

BUSINESS TAXATION

# *INVESTMENT INCOME*

By

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## Applicable Section – Section 7

A person's income from an **investment** for a year of assessment shall be the person's **gains and profits** from that investment for the year.

# “Investment” means – Section 195

- (a) The owning of one or more assets, including one or more assets of a **similar nature** or that are used in an integrated fashion, and:—
  - (i) includes a past, present or prospective investment; but
  - (ii) excludes a business or employment; or
- (b) A game of chance, including lotteries, betting or gambling;

# Investment Income shall be included

- (a) dividends, interest, discounts, charges, annuities, **natural resource payments**, rents, premiums and royalties;
- (b) gains from the realization of investment assets as calculated under **Chapter IV**;
- (c) amounts derived as consideration for **accepting a restriction** on the capacity to conduct the investment;
- (d) **gifts received** by the person in respect of the investment;
- (e) winnings from lotteries, betting or gambling; and
- (f) **other amounts** required to be included under this Act.

# Investment Income shall be excluded

- (a) exempt amounts and **final withholding payments**; and
- (b) amounts that are included in calculating the person's income from an **employment or business**.

# “Dividends” means – Section 195

- (a) means a payment derived by a member from a company, whether received as a division of profits, in the course of a liquidation or reconstruction, in a reduction of capital or share buy-back or otherwise;
  
- (b) includes a capitalisation of profits –
  - (i) whether by way of a bonus share issue, increase in the amount paid-up on shares or otherwise; and
  - (ii) whether an amount is distributed or not; and

# “Dividends” means – Section 195

- (c) excludes a payment to the extent to which it is –
  - (i) matched by a payment made by the member to the company;
  - (ii) debited to a capital, share premium or similar account; or
  - (iii) otherwise constitutes a final withholding payment or is included in calculating the income of the member;

# Dividends contd.

## Exempt amounts - 3<sup>rd</sup> schedule

A dividend paid by a resident company to a member to the extent that dividend payment is attributable to, or derived from, another dividend received by that resident company or another resident company that was subject to withholding under section 84;

## Final Withholding payments – Section 88

Dividend paid by **resident companies to resident persons**



# Dividends contd.

## Exempt amounts - 3<sup>rd</sup> schedule

A dividend paid by a resident company to a member to the extent that dividend payment is attributable to, or derived from, another dividend received by that resident company or another resident company that was subject to withholding under [section 84](#);

## Final Withholding payments – [Section 88](#)

Dividend paid by **resident companies to resident persons**

## Exemption of certain dividends from withholding tax – Second Schedule

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Notwithstanding anything in the **First Schedule**, the rate of tax to be withheld from a dividend paid by a **company to a non-resident member shall be zero**,

If the company paying the dividend has incurred more than USD 1,000 million on depreciable assets (other than intangible assets) in Sri Lanka or entitled to an enhanced capital allowance under subparagraph (5) of paragraph 1, and that dividend is paid out of profits **sheltered by enhanced Capital allowances** under this Schedule

# “Interest” includes – Section 195

- (a) a payment, including a discount or premium, made under a debt obligation that is not a repayment of capital; and
- (b) a swap or other payment functionally equivalent to interest;
- (c) a commitment, guarantee or service fee paid in respect of a debt obligation or swap agreement; and
- (d) a distribution by a building society;

# Interest Income

## Exempt amounts - 3<sup>rd</sup> schedule

The **interest** derived by a **charitable institution**, where it is proved to the satisfaction of the CGIR that such interest is applied **solely** for the purpose of **providing care to children, the elderly or the disabled in a home maintained by such charitable institution;**

An amount equal to the **interest or the discount** paid or allowed, to **any non-resident person** or to **any licensed commercial bank in Sri Lanka**, by the issuer of **any sovereign bond** denominated in foreign currency, issued on or after October 21, 2008, by or on behalf of the Government of Sri Lanka.

# Interest Income

## Final withholding payments – Section 88

Interest paid to or treated as being derived by

- A resident individual (other than such amount of interest paid to a senior citizen falling within the relief threshold in paragraph 2 (d) of the Fifth Schedule to this Act);
- A charitable institution

# Interest Income Reliefs - Fifth Schedule

In the case of an individual who is a **senior citizen** in a year with interest income derived from a financial institution, **Rs. 1,500,000** for each year of assessment, up to the total of the individual's interest income for the year

## **Discount -**

The gains derived from the casual discounting of bills of exchanges etc.

(Gains arising from the discounting of bills of exchange, cheques, etc. in the normal course of business considered as business income.)

## **Charges -**

A charge is a sum received by a person under deed or an order of court which is secured on the income or property of payer.

