

Part B

1. Mr. Speaker, unlike in the past, where the traditional Budget was developed as a short-term exercise to cover objectives for a period of 12 months, with little or no progressive continuity of policies in consecutive Budgets, this UPFA Budget has been deliberately prepared within a three year Budgetary Framework, so as to sequence fiscal measures objectively, and more importantly, to have a sector focused public expenditure management system, that links the output of the economy based on available opportunities and resources. Mr. Speaker, we needed to change the way Budgets are prepared by line ministries, as we need to depart from ad-hoc individual ministry project based Budgeting to targeted, collective sector based Budgeting.
2. In reviewing past Budgets and line ministry votes, I noticed that there are several overlaps in expenditure and consequent duplication of efforts, as well as glaring gaps with zero allocation of funds for vital areas. We made a start this year to reverse all of this, by giving guidance to the line ministries on medium term policy strategies and getting them to focus on collective actions for prioritized sectors. This Budget, will also for the first time, fill the gaps that always go unfilled in the traditional Budgeting exercise, and will reverse the downward trend in Government revenue to ensure a sustainable correction in Budgetary imbalances.
3. Of course, at the same time, we are mindful of the need for continued support of on-going projects, and their relevance to the national economy. One of the key priorities in expenditure allocation is the emphasis on pro-poor growth strategies in the rural sector to reduce poverty. Complementing these efforts, several line ministries and NCED clusters, have formulated new development initiatives that deserve recognition. Empowering our local enterprises and entrepreneurs to become competitive players in the domestic and export markets is the key to creating a vibrant economy. A flourishing local enterprise base will result in not only an increase in jobs and incomes, but also profits which can be channeled into even greater growth investment opportunities. Our country is only tapping a sliver of the entire economic value-chain arising from our resources, and this Budget will hopefully unleash the entrepreneurial spirit in all of us to unlock our full value potential. Therefore, this Government will fully back new capacity value creators.
4. Mr. Speaker, I just spoke about our policy on expenditure. Now let me touch on the all important revenue side. Our prime objective in fiscal policy management is the reversal of the declining trend in Government revenue, which has fallen to 15.7% of GDP in 2003, lowest in recent years. No Government can make

successful fiscal reforms unless it addresses the root cause of fiscal instability that shows a steady decline in Government revenue. Our income tax is the lowest in the region, languishing at 2% of GDP. In the early 90s, Sri Lanka maintained a tax revenue ratio of around 20% of GDP. We had a strong tax base, of which, 5% of GDP was raised from plantation agriculture alone. However, this revenue source is no longer available with the export activity being made free from export taxes. With the increased reliance on indirect taxes, tax system also has become regressive. In this background our challenge is not only to raise revenue to a level that will sustain our economic stability, but also to improve its progressive characteristics to sustain a viable tax regime.

5. Mr. Speaker, this Government appreciates the contribution made by all taxpayers, especially those who make proper declarations, and we think it is unfair to burden them anymore because of the actions of the tax evaders! It is the second group that this Budget will target and not the first. We will not penalize those who have accumulated wealth by properly accounting for it, and can show that they have paid taxes on the money that was used to purchase those assets.

6. Let me now present my Budget proposals to complete my overall presentation.

National Action Plan for Children

7. On the initiative of the Her Excellency the President and with the collaboration of UNICEF, relevant line ministries, provincial authorities and the Department of National Planning of my Ministry, a National Plan for Children (NPC), for the children of Sri Lanka 2004 – 2008 has been now launched. The overall objective of the NPC is to ensure universal access for services that children require for their full and free development as well as to provide them with the opportunity to develop their individual capacities in a safe and enabling environment. Some salient targets to be achieved through the implementation of NPC are the following:
 - Increase in the enrolment of pre-school children from 60% at present to 80% by 2005.
 - Increase in the primary school enrolment from 95% to 100% by 2008.
 - Reduction in the infant mortality rate from 12/1,000 live births to 8 per 1,000.
 - Reduction in maternal mortality from 42/100,000 to 23/100,000.

- Increase in the access to safe water for 70 - 80% of the child population by 2008.
 - Strengthening the enforcement of law pertaining to child labour and reduce domestic child labour by 30% each year during 2004 to 2008.
 - Eradicate child sex abuse.
 - Protect children from all forms of abuse, neglect, exploitation and violence.
8. Mr. Speaker this program requires Rs.14 billion over the planned implementation period. We have already identified Rs.2.2 billion from the National Budget. We are also seeking donor assistance. But it is also a golden opportunity to show our citizen's social responsibility. Therefore. Mr. Speaker I propose to impose 0.25% cess under the Finance Act on all taxes other than VAT, PAL, debit tax and withholding tax on interest income to be earmarked for the National Action Plan for Children. Although this may not generate a large sum, it would reflect our collective responsibility and partnership towards building a better world for our children. Expenditure under NAP is separately identified in the Budget estimates to ensure better accountability and transparency. I expect to collect Rs.450 million from this cess.

'Gamata Thaakshanaya' – Supporting Science and Technology for National Development

9. Economic development cannot take place without technological advance. Appropriate technology can be developed only by encouraging local science and technology institutions to provide necessary research and development. At present Sri Lanka has one of the lowest levels of funding of about 0.18 percent of GDP for R&D in the world. I propose to raise this over the next five years to at least 1 percent of GDP. The reversal of brain drain, International collaboration in research, the popularization of science, the exploration of the full extent of our natural resources, the promotion of innovation and ICT will therefore need funding.
10. For technology to be transferred effectively to the micro small and medium level entrepreneurs, the Ministry of Science and Technology will establish a computer linked Vidatha resource center in each of the 320 Divisional Secretary areas. Each of the Vidatha resource centers will have a science and technology graduate, a computer operator and a link agent. At village level, science & technology societies will be formed to transfer technology to the village and promote SMEs with a view to provide employment and to reduce

poverty. These Resource centers will be linked to the SME Bank and Regional Development Banks to assist in development banking, formulating information to the private sector and the IDB and EDB for technical support. This program will be implemented during a three-year period 2005-2007. I propose to provide an additional Rs.300 million in 2005 to the Ministry of Science & Technology in support of its "Gamata Thaakshanya" - the Vidatha program.

' Pubudamu Wellassa'

11. Badulla - Monaragala Districts remain the poorest and neglected districts in the island. Poverty remains high. School enrolment, access to drinking water, and basic health facilities remain well below national averages. The agricultural base which provides the main livelihood to the people is vulnerable to severe droughts and other climatic conditions. They have poor infrastructural facilities. In this background a three-year accelerated development program dedicated to these two districts, providing a wide range of infrastructure facilities will be implemented under the 'Pubudamu Wellassa' program. The total cost of this three year program is estimated at Rs.1,200 million. I propose to earmark Rs. 300 million in to 2005 to start this program beginning with the poorest villages in all the divisions in Badulla – Monaragala Districts being given priority.

'Rajarata Navodaya'

12. Several villages of the districts of Anuradhapura and Polonnaruwa Districts and border villages have remained poor due to lack of proper maintenance of minor irrigation schemes feeder roads, basic health facilities, and proper transport. A 3-year development program has been now formulated to address infrastructure gaps which are not covered under the existing programs of line ministries and Provincial Councils. Total project cost to be implemented during 2005-2007 is estimated at Rs.1,600 Million of which Rs. 300 Million will be provided in 2005.

'Dayata Sevana' - National Housing Program

13. The Freedom Alliance 'Rata Perata' sets a target of 300,000 housing units to be developed for low and middle income people. The program which has now being finalized to achieve this target through various initiatives will be launched next year. Having recognized the importance of providing housing as a basic need, and its beneficial impact in creating assets among the poor as well as positive backward and forward linkages, the Government proposes to increase the Budgetary allocation for housing in 2005 by Rs. 500 Million and augment it

further in the next 2 years. Priority will be given to low income housing requirements of shanty dwellers, the plantation community, coastal fishing villages and the rural sector.

14. Further, in order to encourage residential house construction for low and middle income earners, I propose to grant a 7 year tax exemption to an owner of a house on the rental income of that house if the floor area of the house constructed for renting does not exceed 1,500 Sq. ft.
15. With regards to house construction, it is also necessary to simplify the approval procedure which is not only complex and time consuming but also leads to corruption and loss of entrepreneur initiative. Therefore the Construction cluster of the NCED together with the National Housing Development Authority (NHDA) simplify the approval procedure for housing construction.
16. I also propose to allocate identified lands among property developers under BOI incentives for the development of residential houses at affordable prices.

Floriculture Sector Development

17. Mr. Speaker our country has a higher diversity of exotic flora and ample opportunity for its productive exploitation. It has potentials of generating annual growth of 7 - 10% at present Rs.1 billion worth of export earnings are brought into the country by large number of small growers as well as large scale exporters engaged in floriculture industry. This sector requires intensive management and expert advise to meet the quality standards to compete in the international market. Small and medium growers are unable to obtain required technical know how and other facilities. Most of the abandoned paddy lands in the wet zone areas particularly in the Western province and under utilized coconut lands can be productively used for this industry. It can provide a good source of employment as well.
18. Therefore I propose to allocate Rs. 20 million provide the necessary technical know how and extension services to small and medium growers in the floriculture industry. As a further incentive agricultural seeds and plants will be exempted from VAT.

Dairy Industry

19. Our Government is giving high priority to make the country self-sufficient in local milk production. This will provide an additional income source to rural people in addition to saving foreign exchange spent on the import of milk products. The Department of Animal Husbandry has been strengthened to provide the required extension services. MILCO has been transformed into a successful business venture. The Livestock Farms are being redeveloped and small holder farming is being encouraged. Large private sector investments in the development of livestock and its value additions is encouraged. The Livestock Cluster of the NCED has formulated an integrated action plan and the Government has already increased the producer prices to Rs. 16/lit. A ten year national dairy buffalo development project, popularization of the use of herbal veterinary preparations for treatment of animal diseases, reduction in the cost of animal feed ingredients, and the importation of dairy animals are also now being implemented. Therefore, in order to make livestock a thriving industry, I propose the following:
- a. Increase milk producer price to Rs. 20/Lit
 - b. Removal of VAT on animal feed
 - c. Allocate a further Rs. 50 million for the development of Dairy Industry in rural areas.
 - d. Gradual phasing out of the prevailing duty waiver on milk powder to endure remunerative prices to local dairy farmers.

