

Tax Incentives, Exemptions, Reliefs and Concessions

INTRODUCTION

This chapter explains the application of the **tax incentives, exemptions, reliefs and concessions** relating to **different business activities** provided under the Inland Revenue Act No.24 of 2017.

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1. Introduction



Based on the Government policies, it has introduced a few tax incentives, exemptions, qualifying payments & reliefs and concessions. As per the Inland Revenue Act No. 24 of 2017 such items have been listed under four headings and given in the Schedules to the Act.

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| • Concessionary Tax Rates | - | First Schedule to the Act |
| • Tax Incentives | - | Second Schedule to the Act |
| • Tax Exemptions | - | Third Schedule to the Act |
| • Tax qualifying payments & Reliefs | - | Fifth Schedule to the Act |
| • Tax Concessions | - | Sixth Schedule to the Act |

This chapter of the text is to cover the tax incentives, exemptions, qualifying payments & reliefs and concessions available **on business activities** only. However, for the purpose of general knowledge the incentives, exemptions, qualifying payments & reliefs and concessions granted under the Act on non business income are also stated below in nutshell.

2. Concessionary Tax Rates (First Schedule)

The taxable income of following **companies** enjoys the concessionary tax rate of 14% on the taxable income;

- On Small and Medium Enterprises (SME),
- Exporting of goods (*whether traditional / non-traditional*) and services*,
- Agriculture business*,
- Educational services*,
- Promotion of tourism*,
- IT services*.

It is to be noted that the **individuals are not entitled** to enjoy these concessionary tax rates.

To enjoy the concessionary tax rate of 14%, **companies** engaged in these businesses shall **predominantly** (earning minimum of 80% turnover from that business) engaged in such businesses.

Small and Medium Enterprises (SME) (Sec. 195)

- Solely in Sri Lanka, other than a professionally qualified individual engaged in providing professional services individually or in partnership
- Does not have an associate entity
- Annual turnover less than Rs. 500Mn.

• **Agricultural Business (Sec. 195)**

Business of providing agricultural, horticultural or any animal produce and includes an undertaking for the purpose of rearing livestock or poultry.

• **Export (Sec. 195)**

Section 195 defines the “exports” as follows;

“Export” includes **specified undertaking**.

• **Specified Undertaking (Sec. 195)**

As per the definition given in Sec.195 of the Act a specified undertaking includes the following;

- Entrepot trading,
- Offshore business,
- Front end services to clients abroad,
- HQ operations of leading buyers for the management of financial supply chain and the Billing operation,
- Logistic services such as bonded warehouse or multi-country consolidation in Sri Lanka,
- Transshipment operations,
- Freight forwarding,
- Supply of services to exporter of goods/services or to any foreign principal,
- Production/manufacture and supply to an exporter of non-traditional goods,
- Performance of any services of ship repair, ship braking repair and refurbishment of Marine cargo containers, computer software, programmes, systems or recording Computer data, or some other gazetted services and
- Sale of gem & jewellery in foreign currencies.

Specified undertaking means (this includes entrepot trading, offshore, service exports, HQ operations, logistic services, transshipment, freight forwarding, services to exporters, production/manufacture and supply to an exporter of non-traditional goods, performance of any services of ship repair, ship braking repair and refurbishment of marine cargo containers, computer software, programmes, systems or recording computer data, or some other gazetted services and sale of gem & jewellery in foreign currencies).

- **Educational Services and tourism** are not defined.

3. Income Tax Incentives/Exemptions (Second Schedule)

As a measure of encouraging investments in to capital assets and to divert some investments in to Northern Province of Sri Lanka, several income tax incentives on new businesses based on investing in capital assets of an entity are given in the Inland Revenue Act (Second Schedule to the Act).

