THE BUDGET FOR 1986- REVENUE PROPOSALS

Yasapala Karunasinghe *(Tax Consultant)*

Although the Final Estimate for 1985 set a target of a budgetary surplus of Rs. 1.7 bn, it has not been possible to achieve this due mainly to the unfortunate events in the North and the East.

The estimated gross expenditure of Rs. 59 bn. for 1985 has shot up to Rs.65 bn pushing the overall deficit from Rs.22 bn to Rs. 29 bn. This deficit is expected to be financed from:

* non-inflationary rupee loans,
* foreign aid- grants and loans, and
* borrowing from the banking system.

The Draft Estimates for 1986 reflect:

Gross Expenditure (Recurrent Rs 37 bn + Capital Rs. 30 bn) = Rs. 67 bn.
Revenue = Rs. 37 bn.

This results in a budget deficit of Rs.28 bn, after adjustments for Savings on Recurrent Expenditure and Advance Account Net Lending. As a percentage of the GDP it is around 15% which is slightly less than the deficit for 1985, which is now likely to be about 17%.

The estimated revenue of Rs. 37 bn is to be raised out of the proposals contained in the Budget Speech delivered on 13.11.1985 which are as follows:

INCOME TAX

Personal Income Tax

a) Reduction of maximum rate for individuals:
from 55% to 50%

Comparative position

Y/A 1979/80	YY/A 1980/81 - 85/86	from Y/A 1986/67 (proposed)
70%	55%	50%

b) Increase of exemption limit for individuals:
from Rs. 24,000 to Rs 27,000

Comparative position

YY/A 1979/80 to 80/81	Y/A 84/85	Y/A 85/86	from Y/A 86/87 (proposed)
Rs.12,000	Rs.18,000	Rs.24,000	Rs.27,000

This measure does not apply to non-resident individuals nor expatriate employees in the first three years.

c) Reduction of the tax bands for individuals:
from 11 to 5

Comparative position

Up to Y/A 1979/80	YY/A 80/81 -85/86	from Y/A 86/87 (Proposed)
14	11	5

SEE ADDENDUM FOR COMPARATIVE TAX TABLES AND CUMULATIVE TAX TABLES

The application of the highest marginal rate over the years in respect of individuals has been as follows:

Up to Y/A 79/80	Y/A 80/81 - 83/84	Y/A 84/85	Y/A 85/86	Y/A 86/87 (proposed)
Rs.86,400	Rs.64,800	Rs.84,000	Rs.126,000	Rs.120,000

Given below are the other Tax Tables consequential to the proposals, along with existing Tables to facilitate comparison:

1. Hindu Undivided Families

Existing	Rate	Proposed	Rate
YY/A 1979/80 - 84/85		from Y/A 1986/87	
Taxable income lst Rs.25,000		1st Rs.25,000	30%
next Rs.25,000	40%	next Rs.25,000	40%
next Rs.25,000	50%	balance	50%
next Rs.25,000	60%		
balance	70%		

2. Trustees including Trustees under last wills

Existing	Rate	Proposed	Rate
YY/A 1979/80-84/85		from Y/A 1986/87	
Trusts created before 15.11.1978 on taxable income	50%	on all Trustees taxable income	50%
Trusts created after 15.11.1978 on taxable income	55%		

(Revenue loss from above changes : Rs. 150 mn)

d) Reduction of the quantum of qualifying payments:
from Rs. 500,000 to Rs.150,000

Note: Qualifying payments fall into 2 categories:

i) those limited to 1/3rd of assessable income, and
ii) those qualifying for 100% deduction from the assessable income, any unabsorbed amount in one year being carried forward to the next year.

Consequent on the proposal contained in the Budget Speech for 1985, the deduction was limited to 1/3rd or Rs.500,000 whichever is less and the aggregate of deductions under both categories was not to exceed Rs.500,000 in the case of any person other than a Company - Amendment Act No. 16 of 1985.

The proposal in the 1986 Budget is to further limit these deductions to-
1/3rd or Rs. 150,000 whichever is less and the aggregate of deductions not to exceed Rs.150,000.

This restriction does not apply to donations to the Government

(Additional revenue anticipated : Rs 50 mn.)

e) Deduction of 20% tax at source on interest accruing on Fixed Deposits in Banks and Financial institutions.

The proposed deduction is similar to that which is now applicable to dividends by a Company.

The institutions concerned are required to deduct from the interest payable by them on or after 01.04.1986 on any deposit with them by a person in his own name or another at 20%.