Assistance for Organic Product Exports

20. Sri Lanka exports a range of organically certified products such as tea, spices, essential oils, herbs, desiccated coconut, oil seeds, pulses, cashew and fresh and dried fruits and vegetables. The local supply base of these products consists of mainly out grower, community and estate plantations. This system provides for a greater farmer/exporter link which helps small and medium producers. Since the certification is exclusively done by the International certifying agencies accredited to the International Federation for Organic Agriculture Movement (IFOAM), export costs go up. Therefore I propose to set up a separate fund of Rs. 10 million to share this cost to enable our entrepreneurs to gain a foothold in the growing international market for organically certified products, and also declare selected areas as watershed protected organic export zones in the country and to set up Organic Product Zones.

Development of Value Added Cinnamon Export Industry

21. Sri Lanka produces more than 90 percent genuine cinnamon (*Cinnamomum Zeylanicum* Blume) in the world. Our exports account for 63 percent of all spice exports in the world. Cheap low quality alternatives have begun to enter the global market leading to increased competition. There is an urgent need for increased investment in research and product development for value addition in cinnamon. Efforts to give "Ceylon Cinnamon" maximum protection under WTO agreement are being intensified. Investments in marketing "Ceylon Cinnamon" is essential to combat this competition. I propose to impose a cess of Rs.2.50/kg. or 0.5% of the value which ever is higher for the development of this industry. The Government will contribute Rs.10 million to set up a Cinnamon Development Fund.

Incentives for Cultivation and Value Addition of rubber

22. Recently a cess has been levied on the export of raw rubber and import products based on the natural rubber content in order to increase the export of value added products. I propose to encourage the rubber cultivation by increasing the replanting subsidy to Rs.100,000 / hectare. Expected cess collection of Rs.475 million will be earmarked to increase the productivity of the rubber sector and expand cultivation.

Incentives for Foundry Industry

23. A cess of 25% will be imposed on export of Ferrous and non-Ferrous in the form of scrap or any other form based on London Exchange Metal Price in order to ensure continuous supply of raw material required by the local industry. The expected income of Rs. 120 million from this cess will be utilized for upgrading technical skills and improving the productivity of the Foundry industry.

Prawn Farming

24. Sri Lanka's prawn farming has declined rapidly in recent years. This is due to lack of infrastructure investments and the absence of a proper regulatory system for disease control. A new project is now being implemented as a BOI zone in Puttalam – Chilaw area and it is proposed to increase the annual production in 2005 to 5,000 mt. from current levels of 1,500 mt. It is expected to generate 30,000 jobs and US\$ 50 million in export earnings. As an incentive, I propose to allocate Rs. 20 million for immediate infrastructure rehabilitation work and environment protection. The National Aquaculture Development Authority (NAQDA) will work on the necessary amendments to

regulate unauthorized farming practices and promote environment friendly farming. I also propose to remove VAT on shrimp feed to improve the cash flow of shrimp farmers. I expect local banks which have shown a keen interest in this export industry to join hands with the Government to exploit the full potential of this industry by extending financial assistance to prawn farming.

Osu Gammana and Reforestation Program

25. Sri Lanka's traditional aurvedic industry heavily depends on the import of basic raw material for the manufacture of aurvedic medicine. Annual import cost is over Rs.200 million (US\$2 million). These are products that can be cultivated in this country. Very valuable medicinal and aromatic plants are not grown in adequate quantities. Having recognized the potential of developing aurvedic plants, the Ministry of Indigenous Medicine has formulated a strategy to develop selected villages to grow medicinal plants. Several private sector aurvedic manufactures have also made similar project proposals. Therefore, I propose to allocate Rs. 100 million for the successful implementation of this program in selected areas in the country.
26. Sri Lanka has more than 3,350 species of plants, about 25 of which occur only in this country. Deforestation is taking place at a dangerous rate. Approximately 42,000 hectares are being lost each year affecting our biodiversity. We need to preserve this valuable asset through an aggressive reforestation program. In order to intensify this, I propose to earmark an additional Rs.50 million to set up a biodiversity and reforestation fund.

Model Farms for Fruits and Vegetable

27. As an integral part of the national export drive, fruits and vegetable producers and exporters the BOI, Export Development Board (EDB) and the Mahaweli Authority, have prepared a new private - public partnership program for Mahaweli areas. Lands have been identified for long-term leases for prospective investors who are required to set up nucleus farms in identified locations. They will develop out grower systems to promote high quality fruits and vegetables. The extent of each nucleus farm will be limited to 20-25 acres. This nucleus would provide seed and planting material and agricultural extension services to out growers. Investors will be responsible for identifying suitable crops for nucleus farms and encourage out growers to grow them. Each nucleus will be working with 50 to 100 farmers with forward buying agreements. In terms of this program the Export Development Board proposes to develop 34 such farms in 2005 and 66 in 2006.

Medium Scale Plantation

28. Mr. Speaker, there are a large number of professionals, particularly those who are associated with the plantation sector, who would like to enter production. We could sell them plantation lands up to 50 acres. They could not only invest their savings but also bring to bear their expertise in growing high yield plantation crops which will give them an adequate monetary return. At the same time their holdings would serve as model production areas, which can spearhead the transformation of small and medium scale land holdings. I will therefore, with the concurrence of my colleague, the Hon. Minister of Plantation Industries identify estates of up to 50 acres from the lands presently held by JEDB and SPC for the purpose of alienation to these worthy middle class planters and other professionals.

Samurdhi Program

29. Under the Samurdhi program the Government provides Rs. 10 billion to be distributed among poor families which account for about 40% of the population. While continuing to provide this assistance to Samurdhi beneficiaries our Government proposes to embark on employment creation and income generating programs for Samurdhi recipients to move them out of poverty levels. Towards this the Ministry of Samurdhi and Poverty Alleviation has now developed a "Suwahas Jana Pubuduwa" program design to empower 100,000 Samurdhi beneficiaries through self-employment and micro enterprises and 50,000 village development activities. In terms of this program all 50,000 village development activities will be executed in all Gramaseveke divisions through Samudhi Societies and community participation.
30. The World Bank assisted Gami Diriya program with Rs.5,000 million will be implemented in Badulla, Monaragala, Hambantota, Matara, Galle and Ratnapura. This program will be extended to 143 villages in these 6 districts. The program is designed to form savings and investment societies in these villages. The Asian Development Bank (ADB) has activated a program to expand rural finance through the strengthening of Samurdhi banking societies. Micro financing projects will be further extended through the National Development Trust Fund in 2005. In support of expanding all these new initiatives, I proposes to provide Rs. 450 million to the Ministry of Samudhi and Poverty Alleviation to develop micro enterprises and self-employment projects for Samurdhi beneficiaries to move them out of poverty.

Off-Shore Export Shopping Village

31. An off-shore export shopping village will be set up to allow all up market, high-value added export manufacturers in Sri Lanka to sell their products for foreign currencies. The Village, which is to be developed and promoted by the BOI and Tourist Board, is expected to be a major tourist shopping center in the region. This will provide Sri Lanka export industries with an opportunity to establish global links.

National Accreditation Board

32. Demand for quality products is on the rise. Our industries need to be supported by a network of accredited certification bodies to meet this challenge. Credibility and acceptance of test reports and certificates are necessary to support a wide range of Sri Lankan products now ready to enter global markets. Therefore, in order to fill this gap, I propose to establish a National Accreditation Board for conformity assessment of technical regulations, standards, and other regulatory measures coming under health, safety and environment. A sum of Rs. 10 million is provided in the 2005 Budget to start this work immediately, particularly in the context of the revival of export oriented SMEs.

Construction Industry Revival Initiatives

33. The construction industry is vital for economic development. However, local construction firms often find it difficult to submit bid bonds and raise funds due to lack of proper securities. Therefore to provide guarantees, I propose to increase the capital of the Construction Industry Guarantee Fund, to Rs. 500 million. A cess of 0.25 from small contractors, 0.5 percent from medium contractors and 1 percent from all large contractors on their contract turnover will be imposed and earmarked for the fund. The Government will also contribute Rs. 250 million towards this fund.
34. The non-availability of required skills is another constraint faced by the local construction industry. Therefore, I propose to set up an Academy for Advanced Construction Training - jointly with the National Construction Association of Sri Lanka. I propose to allocate Rs.100 million for this joint venture which will be beneficial not only to the local construction industry but will also create a core of construction employees from skilled workers to technical managers.

Housing for Migrant Workers

35. Migrant workers have become the main strength of our foreign exchange earnings. Their annual remittances have now reached US\$1,500 million. These migrant workers deserve assistance from the Government. Therefore a new housing loan scheme will be implemented for returning migrant workers. They will be required to maintain a minimum deposit of US\$ 250 in a NRFC account with any of the state banks to qualify for a loan up to a maximum of Rs.250,000 to purchase or construct a house at an interest rate of 5 percent per annum. The interest subsidy and the loan guaranteed against the deposit will be provided by the Sri Lanka Foreign Employment Bureau.

Human Resource and Skills Development

36. The nation's workforce, be it the skilled labour, management, or professionals, in both the public and private sectors, are lagging in adopting global best practices. The need to be familiar with contemporary methods and processes, including the use of technology and other productivity enhancement tools. This defect has negatively impacted on Sri Lanka's competitiveness, it also reduce the employability of the work force. Therefore, the Government plans to increase the intake to vocational training institutes to 50,000. In order to give added value to the existing vocational training institutes, a new University of Vocational Technology will be set up to provide avenues for middle level persons to go up to technology degree level. The "Tharuna Aruna" program will be reoriented into a Skills Development Fund. It will be a collaborative project with the private sector to coordinate skills needs of the private sector and to facilitate training programs in the Vocational and technical training institutes in the country. The private sector will be involved in organizing vocational training programs for those leaving for foreign employment. The Foreign Employment Bureau will provide the required funding for all skills development needed regarding overseas opportunities. In order to make this partnership project a success, I propose to allocate Rs. 100 million. Private sector and NGO are expected to also contribute towards this venture

Fuel Subsidy

37. There are approximately 200,000 three-wheeler operators in Sri Lanka. They have generated self-employment while providing affordable transport for a million people daily. I am well aware that they are faced with hardships due to recent fuel price increases. The Government has decided to mitigate their burden from future price increases. In addition, I propose to exempt leasing of three wheelers from VAT to reduce their cash flow problems. Moreover, I propose to offer concessional funding for those three-wheeler operators who

are willing to convert three wheelers from Petrol to Gas. Similar concessions will also be extended to small fishermen with the assistance of the Ministry of Fisheries. A suitable subsidy mechanism will also be considered for the public transport to insulate the providers from the impact of large price increases. Our aim is to limit the fuel subsidy to the most deserving people.

Incentives for Advance Technology

38. With emphasis on SME based private investment, I propose to implement a new incentive scheme to encourage small and medium industries to acquire advanced technology in order to raise productivity and improve competitiveness. Under this scheme, new companies investing over Rs. 5 million and existing companies investing over Rs. 2 million will be given duty free import of new machinery. The SME Bank will provide the necessary financial support for this venture.

