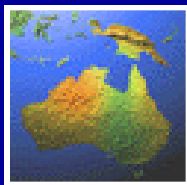
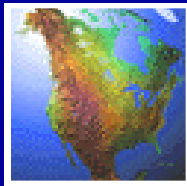


# Doing Business in...

## MGI International Tax and Business Guide



# SRI LANKA

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# **1 Preface**

This booklet has been prepared by GAJMA & CO, Colombo, Sri Lanka, a member of Midsnell Group International, to provide information about Sri Lanka to clients and fellow member firms in Midsnell Group International.

This booklet, where the information has been presented in a summary form, is intended to serve as a general guide to the businessman or potential investor in Sri Lanka.

## **2 Introduction**

This booklet is a brief summary of information about Sri Lanka for foreign companies or persons wishing to live in, do business with or invest in Sri Lanka.

The booklet is a general guide to Sri Lankan laws. However, these laws may change from time to time. They may be subject to interpretation by the Sri Lankan Courts or amended or repealed by Parliament. It is, therefore, strongly recommended that the businessman or potential investor obtain the assistance of local professional advisors before proceeding to do business with or invest in Sri Lanka.

While all reasonable care has been taken in the preparation of this booklet, no responsibility can be accepted for any inaccuracies it may contain whether caused by negligence or otherwise or for any loss howsoever caused or sustained by the person who relies on it.

## **3 Country**

### **3.1 Geography**

Sri Lanka, traditionally known as Ceylon, is an island off the south - eastern coast of the Indian subcontinent. Sri Lanka's close proximity to India and its strategic location, astride the sea routes between the east and the west exposed it to wide cultural, religious, linguistic and political influence throughout its 2500 years history.

Sri Lanka is 270 miles (435 kilometers) long and 140 miles (225 kilometers) wide with an area of 25,330 square miles. The capital city is Sri Jayawardenapura, Kotte. The commercial and business centre is Colombo.

Based on the altitude, Sri Lanka has varied climatic zones ranging from the tropical coast belt through the dry zone midlands to the cool temperate highlands.

Unlike conditions in midlatitudes of the globe, seasons in Sri Lanka bring almost unnoticeable temperature fluctuations. Seasonality primarily results from variations in the rainfall rhythm.

Climatologists divide the Sri Lankan climatic year into five periods:

- The convectional convergence period (March to mid April)
- The pre monsoon period (mid April to late May)
- The south west monsoon period (late May to late September)
- The convectional cyclonic period (late September to late November)
- The north east monsoon period (November to February)

Sri Lanka is one of the most densely populated countries in the world, second only to Bangladesh among the less developed countries in Asia. At present, the population of Sri Lanka is estimated to be nearing the 20 million mark.

About  $\frac{3}{4}$  of the population live in rural areas. Colombo, which is the shipping centre and hub port in the region, has a population of nearly 650,000 more than three times that of any other town in the island.

The population is multiracial and multilingual. The great majority (74%) of the people are Sinhalese. The Tamil population accounts for about 18%. The Muslims form the next largest minority comprising 7% of the population. All other minorities including Burghers, Eurasians and Chinese account for less than 1% but remain as distinct ethnic groups.

Under the Constitution, Sinhala and Tamil are the official languages of Sri Lanka and English is the link language. English is taught as a second language in all schools. In all International schools, English is taught as the first language and functions as the medium of instruction. In Sri Lanka, English is the language of communication, business, travel and domestic and international trade.

The spoken language of the large majority of the people in Sri Lanka is Sinhala while Tamil is the dominant language among the Tamils and Muslims. Use of English is most wide spread among urban and educated classes and it serves as a link language between different linguistic groups. English is widely used and understood almost everywhere in Sri Lanka.

The principal religions are Buddhism professed by about 69%, Hinduism by 15%, Islam by 7% and Christianity by 7%.

The island has been well known to travellers of many nationalities from ancient times. Its reputation for trade and scenic beauty is documented in the tales of Arabs, Greeks, Chinese and Romans. The island, with a coastal fringe consisting of estuaries, beaches and offshore islands, the central massif from which headwaters, of all Sri Lanka's major rivers originate, the long parallel ridges cut by the rivers beginning in the hill country, the rolling hills, the rich flora and fauna, the massive residual rocks adorned by its monuments of ancient civilization is of archaeological and tourist interest. Today the island is one of the fastest growing tourist centres in South Asia. Sri Lanka was selected as the lead country in tourism in the BMIST-EC in 1998.

## **3.2 Government**

Sri Lanka is a Democratic Socialist Republic. The fundamental legal rules relating to the basic framework of the system of Government in the state of Sri Lanka are laid down in the Republican Constitution of 1978, which is autonomous and autochthonous. The Constitution is the fundamental or higher law of the land. It is written and rigid. It cannot be legally amended or replaced with the same ease and in the same manner as ordinary laws. It requires for its amendment the special procedure prescribed in the Constitution.

The Republic of Sri Lanka is a unitary state in which the Central Government exercises supreme power and authority. The supreme legislative, executive and judicial powers are concentrated in the centre. All other governing bodies, the Provincial Councils and Local Government bodies within the state are subordinate to the Central Government.

The Republic of Sri Lanka has a system of government, which is an amalgamation of the Westminster model with the French Presidential system. There is an Executive President with a large concentration of powers and also a Prime Minister and a Cabinet. The Parliament of Sri Lanka is a unicameral legislative organ. The President, who is the Head of the State and the Head of the Cabinet, exercises the executive power of the people and the Parliament exercises their legislative power.

The President and the Members of Parliament are elected by the people at specified periodical elections. The election by the people of the President and their representatives in

Parliament is by the free and secret exercise of the universal franchise at elections. The Members of Parliament are elected by a system of proportional representation. The President holds office for a term of six years and can serve for more than one term.

The executive structure in the Central Government rank from the President to the Cabinet of Ministers, Project Ministers and State Ministers.

The judicial power of the people is exercised through courts and other institutions created by law. The Constitution contains provisions, which are designed to ensure the independent exercise of the judicial function.

The members of Provincial Councils are elected by the people. The President appoints the Governor for each Province. At the Provincial Council level, the executive structure ranks from Governors to Chief Ministers and their Cabinets.

The bureaucracy, which has its own norms for administration and financial procedure, is entrusted with the task of translating Government policy into action.

The office of the Parliamentary Commissioner for Administration was created by Act, No. 17 of 1981 to investigate and report upon complaints or allegations of the infringement of fundamental rights, maladministration and other injustices by public officers and officers of public corporations, local authorities and other like institution.

Sri Lanka is member of the United Nations Organisation, the Commonwealth of Nations, the South Asian Association of Regional Cooperation and South Asian Development Bank.

### **3.3 Legal System**

Sri Lanka, like South Africa, Zimbabwe, Mauritius and the Philippines, has a mixed legal system. It consists of the elements of two foreign laws - the Roman Dutch law and the English Law and other systems of law that exist in Sri Lanka notably the Kandyan law, Muslim law, Tesawalamai law, Buddhist law and Hindu law.

In Sri Lanka, principles adopted from England apply in relation to bills of exchange, sale of goods, partnership, companies, insolvency, banks and banking, maritime matters, insurance, criminal law, procedure and evidence.

English principles also apply in the organisational patterns, practices and traditions of the Courts. The legal concept of judicial precedent separation of powers, rule of law and the independence of the judiciary found in Sri Lanka are principles of English Law.

Roman Dutch law principles apply relating to succession, persons, property and obligations. However, the application of the Roman Dutch Law in these areas is restricted by statutes some of which are based on English principles, judicial decisions or by the operation of personal laws, which are the Kandyan law, Muslim law and the Tesawalamai law.

The Roman Dutch Law is composed of the Law of 1796 and the body of case law developed by the Courts.

Roman Dutch law is the indigenous common law of Sri Lanka. It applies to all sections of the community.

Roman Dutch law is the residuary law of Sri Lanka. It applies in all situations in which there is no relevant statute and in case of those subject to the personal laws, where those laws are inapplicable or silent.

Kandyan law, Muslim law and Tesawalamai law are three systems of law referred to as personal laws of Sri Lanka. A personal law applies to a section of the population in a given territory on account of certain common factors, which they all possess. The application of the personal law is determined by the community to which persons belong by birth or because of adherence to a religion.

Statute law emanating from Parliament, which is the supreme legislative authority, takes precedence over all other forms of law in Sri Lanka.

For over two thousand years of Sri Lanka's long history, there has been a hierarchy of courts in Sri Lanka. In the hierarchical structure today, the Supreme Court is the highest and the final superior court of record in Sri Lanka. The Court of Appeal, High Courts, District Courts and Magistrate's Courts are the other courts in the present structure. The Magistrate's Court is the lowest court.

The Administrative Tribunals determine the legal rights and disputes arising for the most part in the course of administering economic legislation and social legislation. These tribunals are entrusted with judicial functions.

The Inland Revenue Act, No. 38 of 2000 provides for an appeal by a person aggrieved against the amount of an assessment to the Commissioner-General of Inland Revenue and from his determination to the Board of Review.

The Industrial Disputes Act, No. 43 of 1950 provides for Industrial Courts and Labour Tribunals to investigate and settle industrial disputes according to just and equitable principle.

The Workman's Compensation Ordinance No. 19 of 1934 provides for the Commissioner for Workman's Compensation to settle and determine any question relating to the liability of any person to any compensation or as to its amount or duration or as to the age of any workman.

The Licensing of Traders Act, No. 62 of 1961 provides for the licensing authority to ensure the maintenance of business standards and morality and to enable the maintenance of fair and stable prices in essential consumer commodities.

The Rent Restriction Act, No. 7 of 1972 set up a Rent Control Board for each area governed by the Act and a Board of Review to hear appeals from orders made by the Rent Control Board.

### **3.4 Currency and Banking**

In Sri Lanka, the unit of currency is the Rupee (Rs.).

Sri Lanka, accepting Article VIII of the Articles of Agreement of the IMF removed all restrictions on current external transactions.

The Sri Lankan rupee is fully convertible and can be freely used in respect of all current international transactions.

Sri Lanka has taken a major step forward in the liberalization of foreign exchange transactions by allowing commercial banks to determine the exchange rate freely.

The exchange rate of the Sri Lankan rupee fluctuates against the currencies of its trading partners.

The Central Bank of Sri Lanka, which was established under the Monetary Law Act, No. 58 of 1949, commenced operations on 28<sup>th</sup> August 1950. It is responsible for the administration and regulation of the monetary and banking system in Sri Lanka. It acts as Government's fiscal agent, banker and financial adviser. Its functions are to issue currency, examine and supervise the banking institutions and to advance credit to commercial banks and other specialized money lending institutions in times of financial crisis.

