

A COMMENT ON TAX PROPOSALS

The Annual Budget is the instrument which charts the financial course the government in power seeks to pursue in the ensuing year to achieve its policies and programmes.

Deficit Budget have been a regular feature in Sri Lanka for decades now and the Draft Estimates for 1990 envisaged an overall deficit of Rs. 40,220 m - a gross expenditure of Rs. 103,043 m as against an estimated revenue of Rs. 61,000 m.

The revised budgetary estimates for 1989 show a deficit of Rs. 50,796 m. the gross expenditure (Capital Rs. 45,786 m and recurrent Rs. 60,294 m) against revenue receipts around Rs. 55,284 m. In a way therefore, the deficit for 1990 will be lower than that for 1989.

No major changes in the tax law are being considered at this stage in view of the appointment of the Taxation Commission. The Report of which is expected around July 1990. Probably the 1991 Budget and those that follow will take into account the recommendations of the Commission in formulating the revenue proposals for the future based on a re-structured taxation system.

The recommendations of the Taxation Commission will have an impact on the Five year Public Investment Programme (1989-1993)

which was tabled in the House by the Minister on November 15th 1989.

This Programme envisages reforms in the areas of:

- a) Public administration.
- b) Public enterprises (Publicisation & joint ventures.)
- c) Public expenditure.
- d) Industry and trade.
- e) Government procedures.

The main revenue proposals contained in the 1990 Budget are summarised below:

YASAPALA KARUNASINGHE

1. PERSONAL TAXATION

1.1 Income Tax

1.2 Tax credit on employment income for Private Sector Employees:

From the year of assessment 1990/91 an individual in receipt of employment income will be entitled to a tax credit of Rs. 900/=. In the operation of this scheme an employee whose annual employment income is Rs. 36,000 or less will not be liable to income tax. On the other hand an employee with an annual employment income of over Rs. 36,000 will be entitled to a tax credit of 900/= against the tax payable as employment income.

This credit being unrelated to the marginal rate of tax applicable, the benefit to lower income groups will be greater.

The above relief being available only to employees the present tax-free allowance of Rs. 27,000/= will continue in all other cases.

1.3 Raising of exemption limit of terminal benefits of employees:

At the present terminal benefits (Commutated pension, retiring gratuity, compensation for loss of office, provident fund balance and any sum paid at retirement from the E.T.F.) of private sector are subject to tax as follows:

The proposal is to increase the exemption level from the present Rs. 100,000/= to Rs. 200,000/=; (Revenue loss anticipated from the above 2 measures is Rs 60 m.

1.4 Qualifying Payments.

1.4.1 Persons investing in Venture Capital Companies will be entitled to qualifying payment allowance.

4.2 These are Companies to be set up for the purpose of promoting undertakings with high risks and long gestation periods for manufacture, especially for export with possible foreign funding:

3. Such approved companies will be entitled to a 10 year tax holiday.

4.4 It has not been mentioned whether the present limit of

all qualifying payments to 1/3rd of the assessable income or Rs.50,000/= whichever is lower will apply to investments in the proposed Venture Capital Companies.

4.5 It is, however, possible that they may be granted 100% relief since the intention is to encourage the promotion of such companies with a view to enhancing exports which is a crying need in the present situation of Sri Lankan

4.6 The present 5 year tax holiday scheme for the non-traditional export sector will not be extended beyond 31.03.1990 it was announced. However, this incentive is to continue in respect of ventures manufacturing for exports along with the 5 year half tax holiday immediately following the tax holiday. Where the local value added is substantial.

4.7 Although the Minister announced the discontinuance of the tax holiday in his Budget Speech a cabinet decision announced on November 30th 1989 extends it by a further one year on the representation made by the exporters. Pending the recommendation of the Taxation Commission.

1.2 WEALTH TAX

2.1 VALUATION

The valuation of immovable property has been fixed as the market value as at 01.04.1977 for wealth tax purposes

in respect of such properties acquired prior to that date.

The proposal is to adopt the current market value for all properties from 01.04.1990.

The present exemption limit of Rs. 500,000/= remains unaltered.

(Expected additional Revenue: Rs. 30 m)

2.2 PENALTIES FOR LATE

PAYMENT OF TAX

The present scheme of Self-assessment payment of tax requires such payment in quarterly instalment on or before the fixed dates. If payment is not so made the tax is deemed to be in default, attracting penalty.

