

CA Sri Lanka - Strategic Level

Strategic Tax Planning (SL - 25 - 4)

Tutorial 8 – Value Added Tax (III)

Prabath Weerasinghe – ACA,
MAAT, BB Mgt (HRM) SP,
ACMA, FCIT, MBA in
Taxation (PIM SJP)

**IMPOSITION OF VALUE ADDED TAX ON THE
SUPPLY OF FINANCIAL SERVICES BY
SPECIFIED INSTITUTIONS OR BY ANY
PERSON**

VAT ON FINANCIAL SERVICES

Chargeability: Chapter III A Sec 25 (A)

Value Added Tax shall be charged on the supply of financial services in Sri Lanka by **any person** other than,

- a Co- operative Society registered under the Co-operative Societies Law No 5 of 1972 or
- Lady Lochore Loan Fund established under the Act No 38 of 1951, or
- the Central Bank of Sri Lanka established by the Monetary Law Act, (Chapter 422) or
- Sri Lanka Deposit Insurance Scheme established by regulation made under the said Act:

Registration: Every specified Institution or other person, carrying on the business of supplying of any financial services in Sri Lanka, shall be required to be registered

Where the value of such supplies for a period of three months exceeds three million rupees or for a period of twelve months exceeds twelve million rupees, as the case may be, if such registration has taken place for any period on or after May 2, 2016.

- An application for registration in the specified form to the Commissioner-General not later than thirty days from the date of completion of the above requirements

VAT ON FINANCIAL SERVICES

Supply of financial services means -

- a) the operation of any current, deposit or savings account;
- b) the exchange of currency;
- c) the issue, payment, collection or transfer of ownership of any note, order for payment, cheque or letter of credit ;
- d) the issue, allotment, transfer of ownership, drawing, acceptance or endorsement of any debt security, being any interest in or right to be paid money owing by any person other than the transfer of nonperforming loans of a licensed Commercial Bank to any other person in terms of a re-structuring scheme of such bank as approved by the Central Bank of Sri Lanka with the concurrence of the Minister;
- e) the issue, allotment, transfer of ownership of any equity security or a participatory security ;
- f) issue, underwriting, sub-underwriting or subscribing of any equity security, debt security or participatory security

VAT ON FINANCIAL SERVICES

Supply of financial services means –

g) the provision of any loan, advance or credit;

h) the provision -

- of the facility of instalment credit finance in a hire purchase conditional sale or credit sale agreement for which facility a separate charge is made and disclosed to the person to whom the supply is made;
- goods under any hire purchase agreement or conditional sale or hire purchase agreement while have been used in Sri Lanka for a period not less than twelve months as at the date of such agreement, or
- of leasing facilities under any finance lease agreement

VAT ON FINANCIAL SERVICES

Registration

- Provided further, the Commissioner-General shall register any person who has not made an application for registration under this Chapter if the Commissioner- General having regard to the nature of the activities carried on or carried out by such person, is of opinion that such person is required to be registered.
- In the circumstances such person shall be afforded an opportunity of being heard prior to being registered under this Chapter and register such person accordingly with effect from such date as may be determined by the Commissioner-General.

Every registered person shall notify the Commissioner-General in writing or by electronic means of any change-

- a) in the name, address and place at which any taxable activity is carried on or carried out by such person;
- b) in the nature of the taxable activity carried on or carried out by such person;
- c) in the person authorized to sign returns and other documents; and
- d) in ownership of the taxable activity,

not later than fourteen days after the occurrence of such change

VAT ON FINANCIAL SERVICES

- **Taxable period:** The taxable period of every registered specified institution or other person shall be **twelve months** for any taxable period

Provided that, in the case of a specified institution or any person whose accounts are made up for a period of twelve months ending on the 31st day March, such period of twelve months may be commenced on the 1st day of April.

- **Tax Return:** Every registered specified institution or other person shall in respect of each taxable period furnish a return in the specified form within six months immediately succeeding the end of that taxable period.

Provided further, in the event of changing the accounting period with the approval of the Commissioner-General, the taxable period may be adjusted at the time of such change

VAT ON FINANCIAL SERVICES

- **Tax Return**

Documents to be furnished with annual return

Following documents shall be submitted with adjustment referred to the Section 25C (1) of the VAT Act for the purpose of fulfillment of the submission of the return referred to the Section 25B.

- (a) Audited Statement of Accounts for the relevant period.
- (b) Detailed profit and loss account for the relevant period.
- (c) A schedule in respect of emoluments payable.
- (d) A schedule in respect of economic depreciation.
- (e) Breakup of the value of supply declared in the Value Added Tax return furnished for the relevant periods as per Section 21 of the VAT Act.
- (f) Reconciliation of turnover with the Financial Statement in the following format.

