Tax Expenditure Statement – 2023/2024

Issued by the Hon. Minister of Finance, Planning and Economic Development Under Section 20 of the Public Financial Management Act, No. 44 of 2024

This Report includes a statement of Tax expenditures including the total cost of exisiting tax expenditures and the disclosure of new tax expenditures, to be submitted with the Annual Budget.

Tax Expenditure Statement 2023/2024

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6.1 Introduction

This Tax Expenditure Statement (TES) reports estimates of the revenue forgone from tax expenditures which establishes a transparent reporting and offers a platform to understand the impact of government policies on the society including individuals, households and businesses. This report presents Government's latest estimates of the fiscal cost of tax expenditure and assumptions and the methodology used to produce these estimates. This is the first statement published under the Public Financial Management Act, No. 44 of 2024 and a comprehensive TES is expected to be submitted with the Budget 2026.

Types of tax expenditure items and the type of taxes considered in preparation of this report are as follows;

Tax system primarily aims to raise adequate revenue for financing the Government budget. However, by ways of targeted tax exemptions, deductions, deferrals, allowances and others of tax liability and concessional tax rates, Government expects to achieve social and economic objectives. Tax expenditures are estimates of the total revenue forgone as a result of exemptions, allowances, credits, rate reliefs and tax deferrals pertaining to tax.

6.2 Benchmarking in Tax Expenditure Statements

Benchmarking in tax expenditure statements involves defining a normative tax system against which deviations such as exemptions, deductions, credits, deferrals, and preferential rates that are identified as tax expenditures. The benchmark serves as a reference to distinguish between structural tax provisions and policy-induced concessions.

A well-defined benchmark typically includes:

1. The Tax Base – The comprehensive income, consumption, or other tax bases as per standard tax principles.

2. Tax Rates – The standard statutory rates applied uniformly without preferential treatment.

3. Structural Elements – Core features necessary for tax administration, such as loss carry-forward provisions or inflation adjustments.

Table 6.1: Tax Expenditure Classification

Tax Expenditure Items	Tax Expenditure by Type of Taxes			
	Personal Income Tax	Corporate Income Tax	Consumption Taxes (VAT)	Customs
Preferential tax rates	√	√	√	
Tax holidays		√		
Special Zones		√	√	√
Capital Recovery Incentives		√		
Exemptions	√	√		√
Investment Subsidies		√		
Tax deferrals		√	√	√
Fiscal regime benefits for extractive industries		√	√	√

Table 6.2: Tax Expenditure by tax type

Tax Expenditure Items	Reporting Time Period	Tax Expenditure (Rs. Mn.)
Personal Income Tax (PIT)	2023/24	12,248
Corporate Income Tax (CIT)	2023/24	243,224
Consumption Taxes (VAT)	2024	333,104
Custom Import Duties (CID)	2024	375,116
Luxury Tax on Motor Vehicles	2024	1,928

Tax expenditures, therefore, include provisions that deviate from this benchmark, such as:

- Exemptions (e.g., tax-free thresholds or sector-specific exemptions)
- Preferential tax rates (e.g., lower rates for specific industries or income sources)
- Deductions and allowances (e.g., investment allowances, accelerated depreciation)
- Tax credits (e.g., Research & Development tax credits, employment-related incentives)
- Deferrals (e.g., tax deferrals on capital gains)

Tax concessions under trade agreements (e.g., preferential tax treatment for businesses operating under Free Trade Agreements (FTAs) or Double Taxation Agreements (DTAs)) are not considered as tax expenditures as these provisions are policy-driven, and therefore, can be considered as part of the standard system.

Similarly, since Sri Lanka has a progressive income tax system, the tax-free threshold, which is a portion of income that is not taxed to ensure equity, is considered as part of the benchmark and not considered a tax expenditure. Further, the tax-free threshold is designed to reduce the tax burden on low-income earners rather than as a discretionary concession. Considering the above, tax-free threshold can be considered as part of the standard system.

6.3 Basis for Tax Expenditure Calculation

This tax expenditure statement is prepared on the following basis;

a) There are three main approaches to estimate revenue foregone

   (i). The Revenue foregone by providing the raw benefit
   (ii). The Revenue gained by providing the raw benefit
   (iii). Outlay equivalent the amount of direct government funding that would be needed to provide the same financial benefits to taxpayers without the expenditures.

