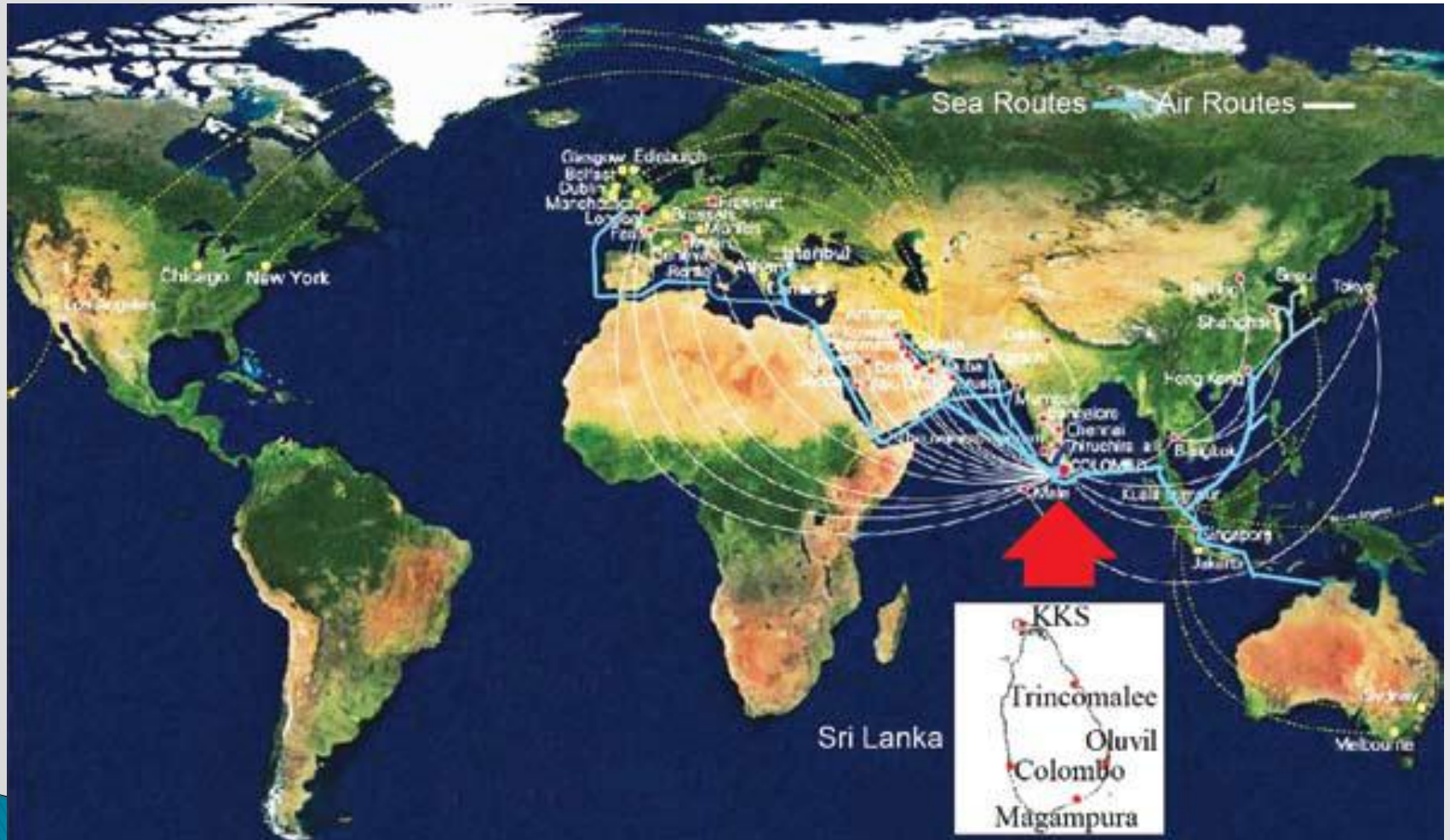
Revenue Mobilization Measures and Current Tax Issues – Sri Lanka

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ASIAN AND PACIFIC COUNTRIES***

Road map

- ▶ Country profile in brief
 - ▶ Revenue mobilization in Sri Lanka – overview
 - ▶ Tax administration and Recent achievements
 - ▶ Challenges currently faces
 - ▶ Concluding remarks
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Item	Units	2005	2010	2016
Population	mn	19.7	20.7	21.9
GDP	USD bn	24.4	49.1	98.0
Per Capita Income	US\$	1,241	2,375	4,470
Inflation	%	5.7	7.0	4.0
Exports	US\$ bn	6.3	8.0	18.0
Earning from Tourism	US\$ bn	0.3	0.5	2.5
Access to Electricity	%	75.0	88.0	100.0
Access to Telecommunication	%	23.6	85.0	100.0
Infant Mortality	Per 1000	11.2	10.9	4.0
Maternal Mortality	Per 1000	0.45	0.39	0.2
Poverty	%	15.2	7.6	4.2
Primary School Enrolment	%	95.0	98.0	100.0
Literacy rate (15–24 years)	%	95.0	97.0	98.0