The term "interest" has been defined in the Inland Revenue (Amendment) Bill as meaning "such part of the interest received by a person chargeable with income tax from bank or financial institution as is not exempt from income tax or in respect of which no deduction has been made under Section 81 (interest payable to person outside Sri Lanka).

As in the case of a Divident Warrant, the institution is required to issue to the person who is in receipt of interest a statement setting out the particulars of the gross interest, the amount, the period and the net amount paid.

On the production of the said certificate the taxpayer will be able to claim a deduction of the sum shown therein from the tax payable by him and claim a refund if the amount exceeds the tax payable.

There is provision in the Bill for the issue of directions to the institutions, (as in the case of PAYE, now) to make necessary adjustments in the deductions.

The institution is required to remit to the Commissioner General, Inland Revenue the sum so deducted before the 15th of the month following the month in which the deduction was made.

The Minister stated in the course of his Budget Speech that the depositor will be required to state on the application for a deposit, his income tax file number and the National Identity Card Number and whether or not he is liable to income tax.

Where the applicant declares that he is not liable to income tax, the institutions would not be obliged to deduct any tax on the interest paid. However, the Inland Revenue officials would be making random checks to ascertain the veracity of the declarations.

The rationale behind the introduction of this new feature into the tax structure is the apparent non-disclosure of interest income by taxpayers to accord with nearly Rs.30 bn. in fixed deposits.

(Additonal revenue envisaged from this measure: Rs.250 mn for a start).

HEALTH TAX

No changes are proposed.

The exemption limit and rates as proposed in the 1985 Budget and embodied in the Inland Revenue (Amendment) Act No. 16 of 1985 will continue.

Being a capital tax, Wealth Tax is being retained (see below Estate Duty andGifts Tax):

1) to enable the Department of Inland Revenue to keep a taxpayers's assets in relation tohis income as declared in his consecutive Returns, and

2) to encourage taxpayers to switch from unproductive investments to productive areas because of the annual levy on the former.

CORPORATE TAX

No changes are proposed in general other than in respect of Public Corporations and Government Owned Business Undertakings

This means that the basis of taxation of Companies imposed by the Inland Revenue Act No. 28 of 1979 as amended from time to time ending in the Amendment Act no. 16 of 1985 will continue. In summary the position is:

i) Public companies: a) 50% of taxable income
b) 20% of gross dividend distributed out taxable income of the Year of Assessment.

ii) Small companies: where the taxable income does not exceed Rs. 250,000/=

On the 1st Rs.50,000	20%
next Rs.100,000	30%
balance	40%

iii) small companies which are quoted public companies: where the taxable income does not exceed Rs.250,000 same rates as those for small companies under ii) above.

iv) small companies which are not quoted public companies:

where the taxable income exceeds Rs. 250,00

on the 1st Rs.50,000	20%
next Rs.100,000	30%
next Rs.100,000	40%
balance	50%

v) quoted public companies: 40 of taxable income

iv) people's companies: 40% of taxable income

vii)non-resident companies: a) 50% of taxable income
b) remittance upto a maximum of 1/9 th of taxable income.

Public Corporations and Govt. Owned Business Undertakings:

These institutions are now required to pay dividends on their profits to the Treasury. The proposal is to require the Department of Inland Revenue to levy a "deemed dividend tax" on after-tax profits at 25%.

(Anticipated revenue: Rs 250 mn)

Ceylon Petroleum Corporation

A special levy of Rs. 358 mn is to be imposed for the year 1986 out of its profits in addition to what it normally pays the Treasuary.

(Anticipated revenue: Rs. 358mn)

Limitation of Liability to Income & Wealth Taxes

The Present limit to which a "person" liable to pay these two taxes is 80% of assessable income. This limit was set when the maximum rate of income tax was 70% (Year of Assessement 1979/80).

The proposal is to reduce the limit from 80% to 60% in keeping with the reduction of the maximum rate to 50% with effect from the Year of Assessment 1986/87.

CAPITAL TAXES

To this category fall: i) Wealth Tax, and
ii) Capital transfer taxes- i.e. Gifts Tax and Estate Duty.

The proposal is to continue the Wealth Tax while abolishing the Gifts Tax and Estate Duty with efffect from 14.11.85.

The rationale behind the proposal is that the annual yield from these two taxes is not commensurate with the cost of collection.

The relevant figures for 1984 are:

Wealth Tax: 44mn
Gifts Tax : 11 mn
Estate Duty: 23mn.

Vey significant changes were introduced in the Budget for 1985 in relation to the two latter levies.

