


Now, Next and Beyond

Budget Review, 2022

#Sri Lanka #NationalBudget - 2022





Will the road to
recovery lead to an
economy that's
revived or reimagined?

■ ■ ■
The better the question. The better the answer.
The better the world works.



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Macro-economic vision for revival

Vision

- ▶ Strengthening the balance of payment
- ▶ Improve public finance and national budget
- ▶ Reforms in banking and financial activities
- ▶ Human resources development
- ▶ Environmental conservation

Key measures

- ▶ To increase foreign reserves to USD 10 billion by 2027
- ▶ To increase export of goods to USD 19 billion by 2022
- ▶ Trade deficit to be maintained at USD 7 billion in 2022
- ▶ External current account to have a surplus of USD 6 billion in 2027
- ▶ Reduce budget deficit from 10% of GDP to 1.5% of GDP by 2027
- ▶ Increase tax collection from 9% of GDP to 18% of GDP by 2027
- ▶ Reduce public debts from 102% to 74% by 2027
- ▶ Foreign debts to be reduced from 36.5% of GDP to 13.6% of GDP by 2027

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Summary of the Budget



Summary of the budget

	2021 Estimate	2022 Budget
Total revenue and grants (Rs. Bn)	1,561	2,284
Tax revenue (Rs. Bn)	1,556	2,274
Total expenditure (Rs. Bn)	3,387	3,912
Budget deficit (Rs. Bn)	(1,826)	(1,628)
Total foreign financing (Rs. Bn)	(48)	(179)
Total domestic financing (Rs. Bn)	1,874	1,807
Total revenue / GDP (%)	9.4%	12.3%

One-time taxes

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One-time taxes

Tax Surcharge

- A Tax Surcharge has been proposed to be imposed
- The qualifying persons are individuals or Companies with a taxable income over Rs 2 billion
- Applicable for the YA 20/21
- The tax rate is 25% to be imposed on such persons
- Whilst the tax base is not clear it is assumed to be on taxable income.
- It is expected to raise Rs 100 Billion.

Possible implications and insights

- ▶ Since the tax base is not clearly mentioned would this apply on all forms of profits and income especially those who are exempt from tax such as the IT sector or those paying a lower rate of tax such as exporters
- ▶ Given the experience with Super gains tax would the impact on groups with group taxable income over Rs 2 billion be liable
- ▶ Marginal relief is generally granted where the criteria to qualify is equal or very close to the qualifying threshold. It is expected that such relief would be given.
- ▶ In large groups it is likely that an operations company would exceed Rs 2 billion in taxable income which would be distributed as a dividend
- ▶ to the holding company which is also likely to have taxable income exceeding Rs 2 billion. Would such a double count be excluded.
- ▶ Would this tax surcharge be deductible from the following years income taxes
- ▶ Would this be a separate law with an appeal and refund process or would it be an amendment to the existing Inland Revenue Act which already provides for such provisions.

One-time taxes (Cont.)

VAT on Banks and Financial service providers

- ▶ The current VAT on Financial Services is to be increased by 3% from 15% to 18%
- ▶ The additional tax of 3% is to be imposed only for 12 months from Jan 2022 to Dec 2022.
- ▶ The tax should be paid monthly.
- ▶ Rs 14 Billion is to be raised by this tax.

Possible implications and insights

- ▶ Since most banks are likely to be liable to the tax surcharge there is likely to be a reduction in the VAT FS liability since the Profit before tax (PBT) of the banks is likely to reduce due to the tax surcharge, despite the increase of 3% in the VAT FS rate.
- ▶ However as a result of the tax surcharge and the increased VAT FS a typical banks total tax liability would increase significantly.

3 Value Added Tax



Value Added Tax

New Exemptions from the supply or import of

- ▶ Medical equipment
- ▶ machinery
- ▶ Apparatus
- ▶ Accessories and parts thereof
- ▶ Hospital furniture
- ▶ Drugs and chemicals.