   This estimate uses the "revenue forgone" method, which is an ex-post calculation of the loss of the revenue incurred by the Government. It assumes that the tax payers' behavior remains unchanged in response to withdrawal of tax expenditure.

b) Inland Revenue Department (IRD) calculations are based on the tax returns submitted.

c) Base erosion of revenue due to valuation issues, procedural errors, transfer pricing and non-compliance are not considered.

d) Tax expenditure on free services provided by Government is not taken into consideration.

e) Tax expenditure calculations on Personal Income Tax and, Corporate Income Tax calculations are based on 2023/24 actual data & estimates.

f) Tax expenditure calculations on Value Added Tax and import taxes are based on 2024 actual data.

g) Tax expenditure calculations for Luxury tax on motor vehicles are based on actual data as at end December, 2024.

h) Any deviations from the Schedules in the Inland Revenue Act, No.24 of 2017 are treated as tax expenditure;

1st Schedule	=	Tax Rates
2nd Schedule	=	Investment incentives
3rd Schedule	=	Exempt Amounts
4th Schedule	=	Capital Allowances, Balancing Allowances and Assessable Charges
5th Schedule	=	Qualifying Payments and Reliefs
6th Schedule	=	Temporary Concessions

i) Tax concessions granted to BOI

undertakings were considered in calculating tax expenditure at the point of importation.

j) Luxury Tax Concession granted under the Scheme for Granting Permits to Import Fully Electric Vehicles for Sri Lankans Employed Abroad (Migrant workers remittance scheme) have been considered in calculating the tax expenditures.

6.4 Tax Expenditure Estimates

Personal Income Tax (PIT)

Effective from January 01, 2023, personal relief was reduced to Rs. 1.2 million per annum from Rs. 3.0 million per annum and the expenditure relief of Rs 1.2 million per annum was removed. Personal Income Tax was levied under 6 slabs of Rs. 500,000 at the rates of 6 percent, 12 percent, 18 percent, 24 percent, 30 percent and 36 percent.

With the tax policy revisions that reduced of personal tax-free limit, the removed expenditure relief, removed exemptions and narrowed the tax slab, the personal tax expenditure amount will most likely be significantly reduced with effect from the year of assessment 2023/2024.

The following PIT rate structure is proposed to be implemented with effect from April 1, 2025;

Table 6.3: Proposed PIT Rate Schedule

Marginal Tax rate (%)	Tax Slab (Rs.)
0	Up to 1.8 Mn.
6	1.8 – 2.8 Mn.
12	-
18	2.8 – 3.3 Mn.
24	3.3 – 3.8 Mn.
30	3.8 – 4.3 Mn.
36	Over 4.3 Mn.

The personal income tax expenditures for the year 2023/24 are provided in Table 6.4.

Table 6.4: Personal Income Tax Expenditure

Expenditure Type	Tax Expenditure (Rs. Mn.) 2023/24
Relief and Qualifying payments	938
Exempted	11,310
Total	**12,248**

Source: Inland Revenue Department

Corporate Income Tax (CIT)

The increase of Corporate Income Tax rate from 24 percent to 30 percent and the removal of sector specific concessionary rates were implemented with effect from October 01, 2022. The impact of the above revisions is not fully reflected in the Tax Expenditure Statement for 2022/23 as the revisions have only been effective for two quarters in the said year of assessment. However, the full impact of the CIT changes are reflected in the CIT expenditure for 2023/24.

Table 6.5: Corporate Income Tax Expenditure for 2023/24

Sector		Expenditure Type	Tax Expenditure (Rs. Mn.)
BOI	SDP	Concessionary Rate	-
		Exempted	123
	Non-SDP	Concessionary Rate	41,682
		Exempted	
Non-BOI		Concessionary Rate	201,419
		Exempted	

Source: Inland Revenue Department

Value Added Tax (VAT)

Value Added Tax expenditures are higher for non-BOI sector compared to the BOI sector. Out of the BOI companies, manufacturing sector and services and utility sector have mostly benefited from VAT incentives. Banks and financial sector are not considered due to their liability for VAT on financial services.

Vast majority of VAT exemptions were removed and VAT registration threshold was reduced from Rs. 80 million per annum to Rs. 60 million per annum with effect from January 01, 2024.

Table 6.6: Value Added Tax (VAT) Expenditure by Sector for 2024

Sector		Tax Expenditure Rs. Mn.
BOI	Agriculture	1,628
	Apparel	355
	Infrastructure	1,085
	Knowledge Services	877
	Manufacturing	17,266
	Services and Utility	11,048
	Tourism	255
	Total	**32,515**
Non-BOI		**300,590**

Source: Inland Revenue Department

Taxes on Imports

Customs Import Duty is the major contributor to tax expenditure on import taxes. Deferral of taxes under Temporary Imports Export Processing (TIEP) scheme was not considered for tax expenditure, since the tax, if paid, is refundable after the goods are exported. Tax deferments granted on project cargo for specified projects where the Government has to bear the tax cost is not taken into account in calculating the tax expenditure.

Tax exemptions granted for BOI undertakings are considered for tax expenditure.