The salient features of these changes were:

* exemption of the first Rs.250,000 of all taxable gifts and net value of estate.
  Upto Y/A 1984/85 the exemption was the first Rs.50,000 of taxable gifts and Rs.100,000 of the net value of the estate.
* reduction of the maximum rate of both these levies from 65% and 70% respectively to 50%.

The relevant laws will apply to gifts made by individuals and Companies or estates of individuals upto 13.11.1985..

(Revenue loss : Rs. 15mn)

EXCISE DUTIES

a) Tobacco: * increase from Rs.371 per Kg. to Rs. 603.50 per Kg.
  * reduction of Turnover Tax from 40% to 20%.
    - net increase in duty on a Kg. of tobacco: Rs.47.50
    – average increase in the price of a cigarette: Cts.05
  Customs Duty on tobacco and cigarettes is correspondinglv increased.
  (Additional revenue Rs 290 mn)

b) Beedi leaves: increase of Customs Duty from Rs.10 per kg. to Rs. 30 per kg.
  - average increase in the price of a beedi: 01 cent.
  (Aditional revenue: Rs. 80 mn)

c) Liquor: : increase are as follows:-

alcoholic beverages other than locally) from Rs.55/40
produced foreign type and those from) per litre to
coconut based alcohol) Rs.65/40 per

alcoholic beverages from coconut) from Rs.61 per
based alcohol.) litre to Rs.71 per
locally produced foreign type)from Rs.73 per
e.g.local brandy, gin etc.) to Rs.80 per litre.

Customs Duty on imported liquor is correspondingly increased. - increase in the price of a bottle of arrack is Rs. 5.

(Additonal revenue: Rs.180mn).

d) Ethyl alcohol (used for manufacture of alcoholic beverages, pharmaceuticals, perfumes, cosmetics etc)

Proposed Duty:-

a) used for manufacture of pharmaceuticals) by a licensed manufacturer)Rs.1.15 per litre.

b) used for other industrial purposes- Rs.64/60 per litre.

TURNOVER TAX

Consequent on the Budget proposals for 1985, new rates of tax were published in Gazette Extraordinary No. 323/20 of 14.11.1984. There were 12 categories of business liable at rates ranging from 1% to 40% (10 bands).

The Budget proposals for 1986 introduced 7 categories of businesses liable at rates ranging from 1% to 20% (6 bands)- reference Gazette Extraordinary No. 375/18 of 13.11.1985 effective from midnight November 13/14, 1985.

A notable feature is the removal of the 40% band applicable to: cigarettes, gold, perfumes and Eau-de-Cologne.

Although the rate applicable to cigarettes has been brought down to 20% from 40%, the increase in Excise Duty on tobacco from Rs. 371 per Kg. to Rs. 603.50 per Kg. (see a) under Excise Duties above) has the net effect of increasing the price of a cigarette by 05 cents.

Part 1(c) of the Order published on 14.11.1984 contained items liable at 6%. The Order dated 13.11.1985 whilst removing the rate of 6%, reduced the rate of some items in the erstwhile rate band to 5% and increased the rate on certain other items to 10%.

Details are:-

a) Increase from 6% to 10% - 19 items including aerated waters.
b) Reduction from 15% to 10%- ready-made garments.
c) Unchanged at 10% - synthetic yarn and synthetic fabrics and tyres.
d) Increase from 15% to 20% - beer and electric fans.
e) Unchanged at 15% - 6 items including cement.
f) Inclusion in the 20% rate band in additon to those items which were listed in the Order dated 14.11.84 - gold, perfumes, Eau-de-Cologne (down from 4%) in addition to beer, electric fans (above).
g) Removal of 2% rate band:

   The two items pertaining to shipowners and aircraft owner which were under 2% have been included in the 3% rate band in addition to the earlier items in that band.
h) Reduction from 4% to 3% : any business using manual labour exclusively for the manufacture of any article.
i) Inclusion in the 3% rate band: new item - the business of operating an approved passenger transport service.
j) Increase from 4% to 5%; non-resident shipowners and charterers in a country with which there is a "Double Tax Agreement" under which shipping profits are not liable to tax.
k) Unchanged at 10%: the 5 classes of business (the business of accepting wages etc.) listed under Part VIII of the Order of 14.11.1984 continue under Part IV of the Order of 13.11.85.

1) Expansion of 1% rate band items: 1) the business of selling ornamental ware.......and 2) the business of running a Hotel....which were earlier listed under 5% rate band have been brought under 1% rate band in addition to the item "businesss of selling or dealing in any article or commodity... """"

Also included in this rate band is "any contract of sub-contract for supply of goods re any contract for construction work........"

