

This report provides helpful information on the current business environment in Sri Lanka. It is designed to assist companies in doing business and establishing effective banking arrangements. This is one of a series of reports on countries around the world.



Global Banking Service

# Report on the Democratic Socialist Republic of Sri Lanka

## Contents

Important to Know	2
Types of Business Structure	2
Opening and Operating Bank Accounts	3
Payment and Collection Instruments	4
Central Bank Reporting	5
Exchange Arrangements and Controls	5
Cash and Liquidity Management	5
Taxation	5

RBC Royal Bank®



## Important to Know

### Official languages

- › Sinhala/Tamil

### Currency

- › Sri Lankan rupee (LKR)

### Bank holidays

2011	
January	15, 19*
February	4, 16*, 17*
March	2*, 19*
April	13, 14, 17*, 22
May	2, 17, 18,
June	15*
July	14*
August	13*, 31*
September	11*
October	11*, 26*
November	6, 10*
December	10*, 26
2012	
January	15
February	3
April	6, 13, 14
May	1
August	20*
October	26*
November	14*
December	5*, 25

\*Dates, which may vary by plus or minus one day, are derived by converting from a non-Gregorian calendar to the Gregorian calendar and cannot be determined in advance with absolute accuracy. Also, some feast days are determined by the actual sighting of a new or full moon. As a result, exact dates may vary from those listed above.

Source: [www.goodbusinessday.com](http://www.goodbusinessday.com).

## Types of Business Structure

Under Sri Lankan law, there are several business structures available.

### Public limited liability company

This is a company whose shares are not registered and has no restrictions on transferring the shares of the company. Public limited liability companies in Sri Lanka must have a minimum of seven shareholders and two directors. Only public companies are permitted to engage in banking activities in Sri Lanka.

### Private limited liability company

This is a company whose shares are registered to their owners and therefore are not publicly tradable. Membership of private limited liability companies in Sri Lanka is limited to between two and 50 shareholders.

### Offshore company

This is a company incorporated in Sri Lanka, but registered as an offshore company. Registration as an offshore company prohibits an entity from carrying out business in Sri Lanka. Offshore companies must obtain a certificate confirming that they have deposited at least USD 100,000 in a Sri Lankan bank to meet their expenses in Sri Lanka.

### General partnership

In a general partnership, all partners have full and joint liability. There can be no more than 20 members of a partnership in Sri Lanka.

### Limited partnership

In a limited partnership, some partners enjoy limited liability (silent partners), although they are not permitted to exercise managerial control. Other partners are considered general partners and have unlimited liability. There can be no more than 20 members of a partnership in Sri Lanka.

### Cooperatives

Sri Lankan companies are entitled to form cooperative societies under the Co-operative Societies Law No. 5 of 1972.

### Other organizational types

Unlimited companies can be formed in Sri Lanka. Shareholders have unlimited responsibility for the liabilities of the company.

### Branches and liaison offices

Non-Sri Lankan companies are entitled to establish a branch or a liaison office in Sri Lanka. A branch's activities are subject to Sri Lankan company law. While branches are permitted to make sales, liaison offices may not be permitted to engage in any trade and investment activities in Sri Lanka.

## Opening and Operating Bank Accounts

### Residency

To be considered resident, a company must have a registered office, or its principal establishment or centre of management in Sri Lanka.

### Domestic and foreign currency account restrictions

Residents are permitted to hold local currency (LKR) accounts outside Sri Lanka. Residents are permitted to hold foreign currency accounts in Sri Lanka and, with permission from the Central Bank of Sri Lanka, outside the country.

Non-residents are permitted to hold local currency and foreign currency accounts within Sri Lanka.

Local currency accounts are fully convertible into foreign currency, although prior authorization from the central bank is usually required.

### Anti-money laundering and counter-terrorist financing rules

- › Account opening procedures require formal identification of the account holder and beneficial owners.

Supplied by BCL Burton Copeland ([www.bcl.com](http://www.bcl.com)). Data as at August 2010.

### Special purpose accounts required by local regulation

There are a number of special purpose accounts available in Sri Lanka.

Exporters foreign currency accounts (EFCA) are held by exporters in the form of current, savings and fixed deposit accounts. They can be credited with export proceeds, but balances may not be transferred to accounts in Sri Lanka that qualify for tax exemptions (including standard resident and non-resident foreign currency accounts).

