



NATIONAL TAXPAYER PERCEPTION STUDY

SRI LANKA 2024



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Sri Lanka's first national taxpayer perception study is anchored under the United Nations Development Programme (UNDP)'s overall support to the Government of Sri Lanka, as a component of the Tax for SDGs (T4SDGs) programme, a global initiative implemented by UNDP in 25 countries. The Tax for SDGs global Initiative is supported by the Government of Finland and the Government of Norway. This programme is implemented in Sri Lanka under the leadership of the Ministry of Finance and the Inland Revenue Department.

T4SDGs programme aids developing nations in boosting domestic resource mobilization and meeting the Sustainable Development Goals. The initiative treats taxation as a revenue tool and a policy instrument to drive sustainable growth and influence behaviour towards climate, nature, well-being, and governance goals. Leveraging UNDP's role as an enabler and catalyst, Tax for SDGs aims to broaden choices for a balanced, sustainable future in line with the 2030 Agenda for Sustainable Development.

The technical partner for this study was the Economic Intelligence Unit of the Ceylon Chamber of Commerce. This study was advised by Dr. Tiloka de Silva, Department of Decision Sciences, University of Moratuwa, and external economic consultant, Mr. Shiran Fernando.

This study would not have been possible without the leadership and the firm commitment of the Ministry of Finance and the IRD towards promoting public engagement on tax policy and administration.

The survey is available online at UNDP, Ministry of Finance and IRD websites.

EXECUTIVE SUMMARY

Boosting tax revenue is crucial for sustainable development. Enhanced tax revenue hinges on compliance, and understanding the factors driving compliance is key. Fiscal contract theory posits that people pay taxes because they appreciate the benefits received in return. As paying taxes involves sacrificing personal income for public good, it presents a collective action dilemma. Therefore, both the citizen-state relationship and the inter-citizen relationship significantly impact tax compliance. Enhancing voluntary compliance and public trust in the fiscal system hinges on a perceived fair and equitable design. Tax administration must deliver service-oriented taxpayer assistance, ensuring citizens have the necessary information and support to fulfil obligations and claim entitlements, crucial for systems fostering voluntary compliance.

This study – the first national taxpayer perception study in Sri Lanka - aimed to assess business and household perceptions of fiscal policies and tax administration in Sri Lanka in light of the economic crisis and the subsequent tax policy effort that is part of broader economic reforms. It provides a comprehensive analysis based on a general survey and Key Informant Interviews (KIs), capturing insights from respondents across all nine provinces. The survey involved 567 participants, while the KIs included 75 key informants, covering all 9 provinces in Sri Lanka and the survey was carried out in all three languages. The study's findings align with initial expectations, confirming the Ministry of Finance and Inland Revenue Department's views on business and public perceptions of tax policy and administration.

The study assessed people's familiarity with tax concepts, perceptions about fairness, satisfaction with tax-related government services, trust in institutions, and transparency of- and participation in budget process. Respondents demonstrated varying familiarity with tax concepts, with TIN holders showing higher familiarity. While direct taxes were perceived as fairer than indirect taxes, less than half viewed the tax system as fair. The complexity of the tax system was a significant concern, particularly among TIN holders. New tax policies introduced since 2023 received unfavourable perceptions, significantly impacting economic activities.

The study also revealed low satisfaction with government services, particularly in efficiency and quality. The study found that corruption within tax administration and the broader government framework significantly reduces the effectiveness of tax collection and erodes public trust, making it challenging to encourage voluntary compliance. Addressing this issue through institutional reforms is crucial to enhance transparency, accountability, and public confidence. Transparency in budgeting and policy formulation was perceived to be low, with education, health, and defence identified as top priority areas for the national budget. Furthermore, the Key Informant Interviews provided additional insights into the adverse impacts of recent tax policies on various sectors. Issues such as reduced disposable income, increased informal sector activities, and inconsistent tax policies were prevalent. The KIs emphasized the need for wider stakeholder consultations, better understanding of sector-specific needs, and avoiding politically motivated tax concessions.

Suggestions for improving tax policy and boosting tax morale included widening the tax base, reducing rates while increasing penalties for evasion, ensuring long-term consistency in tax policies, and simplifying the tax code. There was a strong call for greater transparency, higher accountability, and eliminating corruption to enhance public trust in the tax system. Leveraging digitization was seen as key to minimizing corruption, reducing errors, and increasing compliance. Suggestions included mandating the use of TIN for various transactions, linking databases across institutions, and promoting cashless transactions.

This study provides valuable insights into the current perceptions and challenges related to the tax system in Sri Lanka. The findings and recommendations serve as a foundation for policy improvements aimed at creating a more equitable, efficient, and transparent tax framework.

INTRODUCTION

There is mounting evidence on the importance of taxation to any economy. It is used to raise revenue for government, redistributing wealth and income and allocation of resources among the population. Taxation facilitates good state-society relations through accountability and good governance and is used as a tool for development by providing a sustainable source to raise revenues for provision of social services and improving peoples' livelihoods.

The Sri Lankan economy has longstanding structural weaknesses, which culminated in 2022, in a sovereign external debt default and the worst economic crisis the country has experienced in its post-independence history. Key among these weaknesses have been fiscal sector imbalances driven by poor revenue performance resulting in consistent government budget deficits and an unsustainable public debt. The Sri Lankan tax revenue to GDP ratio is among the lowest in the world and has been characterised by a reliance on distortionary and regressive indirect taxes such as Value Added Tax (VAT), excise tax and customs duties, and an eroded tax base due to a large number of exemptions, high thresholds and low compliance (World Bank, 2022).

Following the sovereign debt default and economic crisis in 2022, where the economy contracted by 7.3% amid historically high inflation, sharp currency depreciation and political unrest, the government entered into an extended fund facility (EFF) with the IMF. The prior actions for the EFF arrangement included several revenue-related measures to support fiscal consolidation to achieve programme benchmarks. Accordingly, from 2022 onwards, many tax policy changes came into effect including increases to VAT rates and removal of exemptions, changes to income tax structures including reduction of thresholds and increases to rates, reintroduction of withholding taxes,

etc. At the same time, reforms to achieve cost-recovery for state-provided utilities (electricity and water) and fuel were enacted, resulting in further tariff and price hikes (Central Bank, 2023). While these (and other) reforms have helped the government move towards achieving the structural benchmarks of the IMF programme and economic stabilization, they have had adverse effects on the disposable income of Sri Lankans. Poverty is estimated to have more than doubled since pre-Covid levels, with increases in inequality and food insecurity, malnutrition and stunting (World Bank, 2024).

Given the context in which the reforms were implemented as well as the nature of the reforms, there has been a heightened focus on tax and related reforms among the general public. A rudimentary sentiment analysis of media coverage of the reforms suggest that a majority of media headlines have been informative (neutral) in nature while the shares of headlines conveying negative and positive sentiments vary based on the language considered (Figure 1 and 2).¹ As Figure 2 shows, the Sinhalese news websites were slightly more likely to use headlines with negative connotations. A few examples of headlines classified as conveying negative sentiments include "The economic crisis should have been considered before the tax cuts" (translated from Sinhala), "The country is losing 500 million taxes due to irregular distribution system of liquor companies" (translated from Sinhala), and "Current Tax arrears amount more than Rs 943 billion". Examples of headlines classified as conveying positive sentiments include "Expert reveals best Tax to increase revenue without hurting poor", "People will get relief from the tax revision in March" (translated from Sinhala), and "Expert reveals best Tax to increase revenue without hurting poor". However, further refinements to the analysis would be required before making definitive conclusions.

¹ The analysis made use of more than 1800 headlines related to tax from selected Sri Lankan news websites in both English and Sinhala. The natural language processing (NLP) algorithm was used to classify headlines into positive, neutral or negative sentiments based on both the type of words used as well as word sequences (for instance, "not good" is categorized as negative). However, it should be noted that inaccuracies in classification may exist and further refinements to the algorithm would be required to make more definitive conclusions.



Figure 1: Wordcloud based on tax-related newspaper headlines

Note: The wordcloud is generated using 1069 headlines collected from five English news websites and 810 headlines collected from four Sinhala language news websites. Headlines appearing from the 1st January 2023 to 13th February 2024 were extracted using the search term “tax”.

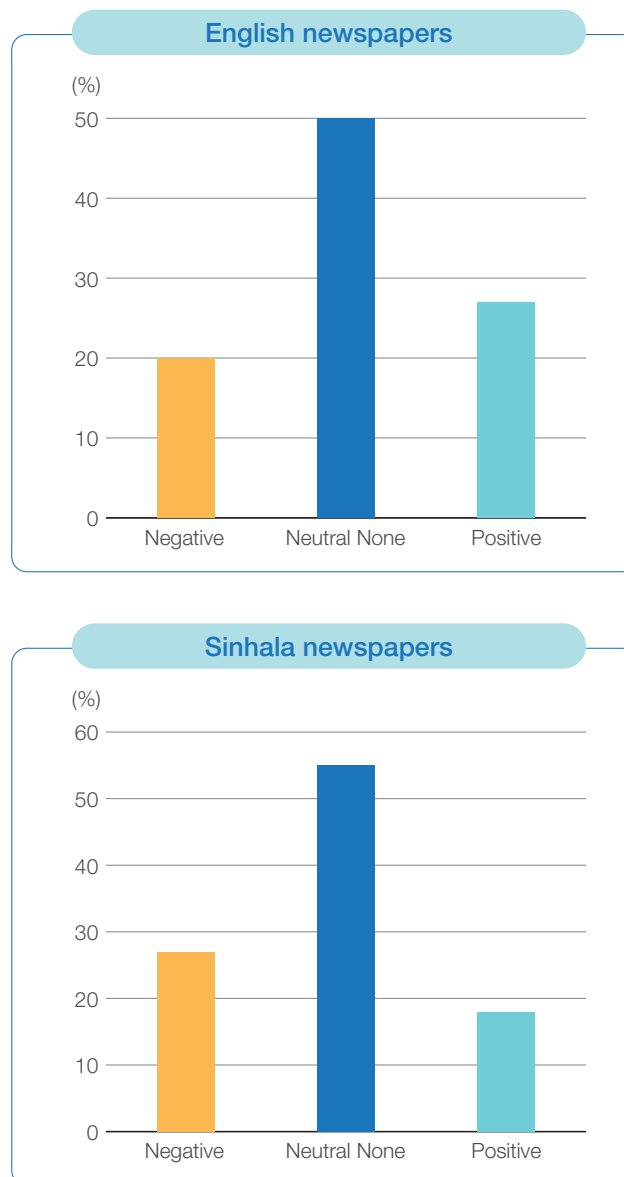


Figure 2: Sentiment analysis of tax-related newspaper headlines

Note: Headlines are classified by sentiment using scores generated using Python’s Vader library.

