



AbeyRatna & Co
(Chartered Accountants)

Budget Highlights 2007

A large, light blue wireframe globe graphic is centered in the background of the page. It features a grid of latitude and longitude lines. Overlaid on this globe is the text 'Budget Highlights 2007' in a large, bold, black, serif font. The word 'INTERNATIONAL' is also visible in a large, light blue, sans-serif font, partially obscured by the globe and the main title.

Budget Highlights 2007

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Determination of Statutory Income

Depreciation Allowance rates have been revised as follows,

Depreciation allowance	<i>Proposed</i> Y/A 2007/2008	<i>Prevailing</i> Y/A 2006/2007
Ships	33 1/3 %	12 1/2 %
Machinery used in the construction industry	25 %	12 1/2 %

Insurance

Proposal

It has been proposed to treat the operations of life insurance and general insurance as two separate businesses in order to preclude the set off of losses from life insurance business against profits from general insurance.

The operations of life insurance and general insurance are treated as one business.

Concessions

Exemptions granted to Unit Trusts

Proposal

It has been proposed to exempt profits derived by a Unit Trust from the sale of shares.

Profits and income derived from sale of shares are currently chargeable at 10%.

Local Film Industry

- **Cinema Theatres**

Proposal

In order to promote technological infusion to local cinema theatres it has been proposed to grant a 10 year tax holiday for newly constructed cinemas with advanced technological facilities and a 5 year tax holiday to existing cinemas if upgraded with the same.

The exemption operates from the date of commencement of operation.

- **Local Film Production**

Proposal

It has been proposed to increase the 'qualifying payment' relief on the cost of film production to Rs 25 Mn a year.

Currently, the qualifying payment relief on the cost of film production that exceeds Rs 5Mn, is subject to maximum claim of Rs 10Mn per annum and any balance is eligible to be carried forward for a further 2 years of assessments.

Reopening of Closed Factories

Proposal

With a view to encourage reopening industries which are located in 'backward' areas and have not been in operation for the past several years, it is proposed to grant 3 year tax holiday to those factories which recommence operations.

Entrepot Trade

Proposal

It has been proposed to widen the scope of articles eligible for the prevailing concessionary tax rate of 10% on profits and income arising from entrepot trade.

Currently articles entitled to this concession are,

- any precious stones or metals not mined in Sri Lanka;
- any petroleum, gas or petroleum products; or
- such other products approved by the Minister, having regard to the foreign currency brought from export

Dividends

Proposal

It has been proposed to introduce provision that would deem dividend on a company, where the gross dividend distributed is less than 25% of the “distributable” profit. In this context the deemed dividend is calculated as the excess of 1/3 of the distributable profit less dividend already distributed and will be taxed at 15%.

15% Tax on Distribution of Corporate Profit

- Where for any tax year commencing on or after April 1, 2007 the gross dividend distributed by any company is less than 25% of its distributable profits for that year, the company will be required to pay additional tax amounting to 15% of the excess of one-third of the distributable profits over the profits already distributed, if any.
- The distributable profits for any year would in this context, be the after-tax profits for that year reduced by the excess of the cost incurred in that year, on the acquisition of land or other capital assets over the depreciation charged thereon.

eg:-

Distributable profit	400,000
25% of that profit	100,000
If company distribute more than 100,000	
no additional tax payable	
If company distribute more than 50,000	
tax payable computed as follows:	
1/3 of Distributable Profit	133,333
Distributable Profit	<u>50,000</u>
Difference	<u>83,333</u>
15% tax payable on 83,333	<u><u>125,000</u></u>

Corporate Tax Rates

Resident /Non –resident companies – rates

	Proposed Y/A 2007/2008	Prevailing Y/A 2006/2007
Resident Companies		
<ul style="list-style-type: none"> • Taxable income < Rs. 5 Mn. <ul style="list-style-type: none"> ○ Group of companies ○ Others 	<p>35%</p> <p>15%</p>	<p>15%</p> <p>15%</p>
<ul style="list-style-type: none"> • Taxable income > Rs. 5 Mn. <ul style="list-style-type: none"> ○ Listed - First five years after quotation - Others ○ Non listed companies 	<p>33 1/3%</p> <p>35%</p> <p>35%</p>	<p>33 1/3%</p> <p>35%</p> <p>35%</p>
<ul style="list-style-type: none"> • Dividends <ul style="list-style-type: none"> - Dividend distributed - Deemed Dividend 	<p>10%</p> <p>15%</p> <p>(calculated on a specific formulae)</p>	<p>10%</p> <p>-</p>
Non – resident Companies		
<ul style="list-style-type: none"> • Taxable income < Rs. 5 Mn. <ul style="list-style-type: none"> ○ Group of companies ○ Others 	<p>35%</p> <p>15%</p>	<p>15%</p> <p>15%</p>
<ul style="list-style-type: none"> • Taxable income > Rs. 5 Mn. 	<p>35%</p>	<p>35%</p>
<ul style="list-style-type: none"> • Remittance of profit (chargeable to tax) 	<p>10%</p>	<p>10%</p>

Profits from Employment

Shipping

Proposal

It is proposed to exempt the remuneration of any resident individual employed on any Sri Lankan ship.

At present there is no specific tax exemptions extended to resident individuals employed on Sri Lankan ships.