In the case of a person who had enjoyed a tax holiday and becomes liable for the first time in an year of assessment, he can defer payment of tax to the November 30th following year and avoid any penalties, as the law now stands.

The proposal is to amend the law to provide for penalties deeming the tax for the preceding year as the tax on total profits inclusive of exempt profits.

(Additional revenue: Rs 775 m.)

2. CORPORATE TAX

1. QUOTED PUBLIC COMPANIES (Q P CC)

A QPC is a resident company of which shares are quoted in the official list of the

Colombo Brokers' Association or a similar body.

At present, rate of income tax on a Q P C is 40% of its taxable income while a resident Non-Q P C is 50% of its taxable income. A "Small Company" is taxed at varying rates in a progressive manner at 20%, 30%, 40% and balance at 50% depending on the quantum of issued capital and taxable income.

The Quotation of its share can be obtained if the requirements of the Colombo Brokers' Association and now the Colombo Securities Exchange (viz. the offer of a minimum of 20% of shares depending on the issued capital to the public) are met.

These Companies that fall in this category number only 177 now and only a few of them are broad-based. The proposal is to restrict the 40% tax rate only to companies satisfying the following

- 1.) have more than 200 share holders, and
- 2.) 60% or less of the issued capital only can be held by not more than 5 persons their wives or minor children directly or through nominees or where such person is a Company by Companies which are controlled by the same shareholders.

2. WITHHOLDING TAX ON DIVIDENDS

At present dividends are subject to a tax deduction at source of

20% except exempt dividends and dividends out of dividends received from other resident Companies.

The proposal is to reduce the rate from the present 20% to 15%.

(No revenue loss envisaged).

3. VENTURE CAPITAL COMPANIES

Please see 1.1.4.1 - 1.1.4.5 above.

4. INCENTIVES FOR EXPORTS

Please see 1.1.4.6 - 1.1.4.7 above.

5. PENALTIES FOR LATE PAYMENT OF TAX

Please see 1.2.2 above.

3. TURNOVER TAX

1. In terms of the new Excise Act certain luxury items are to be subject to Excise Duty. Pending the setting up of the administrative machinery to implement the new law, only a few changes have been announced in respect of the Turnover Tax on the importers and manufactures.

1.1 The present rate of 10% on the following luxury or semi luxury items is increased to 20%.

1) certain food items (eg; cheese, ham, bacon etc.)

11) electrical items (eg: record players, Fax machines Colour TV sets etc.)

111) house-hold items (eg: bidets, bath tubs floor coverings etc.)

IV) items such as pressure cookers, cameras, wall clocks

1.2 The present rate of 20% is increased to 40%.

1) electro mechanical domestic appliances (eg: vacuum cleaners, floor polishers, electric cookers etc.)

11) floor polish and wax, wall paper etc.

111) hair-driers and electrical shavers.

IV) non-industrial air conditioners, cordless tele-phones etc.

Once the new excise law is made operative the above rates will be revised since these items will be subject to Excise Duty.

1.3 The present rate of 5% stipulated in respect of business of manufacturer or importer described in part 1 order in gazette extraordinary No.432/3 of 16.2.1986 is increased to 6% w.e.f. midnight 15th November 1989.

1.4 The rate of 10% was increased to 12 1/2% w.e.f. midnight August 31st/ September 01st 1988. in respect of business of manufacturer/ importer described in Part I of 16.12.86 (above) as amended from time to time.

This rate of 12 1/2% has been increased to 15% w.e.f. midnight of 15th/ 16th November 1989 in respect of the said businesses.

1.5 Above changes will not apply to kerosene oil, fuel oil,

diesel, wheat flour and sugar.
(Additional revenue: Rs.900m)

4. CUSTOMS DUTIES

1. LIQUOR

1.1 By the Revenue Order of November 10.1989 the import duty on all varieties of liquor was raised per litre as follows:

hard	Rs. 30
soft	Rs. 10

1.2 DRY FISH

By the above mentioned Revenue Order (10.11.1989) customs duty of 10% was imposed on dry fish. This item was earlier exempt from duty.

1.3 MOTOR VEHICLES

A surcharge of 25% is imposed on the duty payable on all motor cars including station waggons.

(Additional revenue RS.139m.)