Under this, based on the **investment volume** and/or the **province where the investment is made** a dividend exemption, PAYE exemption on expatriate employees remuneration and in addition to the standard capital allowance (allowable depreciation) an enhanced Capital allowance has been granted. The details there on is as follows;

3.1 Enhanced Capital Allowance as an Investment Incentive

A person who invests in a new business in Sri Lanka during a year of assessment shall be granted enhanced capital allowances (in addition to the standard allowance) on **expenses incurred during that year on depreciable assets other than on intangible assets** computed as follows;

- | | |
|---|------|
| (1) If such expenses incurred is USD 3 million to USD 100 million and are used in any part of Sri Lanka other than in the Northern Province: | 100% |
| (2) If such expenses incurred is above USD 100 million and are used in any part of Sri Lanka other than in the Northern Province: | 150% |
| (3) If such expenses incurred is above USD 3 million and are used in the Northern Province: | 200% |
| (4) If such expenses are incurred by a State-owned company (>50% ownership) and the amount is exceeding USD 250 million and are used in any part of Sri Lanka: | 150% |

The above enhanced capital allowance shall be enjoyed in that year but any **unrelieved losses** there on could be carried forward for number of years as given below;

- If such investment is >USD 1,000 **or** if it is covered under item (4) above 25 years
- In other cases 10 years

However, in the event any of such asset is disposed subsequently, the consideration received in excess of tax written down value is to be treated as a taxable business income while any loss thereon be treated as an additional capital allowance claimable.

3.2 Dividend Exemption

In the case of a company invested more than USD 1,000 in depreciable capital assets **or** if it is covered under item (4) given in para 1.1.1 above (State owned with >USD 250 million investment in depreciable capital assets) no WHT shall be deducted on dividends declared.

3.3 PAYE Exemption

In the case of a company invested more than USD 1,000 in depreciable capital assets **or** if it is covered under item (4) given in para 1.1.1 above (State owned with >USD 250 million investment in depreciable capital assets) no PAYE (WHT) shall be deducted on maximum of 20 expatriate employees.

4. Tax Incentives (Third Schedule)

The tax incentives given in the Third Schedule to the Act is mainly not on the business income and hence, those are not discussed in length in this text. However, to gather some knowledge, the incentives listed in the said schedule are given below.

The **income tax incentives** have been granted to following persons under the Third Schedule to the Act;

- Government and Government related entities,
- Corporative societies,
- Government of foreign countries,
- International organizations,
- Persons suffered with personal injuries and death (on compensations or gratuities received),
- Retired persons (on receipt of pensions from Government of Sri Lanka),
- Persons retiring (on receipt of pension funds, ETF, provident funds),
- Privileged individuals (diplomatic, UN, UN agencies),
- Resident individuals (receiving capital gains above Rs. 50,000 per asset of Rs 600,000 per annum),
- Resident individuals (capital gain on principal place of residence),
- Persons (on disposal gain of shares listed in Colombo Stock Exchange),
- Charitable institutions (on interest income subject to some conditions),

- Persons (on awards received from the President on inventions/ researches),
- Non-resident persons/licenced commercial banks (on interest/discounts on sovereign bonds denominated in foreign currency issued by or on behalf of the Government on or after 21st October 2008),
- Senior citizens (on proceeds from an annuity for life for not less than 10 years),
- Persons (on lottery winning which does not exceed Rs 500,000),
- Shareholders (on dividend received where the paying company has declared out of the dividends received subjected to dividend tax),
- Government employees (on the benefit derived from his vehicle permit),
- Place of public worship (on profit and income from any property donated by royal or other grant before 02nd March 1815),
- Resident company (on dividends from and gains on the realisation of shares in a non-resident company),
- Persons (from sale of gems on which the WHT of 2.5% has been paid to The National Gem and Jewellery Authority).

5. Qualifying Payments & Tax Reliefs (Fifth Schedule)

The Fifth Schedule to the Act gives the qualifying payments and other reliefs applicable to individuals and entities.

5.1 Qualifying payments (referred to in section 52):

- (a)** Following donation made **by an individual or entity** in money to an approved charitable institution:
- (i) established for the provision of institutionalized care for the sick or the needy,
 - (ii) declared by the Minister as an approved charitable institution for the purposes of this sub-paragraph, subject to a maximum of;
 - (iia) in the case of an individual, 1/3rd of the taxable income or Rs. 75,000, whichever is less;
 - (iib) in the case of an entity, 1/5th of the taxable income or Rs. 500,000, whichever is less;

- (b)** a donation made **by an individual or entity** in money or otherwise to the following:
- (i) the Government of Sri Lanka;
 - (ii) a local authority;
 - (iii) any Higher Education Institution established or deemed to be established under the Universities Act,
 - (iv) 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,
 - (v) a fund established by the Government of Sri Lanka,
 - (vi) a fund established by a local authority and approved by the Minister,
 - (vii) the Sevana Fund created and administered by the National Housing Development Authority,
 - (viii) a fund established by a Provincial Council and approved by the Minister,
 - (ix) the Api Wenuwen Api Fund,
 - (x) National Kidney Fund established under the National Kidney Foundation of Sri Lanka.
- (c)** profits remitted to the President's Fund **by a public corporation** as required by the law by or under which such corporation is established.