Conditions to be met

- ▶ These items should be donated to a Govt Hospital or the Ministry of Health for the provision of health services to address any pandemic or public health emergency
- ▶ Approved by the Minister of Finance on the recommendation of the secretary to the ministry of the Minister assigned with the subject of health
- ▶ Effective from January 1, 2022

Standard VAT / GST rates in selected countries in 2020

Europe-America				Asia-Pacific			
Country	Last year rate	Current year rate	Movement in comparison to 2021	Country	Last year rate	Current year rate	Movement in comparison to 2021
Switzerland	7.7	7.7	0	Taiwan	5	5	0
Germany	19	19	0	Thailand	7	7	0
France	20	20	0	Singapore	7	7	0
UK	20	20	0	Sri Lanka	8	8	0
Austria	20	20	0	Japan	10	10	0
Belgium	21	21	0	Malaysia	10	10	0
Netherlands	21	21	0	Indonesia	10	10	0
Italy	22	22	0	Vietnam	10	10	0
Ireland	23	23	0	Korea	10	10	0
Portugal	23	23	0	Australia	10	10	0
Finland	24	24	0	Philippines	12	12	0
Greece	24	24	0	China	13	13	0
Norway	25	25	0	New Zealand	15	15	0
Sweden	25	25	0	Pakistan	17	17	0
Denmark	25	25	0	India *	18	18	0

* The rate of GST varies from 5% to 28% depending upon the category of goods and services, the general rate of tax being 18%.

■ Current year rate



4 Social Security Contribution



Social Security Contribution

Introduction

- A new tax on turnover
- Liable persons are those with turnover exceeding Rs. 120 million per annum
- Applicable from April 1, 2022
- The tax rate is 2.5%
- It is expected to raise Rs 140 Billion.

Possible implications and insights

- ▶ This tax appears to be similar to a turnover tax.
- ▶ It is presumed that the tax will be applicable across all sectors including banks, manufactures, services, exports and retail trade as there is no indication of any exemptions.
- ▶ There may however be exemptions as we have seen in the past for similar types of taxes for certain identified sectors and foreign income earners.
- ▶ It is unlikely that input will be allowed for this tax resulting in a cascading effect.
- ▶ Whether income from sources such as dividend, interest and investment assets would also be subjected to this tax remains to be clarified.
- ▶ The proposals do not make any reference on whether the tax can be collected from the customer

Special Goods and Services Tax

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Implementation of Special Goods and Services Tax

Introduction

As previously proposed by the 2021 Budget, a new tax termed Special Goods and Services tax ("SGST") is proposed to be implemented with effect from January 2022 to cover all goods and services that will be specified in the proposed legislation.

SGST was formally introduced in lieu of certain taxes and levies currently imposed under various fiscal laws and administered by various statutory institutions.

Purpose

SGST is proposed to be introduced as an online managed composite tax in lieu of certain identified taxes and levies applicable for specified industries.

The current regulatory bodies of such industries will be relieved of the role of tax collection, allowing them to focus more on primary regulatory engagements.

Scope

It was originally proposed in 2021 budget that SGST would be applicable for prescribed industries i.e., alcohol, cigarettes, telecommunication, betting and gaming and motor vehicles. However, the applicability of SGST on the current proposal refers to all goods and services specified in the Act.

Implementation of the Special Goods and Services Tax (Cont.)

Way forward

- ▶ Who will be the regulator for SGST? (i.e. collecting, compliance, etc.)?
- ▶ Will SGST cover goods and services other than the proposed industries?
- ▶ Will SGST be a single rate or varying based on goods and services?
- ▶ Will it replace the contemplated industry specific taxes and levies?
- ▶ Does the composite tax incorporate VAT?
- ▶ If so, will there be an input credit mechanism available?
- ▶ Does the proposed excise duty revision incorporate the composite tax?

Implementation of the Special Goods and Services Tax.

Alcohol	Cigarettes	Telecom	Betting & Gaming	Motor Vehicles
VAT at 8% Excise Duty (<i>Various Duty rates applicable for specific items</i>)	VAT at 8% Excise Duty (<i>Various Duty rates applicable for specific items</i>)	VAT at 8% Telecommunication Levy at 11.25% CESS at 2%	VAT at 8% or Levy on Gross Collection at 10% Annual Levy	Excise Duty (<i>Various Duty rates applicable for specific items</i>)