VAT ON FINANCIAL SERVICES

- **Tax Return.....:**

Every registered person who furnishes a return which is not in such form or fails to furnish an interim estimate on every six months or fails to furnish the contents of such return or the interim estimate as specified by the Commissioner-General, shall be deemed, not to have furnished a return of Value Added Tax on the supply of financial services.

Where any registered person furnishes a return of Value Added Tax on the supply of financial services or an interim estimate on or before the date as specified for any taxable period or any six months period, as the case may be, and is deemed not to have furnished a return of Value Added Tax on the supply of financial services, **Assistant Commissioner shall, before the expiry of thirty days from the due date for the submission** of the return or interim estimate, inform such person in writing, that the return or the interim estimate furnished by him does not contain all such particulars in such form and relevant schedules as specified by the Commissioner- General.

VAT ON FINANCIAL SERVICES

- **Tax Return.....:**

Where any registered person receives any notice as stated above, such person may within thirty days of receipt of such notice, furnish to the Commissioner-General all such particulars in such form and relevant schedules required to make the return submitted a proper return, and then the above provisions shall thereafter not apply in respect of such return (will be accepted as a Proper Return)

Tax Payment: Tax payable for any taxable period by every registered specified institution or other person shall be paid on a monthly basis on or before the twentieth day of the succeeding month

The tax payable by every registered specified institution or other person on monthly basis shall be adjusted with the total liability for every six months period with the submission of the interim estimate if the monthly payments made are less than the tax calculated based on the interim estimate.

VAT ON FINANCIAL SERVICES

- **Tax Return.....:**

Where any registered person receives any notice as stated above, such person may within thirty days of receipt of such notice, furnish to the Commissioner-General all such particulars in such form and relevant schedules required to make the return submitted a proper return, and then the above provisions shall thereafter not apply in respect of such return (will be accepted as a Proper Return)

Tax Payment: Tax payable for any taxable period by every registered specified institution or other person shall be paid on a monthly basis on or before the twentieth day of the succeeding month

Any tax which is not so paid as set out as above shall be deemed to be in default and any registered specified institution or other person shall be deemed to be a defaulter.

VAT ON FINANCIAL SERVICES

Calculation of Tax

Every registered specified institution shall be liable to tax for each taxable period on its total value addition of such institution which includes the **net profits or loss**, as the case may be, **before payment of income tax** on such **profit computed** in accordance with **accepted accounting standards**, subject to an **adjustment for economic depreciation**, determined by the Minister having regard to the interest of economy and maintaining the uniformity of allowable depreciation by Order published in the Gazette, **and the emoluments payable to all the employees** of such institution.

Where the amount of profits cannot be accurately ascertained for monthly payments, such amount may be estimated on the basis of available information, and every registered specified institution or any other person shall furnish an interim estimate of the profits in the specified form in respect of each six months.

The estimated amounts shall be adjusted to reflect the actual amounts with the audited statement of accounts on yearly basis and such adjustment shall be submitted within six months after the closing date of the relevant accounting period

VAT ON FINANCIAL SERVICES

Calculation of Tax

Total Value Addition

Net Profit or Loss (before income tax expenses)		XXX
Add : VAT and SSCL on supply of financial services charged to the Income Statement	XX	
Depreciation Charged to the Income Statement	XX	
Emoluments Payable	<u>XX</u>	<u>XXX</u>
		XXX
Less : Economic Depreciation		<u>(XX)</u>
Total value addition prior to tax		XXX
Less : VAT payable – on supply of financial Services		(XX)
SSCL payable – on supply of financial services		<u>(XX)</u>
Total Value Addition		<u>XX</u>

VAT ON FINANCIAL SERVICES

Calculation of Tax

The amount of tax payable for any taxable period shall be eighteen *per centum*, of the value addition

Profit computed in accordance with **accepted accounting standards**

Value addition of such specified institution shall be computed based on the net profit or loss after the deduction of the VAT payable under the supply of Financial Services

Any specified institution or any person who is required to adopt Sri Lanka Financial Reporting Standards (SLFRS) for the preparation of financial statements shall take into account the operating profit prepared as per SLFRS for the above purpose

- If any registered person prepares and maintains separate accounts for supply of financial services and, financial services provided out of Sri Lanka or activities as nonfinancial services, and such accounts are certified by an approved accountant under Section 120 of the Inland Revenue Act, No. 24 of 2017, then the value addition of such activities shall be calculated separately.