Taxation of Terminal Benefits of Retiring Employees

Proposal

The prevailing concessions on the taxation of terminal benefits on retirement, have been extended as follows:

○ **Retirement on or after 20 years of service**

<i>Tax Rates</i>	<i>Proposed Tax slabs (Rs.)</i>	<i>Prevailing Tax slabs (Rs.)</i>
Nil	0 – 5,000,000	0 – 2,000,000
5%	5,000,000 - 6,000,000	2,000,000 - 2,500,000
10%	6,000,000 Upwards	2,500,000 - 3,000,000
15%	-	3,000,000 Upwards

○ **Retirement before 20 years of service**

<i>Tax Rates</i>	<i>Proposed Tax slabs (Rs.)</i>	<i>Prevailing Tax slabs (Rs.)</i>
Nil	0 – 2,000,000	0 – 1,000,000
5%	2,000,000 - 3,000,000	1,000,000 - 1,500,000
10%	3,000,000 Upwards	1,500,000 - 2,000,000
15%	-	2,000,000 Upwards

Employee Share Ownership Schemes

Proposal

To exempt from income tax the value of benefit arising to any employee at the time of disposal of any shares received through an ESOP. However on a sale of such shares, the tax consequences would be as follows:

Shares subject to Share Transaction Levy - Exempt

Shares held over \geq 2 years – Exempt

Shares held \leq 2 years – 15%

Under the present tax regime profits from employment include the value (ie. the surplus over the cost of acquisition of such shares) at the time of the “disposal” of any share received at no cost or less than the market value directly or through an ESOP.

Withholding tax and taxation

Deposits with Banks and Financial Institutions

Proposal

In order to encourage saving by individuals, thresholds for withholding has been increased whilst the rate has decreased

<i>Up to Rs.300,000</i>	<i>- No WHT</i>
<i>Rs.300,000 - 600,000</i>	<i>- 5%</i>
<i>Total interest incomes excess of Rs.600,000</i>	<i>-10%</i>

Total interest income exceeds Rs. 9,000 p.m. or Rs. 108,000 p.a.

OR

10%

Total interest from Bank/ Branch exceeds Rs. 1,000 p.m. or Rs. 12,000 p.a.

Concessions

Profits on Construction - Individuals

Proposal

It has been proposed to exempt profits from construction work carried on outside Sri Lanka by an individual provided remittance of foreign currency to a banking system.

Profits from construction work carried on in Sri Lankan currently taxed at a rate of 15%.

Incentives for Professionals.

Proposal

It has been proposed to allow the deduction of expenditure incurred for acquiring internationally recognized qualifications that are of a higher standard than the standard professional qualifications.

Currently the law allows the deduction of training expenses incurred for training of employees.

Amnesty and penalty due on tax in default.

Proposal

It has been proposed to empower the CGIR to waive off penalties imposed on income tax in default as at 31 March 2005, by giving a period of 3 years for repayment of outstanding taxes on an installment plan agreed for repayment of such taxes outstanding.

Withholding tax on construction fees

Proposal

With the view to improve the cash flow of the construction industry, it has been proposed to reduce the rate of withholding on construction fees to 1%.

Under prevailing tax regime, construction fee is subject to a withholding tax of 5%.



Partnerships

Proposal

It has been proposed to introduce a tax free threshold of Rs.600,000 where divisible profits exceeds Rs. 600,000 if any, income tax will be chargeable on the excess at the rate of 10%.

Currently divisible profits (including other income) are taxed at 10%.



Economic Service Charge

	Proposed	Prevailing
Pre conditions for chargeability <ul style="list-style-type: none"> • Liable turnover • Minimum threshold for liable turnover • Businesses in commercial operation 	Turnover excluding income from off-shore transaction of entrepot trade Rs. 7.5 Mn per quarter 36 months applicable only to manufacturing companies & re-opening of closed factories	Aggregate turnover from trade, business, profession or vocation Rs. 10 Mn per quarter 36 months (Excluding traders)
Carry forward of un-recouped ESC	Set-off against income tax of subsequent 4 years of assessment	Set-off against income tax– of subsequent 2 years of assessment
Administration-Assessments	<ul style="list-style-type: none"> • Time bar effective 18 months from end of quarter • Assessor to give reasons for raising assessments 	<ul style="list-style-type: none"> • No time bar • No such stipulation



Rate changes

Turnover	Proposed	Prevailing
Traders <ul style="list-style-type: none"> • Distributors • Traders of motor vehicles & liquor • Others 	0.05% 0.5% 0.25%	0.1% 0.5% 0.5%
Gem/Jewellery/Diamond (including BOI Companies) <ul style="list-style-type: none"> • Export <ul style="list-style-type: none"> - Cutting & polishing of Gems/Diamonds - Jewellery • Manufacture and sale in local market 	1% (value addition) 0.25% 1%	0.25% 0.25% 1%
Entrepot trade on FOB value of on-shore transaction	0.1%	0.5%
From primary conversion of tea, rubber, or coconut including desiccated coconut, coconut oil, coconut fibre, copra, sheet rubber and charcoal excluding produce of any alcoholic beverages	0.25%	0.5%
Venture capital, Unit Trust, Mutual Funds and companies with taxable income < Rs. 5 Mn	0.5%	1%
Apparel (including BOI) <ul style="list-style-type: none"> • Exporters • Supply to exporters • BOI export trading houses 	Turnover- FOB = 0.1% Other = 1% (value addition irrespective of turnover threshold)	0.25% - 0.5%



Value Added Tax (VAT)

Input credit

- **Restrictions on claiming credit**

Proposal:

It is proposed to limit the credit to actual input tax allowable for that taxable period or 85% of the output tax declared, whichever is lower.