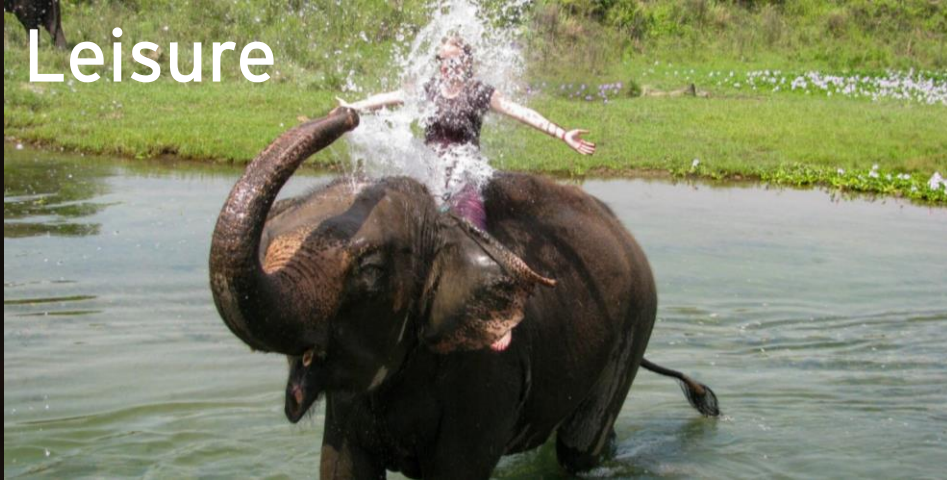
Levies and License fees

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License fee

Leisure



- ▶ A special license fee was proposed to be introduced for designated areas expected to be developed as special zones with respect to leisure activities.
- ▶ The basis and the rates for such license fee is yet to be prescribed.

Telecommunication



- ▶ It is proposed that the Telecommunication Regulatory Commission of Sri Lanka will auction the issuance of license for telecommunication services involving fixed-phone operations, mobile phone operations, internet service, and satellite broadcasting operations.
- ▶ In particular 5G frequencies involving telecommunication technology are proposed to be sold by auction.

Vehicular Fees and Levies

Introduction

It is proposed that three new fees/ penalties will be imposed in respect of motor vehicles:

1. Imposition of a fee on vehicles meeting with motor traffic accidents.
 - ▶ The insurer would reimburse this fee through vehicle insurance.
 - ▶ The intention of this levy is to disincentivize irresponsible driving and reduce the number of vehicular accidents.

2. It is proposed that a fee would be levied on the modernization, modification or upgrading a vehicle.

Possible implications and insights

At present, the Motor Traffic Act (as amended) stipulates that no person shall knowingly use an adapted or modified motor vehicle other than in conformity with an approved prototype. In the event that such provision is contravened, the party shall be guilty of an offence and/ or subject to a fine (with increasing penalties for repeat offenders). The imposition of the levy of vehicle modernization, modification or upgrading appears to mirror such provisions.

3. Authorization of Illegal Vehicles

Unauthorized, road-worthy vehicles, namely motor cars and motor cycles, would be legalized through registration, in the event that a penalty or fine is paid during an amnesty period.

Further, all vehicles seized by Sri Lanka Customs due to non-payment of taxes, or for other reasons, will be released subject to the payment of applicable taxes and a fine.

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Tax administration



Strengthening Large Tax Payer's Unit

It is proposed to further strengthen the consolidated Large Tax Payer Unit (LTU) and Upper Corporate Unit (UCU) of the IRD by bringing in an integrated administration of all the units connected to 80% of the government tax revenue which is derived from 20% of the tax payers.

Addressing deficiencies within the Digitized Platforms of Revenue Agencies

While the Revenue Administration Management Information System (RAMIS) was launched by the IRD in 2018 the full implementation of same has been slow due to various reasons including COVID. It is proposed that expeditious measures are taken for full implementation of RAMIS.

Further, a Single Window System will be established to facilitate the import - export process by integrating all institutions that work with Sri Lanka Customs into one system.

Strengthening tax administration at Excise Department

It is proposed to expedite the implementation of the digital revenue collection platform of Excise Department.

It is proposed to simplify the process of obtaining a liquor license.

Examining the accuracy of the tax documents

It is proposed to allow wherever possible, submission of digital invoices and documents as valid documents in digital tax filing with a proper mechanism in place for verification.