Sri Lanka has a fully developed commercial banking system consisting of about 26 commercial banks. Two (2) of the large commercial banks, which have an extensive network of branches in all parts of Sri Lanka, are public sector banks. In addition, there are four (4) private local banks. All foreign commercial banks in Sri Lanka have operational services in Colombo, which is the commercial centre of Sri Lanka.

Foreign currency banking units, which operate as subsidiaries of commercial banks, carry on transactions in foreign currency with non-resident enterprises such as those established in the Free Trade Zones in Sri Lanka.

### **3.5 Economy and Business Climate**

#### **3.5.1 Framework of the Economy**

Sri Lanka has a liberal economic policy. In 1978, Sri Lanka adopted an open market economy framework placing emphasis on an outward looking and liberal economic policy regime with the objective of establishing a coherent stable macro-economic and financial framework to promote economic growth, diversify the economy, reduce unemployment and

inflation and at the same time creating a social safety net through well targeted welfare programs to improve the average living conditions of the people.

With the transition to an open market policy framework, placing emphasis on economic liberalisation, Sri Lanka began establishing market oriented policies and took keen interest in introducing supply side economic policies. Some of the major policies implemented in this direction:

- liberalising trade and encouraging foreign investment;
- privatising industries and increasing economic efficiency;
- setting the exchange rate at more realistic levels; and
- reducing controls on foreign exchange transactions.

Sri Lanka has been following these policies for more than two decades and the continuation of these policies was highlighted in the Government's Economic Policy Statements of 1999 and 2000.

### **3.5.2 Salient features of Economy 2000**

While Sri Lanka's economy steadfastly maintained an annual average GDP growth of 5% during the decade, Sri Lanka's economy recorded a satisfactory GDP growth rate of 6% in 2000, pointing to an improved performance of the economy as against the GDP growth of 4.3% in 1999. The growth momentum was generated by healthy trends in Manufacturing (9%), Services (7%), Construction (5%), Mining and Quarrying (5%) and Agriculture (2%). While the output increased in all major sectors, the overall service sectors contributed 61% and the manufacturing sector 26% to the overall growth in 2000.

Sri Lanka's per capita income increased to Rs. 64,855/- (US dollars 856) in 2000 from Rs. 58,077/- (US dollars 825) in 1999. With this increase, the country's position in the international classification moved further up within the lower middle income category, which consists of countries with per capita income in the range of US\$ 795 - 3,125.

The unemployment rate declined to 7.7% in 2000 compared to 8.9% in 1999. The private sector remained the major contribution to employment generation as its economic activity grew faster. Manufacturing, agriculture, trade and hotels, finance, insurance and real estate and construction were the major areas of employment generation. About 41,000 employment opportunities were generated through Board of Investment approved projects in 2000.

Inflation increased to 6.2% in 2000 compared to 4.7% in 1999. The single largest factor promoting cost-push inflation has been the international crude oil prices. This astronomic rise in turn increased the overall price level of goods and services in the economy.

The ratio of gross domestic investment increased to 27.3% due to increased private sector investment activities. The relative share of private sector investment in total capital

accumulation increased to 89%, reflecting the growth rate of the private sector in the economy of Sri Lanka.

The contribution of the public sector to industrial output was 12% and that of the private sector was 88%. Output of private sector industries grew by 10.5% in 2000 compared to 5.3% in 1999. Private sector industries accounted for 94% of industrial production in 2000.

The economy attracted foreign investors with Foreign Direct Investment (FDI) inflows amounting to US\$ 175 million in 2000.

Of the 329 Board of Investment approved investment projects in 2000 under section 17 of the Board of Investment Law, 59 were entirely foreign owned, 111 were joint venture collaborations and 159 were entirely domestic owned ventures. The foreign component of the approved investments in 2000 was 27% of the total approved investment. Of the 138 approved industrial projects under section 16 of the Board of Investment Law, the foreign component of these projects was 79% of the total investment.

Both private and public investment programs have been implemented to improve the country's basic infrastructure facilities such as ports, telecommunications, aviation, energy and transport, which today rank as the best available in South Asia.

Sri Lanka's external trade registered a notable upturn with both exports and imports growing at a faster rate in 2000. Exports registered a high growth of 20% against a drop of 4% in 1999. The high growth was mainly in the areas of textiles and garments, tea, coconut, machinery, electrical equipment, rubber based products, gems, diamonds and jewellery.

Sri Lanka derived a total revenue of Rs. 420,114 million in 2000 from:

the traditional exports of agricultural products mainly tea, rubber, coconut, coffee, pepper, cinnamon, cloves, nutmeg cardamoms, cocoa, essential oils, unmanufactured tobacco arecanuts, fruits, vegetables and cashew nuts;

the non-traditional exports of industrial products mainly textiles and garments, chemical, petroleum, rubber, ceramics, leather, paper, wood and plastic products, food beverages and tobacco, machinery, mechanical and electrical equipment, jewellery and diamonds; and exports of minerals mainly natural graphite, ilmenite, metallic ores, precious and semi precious stones.

Sri Lanka's other sources of income were from:

- taxation (direct and indirect)
- customs duty,
- tourist industry and
- migrant employees.

The total import expenditure increased at a higher rate of 22% in 2000.

Sri Lanka spent a total of Rs. 554,290 million in 2000 on the importation of:

- Consumer goods mainly rice, flour, sugar, milk products, fish, motor cars and cycles radio receivers, rubber Tyres and tubes, medical and pharmaceutical products,
- Intermediate goods mainly fertilizers, petroleum, chemical elements and compounds, dyeing tanning and coloring materials, paper and paper boards and textiles.
- Investment goods mainly building materials, transport equipment, machinery and equipment and other unclassified imports.

The total expenditure on the major imports of rice, wheat, sugar, crude oil and fertilizers incurred was Rs. 64,446 million.

### **3.5.3 Business climate for Foreign Investment**

Sri Lanka is an attractive investment location. There are several good reasons for it.

#### **Location**

Sri Lanka is fast becoming an economic powerhouse in the South Asian Region. The Country is ideally located as the gateway to the sub continent of India and it is the logical location for foreign investors to establish manufacturing and service organisations.

#### **Labour**

As a result of extensive investment in public education and welfare programs by successive post independent governments, Sri Lanka has the highest life expectancy (71 years), highest literacy (92%) and lowest infant and child mortality rates among the developing countries in South Asia.

Today, foreign investors in Sri Lanka will find an intelligent educated and energetic work force that is comfortable with modern production techniques and has a level of trainability that is among the best in the region. In fact, the best quality work force is available in Sri Lanka. Skilled manpower and professional managers are available at reasonable cost.

#### **Government policies**

The Sri Lankan government is business friendly and implements market friendly policies and adopts an export oriented growth strategy.

The government is actively pursuing a policy of economic liberalization with emphasis on private sector investment.

## **Private Sector Investment**

The private sector is the engine of economic growth and plays a vital role in traditional areas of public investments such as port, telecommunication, transport and energy. Many enterprises have been privatized since 1978.

There is an increasing role of private and foreign investment in the Sri Lankan economy.

Many foreign companies have set up joint ventures, trading and manufacturing companies in Sri Lanka.

Sri Lanka encourages the establishment of a strategic alliance between public sector enterprises and private sector investors, local and foreign. Several landmark investments have been approved and implemented in the infrastructure, manufacturing and service sectors. The most recent investments are:

Purchase of 35% stake in Sri Lanka Telecom by NTT of Japan for US\$ 225 million.

Two licenses were awarded to set up basic telecommunication services using wireless local loop technology to business groups led by Telia AB of Sweden and GTE Nortel of North America. Approximately two thirds of the anticipated US\$ 350 million dollars investment is already committed and implementation of the projects is on schedule.

The first ever power generation project on a BOO (Build Own and Operate) basis was successfully structured by the Board of Investment. In this US\$ 62 million project, the lead investor is the UK based KHD group.

Sri Lanka welcomes total foreign ownership in most areas of the economy. The largest single foreign direct investment in the manufacturing sector approved by the Board of Investment recently is the US\$ 385 million investment by IMC Agrico Freeport McMoran Resource Partners (both of USA) and Tomen Corporation (Japan) for phosphate mining and processing of DAP fertilizers.

## **Incentives**

The Sri Lankan government has established Export Processing Zones (EPZs) at Katunayake, Biyagama, Koggala, Malwatta, Mirigama, Kandy, Seethawaka and Wathupitiwela to provide investment opportunities and promote exports.

Under the Board of Investment Law, incentives in the form of tax, import duty and exchange control exemptions are available to foreign investors who wish to engage in the following Export Oriented Enterprises in the Export Processing Zones.

- Thrust Industries
- General Export Oriented Projects
- Projects Locating in designated industrial zone
- Exports of Textiles, Software, Gems, Jewellery and Agricultural Products
- Export Trading, Regional Operating head quarters ship repairing and breaking

- New enterprises outside Colombo District
- Non-export Oriented Projects – Tourism, Housing, Hospital and small scale infrastructure
- Large scale investment
- Agriculture and Training Institutions.

A foreign investor can either purchase or lease land for any proposed enterprise. If land is purchased by a foreign investor, a tax payment of 100% of the purchase price is required. But if a foreign investor incorporates a company in Sri Lanka under the Companies Act and buys land in the name of the company, tax payment is not required, even though the shareholders of the company are foreign nationals. This is because a company incorporated in Sri Lanka is deemed to be a citizen of Sri Lanka for the purpose of taxation.

Sri Lanka is progressing on the path of globalisation by gradually removing barriers to trade and investment, while establishing necessary regulatory and supervisory mechanisms and implementing measures required to ensure stability.

Trade barriers are falling throughout the South Asian region. The seven countries which comprise the South Asian Association for Regional Cooperation (SAARC) have resolved to progress towards a South Asia Free Trade Arrangements (SAFTA) over the next five (5) years.

### **Remittance of Earnings and Capital**

There are no restrictions on the repatriation of earnings and capital of foreign investors. Sri Lanka has removed all foreign exchange restrictions on current account transactions.

### **Protection to Investors**

The government has never defaulted nor requested rescheduling of any of the international obligations and this extends to protection given to foreign investors as well.

Bilateral investment agreements, which are supported by a constitutional guarantee, provide strong protection to foreign investment in Sri Lanka. The safety of foreign investment is guaranteed through the acceptance by a two-thirds majority of Parliament of the constitutional guarantees of Investment Protection Agreements. Under Article 157 of the Country's Constitution the agreement enjoys the force of law and no legislative executive nor administrative action can be taken to contravene it.

