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Parliament passes new Foreign Exchange Act

Executive summary

All foreign exchange transactions were governed by the Exchange Control Act, No. 24 of 1953 and regulations and directives issued under such Act. On 25 July 2017, the Parliament passed the Foreign Exchange Act. This new Act which is yet to receive the certification of the Speaker has been analysed by us based on the Foreign Exchange Bill presented to Parliament and amendments made at Committee Stage in Parliament. The salient features of the new Act include:

Let's talk

If you believe you may be affected by the outcome of this law, we would be happy to assist you in reviewing any contracts / agreements you have entered into with offshore persons to identify any potential exposure.

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- ▶ Provision of amnesty for inward remittances which were previously not declared.
- ▶ The now repealed Exchange Control Act prohibited any payment of money out of Sri Lanka except with the approval of the Central Bank. The current transactions were permitted only because of a directive issued by the Central Bank to the authorized dealers. In contrast, the new Act expressly permits current transactions.
- ▶ Similar to the repealed Exchange Control Act, capital transactions are restricted and similar relaxation of such restrictions are expected by way of regulations under the new Act.
- ▶ Special permission for foreign exchange earners to deal in current and capital transactions.
- ▶ Introduction of an appeal process where an authorized dealer refuses to deal in foreign exchange for a current or a permitted capital transaction.
- ▶ Rs. 1 million penalty on persons other than authorized dealers for violating the new Act.
- ▶ Directors, members and partners personally liable for penalties unless it is proved that the violation was without their knowledge or that such person exercised due diligence.

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Detailed discussion

1. Date of operation

The Act will come into operation on such date as ordered by the Minister in a Gazette ("the appointed date")

2. Repeal of the Exchange Control Act, No. 24 of 1953

The Exchange Control Act (Chapter 423) is repealed with the new Foreign Exchange Act. Notwithstanding the repeal of all suits, actions and proceedings instituted under the repealed Act and pending on the day immediately prior to the appointed date shall be deemed to be such actions and proceedings instituted under the repealed Act and will be heard and concluded under the repealed Act.

Further, all investigations and inquiries instituted under the repealed Act and pending on the day immediately prior to the appointed date, shall be deemed to be investigations and inquiries instituted under the repealed Act and shall be concluded under the repealed Act within a period of six months from the appointed date.

3. Purpose of the Foreign Exchange Act

The new Foreign Exchange Act is introduced to provide for the promotion and regulation of foreign exchange and to vest the responsibility of promoting and regulating the foreign exchange in the Central Bank.

4. Authorized Dealers, Restricted Dealers and Other Dealers

Licensed commercial banks and licensed specialized banks will function as "Authorized Dealers" to deal in foreign exchange. The Central Bank may appoint any person as "Restricted Dealer" to deal in foreign exchange as per the authorizations in the permit. The Central Bank may also grant special permission to any person who is not an authorized dealer or a restricted dealer, to deal in foreign exchange for specific purposes, as may be prescribed by the Minister by order published in a Gazette.

5. Current transactions

The Central Bank, under the previous Exchange Control Act, permitted authorized dealers to allow foreign remittances out of Sri Lanka for current transactions, provided that the authorized dealer satisfied the bona fide nature of the transaction. This liberalization of current transactions is continued in the new Act. A noteworthy feature of the new Act is the appeal process, where the bank refuses to deal in foreign exchange for a current transaction. The new Act also provides for a definition of current transactions as follows;

"Any international transaction necessitating a transfer of foreign exchange into or from Sri Lanka and referred to in Article XXX(d) of the International Monetary Fund (IMF).

Article XXX(d) of the IMF states that payments for current transactions means payments which are not for the purpose of transferring capital assets, and includes, without limitation -

- a) all payments due in connection with foreign trade, other current business, including services, and normal short term banking and credit facilities;*
- b) payments due as interest on loans and as net income from other investments;*
- c) payments of moderate amount for amortization of loans or for depreciation of direct investments; and*
- d) moderate remittances for family living expenses"*

6. Capital transactions

Under the previous exchange control regime, special Gazette notifications were published whenever the bank wished to liberalize certain capital transactions. Limits and conditions were always attached to such special permission.