5. EXCISE DUTIES

1 LIQUOR AND TOBACCO

1.1 Excise duty on liquor and tobacco was increased w.e.f. 08.11.1989 resulting in the following price increases:

- 1) hard Liquor Rs.5.00 per bottle
- 11) beer Rs.2.25 per bottle
- 111) Cigarettes Rs.0.20 per cigarette

(Additional revenue: 840 m)

1.2 ETHYL ALCOHOL (EA)

Duty is increased as follows;

EA used for medicinal preparations containing 20% alcohol and in industrial use 25%

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 cent in 1988 and 6.8 per cent in 1989. Recourse to inflationary bank borrowings will be reduced to 0.37 per cent of GDP in 1990. This is a significant achievement in considering the earlier extensive bank borrowings which amounted to the tune of 4.5 per cent of GDP in 1988 and 1.6 per cent in 1989.

Reduced recourse to bank borrowing in 1990 will supplement the policy measures that are already in operation to combat domestic inflation and external imbalance. Among these measures, Treasury Bills have been effectively used to mobilise resources from the non-bank sector. A wide range of maturities are offered for Treasury Bills. The Treasury Bills have become more market oriented and their rates are highly competitive. In the monetary sphere the Central Bank has intensified open market operations to mop up excess liquidity in the economy. In addition, the Central Bank has imposed a partial ceiling on bank credit and 100 per cent cash margins on Letters of Credit opened for non-essential imports.

It is expected that the fiscal programme outlined in the earlier sections and the current monetary measures will help to slow down domestic inflation and to achieve a sustainable external payments balance over the adjustment period.

As Percentages of GDP (at Current Market Prices)

Revenue	20.74	21.42	18.72	21.12	21.57
Expenditure	-32.97	-32.48	-34.32	-33.75	-32.66
Recurrent	-12.94	-20.11	-20.69	-22.79	-22.75
Capital	-12.94	-11.60	-10.26	-8.41	-7.28
Lending minus repayments	-1.11	-0.77	-3.37	-2.55	-1.64
Deficit Before Grants	-12.23	-11.06	-15.60	-12.63	-10.09
Grants	2.09	2.38	2.95	2.67	2.40
Deficit After Grants	-10.14	-8.68	-12.64	-9.96	-7.69
Financing	10.14	8.68	12.64	9.9	7.69
Foreign Loans	5.05	2.91	3.20	3.12	3.72
Domestic	5.09	5.77	9.45	6.84	3.97
Non-Bank	3.40	3.97	4.89	5.24	3.60
Bank	1.70	1.80	4.55	1.60	0.37

Source: Central Bank of Sri Lanka.

EA used for other purposes 100%
 (Additional revenue from liquor & spirits : Rs.170 m)

6. POSTAL AND TELECOMMUNICATION CHARGES

A revised rate schedule is to be issued shortly. The main changes to be effective from January 1990 are:

- 1) ordinary letters and post-cards + Rs. 0.25
 - 11) registration fee + Rs.2.00
 - 111) aerogrammes & airmail letters depending on country + Rs. 2.00 - 5.00
- (Additional revenue: Rs. 125m)

2. OVERSEAS TELECOMMUNICATION CHARGES

- 2.1 The charges are being increased by 10% w.e.f. January (Additional revenue:Rs.75m)
- 1. All government departments and statutory authorities which charge fees for services which have not revised fees to reflect

the cost of such services will revise their fees effective from January 1990.

(Additional revenue: Rs.50m)

8. NON-REFUNDABLE DEPOSIT IN LIEU OF BONDS FOR PASSPORTS

- 1. The proposal is to impose a once-and-for-all non-refundable deposit of Rs.1,000/= for an "all countries" passport thus obviating the need for a guarantee bond requiring the signature of a tax payer or an employee drawing a salary of Rs.2,000 p.m. The effective date will probably be 1st January 1990.

(Additional revenue Rs.51m)

(Total increase in revenue resulting from the above proposals: RS.3,085 m)

The new expenditure proposals contained in the Budget Speech in addition to items in the Draft Estimates are:

- 1. Wages increase of Rs.200p.m. to public and local government service employees inclusive of pensioners to be effective from January 1990.

(Estimated Expenditure: Rs. 1,740-m)

- 2. Increase in the provision for interest payment on Treasury Bills shown in draft estimates by Rs.1,500m.

(Total increase in expenditure under 1 & 2 above Rs.3,240m) When the above revenue and expenditure proposals are taken in to account, in addition to the items in the Draft Estimates, the picture that emerges is that the overall deficit gets increased to Rs. 40,342 m from Rs.40,220.