Indirect exporters foreign currency accounts (IEFCA) are held by suppliers to exporters. Exporters are permitted to pay suppliers in foreign currency as long as the exported product contains at least 35% domestic value added. At the end of every month, any balances above the equivalent of USD 5,000 must be converted into LKR.

Foreign currency accounts for the suppliers of inputs (FCASI) are held by suppliers to exporters. Exporters can credit their suppliers' accounts in foreign currency. The holders of FCASI can pay residents of other countries and for any cost of inputs in foreign currency. Monies can be freely converted into LKR. Foreign currency accounts for professional services providers (FCAPS) work on a similar basis.

### Value-added tax (VAT) on banking services

In Sri Lanka, VAT at 20% is applied on most financial services. Some financial services, such as those provided by cooperative rural banks, are exempt from VAT.

## Payment and Collection Instruments

Cheques are the most common cashless payment instrument for domestic payments in Sri Lanka. In addition to cheques, electronic funds transfers are also an important payment instrument and both cheques and electronic fund transfers are used to make payroll payments. Electronic funds transfers can be initiated using Internet and other electronic banking facilities. Card payments are increasingly used for consumer transactions, with credit cards much more popular than debit cards.

### Payment Instrument Use (domestic)

Payment instrument	Transactions (million)		% change 2008/2007	Traffic (value) (LKR billion)		% change 2008/2007
	2007	2008		2007	2008	
<b>Cheques</b>	46.1	44.5	- 3.5	4,296	4,693	9.2
<b>Drafts</b>	N/A	N/A	N/A	2	1	- 50
<b>Postal Instruments</b>	N/A	N/A	N/A	11	11	-
<b>Debit cards</b>	1,252	2,174	73.6	4	6	50
<b>Credit cards</b>	18,262	18,866	3.3	67	73	8.9
<b>Total</b>	<b>19,560.1</b>	<b>21,084.5</b>	<b>7.8</b>	<b>4,380</b>	<b>4,784</b>	<b>9.2</b>

Source: Central Bank of Sri Lanka Annual Report 2008.

### International Payments

International payments are processed through same-bank networks, through multibank alliances or by using traditional correspondent banking techniques.

### Payment Processing Times

Transactions processed (LKR-denominated)	Value dating rules	Cut-off time(s) in Sri Lanka Time (SLT)
High-value, urgent domestic transfers	Real-time settlement, immediate finality	13:00 SLT
Non-urgent, low-value domestic consumer payments	Settlement usually within two working days, although it can take up to 14 days	15:30 SLT
Cheques and other domestic currency paper instrument payments	Settlement usually within two working days	17:45 SLT

## Central Bank Reporting

The Central Bank of Sri Lanka collects details of all foreign exchange transactions between residents and non-residents, which are reported by commercial banks on behalf of their customers via a web-based online system.

## Exchange Arrangements and Controls

Sri Lanka applies currency exchange controls, which are administered by the Central Bank of Sri Lanka's Exchange Control Department (ECD).

All transactions between residents of Sri Lanka must be carried out in LKR.

Approval from the ECD and Ministry of Finance is required for all outward investment from Sri Lanka.

## Cash and Liquidity Management

Due to high levels of regulation and an underdeveloped market, liquidity management techniques are not widely available in Sri Lanka.

### Physical Cash Concentration

Cash concentration in LKR is available from some international banks operating in Sri Lanka.

### Notional Cash Pooling

Notional cash pooling is not available in Sri Lanka.

### Short-term Investment

#### Bank instruments

Interest-bearing current accounts are not available in Sri Lanka. Interest-bearing savings accounts are widely available. Interest can be paid in a number of ways, including daily, weekly, monthly or annually.

Banks also offer time deposits in a range of maturities. Some banks also issue fixed-rate certificates of deposit (CDs) with a range of maturities. Special foreign investment deposit accounts (SFIDA) are held by non-residents in the form of local and foreign currency time or savings deposits. They must maintain a minimum balance of USD 10,000 and are exempt from corporation and withholding tax.

#### Non-bank instruments

Some Sri Lankan companies issue unsecured commercial paper (CP). Most is issued at a discount.

The Sri Lankan government issues Treasury bills through the Central Bank of Sri Lanka, usually for periods of three, six and 12 months.

Repurchase agreements are also freely available in Sri Lanka.