Software Exports and Business Process Outsourcing

39. The software Industry has considerable potential to penetrate export markets. There are about 100 small and medium scale enterprises together with 5 – 6 large companies now in operation in this country with foreign exchange earnings around US\$ 75 million. This industry has targeted US\$ 1 billion export earning by 2012 with a total workforce of 40,000 taking advantage of the skills available in Sri Lanka. In order to support this industry, the public sector will be required to give preference to locally produced software and services. Further public sector agencies will ensure that a minimum of 50% of value addition from a local partner in Sri Lanka if the software is bought from a foreign supplier. As an incentive to our private sector to use local software, I propose a 100% depreciation in the year of purchase of all locally produced software. The SMEs will be provided with concessional funding for the purchase of local software products and services. The BOI will target Business Process Outsourcing Operators to locate in Sri Lanka under its incentive package.

SME Bank – Jathika Vivasayaka Bankuwa

40. As mentioned earlier, the Government has already taken steps to set up a new SME Bank with a capital base of Rs.5,000 million. It will provide direct funds, credit guarantee schemes, equity and debt capital, restructuring aid etc. to the SME sector. I propose to transfer Rs. 5,000 million held in various Government Accounts as capital contribution of the Government. A provision will be created in the Budget estimate. The SME Bank will commence operations in January 2005.

41. In addition to the SME Bank, the Government will establish a SME authority – modeled on the lines of EDB and BOI to function as the apex body for SME development. I propose to allocate Rs. 100 million for this authority to commence work in January 2005.

A New University for Uva-Wellassa

42. There are twelve conventional universities and the Open University conducting various degree programs in the country. These universities with about 80,000 students operate in their full capacity but can absorb only 2.3 percent of eligible students. This is grossly inadequate to support the country's long-term development needs. Any meaningful increase in the university intake would require a systematic creation of new ventures. For many years, the public in the Uva Wellassa Province have been asking for a center of higher learning. For this province which is incidentally the only province without a university, Her Excellency the President in her capacity as Minister of Education has proposed the establishment of an University at Badulla. The new university will cater to modern demands of Science, Mathematics, Information Technology, Business Management, Agricultural Engineering and Animal Science. Student admission to this university would commence from the 2005 Advance Level Examination in take. A fully residential university will be developed and completed by April 2006 at a cost of Rs. 350 million.

Hostel Facilities for the Rajarata University

43. The Rajarata University, which is targeted to have a student population of around 1,800, provides accommodation facilities only for 586 students. Provision of a fully-fledged high learning environment is the priority of the Government and it is expected to develop these facilities at Mihintale and Pulliankulame areas. The Government proposes to allocate Rs. 78 Million for this project.

Building Facilities for the Eastern University

44. The Trincomalee Campus of the Eastern University, which was established in June 2001, is handicapped due to insufficient building space for both lecture rooms as well as for residential facilities. As the existing location cannot be further developed, the Trincomalee Campus will be relocated in a land area of 250 acres at Konesapuri in Trincomalee. I propose to provide Rs. 91 million for

phase I, which will develop hostel and lecture room facilities as well as an administrative complex.

Youth Employment

45. Mr. Speaker one of the first priorities of this Government was to provide employment to unemployed graduates. We have selected about 42,000 such graduates to the Government service. They are now going through their orientation program in the public service. The orientation program covers communication skill, English as a working language, awareness to IT, economic policy and management. We have made a provision of Rs. 2,885 million in the 2005 Budget estimates to place them on permanent positions in the public service in January/February next year. In addition a further provision of Rs.1,100 million has been made to recruit 30,000 Advance Level qualified youth to vacant positions in the public service. Mr. Speaker the recruitment of these graduates and non-graduates youth will add new blood to the public service with training in languages like Tamil and English, software usage and variety of other modern skills required to provide an efficient and modern public delivery system.

Film Academy

46. Our Government has taken special steps to improve the local film industry. There has been a demand by the industry that a film academy should be set up for the benefit particularly of young professionals. Today, TV and film productions engage a large number of young people. Many of them have been associated with productions, which have even received international recognition. I, therefore, propose to set up a film academy for which premises have already been found within the film complex in Colombo. Fortunately, this land adjoins the Film and Television Institute which was set up with funding from the Republic of Germany. I propose to set up a film and TV Academy which could draw on the resources of the TV Training Institute as well. It will be possible to obtain foreign funding particularly from UNESCO for this project. I propose to include a token contribution of Rs. 1 million in the vote of the Ministry of Cultural Affairs, which will be supplemented with foreign funding during the course of 2005.

Assistance to Develop Craft Products for Export Markets

47. There is considerable export potential for crafts products such as handloom, soft-toys, handloom fabrics, giftware, curtaining and linen manufactured by a large number of small entrepreneurs in most parts of the country. Core group of SMEs manufacturing craft products targeting niche markets will be assisted with designs and a better range of products, external market access, concessionary micro credit schemes and development grants. Having seen the strengths of the entrepreneurs in recent industrial exhibitions at the BMICH, I propose to setup a large shopping complex cum exhibition center in Colombo to provide a permanent marketing infrastructure to craft product manufactures. This will be jointly developed by the Board of Investment, Export Development Board, Tourist Board, National Craft Council and Laksala using EDB and Tourist Board cess funds.

Export Development Incentive Schemes

48. Recently the Government imposed a cess on selected products with a view to providing incentives to local value added production with export potential. These industries require initial support by way of technology infusion and product development. In order to promote such diversified export activities, an incentive scheme will be implemented for non-traditional exports other than primary products and apparels with a minimum 35 percent local value addition. A cash grant will be made annually on the incremental value of exports. Branding of unique Sri Lanka products with an image differentiate in the international markets will be promoted. Selection criteria will be gazetted soon to make it a transparent process. Showroom space will be provided at the arrival and departure lounges at the Bandaranaike International Airport, and the exemption from VAT applicable to imported goods at duty free shops for payment in foreign currency will be extended to locally supplied goods as a means of popularizing Sri Lankan products.

Apparel Industry

49. The apparel industry which employees 300,000 people directly and has become US\$ 2.5 billion export industry is entering a decisive stage with the elimination of quotas from 2005 onwards. However the industry together with the NCED cluster have formulated a strategy to consolidate its investment and export potential in a competitive global environment. Towards promoting the apparel industry, I propose to give priorities to the following;

a. Financial Assistance to Technology Improvements

A large number of apparel industry manufactures fall into the SME category in terms of the international standard. The urgent need for them is to improve competitiveness. This requires upgrading of infrastructure and technology to comply with quality standards. Some of such manufactures do not have access to long-term financial assistance. Therefore I propose to provide a guarantee through the proposed SME Bank to enable banking and financial institutions to provide required working capital and investment needs of the apparel industry to modernize their factories. A total sum earmarked for the issuance of this guarantee will be Rs.600 million so that the industry will be able to raise Rs. 2,000million from the banking system and other financial institutions.

b. Simplified VAT application

The application of Value Added Tax to the apparel industry causes considerable administrative and procedural difficulties. By definition export being zero rated, the apparel industry is eligible for a full input credit. This industry being dependent heavily on a large volume of raw material, the present deferral mechanism imposes heavy administrative work on the Department of Inland Revenue as well as to the industry. I therefore propose that all apparel manufactures who are registered with the Textile Quota Board be exempted from the payment of VAT on the import of textiles and the ancillary inputs on condition that each manufacturer both BOI and Non BOI does file quarterly returns and accounts certified by the Textile Quota Board with a statement showing input and output to the Commissioner General of Inland Revenue. I expect a considerable efficiency gain in the industry as well as in the Deptment of Inland Revenue from this change.

c. Incentives for Garment Buying Offices

Garment buying offices in Sri Lanka render an extremely valuable service in facilitating overseas buyers to place their orders with Sri Lankan manufacturers. Their services need to be encouraged. When quotas are removed they would become trade representatives who could support sourcing from Sri Lanka. Hence I propose to include the services provided by such companies in the Zero rated category for VAT so that they will be able to maintain their international competitiveness.

d. Incentives for Productivity Improvement

Productivity improvement is essential for a successful transition towards the post 2005 trade regime. Therefore, I propose a grant of Rs. 100 million for productivity improvement measures in the apparel industry. A further Rs. 50 million will be granted for international image building campaigns to project the high quality corporate image of the apparel industry in Sri Lanka.

e. Incentives for Product Design

A Fashion Design Degree Program is offered by the University of Moratuwa with consultancy assistance from the London School of Fashion. However, this program is not functioning at an efficient level due to lack of funds for staffing and infrastructure requirement. Therefore I propose to provide Rs.100 million to improve the designer degree program at the University of Moratuwa in support of promoting up market apparel exports products from Sri Lanka.

f. Backward Linkage

BOI will set up an Industrial Park with a waste and effluent treatment plant at Biyagama Zone to facilitate fabric manufacturing in Sri Lanka for the use of the Apparel industry.

Incentives for Small Exporters

50. Sri Lanka's success in creating intermediate supply sources heavily depend on the recognition that such products are supplied to the exporters by small and medium manufacturers. The integration of this sector into our export industry therefore is essential to increase value added export from this country and promote backward integration. However, these supplies are not recognized in the Value Added Tax legislation as zero-rated supplies. As a result, the value added tax system has become a major barrier to promoting backward integration in our export development strategy. Therefore, to keep in line with our development objectives for the creation of domestically sourced export industry, local suppliers of exportable products to an export company registered with the Textile Quota Board and finished goods supplied to BOI registered trading houses for export by a registered manufacturer will be recognized for the purpose of input credit under the Value Added Tax.

Alternative Energy Development

51. The small hydropower sector which began as a 1 MW power plant commissioned in 1996 has now emerged as a reliable player in the energy field. 28 small hydropower projects have been commissioned with 65 MW of install capacity. 30 projects with 143 MW of capacity projects are in the pipeline, of the World Bank funded Renewable Energy Program. The CEB has issued letters of intent for 210 Mw small hydropower projects for future development. This will raise the supply of around 300MW only from small hydropower units of less than 10MW. There are also a large number of sites in Mahaweli regulated waterways with a large investment potential. All these projects can be commissioned before 2008. In order to provide incentives for these investments by local investors I propose to guarantee an all inclusive tariff rate of US\$ 0.06cts. per unit for such projects. The Treasury will support the Ceylon Electricity Board by sharing such expenditure. I propose to encourage local SMEs to develop hydropower projects of upto 50MW, through public private partnership arrangement. In order to exploit the full potential of Dendro power and solar energy the standard power purchase agreements will be modified.