Revenue Mobilization- Overview

Tax Revenue (90% of Total Revenue)

Income Tax

- Personal and Corporate
- Economic Service Charge
- Interest Income

Tax on Goods and Services

- VAT
- Excise Tax
- Other Taxes and Levies

Tax on External Trade

Non Tax Revenue (10% of Total Revenue)

Property Income

	2006	2007	2008	2009	2010
Total Revenue (Rs. bn)	477.8	565.1	655.2	699.6	817.3

Tax Revenue	428.4	508.9	585.6	618.9	724.7
Income Tax	80.5	107.2	126.5	139.6	135.6
Taxes on Goods and Services	289.3	328.6	356.2	352.0	435.4
Taxes on External Trade	58.6	73.2	102.9	127.4	153.7

- Total revenue increased by 16.8 % in 2010
- Revenue from VAT increased due to improvement in domestic economic activities and improved performance in imports
- Income tax has marginally declined in 2010 due to tax exemptions

Revenue sur/deficit	-70.1	-57.7	-88.5	-179.9	-119.8
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Budget Sur/Deficit	-205.7	-246.0	-309.6	-476.4	-446.0
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As a % of GDP

Revenue	16.3	15.8	14.9	14.5	14.6
Tax Revenue	14.6	14.2	13.3	12.8	12.9
Non Tax revenue	1.7	1.6	1.6	1.7	1.7
Revenue sur/Deficit	-2.4	-1.6	-2.0	-3.7	-2.1
Budget Sur/deficit	-7.0	-6.9	-7.0	-9.9	-7.9

Total revenue as a % of GDP increased marginally to 14.6% from 14.5% in 2009 – Reflect declining trend over the years.

Tax Administration and Recent Achievements

- ▶ Tax system – direct and indirect taxes
- ▶ The main indirect tax is Value Added Tax (VAT) about 34% of the Government revenue
- ▶ The indirect taxes applied in Sri Lanka are administrated by the Central Government (Commissioner General of Inland Revenue)
- ▶ prior to implementation of Value Added Tax – the following indirect taxes were applied from time to time
 - Turnover Tax (TT), Business Turnover Tax (BTT),
 - National Security Levy (NSL), Goods and Services Tax (GST)

- ▶ These taxes had an ill effect on the economy because of its cascading effect (tax on tax)
- ▶ NSL and GST were abolished with the introduction of the VAT in 2002
- ▶ Basic concept of VAT system is – complete elimination of cascading effect – anti cascading method applied
- ▶ Application of VAT – Mainly in two areas
 1. Supply of goods and services in SL by a registered person in any taxable period
 2. Importation of any goods, other than exempt goods, into SL by any person

Main Taxes	Direct Tax	Indirect Tax	Admin by (Central/ Provincial)
Value Added Tax		yes	Central
Economic Service Charges	yes		Central
Debit Tax	yes		Central
Social Responsibility Levy	yes		Central
Stamp Duty	Yes		PC
Nation Building Tax		Yes	Central
Share Transaction Levy	Yes		Central
Betting and Gaming Levy	Yes		Central

Reform Initiative

- ▶ 10 member Presidential Commission on Taxation submitted their report in October 2010 – valuable recommendations on the desired changes and reforms.
- ▶ This report prepared after extensive discussions with investors, businessmen, private and public sector officials, representatives of trade chambers and lawyers
- ▶ 2011 /12 Budget accommodated most of the proposals and simplified tax system– continued in 2012 budget

A new tax regime – Corporate Income Tax

	Before 01/04/2011	After 01/04/2011
Standard	35%	28%
Export	15%	10 – 12%
Agriculture	Exemption available	Conces. rate of 10%
Construction	15%	12%
Tourism	15%	12%
Corporative	Exempt	Extended the exemptions
Liquor, Tobacco and Casino	35%	40%

Indirect Tax

	Before 01/01/2010	After 01/01/2011
VAT	12%-20%	12%
NBT	3%	2%
Customs Duty	5 bands	4 bands
ESC	0.5- 2 %	0.1 ,0.2, 1%
Telecom Sector	Multiple	Single 20%
PAL	5%	5%

Institutional Reforms

Interpretation Committee

Consists of the Senior Officers of the IRD - eliminate individual arbitrariness relating to interpretations

Tax Write-off for SMEs

Any Enterprise with a turn over less than 100 mn per quarter,

- in a conflict environment and, financial constraints prior to 31/12/2010
- based on the request of the tax payer subject to future Tax Compliance