A registered person is entitled to claim full input tax against output tax subject to certain restrictions.

The above restriction would not apply to:

- *Zero rated supplies*
- *TQB or EDB registrants who supply goods or certain services to exporters*
- *New businesses registered under Section 22 (7) of the VAT Act on undertaking to make taxable supplies within 30 months*

Effective date – 1 January 2007

- **Motor vehicles – input tax credit**

Proposal:

The 50% claimability of input VAT on traveling vehicles is to be removed with effect from 1 January 2007.

Full input tax credit available for:

Motor cycles / bicycles, motor coaches provide by an employer for transportation of employees, motor vehicles used for excursion tours / transportation of tourists / transportation of goods, hiring cars and motor vehicles forming part of stock in trade.

50% input tax credit available for:

Traveling vehicles

- **Removal of restrictions on claiming input tax credit**

Proposal:

It has been proposed to remove the following restrictions on claiming input tax credits with effect from 1 January 2007:

- *15% restriction of claiming input tax paid at the rate of 20% on raw-materials imported for manufacture and export*
- *Transitional adjustment which disallows input tax credit claimed on any taxable supply which subsequently becomes an exempt supply*

- Presently, the input tax paid at 20% on any item is restricted to 15% for claiming credit.

- Input tax relating to goods and services used in the making of taxable supplies can be claimed as input credit. However, in the event such supply becomes



exempt, input tax attributable to it should be disallowed within the taxable period in which such supply becomes an exempt supply.

Value of supply

- **Value of imports**

Proposal:

The proposed formula to ascertain the value of imports is as follows:

Value of imports = [CIF x 110%] + Customs Duty + Surcharge + Cess + Excise Duty (payable under Excise (Special Provisions Act No. 13 of 1989)) + Port and Airport Development Levy

At present the value of goods at the point of import is:

Value of imports = [CIF x 107%] + Customs Duty + Surcharge + Cess + Excise Duty (payable under Excise (Special Provisions Act No. 13 of 1989)) + Port and Airport Development Levy

Deferment of VAT on local purchase by BOI companies

Proposal:

On purchase of material from local industries, BOI projects to be granted a VAT deferment facility. For making payments in foreign currency for such transactions a special foreign currency account to be opened by the Central Bank of Sri Lanka.

Persons on the borderline of threshold for registration

Proposal:

A person on the border of the VAT threshold of Rs. 1.8m may pay 5% as non refundable VAT on voluntary basis.

Such person is to be given the benefit of paying VAT at 5% until;

- *Turnover reaches Rs. 2.5m*
- or*
- *3 years from the date of entering into this scheme whichever is earlier*

No input tax to be allowed and no tax invoice to be issued by such person. However the option to enter in to the normal VAT system is available.

At present any person who carries on taxable activity in Sri Lanka is required to be registered if;

- *at the end of the taxable period of one month or three month the total value of taxable supplies exceed Rs. 500,000 or*



- in twelve months period the total value of supplies exceed Rs. 1.8m or
- at any time where there are reasonable grounds to believe that the total value of taxable supplies has reached the aforesaid criteria.

Withholding of 1/3 of VAT on supplies to government agencies

Proposal:

Government agencies to withhold 1/3 of VAT payable to contractors and other service providers and remit to the Department on the same date of the payment.

Government agencies to include;

- *Ministries*
- *Departments*
- *Government own Business Undertakings*
- *Public Corporations*
- *Provincial Councils*
- *Universities*
- *The Board of Investment*
- *State Banks*
- *Projects funded by the Government*
- *The institutions for which funds are provided from the Consolidated Fund*



Miscellaneous Taxes

Ports and Airport Development Levy

Proposal

It is proposed:

- to increase the rate of PAL to 3%
- to introduce a concessionary rate of 2% on importation of selected plant and machinery used for high value adding industries and pharmaceuticals
- to exempt PAL from importation of films or teledramas that have been produced outside Sri Lanka and sent outside Sri Lanka for further processing or printing with the approval of Film Corporation; and
- to abolish PAL on importation Gems, Diamond and Gold that are mainly raw or semi processed or semi manufactured

Every article originating from Sri Lanka and imported into Sri Lanka is subject to PAL at 2.5% on its CIF value for customs purposes.

Imports by diplomatic missions would continue to be exempt from PAL while imports for processing and re-export; or imports to be used for manufacture of goods for export would continue to be excluded from the scope of PAL.

Effective : 1 January 2007



LEGISLATIVE CHANGES – INTRODUCED BY ACT NO.10 OF 2006

1. Group Companies

1.1 Thin Capitalisation

A prohibition has been introduced on the deductibility of the cost of inter company borrowings exceeding prescribed gearing limits.

- **To whom does this prohibition apply:**

The prohibition would apply to a *subsidiary company* if geared in excess of the thresholds prescribed in Statute, via 'loans' obtained from its holding company, or any other subsidiary company within the group. The following would be of relevance to the 'subsidiary' in question.

- **Measurement of gearing :**

Ratio of related party loans : Aggregate of issued share capital and reserves (excluding revaluation reserves).

- **Gearing thresholds**

Manufacturer	- 3 : 1
Any Other Business	- 4 : 1

- **Time of companies with ratio**

End of relevant year of assessment. (Where statutory income is determined to a date other than 31 March, reference date would presumably be such other date).