While a governments' ability to collect taxes depends on the people's ability and willingness to pay them, encouraging tax compliance demands a careful understanding of how taxpayers think about and experience taxation. Knowledge about taxpayer attitudes and behaviour is essential when analysing opportunities and constraints for reform, and for the design and implementation of effective policy and administrative measures to enhance compliance. However, at present, there is little in the way of analytical work that examines taxpayer perceptions and attitudes related to tax policy and administration in Sri Lanka.

The National Tax Perception Study – Sri Lanka 2024, a collaborative effort between the UNDP and the Ceylon Chamber of Commerce, offers an in-depth analysis of public opinions and attitudes towards the tax system in Sri Lanka. The study, which is the first of its kind for Sri Lanka, integrates findings from a nation-wide survey of 567 participants covering all districts and detailed Key Informant Interviews (KIIs) with 75 experts from various sectors across all nine provinces. This dual approach ensures a robust representation of views, encompassing both broad public sentiments and specialized insights from knowledgeable informants.

The study's objective is to identify key challenges and opportunities within the current tax framework, with a focus on taxpayer attitudes, the perceived fairness of tax policies, and the effectiveness of tax administration. Despite some limitations, such as the overrepresentation of respondents from certain regions and strata, the findings provide a solid foundation for understanding how people perceive and experience the Sri Lankan tax system. These insights are crucial for formulating policies that enhance compliance, transparency, and overall efficiency. The study also underscores areas for future improvement, aiming to foster a more equitable and transparent tax environment.

METHODOLOGY

1. Overview

Utilizing a mixed-methods approach, the study unfolded in two sequential phases over six months. The first phase involved a quantitative survey using structured questionnaires to provide a broad, generalizable view of taxpayer categories. The data collected in this phase informed the second phase, which delved deeper into taxpayer attitudes through Key Informant Interviews (KII) facilitated by the Chamber of Commerce. The integration of quantitative and qualitative data during the interpretation stage ensured a comprehensive understanding of taxpayer perceptions, offering both breadth and depth of insight.

2. Methodological Framework and Research Design

The Tax Perception Study was designed with a framework to capture various aspects of public perceptions, experiences, expectations, attitudes, and sentiments towards the tax system in Sri Lanka. The study consisted of two primary components: secondary research for context mapping and primary research for detailed perception analysis. The secondary research aimed to provide a comprehensive understanding of the context within which public perceptions are formed by analyzing various sources, including public finance data, macroeconomic data, media reports, parliamentary records, and other public documents. This phase included sentiment analysis of media reports in Sinhala, Tamil, and English, and utilized reports published by the Ministry of Finance and Parliament to extract data on past and current tax policies and reforms. This mapping exercise helped set the context for understanding public experiences and satisfaction with the tax system.

Building on this foundation, the primary research was designed to capture detailed public perceptions through quantitative and qualitative methods. The quantitative component involved administering a general survey both online and via enumerators sent across the country, covering all districts, to ensure a wide representation of taxpayer perceptions. Two separate questionnaires were prepared: one for the general survey and one for the Key Informant Interviews (KIIs). The qualitative component consisted of KIIs with representatives from various categories, including individuals, small-scale

businesses, medium-scale businesses, large-scale businesses, other large taxpayers, and chambers, trade, and industry associations, covering all nine provinces. This mixed-methods approach facilitated a detailed and nuanced analysis of public perceptions, sentiments, and attitudes towards the tax system in Sri Lanka, thereby enriching the study's foundation established through secondary research.

To further enhance the study, an explanatory sequential design was employed, where quantitative data informed the qualitative phase. Data integration occurred during the interpretation and reporting stages, synthesizing findings from both phases to provide a comprehensive understanding of taxpayer perceptions. This approach allowed the qualitative data to explain, elaborate upon, and clarify the quantitative findings, resulting in a holistic and nuanced analysis.

To structure this analysis, the study framework unpacked six key elements: tax policies and regulations, tax administration, tax utilization, trust in government and credibility, citizens' general perspectives and attitudes towards the tax system, and the evolution of perceptions of the tax system amongst taxpayers and businesses in Sri Lanka since the beginning of 2023. These elements covered enforcement of tax laws, fairness and consistency in tax structure, ease of compliance, clarity of tax rules, services provided by key revenue agencies, satisfaction with budget allocation, quality of government services, transparency, public accountability, and opportunities for citizen participation. Understanding the level of acceptance of a tax system and willingness to comply begins with the question of perception, influenced by past experiences, interactions, and expectations of the future, and framed by institutional and policy structures as well as public discourse. This comprehensive framework allowed for a thorough examination of the factors influencing public perceptions and provided valuable insights for potential reforms, thus connecting the primary and secondary research findings seamlessly.

The overall objective of this study was to understand citizens' perceptions and sentiments on the current tax policy, administration, efficiency, accountability, and citizen involvement in tax policy processes in Sri Lanka. The findings were expected to inform the

ongoing discussion and debate on ways and means of improving existing tax policies and tax administration to enhance taxpayer compliance. Additionally, the study aimed to facilitate tax justice campaign interventions in the country by providing a detailed understanding of public attitudes towards the tax system, capturing the interplay between past experiences, current realities, and future expectations in shaping these perceptions.

3. Quantitative Research Component

The quantitative phase involved collecting data through a structured general survey administered to a purposively selected sample representing various taxpayer categories. This phase aimed to provide a broad understanding of taxpayer attitudes across different categories and provinces. Enumerators were deployed to cover all districts for the general survey, ensuring comprehensive geographic coverage. The sample size determination, based on population estimates and confidence levels, ensured robust data collection.

Survey Instrument Development: The structured questionnaire was designed to capture a range of variables related to taxpayer satisfaction, attitudes toward tax fairness, and perceptions of tax administration efficiency. The questionnaire underwent rigorous pilot testing with a small, diverse group of taxpayers to ensure clarity, relevance, and reliability. Both online and

offline survey methods were utilized to maximize reach and respondent convenience. Enumerators received comprehensive training to ensure consistency and accuracy in data collection. The survey was conducted in all three languages: Sinhala, Tamil, and English, to ensure inclusivity and comprehensive coverage.

Data Analysis: The collected survey data were subjected to descriptive statistical analyses to identify common experiences and sentiments among respondents. For the most part, the analysis separates respondents who had a tax identification number (TIN) and those who did not as the two groups were likely to have different levels of engagement and familiarity with the Sri Lankan tax administration and policy. The findings from the descriptive analysis of the survey data are supplemented with more detailed insights and excerpts from the KIs allowing for a fuller narrative.

3.1 Sample description – background of the respondents

The survey comprised 567 respondents, with 240 responses collected through an online survey and 327 by enumerators (see Table 1). This methodology ensured comprehensive reach and representation across all districts, capturing diverse demographic and economic backgrounds essential for a holistic understanding of tax perceptions in Sri Lanka.

Table 1: Sample size by province

Province	Population Estimate (2021)	Sample Size
Central	2,811,000	42
Eastern	1,783,000	36
North Central	1,402,000	28
Northern	1,165,000	66
North-Western	2,592,000	24
Sabaragamuwa	2,088,000	31
Southern	2,696,000	71
Uva	1,400,000	34
Western	6,219,000	235
Total	22,156,000	567

The pilot data collection phase was conducted from 19th January 2024 to 7th March 2024, accounting for 20% of the data, with the remaining 80% collected from 8th March 2024 to 3rd May 2024.

Demographic Distribution

The average age of the respondents was 40 years, while the age distribution (Figure 3) showed that close to a third of respondents were less than 30 years old, close to half aged 30-54, and close to a fifth aged 55 years or older. This diverse age representation ensures that the survey captured perspectives from both younger and older individuals, providing a well-rounded understanding of tax perceptions across different life stages.

The gender distribution (Figure 3) shows a much higher representation of males of close to two-thirds. While the survey does include enough female respondents to ensure that the survey findings reflect the experiences and perceptions of both genders, future studies may aim for a more balanced gender distribution to further enhance representativeness.

The respondents were also generally well-educated, with 32.71% holding a Bachelor's degree and 23.24% having education above the Master's level. Additionally, 29.56% had completed secondary education or less,

and 14.5% had vocational qualifications. This high level of educational attainment indicates that the respondents had a strong capacity to understand and critically evaluate tax policies and administration.

Provincial Representation

The survey achieved representation from all provinces, with the following distribution: Western Province (41.45%), Southern Province (12.52%), Northern Province (11.64%), Central Province (7.41%), Eastern Province (6.35%), Uva Province (6%), Sabaragamuwa Province (5.47%), North Central Province (4.94%), and North Western Province (4.23%).

Figure 4 shows the provincial distribution of the collected responses as well as the population share of each province based on the mid-year population estimates. The Figure suggests that there is an adequate representation of all provinces though the Western Province and Northern Province tend to be over-represented in the sample. The higher response rates from the Western and Northern Provinces may reflect greater accessibility and engagement in these regions.

