



Higher VAT on Financial Services Offset by SSCL Removal

FLASH NOTE

The Key Revisions Proposed under the Bill:

A [Bill](#) to amend the Value Added Tax Act No. 14 of 2002 was issued on 29 April 2026 and is expected to become legally enforceable upon completion of the constitutional approval process in Parliament.

Changes to Existing Provisions:

- ✓ VAT on financial services increased to 20.5% (from 18.0%) effective 01 July 2026.
- ✓ VAT registration threshold reduced to LKR 36.0Mn annually from LKR 60.0Mn (LKR 9.0Mn per quarter from LKR 15.0Mn) effective 01 July 2026.
- ✓ Submission of VAT schedules allowed progressively from the start of the taxable period (instead of end-period submission).
- ✓ VAT benefit on project-related imports (plants, machinery, equipment or vehicle) is withdrawn if the items are not re-exported within one month after project completion.
- ✓ Maximum penalty for VAT offences increased to LKR 1.0Mn (from LKR 25,000) with imprisonment up to 6 months effective from 01 October 2025.
- ✓ Public disclosure of VAT-registered persons (name, address, TIN, status) enabled for transparency and compliance.
- ✓ VAT exemption/zero-rating extended to selected export-related and strategic business supplies (including BSI entities) effective

New Additions:

- ✓ VAT introduced on non-resident digital services supplied to Sri Lanka effective 01 July 2026.
 - Applies if services are consumed in Sri Lanka.
 - B2B exemption: Digital services supplied by non-residents to VAT-registered businesses in Sri Lanka are not subject to VAT, provided proper documentation is maintained.
- ✓ Deemed input VAT credit granted on opening stock for newly registered wholesale/retail traders effective 01 April 2026.
 - A deemed input VAT credit allows newly VAT-registered businesses to claim a VAT credit on existing unsold stock, avoiding double taxation.
- ✓ Mandatory adoption of CGIR-approved secured POS systems for VAT-registered persons within 3 months of implementation date.

Impact on Financial Services:

- The primary impact arises from the increase in VAT on financial services to 20.5% (from 18.0%) effective 01 July 2026.
- However, this increase is offset by the removal of the 2.5% Social Security Contribution Levy (SSCL) previously applicable to the sector.
- Accordingly, the tax structure shifts from two parallel levies (18.0% VAT + 2.5% SSCL) to a single consolidated VAT of 20.5% on value addition.
- **As a result, the effective tax incidence on value addition remains broadly unchanged, implying minimal to no impact on sector profitability from this revision.**
- The Bill also introduces technical refinements to the definitions of 'emoluments' and 'dividend income', with implications for the VAT computation base.
 - 'Emoluments' aligned with Inland Revenue Act No. 24 of 2017: Broadens and standardizes the definition of employee remuneration used in VAT computations, ensuring consistency with income tax treatment.
 - Clarification on dividend income: Dividend income earned by entities outside specified financial institutions is explicitly excluded from business profits for VAT purposes, thereby limiting VAT exposure on non-core income streams.



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