Table 6.7: Sector wise Tax Expenditure on Custom Duties for 2024

Sector	Tax Expenditure (Rs. Mn.)
BOI	92,725
Non-BOI	282,391
Total	**375,116**

Source: Sri Lanka Customs

Luxury Tax on Motor Vehicles

Luxury tax on motor vehicles is a special levy imposed under Section 19 of the Finance Act, No. 35 of 2018, on high-value vehicles, primarily to regulate luxury consumption, generate government revenue, and promote social equity in taxation. This tax is generally applicable to vehicles exceeding a specified threshold based on CIF (Cost, Insurance, and Freight) value or ex-factory price, for locally assembled vehicles.

The luxury tax threshold for electric vehicles is Rs. 6 million, with any amount exceeding this threshold subject to a 60% tax rate. However, under the Scheme for Granting Permits to Import Fully Electric Vehicles for Sri Lankans Employed Abroad, the threshold was revised to Rs. 12 million, allowing eligible individuals to receive a maximum concession of Rs. 3.6 million under this scheme.

Table 6.8: Summary of Luxury Tax on Motor Vehicles Exemptions- As at 31.12.2024

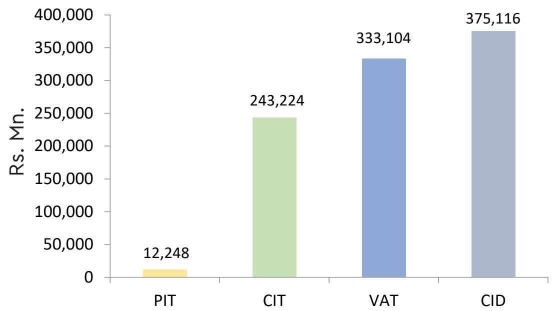
Year	Number of beneficiaries	Tax Expenditure (Rs. Mn.)
2023	162	491
2024	721	1,928

Source: Sri Lanka Customs

6.5 Conclusion

Highest amount of tax expenditure has been incurred through tax expenditure incurred for CID followed by VAT.

Chart 6.1: Summary of Tax Expenditure (Rs. Mn.) for 2023/24*



**Different types of tax expenditures which are calculated for different taxable periods cannot be aggregated.*

However, with the recent tax policy reforms including the removal of a vast majority of VAT exemptions from January 01, 2024, the tax expenditure estimated for the year 2023/24 and onwards is expected to be significantly lowered.

Table 6.9: Individual Income Tax Expenditure 2023/24

Exemption		Total Relief Amount (Rs. Mn.)	Tax after including exempt or relief (Rs. Mn.)	Actual (Rs. Mn.)	Tax expenditure (Rs. Mn.)
Relief for Rent income		7,253	157,367	148,256	9,111
Relief for Expenditure*		2,270			
Qualifying Payment		938			
Exemption	– Employment				
	– Business	11,310			
	– Investment				

**Relief for expenditure only include solar panal*

Source: Inland Revenue Department

Table 6.10: Corporate Income Tax expenditure 2023/24

Description	Tax base (Rs.)	Tax Rate (%)	Tax (Rs.)	Tax base (Rs.)	Standard Rate	Tax (Rs.)	Tax expenditure (Rs.)
Tax Laible income tax under concessionary Rate	1,217.88	1	12	1,218	30	365	353
	216.40	2	4	216	30	65	61
	21.25	6	1	21	30	6	5
	1.34	7.5	0	1	30	0.403	0
	0.02	8	0	0	30	0.005	0
	114.19	10	11	114	30	34	23
	406,261.98	14	56,877	406,262	30	121,879	65,002
	43,212.96	15	6,482	43,213	30	12,964	6,482
	8,143.28	20	1,629	8,143	30	2,443	814
	1.75	24	0	2	30	1	0
Total	**459,191**		**65,017**	**459,191**		**137,757**	**72,740**
Exempt Amounts under Third Schedule of the Inland Revenue Act, No. 24 of 2017	413,589			413,589	30%	124,076.84	124,077
Exemptions under the Provisions of the Inland Revenue Act, No. 10 of 2006	15,341			15,341	30%	4,602.31	4,602
Total	**428,931**			**428,931**		**128,679**	**128,679**
Grand Total	**888,122**			**888,122**		**266,436**	**201,419**

Source: Inland Revenue Department

Table 6.11: VAT Expenditure by Sector for BOI Companies 2024

Rs. Mn.

Sector	Tax Base	Tax Rate	Tax Rate	Estimated Tax	Tax Expenditure
Agriculture	9,047	Exempted	18%	1,628	1,628
Apparel	1,974	Exempted	18%	355	355
Infrastructure	6,029	Exempted	18%	1,085	1,085
Knowledge Services	4,872	Exempted	18%	877	877
Manufacturing	95,923	Exempted	18%	17,266	17,266
Power	–	Exempted	18%	–	–
Services and Utility	61,377	Exempted	18%	11,048	11,048
Tourism	1,416	Exempted	18%	255	255
Grand Total	**180,637**			**32,515**	**32,515**

Source: Inland Revenue Department