The new Act too seeks to control capital transactions in a similar manner. There is no general permission given in the new Act for capital transactions. Authority is given to the Minister in consultation with the Monetary Board and with the approval of the Cabinet of Ministers to issue regulations permitting certain capital transactions.

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It is presumed that new regulations will be issued on capital transactions and the existing regulations will cease to exist. Whether the new regulations will have the same limitations and conditions that previously prevailed cannot be commented upon at this point in time. The continuity of the following regulations is uncertain at this point in time;

- a) Minimum investment requirement of US\$ 1 million if investing in a company engaged in retail trade
- b) Requirement to bring in US\$ 100,000 if registering an overseas office which is engaged in commercial operations
- c) Minimum investment requirement of US\$ 2 million if an overseas office is to engage in retail trade
- d) The cap of US\$ 100,000 for a Sri Lankan company purchasing shares of a foreign entity (other than with the funds in the Foreign Exchange Earners Account ("FEEA"))

Whatever the new regulations may entail, it is expected that these new regulations would be issued almost immediately upon passing the new Act so as not to disrupt foreign investments into the country.

It is expected that the regulations will provide for the manner in which to channel the capital investments. The continuity of key accounts such as the Securities Investment Account ("SIA") will be dependent upon such regulations.

A capital transaction is defined to mean a transaction which is not a current transaction within the meaning of the Act.

7. Powers of authorized dealers

It is mandatory for an authorized dealer to request for documents and other information as is reasonably necessary in order to satisfy himself that the requirement is in relation to a current transaction or to a permitted capital transaction. Where such information is not provided or the authorized dealer is not satisfied that the remittance is for a current transaction or a permitted capital transaction, the authorized dealer can refuse the remittance of money.

8. Right to reasons

Where the authorized dealer refuses to deal in foreign exchange in relation to a current transaction or a permitted capital transaction, the aggrieved person can request for the reasons for the refusal in writing.

9. Right to appeal

The aggrieved person can appeal to the Central Bank within 14 days after such decision is communicated to such person. The Central Bank, after giving such person and the authorized dealer a reasonable opportunity of being heard, can affirm, vary or revoke such decision.

10. Exemption for foreign exchange earners from current and capital payments

Despite the restrictions and limitations on capital transactions, the previous exchange control regime allowed certain exemptions for foreign exchange earners. As such, foreign exchange earners were permitted to engage in capital transactions without restrictions though the FEEA.

The new Act too affords exemptions to foreign exchange earners. Accordingly, any person who

- a) holds foreign exchange in a bank account in Sri Lanka or outside Sri Lanka; or
- b) owns any foreign asset,

may utilize such foreign exchange or foreign asset for making of any payment for, or in respect of, any current or capital transaction of such person, within or outside Sri Lanka, through an authorized dealer.

It is unclear at this point whether such investments must continue to be channeled through the FEEA in order to avail the exemption.

11. Possession of foreign exchange

Regulations will be issued specifying the limits and other conditions of holding foreign exchange in a person's possession or in a bank account in Sri Lanka.

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12. Export and import of currency

Regulations will be issued specifying the limits and other conditions of export and import of foreign currency or Sri Lankan currency.

13. Amnesty for inward remittances

Application of the amnesty

Any Sri Lankan citizen resident in Sri Lanka, who remits to Sri Lanka any foreign exchange which has not been declared to the Commissioner General of Inland Revenue ("CGIR") or to the Head of the Department of Foreign Exchange before the appointed date, is granted amnesty.