52. As renewable energy sources have gathered momentum in rural areas, I propose to exempt the supply of such energy sources providing electricity to rural areas from VAT. The Government owned Private Sector Infrastructure Development Company Ltd (PSIDC) therefore would be reoriented to perform as a public private infrastructure financing facility, to fund small and medium infrastructure projects and alternative energy projects, Mini hydro, Dandro power etc. will be given top priority

Incentives for the Textile Industry

53. With the complete liberalization of the global textile industry, our manufactures have gone through a difficult transition. However they have admirable resilience in a competitive market environment. Recognizing the value addition contribution made by this sector, the Government has encouraged the local textile industry to manufacture quality products to satisfy a large local requirement. With this objective this Government decided to source school uniform material which are distributed among 4.5million children in this country to the local textile industry. The local textile industry successfully took up this challenge. It has now produced all of the next year's requirement on time. Mr. Speaker, I am proud to state that free school uniform material that will be distributed among school children in 2005 were manufactured within a short period of time in this country. Taking this process forward the President has directed that all textile requirements of armed forces, police, health services, prisons and other Government agencies must also be procured from local

textile manufactures. In order to facilitate this operation the Government will use the expertise of the Textile Quota Board to make in a transparent manner. Priority will be given to the manufactures who have successfully supplied school uniform material for 2005. The potential of the local textile industry, if successfully managed is over US\$ 100 million. This process over the medium term will also help the local textile industry to appropriately integrate itself with the apparel industry whose requirements are very large. Such textiles manufactures will be assisted through the new SME Bank to restructure and modernize their factories.

Incentives for Fishermen

54. Small and medium fisherman's need assistance to enable them to purchase their fishing nets, equipment and also to replace them on a regular basis to sustain their income. I therefore, propose to implement a special loan scheme enabling them to purchase fishing boats and equipment at concessionary interest rates. These lending schemes will be formulated by the new SME Bank to promote a comprehensive micro enterprise-lending program.

Modernization of Small and Medium Paddy Mills

55. Small and medium paddy millers scattered primarily in rice producing areas play a significant contribution in the value change in rice processing, storage and marketing. Our Government having recognized their important role restructured their loans with the assistance of the State Banks. The Government will share part of the non-performing debt as a measure of relief to Paddy Millers. The State Banks have already arranged working capital requirements of these mills to be prepared for the forthcoming Maha harvest. I also see a strong need to modernize these mills to improve quality of their milling. Therefore, special credit line will be implemented through the SME bank for this sector in 2005.

Gem and Jewellery Industry

56. We have to build up our gem and jewellery industry from the bottom up. I am advised by the relevant trade chambers that the establishment of modern, well equipped lapidaries is a pre-requisite for such a re-generation. Accordingly, the new SME Bank that we propose to establish will be instructed to fund the setting up of 10 lapidaries spread out in the gem producing areas which will be able to add value to the raw stones. This approach to modern cutting and polishing of precious stones should not only raise the quality of our product in the local and international markets, but also create employment opportunities

in the manufacturing field. Such skilled workers can easily find employment both in the local industry as well as in the gem centers in the region.

Development of Religious Activities

57. All temple funds are deposited, managed and controlled by the Public Trustee / Buddhist Commissioner under the Buddhist Temporalities Ordinance introduced in 1931. It has become necessary to amend this Ordinance to recognize the Sangha Council comprising of all Nekkayas together with sub councils and advisory councils to control and manage funds and utilize the same for the development of Buddhist activities, restoration of Buddhist Temples including those in the North and East and for the furtherance of Buddhism in Sri Lanka and abroad. Therefore I propose that this ordinance be amended to utilize these funds in a more desirable manner. Our Government deeply appreciates the leadership given by religious leaders to uplift poor rural families and develop their religious values through community empowerment programs. I propose to allocate an additional sum of Rs. 100 million in support of such programs.
58. Mr. Speaker, the religious Sunday Schools play a very vital role not only in religious education, but also in transferring traditional ethics and values. It is my intention to encourage such religious Institutions. Therefore, under the special grant of Rs.100 million, free uniform materials will be provided to all teachers of Sunday Schools, irrespective of their religious denomination. I am also exploring the possibility of setting up of a training college for Sunday school teachers. These teachers who have a high moral commitment to creating an ethical and peaceful environment in the country need to be supported to improve their pedagogical skills.

Revenue Proposals

Value Added Tax (VAT)

59. Mr. Speaker the single rate VAT reflects regressive characteristics in our tax system. The taxing luxury motor vehicles and an essential commodity like Dhal at the same rate of 15% while exempting precious Gem and Gold is not socially reasonable, however strong the argument may be for a single rate tax. Therefore, I propose to create a basic commodity rate of 5%, for essential food items and a luxury rate of 18% for selected consumer items. The standard rate of 15% will apply for general items.
60. Accordingly I propose to reduce VAT on sugar, dhal, potatoes, onions, dry fish, milk powder, vegetables and chillies from 15% to 5%. Input tax credit under

items taxed at basic rate of 5% will not be allowed other than VAT paid on the purchase of vehicles for transport and machinery for production.

61. Further I propose to increase the VAT rate from 15% to 18% on any kind of liquor, air conditioners, refrigerators, washing machines, TV sets, TV Antennas, cameras, jewellery, motor vehicles other than three wheelers and passenger buses and services such as hotel services for wedding receptions and such other kinds of receptions including hiring of halls. Input credit will be restricted to 15%. Further gem & gold which is currently exempt will be taxed at the rate of 15%.
62. I also propose that the valuation at the Customs point on goods imported will be up lifted by a 5% mark up on the CIF for charging VAT in order to capture trading margins. Further the Port and Airport Levy will be part of the VAT base to ensure consistency.
63. Mr. Speaker with these modifications I anticipate to mobilize additional revenue in addition to bringing about a more equitable distribution in the tax burden.

VAT on Large Investments

64. Application of Value Added Tax on large investment projects imposes upfront cash flow problems to investors engaged in investments of that scale. Therefore, I propose that import of project related capital goods other than the items in the negative list of a new venture during the project implementation period not exceeding three years from the date of commencement of the project will be free from VAT, if such projects involve an investment exceeding Rs.100 million and liable to VAT once the project is completed.

Income Tax Exemption to Agriculture

65. Our Government is committed to develop agriculture. In order to encourage investment in agriculture I propose to exempt income/profit arising from cultivation of land with plants of any description and sale of such unprocessed products for a period of 5 years effective from 1.4.2005. This should provide incentives for the local private sector to move onto high value agricultural crops including fruits, vegetables, floriculture etc.

Removal of Income Tax Exemption from the Sale of Gold, Gem and Jewellery

66. This is an area where considerable amount of revenue is earned without paying taxes except VAT by a few jewellery manufacturers. It is necessary to bring them in to the tax net. Therefore, I propose to remove the exemption of tax on income earned from the sale of gem, gold or jewellery. However in order to encourage export earnings the income earned from export of Gold, Gem and jewellery will be exempt from income tax.

Concession to Senior Citizens

67. Our senior citizens deserve special attention and respect. We need to increase saving for them in addition to assisting them in their retirement. I therefore propose to exempt interest income from special saving schemes offered by the National Savings Bank and the two State banks for citizens over 60 years of age from withholding tax on interest income up to a limit. Interest income not withdrawn up to age 60 years will also be permitted to qualify for this concession in order to promote long-term savings. An additional 1% interest over and above the normal interest income from fixed deposit accounts will be granted to fixed deposit accounts held by senior citizens. I also propose to exempt interest income up to maximum of Rs. 100,000 per annum for senior citizens on deposits made in State banks. This is in addition to normal tax-free threshold income of Rs. 300,000 available on interest income.

Incentive for Foreign currency Holders

68. I propose to provide the following incentives to attract foreign currency deposits in to our banking system.

- i. Introduce a Resident Guest Scheme to attract business migrants having net assets of not less than US\$ 250,000 and invested in Sri Lanka before submission of his application for emigration to residential status
- ii. There are large numbers of Sri Lankans who are living abroad particularly after 1983 riots and holding dual citizenship. Many of these Sri Lankans like to maintain this status but are reluctant to work in Sri Lanka due to the concern that local tax authorities will impose tax on their global income. In order to encourage Sri Lankans living abroad who have dual citizenship to come back to Sri Lanka, I propose to exempt their income from sources outside Sri Lanka from taxation in Sri Lanka

Employment Income of Public Servants

69. At present any resident in Sri Lanka earning up to Rs.25,000 per month or Rs.300,000 per annum is exempt from income tax. In terms of the low salary structure in the public service about 80% of the public servants, therefore are not liable to pay taxes. Nevertheless, exemption of salary income of public servants made out of consolidated fund payments has created a perception that they are a privileged class. It has also diminished the dignity and respect of the public service. Beginning from April 2003 this was partially corrected by introducing a tax credit mechanism but the method of computation has resulted in high tax burden particularly on certain professional categories. We have to

recognize the fact that public servants, if they earn as much as their private sector counterparts in salaries and if they have private incomes, should pay normal tax as a citizen of this country.

70. It must also be appreciated that public service salaries are exceptionally low in this country. Therefore taxing public servants should be done in a manner that will not reduce the already poor income of public servants. Taxation should also not be a disincentive for professionals to work in the public service. Therefore, I propose that public servant's be brought under the PAYE scheme but the income will be assumed to be half of the gross salary of the public servant. On this basis public servants will get a relief and pay tax only if they have a private income. In case of exceptional categories, where even half of the public service salary become liable for PAYE, the Government will provide a tax allowance like in the case of public corporation and state banks. The payment of tax by the employer on behalf of the employees will be treated as final tax if that is the only sources of income. However, deduction will be given on interest payments on housing loans, capital repayment of housing loans and contribution to provident funds. Tax systems will not be extended to pensions in the Government service.

Personal Income Tax

71. When we encourage all socially responsible citizens to come into the tax net we must also make sure that the tax system itself is affordable for people. Therefore, our Government is strongly of the view that the present personal income tax structure should be simplified in such a manner that maximum tax rate will not exceed 15% until income exceed Rs.1 million. Therefore, I propose the following:

- i. Tax free allowance for any individual to remain at Rs.300,000.
- ii. The next Rs.300,000 to be taxed at 5%, the next Rs. 200,000 at 10%, the next Rs. 200,000 at 15%, the next Rs.200,000 at 20%, the next 200,000 25% and the balance income to be taxed at 30%

Taxation of Employment Benefits

72. Mr Speaker, I propose to make several changes in updating the computation of various non-cash benefits from employment. Rental value of a house at present is restricted to Rs. 120,000 per annum. This is not a realistic value. Therefore, the value to housing benefits will be increased to Rs.180,000 per annum in cases where such facilities are enjoyed by executive officers whose salaries exceed Rs. 150,000 per month.