- **How does this prohibition apply**

The interest applicable to the component of the loan in excess of the specified gearing ratio would be precluded from deduction in ascertaining the statutory income of the subsidiary.



1.2 Transfer pricing

Transfer pricing provisions have been introduced into the Sri Lanka tax legislation and provides essentially for the enforcement of the arm's length price in transactions between associated undertakings.

“Associated undertakings”

An undertaking shall be deemed to be associated undertaking of another, if the first mentioned undertaking participates directly or indirectly or through one or more intermediaries, in the *control* of the second mentioned undertaking in such manner or to such extent as may be prescribed.

“Arm's length price”

A price which is applied in uncontrolled conditions in a transaction between persons, other than associated undertakings.

The Revenue Authorities are still to gazette the pricing mechanism for the determination of the arm's length price.

Where a transfer pricing assertion is made by the Revenue Authorities, the onus is then on the taxpayer to establish that the transaction price is in fact arm's length. Failure to establish arm's length price would result in the Revenue Authorities estimating the additional profit for chargeability to tax.

2. Concessions of interest

2.1 Professional services – foreign currency earnings

- **Individuals and Partnerships**

Profit attributable to professional services, whether rendered in or outside Sri Lanka, would be exempt from income tax.

Pre-requisites for qualification

- Services should be provided to a person or partnership outside Sri Lanka.
- Payment to be received in foreign currency through the Sri Lanka banking system.
- In the case of offshore services, remittances of fees could be net of reasonable expenses.



2.2 Shipping Agents – Transshipment service in foreign currency

The profit arising from transshipment services provided to non – resident ship owners or charters for payments in foreign currency, would enjoy a concessionary rate of income tax of 15%.

Note :

- The shipping agent should be approved by the Director of Merchant Shipping.
- Qualifying profits of a shipping agent :

$$\text{Statutory Income} \times \frac{\text{Agency fees from transshipment}}{\text{Total receipts}}$$

- The non resident ship owner / charterer is excluded from charge on transshipment profits.

2.3 Service to garment exporters

The profit of any garment manufacturer approved by the Textile Quota Board (TQB), from supply of services to an exporter also registered with the TQB, which results in the improvement of the value of any garment, chargeable at concessionary rate of 15%.

Pre – requisites for qualification

- (a) The fabric is supplied to the manufacturer by the exporter who would eventually make the export directly or through an export trading house which has entered into agreement with the Board of Investment under Section 17.
- (b) The supply of service is covered by a L/C opened in a bank of Sri Lanka on a back-to-back basis against an international L/C for the remittance of foreign currency to Sri Lanka

or

The payment for the supply is made in foreign currency by draft or telegraphic transfer made in favour of the manufacturer by the exporter

and

Documentary evidence in support of the export is adduced.



2.4 Agriculture

An exemption from income tax on profit from any 'agriculture undertaking' for a period of five years of assessment commencing 1 April 2006 has been legislated. This is an essence an expansion on the prevailing concessions on profit from the cultivation and sale of any primary agriculture produce, mainly aimed at including profits from the primary processing of such agricultural produce, and also profit from the conversion of such produce into certain value added products as may be specified by the Commissioner General of Inland Revenue by Gazette Notification. (To date, only tea bag < 4 gms gazetted).

2.5 Regional development – areas outside districts of Colombo/Gampaha including overlap areas

With a view to developing the regions outside the Western Province, a scheme of incentives has been introduced for the *corporate sector*.

2.5.1 New undertakings

Pre-requisites for qualification

- Minimum capital investment in plant, machinery, fixtures and buildings – Rs 30 Mn. (Land only for agricultural undertakings).
- Investment to be made prior to 31st March 2008.
- Minimum employment generation by 31st March 2008.
 - IT services, printing, packing materials 50
 - Others 200
- No reconstruction or acquisition of an existing undertaking.
- Undertaking could be *commenced* by existing or new company.

Concessions

- **Tax holiday on profits of the ‘undertaking’:**

5 – 10 years depending on quantum of investment and location.

Investment (Rs).	Period of exemption	
	Overlap Area	Other
30 – 50 Mn	5 years	7 years
50 – 100 Mn	6 years	8 years
> 100 Mn	8 years	10 years

Tax holiday to be reckoned from the year of assessment in which the new undertaking makes profits but no later than three years from commencement of commercial operations.

- **Qualifying payment relief on capital investment (in plant, machinery.....etc).**
 - Maximum claim per year of assessment – Rs 100 Mn.
 - Excess indefinite carry forward.

2.5.2 Relocation of existing undertaking

Pre-requisites for qualification:

- An undertaking carried on within Colombo/Gampaha districts prior to 1st November 2005 with a minimum of 100 employees.
- Relocation and commencement of commercial operations prior to 31st March 2008.
- Minimum expenditure on relocation – Rs 100 Mn.
- No reduction in employment cadre prevailing as at 1st November 2005.

Concessions

- **Tax holiday – profits of relocated undertaking**
5 years, to be reckoned from year of assessment in which relocated undertaking commences commercial operations.
- **Qualifying payment relief**
On quantum of relocation expenses with indefinite carry forward of un-availed relief.