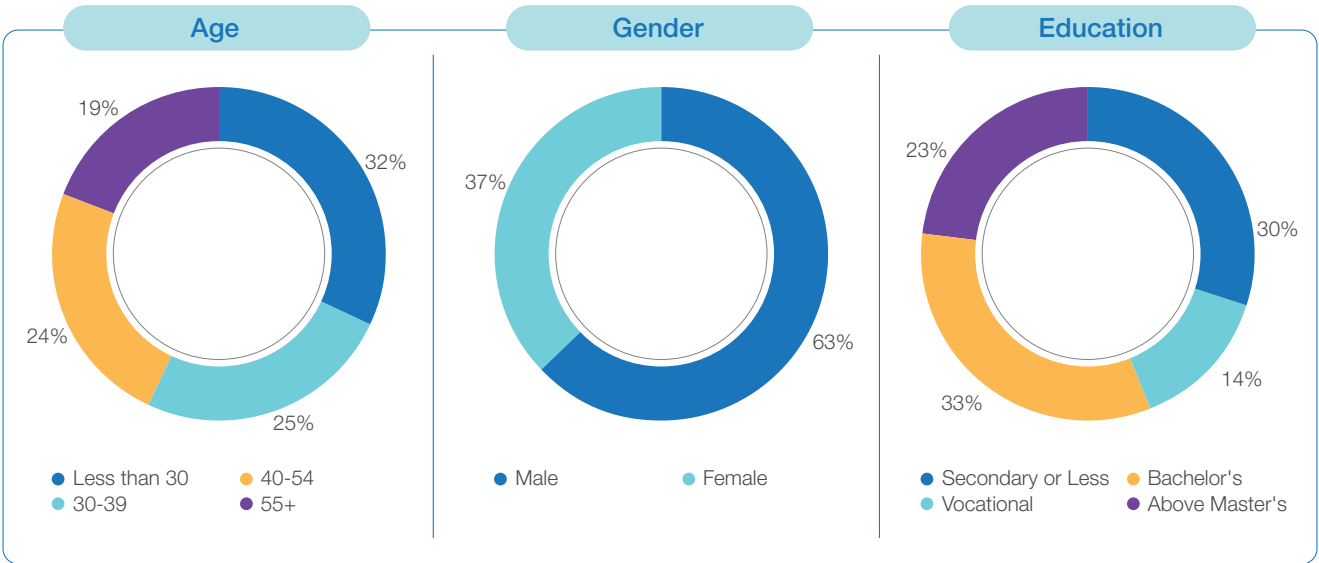


Figure 3: Demographic characteristics

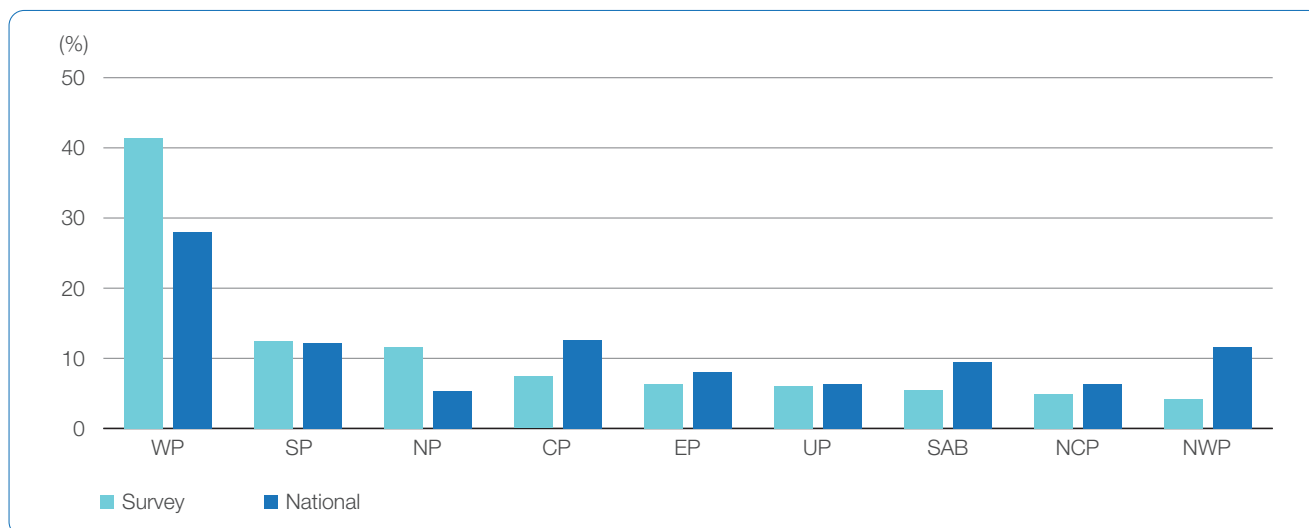


Figure 4: Provincial distribution of the sample

Note: National estimates for mid-year population are taken from Department of Census and Statistics (2024).

Employment profile

The economic background of the respondents provides insights into how employment status and occupational categories influence tax perceptions. A majority (81%) of the respondents were employed, with significant representation from both the private sector (52.65%) and government employment (20.81%). Additionally, 16.35% of employed respondents were self-employed, and 5.1% were employers.

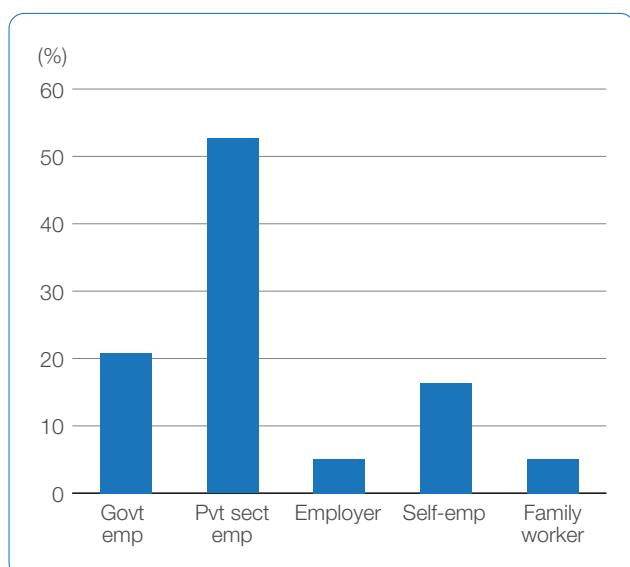


Figure 5: Employment status among employed respondents

The occupational distribution (see Figure 6) showed a substantial representation of professionals (32.08%) and managers (24.78%), with other categories including elementary occupations (15.49%), service and sales workers (9.73%), clerical support workers (5.75%), and technical and associate professionals (4.2%). In terms of sectoral representation, respondents worked across various sectors, with notable participation from manufacturing and industry (32.55%) and health and social work (21.77%). Other sectors included ICT (9.7%), finance (8.84%), education (7.97%), professional, scientific, and technical activities (10.13%), and services (9.05%). The diverse representation across employment status, occupation and sector of employment ensures that the survey captures a broad spectrum of economic activities and their associated tax perceptions.

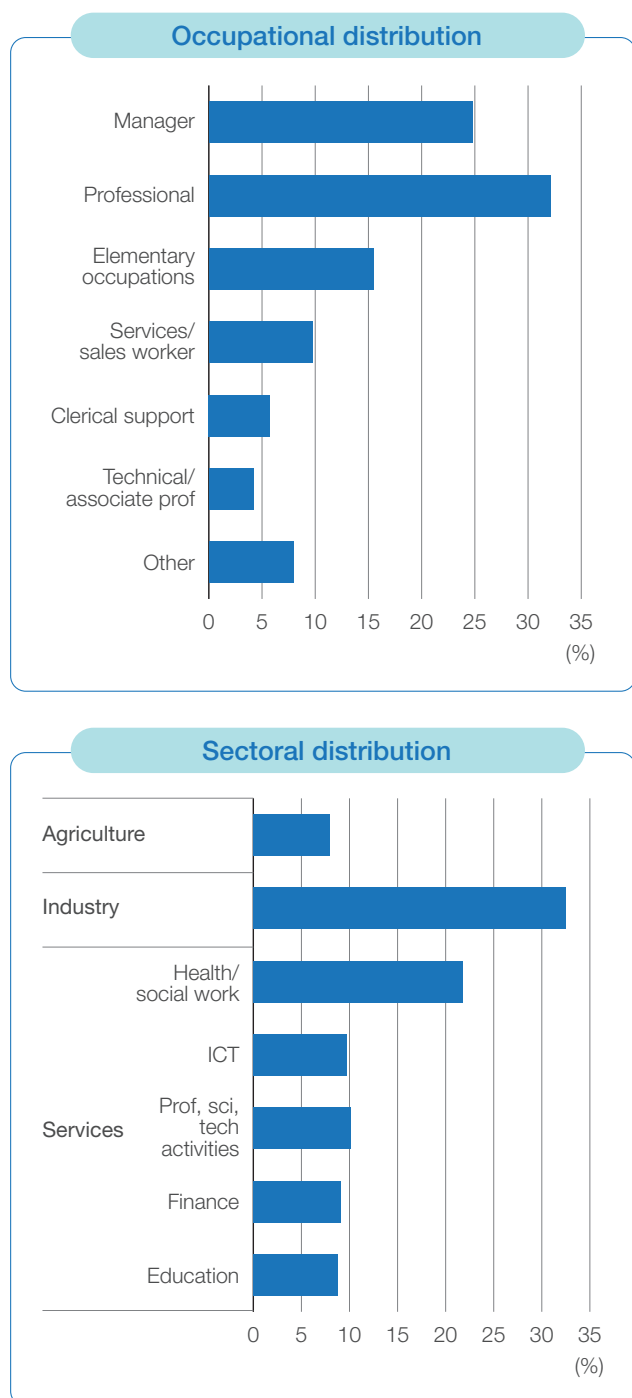


Figure 6: Occupational and sectoral distribution

4. Qualitative Research Component

The qualitative research phase focused on Key Informant Interviews (KIIs) with multiple stakeholders to gather nuanced insights into taxpayer attitudes and behaviours. Enumerators were deployed to cover all provinces for the KIIs, ensuring comprehensive geographic and demographic representation. This phase targeted a diverse range of stakeholders, including:

1. Individuals
2. Small businesses
3. Medium-sized businesses
4. Large businesses
5. Other large taxpayers

Interview Instrument Development: Structured and semi-structured interview guides were developed and pilot-tested for effectiveness. These guides were designed to elicit detailed, context-rich information on taxpayer attitudes, behaviours, and experiences. The semi-structured format allowed for flexibility in the discussion while ensuring that key topics were covered.

Data Collection: KIIs were conducted both online and offline, leveraging the Chamber's extensive network for business categories. The interviews targeted key informants, including tax professionals, government officials, and business leaders, to provide expert insights into the functioning, challenges, and areas for improvement of the tax system. The interviews were conducted in all three languages: Sinhala, Tamil, and English, to ensure inclusivity and comprehensiveness.

Data Analysis: The qualitative data were analyzed through thematic analysis, identifying recurring themes, sentiments, and patterns. The analysis involved developing transcripts of all recorded interviews and discussions, which served as the primary data source. Themes were identified with special attention to topics that aligned with the study's objectives, providing context and explanations for the quantitative findings.

4.1 KII Sample description - background of the respondents

In-depth interviews were carried out with 75 key informants (KIs) to gain a deeper understanding of tax perceptions among influential and knowledgeable individuals in various sectors. The key informants were selected based

on their expertise and roles within their respective sectors and covered all nine provinces of Sri Lanka, ensuring a comprehensive geographical representation.

The average age of the key informants was 44 years, with the majority (69%) being male. Geographically, 60% were from the Western Province, 11% from the Central Province, and 8% from the Southern Province. A significant portion (88%) of the key informants were employed - 70% belonged to higher management or professional strata and represented a diverse range of sectors, including conglomerates (10%), agriculture (4%), manufacturing, construction, and energy (12%), and services (84%), where the last included professionals from the financial, logistics, ICT, hospitality, management consulting, legal and real estate sectors.