73. I propose the following amendments to the application of taxes on terminal benefit. The present exemption of Rs. 2 million applicable to terminal benefits such as Provident Fund, ETF etc. will now be available only if the period of contribution to such fund is more than 20 years. If the period of contribution is less than 20 years the applicable exemption will be limited to Rs. 1 million and the balance will be subject to the following concessionary rates.

- On the first Rs. 500,000 5%
- On the next Rs. 500,000 10%
- Balance at 15%

Compensation Paid under VRS or Retrenchment Scheme

74. In the 1998 Budget an exemption was introduced for compensation paid under Voluntary Retirement Scheme (VRS). However it has been observed that there are many irregularities in the implementation of this provision. Therefore I propose to limit the tax-free allowance under VRS/Retrenchment to Rs. 2 million. This is over and above the concession offered under terminal benefits.

Grant Received by NGOs

75. There are many Non-Governmental Organizations (NGO) carrying out activities which are not monitored adequately. It is necessary to adopt a proper system of monitoring of such organizations particularly in areas of activities carried out and funds utilized by them. Those institutions are now required to be registered with the Registrar of Companies and open tax files. I propose to impose a presumptive tax at the rate of 30% by taking 6% of the funds received as income of the institution, other than the institution carrying out activities solely related to rehabilitation work of North & East and any other activities which are approved by the Minister on humanitarian grounds.

Withholding Tax on Interest

76. Growth of corporate debt market is constrained by the current withholding tax system. For instance commercial paper, which was a popular source of financing in the past has lost popularity due to an unequal tax status when compared with other sources of financing. This is due to the upfront deduction of withholding tax from the difference between the face value and issue price of commercial paper. As a result commercial paper has now become more expensive compared to bank borrowings. Commercial Papers are a cheaper source of financing as the banks that arrange the commercial paper does not have to maintain liquid asset ratio with the Central Bank. Due to not having to provide extensive collateral as in the case of loan funds, this type of financing provides considerable support to SMEs as well as to those whose ability to secure debt finance from traditional sources is limited. Therefore to revitalize

corporate debt market withholding tax on corporate debt will be removed and only the final tax is retained.

77. In terms of the amendment made to the Inland Revenue Act trading profits of secondary market transactions of Treasury Bills have been made liable to income tax. Consequently, the dealers have expressed some concern as to whether the trading profit of secondary market transactions consist of capital gain and interest as well. As the Department of Inland Revenue already clarified and in line with international practice I must reaffirm that there is no distinction between interest and capital gain made, if a person is in the business of buying and selling Treasury Bill and bonds. However, I propose to give relief by implementing this measure effective from the year of assessment 2003/2004 and exempt the year 2002/2003 from this tax
78. In the case of individuals where 10% withholding tax is deducted, the withholding tax will become final tax. Therefore, such income will not become part of their assessable income

Corporate Taxation

79. Mr. Speaker In order to consolidate a lower tax regime it is necessary that we consolidate our tax base effectively to make higher yield from present tax rates. Therefore, I propose to impose restrictions on various deductions which are applicable to both corporate and non corporate sectors.
- a. At present if a company does not distribute dividend, action can be taken only if such company is controlled by 5 persons or less. I propose to remove this restriction in order to tax dividend not distributed by such companies.
 - b. At present 25% of the VAT on financial services paid is deducted as an expenditure. However, this is a tax calculated after arriving at net profit. Since, it is not an expenditure incurred in the production of income it will be disallowed in full.
 - c. The claims on traveling outside Sri Lanka will be restricted to expenses incurred solely in connection with the promotion of export trade of any article or provision of any services for payment in foreign currency
 - d. Entertainment expenditure and entertainment allowances paid to executives.
 - e. Allowances paid on fuel or expenditure incurred on the provision of vehicles will be restricted to 75% such expenditure.

- f. Advertisement expenditure will be restricted to 50%.
 - g. Head Office expenses or management fees paid to head office will be restricted to 10% of taxable income or actual expenses whichever is less. If there is no taxable income the average of the aggregated taxable income of 3 preceding years of assessment to be taken.
80. Mr. Speaker in certain countries only a percentage of total interest incurred by a company is deductible in computing the taxable income of that company. However. This is done to overcome many difficulties by tax administrators particularly to deal with related party transactions. Such a practice may also not be unfair when considered the benefits of debt financing as oppose to equity financing. In this context promoting debt equity balance in enterprise financing there is a justification to limit interest expenditure for tax deductions. However considering the heavy reliance of SMEs on debt financing this may still hurt the development of SME sector. Nevertheless, it is time that our corporate sector gives some consideration as to whether it is desirable to move on to such advance practices in corporate taxation. I do not propose such a change immediately but invite the corporate leaders and the tax professional to debate this issue seriously for our future benefits.

Capital Market

81. The capital market though small, must be transformed into a vehicle for capital formation to our enterprises. In the context of promoting a low interest policy regime, we need to maintain a buoyant stock market and attractive shares so that people will have more income earning opportunities than keeping money in fixed deposits. This is made worse when the interest rates come down. This deliberate shift to creating a capital market environment that was driven on fundamentals instead of sentiments, led to local investors picking sectors like hotel stocks, instead of the past practice of following market rumors. With the low interest regime we expect dividend income also to go up, as companies will have lower borrowing costs. We also expect export companies as well as domestic manufacturers of consumer goods and food products to perform well under our economic policy. We are assuring a level playing field for them with importers. Local producers will become more competitive. This will obviously lead to greater profits which will translate to higher dividends. This combined with our aggressive SME empowering program, the potential pipeline of Initial Public Offerings (IPO) of local companies waiting to get listed in the Stock Market should move up local market capitalization.
82. In this context I will also simplify the application of VAT on financial services on stock market transactions and income tax imposed on the profit on sale of

shares introduced by the previous Government by replacing a simple 0.2% tax on transaction value on each side of the transaction of the stock market.

83. Further, in order to deepen stock market activities I propose to offer Government stocks in hospitality industry to make attractive gains for the Treasury.

Economic Service Charge (ESC)

84. The Economic Service Charge of 1 % is too high for certain categories including wholesale and retail trade. Therefore, I propose to reduce ESC rate to 0.5% to the wholesale or retail trade whether they are trading in local or imported goods. In the case of such trade, 3 years exemption from the commencement of business will not be applicable. There are also some ambiguities in the interpretation of turnover in certain types of activities. Therefore the Law will be amended to permit the Minister to issue regulations clarifying these definitions in categories of trade, business, profession or vocation other than areas already defined in the Act. The regulations will be published in the gazette and later placed before the Parliament.
85. In case of partnerships if an excess of any ESC paid over the partnership income tax, it will be distributed to the partners and the partners are entitled to claim credit against their income tax payable on the share of profit.

Tax Administration

86. Our tax administration remains outdated. It has been neglected for the past 25 years without any attempts of modernization. My predecessor attempted to create an enclave Revenue Authority without realizing that the Department of Inland Revenue is the Revenue Authority in Sri Lanka. We are now in the process of introducing a modern administrative structure supported by technology and human resource development to modernize the Inland Revenue Department. Towards improving the tax administration, I propose the following additional measures as well:
 - Establishment of an appeals unit under a separate Commissioner to deal with settlements of appeals made by tax payers against assessments sent by assessors. This unit will be supported by at least two deputy commissioners and four experienced senior assessors.
 - Implement a Tax Charter clearly explaining tax payer rights and obligations and a code of conduct for officials of the Inland Revenue Department

- Set up an information centre to collect and analyze information on tax evaders and strengthen the surveillance mechanism.
 - Codify the Income Tax law to make it simple and clear.
 - Appoint a three member committee of tax commissioners to certify every refund made by the Department of Inland Revenue. The committee should clear every such refund within one week of receipt.
 - Inaugurate dedicated Tax Courts in Colombo , Gampaha, Kandy, Galle to deal with tax recovery cases and offences relating to tax compliance enforcement and other disputes connected to tax administration. They will dedicate at least two days per week on tax related matters.
87. The Tax administration is confronted with certain difficulties in issuing assessments etc. due to the application of provisions of the controversial tax amnesty law. In order to strengthen the recoveries with the amendment to that Act it has become necessary to relax the time bar provision applicable in respect of issue of assessments, settlement of appeal and collection of taxes. Therefore, I propose to introduce necessary amendments to the relevant Acts.

Tax Ombudsman

88. Due to arbitrary, inequitable and ill-considered actions of the revenue administration, it is a true but a sad fact that even compliant tax payers have been driven to a state of non compliance due to a break down of trust and confidence. In many instances there is no action that provides comfort to the tax payer that his issue is being dealt in a fair and equitable manner. To provide this assurance and to bring about greater transparency in the system, I propose to appoint an independent revenue ombudsman to facilitate fair and expeditious settlement of tax payer grievances

A consultative process to prepare regulations and Tax Laws

89. Absence of a proper consultative process has resulted in misinformation regarding tax laws and regulations. Lack of interaction by the relevant authorities and by the relevant professional bodies have created serious doubts among tax payers regarding proper interpretation of tax laws. A taxation cluster comprising tax professionals, private sector representatives, officials from the Revenue Department and various other regulatory agencies has been set up to bridge this gap. Relevant regulations and amendments to tax laws will be made by the Ministry of Finance and Planning only after going through this consultative process in order to ensure wide acceptability.

Tax Compliance

90. Tax compliance remains unsatisfactory. The number of tax files are as low as 200,000 in a country where 4 million people are in the work force. In this background we propose to take several measures to improve tax compliance.

- a. Impose a withholding tax of Rs. 5,000 on each motor vehicle imported or newly registered in the case of vehicles added into the new fleet and Rs. 1,000 at the time of registration for already registered vehicles other than three wheelers, lorries and public transport buses. This can be set off against income tax.
- b. Any individual having four out of five of the following will be required to declare his/her income to the Commissioner General of Inland Revenue each year before the end of the tax year.
 - i. Has paid a monthly residential electricity bill exceeding Rs.10,000 (net)
 - ii. Has incurred a monthly credit card bill exceeding Rs. 25,000
 - iii. Has paid a monthly residential telephone bill exceeding Rs.10,000 (net)
 - iv. Has purchased an Air-ticket to travel abroad (other than official travel)
 - v. Owns a car

Non compliance to file a return will be liable to a penalty of Rs.50,000.

- c. Reward honest tax payers by issuing them a Gold Card with the following benefits
 - i. Qualify for a lottery conducted by the Deptment of Inland Revenue
 - ii. Special treatment from Government Agencies
 - iii. Discount prices at national parks, museum, paying wards etc.
 - iv. Special lounge at the Air Port to facilitate their travel.
- d. Tax clearance certificate will be made a mandatory requirement for bidding for Government tenders. In case of large transactions the bidders are required to declare the Income Tax file number as well as VAT file number.

