Daily News Editor - 429221 Fax - 429220 e.mail - business@dailynews.lk

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Ten percent VAT from January 2003

Bank margins expected to increase

By Ravi Ladduwahetty

Bank margins are expected to rise with the Government's decision to implement the Value Added Tax (VAT) regime with effect from January 1.

However, the Bankers' Association of Sri Lanka is awaiting clarifications from the Treasury on a series of issues related to the amendments to the legislation on VAT and the real effect on the bank margins due to the impending Value Added Tax will be known only after that, the banking community told the *Daily News* in individual interviews yesterday.

The Colombo based banks cannot pass on the effect of the Value Added Tax directly to the customers as the VAT will be depended on the pre-tax profits of these financial institutions and employee emoluments, Chairman of the Bankers' Association of Sri Lanka Kapila Jayawardena said.

Jayawardena, who is also the Country Head/ Chief Executive Officer of Citibank NA said that there could be a slight increase in lending rates and the margins to compensate for the VAT but added that it was a little too premature to comment on it.

He said that the banking community was awaiting the clearance from the Ministry of Finance on a plethora of issues.

Secretary of the Bankers' Association of Sri Lanka Gaston Gunewardena said that the Ministry of Finance had sent the draft of the amendments to the Value added Tax Act No. 14 of 2002 which was passed in Parliament in August which had certain implications on the banking sector and that the Treasury was awaiting the response of the banking community to it.

"We received the amendments only two days ago and we are currently studying it. We will be submitting our recommendations to the Treasury before the end of the month," he said.

Hatton National Bank Managing Director/CEO Rienzie.T. Wijetilleke said that the banks and financial institutions were awaiting some relief from the Ministry of Finance on employment expenses on which banks are expected to pay 10 percent VAT.

He said that they were also awaiting the Treasury to clarify on the 50 percent of the VAT being set off against Corporate Tax and that the possibility existed that lending rates could go up because of that.

He said that the banks were considering the lowering of interest rates on borrowing in selected areas such as for small and medium scale industries and also for housing and construction.

Deputy Chairman of the Ceylinco Securities and Financial Services Group Bandula Ranaweera said that the lending rates would definitely go up once VAT is introduced in January as the banks and the financial institutions would be passing on the tax to the borrowers.

This will certainly upset the Government's low interest regime and the higher cost of borrowings will have a series of impacts on the overall economic growth, he said.

The sector which will be mostly affected will be exports due to higher cost of borrowings. The competitiveness of Sri Lanka's exports will be seriously affected in the light of lower single digt interest rate which prevail in developed countries. Bank of Ceylon Chairperson, Sumi Moonesinghe said that her bank will engage in a overall re-pricing strategy aimed at drastically pruning down cost and wastage which will be instrumental in cushioning the potential increasing lending rates which is likely following the implementation of the VAT regime in January 2003. "Our strategy is not to raise the lending rates with the VAT but to compensate the possible escalation of lending rates with the reduction and so that lending rates will remain at the same level.

Commercial Bank, CEO/MD Amitha Gooneratne said the Treasury is yet to clarify the mechanism of the implementation of VAT and there are certain criteria which have to be clarified. It is only after that the impact on lending rates can be commended upon.