5. Ethical Considerations

All research activities adhered to the highest ethical standards, ensuring the confidentiality and anonymity of respondents. Informed consent was obtained from all participants, who were fully apprised of the study's purpose and how the data would be used. Special steps were taken to minimize any potential harm to participants, particularly when dealing with sensitive topics or materials.

6. Limitations

While the National Tax Perception Study – Sri Lanka 2024 provides valuable insights into public perceptions and experiences with the tax system, there are several limitations that need to be addressed to enhance the robustness and comprehensiveness of future studies.

One limitation is the geographic representation; although the study covered all nine provinces, there was an overrepresentation of respondents from the Western Province, accounting for 60% of key informants. This skew may overemphasize issues and perspectives prevalent in this region, potentially underrepresenting the views and experiences of taxpayers from other provinces. To address this, future studies should aim for a more balanced geographic representation by ensuring an equitable distribution of respondents across all provinces. Additionally, efforts should be made to include a broader range of occupational and income groups to capture a more comprehensive understanding of tax perceptions nationwide.

Another limitation is the sectoral bias, with the majority of key informants being from higher management or professional strata, representing 70% of the sample. This may introduce a bias towards the opinions of individuals in higher income brackets and influential positions, potentially overlooking the challenges faced by lower-income and less influential taxpayers. To mitigate this, future studies should increase the sample size and diversity, targeting underrepresented groups such as younger workers, self-employed individuals, and government employees to ensure their views are adequately represented.

The response rate variability across different methods (online and enumerator-assisted) also presents a challenge, potentially affecting the comparability of data. Moreover, the lower TIN coverage among younger workers, self-employed individuals, and government employees may lead to underrepresentation of these groups' tax perceptions and experiences. Enhancing data collection methods to increase response rates and ensure consistency across different survey methods will improve the reliability of the findings. Comprehensive training for enumerators and leveraging technology for data collection can enhance accuracy and reach.

Additionally, while the KIs provided rich qualitative data, the relatively small sample size of 75 key informants may not capture the full diversity of opinions and experiences within each sector. However, the size of the sample should not undermine the transferability of insights gained from the KIs to other profiles, situations and times. Expanding the mixed-method approach by incorporating more in-depth qualitative research, such as focus groups and case studies, can provide richer contextual data and explore the nuances of tax perceptions and experiences more thoroughly.

Lastly, establishing a continuous feedback mechanism from respondents can help identify emerging issues and trends over time. Regularly updating the survey instruments based on feedback will ensure that the study remains relevant and responsive to changing taxpayer concerns and conditions. By addressing these limitations, future studies can provide an even more detailed and accurate picture of tax perceptions in Sri Lanka, thereby supporting more effective and equitable tax policy development.

FINDINGS AND ANALYSIS

This section presents the findings from the analysis of data from the Tax Perception survey and the key informant interviews. The results are presented under the following themes: knowledge of tax concepts, perceptions about the Sri Lankan tax system, perceptions on tax revenue utilization in Sri Lanka, trust in tax-related institutions and perceptions about

services offered by the Inland Revenue Department. The results of the survey are complemented with more detailed insights from the KIs. As mentioned previously, the results of the survey are disaggregated by TIN holder status (as justified in Box 1 and subsequent sections) as the experiences of the two groups in terms of interactions with the tax system vary substantially.

Box 1: Availability of Taxpayer Identification Numbers (TIN)

As part of the drive for increased tax compliance, the amended Inland Revenue Act specifies that all individuals aged 18 years or above are required to register with the Inland Revenue Department and obtain a unique Tax Identification Number (TIN). This was enforced from the 1st of January 2024 with individuals able to apply for the TIN online, by post or by visiting the IRD, with the only documentation required being a copy of the national identify card.

At the time of data collection, it was found that only 35% of respondents had or had applied for a TIN (all respondents were aged 18 or above). Lower TIN coverage was observed among younger workers, self-employed individuals, and government employees. This is potentially due to the majority of TIN holders being those who are currently paying direct taxes (89% reported paying taxes), with those who are not eligible to pay taxes or whose taxes are deducted at source as Pay-As-You-Earn (PAYE) tax currently being unregistered. For instance, 17% of those without a TIN also reported paying direct taxes, consistent with this explanation.

Closer examination of the type of respondent who was more likely to have the TIN showed that TIN coverage was higher among employers and private sector employees and older respondents (Figure 7). For instance, around two-third of the 55+ age group reported having a TIN, whereas just 18% of those below 30 years reported the same. Interestingly, the TIN coverage was quite low among government employees, again possibly because many of them were either below the tax threshold or because they are subject to PAYE taxes which are deducted at source.

The strong correlation between having a TIN and filing for and paying direct taxes suggests that knowledge about the Sri Lankan tax system and experiences of interacting with the IRD are likely to be significantly different between those with and without a TIN.

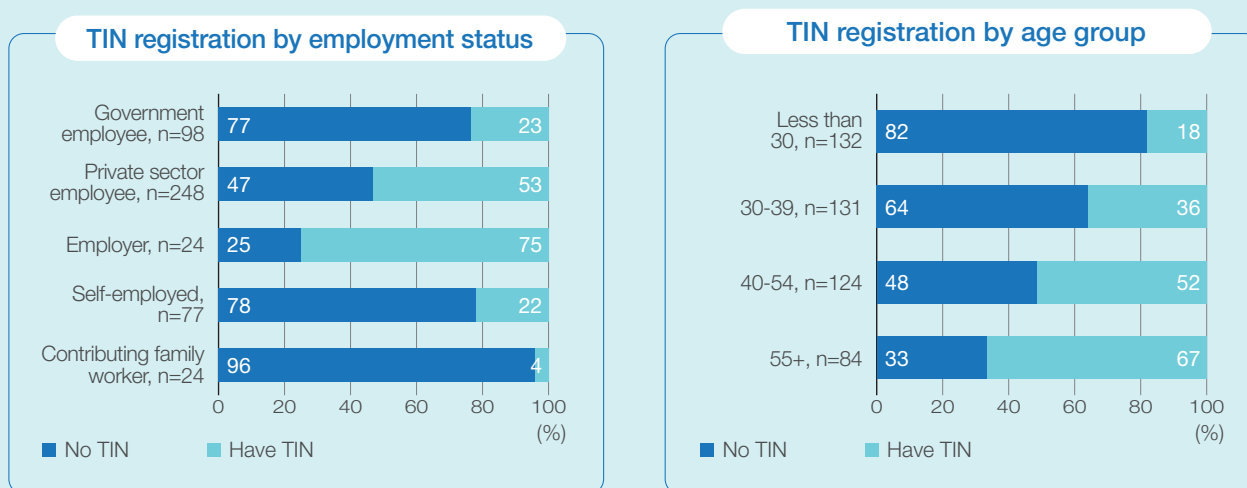


Figure 7: TIN registration by employment status and by age group

Respondents who did not have a TIN were questioned on their intention to obtain one. The data suggests that the intention to obtain a TIN was moderately high, with 46.72% of respondents who did not already have one considering it and another 11.48% intending to get it soon. This indicates a positive trend towards formal tax compliance, possibly supported by recent government initiatives to streamline the tax registration process. However, 42% of unregistered respondents still indicated that they did not intend to get a TIN (regardless of it being mandatory), highlighting that further efforts to increase awareness on this requirement and process are required.

1. Knowledge of tax concepts

Tax is an integral part of the social contract between the government and citizens of a country, whereby through paying taxes, citizens are empowered to hold their governments accountable for how their money is spent. However, while lower-income households tend to be more heavily taxed as a share of their income because of indirect taxes on consumption (which compose most of the tax revenue in Sri Lanka), the sense of tax ownership tends to be stronger when personal income or wealth is directly taxed. Accordingly, it is posited that those paying value-added and similar indirect taxes tend to be less aware, weakening their role in enforcing the social contract (International Monetary Fund, 2022). Apart from the social contract perspective, citizens' understanding of tax concepts and laws has manifold additional implications on individual decisions including how much to work, whether or how much to borrow and save, their tax compliance and voting choices (Lyon and Catlin, 2020).

As such, the first part of the survey aimed to assess the respondents' familiarity with tax concepts such as the purpose of tax collection, familiarity with the concept of direct and indirect taxes and perceptions about their fairness. These responses provide a basis

to interpret the remaining results as basic knowledge of taxes and the social contract would have an obvious impact on perceptions about taxation in Sri Lanka and the roles and responsibilities of the institutions involved in taxation.

Familiarity with Direct and Indirect Tax Concepts

The survey data revealed a significant variation in familiarity with tax concepts among respondents. The analysis showed that respondents with a Taxpayer Identification Number (TIN) demonstrated greater familiarity with tax concepts compared to those without a TIN. Specifically, 22.34% of TIN holders reported being "very familiar" with tax concepts, and 51.27% reported being "familiar." In contrast, a higher percentage of respondents without a TIN were "unfamiliar" (32.79%) or "very unfamiliar" (13.93%) with tax concepts. This indicates that formal registration and engagement with the tax system likely enhance taxpayers' understanding of tax concepts, which is crucial for informed participation in the tax system. Given that most TIN holders are those who are paying direct taxes, their greater familiarity and knowledge of tax related concepts is consistent with the theory of tax and the social contract.