NOTE: This last item was and continues to be an item in the Order under Section 50 of the T.T. Act where the T.T. has to be deducted from payments made to contractors.

(Total revenue increase from the proposal (simplification and rationalisation) anticipated: Rs. 255 mn in addition to the yield of about 10bn (1984) on the pre-budget basis).

CUSTOMS DUTIES

Textiles

Import of textiles has been under control, Salu Sala having a monopoly. Although it has not imported during the last 2 years the presence in the country of large quantities of foreign textiles had led to the belief that they are either smuggled in or are releases by manufactures of garments who are permitted to import textiles for their business. This phenomenon has led to heavy revenue losses. The proposal is to lift the import control on textiles and to impose the following duties:-

Cotton - 100% or Rs.25/= per sq. metre whichever is higher, and Synthetic Textiles 100% or Rs.40 per sq. metre whichever is higher.

(Anticipated additonal Revenue: Rs 200 mn.)

POSTAL & TELEGRAPH CHARGES

Changes effective from 01.12.1985

	from Rs. cts	to Rs. cts
Postage (local)		
Ordinary letters 30 grams or part thereof	.60	.75
post cards	.35	.50
registered letters	4.00	4.50
Air Mail		
Air Mail		
letters up to 10 grams		
group A countires -e.g.India	5.50	6.50
" B "-e.g.Singapore	6.00	7.50
" C " -e.g. Britain	7.00	8.50
" D " -e.g. U.S.A.	9.00	10.00
aerogramme to all palces	5.50	6.00
(Additional revenue: Rs 105 mn)		
Telegraph		
telegrams up to 15 words		1.00
each additional word	.15	.25
(Additional revenue: Rs 10 mn)		

STAMP DUTY ON RECEIPTS

Receipt or discharge given for any money or other property amounting to Rs.100 upwards increased from Cts.50 to Re.1.0. The Regulation under Section 69 of the Stamp Duty Act No. 43 of 1982 has been gazetted on 13.11.1985 to be effective from 14.11.1985.

(Additonal revenue: Rs. 25 mn.)

TELEPHONE CHARGES

Proposed charges are:

a) increase from .90 to Rs.1.10 per Unit.
(An "Unit" - within Colombo: 120 seconds and between Colombo and outstations (e.g. Kandy : 50 seconds.

b) charges for a call between 6 p.m. and 8 a.m. at .55 cts per call.

c) i) charge for a new connection for one on the waiting lsit increased by Rs.500 - from Rs. 7,000 to Rs.7,500

ii) charge on a person who requires a connection on priority basis Rs. 15,000/= - connection if given within a month from the date of application.

iii) a charge of Rs.250/- per applicant on the waiting list as a deposit.

(Increase in revenue: Rs.200 mn.)

AIRPORT CHARGES

The embarkation tax is increased from Rs.100 to Rs.200. This tax (Airport tax) is shared between the Airport & Aviation Services (Sri Lanka) Ltd. & Aviation Services (Sri Lanka) Ltd. and the Treasury in the proportion of 60: 40 respectively.

(Additional revenue to Treasury : Rs 20 mn.)

RAILWAY CHARGES

Increase in passenger fares:

lst Class : 30%
2nd Class: 15%
3rd Class: 08%
Season Tickets 08%

It is also proposed to increase the charge for transport of goods.

(Additional revenue : Rs. 100mn.)

Note: At the Cabinet Meeting held on 18.12.85 it was decided not to effect the proposed increases in respect of both the 3rd Class fares and Season Tickets .

EXPORT DUTIES

a) Tea In view of the presetn low prices fetched by this commodity which are not commensurate with the cost of production, relief is proposed as follows:-

i) a reduction in Export Duty:

	current	proposed
in bulk	Rs.7.00 per Kg.	Rs.5.00 per
in packets	5.50	3.50
in bags	1.50	.50
instant	12.00	10.00
green	7.00	5.00

ii) raise in the ad valorem tax threshold:

current	proposed
Rs.32.00 per	Kg.Rs.40.00 per

iii) an ad valorem tax of only 50% on teas fetching prices in excess of Rs.40.00

Note: The present ad valorem tax rebate is abolished.