### Short-term Borrowing

#### Bank

Overdrafts, bank lines of credit and bank loans are usually all available in Sri Lanka.

#### Non-bank

Larger companies issue CP into the domestic market.

## Taxation

### Corporate Taxation

- ▶ Resident companies are taxed on their worldwide income.
- ▶ The standard rate of corporation tax is 33⅓% for publicly quoted companies that have been listed for less than five years and 35% for all other companies.
- ▶ Non-resident companies are taxed at the standard rate of 35% on profits from activities in Sri Lanka.
- ▶ Resident and non-resident small companies pay tax at a rate of 15%. Small companies are companies that have taxable profits of less than LKR 5 million.
- ▶ Lower rates of 10%, 15% or 20% apply to specific industries or activities provided certain conditions are met (e.g. fisheries, tourism, construction, profits from exports and warehousing facilities).
- ▶ Non-resident companies are liable for remittance tax at a rate of 10% on certain profits remitted abroad.
- ▶ Tax returns are required by November 30 following the end of the fiscal year.
- ▶ Tax is payable in four quarterly instalments by August 15, November 15 and February 15, with the final instalment payable by May 15 following the end of the tax year. If paid

on a prior-year basis, however, any underpayment can be made by November 30 following the end of the tax year.

- › Tax losses may be carried forward and set against 35% of the year's total statutory income.
- › Social Responsibility Levy (SRL) is payable on income tax or corporate tax at a rate of 1.5%.

#### Financial instruments

- › General tax principles apply; there are no specific tax rules for financial instruments.

#### Interest and financing costs

- › Please refer to Thin Capitalization section below.

#### Foreign exchange

- › Foreign exchange differences on transactions of a revenue nature are taxed as a separate item. Capital gains or losses on foreign exchange differences are not taxable to the extent that they are of a capital nature.
- › The Sri Lanka Accounting Standards has specific rules for the calculation and recognition of foreign exchange differences.
- › Specific rules govern the calculation of income tax in a local currency.

#### Advance Tax Ruling Availability

- › Rulings on the interpretation of tax laws are currently available.
- › Advanced tax rulings on transfer pricing issues are negotiable with the Inland Revenue Department.

#### Withholding Tax (subject to tax treaties and other exemptions)

Payments to	Interest	Dividends	Royalties	Remittances and other income
Resident companies	10%*	10%	10%	N/A
Non-resident companies	10%* to 15%** N/A†	0% to 10%††	10% to 15%	0%, 5% or 20%‡

\* Paid by financial institutions.

\*\* Paid by others.

† Withholding tax is not applicable if the non-resident recipient is a bank or if the interest is paid by a Foreign Currency Banking Unit in Sri Lanka.

†† Some dividends are exempt from income tax under domestic law.

‡ 20% on payments of rent, ground rent and annuities; 5% on specified fees and management fees and 0% on other categories.

- › The treaty withholding tax rates applicable to payments to non-residents are as follows:
  - › interest, dividends, remittances and other income – as per the table above; and
  - › royalties – 10% to 15%.

### Capital Gains Tax

- › There is no capital gains tax.
- › Capital losses are disregarded.
- › The sale of shares in a quoted company is subject to a share transaction levy at a rate of 0.2% of the sale price charged to both the buyer and seller. The levy is collected at the Sri Lankan Stock Exchange.

### Stamp Duty

- › Stamp duty is payable to provincial councils on the transfer of immovable assets and on certain documents.
- › Stamp duty is payable on “specified instruments” that are executed, drawn or presented in Sri Lanka. Stamp duty is also payable on instruments executed outside Sri Lanka that relate to property situated in Sri Lanka at the time such instruments are presented in Sri Lanka.

### Thin Capitalization

- › Tax relief on interest payments between group companies is granted up to a debt-to-equity ratio of 3:1 for manufacturing companies and of 4:1 for other companies.

### Transfer Pricing

- › Specific guidelines and rules have been published by the Inland Revenue Department for Transfer Pricing:
  - › certain transactions and dispositions are disregarded if they are artificial or fictitious; and
  - › transactions between related persons must be at arm’s length.

### Sales Taxes / VAT

- › VAT is payable on goods and services, including imports.
- › Certain goods and services are exempt from VAT.
- › The standard VAT rate is 12%, with a reduced rate of 5%

applying to essential goods. A 20% rate is applied to luxury items.