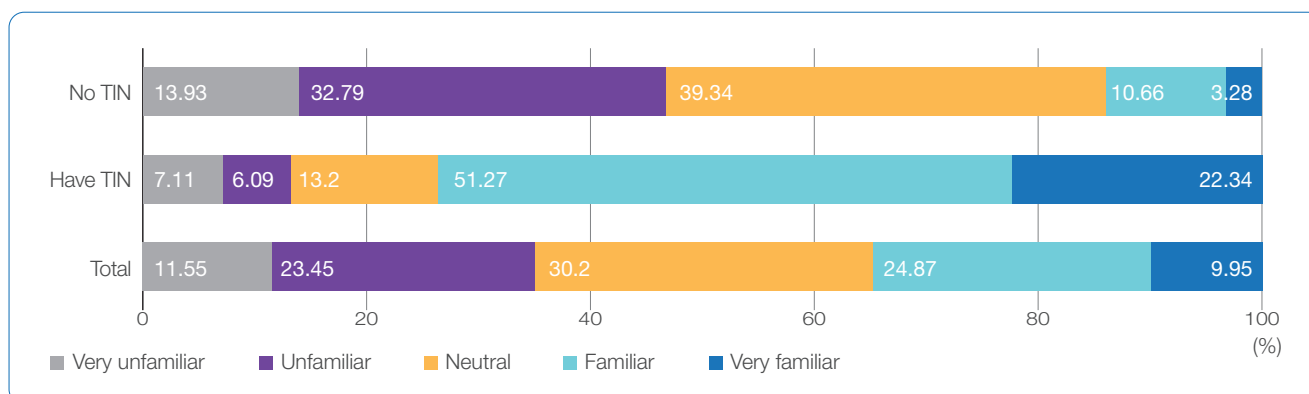


Figure 8: Familiarity with tax concepts

Perceived Fairness of Direct and Indirect Taxes

The perceived fairness of direct and indirect taxes would be influenced by both the respondents' knowledge of tax related concepts (direct taxes are equitable and indirect taxes inequitable by nature) as well as their perception of how the government uses tax revenue – if it is perceived that the government is misusing tax revenue, it is more likely that citizens consider the paying of taxes to be unfair or unnecessary (Castaneda, 2024).

When evaluating the perceived fairness of direct and indirect taxes (Figure 9), the results showed a notable difference between respondents with and without a TIN. Among TIN holders, there was a much lower tendency to provide a neutral response: 19.1% compared to 45% among non-TIN holders. Interestingly, similar shares of TIN holders found direct taxes to be fair (36%) and unfair (26), while among those without a TIN, a much larger proportion of respondents found direct taxes to be “unfair” (36%). The higher likelihood for TIN holders to consider direct taxes to be fair than the non-TIN holders is potentially linked to the higher tax literacy among TIN holders – despite being more likely to be paying direct taxes, these respondents were also more aware about the equity aspects of different tax types. However, the sizeable share of TIN holders who consider direct taxes to be unfair could potentially be due to the respondents' experiences with the recent tax reforms in the country (even though these questions were referring to the concepts in general and not to the Sri Lankan context specifically) - increased tax rates and lower tax thresholds imposed from 2023 or the lack of tax morale on tax revenue utilization may colour perceptions about the taxes themselves.

Regarding indirect taxes, 16.08% of TIN holders perceived them as “very unfair,” and 41.71% found them “unfair”, while 19% considered them to be fair or very fair. Among respondents without a TIN, 44% viewed indirect taxes as unfair or very unfair, though 35.52% remained neutral. These results are more in line with theoretically inequitable nature of indirect taxes as well as the increases to VAT and other indirect taxes enacted as part of the recent tax reforms.

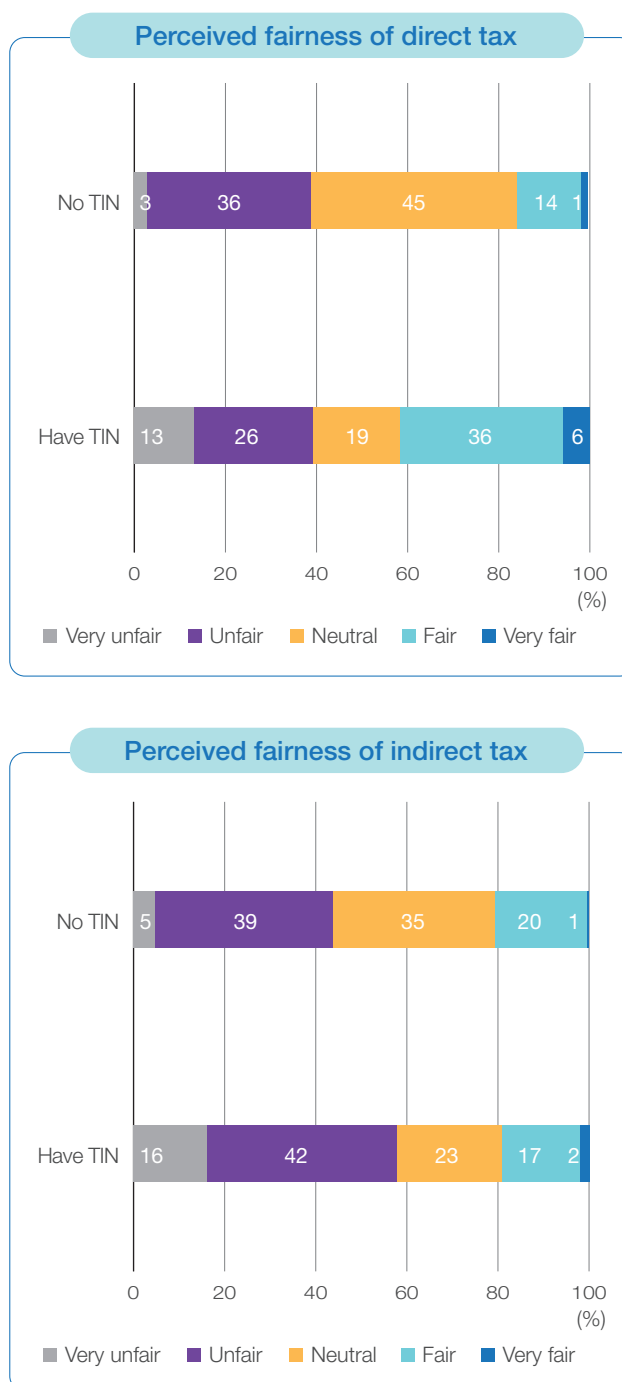


Figure 9: Perceived fairness of direct tax and indirect tax

Taken together, these findings suggest that direct taxes are generally perceived as more equitable than indirect taxes (although less than half of the respondents viewed direct taxes as fair). Given the prevailing tax mix in the country, where there is a heavy reliance on indirect tax revenue, policymakers should consider these perceptions when designing tax policies to ensure greater acceptance and fairness of the tax system.

Perceptions on the Purpose of Tax Collection

The survey explored respondents’ perceptions of the primary purpose of tax collection. A majority of respondents (64%) identified funding public services as

the main reason for collecting taxes (Figure 10). This perception was slightly higher among TIN holders, with 80.4% recognizing public service funding as the primary purpose. Improving equity was the second most cited reason, with 36.2% of respondents acknowledging it as a purpose of tax collection. These results highlight the importance of emphasizing the public benefits derived from tax revenues in terms of public service delivery as well as reduced social inequality to enhance compliance and support. Notably, 17% of respondents indicated they “don’t know” the purpose of tax collection highlighting the need for enhanced communication and education efforts to improve public understanding of the role of taxes in national development.

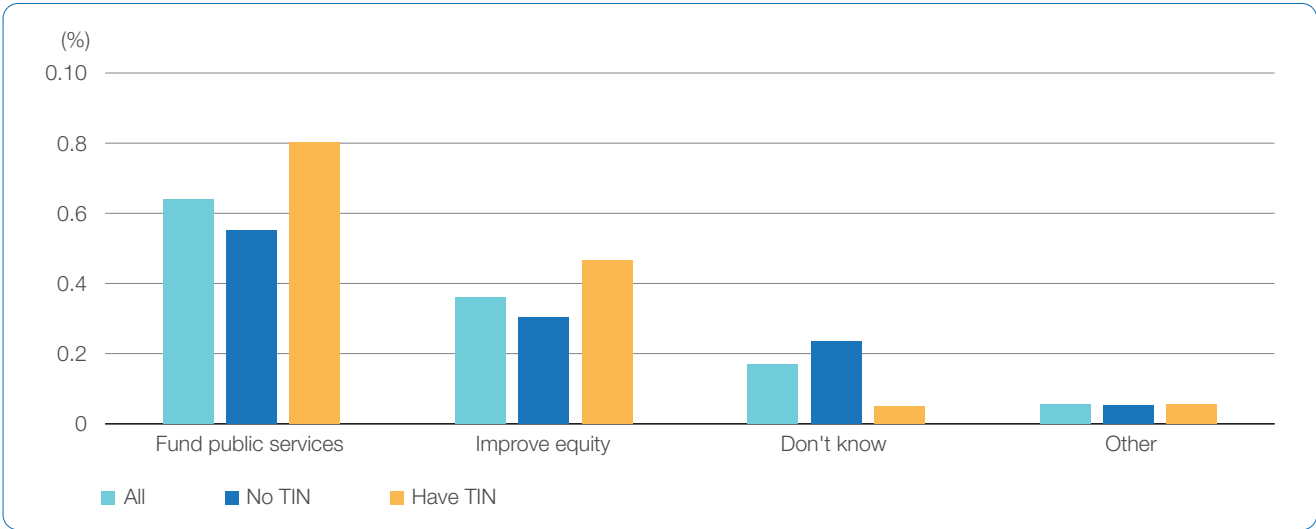


Figure 10: Perceived purpose of tax collection

2. Perceptions about the Sri Lankan tax system

Having obtained the respondents’ perceptions about taxes in general, the next part of the survey focuses on their self-assessed knowledge and perceptions about the Sri Lankan tax system and the reforms that were enacted since January 2023.

Knowledge of Sri Lankan Tax System

Just over 20% of respondents reported having a good and very good knowledge of the tax system, with a significantly higher percentage among TIN holders. Specifically, 30.3% of TIN holders rated their

knowledge as “good,” compared to only 1.65% of non-TIN holders. This discrepancy highlights the impact of formal engagement with the tax system on taxpayers’ understanding, as well as the broader implications for the social contract between the state and its citizens. On the other hand, a substantial portion of respondents without a TIN rated their knowledge as “poor” (25.07%) or “very poor” (3.6%), indicating a need for enhanced tax education and awareness initiatives.

On a related note, the complexity of the tax system was a common concern among respondents, with more than half perceiving it as complex (Figure 11). Among TIN holders, 71% described the tax system as complex or

very complex. This perception was slightly lower among non-TIN holders, with 41.58% considering the tax system complex. This shows that those who have in fact engaged with the system were more likely to consider it as more complex. The perceived complexity can deter compliance and highlight the need for simplification of tax procedures and better communication to improve understanding and engagement.