3 Corporates – Rates and Dividends

3.1 Rates

<i>Resident</i>	<i>Y/A 2006/07</i>	<i>Y/A 2005/06</i>
Taxable income < Rs. 5 Mn	15%	20%
Taxable income > Rs. 5 Mn		
• Listed – 5 years after listing	33 1/3%	30%
– Others	35%	30%
• Unlisted	35%	32.5%
Dividends	10%	10%
Non-resident		
Taxable income < Rs. 5 Mn	15%	20%
Taxable income > Rs. 5 Mn	35%	32.5%
Profit repatriation	10%	10%
Social Responsibility Levy (on income tax)	1%	0.25%

4 Personal Tax Rates

- Marginal rate - Y/A 2006/2007 – 35% (Threshold taxable income Rs. 1.6 Mn)
- Y/A 2005/2006 – 30% (Threshold taxable income Rs. 1.1 Mn)
- **Residents** – tax free allowance Rs. 300,000/-
- **Expatriates employees (non-citizens)**

	<i>Amendment</i>	<i>Prior legislation</i>
<ul style="list-style-type: none"> • Employer – flagship company <ul style="list-style-type: none"> ○ First 5 years (deemed non resident) ○ Next 5 years (within tax holiday of company) ○ Thereafter 	<p>15% 20%</p> <p>Normal rates</p>	<p>15% 15%</p> <p>Normal rates</p>
<ul style="list-style-type: none"> • Others <ul style="list-style-type: none"> ○ First 3 years (deemed non resident) ○ Next 2 years ○ Thereafter 	<p>15% 20%</p> <p>Normal rates</p>	<p>15% 15%</p> <p>Normal rates</p>

5 Statutory administrative measures

5.1 Compliance, assessments and appeals

- **Filing of return**

The due date of filing of Return of Income has been brought forward to 30th September immediately succeeding the end of the year of assessment, which would coincide with the date of final payment.

(Measures are underway to enable the tax payer to file the Return by electronic means).

- **Time bar on assessments**

Return filed :	<i>Amendment</i>	<i>Previous</i>
Before 30 September / November	18 Months	3 years
After 30 September / November	3 years	6 years
Foard, evasion or willful default	None	None

- **Acknowledgment and settlement of appeals**

- The receipt of every appeal should be acknowledged within 30 days from lodgment. Where an appeal has not been acknowledged, it is deemed to have been received by the Commissioner General on the day of delivery.

5.2 Relief measures – individuals

The following have been introduced with a view to encouraging compliance

<i>Pre-requisite</i>	<i>Incentive</i>
Assessable income <Rs. 1Mn. Furnishes Return and tax paid	No assessment Submission of accounts – waived
Return of income filed 3 preceding Y/A Tax paid > 120% of PY Or Assessable Income declared > 125% of PY Affidavit (no fraud, evasion or willful default)	Return accepted. No assessments.
Quarterly installment paid before 30 days from due date	10% discount – installment due.

Annexure I

Synopsis of Withholding of taxes mandated under the Inland Revenue Act

	Nature of payment	Rate	Time of WHT	Mandated exclusions	Recipient	
					Directions	Tax credit
1.	Interest/Discount					
1.1	Deposits-Bank & financial institutions (Payable to persons outside SriLanka-Refer-1.4)	10%	<ul style="list-style-type: none"> Interest-paid/credited, Discount-allowed. 	<ul style="list-style-type: none"> Exempt. Payable to foreign Governments. Individuals: Written declaration aggregate interest ≤ Rs.9,000 p.m. or Rs.108,000 p.a. Interest from Branch ≤ Rs.1,000 p.m. or Rs.12,000 p.a. 	<ul style="list-style-type: none"> Corporates- Yes. If b/f losses> estimated SI. Individuals- No. 	<ul style="list-style-type: none"> Persons other than Corporates: excluded from AI - WHT final tax, no credit. Corporates: Yes.

¹ A financial Institution means any person or body of persons, corporate or unincorporated, whose business or part of whose consists in the acceptance of money by way of deposit, or loan in the form of debenture or bond in any other form, and the payment of interest thereon, whether such acceptance is on its own behalf or on behalf of any other person.



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

	Nature of payment	Rate	Time of WHT	Exclusions	Recipient	
					Directions	Tax credit
1.2.	Government Securities ²	10%	On issue.	Nil	N/A	<ul style="list-style-type: none"> • Individuals: Interest on SMT Excl. from AI. • Other incl. Corporates: Gross up and notional tax credit.
1.3	Corporate debt securities ³ (to person outside Sri Lanka – refer 1.4)	10%	<ul style="list-style-type: none"> • Interest – paid / credited, • Discount – allowed. 	Nil	<ul style="list-style-type: none"> • Corporates – Yes If b/f losses > estimated SI. • Individuals - No 	<ul style="list-style-type: none"> • Persons other than corporates : excluded from AI. – WHT final tax, no credit. • Corporates : Yes

² Treasury Bonds, Treasury Bills, or Central Bank Securities.

³ A corporate debts security means, any interest bearing or discounted security issued by or on behalf of any company, and includes any bond, note, paper or mortgage which obligates such company to pay the holder a specified sum of money on demand or upon reaching maturity or thereafter, but does not include any loan, advance, overdraft or other similar facility obtained from a bank or financial institution.