## **Premiums -**

Premiums are payments received as a consideration for obtaining the right to use a property rather than for the actual use of the property.

*Example-* Receipt of key money on letting a premises

## Annuities

An annuity is a fixed sum receivable annually **which is not a capital nature**. The payment of an annuity which should be made with reference to a year may be in periodic instalment.

*Example -* Receipt of monthly payment after contributing of pension fund



# Annuities

## Exempt amounts – Third Schedule

Any amount derived by a **senior citizen** from an **annuity** for life for a period of **not less than ten years** purchased from a bank or an insurance company registered under the Regulation of Insurance Industry Act, No. 43 of 2000;

# Natural resource payments - Section 195

**“natural resource”** means minerals, petroleum, water or any other non-living or living resource that **may be taken from land or the sea**;

**“natural resource payment”** means a payment, including a premium or like amount, for the **right to take natural resources from land or the sea** or calculated in whole or part by reference to the quantity or value of natural resources taken from land or the sea;

## **Example :**

Mr. perera owns a property that he mainly uses for agricultural purposes.

ABC company is a mining company.

In year 1 it agreed pays Rs. 2 million for the right to enter his property and test for the existence of certain minerals.

In year 2 Company has discovered substantial quantities of various minerals and signs a 5 year agreement under which it agrees to pay Mr. perera what is described as a "royalty" of 10% of the value of minerals extracted.

Extraction begins in year 3 and during that year Company Z pays Mr perera "royalties" of Rs. 2 million under the agreement.

**Provide the guidance to Mr. perera as provision of IR Act No. 24 of 2017**

## Example contd.

| Incident                       | Amount                    | Income                   |
|--------------------------------|---------------------------|--------------------------|
| Year 1 - Right to enter        | 2,000,000                 | Rent                     |
| Year 2 – Discovers the mineral |                           |                          |
| Year 3 - Extraction begins     | 10% of minerals extracted | natural resource payment |
|                                |                           |                          |

# “Rent” – Section 195

- (a) means a payment, including a payment of a premium or like amount, for the use of or right to use property of any kind;
- (b) includes a payment for the rendering of, or the undertaking to render, assistance ancillary to a use or a right referred to in paragraph (a); but
- (c) excludes a natural resource payment or a royalty;

# Rent Income Relief - Fifth Schedule

In the case of an **individual with rental income** from an investment asset,

an amount equal to **25 percent of the total rental income** for the year of assessment, being **a relief for the repair, maintenance, and depreciation** relating to the investment asset,

but **shall only be allowed** to the extent no deduction or cost is claimed for any actual expenditures incurred by the taxpayer for the repair, maintenance, and depreciation of the investment asset.

# “Royalty” means – Section 195

A payment, including a payment of a premium or like amount, derived as consideration for –

- (a) the use of or right to use a copyright of literary, artistic or scientific work, including cinematograph films, software or video or audio recordings, whether the work is in electronic format or otherwise;
- (b) the use of or right to use a patent, trade mark, design or model, plan, or secret formula or process;

## “Royalty” means – Section 195

- (c) the use of or right to use any industrial, commercial, or scientific equipment;
- (d) the use of or right to use information concerning industrial, commercial or scientific experience;
- (e) the rendering of or the undertaking to render assistance ancillary to a matter referred to in paragraph (a), (b), (c) or (d); or
- (f) a total or partial forbearance with respect to a matter referred to in paragraph (a), (b), (c), (d) or (e);



# **Gains from the realization of investment assets as calculated under chapter iv;**

**This is related to the capital gain**

# Gifts received by the person in respect of the investment

“Gift” means - [Section 195](#)

“gift” means a transfer without consideration or a transfer with consideration to the extent that the market value of the property exceeds the market value of the consideration.

## Winnings from lotteries, betting or gambling

Winnings from lotteries, betting or gambling are specifically deemed to be income from an investment.

However, **no deduction is allowed** for amounts incurred on lotteries, betting or gambling under Section 10(a)(IX). This prohibition against deduction does not apply to amounts incurred from conducting a business of gambling.

# Winnings from lotteries, betting or gambling- contd.

## Exempt amounts - **Third Schedule**

any winning from a lottery, the gross amount of which does not exceed Rs. 500,000;

## Final withholding payments – **Section 88**

Receipts by winning lotteries, rewards, betting or gambling (other than business receipts of betting and gaming)

## Example

- Mr. A won Rs. 1 million from a lottery. He spent Rs. 100,000 on lottery tickets for that draw. Mr. A must recognize all Rs. 1 million as income from an investment, but may not deduct the Rs. 100,000 as expenses incurred in the production of income from the investment.
- Assume Mr. A runs an illegal gambling operation. The illegality of the operation does not preclude the income derived from income taxation. Mr. A must recognize all income derived from the gambling operation as income from a business, and he may deduct expenses and losses incurred in conducting the business .