Bilateral Investment Agreements are valid for 10 years. They are extended automatically unless terminated by either party. If the agreements are terminated, investments already made are protected for another 10 years. The constitution ensures the sanctity of the agreements. The bilateral agreements provide for the following:-

- protection against nationalization.
- prompt and adequate compensation if required.
- free remittances of earnings, capital and business fees.
- settlement of dispute under the International Convention for the Settlement of Investment Disputes (ICSID).

Sri Lanka is a founding member of the multilateral Investment Guarantor Agency (MIGA). This provides future safeguards against expropriation and non-commercial risk.

Property insurance can be obtained in foreign currency through domestic or foreign insurers.

Tax in Sri Lanka is being simplified under a broad based low tax regime. Sri Lanka has a well-established legal system with independent judiciary and an excellent and well-developed accountancy and legal profession.

### **3.6 Pollution Control**

The National Environmental Act of 1980 with its subsequent amendments in 1988 and 2000, which applies to both local and foreign investors stands as the most important single piece of legislation on environmental protection and management in Sri Lanka. It lays down stringent standards and restrictions to curb discharges of pollutants to air, water and soil, to control the handling of chemical substances and hazardous wastes and to restore contaminated properties.

This Act requires environmental impact assessments and licenses for industries, which discharge deposit or emit waste into the environment. The Central Environmental Authority has been established by this Act to implement the provisions of this Act.

The Central Environmental Authority (CEA), the regulator of the environment, deals with:

- the issue of Environmental Protection Licences (EPL) for polluting industries,
- preparation of pollution control guidelines,
- monitoring activities which include the monitoring of major water bodies and industrial pollution,
- setting pollution control standards,
- conducting Environmental Impact Assessments in connection with major development projects,
- conducting Environmental Evaluations,
- receiving environmental complaints from the public and
- establishing and enforcing the pollution laws through regulatory requirements.

For granting location approval and issuing of Environmental Protection Licence for projects within the Export Promotion Zones of the Board of Investment, the Board is empowered to enforce the provisions of the National Environmental Act.

For enterprises located outside the Zones, granting of location approval and issuing of Environmental Protection Licence are carried out by the Board of Investment with concurrence from the Central Environmental Authority. The required confirmation is obtained by the Board of Investment on behalf of the investor and the investor only deals with the Board of Investment.

The Constitution of 1978 provides for environmental protection in Sri Lanka.

Article 28(f) of the Constitution states:

“The exercise and enjoyment of rights and freedoms is inseparable from, the performance of duties and obligations, and accordingly it is the duty of every person in Sri Lanka, to protect nature and conserve its riches.”

In Sri Lanka, the Ministry of Forest and Environment formulates environmental policies at the national level. The Ministry has developed a National Policy on air quality management under Clean Air 2000 Action Plan and a National Safety for Social Waste Management. The Ministry has prepared a directory of Eco-business and theoretical and field manuals for application of environmental techniques for project appraisal.

Sri Lanka has signed more than 30 environmental related international conventions and protocols involving various public sector institutions. It has planned to setup an International Secretariat. The Ministry of Forest and Environmental Authority is the Competent Authority for the implementation of the Basel Convention on the Control of Transboundary Movement of Hazardous Waste, the Montreal Protocol to Control the use of ozone depleting substances and the United Nations Framework for Convention of Climate Change.

### **3.7 Education**

Section 27 (2) of the 1978 Constitution of Sri Lanka states that the State is pledged to establish in Sri Lanka a Democratic Socialist Society, the objectives of which include the complete eradication of illiteracy and the assurance to all persons of right to universal and equal access to education at all levels.

Basically, Sri Lanka has always aimed for equal opportunity in education regardless of social class, national origin or racial or ethnic group. A high general level of education has always been seen as a necessity in this democratic society. Education in Sri Lanka has traditionally served the goal of bringing people together. Schools in Sri Lanka serve to bring together the hundreds of various cultural linguistic religious and social groups represented by the millions of people.

In Sri Lanka, there are approximately 10,400 government schools, 561 pirivena schools and 78 private schools. In addition, there are about 95 international schools catering to around 60,000 local and foreign students. The international schools in Sri Lanka provide to students, the opportunities to gain admission to foreign Universities and Technical Institutes. All schools in Sri Lanka provide general education, which includes the teaching of English and developing the technical and practical skills of students at the primary and secondary level. Education is available free of charge in all government schools and universities. The total number of teachers in Sri Lanka is about 195,000.

The Sri Lankan ideal of mass education for all is matched by awareness that Sri Lanka needs highly trained academics, professionals, and specialists in various fields. In higher education therefore, and especially in universities, Sri Lanka has an extremely competitive and highly selective system.

To provide tertiary education in Sri Lanka, there are 13 national universities including the Open University of Sri Lanka. The total university students population is about 69,007. In addition to the first degree, many universities offer post-graduate degrees. There are six post-graduate institutes affiliated to the Universities, which offer post-graduate degrees. The total enrollment for post-graduate studies is about 3,617. There are 7 institutes affiliated to universities, which offer Bachelor's Degree in specialized fields. A few private sector educational institutions offer degree programmes in collaboration with foreign universities. Most universities have staff development and career guidance units.

The technical education and vocational training sector consists of Technical Colleges. These colleges conduct Diploma Courses in Engineering, Accountancy, Commerce and Business Management.

Sri Lanka has given importance to Information Technology in the educational system. The private sector has taken the leadership in training IT personnel demanded by the market. Several IT institutions conduct degree programmes by linking themselves with foreign universities. On the state sector, the University of Moratuwa, Institute of Computer Technology of the University of Colombo and the National Institute of Business Management provide IT education. The Sri Lanka Institute of Information Technology produces approximately 2000 IT professionals per year. Fifty(50) IT centres have been established in rural areas with private sector participation.

The Information Technology industry is granted a five year tax holiday for the establishment of Information Technology training institutes outside the district of Colombo with a minimum of 300 students being trained each year.

In Sri Lanka, educational policies encompassing all areas of primary, secondary and tertiary education have been introduced with the broad objective by enhancing learning achievements at all levels, in the line of a market driven economy. The educational policies, which are being implemented include other than book knowledge, versatility and adaptability, confidence to face challenges, a positive work ethic, productivity and discipline, leadership and team work and communication skills in English, which are qualities and attributes needed in the present day labour market.

Sri Lanka has a literacy rate of 85.6, one of the highest among the developing countries in South Asia.

Education is compulsory to all children between ages of 5 and 15.

### **3.8 Housing**

In Sri Lanka, the total number of dwelling places is estimated to be 3,029 million, of which 2,924 million are housing units and 0.105 million are living quarters, other than housing units. The construction of houses by owners themselves still forms a large part of housing construction. The acute housing problem, like other urbanization problems is mostly confined to urban areas in Sri Lanka.

Several housing programs are being implemented by both public and private sector to provide reasonable housing facilities for all.

Private sector housing providers focus mainly on the urban sector housing market. They cater to middle and high income categories.

The Government encourages the private sector investment in housing by way of granting attractive tax incentives.

Housing construction undertaken by the private sector includes the Sustainable Townships program in the Colombo city and the Board of Investment housing projects in the Greater Colombo area.

The public sector housing programs focus mainly on improving rural and estate housing. Public sector housing is mainly for low income families.

The major public sector institutions involved in the provision of housing are the National Housing Development Authority, Plantation Housing and Social Welfare Trust, State Mortgage and Investment Bank and the Housing Development Finance Corporation.

The National Housing Development Authority implements the key state sector housing programs by providing loans to build or upgrade houses.

The Plantation Housing and Social Welfare Trust provides housing facilities to estate employees under the Plantation Development Support program.

Loans are granted by commercial banks and other financing institutions for the construction of individual houses.

The construction sector has recorded a 4.8 growth rate due to the increase in investment in housing programs. While the performance of the state sector housing program has slowed down, the housing construction undertaken by the private sector has expanded in Sri Lanka.

The Urban Development Authority is responsible for planned development of major urban centres in the country. The main development activities are the construction of administrative commercial and industrial complexes town improvement projects integrated projects and social and cultural projects.

### **3.9 Transport**

The transport sub-sector which includes passenger and freight transport has segments of roads, rail and air. The combined growth rate of these sectors has been 4 percent.

Sri Lanka has developed an enormous modern transportation system, an extensive network of roads and highways, which enable people to travel freely and comfortably. There are trains, buses, luxury coaches, and trucks to take people to any part of Island.

The improvements in the road haulage have been associated with the growth in domestic production as well as external trade.

The Sri Lankan highway system stretches over 100,000 km. The responsibility for the development and maintenance of the road network and bridges is vested with the Government Institutions at various levels. The National Highway network consisting of major road and bridges comes under the direct preview of the Central Government. The executive agency for developing and maintaining these roads is the Road Development Authority, which is also in charge of planning, designing and constructing new highways and bridges. Provincial Councils and local authorities maintain the less major and minor roads and bridges within their regions.

The Road Development Authority has implemented several construction and rehabilitation projects with the help of foreign funds obtained from the Asian Development Bank, Kuwait Fund for Arab Economic Development, Nordic Fund, Economic Development Co-operation Fund and JBIC.

Bus services are operated both by the public sector and the private sector. The private bus operators provide a greater part of the services in Sri Lanka. The introduction of luxury and semi-luxury buses for public transport has enhanced the value addition of the passenger transport sector.

The National Railway transportation works best and most probably where distances are long and getting to and from a place is inconvenient and expensive by bus. Trains are mostly used for freight transportation by goods transporters on account of its greater flexibility, reliability and convenience.

There are goods trains, passenger trains, express trains and slow trains.

The civil aviation sector includes air passenger transportation by National Carrier and foreign airlines. There are 27 foreign airlines servicing Sri Lanka. The total number of passengers who pass through the Bandaranayake International Airport for a year is about 2.9 million. The total freight handled at the Airport is about 211,930 metric tons.

Sri Lankans and other foreigners are able to fly to and from other countries to do business with or in Sri Lanka.

### **3.10 Telecommunications**

In Sri Lanka, there has been an unprecedented growth in the telecommunications industry after the restructuring of the telecommunications sector in the early 1990's and the liberalisation of the industry in 1997. This strong growth was supported by the partnership of Sri Lanka Telecommunication with Nippon Telegraph and Telephone (NIT) of Japan, and heavy investment and competition from private sector operators that include NNT, Telia, Telstva, GTE, Nortel, Hutchison and Malaysia Telecom, which are global market players.

The rapid development in the telecommunications industry has helped to bring a convergence of all communication modes by integrating voice and data communications, internet, e-mail, television broadcasting, video conferencing and business communications.