Synopsis of Withholding of taxes mandated under the Inland Revenue Act

	Nature of payment	Rate	Time of WHT	Exclusions	Recipient	
					Directions	Tax credit
1.4	Interest payable – persons outside Sri Lanka <ul style="list-style-type: none"> • Loans to companies and other bodies of persons • Deposits/other loans 	15% 20% (or lower treaty rate)	Time of payment	<ul style="list-style-type: none"> • Paid out of income not arising in Sri Lanka • On loans advances made by a banker • On FCBU deposits 	Yes	Yes
2.	“Specified fees”⁴ Payable by a “specified persons”⁵	5%	Payment of specified fee	None	Yes	Yes

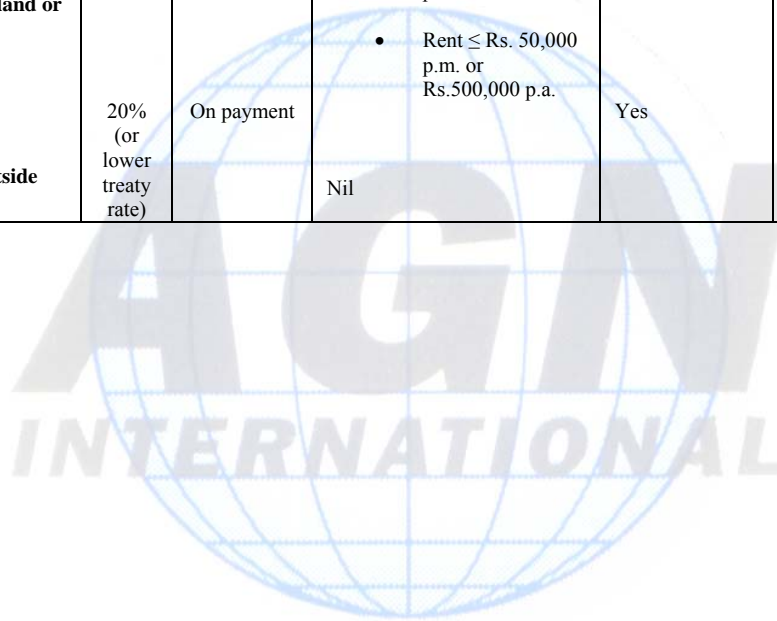
⁴ A “specified fee” means any sum or aggregation of sums exceeding specified thresholds in a year of assessment (Rs. 50,000 p.m. or Rs. 500,000 for the year of assessment) payable in consideration for services rendered in the course of business, profession, vocation or activity of an independent character, excluding payments under contracts and residential / non-residential rent.

⁵ A “specified person” means any person who or which is likely to pay in any year of assessment or has paid in the year of assessment immediately preceding, specified fees



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
3.	Rent "Specified land or building"	10%	On payment	<ul style="list-style-type: none">Residential premisesRent ≤ Rs. 50,000 p.m. or Rs.500,000 p.a.	Yes	Yes
3.1						
3.2	Payable to persons outside Sri Lanka	20% (or lower treaty rate)	On payment	Nil	Yes	Yes





Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
4.	Lottery prizes, winnings from gambling or betting	10%	On payment	Payments ≤ Rs. 500,000	N/A	No (excl. from AI final tax)
5.	Reward payments to informants and distribution of share of fines by a Government institution	10%	On the last working day of month or date of last payment in any month ⁶	Made out of the Consolidated fund or forms part of profits from employment	N/A	No (excl. from AI final tax)

⁶ Payments in calendar month considered as one payment



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
6.	Annuity or royalty					
6.1	Payable with Sri Lanka	10%	On Payment	<ul style="list-style-type: none"> Rs. ≤ 50,000 p.m. or Rs. 500,000 in any year 	Yes.	Yes
6.2	Payable to persons outside Sri Lanka					
	<ul style="list-style-type: none"> Royalty 	15 % (or lower treaty rate)	Time of payment	Payable by company <ul style="list-style-type: none"> Agreement vide Sec 17 of BOI Law per 1/4/2004, and During tax holiday period 	Yes	Yes
	<ul style="list-style-type: none"> Annuity 	20 % (or lower treaty rate)	Time of payment	None	Yes	Yes



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
7.	Management fee or similar payment	5%	On Payment	None	Yes	Yes
8.	Dividends (in money or order to pay money)	10%	Time of payment	<ul style="list-style-type: none"> • Distribution by SEC approved Unit trust / Mutual funds • Payable SEC approved Unit Trust or Mutual funds. • If exempt to shareholder (Sec 10). • Out of dividends already subject to the WHT. • Payable to exempt institution – Sec 7 (a) / (c) 	N/A	<p>Persons other than corporates : excl. form AI WHT final tax, no credit</p> <p>Corporates : excl. from SI, no credit</p>



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
9.	Remuneration of employees (and quasi employees) by employer					
9.1	Remuneration ⁷ paid to employees	Per PAYEE Tables	Time of payment	Nil	Yes	Yes
9.2	Remuneration, any benefit in cash or kind to any director, chairperson or any other person not considered an employee	10%	Time of payment	Nil	N/A	Yes – no refund

⁷ Remuneration including valuation of any non-cash benefits



Synopsis of Withholding of taxes mandated under the Inland Revenue Act

					Recipient	
	Nature of payment	Rate	Time of WHT	Exclusions	Directions	Tax credit
10	Terminal Benefits <ul style="list-style-type: none"> • Releases from super annuation funds • Payments by employer 	Depending on whether uniform	On payment	<ul style="list-style-type: none"> • Employees contributions to Provident Fund • Interest on ETF, Pension/Provident Funds after 1 April 1987 	Yes	Yes
11	Payment to a non citizen entertainer or artist for services rendered in Sri Lanka	15% (or lower treaty rate)	Time of payment	Nil	N/A	Yes – claim refund