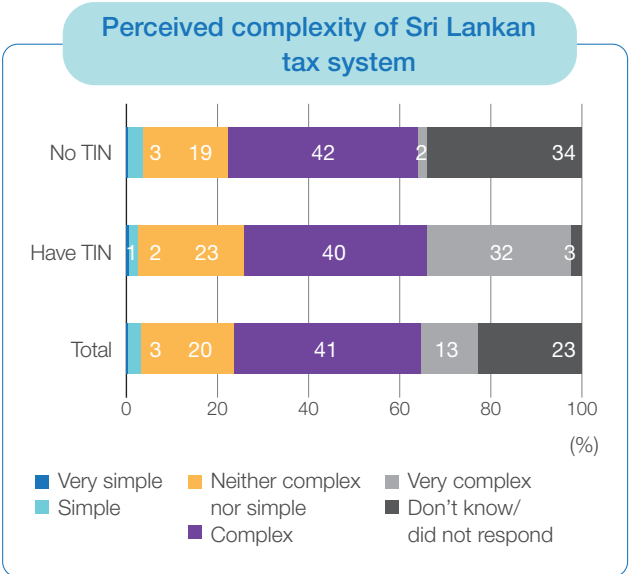
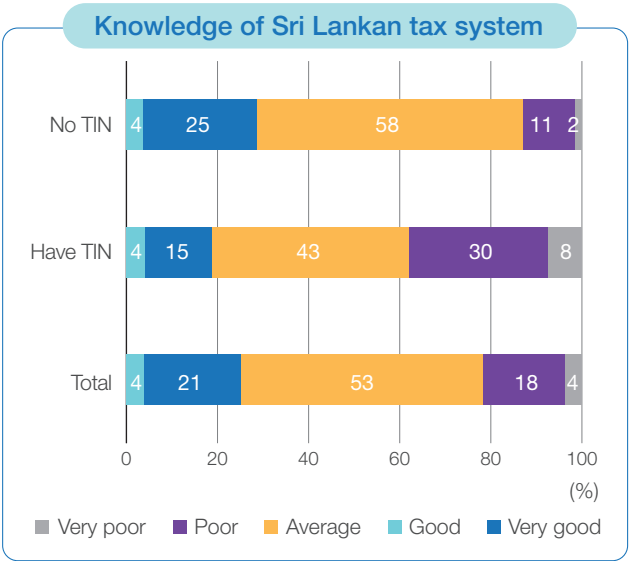


Figure 11: Knowledge and perceived complexity of Sri Lankan tax system

Insights from KIs: Many key informants felt that improving tax literacy among the population using awareness sessions via news and social media and incorporating tax education into the education system from a younger age, could be useful for improving tax morale and tax compliance. For instance, one interviewee provided the following response to the question of how the government could bolster tax morale, encourage compliance and foster a stronger social contract among the public:

“People should be educated on taxation. Educating individuals, particularly younger generations, about tax filing through school curricula would be beneficial. Presently, there are no knowledge sessions or dedicated chapters in school curricula regarding tax education. However, integrating this education into schools is crucial. In my opinion, this should commence around year 6, as children at this age begin actively seeking information. Starting at this point has the added advantage of involving not just children but also their parents, who are typically engaged in their education until year nine.

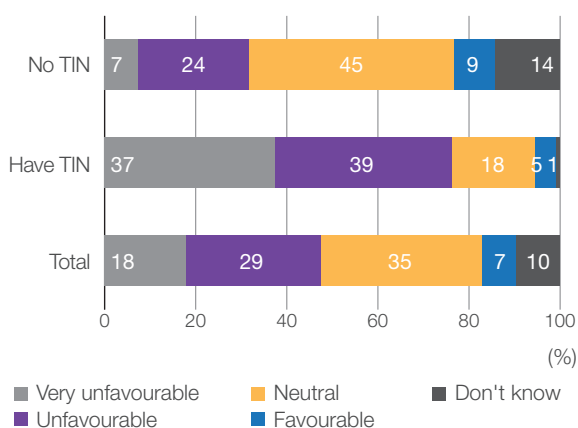
Creating a mindset and imparting knowledge are essential steps in promoting tax compliance and facilitating technological adaptation. Government initiatives, including TV programs and dedicated sessions, can play a vital role in educating the public about tax matters.”

Perceptions about the tax policy reforms since 2023

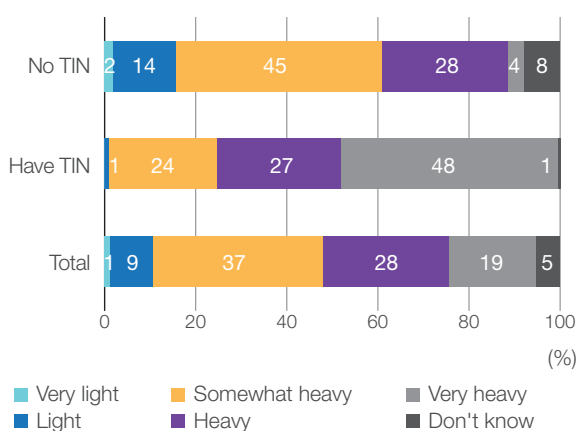
Close to half of the respondents, particularly those with TINs, expressed unfavourable perceptions about the new tax policy introduced in 2023 (Figure 12). Specifically, 37.37% of TIN holders rated the new tax policy as “very unfavourable,” and 38.89% as “unfavourable.” In contrast, a smaller proportion of non-TIN holders (7.38%) found the new tax policy “very unfavourable.” TIN holders were subsequently more likely to perceive the tax burden as heavy or very heavy (75% vs 31% among those without the TIN) and the prevailing tax rates to be unreasonable (80% vs 35%).

This suggests that those who are more likely to be paying direct taxes are feeling more of the burden as a result of the significant changes to the income tax. However, when questioned specifically on indirect taxes, it appears that close to 50% of respondents now consider indirect taxes (moderately or more frequently) when making purchasing decisions while 2/3 believe that the brunt of indirect taxes is passed completely to the consumer.

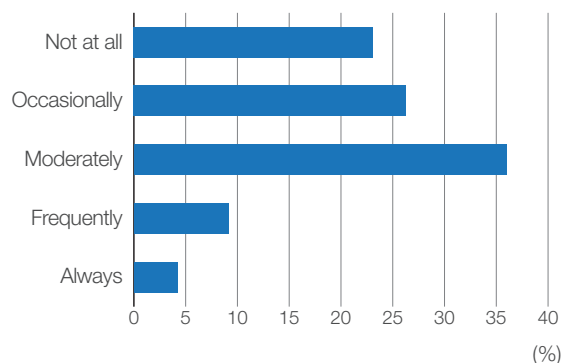
Perceptions of new tax policy



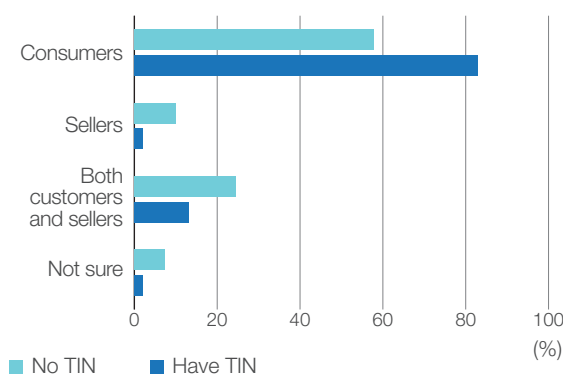
Perceived tax burden



Consideration about indirect taxes when making purchasing decisions



Burden of higher indirect taxes



Perceptions about prevailing tax rates

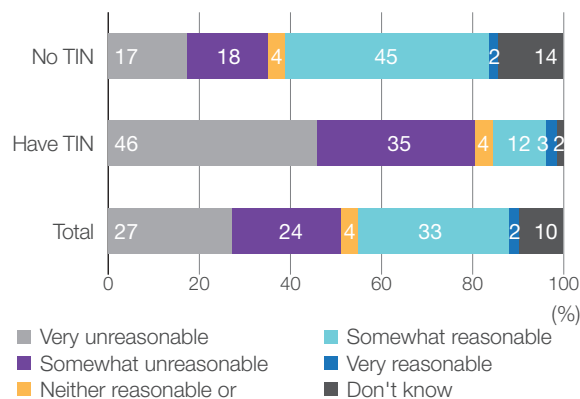


Figure 12: Perceived tax burden

The heightened sense of a heavy tax burden and unreasonable tax rates are unsurprising given the context in which the reforms were enacted. Following the economic crisis that the country plunged into in 2022, the government enacted many changes to fiscal policy directed towards fiscal consolidation. For instance, income tax policy was revised with a reduction in the taxable income threshold from LKR 3 million per annum in 2022 to LKR 1.2 million and an increase of rates from 6-18% to 6-36%. Together with the reintroduction of PAYE tax, this resulted in many more citizens becoming eligible for taxes as well as paying much more in terms of taxes. During the same period, VAT was increased to 12% and 15% during 2022 and finally to 18% by January 2024. Reforms to the pricing of fuel, electricity and water, also led to significant price hikes that had ripple effects on the pricing of other goods and services.

These significant changes to the individuals' purchasing power colour perceptions about the tax burden and how reasonable the tax rates are. Balancing tax rates with the taxpayers' ability to pay and ensuring that relief measures effectively address fairness concerns are essential steps in fostering trust and compliance and strengthening the social contract between government and the public.

Micro, small, and medium-sized enterprises (MSMEs) in Sri Lanka have faced significant challenges due to these tax increases. According to an ILO study conducted in late 2023 titled 'Impact of multiple crises on Sri Lanka's micro, small and medium-sized enterprises', the financial strain from these tax hikes has made it nearly impossible for many MSMEs to maintain their operations, leading to severe disruptions in business continuity. The increased tax burden has compounded the effects of other crises, causing businesses to downsize, lay off employees, or even shut down entirely. This situation highlights the urgent need for supportive policies to help these enterprises navigate these challenging times and ensure their survival and growth.

Insights from KIs: nearly all of the KIs who were speaking from a business perspective reported negative impacts of the policy changes on their businesses, even while acknowledging the need to boost tax revenues. The following response was provided by a KI working in the financial sector:

***"The tax policy should factor in the cost-of-living escalation when it is being designed. What is currently being done is that the tax brackets have been reduced significantly and increased the tax percentage. This was done when there was inflation of more than 60% and the cost of living over the past few years have increased by more than 2 or 3 fold. So people are affected by both the ends, as income after tax has reduced and the expenses have significantly increased. There should be some fairness in terms of setting these limits and rates."** - Financial sector*

Respondents cited reduction in disposable income of clients dampening economic activity, creation of an informal sector/grey market due to the high tax rates resulting in unfair competition.