- e. Provision will be made in the Act to make all tax returns to include the wealth declaration on the last day of the year of assessment and a declaration on income from tax exempted sources.

These measures are designed to develop a database to be used for the expansion of the tax base.

Advance Ruling for Income Tax and VAT

- 91. The prevailing Income Tax and VAT laws in Sri Lanka do not provide authority to the Commissioner General of Inland Revenue to issue advance rulings that are binding in law. As a result certain business transactions cannot be carried out with certainty as tax consequence of such transactions are not known in advance. In such circumstance the tax payers need to be given the opportunity to place the full facts before Revenue Authorities and obtain confirmation as to the tax implications. In order to encourage business transactions and simultaneously protect the tax base as well as to provide compliant tax payers with more certainty and confidence in the tax system, I propose that a legally binding system of issuing advance rulings be introduced into the tax laws. This would render tax administration more efficient and effective while promoting tax payer confidence in the system
- 92. The proposed changes with regard to income taxes will be effective from 1.4.2005. The changes proposed with regard to VAT will be effective from 1.1.2005. However, relevant amendments will be introduced to the Statute to make the Tax deduction proposed in respect of food items to be made with immediate effective.

Transfer Tax on Land

- 93. As promised in our 'Rata Perata' the election manifesto of the UPFA, our Government reintroduced the 100% transfer tax on land on non-citizens with a view to developing a proper regulatory mechanism to utilize our limited land in the best interest of the county. The provisions of the Finance Act permits the Minister to issue regulations governing the application of this tax. I propose to issue regulations in order to exclude the purchase of condominium premises and apartments above a 3rd floor of a building or acquisition of a land which will be developed as a residential housing in excess of 100 units, hospitals, or large scale public infrastructure facilities from the application of this tax. I also propose that non-citizens purchasing land in Sri Lanka and maintaining a foreign currency deposit in long term Sri Lanka Government issued securities to the value of US\$150,000 will also be given concessional treatment. The

restricted areas for purchase of land for foreign residents will also be gazetted shortly.

Customs Tariff

94. Consistent with our overall policy strategy towards facilitating a fair trading environment for both export and import sectors it is necessary to rationalize the Custom tariff structure. As suggested by the Trade and Tariff Cluster of the NCED, our Governments considers that duty on basic raw material should be maintained at the lowest rate band and work out intermediate bands depending on domestic value addition. On this basis I propose to implement a 5 band rate structure for the application of custom tariff as opposed to the prevailing 6 rate bands. Accordingly, I propose to reduce custom duties on basic raw material to 2.5% and maintain the semi processed raw material duty at 6%. To a best possible extent all intermediate products, spare parts etc. will be brought under the 15% rate and items such as motor vehicles and other finished products will be classified under 28% rate band.
95. Items which are not manufactured locally or are considered absolutely essential remain under exemption categories. The exemptions will be strictly in accordance with the regulations published in the gazette. Anomalies and other trade related issues will be constantly reviewed by the Trade & Tariff Cluster of the NCED with necessary recommendations for periodic corrections. The new Revenue Protection Order (RPO) giving effect to these changes has been already gazetted and will come in to immediate effect.
96. While rationalizing Customs tariffs, I have also take several steps to deal with under valuation and mis-description of goods by importers. In many cases we have found that importers and exporters continue to defraud by resorting to various illegal practices. In this background in the interest of the national economy we have to use some trade defensive measures. One such option is to take over such imported goods by the Government and reimburse the declared value by the importer if the custom is of the view that goods are grossly undervalued. I am seriously considering to resort to such measures if gross under valuations continue. In fact prior to 1988 there was a provision in the Customs Ordinance making provisions to take measures of this nature. In many of our neighboring countries such measures are being practiced. I will reintroduce similar amendments to the Customs Ordinance if the situation does not improve.
97. In the meantime, the Customs intelligence and surveillance unit will be strengthened and post audit investigation on selected items which are generally liable to under valuations will be intensified. As a trade defensive measure I

also propose to introduce anti dumping legislation to the Parliament shortly. In addition to under-invoicing there are also sub standard products that are being dumped into this country by various traders. Sri Lanka Customs is working very closely with the Sri Lanka Standard Institute and has recognized standards for 84 items to be applied for both locally manufactured as well as imported products to prevent substandard products being traded in this country. Through a wide consultative process standards for other important products will also be developed. In addition to strict application of quality standards the Customs will also ensure that products entering into Sri Lanka comply with ILO regulations on labour standards and environmental regulations applicable in Sri Lanka. Products manufactured using child labour will not be permitted to be imported to Sri Lanka.

98. In order to strengthen Customs surveillance, the Government welcomes the container security initiative of the US and as a first step US bound cargo will be brought under this arrangement during 2005. As part of the Customs modernization program, the cargo clearance process will be fully automated in 2005 and the construction of a modern Customs complex will commence in early January next year.

Port and Airport Levy

99. As a revenue measure, I propose to increase the Port and Aviation levy from 1% to 1.5% with immediate effect. However, the Port and Aviation levy applicable to exports will be reduced to 0.25% as an incentive for exports.

Excise Tax on Liquor

100. The Presidential Task Force on alcohol , tobacco and illicit drugs has prepared a national policy to reduce alcohol and tobacco use with a view to improving health decreasing poverty and improving productivity of the labour force. The task force recommends that taxation on alcohol and tobacco should be increased annually. I have already increased Excise Tax on cigarettes for this year. I now propose to increase Excise Duty on hard liquor by Rs.15/proof Lt. and Rs.5/proof Lt. for Beer. This will come into effect from midnight today.
101. Customs have made considerable progress in curtailing smuggling of cigarettes with the enforcement of the Tobacco Tax Act as amended in 2004. I have instructed Customs to intensify the enforcement of these measures to curtail smuggling.

Excise (Special Provisions) Duty

102. Excise (Special Provisions) tax is now confined to cigarettes, petroleum products, aerated water and motor vehicles. A large number of consumer durables remain outside this tax and even some of the imported products enjoy only 3% duties. This is not fair. Therefore I propose to include air-conditioners, refrigerators, washing machines, Televisions, TV antennas and electrical items under this tax. I also propose to increase the Excise (Special Provisions) Duty from Rs. 5.50 per Lt. to Rs.6.00 per Lt. for aerated water. These will come in to effect from midnight today.
103. The recent revision in Excise (Special Provisions) Duty on motor vehicles has been already operationalized in view of the national importance of securing Government revenue.

Betting and Gaming Levy

104. There are many betting and gaming centers operating under registration from local authorities. These are not regulated or supervised effectively. Most of these operators escape from law enforcement authorities by simply producing some of their tax receipts to establish their credentials. These taxes are recovered in terms of Betting and Gaming Levy Act No 40 of 1988 which requires the payment of taxes whether they are legal or illegal operations. All these operators should understand that payment of taxes will not prove their bona fides as legally valid operations. I propose that prohibitive taxes should be imposed in addition to combating these through appropriate law enforcement authorities. Therefore, I propose to increase the annual levy from Rs. 10,000 per center to Rs. 25,000 per center on all betting businesses. The levy on betting business done through agents will be raised to Rs. 1 million while betting business done with live telecast will be liable to an annual levy of Rs.500,000 per center. The levy on casino centers will be raised from the Rs. 12 million to Rs. 50 million per center with effect from January 2005. Ruginos Centres will be treated on par with Casino Centers. The Fines and Penalties that I have proposed hereunder will capture many other illegal activities to ensure strict law enforcement towards combating such operations. Amendment to the Betting and Gaming Levy Act will be introduced to strengthen the application of tax in respect of related operations.

Administrative Fees and Charges

105. The fees and charges imposed by various Government institutions for the provision of services remain unrealistic in comparison to related costs. Therefore, I propose that prices of all Government publications issued by the

Publications Bureau will be increased subject to the minimum price being fixed at Rs.50/=.

106. There are various statutory bodies and agencies which will also require to adjust their charges to reflect the present cost. I expect to recover Rs.250 million from these changes.

107. At present only Rs.150/month is charged on officials assigned to use official vehicle for private use. I propose to increase this to Rs. 500/month.

108. Rent on Government properties will be increased by 25%

Fines and Penalties

109. In keeping with the Government commitment to make law enforcement more effective, it has become vital to review fines and penalties currently in operation through various Statutes. While imprisonment or sentences are imposed on more serious offences a large number of offences are dealt with by imposing fines and penalties. However, Mr. Speaker, most of our laws have not been revised for many years. The fine and penalty structures in respect of criminal offences have remained unchanged for 25 years. Therefore, fine and penalty structure in many of our statutes should be amended and I have attached a schedule indicating the proposed changes. As several statutes come within the purview of provincial Councils, I also urge them to adopt appropriate resolutions as well.

110. Mr. Speaker, in terms of the Government commitment towards crime prevention Her Excellency the President has set up an advisory council comprising the clergy, civil society representatives, law enforcement Officer and business community representatives. The council has come up with a series of measures to prevent crime including special incentives to police officers who are genuine in their effort to prevent crime. Therefore, I propose to apportion part of this money to provide necessary incentives and welfare measures to the law enforcement officers and upgrading the Judiciary. In order to improve law and order it is also necessary to equip our Police force which has been neglected for several years. In order to improve their effective deployment, I propose to allocate Rs. 200 million to provide communication equipment and Motor Bicycles to them on a priority basis. A reward cum compensation mechanism will be implemented for law enforcement officers and the general public sharing information.

Dividend from Strategic Enterprises

111. Strategic State Enterprises have formulated business development plans with the assistance of SEMA. Development plans for State Banks include productivity improvement, loan portfolio improvements, promotion of international market links and, improvement in geographical coverage and customer services, complete automation of core banking and further strengthening the balance sheet to improve credit ratings of banks. In case of People's Bank a further capitalization by the Government will be implemented in a phased manner based on its quarterly performance. These business development plans will be presented to the Cabinet shortly.
112. The business development plan of the National Water Supplies and Drainage Board focus on the operations efficiency improvement in the operation efficiency through the reduction of non-revenue water and better Treasury management. In respect of Ceylon Petroleum Corporation, financial viability and operational efficiency is to be assured by promoting CPC brands and improving its image to compete in the market as a public enterprise. The business development plan also includes the upgrading of the refinery, introducing additives for fuel and a comprehensive human resource development program. The development strategy of the Ceylon Electricity Board is based on the a least cost power generation plan in the medium to long term, decentralize operational units within the CEB structure, adoption of commercial procurement procedures and a reliable tariff policy. A complete balance sheet restructuring is being formulated to reduce the present debt burden.
113. The business development strategy of the Sri Lanka Prot Authority is to increase terminal productivity through improved terminal management. The Airport and Aviation Ltd. aims at promoting BIA as a passenger transit hub and increase the traffic volume to 6 million passengers by 2007. Its plan also includes the development of a cargo transshipment hub. The public transport enterprises namely Sri Lanka Railways and the Cluster Bus Companies aim at reducing their revenue gap to reach breakeven operations. The Government will provide the cost of school children transportation and uneconomical routes. The two enterprises will adopt tariff formulas to ensure their operational viability.