- › Financial services are liable to VAT at a rate of 20%.
- › Businesses with a turnover of LKR 3 million or less per annum do not have to register for VAT.
- › Excise duties apply to tobacco products, alcohol, motor vehicles and oil products.
- › Turnover tax at 1% or 5% of the turnover of any retail or wholesale business is payable to the provincial council.

### Financial Transactions / Banking Services Tax

- › Debits to current and savings accounts held at banks are taxed at 0.1% of the amount withdrawn (Debit Tax).
- › Traveller’s cheques and certificates of deposit are similarly taxed on encashment (Debit Tax).
- › VAT is applicable for financial services supplied by a bank or financial institution in Sri Lanka.

### Payroll and Social Security Taxes

- › SRL is applied at a rate of 1.5% of corporation tax payable.
- › Employees’ provident funds: employers contribute 12% of employees’ salaries to the Employees Provident Fund (EPF) or an approved private provident fund.
- › Employees contribute 8% of their salary to an EPF.
- › Employers contribute 3% of their payroll to the State Employee Trust Fund. Employees are entitled to a gratuity payment at the time of leaving, if the employee has had continuous service exceeding five years. The gratuity is an amount of 50% of the last drawn salary multiplied by the number of years of service.
- › Generally, employers establish gratuity funds and contribute to them periodically, according to the fund rules. The gratuity fund is a separate legal entity.

### Economic Services Charge (ESC)

- › ESC is payable quarterly on total turnover at rates from 0.1% to 1% depending on the nature of the business.
- › There is no ESC payable if quarterly turnover is less than LKR 7.5 million.

- › ESC is deductible against corporation tax for up to five years but not refundable.

#### Nation Building Levy

- › Nation Building Tax is payable by importers, manufacturers and service providers.
- › The tax is 1% of the turnover of the amount received or receivable, in respect of manufacturers and service providers, and 1% of the value of the imports of the importer.

- › For manufacturers and service providers, there is a threshold of LKR 650,000 per quarter; for importers, the threshold is the actual value of the imports.

- › Payment is due every month by the 20th day of the following month. The final payment is due on or before the 20th day immediately following the end of the quarter.

All tax information supplied by SJMS Associates ([www.sjmsassociates.lk](http://www.sjmsassociates.lk)), a correspondent firm to Deloitte Touche Tohmatsu ([www.deloitte.com](http://www.deloitte.com)).  
Data as at May 1, 2010.

Report prepared September 2010.

#### Take your business around the world with confidence.

Take advantage of our expert advice and global reach. With your trusted RBC® team in Canada as your single point of contact, you can take your business around the world with confidence.

For more information about our global capabilities and how we can help:

- › Call 1-800 ROYAL® 2-0 (1-800-769-2520) to contact an RBC Royal Bank® Business Banking centre
- › Visit us at [rbccroyalbank.com/go-global](http://rbccroyalbank.com/go-global) to locate a specialist near you.



RBC Royal Bank®

The material provided by Royal Bank of Canada (RBC) and its contracted information supplier on this website or in this document if in printed form (the “Information”) is not intended to be advice on any particular matter. No reader should act on the basis of any Information matter provided by RBC and its contracted information supplier and third party suppliers in this document without considering appropriate professional advice. RBC and its contracted information supplier expressly disclaim all and any liability to any person in respect of anything and of the consequences of anything done or omitted to be done by any such person in reliance upon the Information of this website. The Information provided is frequently subject to change without notice. RBC and its contracted information supplier make no warranties, expressed or implied, with respect to the Information, and specifically disclaim any warranty, merchantability or fitness for a particular purpose. RBC and its contracted information provider do not represent or warrant the Information contained or on referred sites or sites accessible via hypertext links is complete or free from error and expressly disclaim and do not assume any liability to any person for any loss or damage whatsoever caused by errors or omissions in the data, whether such errors or omissions result from negligence, accident, quality, performance of the website, or any other cause. All rights reserved. No part of the material provided by RBC (including the Information) and its contracted information supplier and third-party suppliers may be reproduced, stored in a retrieval system or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without the prior written permission of RBC and its contracted supplier.

® Registered trademarks of Royal Bank of Canada. RBC and Royal Bank are registered trademarks of Royal Bank of Canada.

© Royal Bank of Canada 2010.