## Investment income of a business

It is important to determine first whether the taxpayer is conducting a business or an investment

# Investment returns that are “effectively connected” with a business - Business income.

## Example 1

Mr. Kumara is engaged in sale of motor vehicles. He purchased showroom in order to expand his business.

Currently, he does not need all the floor space but hopes to use it in the near future. Mr. Kumara leased out the excess space to another businessman for a rent.

**Provide the guidance to Mr. Kumara for decide the relevant tax source.**

## Example 2

Mr. Kamal runs a hotel. As it is profitable Business, He invests some of excess funds in a bank and gets an interest. Further Mr. Kamal purchased a residential property from excess funds and rented it out. Received rent income from such property.

**Provide the guidance to Mr. Kamal for decide the relevant tax source.**



# Final withholding payments – section 88

- Dividend paid by resident companies to resident persons
- Interest paid to a resident individual (other than such amount of interest paid to a senior citizen falling within the relief threshold in paragraph 2 (d) of the Fifth Schedule to this Act) or to charitable institutions
- Receipts by winning lotteries, rewards, betting or gambling (other than business receipts of betting and gaming)
- Payments to Non resident persons (other than payments derived through Sri Lankan PE)

# Calculation basis

Investment Income calculation for income tax purpose

Individual - Cash Basis

Others - Accrual basis

a person must calculate their income from each investment separately.

# Jointly owned investments - Section 29

Amounts to be included and deducted shall be apportioned among the joint owners in proportion to their interests in the investment.

Where the interests of joint owners cannot be ascertained they shall be treated as equal.

# Calculation Of Assessable Income Of Investment

|  |     |                     |
|--|-----|---------------------|
| Income from Investment                       |     | *****               |
| Less : Exempt amounts                        | *** |                     |
| : Final withholding payments                 | *** |                     |
| : Amounts included in employment or business | *** | <u>(****)</u>       |
| Liable income from Investment                |     | ****                |
| Less : Allowable deductions                  |     | <u>(***)</u>        |
| <b>Assessable Income of Investment</b>       |     | <b><u>*****</u></b> |

# Theory Checker

Determine whether following items can be taken when calculating the investment income

- Dividend income which is subject to WHT at 14%
- Royalty income which is subject to WHT at 14%
- Rent income which is subject to WHT at 10%
- Interest on savings Account which is subject to WHT at 5%
- Gain from realization of land
- Gain from realization of machine for which capital allowance has claimed for tax purpose
- Rent income received for partial renting of business premises

# *REALIZATION OF INVESTMENT ASSET (CAPITAL GAIN)*

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**INLAND REVENUE ACT NO. 24 OF 2017**

# Gain from Realization of Investment Assets

Realization of capital assets or liability is dealt in Chapter IV

If such capital asset is effectively connected to business or just a passive investment asset, it is required to apply the same set of provision in order to ascertain the gain or loss from the realization.

It is applicable when transfer of ownership of asset or liability including sale, exchange, transfer, distribute, cancel, redeem, destroy, loss expire, expropriate or surrender of an investment asset.

# Calculation of the Gain

|                                |              |
|--------------------------------|--------------|
| Consideration received         | XXXX         |
| <u>Less</u>                    |              |
| Cost of the asset or liability | <u>(XXX)</u> |
| Gain or loss                   | <u>XXXX</u>  |



# Exemption/Exclusion on realization of assets

- For a resident individual, any capital gain **not exceeding Rs. 50,000** and Total capital gain **not exceeding Rs. 600,000** for a year of Assessment.
- In the case of a jointly owned asset, the **same threshold applies** to all owners.
- For a resident individual, the capital gain on the disposal of his principle place of residence if it has been **owned by him continuously for 3 years** before the disposal and lived in by him for **at least 2 years**.
- Capital gain on the realization of **quoted Company shares**.

# Tax Rate

- Capital gain are taxed at the rate of 10%
- Personal Tax Free allowance of Rs. 500,000 is not allowed to be claimed against the gain on realization of assets.

# Submission of Capital Gain Return

- Return is to be filed **not later than one month** after the date of realization.
- Realization of nearest asset which causes to **exceed total gain of Rs. 600,000**
- Must be account on **cash basis**, unless approved by CGIR.
- A **tax credit is available** on any tax paid by the person for the year by installment attributable.