Strengthening efficiency of online payments

An online tax payment platform which integrates all Banks and Financial Institutions with Lanka Clear to be made an element of tax administration of the IRD

Further, it is proposed to expeditiously introduce amendments to the tax law in relation to the use of digital identification numbers and other legal requirements in this regard.

Application of Technological Processes to Tax Administration

Given that tax payers evade payment of due taxes by resorting to various mechanisms it is proposed that technological processes are introduced to strengthen collection of tax revenue. For instance, although tax evaders are sent a notice of tax assessment by IRD, there is a belief that the payment of due taxes can be evaded/postponed by payment of such penalties.

In order to change such practices it is expected to introduce legal provisions to apply technological processes to tax administration activities.

Revisions to the HS Code System

It is proposed to avoid deficiencies that occur or can occur in charging custom duties by updating the HS code system currently being used by Sri Lanka Customs, while also introducing advanced technological tools globally used in customs operations.

Other Reforms



- Public sector retirement age increased to 65 years
- Foreign direct investment conditions to be relaxed
- Foreign currency conversion and transfers to be relaxed for exporters through a special Finance Bill
- Agriculture sector to be increased for the use of organic fertilizer and non-toxic weedicides

Global Tax Rates



Corporate income tax rates in selected countries in 2020

Europe-America

Country	Last year rate (%)	Current year rate	Movement in comparison to 2021
Ireland	12.5	12.5	0
Germany	15	15	0
UK	19	19	0
Finland	20	20	0
Portugal	21	21	0
USA	21	21	0
Switzerland*	21	21	0
Sweden	21.4	20.6	-0.8
Denmark	22	22	0
Norway	22	22	0
Italy	24	24	0
Austria	25	25	0
Netherlands	25	25	0
Belgium	25	25	0
France*	31	27.5	-3.5

* Conditions may apply

Asia-Pacific

Country	Last year rate	Current year rate	Movement in comparison to 2021
Singapore	17	17	0
Taiwan	20	20	0
Thailand	20	20	0
Vietnam	20	20	0
Japan	23.2	23.2	0
Malaysia	24	24	0
Sri Lanka	24	24	0
Indonesia*	25	22	-3
Korea	25	25	0
China	25	25	0
New Zealand	28	28	0
Pakistan	29	29	0
Australia	30	30	0
Philippines*	30	25	-5
India*	30	30	0

■ Current Year Rate (%)

■ Change (%)



Personal income tax rates in selected countries in 2020

Europe-America

Country	Last year rate	Current year rate	Movement in comparison to 2021
Norway	16.2	16.2	0
Brazil	27.5	27.5	0
Luxembourg	45.78	45.78	0
Finland	31.25	31.25	0
USA	37	37	0
Ireland	40	40	0
Germany	45	45	0
Italy	43	43	0
Spain	45	47	2
UK	45	45	0
Belgium	50	50	0
Netherlands	49.5	49.5	0
Austria	55	55	0
Denmark	56.5	56.5	0

Asia-Pacific

Country	Last year rate	Current year rate	Movement in comparison to 2021
Sri Lanka	18	18	0
Singapore	22	22	0
Malaysia	28	30	2
India	30	30	0
Indonesia	30	30	0
Pakistan	35	35	0
New Zealand	33	39	6
Philippines	35	35	0
Thailand	35	35	0
Vietnam	35	35	0
Taiwan	40	40	0
Korea	42	45	3
Australia	45	45	0
Japan	45	45	0
China	45	45	0

■ Current year rate

■ Change

Capital Gain Tax (CGT) in selected countries in 2022

Europe-America

Country	Last year rate	Current year rate	Movement in comparison to 2021
Ireland	33	33	0
Belgium	29	29	0
Netherlands	25	25	0
Austria	25	25	0
Greece	24	22	-2
Italy	24	24	0
Norway	22	22	0
Denmark	22	22	0
Sweden	21.4	20.6	-0.8
USA	21	21	0
Portugal	21	21	0
Finland	20	20	0
UK	19	19	0
Germany	15	15	0

Asia-Pacific

Country	Last year rate	Current year rate	Movement in comparison to 2021
Australia	30	30	0
Cambodia	20	20	0
China	25	25	0
India	20	20	0
Japan	23.2	23.2	0
Korea	25	25	0
Malaysia	30	30	0
Myanmar	10	10	0
Pakistan	15	15	0
Philippines	6	6	0
Sri Lanka	10	10	0
Taiwan	20	20	0
Thailand	20	20	0
Vietnam	20	20	0