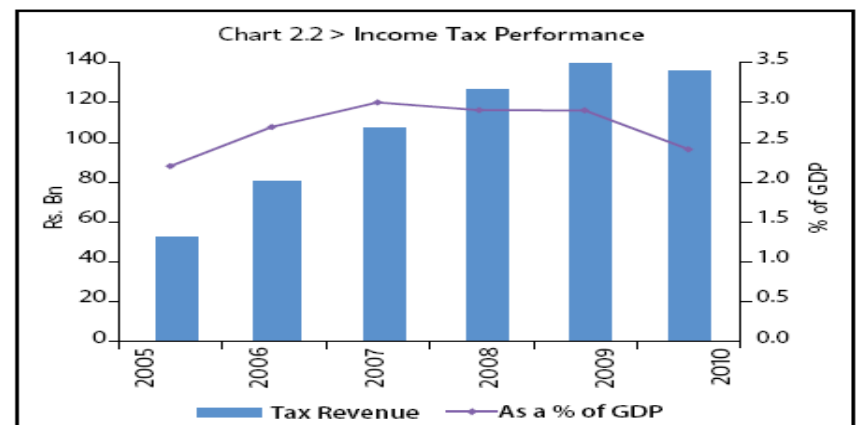
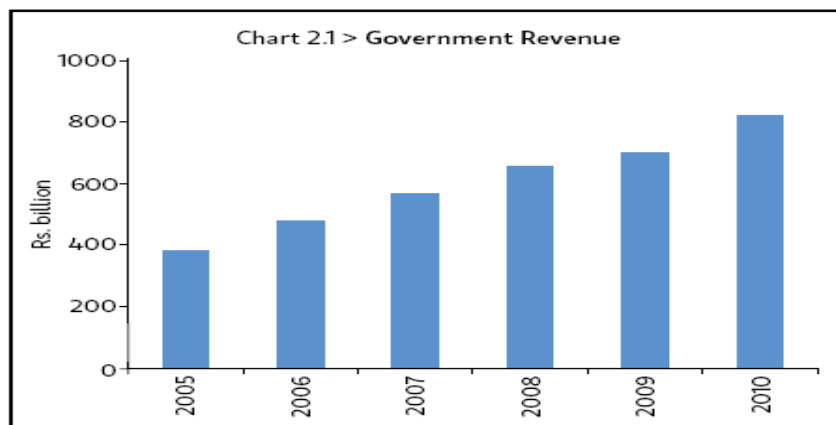
Tax Appeal Commission Act No. 23 of 2011

Functions of the Board of Review of the IRD shall be transferred to the Appeal Commission to ensure independent and early decisions

- 3 Retired Judges of the Supreme Court or the Court of Appeal

Challenges Currently Faces

- ▶ The most fundamental [problem – the system is not delivering the potential revenue
- ▶ As income increases the revenue should increase although the rate of increase will decline after some time.
- ▶ This is not happening in SL – Our per capita income has increased from US\$ 720 in 1995 to US\$ 2053 in 2009
- ▶ but our tax revenue has declined from 20.4% GDP to 14.6% GDP during the period. Tax elasticity less than 1 not a healthy sign



The key reasons

- ▶ Tax base has not broadened in line with the increase in income or economic activities
- ▶ Imposition of ad hoc taxes from time to time by successive govt. – address the issues of weak tax revenue. There were about 25 taxes in operation (should be 8–10 taxes)
- ▶ successive governments have heavily depended on indirect taxes for tax revenue – 80% indirect, 20% direct – Bulk of the tax fall with less well off people– better balance 60%–40%).

Tax exemption

- ▶ 1979 public servants were exempted from taxes because their salary is not on par with private sector
- ▶ BOI tax exemptions and tax holidays approximately 1% of GDP
- ▶ Various exceptions on VAT and import duty from time to time

Tax evasion

- ▶ Some professionals do not disclose their true income
- ▶ Successive governments have implemented tax amnesties
- ▶ Under invoicing of imports
- ▶ Over stating of expenses and transfer pricing
- ▶ Illegal flows of imports to the country

Issues relating to VAT

- ▶ VAT still does not bring the same revenue as the former BTT and GST. VAT brings 34% of tax revenue which amounts 5.5 of GDP.
- ▶ BTT brought an average of 6.5% GST brought an 6% of DGP revenue.
- ▶ VAT is yet to achieve this after 8 years of operation and 8 amendments to the ACT. We are still on a learning curve in regard to VAT.
- ▶ VAT there are computational problems and identification issues.
- ▶ More ground work needed to firmly establish the VAT to the wholesale and retail sectors.

- ▶ IN 1987 provincial council system came to operation, turnover tax at the wholesale and retail levels and Stamp Duty were devolved to the PCs. TT was abolished from PC from 1/1/2011
- ▶ Turnover tax is the highest revenue earner to PCs accounting for 44% of revenue. This is followed by stamp duty 28%, licensing fee for motor vehicles and exercise 13% and other 15%
- ▶ provinces lack adequate tax administration capacity and specialized technical skills
- ▶ There is a lack of motivation among PC revenue collectors in seeking new and innovative sources of revenue. – partly due to the dependence on an annual grant received from the centre which almost ensures PCs that recurrent expenditure needs will be met

Concluding Remarks

- ▶ Final aim – Increase revenue to 20% of GDP during the next 4–5 years.
- ▶ Such revenue will facilitate Sri Lanka to maintain current expenditure at around 18% of GDP and capital expenditure at 6% of GDP and keep the budget deficit at about 4% of GDP – Fiscal Responsibility Act No 3 of 2003.
- ▶ Broaden the tax base and promote business and people friendly taxation system.
- ▶ less complicated border tariff structure which gives reasonable protection and revenue.

Thank You