This modernization of telecommunication technology and introduction and expansion of new services such as internet, e-mail and video conferencing facilities have increased available services to customers and also improved the quality of communication services in Sri Lanka.

In Sri Lanka, there are 37 telecommunication system operators, including three companies providing fixed access telephone facility and few companies providing mobile services enhancing competition in the telecommunications sector.

In Sri Lanka, the subscriber base of telephone services including mobile telephones has exceeded more than one million. The telephone density in Sri Lanka is 6.3 per 100 persons. The private sector led telecommunications industry in Sri Lanka is now in a position to adopt a new technology to provide better service to end users.

The telecommunications market in Sri Lanka has become increasingly more competitive especially for cellular mobile telephones, data communications services, wireless fixed access services and pay phone services.

## **4 Forms of business enterprise in sri lanka**

Foreign investors may establish a business presence in Sri Lanka, through any of the following forms:

- Sole Proprietorship
- Partnership
- Private and Public Companies
- People's Company
- Limited and Unlimited Companies
- Offshore Companies
- Foreign Branches
- Liaison Offices
- Joint Ventures
- Co-operatives

Each of the above entities has its own unique characteristics and the exercise and operation of the different entities are governed by statutory laws based on English Law.

### **4.1 Sole Proprietorship**

A Sole Proprietorship where a single foreign investor owns the business involves the least number of formalities before a business can commence. However, this carries with it some advantages and disadvantages.

Advantages:

- The ability to set off certain business expenses against trading profit for tax purposes.
- Individual business accounts do not need to be audited although it is generally desirable to draw accounts up to 31<sup>st</sup> March each year.

Disadvantages:

- No limitation of personal liability for trading debts.
- Higher liability to Sri Lankan taxation on trading profits than a company.

### **4.2 Partnership**

It is possible for foreign investors to enter into Partnership with either residents or non-residents of Sri Lanka to do business in Sri Lanka.

In Sri Lanka, the law that governs Partnership is the English Partnership Act of 1980, which was introduced in Sri Lanka by statute.

Partnership is a relationship, which subsists between two or more persons carrying on a business in common with a view to profit. Business includes any trade, occupation or profession.

To create a Partnership, no formalities are necessary, although for practical reasons writing is usually used.

The maximum number of partners is 20.

In a Partnership:

- the partners share profit and losses in accordance with the partnership agreement;
- partnership is not taxed separately but rather each partner is taxed on the share of the partnership profits;
- shares of a partnership losses may be offset against other income of a partner for the purpose of determining the taxable income;
- partnership has unlimited liability and has tax advantages over sole proprietorships;
- partners are jointly and severally liable for the debts of the partnership which means the creditors can, if they wish, recover partnership debts from any of the partners, leaving the partners to seek recovery from other partners.
- partnership is normally regulated by specific agreements between the partners, but in the absence of specific agreement, the partnership Act of 1890 makes provisions for certain matters.
- a Sole Proprietorship and Partnership are not generally found suitable by foreign investors due to unlimited liabilities for debts.

## **4.3 Companies in Sri Lanka**

In Sri Lanka, the law that governs the creation and operation of companies is the Companies Act of 1982, which is based on the principles of the English Companies Act of 1948.

### **4.3.1 Categories of Companies**

#### **Private and Public Companies**

A Private Company can restrict the right to transfer its shares, limit the number of its members to not more than 50 and prohibit public subscription to its share capital or debentures of the company. Any other company, which has no such limitations, is a public company.

A Private Company may be converted into a public company and in certain circumstances deemed to be a public company.

The Companies Act of 1982 has widened regulations for public companies in respect of management and operation due to greater public participation.

## **People's Company**

A People's Company is a company, which satisfies the following conditions:

- maximum membership is unlimited;
- the nominal value of a share shall not exceed Rs. 10/-;
- no person can hold more than 10% and no company other than people's company can hold shares;
- minimum number of directors 3 and each director should hold at least 1 share and each director must be elected annually;
- transfer of shares is subject to the Articles of Association;

## **Limited and Unlimited Companies**

In Sri Lanka, the most common form of company is the limited liability company. A limited liability company is the most suitable form of business enterprise for a foreign investor in Sri Lanka because:

it ensures clean cut off between affairs in Sri Lanka  
it provides limited liability to the share holders in the event of insolvency  
it limits the liability of each shareholder for the debts of the company to the amount he has undertaken to pay to the company for his "Shares" or by way of guarantee.

## **Off shore Company**

Any company either incorporated in Sri Lanka or outside Sri Lanka may apply to the Registrar to be registered as an Off Shore Company. The Registrar may having regard to national interest or in the interest of the national economy issue a Certificate of Registration after the required fee is paid and a Certificate is produced from a bank that a sum of US\$ 100,000 has been deposited to meet its expenses in Sri Lanka. Such company shall be exempt from complying with any other provisions of the Act.

An Off Shore Company cannot carry out any business in Sri Lanka.

## **Non-resident Companies**

A non-resident company may establish a branch or a liaison office in Sri Lanka.

### **a) Foreign Branch**

A company incorporated outside Sri Lanka, which establishes a place of business within Sri Lanka need to seek registration within one month of the establishment of the place of business.

Such a company has the same powers to hold lands in Sri Lanka as if it was a company incorporated in Sri Lanka.

Any non-citizen who purchases land in Sri Lanka is subject to a 100% transfer tax.

All branches in Sri Lanka are registered as foreign branches.

#### b) Liaison Office

Companies incorporated outside Sri Lanka can have a liaison office in Sri Lanka for any of the following purposes: -

- market intelligence, planning and coordinating business promotion activities;
- technical support and quality control;
- sourcing of raw material and manufactured products;
- not engage in any import, export, trade or investment in Sri Lanka.

Most of the foreign companies in Sri Lanka seek registration as liaison office.

#### **Holding and Subsidiary Companies**

A company is deemed to be a subsidiary of another company if:

- the other company holds more than half of the nominal value of its equity share capital; or
- is a member of it and controls the composition of its board of directors.
- A company is a Holding Company of another company if that other company is its subsidiary

#### **4.3.2 Formation of a Company**

Under the Companies Act of 1982, the formation of a company requires:

- Selection of a name, which has to be approved by the Registrar of Companies.
- Drafting a Memorandum of Association which mentions the name of the company, the district in which the registered office is situated, the objects for which the company is formed and its capital, the limited liability of its members and the Articles of Association which set out the regulations for its internal management including the rights and duties of members in their capacity as members.
- Preparation of documents for submission to the Registrar of Companies for registration along with requisite fees.

Memorandum and Articles of Association lay down the objects for which the company is formed.

The Articles of Association will contain details of how the company will be run from day to day.

A registered company in Sri Lanka is a legal person.

### **4.3.3 The Essential Characteristics of a Company**

#### **Capital**

In Sri Lanka, there are statutory provisions, which ensure that the “capital” of a company is maintained and could only be reduced through certain established procedures. The term “capital” for this purpose comprises of paid up share capital and any share premium account.

In the memorandum, if the company is a company limited by shares, the amount of capital with which it proposes to be registered should be stated. This registered capital may be increased by an ordinary resolution. The share capital may be reduced if the reduction is authorised by the Articles of Association, by a special resolution and if the resolution is confirmed by the court.

#### **Shares**

Issue of shares requires compliance with various provisions of the Companies Act, of 1982. A company may issue different categories of shares: ordinary, preference, deferred and non - voting shares. Redeemable preference shares may be issued if authorised by the Articles of Association.

Share warrants may be issued by public companies subject to certain conditions. In order to issue or transfer such share warrants to non-residents, the permission of the Central Bank is required.

A company cannot purchase its own shares. It also cannot provide financial assistance for the purchase of or subscription of its shares except in regard to schemes for the purchase of shares by the trustees to be held for the benefit of the employees. When offering shares to the public, a prospectus must be issued.

#### **Borrowing Powers**

The borrowing powers of a company may be limited by the Memorandum or the Articles of Association. The issue of debentures, which are offered to the public, is prohibited unless a prospectus is issued. The reissue of redeemed debentures is allowed unless otherwise prohibited by the Article, a contract or a resolution. Floating charge is permitted.

#### **Directors**

A public company has a minimum of two (2) directors and a private company has a minimum of one (1) director. The first directors of the company are nominated by the subscribers to the Memorandum and any subsequent appointments and retirements are governed by the Articles of Association.

The retiring age is 75 years. A company is prohibited from granting loans to its directors of its Holding Companies. Neither can it enter into guarantee or provide security in connection with a loan granted to such directors by any other person.

## **Shareholders**

There must be at least two (2) shareholders in the case of a private company and at least seven (7) shareholders in the case of a public company.

A company cannot be a shareholder in a People's Company. Where a share is transferred by a resident person to a non-resident person, the non-resident person's name cannot be entered in the register of members without the permission of the Central Bank.

## **Company Secretary**

Every company must have a secretary. The secretary is usually appointed by the directors. He is the chief administrative officer of the company. Every public and private company with a turnover of Rs. 1 million or an issued share capital over Rs. 500,000/- requires a company secretary.

## **Auditor**

Every company is required to keep proper books of accounts with respect to:

- all receipts and expenditures
- all sales and purchases of goods by the company
- the assets and liabilities of the company

Every company requires that the Balance Sheet of the Company be signed on behalf of the Board by two (2) directors.

The Profit & Loss Account and the Balance Sheet should give a "*true and fair view*". Only a member of the Institute of Chartered Accountants of Sri Lanka or a registered auditor can function as an auditor of the company.

### **4.3.4 Dissolution of a Company**

A company may be dissolved by:

- removal of the name of the defunct company
- consequent to a scheme of arrangement sanctioned by court
- winding up:
  - By a court (compulsory winding up)
  - Voluntary
    - members voluntarily wind up
    - creditors voluntarily wind up
  - Under the supervision of the court

#### **4.3.5 Joint ventures**

Joint ventures with majority non-resident ownership may have access to the domestic credit market on a case-by-case basis with prior approval from the Central Bank.

#### **4.3.6 Co-operatives**

Legislation has been passed to establish the Co-operative Employees' Commission and it makes special provisions with regard to wages and salaries in respect of employees of Co-operative Societies and their terms and conditions of employment. The Commission consists of 3 members appointed by the Minister in charge of the subject of co-operative development.

## **5 Taxation**

### **5.1 Overview and introduction**

The extent of the tax liability to Sri Lankans and non-nationals on profits and income depends on the residence status of the individual, company and body of persons in Sri Lanka.

Residents are taxed on worldwide income while non-residents are taxed on Sri Lankan source income only.

The maximum income tax rate in Sri Lanka is 35 per centum. Expatriate employees enjoy a concessionary rate of 15 per centum during their deemed non-residency period.