Incentive to Public Servants

114. Mr. Speaker, in the context of the enormous responsibilities assigned to public service and its expected contribution towards promoting a balanced and efficient public-private sector economy, it is necessary to develop a proper

incentive structure to encourage public servant to play a pivotal role in the society. It is the public servants who are performing responsible tasks such as the provision of all island teaching, health services, wide range of field level extension services, law enforcement, and civil administration. In this background I consider it is necessary that the public servants be given sufficient incentives to give their best to the society.

115. Therefore Mr. Speaker, I propose to offer a comprehensive medical insurance scheme to all Government servants with a ceiling of Rs. 150,000. This medical insurance policy will provide indoor and outdoor treatment. The Government will provide Rs.500 million for this scheme and deduct Rs.75 per month from each employee. All employees will be given the same benefits regardless of whether they are low salary employees or high salary executives.
116. Housing is a basic need. Many of the public servants with their low salaries struggle to build a house often spending their entire savings in the process. In order to create a valuable asset to each public servant, I propose to implement a scheme through the banking system to provide a housing loan up to Rs.1 million with a interest rate of 4% per annum payable over a period of 25 years. The entire loan is guaranteed by the Government against their salaries and retirement benefits. In implementing this facility, priority will be given to all those public servants who do not possess a house at present and also those who are in the process of constructing houses. In order to ensure that this guarantee will not impose a burden on the Government, I propose to set up a separate Guarantee Fund in the Central bank of Sri Lanka to which the treasury will transfer Rs.1 billion each year. Accordingly, out of Rs.3,000 million provided under the advance account Rs. 1,000 million will be transferred in 2005 to this fund. Provision of a block of a land to public servants at a low and concessionary rate to build a house will also be made depending on the availability of such lands.
117. Public servants should also be provided with skills training and other opportunities for career development and productivity improvements. Unfortunately provision of training has been confined to a regular group of public servants and not to those who really need such training. I propose to change this practice and encourage professional training, skills development and productivity improvement programs among public servants. A wide range of technical assistance provided by various donors will be exploited to make available the required resources for such training. A new scheme will be formulated to make it mandatory for every public servant to follow at least a 2 weeks training program in the relevant field each year. Retiring professionals will be invited to develop and conduct training models for public servants.

Relief for Widows

118. There are a large number of young widows who are unable to plan their future due to the fact that they are denied the WNOP allowance from the Government if they remarry. I think this is unfair and outrageous in the context of social justice. Therefore, I propose that those who like to remarry be given 50% of the allowance that they are drawing as widows.

Child Care

119. Mr. Speaker nation need to pay serious attention to children. This requires in terms of our cultural and social values to have close attention of mothers. Presently 84 days (4 months) are granted for working women as full pay maternity leave. I consider this is inadequate. Therefore I propose that a further 84 days should be granted on half-pay-leave and the further 84 days on no pay leave so that those infants who deserve full year attention of a mother is given the flexibility to take a decision to spend time with the child on these concessions.

Salaries of Public Servants

120. Salaries of public servant are grossly inadequate. The basic salary of a lower rank employee is only Rs.4,620 per month while at the Secretaries level it is only Rs.22,910. These amounts are under any definition not decent. Therefore I propose to make a decisive change in this structure despite the very difficult times that we are going through. I am taking this bold step because my expectation is that a greatly motivated public sector could bring many benefits far in excess of the cost that will be reflected in the Budget. Therefore, I propose to grant a 40% increase of the current basic salaries subject to a minimum of Rs. 3,250 per month and a maximum Rs. 9,000 per month plus allowances already granted. This increase is 70% over the basic salary of a lower rank employee. The proposed increase will also correct the prevailing anomalies in the public service salary structure. In view of the current financial constraint to implement this in full immediately, I propose to give Rs. 2,500 or 50% of the proposed increase whichever is higher with effect from December 2004 and the balance from January 2006.

121. Mr. Speaker salaries of some of the firms in the organized private sector have collective agreement process to adjust salaries inline with cost of living as well as productivity considerations. There are sectors that comes under the Wages Board which adjust salaries according to market conditions. However, certain

sectors remain passive when it comes to periodic salary revisions. I request such sectors to fall in line with the salary increase recommended to public servants.

122. I also propose an increase in pension payment by 15% of the basic pension subject to a minimum of Rs.750 per month and maximum of Rs. 1,500 per month with effect from December 2004.

123. The public Sector also needs to consider some measures to improve productivity towards this end. I wish to make two further proposals

i. As an incentive to discourage public servants from using their full quota of Annual Leave, I propose that unutilized Annual Leave of any public servant be permitted to be carried forward with the ability to en-cash at the time of retirement for a lump sum based on the last drawn salary.

ii. In view of the large number of public holidays and the new incentive structure I have proposed, I also like to see slightly longer working hours in the public service. Therefore I propose that working hours in the public service be extended by 1 hour per day. Suitable adjustment could be made by starting office half an hour earlier and closing half an a hour late.

Management of Surplus Funds of State Institutions

124. Several Government agencies including those which depend on Treasury grants maintain various funds collected through statutory provisions and invest them mostly in Government securities or bank deposits in an ad hoc manner. The Treasury has undertaken a survey which reveals that the total value of this sum is in excess of Rs.15 billion. While recognizing the fact that transfer of such funds to the Consolidated Fund will not bring about much value, it seems necessary to ensure that these funds are managed by professional fund managers on behalf of the Government in a most productive manner while ensuring the flow of income to respective agencies to perform their operations. Therefore, I propose to set up a Trust under the Trust Ordinance and appoint a Board of Trustees to manage this fund. The Central Bank will be appointed as a custodian bank for this purpose. All surplus funds will be transferred to this trust and the Trustees will assign the fund management to a professional fund manager/s. The Trustees will appoint an internationally reputed Audit Firms to maintain, and audit the accounts of the trust on a regular basis. This will

enable the Government to reduce Budgetary allocations made in the annual estimates.

Strengthening Public Expenditure Control and Management

125. Two oversight committees of Parliament namely the Public Accounts Committee and the Committee on Public Enterprises can play a pivotal role in ensuing public accountability and productive use of Government expenditure. It has been brought to my notice that the capacity of the two oversight committees both in terms of human resources as well in terms of technology application requires considerable improvement. At a recent meeting held by the two oversight committees with my officials, it has been agreed to setup a three year capacity building program to develop a well equipped, professionally managed secretariat to facilitate the effective functioning of these two committees. My ministry has recommended a dedicated provision of Rs. 100 Million over a three-year period for this purpose. Accordingly I now propose Rs. 100 Million for this project, to be specifically managed by a project management team directly accountable to a Steering Committee co- chaired by the Chairman of the two committees, and consisting of officials from the Parliament, my ministry and the Auditor General.

Savings in Public Expenditure

126. The Ministry of Finance and Planning has developed a technology driven monitoring system of public expenditure and has set up a Treasury Operation Department to streamline public expenditure management. The release of funds will be made on the basis of performance monitoring. Procurement systems have been streamlined to prevent market manipulations. I must mention here that the recent intervention by the Government on a fertilizer tender has reduced the bidding price by US\$ 150/mt. which will allow us to continue with the concessional prices we have offered to our farmers for fertilizer. This clearly shows that we have to be vigilant in Government procurements. Therefore, I am hopeful to generate savings from locally funded capital expenditure programs provided for in the estimates.

Interest Payments on Public Debt

127. Within our domestic debt portfolio, Rs. 68 billion of Rupee loans carry interest rates in the range of 11 – 13%. I propose to convert these loans into relatively low cost medium to long-term debt instruments which in my opinion could save Rs.4.3 billion over the medium term. I expect Rs. 1.1 billion saving next year

alone. The relevant amendments to the Appropriation Bill will be made at the committee stage.

A summary of the Budgetary implications of my proposals are given in Annex II and III.

Budget Outlook

Mr. Speaker, table 1 of the annexed document provides details relating to Budgetary Projections for 2004 and 2005. The proposals that I have outlined in my presentation will increase Government expenditure by Rs. 19,463 Million and Government revenue by Rs. 27,935 Million. I also anticipate Rs. 7,500 million from capital revenue and the sale of Government stocks in hospitality industry which are offering good values. Consequently, total Government revenue in 2005 will be Rs. 389.5 billion - 17.2% of GDP compared to 15.6% in 2004. In view of the fact that full annual impact of the revenue measures implemented towards the end of 2004 and the new measures that I have announced will be reflected in 2005, this level of revenue is realizable. As regards expenditure, the current expenditure will be Rs. 419 billion - 18.5% of GDP. despite the wage increase, recurrent expenditure is lower from 19.3% of GDP in 2004. Thus the revenue deficit is reduced from Rs. 74 billion – 3.7% of GDP to Rs. 29 billion – 1.3% of GDP, a solid 2% of GDP improvement in the revenue account.

Mr. Speaker, public investment is projected at Rs.144 billion - 6.4% of GDP an increase from Rs. 101 billion - 5% of GDP in 2004. This is after making provision for usual under expenditure and for the proposed new expenditure programs. The 2005 Budget counts on Rs. 69 billion from net foreign loans and grants, after making adjustment for debt repayments. In gross terms that is Rs.101 billion (approximately US\$ 980 million) without counting Budget supports. This helps us to keep our domestic finance at Rs.105 billion - 4.6% of GDP for next year as compared to 6.8% GDP this year. The level of domestic financing is not only lower than this year but is also considerably below the total available resources in the economy, of which Rs.115 billion available from non bank sources. This in economic terms means that the market has excess funds which the Central Bank can mop up to keep monetary growth in check and thereby lower inflation to ensure a positive rate of interest. In conclusion, the salient feature of this Budget outcome is that the consumption expenditure of the Government is phased out to allow increased revenue to support public investments and to reduce domestic borrowings.

CONCLUSION

Mr. Speaker, let me now summarize the benefits cascading from this Budget and our economic policy. Let me begin first by recapping the pre-Budget economic policy initiatives that have already achieved success.

As soon as our Government came into office, we realized that markets were driven by sentiment and that various speculators were manipulating the share market, the treasury bills and bonds market, as well as the foreign currency market through rumors and false premises. The first task of the Government was to break this sentiment based activity and shift to a economic fundamentals driven market activity, so that the investor public and stakeholders are protected from ill-motivated speculators.