■ Current year rate

Corporate Tax at a Glance



Tax rates

Description	Rate
Standard tax rate	24%
Small and Medium Enterprise (excluding betting and gaming and liquor)	14%
Sale of goods including exports for foreign currency	14%
Entrepot trade	14%
Offshore business without bringing goods to Sri Lanka	14%
Front end services to clients abroad	14%
Headquarter operations of leading buyers for management of financial supply chain	14%
Logistic warehouses including bonded warehousing	14%
Transshipment operations	14%
Freight forwarding	14%
Supply of services to an exporter of goods or services or to foreign principle for payment in foreign currency - including agent of a ship operator	14%
Manufacture and supply to an exporter of non-traditional goods	14%
Ship repair/refurbishment of marine cargo containers for payment in foreign currency	14%
Provision of computer software, programs or systems or recording computer data for payment in foreign currency	14%
Sale of gem or jewelry in foreign currency made in Sri Lanka	14%
Sale of goods manufactured in Sri Lanka by a BOI company as import replacement	14%
Educational services	14%
Promotion of tourism	14%
Construction Services	14%
Agro Processing	14%
Health care services	14%
Sale of health protective equipment by a BOI company to specified government bodies	14%
Gem and jewelry	14%
Manufacturing	18%
Betting and gaming	40%
Manufacture and sale or import and sale of any liquor or tobacco product	40%
Dividend received from a resident company	14%

Note: Reduction of tax payable

A company which lists between January 1, 2020 and December 31, 2021 - tax payable reduced by 50%

Agro processing using self farmed agro produce -25% of reduction on tax payable(for 5 years)

Exemptions

Description
Interest derived by a Charitable Institution, which is applied solely for providing care for children, elderly or the disabled in a home maintained
Interest earned by a person outside Sri Lanka on a loan granted to a person in Sri Lanka or the Government of Sri Lanka
Interest earned by a person from foreign currency account opened any commercial Bank or in any specialized bank with the approval of Central bank after January 1, 2021
Interest earned by a person from term deposit account titled Special Deposit Account opened on or after April 8, 2020
Interest earned by any welfare society after April 1, 2021
Interest earned by any multi national company on any deposit opened and maintained in foreign currency to cover import expenditure on or after April 1, 2021
Income (Interest and realized gain) earned by any non-resident (other than Sri Lankan permanent establishment) from sovereign bond denominated in local or foreign currency
Income earned by any person from sovereign bond denominated in foreign currency including Sri Lanka Development bonds
Gain derived by a Commercial bank or authorized dealer from the realization of Sri Lanka International sovereign bonds where an investment of not less than USD100Mn made on or after April 1, 2021
Any winning from a lottery which does not exceed Rs.500,000/-
Gain made on realization of an asset consisting of shares quoted in CSE
Dividends distributed prior to January 1, 2020 out of dividends received which has been subjected to deduction of tax
Dividends distributed after January 1, 2020 out of dividends received from another resident company
Dividends distributed to a non resident person
Dividends distributed by certain companies identified in terms of part IV of the Finance Act. No 12 of 2012 in relation to Hub regulations
Dividends and gains received by any person from the realization of shares in non-resident company with more than 10% ownership or control
Dividends and gains on the realization of units or amounts derived as gains from the realization of capital assets from real estate investment trust (REIT) listed in CSE

Exemptions (Cont.)

Description
Amount derived from the sale of gem through an auction conducted by NG&J Authority, on which tax has been deducted
Any gains and profits from the sale of produce from agro farming commencing from April 1, 2019 - Exempt (5 years)
Any gains and profits from providing Information Technology and enabled services on or after January 1, 2020
Any gains and profits from services rendered in or Sri Lanka and utilized outside Sri Lanka and payment remitted to Sri Lanka in foreign currency through a bank on or after Jan 1, 2020
Any gain and profits which has a foreign source and remitted to Sri Lanka in foreign currency through a bank on or after Jan 1, 2020
Any gain or profits from export of gold, gem or jewellery or cutting and polishing of gems where income is earned in foreign currency after April 1, 2021
Any amount derived by a non-resident after January 1, 2020 from laboratory services or standards certification
Gains and profits from business to recycle materials used in the construction industry after April 1, 2021 - Exempt (10 years)
Gains and profits from the business of manufacturing boats or ships by resident person - Exempt (7 years)
Gains and profits from the business of any renewable energy project with a capacity to produce not less than 100 mega watts of solar or wind power and supplied to the national grid - Exempt (7 years)
Gains and profits from business by a resident person from constructing and installing communication towers and provision of related technical services after January 1, 2021 - Exempt (5 years)
Gains and profits from the business by an undertaking for letting bonded warehouse or warehouses related to offshore business in the Colombo or Hambanthota port