### **5.2 Administrative system**

The Department of Inland Revenue is within the purview of the Ministry of Finance of the Government of Sri Lanka, which advises Government on tax policy formulations. The Department of Inland Revenue is composed of the Commissioner-General of Inland Revenue who is the head of the Department and number of Commissioners, Deputy Commissioners, Senior Assessors, Assessors and Tax officers.

Further, the Department of Inland Revenue is responsible for the efficient administration of the following:

Direct Taxation

- Income Tax;
- Surcharge on Income Tax; and
- Save the Nation Contribution.

Other Forms of Taxation

- Goods and Services Tax;
- Turnover Tax;
- National Security Levy; and
- Stamp Duty.

Apart from the Central Government, Provincial Councils are also authorized to collect Turnover Tax under the constitution. At present, there are eight Provinces in the country and each Province has its own Provincial Council.

## **5.3 Direct taxation**

### **5.3.1 Income tax**

#### **Enforcement**

The existing income tax in Sri Lanka is based on the Inland Revenue Act, No. 38 of 2000 applicable from the year of assessment commencing on 1<sup>st</sup> April 2000.

#### **Basis of liability**

Income tax is an *annual tax* chargeable for *every year of assessment* of every person. In the case of a:

##### Resident Person

Liability is based on the profits and income wherever arising, i.e. his world income

##### Non-Resident Person

Liability is based on the profits and income arising in or derived from Sri Lanka which includes the following:

- Profits and Income derived from services rendered in Sri Lanka; or
- Profits and Income from property in Sri Lanka; or
- Profits and Income from business transacted in Sri Lanka whether directly or through an agent;
- Interest on certain loans payable to a non-resident;
- Certain royalties.

#### **Year of Assessment**

An year of assessment is a period of twelve months from the 1<sup>st</sup> of April of an year to the 31<sup>st</sup> of March of the immediately succeeding year.

Income tax is charged under the following categories :

- Individual
- Company
- Body of Persons

### **5.3.2 Individuals**

Threshold for the tax free income of the resident individuals as well as the non-nationals who are deemed to be non-residents and earn an income which solely arose from services rendered in Sri Lanka is Rs.144,000 per annum.

Tax rates are applied to individual income on a progressive scale through a 4-band rate system ranging from 10 to 35 per cent. (Refer appendix 2.1)

In case of a 'partnership,' partners' income is liable under the individual category in general circumstances.

Income of spouses is taxed separately. The total statutory income of a child (below 18 years) of a resident individual is aggregated with that of his father if the marriage persists or with the parent who maintains him if the marriage ceases to subsist.

Gross dividend income is aggregated with advance company tax paid in respect of the dividend.

### **5.3.3 Company**

Company income tax is made up of a tax on corporate income and tax on dividend is 15% of the gross dividends declared by the company. Generally, companies are liable to income tax on its taxable income at the rate of 35 per centum.

If a resident company pays dividend consisting of a qualifying distribution, it is required to pay advance company tax. A credit is given for this advance company tax paid, against the company's final tax liability.

### **5.3.4 A body of persons**

Executors and receivers, trusts, charitable institutions, welfare societies, provident funds, clubs and associations and other bodies of persons are also subject to income tax. The tax rates vary with a 10 per cent rate applying to charitable institutions, welfare societies and provident funds, 20 percent to clubs and associations and 35 percent to trusts and executors. (Refer Appendix 4)

#### **Resident or Non-resident**

*“Residence”* in the case of an individual, is determined on the basis of the physical presence in the country during the year of assessment, and in the case of a company or a body of persons on the basis whether its principal or registered office is located in Sri Lanka or whether its control or management is exercised in Sri Lanka.

An individual who is physically present in Sri Lanka for 183 days or more during an year of assessment shall be deemed to be resident in Sri Lanka throughout that year of assessment.

### **Sources of Income**

Income tax is charged on the profits and income arising from the following sources :

- Trade, business, profession or vocation
- Employment (Refer appendix 2.2)
- Net annual value of land and improvement
- Dividends, interest or discounts
- Charges or annuities
- Rents, royalties or premiums
- Capital gains (Refer appendix 1)
- Any other sources not including profits of a casual and non-recurring nature.

### **Filing of Return**

Every person who is chargeable with income tax for any year of assessment should furnish a return, on or before the 30<sup>th</sup> day of November immediately succeeding the end of that year of assessment.

### **Collection of Tax**

#### Deduction of Tax at Source

##### a) Pay-As-You-Earn (PAYE)

A PAYE scheme applies for specified employees on their employment income. Deduction of tax is made at source by the employer. Pay-As-You Earn taxes are calculated according to the tables provided by the Revenue authorities.

##### b) Withholding Tax

#### *Residents*

Every payer is required to deduct tax at the time any sum of money representing any dividend, (except quoted public companies and the companies which declare dividend out of exempt profits or dividend received) interest and specified fee (except the specified fee and interest payments made to the payees who were issued with a direction stating no need to deduct by the Department of Inland Revenue) is paid or credited.

Where withholding tax is deducted, such tax is treated as a credit and eligible to be set off against a person's income tax liability.

#### *Non-Residents*

Dividends paid by companies to non-residents are subject to withholding tax at 15%.

### *Non- Citizens*

Payments to foreign entertainers or artistes, who are non-citizens of Sri Lanka, are subject to withholding tax at 15%.

### *Person or Partnership outside Sri Lanka*

Payments to any person or partnership out of Sri Lanka as interest, rent, royalties or annuities attract a withholding tax at 20%.

### **Self Assessment**

All taxpayers are required to pay their taxes by self-assessment for any year of assessment, in four installments on or before the 15<sup>th</sup> of August, 15<sup>th</sup> of November, 15<sup>th</sup> of February in that year of assessment and 15<sup>th</sup> of May in the next succeeding year of assessment.

However, if a person has paid quarterly installment of tax of any year of assessment, a sum which is not less than one-quarter of the income tax payable by him for the year immediately preceding that year of assessment, then he is not liable to pay any penalty in respect of those quarterly installments until 30<sup>th</sup> of September immediately succeeding the end of the year of assessment.

## **5.3.5 Surcharge on income tax**

### **Enforcement**

Surcharge on corporate income tax has been imposed by the Surcharge on Income Tax Act, No.6 of 2001 for a period of one year commencing from April 1, 2001 as proposed in the Budget Speech 2001.

### **Basis of Liability**

Every company, which is chargeable with income tax under the Inland Revenue Act, is liable to pay a surcharge on the income tax payable by the company for the year of assessment ending on March 31, 2002.

### **Rates**

Surcharge is calculated at a flat rate of 20 per centum of the income tax payable.

### **Filing of Return**

If a company furnishes a return of its income tax for that year as per the requirements of Inland Revenue Act, then it will be deemed as, that it has sufficiently complied with the requirement of this Act.

### **Collection of Tax**

Every company liable to pay surcharge, should pay a sum of not less than 50 per centum on or before 15<sup>th</sup> of August 2001 and the balance on or before 15<sup>th</sup> November 2001 of the Surcharge payable for that year of assessment.

However, penalty will not accrue if, 10 per centum is paid on or before August 15, 2001 and another 10 per centum is paid on or before 15<sup>th</sup> November 2001 of the income tax payable for the year of assessment commencing on 1<sup>st</sup> April 2000, and the excess of the surcharge payable for that year of assessment on or before 30<sup>th</sup> November 2002.

### **5.3.6 Save the nation contribution**

#### **Enforcement**

Save the Nation Contribution is charged under the Save the Nation Contribution Act, No. 5 of 1996 from the quarter commencing from April 1, 1996.

#### **Basis of Liability**

Emoluments of every Citizen of Sri Lanka, if he/she is an employee or an individual engaged in any profession or vocation or similar activity, individually or in partnership with other is liable for Save the Nation Contribution. Police, Army, Navy and Air Force personnel are exempt from the payment of this contribution.

#### **Rates**

Quarterly emoluments are taxed under 3 – band rate system. (Refer appendix 5)

#### **Filing of Return & Collection of Tax**

Every employer who collects the contribution on behalf of the employee, who is liable for the Save the Nation Contribution deduction, should pay the monthly recoveries on or before the 15<sup>th</sup> day of succeeding month, while professionals should make quarterly payments on or before the 15<sup>th</sup> day of the month after the expiry of the quarter.

Return should be furnished, each quarter to the Commissioner-General not later than the 15<sup>th</sup> day of the month after the expiry of each quarter.

## 5.4 Other forms of taxation

### 5.4.1 Goods and services tax - GST

#### **Enforcement**

The Turnover Tax, which was a multistage tax mainly on the domestic consumption of goods and services, was replaced by a value added tax from April 01, 1998 through the Goods and Services Tax Act, No 34 of 1996. i.e. By the Goods and Services Tax (GST) except on the financial services sector.

#### **Basis of Liability**

Goods and Services Tax is imposed:

- On the **taxable supply** of Goods and Services by a **registered person** carrying on a **taxable activity** in Sri Lanka; and
- On the importation of goods into Sri Lanka by any person.

#### Taxable Supply

'Taxable supply' means any supply of goods or services made or deemed to be made in Sri Lanka by a registered person carrying on a taxable activity, including tax charged at the rate of zero per cent.

#### Registered Person

A 'Registered person' means a person who –

Conducts a taxable activity and supplies goods or services in Sri Lanka in excess or likely to be in excess of Rs. 500,000 in any quarter,

Conducts a taxable activity and supplies taxable goods and services in Sri Lanka in excess or is likely to be in excess of Rs. 1,800,000 in four successive quarters,

Imports goods irrespective of the value of the imports, and who is **registered** or is **liable to be registered** or is **deemed to be registered** under the GST Act.

## Taxable Activity

'Taxable activity' means:

- Any activity carried on or carried out as a business, trade, profession or vocation other than in the course of employment or every adventure or concern in the nature of a trade;
- The provision of facilities to its members or others for consideration and the receipt of subscription in the case of a club, association or organization;
- Anything done in connection with the commencement or cessation of any activity or provision of facilities referred to in the first two activities;
- The hiring or leasing of any movable property or the renting or leasing of any immovable property or the administration of any property;
- The exploitation of any intangible property such as patents, copyrights or similar assets.

## **Rates**

The standard rate of GST is 12.5 per centum while the export of goods and certain services are zero-rated. Supply of goods and services listed under the Schedule of the Goods and Services Tax Act are exempt from tax.

## **Credits for Input**

A registered person is entitled to a credit for his input tax except the input tax attributable to the exempted supplies against the output tax.