What is the amnesty

- ▶ Any such person, who remits to Sri Lanka, such foreign exchange before the appointed date is liable to pay only a 1% Remittance Fee to the CGIR. No other fee, tax, surcharge, levy or penalty will be imposed.
- ▶ The Remittance Fee of 1% will only apply for amounts remitted in excess of US\$ 1 million. Therefore, up until US\$ 1 million, there will be absolutely no fee, tax, surcharge, levy or penalty.
- ▶ Where the amount exceeds US\$ 1 million there will be no Remittance Fee (of 1%), other fees, tax, surcharge, levy or penalty, if such funds are invested in development bonds issued by the Government of Sri Lanka.

Other benefits - Relief under the Prevention of Money Laundering Act, No. 5 of 2006

The Prevention of Money Laundering Act, deems property to be acquired from an unlawful activity (until the contrary is proved) if, such property cannot or could not have been a part of the known receipts of a person.

The Foreign Exchange Bill states that any property to which the amnesty applies shall not be deemed to be the property obtained by the commission of an offence under the Prevention of Money Laundering Act, even if such foreign exchange had been held outside Sri Lanka without the permission of the Central Bank.

Therefore, whilst action could still be instigated under the Prevention of Money Laundering Act, the Foreign Exchange Bill does away with the guilty presumption. Therefore, the burden of proof shifts to the authorities.

Disqualifications

The property cannot be property in respect of which proceedings are pending in a court of law or Convention of the Suppression of Terrorist Financing Act, No. 25 of 2005 or the Bribery Act (Chapter 26) or an order has been made by a court of law under the Prevention of Money Laundering Act, No. 5 of 2006. Such property will not be eligible for the amnesty.

Application of the Bribery Act

There is no relief given from the application of the Bribery Act.

Amnesty period

The amnesty applies to foreign exchange that is remitted, which have not been declared to the CGIR or the Head of the Department of foreign exchange, before the appointed date.

The "appointment date" is the date in which the Act comes into operation, as will be published in a Gazette. Therefore, in order to enjoy the amnesty, it is presumed that the foreign exchange will have to be brought in before this "appointed date".

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14. Penalty for violations

Violations by authorized dealers

Where an authorized dealer or a restricted dealer fails to comply with the provisions of the new Act, or any regulation, order, directive or guideline issued under the new Act, the Central Bank may, with the approval of the Minister, issue a notice directing such authorized dealer to comply.

Where the authorized dealer fails to comply even after such notice is issued, the Central Bank has the authority to suspend the license issued to the authorized dealer to deal in foreign exchange. Subsequent to the suspension, the authorized dealer will be given an opportunity to be heard. Thereupon with the approval of the Monetary Board, the Central Bank has the power to revoke the permit given to such authorized dealer.

Alternatively, without suspending the license, the Central bank may impose a penalty not exceeding the amount or value of such foreign asset or any part thereof in foreign exchange or Sri Lankan currency, together with such expenses incurred by the Central Bank for the detention and investigation of such transaction; or impose a limitation in dealing in current or capital transactions in relation to foreign exchange for a period not exceeding 12 months.

Appeals in relation to the above can be made to the Board of Inquiry. The procedure relating the Board of Inquiry is prescribed in the Act.

Violations by those other than authorized dealers

The Central Bank, upon informing the Minister, may impose a penalty not exceeding Rs. 1 million or to pay a penalty of an amount not exceeding the amount or value of such current transaction or capital transaction, or value of such foreign asset. Prior to imposing this penalty the Central Bank must give the person a reasonable opportunity of being heard. Appeals in relation to this can be made to the Board of Inquiry within 30 days after being communicated of the penalty.

Personal liability of directors, members and partners

Where a penalty is imposed on a body (whether incorporated or unincorporated), every director, member or partner shall also be personally liable (jointly or severable) to pay such amount.

If the director, member or partner wishes to be absolved of this liability, such person must prove that the act or omission was done or omitted to have been done without the knowledge of such person or that such person exercised due diligence to prevent such act or omission.

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