# Losses from Investment

- Unrelieved losses from investment shall be only in calculating income an investment.
- Gain from realization of investment asset shall not be reduced by any loss on the disposal of another investment asset.

# *WITHHOLDING TAX*

## *-WHT-*

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# WHT on investment returns – (S.84)



# WHT – SECTION 84

11/26/2019

| Income   | Rate |
|--|------|
| Interest or discount paid to a person (other than to an individual who is a senior citizen in relation to a bank deposit account)  | 5%;  |
| Interest paid to a senior citizen exceed 1.5M (On their declaration)   | 5%;  |
| Rent paid to a resident person   | 10%; |
| Dividend, charge, natural resource payment, royalty, premium or retirement payment or pays amounts as winnings from a lottery, reward, betting or gambling<br>Payment or allocation has source in Sri Lanka (None Residents) | 14%  |
| Gem sold at an auction conducted by National Gem Authority from the sum payable to the seller  | 2.5% |
| Share of partnership Income  | 8%   |

# Not Subject to WHT – (S.84) **X**

Individual not doing Business



Resident or none resident Person

Person



Financial Institutions

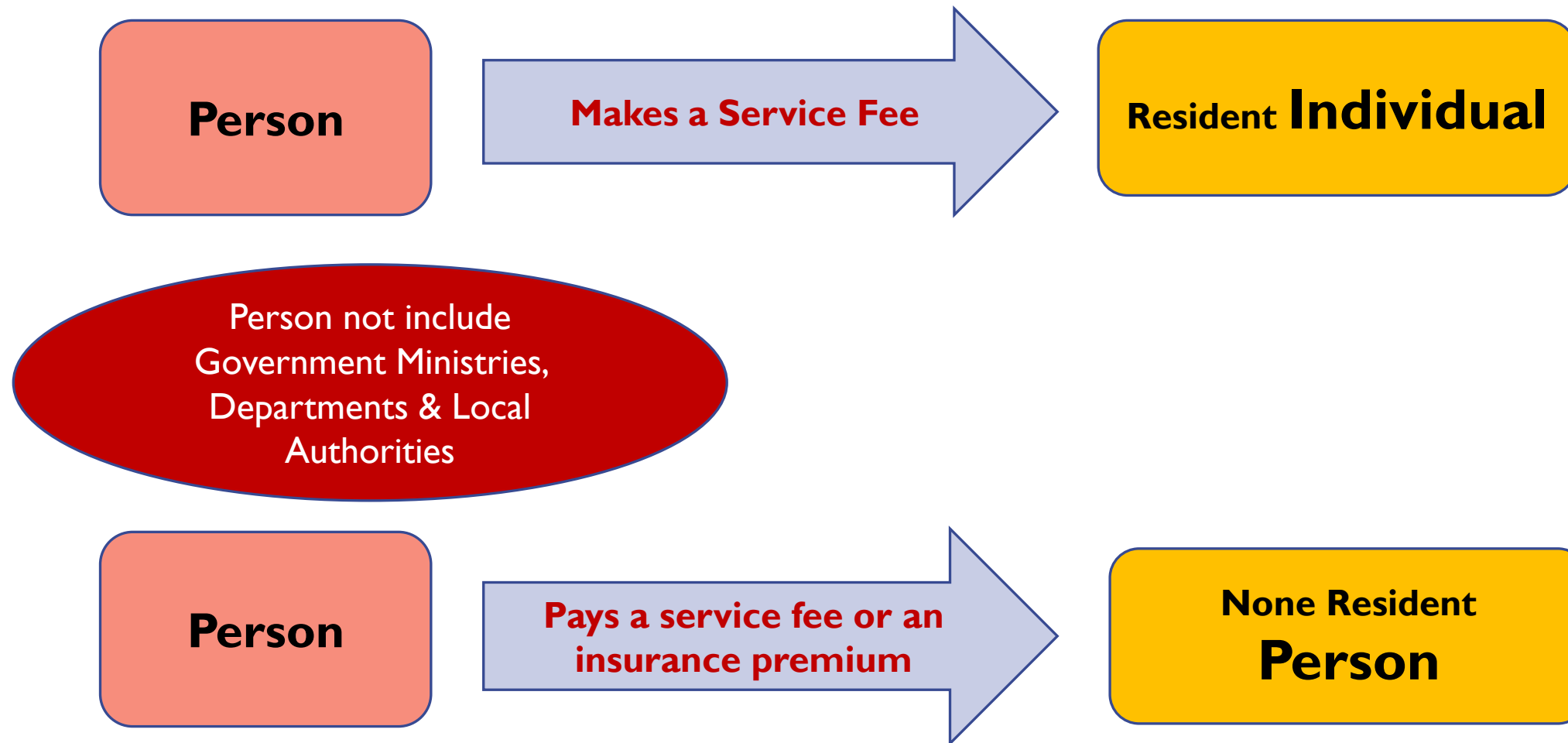
Person



Resident or none resident Person



# WHT on Service fee and contract payments – S.85



# WHT on Service fee and contract payments – S.85 11/26/2019

| Income (Aggregate Payment more than 50,000 per month)  | Rate |
|--|------|
| <ul style="list-style-type: none"><li>➤ Teaching, lecturing, examining, invigilating or supervising an examination</li><li>➤ Commission or brokerage to a resident insurance, sales or canvassing agent</li><li>➤ An endorsement fee</li><li>➤ Supply of any article on a contract basis through tender or quotation</li></ul> | 5%   |
| <p>➤ <b>Other Matters prescribe by the Regulations</b></p>   |      |
| <p><b>Section 85 (b)</b> Pays a service fee or an insurance premium with a source in Sri Lanka to a non-resident person.</p>   | 14%  |
| <p><b>Section 85 (2)</b><br/>A resident person shall withhold tax when the person makes a payment to a non-resident person of a type referred to in paragraph (h) or (i) of section 73 (land, sea or air transport or telecommunication services)</p>  | 2%   |

# Other Matters prescribe by the Regulations

for any service provided in the capacity of independent service providers such as doctors, engineers, accountants, lawyers, software developers, researchers, academics, or any other similar service; \*\*

for any service of construction work, security service, janitorial service, consultation work of any kind, organizing of events, catering, designers, dress makers, tour guidance, entertainment, agency functions or any similar services or connected work where such services are provided under an agreement or otherwise; \*\*

for any management service; \*\*

for any type of vocational services provided as an independent service provider. \*\*

# Not Subject to WHT – (S.85) **X**

**Individual not  
doing Business**

**Makes a Service Fee**

**Resident Individual  
or  
none resident Person**

**Person**

**Makes a Service Fee**

**income exempt from tax  
(Resident or none resident)**

**Person**

**Pays Interest on Treasury  
bills and Bonds**