Excess input tax is refunded upon application made to the Commissioner-General. In the case of a person whose supplies are zero-rated, input tax will be refunded within one month from the end of the taxable period or from date of receipt of the return for the taxable period, whichever is later. In most of the other cases, excess input tax will be carried forward to the next taxable period and setoff against the output tax of that taxable period. Any residue not setoff in the period of six months will be refunded within one month after the end of the said six months. Any refund made after this will be paid with interest.

## **Filing of Return & Collection of Tax**

Every registered person should furnish a return of his supplies relating to the taxable period to the Commissioner-General not later than the last day of the month after the expiry of each taxable period and pay the tax accordingly.

## **5.4.2 Turnover tax - TT**

### **Enforcement**

#### Central Government

Turnover Tax was introduced by the Turnover Tax Act, No. 69 of 1981, which came into effect from 13<sup>th</sup> November 1981.

#### Provincial Council

From 1<sup>st</sup> January 1991, turnover tax is charged by Provincial Councils of each Province under its Financial Statute.

### **Basis of Liability**

#### Central Government

Presently, turnover tax is charged only on the turnover of finance, money lending, pawn broking and banking business.

#### Provincial Council

Every person who carries on a wholesale or retail business in every Province is chargeable with turnover tax on the turnover except in the case of the sale by a manufacturer.

### **Rates**

#### Central Government

Currently, Turnover Tax is charged at a standard rate of 1 per centum except in the business of pawn broking, which is charged at 2 per centum.

#### Provincial Council

Generally turnover tax is charged at 1 per centum but it is subject to a maximum of 5 per centum.

## **Filing of Return & Collection of Tax**

### Central Government

Persons who are liable for turnover tax, should pay the tax on or before the 15<sup>th</sup> day of succeeding month if the turnover is more than 5million, else on or before the 15<sup>th</sup> day of the month succeeding the quarter and furnish a return of his turnover for each quarter to the Commissioner-General not later than the 15<sup>th</sup> day of the month after the expiry of each quarter.

### Provincial Council

Every person who is liable to turnover tax, should pay the tax and furnish a return of his turnover for each quarter to the Provincial Commissioner not later than the 15<sup>th</sup> day of the month after the expiry of each quarter.

### **5.4.3 National security levy - NSL**

#### **Enforcement**

This was introduced in January 1992 by the Defence Levy Act, No. 52 of 1991 as Defence Levy and renamed as National Security Levy by the Amendment Act, No. 36 of 1995.

#### **Basis of Liability**

Every person who carries on the business of manufacture, insurance, banking, finance, providing a service of any description or imports any article is chargeable with this levy. However, for the calculation of levy, certain classes of turnover are excluded.

#### **Rates**

Prevailing rate for National Security Levy is 7.5 per centum on the turnover other than the turnover from import or manufacture of any plant, machinery and equipment. Levy of 0.5 per centum is charged on the turnover from import or manufacture of any plant, machinery and equipment.

#### **Credits for Input**

Levy paid by a **manufacturer** on any article imported by him or purchased from a registered manufacturer, could be claimed as a credit against the National Security Levy payable on the turnover, if, such article is

- used exclusively in the manufacture, and
- not a capital asset.

## **Filing of Return & Collection of Tax**

Every person who is liable to National Security Levy, should pay the levy on or before the 15<sup>th</sup> day of succeeding month and furnish a return of his turnover for each quarter to the Commissioner-General not later than the 15<sup>th</sup> day of the month after the expiry of each quarter.

### **5.4.4 Stamp duty**

#### **Enforcement**

Stamp Duty is charged in terms of the Stamp Duty Act, No. 43 of 1982 and has been applicable from 1<sup>st</sup> January 1983.

#### **Basis of Liability**

Stamp Duty will be charged at prescribed rates on the following:

- Every instrument, which is executed, drawn or presented in Sri Lanka.
- Every document presented or filed in Civil Proceedings instituted in the Courts.
- Every bill of exchange, cheque or promissory note drawn outside Sri Lanka and accepted or paid or presented for acceptance or payment or endorsed, transferred or otherwise negotiated in Sri Lanka.
- Every instrument (not being a bill of exchange or promissory note) executed outside Sri Lanka and received in Sri Lanka being an instrument which relates to any property situated or any matter or thing done, or to be done in Sri Lanka.
- Every document in relation to any transaction, which a person enters into with any bank in Sri Lanka for the withdrawal or transfer of money.

#### **Rates**

Depending on the different classes or categories of the instrument, different rates will be prescribed.

#### **Collection of Tax**

Stamp Duty should be paid before or at the time of executing the instrument and such payment will be indicated on such instrument by means of affixing adhesive stamps, by embossing documents or by composition duty.

#### **5.4.5 Taxation of foreign enterprises and operations**

##### **Foreign investments**

The principal law applicable to foreign investments is Board of Investment Law No. 4 of 1978. Board of Investment of Sri Lanka is the major body, which approves foreign investments under Board of Investment law. The Board of Investment is structured to function as a central facilitation point for investors. Significantly, when an agreement is signed with the Board of Investment, the specific incentives granted to an eligible company remain valid for the life of the enterprise. The provision and the spirit of the agreement cannot be changed by successive governments.

##### **Tax incentives**

###### Tax Incentives for Board of Investment Approved Companies

Board of Investment has the power under the Board of Investment law to supersede the Inland Revenue Act and grant tax holidays, preferential tax rates, exemption from custom duty and foreign exchange controls in accordance with the investment criteria such as priority sectors, capital inflow, location, etc.

###### Expatriate Concessions

Expatriate employees will be deemed as non-residents for the first three years of employment in Sri Lanka. If employed in a Board of Investment company this period is extended to five years. Reduced rate of 15 per centum is applicable in this period.

###### Resident Guest Scheme

Non-citizens in Sri Lanka who come under this are deemed to be non-resident and excluded from liability to tax on profits and income arising outside Sri Lanka and income accruing from any account opened by such person in a commercial bank.

###### Taxation of Investment Income

Non-residents are not subject to tax on non Sri Lankan investment income.

###### Exemptions

Interest, annuity, ground rent and royalty received by a non- resident person from a person outside Sri Lanka are exempt from income tax.

Dividend from a non-resident company is exempt in the hands of a non-resident person. Services rendered by a non-resident is exempt from income tax, if it doesn't exceed Rs.144,000.

### Reduced Rates

Certain interest income, royalties and employment income are taxed at reduced rates.

### Transfer Pricing

Where a non-resident person and a resident person are closely connected and their affairs are so arranged that it produces to the resident person no profits or less than the ordinary profits which might be expected to arise from such business in the normal course of trading, their affairs may receive scrutiny by the revenue authorities. In such circumstances, the business done in pursuance of such connection by such non-resident person is deemed to be done in Sri Lanka and is assessable and chargeable with income tax in respect of any profits evaded by such arrangement, in the name of the resident person.

#### **5.4.6 Double tax treaties**

With a view to avoiding double taxation, Sri Lanka has entered into Treaties with most of the countries. Sri Lanka's tax treaties have generally followed the UN model convention.

##### **Countries with which Treaties are in Force**

Canada	Malaysia
Korea	Singapore
Australia	Egypt
Iran	Mauritius
Poland	Sweden
Bangladesh	Finland
Italy	Nepal
Romania	Switzerland
Belgium	France
Japan	Netherlands
Russia	Denmark
Saudi Arabia	

##### **Awaiting Entry into Force**

Philippines

##### **Under Negotiations**

Austria  
Jordan  
New Zealand  
Bulgaria  
Kuwait

## **6 Exchange control**

The law that deals with foreign exchange in Sri Lanka is the Exchange Control Act No24 of 1953 and its subsequent amendments. The Central Bank is responsible for carrying out the provisions of this Act.

The Exchange Control Act applies to a variety of exchange transactions involving importation of capital, repatriation of capital, exports, imports, etc. Since March 1994, in Sri Lanka a rupee (LKR) has been made fully convertible on the current account. Commercial banks now have complete freedom in transactions related to imports, exports and services. Current account controls have been abolished.

The Department of Exchange Control is the administrative agency for foreign investments, which fall under the Board of Investment.

The Board of Investment 1978 has stipulated that investments made under agreements with the BOI may be exempted from the provisions of the Exchange Control Act.

The following outward remittances may be made by foreign investors under the prevailing liberal exchange control regulations:

- Profits (interim and final) of branches in Sri Lanka to their parent companies and to non-resident partners of partnerships operating in Sri Lanka.
- Dividends (interim and final) accruing to non-resident shareholders of companies incorporated in Sri Lanka.
- Interest, royalties and technical service fees by enterprises established in the BOI area in accordance with the agreements entered into with the Greater Colombo Economic Commission.
- Life insurance premiums by foreign nationals temporarily residing in Sri Lanka.
- Remittance of Shares in a company incorporated in Sri Lanka (for the purpose of investing in the Economic Commission area) to a resident in Sri Lanka or to a non-resident outside Sri Lanka.
- Any unutilised balance in excess of the minimum requirement of the investor.
- Capital gains and income from investment.
- Sale proceeds of investments.
- Capital, including liquidation proceeds
- Pensions, salaries and commissions paid to non-residents

### **6.1 Remittance of Family Maintenance**

Indian and Pakistani nationals may remit for family maintenance a sum not exceeding the equivalent of LKR 750 per month or one third of their gross monthly income whichever is less.

Other foreign nationals may remit GB P 85 per month for a wife, GBP 105 for a boy in a senior school, GBP 100 for a girl in a senior school, GBP 75 for a child in a junior school and GBP 25 for other children.

The total remittance cannot exceed two thirds of the foreign national's gross monthly income in the case of other direct dependents. Foreign nationals who are temporarily residing in Sri Lanka on short-term contract may remit for family maintenance upto two thirds of their gross monthly income.

The balance may be transferred at the time of departure.

Sri Lankan nationals are not entitled to any exchange for family remittance

## **6.2 Emigrants**

Emigrants will be allowed the following exchange facilities subject to the following restrictions:

- Foreign exchange allowance.
- Cost of passage to the country of intended residence
- Transfer of funds realised from capital assets of the emigrant.
- Cost of transport of goods by sea,
- The cost of passage and cost of transport of goods by sea are limited to the cost of passage by the most direct route certified by a travel agent and the cost of transport of goods by sea certified by a freight agent.
- Authorised dealers may at their judgement and direction release a reasonable amount of foreign exchange as an exchange allowance for each individual emigrant.
- Transfer of funds realised from capital assets is limited to a sum of rupees seven hundred and fifty thousand for each individual emigrant subject to a ceiling of rupees one million per family.

An emigrant is required to submit the following documents in applying for the foreign exchange facilities.