VAT ON FINANCIAL SERVICES

Calculation of Tax

Profit computed in accordance with **accepted accounting standards**

- If any registered person who is liable to pay VAT on Supply of Financial Services, does not keep separate accounts for non-financial services, such person is required to calculate the value addition on the proportionate basis.

For such purpose, the value addition attributable to the non-financial services is to be taken as the sum which bears to the total value addition, as the same proportion of the turnover of the nonfinancial services for the month bears to the total turnover of the same month, if there is no material difference in the recognition of receipts for the calculation of the profits and for the purpose of calculation of the turnover.

VAT ON FINANCIAL SERVICES

Calculation of Tax

The computation of Value Addition attributable to supply of financial services shall be as follows;

$$\text{Value Addition attributable to the financial services} = \text{Total Value Addition} - \left\{ \text{Total Value Addition} \times \frac{\text{Turnover for Non-Financial Services}}{\text{Total Turnover as per Income Statement}} \right\}$$

VAT ON FINANCIAL SERVICES

Calculation of Tax

Emoluments paid to all the employees shall include;

- In the case of specified employees under Inland Revenue Act, the gross remuneration payable to such employees and reflected in the pay sheet maintained for the requirement of the Inland Revenue Act,; and
- In the case of an employee other than a “specified employee” the gross remuneration paid to such employee reflected in the pay sheet maintained

Emoluments payable” means gross remuneration payable to all the employees. “Gross remuneration” means the aggregate of both benefits in money and benefits not in money payable to the employees and it includes any payment, contribution or provision in relating to terminal benefits which is charged to the income statement in arriving at the operating profit.

VAT ON FINANCIAL SERVICES

Calculation of Tax

Economic Depreciation, shall not apply in relation to any assets of any person registered under the Finance Leasing Act, No. 56 of 2000, being an asset which forms part of the leasing stocks of such person

Economic Depreciation

Rates of economic depreciation determined by the Minister and published in the Gazette Notification No. 1606/30 of 19.06.2009 are as follows;

Asset

Rate (Per annum)

Data Processing equipment and accessories including Computer Software

25%

Motor Vehicles

20%

Other Machinery, Plant, Equipment, Furniture or Fixture

12 1/2%

Intangible assets (other than Goodwill)

10%

Buildings

6 2/3%

VAT ON FINANCIAL SERVICES

Calculation of Tax

Economic Depreciation

- Statement of economic depreciation should be prepared for the whole year. These depreciation rates shall be applied on the basis of the cost and straight line method (equal installment method).
- Restrictions imposed by the Inland Revenue Act on allowances for depreciation shall not be applied
- The classification of assets shall be on the basis of SLFRS (any asset acquired prior to the adoption of SLFRS, the classification followed earlier shall be continued in calculating economic depreciation)
- No deduction is available as economic depreciation in relation to any asset of any person registered under the Finance Leasing Act, No. 56 of 2000 or Finance Business Act, No. 42 of 2011, being an asset which is leased under the provision of the aforesaid Act s

VAT ON FINANCIAL SERVICES

For the purpose of calculating the tax, the value addition attributable to;

1. Exempt supplies (other than item (x) of paragraph (b) of PART II of the First Schedule – Financial services is exempted for VAT for supply of nonfinancial services)
2. Zero rated supplies
3. Taxable supplies on which tax has been paid or is payable in terms of this Act, other than the value addition in relation to supplies taxable under the financial services
4. The profit or income (not being profit from a business) on interest arising or accrued from inter-company transactions of a group of companies relating to any loan, advance or credit, other than any profit or income arising to a company in that group which is a “specified institution” within the meaning of this Chapter or a person not registered with the Central Bank of Sri Lanka, but providing services similar to the services provided by a finance company
5. The dividend income (not being profit from a business) arising to any person, other than such income arising to any “specified institution” within the meaning of this Chapter or to a person not registered with the Central Bank of Sri Lanka, but providing services similar to the services provided by a finance company

VAT ON FINANCIAL SERVICES

For the purpose of calculating the tax, the value addition attributable to;

6. the profits or income not being profit from business arising to any person from the sale of company shares owned by such person or to any person who is instrumental in the purchase and sale of such shares by other persons, other than such profits and income arising to any “specified institution” within the meaning of this Chapter or a person not registered with the Central Bank of Sri Lanka, but providing services similar to such services provided by a finance company
7. The profits or income (not being profits from a business) from the exchange of currency other than such profits or income arising or accruing to any person primarily engaged in the business or exchange of currency or any “specified institution” within the meaning of this Chapter or a person not registered with the Central Bank of Sri Lanka, but providing services similar to such services provided by a finance company

included in the profit calculated as specified in computation of value addition shall be treated as zero