**Person income chargeable  
with ESC**

## **Registration**

All WHT Agents are required to obtain a registration number from the tax type registration for the purpose of deducting WHT from withholder.

## **Calculation of WHT**

The WHT deductions should be made on the gross amounts of the invoice value (inclusive of all taxes other than VAT)

## **WHT Certificate**

The WHT Agent is required to issue a certificate in the specified format. The certificate shall cover a calendar month and be served within 30 days from the end of the month

# WHT Payments

Any tax that has been withheld during each calendar month by the withholding agent, must be paid to the Commissioner-General ( to the People's Bank Account No. 014-1002-6-9026620 by using the paying in slip issued by the IRD) within 15 days from the end the month. Any withholding agent who fails to withhold tax in accordance with this Division must nevertheless pay the tax that should have been withheld in the same manner and at the same time as tax that is withheld.

## Furnishing WHT Returns

Every withholding agent should file an annual statement specified by the Commissioner General of Inland Revenue, for each year of assessment within 30 days from the end of year ( on or before 30<sup>th</sup> April) Return should be furnished by all registered withholding agents even in the instances where no any tax is payable.

## WHT Schedules



WHT 84 n 85.pdf

Schedules prepared in the relevant formats as specified in the Annexure 2(a) or 2(b) or 2(c) for the payments on which WHT deducted, and Annexure 3 in respect of the payment on which WHT not deducted, should be furnished along with the annual statement.

The schedules are required to be furnished in electronic form (Excel csv format).

# OTHER INCOME

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**INLAND REVENUE ACT No. 24 of 2017**



## Applicable section – Section 8

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A person's income from other sources for a year of assessment shall be that person's gains and profits from any source whatsoever for the year, not including profits of a **casual** and **non-recurring nature**

# **In calculating gains or profits from any source whatsoever, shall be excluded:**

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- (a) exempt amounts and final withholding payments; and
- (b) amounts that are included in calculating the person's income from an employment, business or investment.

# Calculation of assessable income of other source

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|   |     |                     |
|---|-----|---------------------|
| Income from other source                  |     | *****               |
| Less : Exempt amounts                     | *** |                     |
| : Final withholding payments              | *** |                     |
| : Amounts included in emp., busi. or Inv. | *** | <u>(****)</u>       |
| Liable income from other source           |     | ****                |
| Less : Allowable deductions               |     | <u>(***)</u>        |
| <b>Assessable Income of other source</b>  |     | <b><u>*****</u></b> |



**T H A N K S**

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