- An affidavit by the emigrant declaring.
- The final and irrevocable decision of the emigrant to leave Sri Lanka for permanent residence abroad.
- The date of intended departure.
- That the emigrant is not a director of any company incorporated in Sri Lanka.
- That the emigrant is or is not a taxpayer in Sri Lanka.
- An income tax clearance certificate in the case of an emigrant who is a taxpayer in Sri Lanka or when the total exchange allowance exceeds rupees two hundred thousand or in the case of transfer of funds realised from capital assets.
- In the case of an emigrant who was employed immediately prior to departure, a letter from the employer accepting the resignation of the emigrant.

- Certified copies of the passport of the emigrant and of the immigration visa to the country of destination if such immigration visa is required in that country.

An emigrant on departure from Sri Lanka is entitled to the following facilities.

- Export of personal effects other than personal jewellery, up to the value of rupees forty five thousand per individual emigrant above the age of twelve years and rupees fifteen thousand per child under the age of twelve years.
- Export of personal jewellery to the value of rupees one hundred and fifty thousand per married female, rupees sixty thousand per unmarried female above the age of 12 years, rupees thirty thousand per female under the age of twelve years and rupees thirty seven thousand five hundred per male.
- An authorised dealer may permit an emigrant, after his departure from Sri Lanka, to remit the full value of the income of the emigrant (including the interest and rent) derived from any investment made by the emigrant in Sri Lanka and the interest earned on funds in a blocked account maintained by the emigrant.
- Any applicants for remittance of any other funds after the emigrant's departure from Sri Lanka shall be forwarded to the Controller of Exchange and such remittance shall be made from a blocked account in the name of the emigrant.

Travel for the following purpose may be permitted without any restrictions on the number of trips per year or the selection of the airline.

- Official duty,
- Business and
- Medical, holiday and pilgrimage, employment, education, private training, conferences and workshops and similar purposes.

Foreign Exchange will be allowed for persons undertaking travel on government business on the basis of certificate issued by the head of the relevant government institution.

Foreign Exchange may be released for business travel if there is a letter from the chairman or director of the company or partner recommending the trip abroad and stating that the journey is being undertaken on company partnership business and that the full cost of the journey is being charged against company/partnership funds; and details of the foreign exchange are required.

Exchange may be allowed as follows:

For Chairman, Directors of Companies and Partners:

- LKR 350 per diem up to maximum of 30 days for Bangladesh, Burma, India, Maldives, Island, Nepal and Thailand.
- USD 75 per diem up to a maximum of 30 days for other countries.

For other business executives:

- LKR 225 per diem for Bangladesh, Burma, India, Nepal, Pakistan & Thailand.
- USD 50 per diem for other countries up to a maximum of 30 days.

To verify the bona fide of a request for release of foreign exchange for travel abroad, besides valid visas, other relevant documents may be called for.

### **6.2.1 Blocked Funds held by Sri Lankan emigrants and Foreign Nationals.**

Funds realised on the sale of capital assets belonging to Sri Lankan emigrants are kept, in blocked accounts while the interest earned on such accounts are permitted to be remitted after meeting tax liabilities, if any.

Release of such fund is remitted through commercial banks subject to a limit of Rs.750,000 per individual and Rs.,1 million per unit.

## **6.3 Capital Transactions**

### **6.3.1 Non-resident Investment in Sri Lanka**

With effect from March 2000, non-resident investment in shares in a banking institution was permitted up to 60 percent; the earlier stipulated limit was 49 percent. The limit with respect to companies engaged in insurance business was specified at 90 percent.

In companies engaged in stock brokering, the limit was 49 percent but where permission was granted by the Securities Exchange Commission was allowed up to 100 percent. Other financial sector activity is 49 percent.

Non-residents are permitted to invest in unit trusts registered with the Securities and Exchange Commission, on condition that Trust Deed creating the unit trust and agreement between the Trustees and the Managing Company contains a restriction that not more than 20 percent of the deposited property is to be invested in government securities.

Rupee lending to non-resident controlled companies.

With effect from April 2000, banks lend the following percentages of loans to non-resident controlled companies approved under section 17 of the Board of Investment Act.

Foreign Banks	-	No limit
State Banks	-	2 % of total lending to the private sector
Domestic Private Banks	-	3 % of total lending to the private sector
Licensed Specialised Banks	-	5 % of total lending to the private sector

### **6.3.2 Credit facilities to foreign controlled companies**

A loan overdraft or other credit facility by a person resident in Sri Lanka to a firm or company (other than a banking company) controlled directly or indirectly by persons resident outside Sri Lanka require the general or special permission of the Controller of Exchange.

For the above purpose a public company quoted in the Colombo Stock Exchange notwithstanding that a majority of its shares is owned by persons resident outside Sri Lanka will not be treated as a company controlled directly or indirectly by persons resident outside Sri Lanka and the grant of loans, overdrafts and other credit facilities to such companies does not require the general or special permission of the Controller of Exchange.

Subject to this condition a firm or company applying to general or special permission for the grant to such firm or company of a loan, overdraft or other credit facility is required to make its application to the Controller of Exchange through, an authorised dealer.

The Controller of Exchange has granted permission to authorised dealers to issue or renew any guarantee the implementation of which would involve payment of Sri Lankan rupees remittable to a person resident outside Sri Lanka in foreign exchange or payments outside Sri Lanka in foreign currency for export purposes and to make payments in respect of claims on any such guarantee.

### **6.3.3 Share Investment External Rupee Accounts (SIERA)**

Foreign investors may invest in shares of:

- companies listed at the Colombo Stock Exchange; and
- unlisted companies in which foreign investment has been approved by the Board of Investment of Sri Lanka or the Government of Sri Lanka or by any legal or administrative authority set up for approval of any such investment.

subject to the exclusions, limitations and conditions set out by the Controller of Exchange in the notice published in the Government Gazette (Extraordinary) No.721/4 of 29<sup>th</sup> June 1992.

To facilitate investment by foreign investors in shares of companies, the authorised dealers are permitted to open and maintain Share Investment External Rupee Accounts, hereafter referred to as “SIERA” for :

- Country funds and Regional funds as may be approved from time to time by the Ministry of Finance;
- corporate bodies incorporated outside Sri Lanka;
- citizens of foreign states, whether resident in Sri Lanka or resident outside Sri Lanka;
- citizens of Sri Lanka resident outside Sri Lanka.

A SIERA shall only be credited with -

- inward remittances or transfers from a Non Resident Foreign Currency account or from an off shore unit of a bank and converted into Sri Lankan rupee at the prevailing rate of exchange;
- sale proceeds of shares;
- dividends on shares;
- commissions related to transactions in shares;

and funds in a SIERA may be utilised for:

- payments to brokers or commercial banks for investment in shares in accordance with instructions issued by the account holder;
- expenses in Sri Lanka of the account holder;

Authorised dealers may enter into contracts with foreign investors for the purchase of foreign exchange forward, for settlement of payments in respect of shares purchased on their behalf up to a period calculated in accordance with the rules laid down by the Colombo Stock Exchange for buyers' settlements. The duration of such contract is limited to a period from the date of transaction to date of settlement i.e., trade day plus five market days. Buyers' settlements in respect of foreign exchange purchases forward shall be routed through the SIERA of the purchaser.

#### **6.3.4 Non-Resident accounts**

Non-resident accounts may be held by:

- Emigrants
- Foreign investors, foreign collaborators in local industrial and agricultural development projects
- Foreign organisations extending financial aid for local projects
- Foreign banks
- Non-national resident outside Sri Lanka
- Firms and companies registered outside Sri Lanka
- Sri Lankan nationals resident outside Sri Lanka

#### **6.3.5 Foreign Currency Accounts**

Banks may be authorised by the Board of Investment to operate secret numbered banking accounts in local currency on behalf of persons who are not citizens of Sri Lanka.

### **6.3.6 Visa**

Non-national Enterprises that wish to employ expatriate personnel must obtain a letter of recommendation from the Appraisal Department. This letter must then be submitted to the Department of Immigration and Emigration to obtain necessary visas and work permits.

Foreign investors should obtain an entry visa to Sri Lanka.

## **7 Labour standards and labour relations**

The Sri Lankan industrial law consists of about forty labour statutes, regulations gazetted under the labour statutes, decisions made by the Labour Courts and the Appellate Courts and collective agreements.

The labour laws of Sri Lanka are equally applicable to enterprises by foreign investors in the Export processing zones and other Board of Investment enterprises. No power has been granted to the Board to enter into an agreement with any business enterprise, to exempt, modify or vary the provisions of labour legislations of Sri Lanka. The labour legislations have been applied without any change in the context of foreign investment.

The Board of Investment in Sri Lanka will oversee the industrial relations situation in the enterprises coming under its purview. Enterprises are expected to maintain healthy labour relations.

### **7.1 Contract and Employment**

An employment relationship arises from a contract of employment. An employer and an employee must negotiate an employment contract or the court may imply the existence of an employment contract to accomplish justice.

A written contract of employment embodying terms and conditions of service including the designation or category of the employee, normal hours of work, rate of pay, period of training if any, probationary period, leave, holidays and superannuation contributions has to be issued to every worker including trainees and acknowledgement of receipt obtained by the employer.

### **7.2 Classification of Workers**

#### **Trainees**

Training period consists of 6 months/156 working days. Minimum wages payable are determined.

#### **Unskilled**

Work, which does not involve any training. Minimum wages payable are determined.

#### **Semi-skilled**

On completion of a training period of 6 months, a worker is classified as semi-skilled. Minimum wages payable are determined.

#### **Skilled**

Wages are determined by the contract of employment. However, such wages should necessarily be more than wages paid to semi-skilled worker.

## **7.3 Nature of Employment**

### **Permanent**

A permanent employee is one whose contract of employment is automatically renewed until the employee reaches the age of retirement.

### **Temporary**

A temporary employee is one whose employment is of temporary nature, the duration of which is limited by the job or time.

### **Casual**

A casual employee is one who is employed on a daily basis and not on a regular contract of employment.

### **Probationary**

A probationary employee is one who is employed by an organisation to assess his aptitudes, abilities, characteristics and his devotion to work before taking the employee into the permanent cadre.

### **Fixed term contract**

A fixed term contract employee is one who is on a contract of employment, which expires on a specific date. When the employee is on a fixed term contract, his term of employment is confined to the period stipulated in the contract.

## **7.4 Recruitment**

Minimum age for recruitment shall be 18 years.

Persons below 18 years but above 16 years can be employed subject to the following conditions:

- Persons under 18 years cannot be employed for more than 10 hours of overtime during any week
- Persons under the age of 18 years cannot be employed in the night from 10 p.m. to 6 a.m.

## **7.5 Retirement**

The normal age of retirement is 55 years. However, extension beyond 55 years can be granted at the discretion of the management.