Capital Allowance

Class of Asset	Description of Asset	No of Years
1	Computers and data handling equipment together with Peripheral devices.	5
2	Buses and minibuses, goods vehicles; construction and earthmoving equipment, heavy general purpose or specialized trucks, trailers and trailer mounted containers; plant and machinery used in manufacturing	5
3	Rail road cars, locomotives, and equipment; vessels, barges, tugs, and similar water transportation equipment; aircraft; specialised public utility plant, equipment, and machinery; office furniture, fixtures, and equipment; any depreciable .asset not included in another class.	5
4	Buildings, structures and similar works of a permanent nature	20
5	Intangible assets, excluding goodwill	The actual useful life of the intangible asset, or where the intangible asset has an indefinite useful life, 20
6	Milking machines with latest technology, used to manufacture local liquid milk related products	2

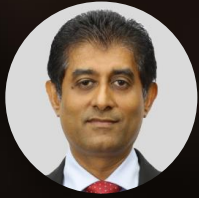
Qualifying Payments

Type of qualifying payment	Conditions	Eligibility (maximum deduction)
In money to an approved charitable institution	a charitable institution established for the provision of institutionalized care for the sick or the needy and declared by the Minister as an approved charitable institution.	One-fifth of the taxable income of the entity or Rupees five hundred thousand, whichever is less;
In money or otherwise to Government	A local authority - any Higher Education Institution established or deemed to be established under the Universities Act, No. 16 of 1978 - the Buddhist and Pali University of Sri Lanka or any Higher Educational Institution established by or under the Buddhist and Pali University of Sri Lanka Act, No. 74 of 1981 - a fund established by the Government of Sri Lanka; - a fund established by a local authority and approved by the Minister.	100% of the donation
Any financial institution	Cost of acquisition or merger of any other financial institution where such cost is ascertained by considering all the facts on case-by-case basis and as confirmed by the Central Bank of Sri Lanka.	Deductible expenditure shall be apportioned in equal amounts over a period of three years of assessment and be deductible

Personal Tax at a Glance

Individual Income Tax Chart

Description	2022/2023
Tax Free Allowance (Resident or citizen)	Rs.3,000,000
Tax Rates	First Rs.3,000,000 - 6%
	Second Rs.3,000,000 - 12%
	Balance - 18%
Rates for Terminal Benefits	Not exceeding Rs. 10,000,000 - 0%
	Rs. 10,000,000 - Rs. 20,000,000 - 6%
	Exceeding Rs. 20,000,000 - 12%
Capital Gains Tax	10%
Qualifying payment relief	
Health expenditure including contributions to medical insurance	Rs. 1,200,000 in the aggregate per annum
Educational expenditure incurred locally for such individual or on behalf of his children	
Interest paid on housing loans	
Contributions made to an approved pension scheme	
Investment in Government Securities and shares of listed companies	
Exemptions	
Interest or discount earned by any person from any sovereign bond denominated in foreign currency including Sri Lanka Development Bonds	Exempt
Rental income	
By a resident individual (from an investment)	25% deduction available



Mr. Duminda Hulangamuwa
Partner,
Head of TAX Services
Ernst & Young, Sri Lanka and Maldives
duminda.hulangamuwa@lk.ey.com



Mr. Sulaiman Nishtar
Partner, TAX
Ernst & Young, Sri Lanka
sulaiman.nishtar@lk.ey.com



Ms. Roshini Fernando
Partner, TAX
Ernst & Young, Sri Lanka
roshini.fernando@lk.ey.com



Ms. Shehani Paranavitane
Prinsipal, TAX
Ernst & Young, Sri Lanka
Shehani.Paranavitane@lk.ey.com

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