(Loss to revenue Rs.460mn. A sum of Rs.100 mn is to be drawn from the Tea Stabilisation Fund to reduce the loss).

b) Coconut. Due to low prices fetched by this commodity too relief is proposed, in additon to that given in the last Budget by a reduction is Export Duty as follows:

	current	proposed
Desiccated	Rs.5,000 per mt.ton	Rs.2,500 per metric- ton
Edible copra	7,250	4,750

(Loss to be recouped from Coconut Stabilisation Fund)

c) Graphite To make this commodity more competitive in the World Market and to encourage more exports an exports Duty reduction is proposed.

current	proposed
25%per metric ton	15% per

(Loss to revenue : Rs 10mn)

GUARANTEED PRICES AND SUPPORT PRICES-AGRICULTURE

Following increase are proposed:

	current Rs.	proposed Rs.
paddy	62.50 per bushel	70.00 per bushel
cowpea	5.00 per Kg.	8.50 per Kg.
green gram	7.50	10.00
black gram	4.50	10.00
maize	3.00	4.00
soya	6.00	7.00
gingelly	6.00	7.00

SCHEME OF PENSION FOR FARMERS

The proposal is to establish a Contributory Pension Scheme for all farmers in the age group of 18-59 years.

A special rebate on monthly premia between 20% to 50% is to be given on the farmers' contribution in the first two years. This is to help the older farmers whose premia will be high. After the initial period normal premia will apply based on the age of joining the Scheme.

Besides the monthly pension, there will also be a Group Insurance Scheme to cover all contributions entitling them to a death gratuity payment between Rs.2,000 and Rs. 10,000 depending on the age of contributor.

A member disabled partially or totally before completing the minimum pension contributions needed to qualify will be entitled to a lump sum gratuity or the pension on attaining the pensionable age without further contributions. Furtehr, he will receive a disability allowance from the time of the disability.

Initial capital grant by the Treasury towards the Farmers' Pension Fund for a period of 10 yearswill be Rs.750 mn.

SUMMARY

The above proposals result in:

i) revenue increse	Rs.2,375 mn
ii) revenue decrease	Rs. 540 mn
Net increase	Rs.1,833 mn

Thus teh overall deficit of Rs. 28 bn referred to at the beginning gets reduced to Rs.26 bn after adjusting for the net increases in revenue (above) and providing for Capital Expenditure of Rs. 75 mn for the Farmers' Pension Fund and Rs.50 mn for the Price Support Scheme for minor food crops.

It is proposed to finance this deficit as follows:-

a) foreign grants	Rs.3,360 mn
b) foreign projects and commodity loans	10,840mn
c) domestic rupee loans	10,800mn
Total	Rs.25,000 mn

The balance unfinanced gap of Rs. 1,986 mn is proposed to be bridged out of borrowing from the banking system.

It is also proposed to increase the borrowing limit on Treasury Bills from Rs.23,000 mn to Rs.25,000 mn.

COMPARATIVE INCOME TAX TABLES

Y/A 1987/79

Taxable income:

lst and 2nd slabs of Rs. 1,800 -7½% and 10% respectively

next 3rd to 8th slab of Rs.3,600-12½%,15%; 20%; 25%; 30% and 35% respectively

next 9th slab of Rs. 4,800 - 40%

next 10th to 14th slab of Rs.7,200 -45%; 50%; 55%; 60% and 65% respectively

Balance -70% (15 slabs)

Y/A 1979/80

Taxable income:

lst to 8th slab of Rs. 4,800 - 7½%; 10%; 15%; 20%; 25%; 30%; 35% and 40% respectively

next 9th to 13th slab of Rs.7,200 - 45%; 50%; 55%; and 65% respectively.

balan e -70% (14 slabs)

YY/A 1980/81 .1983/84

Taxable income:

lst to 8th slab of Rs. 4,800 - 7½%; 10%, 15%, 20%; 25%; 30%; 35% and 40% respectively.

next 9th & 10th slabs of Rs. 7,200 - 45% and 50% respectively

balance 55% (11 slabs)

Y/A 1984/85

Taxable income:

lst to 8th slab of Rs. 6,000 - 7½%; 10%; 15%; 20%; 25%; 30%; 35% and 40% respectively

next 9th and 10th slabs of Rs. 9,000 - 45% and 50% respectively

balance -55% (11 slabs)

Y/A 1985/86

Taxable income:

lst to 8th slab of Rs.9,000 - 7½%; 10%; 15%; 20%; 25%; 30%; 35% and 40% respectively

next 9th and 10th slabs of Rs. 15,000 - 45% and 50% respectively

balance -55% (ll slabs)

Y/A 1986/87 onwards (proposed)

Taxable income:

lst slab of Rs. 21,000 - 10%

next, 2nd to 4th slab of Rs. 24,000 - 20% 30%; and 40% respectively

balance - 50% (5 slabs)