5.2 The reliefs (referred to in section 52)

- (a)** Allowance of Rs. 500,000 per year of assessment, (an individual who is a trustee, receiver, executor or liquidator shall not be entitled to deduct this personal relief while it is not available to be deducted against gains from the realisation of investment assets),
- (b)** Employment allowance of Rs. 700,000 per year of assessment to an individual subject to the individual's employment income for that year),
- (c)** An allowance of 25% of the investment asset's rental income of an individual only if the actual cost is not claimed,
- (d)** An allowance of Rs. 1,500,000 per year of assessment against interest income of a senior citizen subject to the individual's interest income for that year,
- (e)** A resident individual's or partner's foreign currency income of Rs. 15,000,000 for each year of assessment from any service rendered in or outside Sri Lanka to any person to be utilized outside Sri Lanka, subject to the actual said income for that year.

6. Temporary Tax Concessions (Sixth Schedule to the Act under Sec. 201)

6.1 Enhanced Capital Allowances as a Temporary Concession (Valid till 31.03.2021)

A person who invests in Sri Lanka (other than on existing business) on depreciable assets (buildings, structures and similar works of a permanent nature and plant or machinery, other than intangible assets, that are used to improve business processes or productivity and fixed to the business premises) during a year of assessment shall be granted **enhanced capital allowances computed as follows** (in addition to the capital allowances computed under the Fourth Schedule);

- If such expenses incurred is up to **USD 3 million** and are used in any part of Sri Lanka other than in the Northern Province: 100%
- If such expenses incurred is **up to USD 3 million** and are used in the Northern Province: 200%

The enhanced capital allowances arising with respect to a particular year of assessment shall be taken in that year and cannot be deferred to a later year of assessment.

6.2 Assessable Charges and Balancing Allowances (Valid till 31.03.2021)

Where an asset for which capital allowances has been granted under this paragraph is disposed of (or deemed to be disposed of) during a year of assessment the taxable profit/loss be treated as follows;

- where the consideration received exceeds the tax written down value of the asset, the excess (profit) shall be included in calculating a person's income for a year of assessment from a business in which the depreciable assets are or were employed; and
- where the tax written down value of the asset exceeds the consideration received (loss), an additional capital allowance shall be granted for an equal amount.

6.3 Profit on Life Insurance

The portion of the gains and profits of life insurance business [life insurer's deemed profit under section 67 (2)] shall be **taxed at the rate of 14%** until 31st March 2021.

6.4 Profit on Information Technology

Companies engaged in following activities are entitled to **an additional deduction** equal to 35% of the taxable remuneration paid to their employees (other than its directors) in calculating the company's income from business;

- conducts a business which predominately consists of providing **information technology services** within the meaning of the First Schedule,
- has at least **50 employees** during the whole of the year; and
- report those employees in the statement that the company, as a withholding agent, is required to file under section 86.

A company which is entitled for deduction under this paragraph shall not be entitled to an enhanced capital allowance under paragraph 5.1 above. (paragraph 1 of Sixth Schedule to the Act).

Notwithstanding anything in section 19(1) of the Act, where the deduction under this paragraph results in an unrelieved loss for a company that unrelieved loss shall not be deducted in any succeeding year of assessment.

Remarks:

In the case where 35% of the taxable remuneration paid to their employees during the period from 01st April 2018 to 31st March 2021 is lesser than the volume of capital expenses incurred on depreciable capital assets during the same period, the tax payer is losing.

6.5 Taxing of Relocated Headquarters

Notwithstanding anything in the First Schedule to the Act, any institution, established on or after October 1, 2017 **by relocating in Sri Lanka** the headquarters or regional head offices of institutions in the international network, as specified by the Commissioner-General by Notice published in the Gazette shall be **taxed at the rate of 0%** until 31st March 2021.