Note:

- SI = Statutory Income
 AI = Assessable Income
 SMT = Secondary market transaction

Annexure II

Qualifying Payments – 2006/2007

Tax Payer	Ceiling	Carry Forward
Individuals		
<ul style="list-style-type: none"> • Donations to Government <ul style="list-style-type: none"> ○ Cash ○ In kind (up to Rs. 2 Mn¹) 	None	No time limit
<ul style="list-style-type: none"> • Film production (Min. cost Rs. 5 Mn) 	Rs. 10 Mn	2 years
<ul style="list-style-type: none"> • Housing (First house after 01/04/2001) <ul style="list-style-type: none"> ○ Repayment of approved loan ○ Own Funds 	Lower of Rs. 100,000 or 1/3 of AI	N/A 9 years
<ul style="list-style-type: none"> • Equity investments – Venture Capital Company (Min. Rs. 500,000) made during tax holiday of VCC. 	Lower of 50% of investment or 1/3 of AI	N/A
<ul style="list-style-type: none"> • Others <ul style="list-style-type: none"> ○ Government Development Plan ○ Cash donations – Approved Charities ○ Contributions to approved Provident/Pension Fund² ○ Life & Medical Insurance Premia ○ Cash donations – Specified Institutions ○ Contributions to approved Provident Funds – self employed persons ○ Un-availed housing relief (prior to 31/03/1994) ○ Un-availed relief on equity investments – BOI infrastructure (prior to 31/03/2000) 	Rs. 25,000	No time limit
	Lower of Rs. 75,000 or 1/3 AI	N/A
	Lower of Rs. 25,000 or 1/3 AI	N/A
	Lower of Rs. 25,000 or 1/3 AI	14 years
	1/3 AI	No time limit

¹ The Rs. 2 Mn cap which was withdrawn w.e.f. 1st January 2005 has been reintroduced.

² Contributions up to 12% emoluments only deductible.



Qualifying Payments – 2006/2007

Tax Payer	Ceiling	Carry Forward
Companies		
<ul style="list-style-type: none"> • Donations to Government <ul style="list-style-type: none"> ○ Cash ○ In Kind (up to Rs. 2 Mn) 	None	No time limit
<ul style="list-style-type: none"> • Film Production (Min. cost Rs. 5 Mn) 	Rs. 10 Mn	2 years
<ul style="list-style-type: none"> • Equity investment – Venture Capital Company (Min. Rs. 500,000) made during tax holiday of VCC. 	Lower of 50% of investment or 1/5 of AI	N/A
<ul style="list-style-type: none"> • Regional Development <ul style="list-style-type: none"> ○ New Undertaking investment in capex ○ Relocation expenses 	Rs. 100 Mn	No time limit
<ul style="list-style-type: none"> • Others <ul style="list-style-type: none"> ○ Government Development Plan ○ Cash donation – Approved Charities ○ Cash donation – Specified Institutions ○ Un-availed relief on Equity investments BOI infrastructure (prior to 31.03.2000) 	None	No time limit
	1/5 of AI	N/A
	1/5 of AI	N/A
	1/5 of AI	No time limit

Notes:

AI = Assessable Income

³ The Rs. 2 Mn cap which was withdrawn w.e.f. 1st January 2005 has been reintroduced.

Employment Benefit Valuation
Year of Assessment 2005/2006

<i>Employment Benefit</i>	<i>Employee Benefit Valuation</i>	<i>Employer Tax Effects</i>
<p>HOUSING AND ALLIED BENEFITS Provision of Housing¹</p> <ul style="list-style-type: none"> • Rented accommodation <p>• Company owned accommodation</p> <p>Furniture, Furnishing and Household Appliances</p>	<p>Salary > Rs. 150,000 Lower of rent or Rs. 15,000 p.m.²</p> <p>Others: Lower of rent or Rs. 10,000 p.m.²</p> <p>Salary > Rs. 150,000 Lower of rental value or Rs. 15,000 p.m.²</p> <p>Others: Lower of rental value or Rs. 10,000 p.m.</p> <p>Max. Rs. 1,500 p.m.</p>	<p>Directors/Snr. Execs. (Salary > Rs. 50,000) 75% (Housing exp.¹ – BV³) disallowed.</p> <p>Others: 50% (Housing exp. – BV³) disallowed.</p> <p>Same as Rented Accommodation</p> <p>Tax depreciation, maintenance not deductible.</p>
<p>TRAVELING Employer Vehicle (for private traveling)</p> <ul style="list-style-type: none"> • No mileage record <ul style="list-style-type: none"> ○ 1500c.c. and above ○ below 1500c.c 	<p>Rs. 15,000 p.m.</p> <p>Rs. 7,500 p.m.</p>	<p>Depn/lease rental not deductible.</p> <p>Maintenance & fuel costs fully deductible only for 1st Vehicle⁴.</p>

¹ Includes rent, lease rent, rates, repairs, maintenance, or other expenses relating to residences incurred directly or indirectly by employer

² BV limited in the following cases: Un-rates areas – Rs. 3,000 p.m.

³ BV; Benefit valuation

⁴ Subject to benefit valuation on employees.