## **7.6 Equal status**

Male and female employees shall get equal remuneration and facilities in Sri Lanka.

## **7.7 Hours of work on normal working days**

Normal working days for office employees are from Monday to Saturday.

From Monday to Friday, office employees work for 8 hours duration inclusive of interval for meal or rest.

Saturday is a half-day of 5 hours duration.

Factory workers work in shifts:

One shift operation is from Monday to Friday for 9 hours per day inclusive of an interval of one hour for a meal or rest. Saturday is a short working day of 6 ½ hours inclusive of an interval of one hour for a meal or rest.

The two three-shift operations are from Monday to Saturday. From Monday to Friday factory employees work for 8 hours per day inclusive of an interval of half an hour for a meal or rest. Saturday is a short working day of 5 ½ hours inclusive of an interval of half an hour for meal or rest.

## **7.8 Night Work**

There are no restrictions on employment of male workers on night shift from 10 p.m. to 6 a.m.

Employment of female workers on night work from 10 p.m. to 6 a.m. will be allowed on the following conditions:

- written consent of the worker
- the employer should get prior approval from the Industrial Relations Department of the Board of Investment.

A maximum of 10 days night work is allowed per female worker in any one month.

## **7.9 Wages**

All employees are paid a monthly salary. Only authorised deductions such as loans, cash advances obtained by the employees, income tax, National Security Levy, workers contribution to EPF and any other approved deductions can be made from wages.

Any work performed in excess of the normal working day is to be treated as overtime work and employees shall be remunerated accordingly.

Proper wages records indicating basic wages, allowances, overtime Sunday/Public Holiday earnings and deductions shall be maintained and kept in the enterprise.

## **7.10 Holidays**

Office employees are granted half-holiday on Saturday afternoon and a whole holiday on Sunday with full remuneration. If a statutory holiday falls on such days, an alternative half holiday or whole holiday shall be granted either in the same week or in the week immediately succeeding.

For factory workers, Sunday shall be a weekly holiday and it is an unpaid holiday.

Statutory Public Holidays declared by the Government for the mercantile sector shall be allowed with full remuneration.

If an employee works on a Public Holiday, he shall be paid not less than double the daily rate of wages.

## **7.11 Leave**

### **Annual Leave**

An employee shall be granted 14 days vacation leave with pay in respect of the second and any subsequent year, if he has been continuously in employment during the year.

Annual leave earned during particular year has to be taken in the succeeding year on days mutually agreed upon by the employer and employee.

### **Casual Leave**

An office employee has to be granted 7 days casual leave with pay from the second year of employment and on the basis of one day per every two months service during the first year of employment.

### **Sick Leave**

Sick Leave shall be granted and extended at the discretion of the management.

### **Maternity Leave**

A female factory employee shall be allowed 12 weeks leave with pay. Such leave shall be in addition to other paid leave holidays she is entitled to.

## **7.12 Suprannuation Benefits**

### **Employees Provident Fund**

- All employees are entitled to EPF.
- Employees' contribution is 8 percent and the employer has to contribute an amount equivalent to 12 percent of the employees' total earnings.
- Earnings include wages allowances, payments in respect of holidays and leave, cash values of food provided by the employer and meal allowance, but exclude overtime payments.

## **Employees Trust Fund**

- There is no contribution to this fund by the employee.
- The employer should contribute 3 percent of the total monthly earnings of the employee.
- The receipts of payments of EPF and ETF should be kept in the premises of the enterprises.

## **Gratuity**

- The payment of Gratuity Act, No. 12 of 1983 governs payment of gratuity.
- An enterprise which employs fifteen or more workers is liable to pay gratuity.
- An employee who has completed 5 years of service shall be paid gratuity on cessation of his employment.

## **7.13 Employment Injury Compensation**

In Sri Lanka, the statutory law provides for the payment of compensation to a worker for personal injury caused by accident arising and in the course of employment or for occupational diseases, which is reasonably attributable to the nature of the workman's employment.

An insurance policy to cover such risks should be obtained from a recognised insurance agent.

## **7.14 Termination of Services**

An employer can terminate the services of an employee on disciplinary and non-disciplinary grounds.

### **Disciplinary grounds**

An employer can terminate the services of an employee on disciplinary grounds such as misconduct, fraud, refusal to carry out lawful orders provided the normal disciplinary procedure has been followed.

Under the Industrial Disputes Act, No. 43 of 1952, for wrongful termination of services, an employee can seek redress in the Labour Tribunal before the expiry of 6 months from the date of such termination.

### **Non-disciplinary grounds**

In the case of workers who have been in employment for more than one year, layoff, retrenchment or termination of services for reasons other than on disciplinary grounds can be effected only with either the prior written consent of the worker or the prior written approval of the Commissioner of Labour.

Such approval will be granted after due inquiry.

On termination of employment, a worker should be issued with a letter stating the reasons for the cessation.

On termination of services, an employee's salary should be paid within two working days.

On termination of employment, payment should be made for any leave standing to the credit of an employee.

On termination or resignation of the employee, all certificates in the custody of the management shall be returned to the worker at least within 30 days from the date of termination or resignation.

## **7.15 Industrial Disputes**

The settlement of Industrial disputes is essential for the maintenance of harmonious industrial relations.

The mechanism provided by the Industrial Disputes Act for the settlement of industrial disputes consists of collective agreement, conciliation, arbitration and settlement by the Labour Tribunal and Industrial Court.

Settlement of Industrial disputes by collective bargaining or conciliation is more appropriate than other methods of settlement, since these methods are inexpensive, not time consuming and the terms are decided not by a third party but by the parties of an industrial dispute. To achieve this objective, the Board of Investment has set up an industrial Relations Department.

Any dispute or difference between the employer and employee/employees connected with the employment or non-employment, the terms of employment, the conditions of labour (health and industrial safety) or the termination of services of an employee shall be brought to the Notice of the Industrial Relations Department of the Board of Investment, so that such dispute could be resolved.

Whenever layoff, retrenchment, closure or termination of services of employees due to non-disciplinary reasons occur, requests shall be made to the Industrial Relations Department of the Board of Investment in advance so that suitable arrangements could be made with regard to such situations.

## **7.16 Social Partnership**

There are different forms of worker participation in Sri Lanka. They are Joint Consultative Council, Employees' Council and Quality Circles.

Employee's Councils are formed in the enterprises of the Free Trade Zones.

Every enterprise shall establish an Employee's Council with the concurrence of the Industrial Relations Department of the Board of Investment.

The Council shall consist of 5-10 members representing different Departments of the Factory. The Electoral Board of the Board of Investment will conduct the election to elect members to the Employees' Council.

The Council is an effective forum to achieve mutual cooperation of the employer and the employee in achieving greater efficiency and productivity, to promote employee welfare and resolve disputes between employees and management.

The progress of Council discussions and follow-up action taken will be monitored by the Board of Investment.

## **8 Accounting and auditing**

### **8.1 Accounting Profession**

The Institute of Chartered Accountants of Sri Lanka (ICASL) was established under the Institute of Chartered Accountants Act, No.23 of 1959 by the parliament. Council of the Institute is responsible for the management of its affairs, for the issue of Sri Lanka Accounting and Auditing Standards, and for the registration of and control of the maintenance of professional standards and discipline by the persons practicing or acting as accountants in Sri Lanka.

### **8.2 Auditing Requirements**

Companies Act, No 17 of 1982 has a mandatory requirement to all the companies to have their financial statements audited by the members of the Institute of Chartered Accountants or Registered Auditors.

Inland Revenue Act, No.38 of 2000 provides authority to the assessor to require to furnish a statement of accounts prepared by the approved accountant, in support of the return of the income. However, persons other than companies whose turnover exceeds 5 million and companies have to furnish the statement of accounts irrespective of whether notice is given or not.

### **8.3 Accounting Standards And Auditing Standards**

Sri Lanka Accounting and Auditing Standards Act, No 15 of 1995 recognizes the ICASL as the formulating body for Sri Lanka Accounting Standards (SLAS) and Sri Lanka Auditing Standards (SLAuS). The ICASL publishes these standards as a Gazette notification and informs general public of any revisions, alterations and amendments either through a Gazette notification or through other means.

Further, this Act has made provisions to formulate an Accounting Standards Committee and Auditing Standards Committee with the objective of making recommendations and assisting the ICASL to formulate and revise the SLAS and SLAuS.

Sri Lanka Accounting and Auditing Standards Monitoring Board is also created under the provisions of this Act to monitor the compliance with the SLAS and SLAuS by Specified Business Enterprises.

## **9 Appendices - Rates**

### **9.1 Appendix 1**

#### **Profits from Employment**

On the first Rs. 500,000 of the taxable income	Nil
On the next Rs. 150,000 of the taxable income	5%
On the next Rs. 150,000 of the taxable income	10%
On the balance of the taxable income	15%

### **9.2 Appendix 2**

#### **Capital Gains**

Period of Ownership	Maximum Rate
More than 2 years but not more than 5 years	25%
More than 5 years but not more than 15 years	17.5 %
More than 15 years but not more than 20 years	12.5 %
More than 20 years but not more than 25 years	5%
25 years or more	Exempt

### **9.3 Appendix 3**

#### **Income Tax for Individuals - Persons other than Expatriates**

On the first Rs. 100,000 of the taxable income	10%
On the next Rs. 100,000 of the taxable income	15%
On the next Rs. 100,000 of the taxable income	25%
On the balance of the taxable income	35%

### **9.4 Appendix 4**

#### **Income Tax for Companies**

Companies including Unit Trust and Mutual Fund	35%
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## 9.5 Appendix 5

### Income Tax for Body of Persons

Hindu undivided families	35%
Charitable Institutions	10%
Executor and Receivers	35%
Trustees	35%
Partnerships	35%
Co-operative Societies	20%
Mutual Life Assurance Companies	20%
Governments (Other than the Government of Sri Lanka and the Government of United Kingdom)	35%
Employees Trust Fund and Provident Fund or Pension Funds	10%
Any thrift, saving, or building society or welfare fund to which contributions are made by employees only or any gratuity fund approved.	10%
Liquidators of Companies	Rate of tax chargeable in company concerned
Business Undertaking vested in the Government under Business Undertaking (Acquisition) Act, No. 35 of 1971	
(i) on taxable income	35%
(ii) on the balance of the profits after deduction there from, of the tax payable under paragraph (i)	25%
Persons other than those who were not referred to above	20%

## 9.6 Appendix 6

### Save the Nation Contribution

Quarterly Emoluments :

Rs. 0	to	45,000	Exempt
Rs. 45,001	to	90,000	2%
Rs. 90,001	and above		3%