6.6 Taxing of Persons engaged in providing of Renewable Energy

Notwithstanding anything in the First Schedule, any person, who has entered into a Standardized Power Purchase Agreement on or before November 10, 2016 with the Ceylon Electricity Board to provide electricity generated using renewable resources shall be taxed at the **rate of 14%** until 31st March 2021.

6.7 Additional Deduction on Research and Development expenses

When calculating a person's income from business, it is entitled to a **100% additional deduction** of research and development expenses which is deducted for the year under section 15, until 31st March 2021.



- 1. Determine the relevant income tax rate/s applicable** in the following situations during the year of assessment 2018/2019 with reference to the respective tax concessions and **tax exemptions, if any.**
- (1) Merlin (Pvt) Ltd is engaged in providing educational services for students reading for examinations of a professional body.
 - (2) Arthur (Pvt) Ltd is engaged in manufacturing toys for local market and their annual turnover is Rs.350Mn.
 - (3) New Arthur (Pvt) Ltd is engaged in trading toys in local market and their annual turnover is Rs.350Mn.
 - (4) Dolby Bank PLC is a commercial bank and opened a new branch in Kandy. Annual turnover of the branch is Rs 495Mn while that of the entire company is Rs.750Mn.
 - (5) Sarasi (Pvt) Ltd is engaged in manufacturing of handloom products and generated a turnover of Rs. 350 Mn during the year.
 - (6) Durga PLC is a fully owned subsidiary of Dark Angel PLC. It is engaged in providing healthcare services locally and had an annual turnover of Rs. 400Mn.
 - (7) Lord PLC is engaged in providing valuation services for the local market and is an associate company of Malawi PLC. It has generated an annual turnover of Rs. 250 Mn.
 - (8) Shasha PLC, a member of a group is engaged in manufacturing and export of packaging material and has an annual turnover of Rs. 950 Mn.
 - (9) Zenith PLC is engaged in manufacturing, import and sale of liquor. The company had an annual turnover of Rs. 450 Mn during the year.
 - (10) Manawa PLC is engaged in construction of drainage systems in Sri Lanka and its annual turnover generated is Rs. 550 Mn.
 - (11) Alpha PLC is a manufacturer of raw material for garment items and supplies to a direct exporter in the country. The annual turnover of the company is Rs. 950 Mn.
 - (12) Kalawana Estate Co. Ltd, having an associate is engaged in the manufacture of agriculture products for the local market. The company enjoyed a five-year tax holiday up to the year of assessment 2017/2018.
 - (13) Vijaya Brothers (Pvt) Ltd is engaged in the supply of manpower to other limited liability companies. Annual turnover of the company is Rs. 350 Mn.
 - (14) PQR (Pvt) Ltd is engaged in the poultry farming business since 2012. Taxable income of the undertaking is Rs.19,500,000 while the turnover is Rs. 100Mn.
 - (15) Sea Line Ships (Pvt) Ltd is engaged in providing risk management facilities to foreign shipping agencies situated in Malaysia. Taxable income of the company is Rs. 15,500,000 and the annual turnover of the undertaking is Rs. 497,000,000.
 - (16) XS Packaging (Pvt) Ltd is engaged in providing of printing services to companies situated in Australia. Its annual turnover is Rs. 950 Mn and such turnover its received through a FCBU account of XS Packaging (Pvt) Ltd. Its adjusted profit from business is Rs. 17,700,000.

- (1) 14% Rate of tax on educational services.
- (2) 14% Turnover is below Rs. 500 Mn. & hence an SME.
- (3) 14% Company turnover exceeds Rs. 500 Mn. & hence standard rate applies
- (4) 28% Turnover is below Rs. 500 Mn. & hence SME rate applies.
- (5) 14% Having an associate, hence not eligible for the SME rate.
- (6) 28% Having an associate, hence not eligible for the SME rate.
- (7) 28% Having an associate & hence not a SME.
- (8) 14% Engaged in (any) exports & hence the rate is 14%.
- (9) 28% Not an SME & hence the standard rate of 28% applies.
- (10) 28% Specified Undertaking covers with exports.
- (11) 14% This is a Specified Undertaking covers with exports.
- (12) 14% Rate of tax on agriculture applies.
- (13) 14% Turnover below Rs 500 Mn hence an SME.
- (14) 14% Specified Undertaking covers with exports.
- (15) 14% Specified Undertaking covers with exports.
- (16) 14% Engaged in Specified Undertaking covers with exports.