Employment Benefit Valuation

<i>Employment Benefits</i>	<i>Employee Benefit Valuation</i>	<i>Employer Tax Effects</i>
<p>Employee vehicle</p> <ul style="list-style-type: none"> • No mileage record Fuel cost: <ul style="list-style-type: none"> ○ 1500c.c. and above ○ Below 1500c.c. Maintenance cost 	<p>Rs. 5,000 p.m. Rs. 5,000 p.m. Total cost reimbursed</p>	<p>Fully deductible⁵ Fully deductible⁵ Fully deductible⁵</p>
<p>Employer/Employee vehicle</p> <ul style="list-style-type: none"> • With mileage record <ul style="list-style-type: none"> ○ 1500c.c. and above ○ Below 1500c.c. <p>Reimbursement of official traveling expenses</p> <p>Chauffer – Reimbursement of wages</p> <p>Sale of Company car to employee</p>	<p>Rs. 15 per km (private travel) Nil Nil Nil. (on premise of sale at current market value)</p>	<p>Fully deductible⁵ Fully deductible. Fully deductible. No impact.</p>
<p>MEDICAL EXPENSES</p> <ul style="list-style-type: none"> • Reimbursed • Insurance premia • Reimbursement of expenses under insurance 	<p>Actual cost. Premia paid. Nil.</p>	<p>Fully deductible. Fully deductible. No impact.</p>
<p>ENTERTAINMENT</p> <ul style="list-style-type: none"> • Company entertainment expenses reimbursed • Entertainment allowance 	<p>Nil. Full allowance.</p>	<p>Disallowed. Disallowed.</p>

⁵ Subject to benefit valuation on employees.

Employment Benefit Valuation

<i>Employment Benefits</i>	<i>Employee Benefit Valuation</i>	<i>Employer Tax Effects</i>
OTHER PERSONAL EXPENSES REIMBURSED e.g. <ul style="list-style-type: none"> • Electricity Bills • Telephone Bills & Rental • Security guard at residence • Club entrance/subscription fee <ul style="list-style-type: none"> ○ Personal ○ Company 	Actual cost. 50% of actual cost. Nil. (if company premises – owned or rented). Actual cost. Nil.	Fully deductible. Fully deductible. Included in housing adjustment. Fully deductible. Disallowed.
COST OF PASSAGE AND ALLOWANCES FOR TRAVEL OVERSEAS <ul style="list-style-type: none"> • In connection with employment • Expatriates (home leave and travel to take up/terminate employment) • Reimbursement or private travel 	Nil. Nil. Actual cost.	Deductible (if o/a exports/training) Fully deductible. Fully deductible.
CHILDREN'S EDUCATION	Actual cost.	Fully deductible.
MEALS ON DUTY	Nominal rate (to be agreed with Revenue)	Fully deductible.
Wages <ul style="list-style-type: none"> • Outdoor Domestic Aids. • Indoor Domestic Aids. 	Nil. (Company bungalow). Actual cost.	Included in housing adjustment. Fully deductible.
ESOP	Value at disposal ⁶	N/A.

⁶ Value at time of disposal – i.e. taxable benefit.

- **Sale (whilst in employment)**
- Sale price or market value, whichever is higher, less cost.
- **Disposal other than sale (whilst in employment)**
- Market value less cost.
- **Termination of employment**
- Market value at date less cost.
- **Death in service**
- Nil.



Recognition of good taxpayers (individuals)

1. Motor vehicle concessionary levy – concession on importation levies on a motor vehicle

The following concession has been gazetted in terms of the Finance Act No. 11 of 2006 and is effective from May 2006.

Any individual who meets the following criteria with regard to the payment of income tax, would be entitled to the concession whereby the aggregate taxes and levies¹ ordinarily payable on the import of a vehicle would be reduced to 75% thereof (i.e. 25% discount). The concession would be available on the importation of one vehicle.

Pre-requisites for qualification

- Payment of income exceeding Rs. 250,000/- for each of the five consecutive years of assessment, commencing year of assessment 2000/2001.
- Certification of payment of tax by the Commissioner General of Inland Revenue.

Note:

The law enables availability of a one time concession if the prescribed minimum payment is made during the five years of assessment commencing 2000/2001. It is understood that the law is to be amended such that the concession would be available where the minimum tax payment criteria is met for any five consecutive years of assessment, arising after 1st April 2000.

¹ Under Customs Ordinance (Chapter 235), the Excise (Special Provisions) Act No. 13 of 1989 and the Value Added Tax Act No. 14 of 2002.



2. Privilege Cards – Gold and Silver Cards

The Commissioner General of Inland Revenue has announced the extension of the scheme to award privilege cards to any individual satisfying certain pre-requisite criteria pertaining to the year of assessment 2004/2005 on application being made by the said individual.

Pre-requisite for qualification

- Return filed by 30 November, 2005
- Payments made by due dates (i.e. quarterly installments by 15th August 2004, 15th November 2004, 15th February 2005 and 15th May 2005 and final payment by 30th September 2005).
- Payment of income tax exceeding following thresholds,

	Gold Card	Silver Card
Citizens	> Rs. 1 Mn	> Rs. 500,000
Non Citizens	> Rs. 2 Mn	> Rs. 1 Mn

Benefits flowing from award of privileged cards

- Priority treatment at Government Agencies (including Airport and Customs) and Statutory boards,
- Special benefits from Bank of Ceylon and People's Bank.

Note:

This scheme was first introduced and awards made in 2006 in recognition of good taxpayers for the year of assessment 2003/2004.