Mr. Speaker, the Government saw benefits in continuing with the policy of low interest rates. This was not an easy task, as we had to overcome the pressures and obstacles planed by interest rate speculators. Except for occasional inter-bank borrowing pressures, the treasury bills and bond market has stabilized at around an average interest rate of 7 - 8% . This also meant that the local stock market benefited, too. It is far more attractive to invest in shares than keep the money in fixed deposits, when the interest rates come down.

Equally we are confident that we will maintain the stability in the exchange rate as well. During the first nine months additional burden on account of the import of fuel and motor vehicle was in excess of US\$ 300 million. This cannot be cleared simply by letting exchange rate changes. The current exchange rate is in fact under valued and favour exports. The Government of India, in addition to extending about US\$ 150 million on project financing has also extended us a credit line to the value of US\$ 150 million to finance our petroleum imports. Government of Iran and Malaysia have also agreed to provide nearly US\$ 200 million credit on our crude oil financing. The expected foreign exchange inflows through aid disbursement towards the end of the year will also strengthen market conditions. Therefore pre-Budget speculative pressures are unwarranted.

Mr. Speaker, on that note, let me now summarize the benefits of this Budget

- 41,305 graduates will be employed in permanent positions in the Government services from January 2005. In addition to providing opportunities to the qualified youth to contribute towards nation building, an equal number of families see relief from being able to see their sons and daughters, finally in employment.
- 30,000 Advance Level qualified persons will see similar openings in Government vacancies in 2005.

- The 10,000-irrigation tank and watershed rehabilitation program will support 560,000 beneficiaries on farm income. Each tank will support at a minimum 10 farmer families, who on average have 5 family members to support, and have the potential to earn, minimally Rs.60,000 a year.
- The proposed SME Bank with a Rs. 5,000 million capital base to revive the SME sector, will create at a minimum, 25,000 new jobs either through existing enterprises that expand, or from entrepreneurs launching new enterprises.
- The 10,000 Entrepreneur Village Program will target cluster economic activities in various parts of the country, providing gainful employment for 30,000 people.
- Our integrated rural infrastructure development program, known as the Sanwardhana Sangramaya, targeting urban, provincial, and rural renewal, including the housing program will create 300,000 new houses, 300 Vidatha resource centres, 260 new school buildings, 1000 new hospital buildings, 1000 public libraries, 25,000 miles of new roads covering 360 AGA areas, electricity to 100,000 new homes and 50,000 existing homes, pipe borne water to 100,000 homes and 5 new export zones and supply chain centers throughout the country. These projects translate into work for 120,000 skilled and semi-skilled persons, suppliers of building materials, and other construction inputs.
- Skills development and foreign employment program will raise the current level of foreign employment of around 1.2 million to 1.5 million - 300,000 additional employment toward the next 3 years.
- As enunciated in our overall policy vision, we will aim at the final outcome that will reflect in the medium term growth target of 6-7% of GDP.
- We expect to maintain the inflation rate at around 7 - 8% with the overall National Savings Rates at 24% of GDP.
- We expect quoted companies in the stock markets to increase their shareholder value by a further 50%, from the present 262 billion market capitalization to 400 billion in 3-years. The creation of 3400 new entrepreneur owned enterprises in the SME sector will lead to the unemployment rate been kept at 6% .
- The foreign commercial borrowings and short term domestic borrowings will be maintained at prudential levels.
- The Human Development Index (HDI) and Human Well Being Index (HWI) are also other valid barometers, as they reflect social progress such as the literacy

rate, life expectancy and the environment that provides us our food, water and natural resources. Therefore our target is to achieve Millennium Development Goals well in advance.

Mr. Speaker, I have deliberately departed from tradition and included measurable output targets in this Budget, so that the country has objective targets to aim for, and of all, be they politicians, public servants, or the private sector are made to realize that we must come together to achieve the targets and development goals set therein. It is only through such a partnership that we could achieve national goals.

This Government, as you can see from the Budget proposals, is firmly committed to greatly enhance the export competitiveness and to level the playing field for local market producers, with the obvious objective of increasing our domestic earning capacity. That is the only way we can fight the cost of living pressures arising out of the oil price hike that is beyond our control. No responsible Government could bring the cost of living down on imported items, without a ballooning subsidy scheme that is funded through borrowings or taxes. That is not a sustainable path.

Equally, our public service has a special responsibility to increase their efficiency and productivity. They have to ensure that the tax payer's money is spent properly without wastage and corruption. The UPFA Government has faith in the public service, and believes that they can deliver, which is why we have stopped privatization, stopped retrenchment, stopped creating independent agencies, stopped cutting salaries, stopped cutting recruitment, and stopped freezing benefits. Therefore all public servants have a duty to deliver this year, and to convert our public service to a quality service.

This is our last chance, to maintain our dignity. I myself was a civil servant, and I know how much more we can all contribute to our motherland. We must stop treating a Government job as a job with no accountability. We are being paid by the hard earned income of the working population of this nation. Thus, it is only reasonable that they expect us to perform much better than we do today. We can and we must. Our Government has taken steps to fulfill your wishes and now we expect you to do your part honestly and efficiently.

I would be failing in my duty, if I, as a fellow politician, also do not turn the lamp inwards, as there is much we can also do to create exemplary standards, particularly with regard to our expenditure. After all, our costs too are met by tax payers. If we continue the way we spend public funds, there will come a day when they will say, enough is enough.

In closing, I would like to reiterate the essence of our economic policy as set forth in our vision statement published in June this year. This statement captures the spirit of this Government's Budget:

"The strength of this nation lies uniquely within. The policies we develop will take advantage of our competitive strengths and proactively plan the development path based on our culture, resources and regional dynamics. It is time to look ahead and convert strategies into action and make genuine progress towards sustainability for the benefit of society, the environment and creation of wealth in Sri Lanka."

Thank you

Summary of The Budget

	2004 Revised Rs. million	2005 Estimate Rs. million
Total Revenue	312,482	389,492
Tax Revenue	282,369	351,119
Income Tax	43,467	55,361
Taxes on Goods and Services	184,898	224,262
Taxes on External Trade	49,590	66,243
Non tax Revenue	30,113	38,373
Total Expenditure	485,302	560,638
Current Expenditure	386,568	418,988
Salaries and Wages	107,962	140,517
Interest payments	120,232	128,000
Subsidies and Transfers	102,280	92,435
Other Goods and Services	56,093	58,936
Public Investments	101,279	144,440
Other	-2,545	-2,790
Revenue Surplus/Deficit(-)	-74,086	-29,496
Budget Deficit	-172,820	-171,146
Total Financing	172,820	171,146
Total Foreign Financing	24,480	48,684
Net Foreign Borrowings	24,480	48,684
Foreign Borrowings	57,652	91,000
Debt Repayments	-33,172	-42,316
Foreign Grants	9,888	10,200
Domestic Financing	136,015	104,762
Non Bank Borrowings	106,417	104,762
Bank Borrowings	29,598	0
Other	0	0
Capital Receipts	2,437	7,500
As a % of GDP		
Revenue	15.6	17.2
Tax	14.2	15.4
Non Tax	1.5	1.7
Expenditure	24.4	24.6
Current Expenditure	19.3	18.4
Public Investments	5.0	6.4
Revenue Account	-3.7	-1.3
Budget Deficit	-8.6	-7.6
Foreign Aid	1.7	2.5
Domestic Non Bank Financing	5.3	4.6
Domestic Bank Financing	1.5	0.0

Revenue

	Rs. Million
- Cess	2,850
- Reformulation of VAT to a 4 band rate structure	3,100
- Exemption of agriculture from income tax	(100)
- Removal of income tax exemption from Gold, Gem And jewellery	75
- Rationalization of taxation of employment benefit	50
- Simplification of personal income tax (revenue neutral)	0
- Presumptive tax on NGOs	50
- Rationalization of Corporate tax	1,675
- Simplification of Economic Service Charge	400
- 0.2% tax on transaction value	450
- Tax Administration	850
- New Tax compliance measures	800
- Rationalization of Custom Tariff within a 5 rate band and strengthening custom administration	3,100
- 0.5% increase in Port and Airport development Levy	2,500
Excise Tax on Liquor	950
- Countervailing measures on smuggling of cigarettes	850
- Expansion of the coverage of commodities under Excise (Special Provision) Duty	1,850
- Excise (Special Provisions) Duty on motor vehicles	2,800
- Increase levy on Betting and Gaming	450
- Revision in Administrative fees and charges	350
- Fines and Penalties	750
- Dividend from Strategic Enterprises	2,500
- Other	1,135
- Capital revenue	7,500

Expenditure

Annexure II

	Rs. Million
Recurrent Expenditure	
a. Salaries and Medical insurance for Public servants	24,000
b. Pension	3,400
c. Saving due to surplus funds	(750)
d. Grant to oversight committees of parliament	100
e. Targeted fuel subsidy	1,000
Development Expenditure – New initiatives	
1. “Gamata Thakshanaya” Vidatha Resource Centers	300
2. Pubudamu Wellassa infrastructure program	300
3. Rajarate Navoday - Provincial infrastructure program	300
4. Dayate Sevena - National housing program	500
5. Floriculture sector development program	20
6. Dairy industry Development program	50
7. Assistance for organic product export	10
8. Rehabilitation of Puttalam-Chillaw Prawn farming Zone	20
9. Osu Gammana and Reforestation program	150
10. Samurdhir – Suwahas Jana Pubuduwa – Self employment/micro enterprise development program	450
11. National Accreditation Board	10
12. Contribution to Construction guaranteed fund	250
13. Setting up of Academy for Advance Construction training	100
14. Skills Development program	100
15. SME Authority	100
16. SME Bank (book transfer)	5,000
17. Contribution to University facilities - Uva, Rajarata and Eastern	519
18. Export development incentives	1,000
19. Incentive for productivity improvement & product design for apparel industry	150
20. Development religious activities	100
21. Contribution to cinnamon Development fund	10
22. Law enforcement initiatives – Sri Lanka Police	200
23. Film Academy (token provision)	200
24. Youth employment – Graduates – already provided	2,885

	1,100
25. 30,000 Advance Level and 1,000 Ordinary Level qualified Youth (already provided)	350
26. Modernization of Small and Medium paddy mills	
Expenditure Savings	900
1. Recurrent	3,690
2. Capital	1,500
3. Advance accounts	

Gross Borrowing Requirement - 2005

	Rs. billion
Total receipts other than Government Borrowings	421.7
Total payments	857.3
Total gross borrowing requirements to be recorded in government accounts	435.6
Total Debt Repayment	264.4