***"Every citizen bears a responsibility to address Sri Lanka's national debt. Increasing taxes seems logical, but doing so without addressing existing leaks in the system would only exacerbate corruption. Prioritizing the sealing of these leaks before implementing tax collection mechanisms is essential. While both efforts must run concurrently, perhaps 60% of our efforts should be directed towards plugging existing loopholes. This approach is vital in preventing further leakage caused by various factors."** - Agriculture*

Different taxes were mentioned by different sectors: for instance, vehicle importers were most concerned about VAT and import duties whereas those working in the financial sector were more concerned about taxes on income and interest. It was indicated that some of the tax policy changes were done without a good enough understanding of the sector-specific features, resulting in a lack of effectiveness. The excerpt below frames concerns flagged by a respondent working in the vehicle import sector.

“In the automotive industry, tax rates are disproportionate, affecting lower-income customers at a much higher percentage compared to higher-income customers. For instance, taxation is not based on the value of the vehicle but rather on the size of the engine. For instance, a 1000 CC vehicle incurs the same tax value as a Rolls Royce. This discrepancy highlights a significant gap and a substantial potential for revenue generation for the government.

With the addition of an 18% VAT on each trade of a used vehicle through a legitimate business, the true value is obscured. For instance, a Rs. 10 million car incurs an additional Rs. 1.8 million with each trade. Subsequently, with each subsequent trade, another 18% is added, resulting in a loss of the true value.

Those conducting transactions in cash or outside the system remain unaffected. Consequently, the entire used vehicle industry has transitioned off the books and into the black market. This shift means that tax collections from legitimate businesses are lost, resulting in both corporations and the government experiencing a loss in tax revenue.”

However, when asked to compare the tax burden and incentives in Sri Lanka with other countries or regions in which their business operates, the responses were mixed. Some respondents reported that Sri Lanka’s tax rates were relatively lower than in other countries but that in other countries there is more accountability for how those tax revenues are generated. Others felt that the taxes in Sri Lanka were too high or that even with a similar tax burden, given the lack of ease of doing business, Sri Lanka would not be able to compete internationally. When questioned on whether the current tax system was influencing Sri Lanka businesses to relocate to other countries, a majority answered in the affirmative, maintaining that the tax burden together with policy inconsistency and other restrictions to doing business were pushing more businesses to move their operations overseas as well as more professionals to migrate.

Perceived fairness of the Sri Lankan tax system

Following on from the perceptions about the tax burden, more than 40% of respondents felt that the tax administration in Sri Lanka was not fair (Figure 13). This sentiment was much stronger among TIN holders, with 82%, compared to below 20% among those without a TIN. To further understand these perceptions, the study covered the topics of tax concessions and the issue of tax evasion.

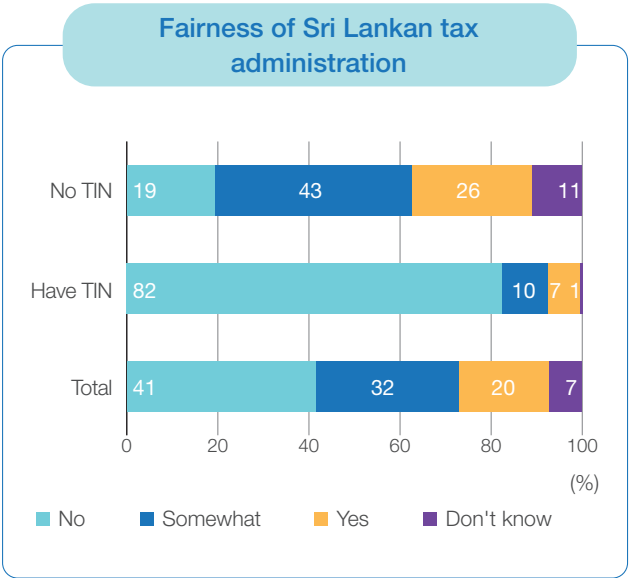


Figure 13: Perceived fairness of Sri Lankan tax administration

Reliefs and Exemptions

The Sri Lankan tax system offers tax exemptions, reliefs and incentives in both the direct and indirect tax categories. These include tax holidays, low and differential rates of tax, increased tax-free allowances, etc. These concessions are primarily made on the basis of ensuring fairness (e.g. exemptions for essential food items for certain indirect taxes) and encouraging domestic businesses and foreign investment. However, the empirical justification for these tax policy tools is weak, given that many of these benefits are enjoyed by larger enterprises or that the promised economic benefits arising from these concessions have failed to materialise (Kelegama, 2017).

Despite the intended goals, tax exemptions and reliefs potentially benefit larger enterprises and high-net-worth individuals. These exemptions include luxury tax exemptions on imported electric vehicles, often granted to individuals purchasing high-value vehicles, indicating a preference for higher-income brackets. Additionally, significant tax reliefs are offered to companies through Board of Investment (BOI) tax certificates across various sectors, including utilities, manufacturing, apparel, and infrastructure. Many projects and companies also received tax exemptions through the Strategic Development Project (SDP) Act - through its discretionary tax breaks, which is now put on halt so that the Government of Sri Lanka can look into introducing transparent, rules-based eligibility criteria for granting time-bound incentives.

The financial impact of these tax concessions has been significant. For the fiscal year 2022/23 (April to March), tax concessions resulted in a total of LKR 978 billion in foregone revenue, which amounts to 56% of the total tax revenue collected by the government in 2022. This substantial loss in revenue underscores the need for careful evaluation and reform of the current tax exemption policies to ensure that they achieve their intended objectives. This information was reported in the “Tax Expenditure Statement” published by the Ministry of Finance of Sri Lanka on March 31, 2024 ²

In the survey, more than half of the respondents felt that prevailing tax reliefs and exemptions ensured fairness only to a small extent or not at all (Figure 14). Among TIN holders, 50.25% believed that reliefs and exemptions ensure fairness only to a small extent, while 14.71% felt they did not ensure fairness at all. This suggests that current relief measures may be insufficient in addressing taxpayers’ concerns about fairness and equity in the tax system.

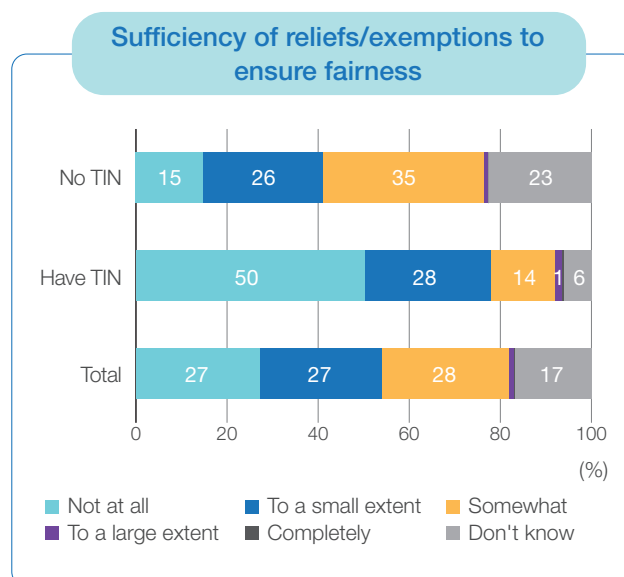


Figure 14: Perceptions about fairness of tax reliefs and exemptions

Insights from KIIs: While the survey did not allow the identification of whether individual respondents belonged to sectors that benefited from tax concessions, the KIIs provided more depth on this topic. Among the interviewees, there was a general perception that while incentives could be used beneficially but many respondents were not positive about the current tax incentives reporting that many of the tax reliefs and exemptions are currently awarded based on political clout and favouritism and that there was a lack of transparency in this process.

“The sectors that should be given concessions have not been identified exactly. It appears that it has been implemented only according to the needs of a few people.” - Agriculture

“From an export perspective, the current situation is far from ideal as it lacks any substantial incentives for exporters. Our longstanding contention has been that to encourage companies to venture into exports, there must be tangible incentives in place. Regrettably, existing policies fail to provide such incentives to exporters.” - Apparel

² <https://www.treasury.gov.lk/news/article/257>

It was suggested that the cost-benefit analyses be conducted prior to granting these incentives and that the impacts of providing these exemptions (e.g. through increased job creation or foreign exchange generated) should be actively monitored and reported, given the substantial tax expenditures generated by these reliefs.

Tax Evasion

Tax evasion has long been a cause of concern in the Sri Lankan context. While its immediate consequence is the loss of revenue, it distorts the objectives of a fair tax system. Tax evasion was identified as a significant issue among the survey respondents, with 75% of respondents perceiving it as a significant or very significant problem (Figure 15). TIN holders were much more likely to do so with 59.8% identifying it as a “very significant” issue.

Perceived reasons for tax evasion included high tax rates, complex tax systems, misuse of revenue by the government, lack of transparency, and weak enforcement (Figure 16). While TIN holders most likely to select options related to accountability and transparency in tax revenue utilization, they were also more likely than non-TIN holders to cite weakness in the tax collection system (e.g. lack of trust in tax collectors or weak enforcement), potentially due to their greater familiarity with the system. Non-TIN holders, on the other hand, were most likely to select high tax rates as a reason behind tax evasion in Sri Lanka.

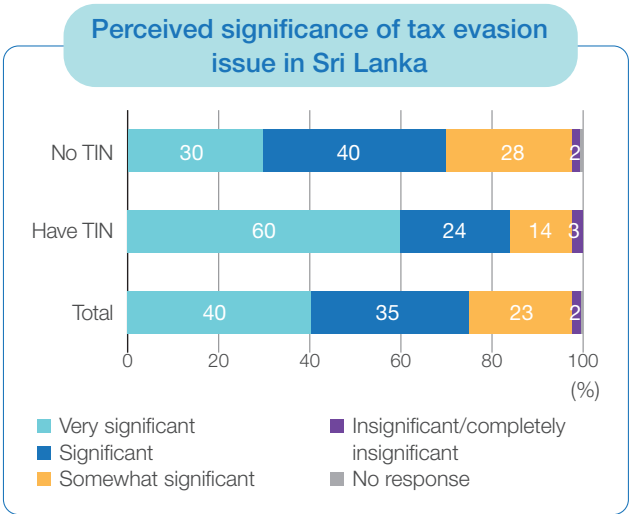


Figure 15: Perceived significance of tax evasion in Sri Lanka

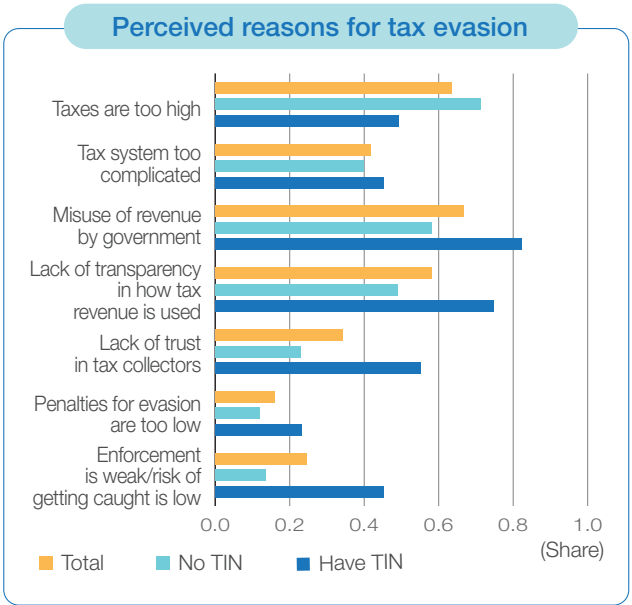


Figure 16: Perceived reasons for tax evasion in Sri Lanka

Insights from KILs: these findings from the survey were echoed in the KILs, where among the taxpayers’ (e.g. formal sector businesses and individuals) responses there was a sense of grievance about registered taxpayers having to pay ever more tax and only limited efforts to widen the tax net. Some responses to the question of what respondents thought about the fairness of tax laws and regulations introduced as a result of the crisis include:

- “Placed an over emphasis on formal sector companies and individuals for tax collection with many leakages in the informal sector not properly analyzed and targeted”
- “Unfairly designed to make existing taxpayers businesses uncompetitive”
- “It’s not fair as there is there is more potential invisible taxpayers outside the tax base and the same visible taxpayers have to bear the burden of the increased tax rates.”
- “Companies in the financial sector are very compliant and it is not something that can be run behind closed doors. Therefore the authorities identify it as an easily taxable area and keep increasing tax rates and introducing more tax. This threatens the business models.”

“Avoiding taxes might seem like a way to dodge complicated rules. Sometimes, people delay paying taxes because the process is confusing. Even big companies can struggle with taxes, facing long negotiations or legal battles...While everyone agrees on the importance of taxes, some may disagree with specific rules. However, rather than dodging taxes, it’s better to improve the system for everyone’s benefit.”

Several respondents cited the high tax rates as encouraging informality and a grey market and deterring potential taxpayers from paying their dues, while others felt that the current penalties for evasion were not large enough.

“The penalties for not paying taxes are currently inadequate. This creates a situation where individuals or organizations may deliberately choose to default on their taxes, knowing that even if caught, the penalties are relatively minor. This issue is particularly concerning for large-scale organizations capable of perpetrating significant frauds. Whether intentional or unintentional, negligence shouldn’t be excused by lenient penalties.”

Another factor highlighted in the KIs as driving up the cost of compliance are the administrative costs involved in complying with current tax regulations. Reasons for high administrative costs include: costly litigation with the IRD, difficulties in processing refunds, having to obtain tax advisory services or spend large amounts of time due to complex and burdensome administrative procedures and formalities.

“Navigating compliance challenges and obligations can be particularly daunting for companies in the construction sector, especially smaller and medium-sized enterprises. While larger corporations may have the resources and expertise to handle tax compliance effectively, many smaller firms struggle due to a lack of knowledge and resources....

Overall, while businesses in the construction sector are willing to comply with tax obligations, the lack of resources, expertise, and consistency in regulatory requirements make it extremely challenging for them to do so effectively.” - Construction

While the government has currently made efforts to widen the tax net, these results highlight the urgent need for further measures to minimize the tax evasion issue not just for revenue generation purposes but also to ensure that current taxpayers do not get demoralized and lose tax morale. These measures span from identification of potential taxpayers to creating a tax ecosystem that is more conducive to compliance (e.g. through more moderate rates or simplification of procedures). Additional suggestions for tackling the issue of tax evasion provided by respondents are discussed in subsequent sections.

3. Tax revenue utilization

Taxation provides governments with the resources to promote the collective will of their constituents (Dagan, 2024). Accordingly, tax revenue utilization forms the opposite end of the social contract: citizens hold up their obligation by paying tax while the government should do by utilizing tax revenues in an accountable and responsible manner. While the previous section covers citizens’ perspectives on tax payment, this section focuses on perspectives on the government’s usage of tax revenues.

Transparency of Budgeting and Policy Formulation

According to the 2008 UNDP study titled “Tackling Corruption, Transforming Lives: Accelerating Human Development in Asia and the Pacific,” corruption significantly shapes people’s perceptions and undermines trust in governance. The study highlights how pervasive corruption distorts public institutions, erodes trust in governmental and fiscal policies, and creates widespread disillusionment, particularly among the poor who suffer most from reduced access to essential services. This erosion of trust fuels perceptions of inefficiency and injustice, further diminishing public confidence in government actions and initiatives.

Transparency in budgeting and policy formulation was perceived to be low among respondents (Figure 17). A substantial 47.95% of respondents felt that transparency was lacking, with TIN holders again expressing stronger dissatisfaction (53%) compared to non-TIN holders (45%). There were no respondents reporting that they consider the process to be “very transparent”. This perception of low transparency could

undermine trust in the government's fiscal policies and encourage tax evasion (as seen in the preceding section), highlighting the need for more open and participatory budgetary processes. It also suggests that the public consultation process for the national budget and other policies is poorly implemented resulting in poor public engagement between the state and the public (UNICEF, 2019).

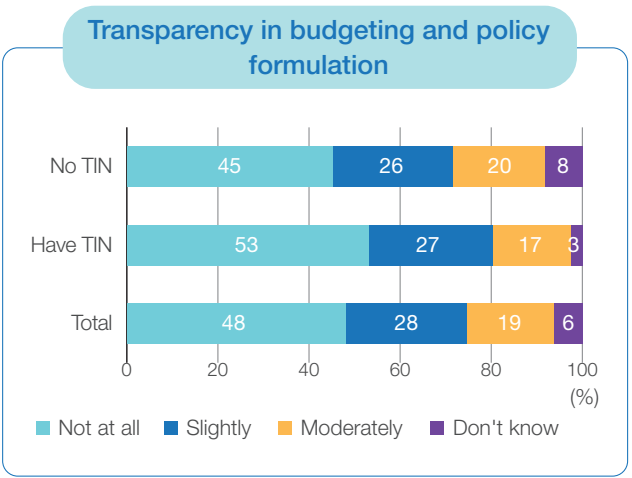


Figure 17: Perceptions about transparency in budgeting and policy formulation

Insights from KIs: one of main concerns related to the Sri Lankan tax system was the lack of transparency and accountability in the utilization of tax revenue. While absence of reliable data, vested interests and political lobbying influencing decision making were cited as factors hindering transparency, better reporting of tax revenue collection and their usage and minimizing wasteful expenses were commonly reported as means of improving tax morale.

KIs were also asked to comment on any experiences of actively participating in discussions related to tax policies with the government. While a few KIs reported positive experiences of their suggestions being considered (e.g. respondents working in think tanks or in conglomerates), there were others who felt that the policy discussions take place too late or that their concerns were not given due consideration (e.g. respondents in manufacturing, finance sectors). There was also a perception that the tax officials tended to be receptive to reasonable proposals but that this did not translate to higher levels of decision making.

“Tax proposals were given through the Ceylon Chamber, CIMA and CFA usually around budget time, almost every year. But there has been very little engagement with the MoF or the IRD. Engaged in conversations with the Secretary of the Treasury, but nothing happens after.” - Finance sector

“In terms of tax policy, our involvement typically occurs after the fact. We find ourselves reacting to policies once they’ve already been implemented, rather than being involved in their development from the outset. While we understand it’s impractical to consult everyone before every decision, there needs to be a more structured process in place... Overall, our trustworthiness isn’t in question; rather, it’s the timing and nature of our involvement in the policymaking process that need improvement.” - Apparel

“Officials are willing to listen and engage but unfortunately they may not have the authority to make decisions” - Thinktank

There was a common perception among the KIs that since parliament is a representation of the people, citizens do not need to be directly involved or that those who are involved should have an adequate understanding of taxation. However, several raised the point that the citizenry must be kept informed on policy decisions in a transparent and consistent manner.

“Tax policy should be in line with the industrial policy, which is aligned to the country’s growth objectives and strategies. The citizens can vote for it. Citizens can’t be deciding on the tax policy. All would prefer zero (taxes).” – Finance

Perceptions on Budget 2024

The survey examined respondents’ perceptions of the national budget, particularly the 2024 budget. Nearly half of the respondents felt that the Budget 2024 did not adequately address the needs of the country (Figure 18). Specifically, 49.29% of all respondents expressed this sentiment, with TIN holders (67.84%) showing a higher level of dissatisfaction compared to non-TIN holders (39.06%). This indicates a significant perception among taxpayers that the budgetary allocations and priorities may not align with the country’s pressing needs.

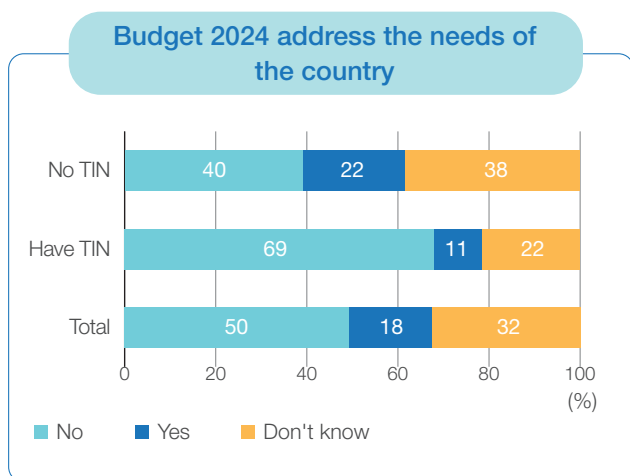


Figure 18: Perceived effectiveness of Budget 2024

Respondents were then asked to identify priority areas for the national budget (Figure 19). Education, health, and defence were identified as the top priority areas by respondents. Health was listed as the top priority by 27% of respondents, defense by 26% and education by 25%. These three sectors were also most likely to be listed among the top three priorities, with education and health being the most prioritised sectors by that criterion. This indicates a clear public demand for increased investment in human capital and essential services, reflecting concerns about the country's future development and security.

Focusing specifically on the current context, respondents were asked to rate their satisfaction with the quality and efficiency of government services and their views on measures to address the ongoing debt crisis (Figure 20). Respondents expressed extremely low levels of satisfaction with government services. A significant 37% were "very dissatisfied," and 42% were "dissatisfied," with only a small fraction expressing neutrality or satisfaction. TIN holders were particularly critical, with 57% indicating "very dissatisfied" compared to 26% of non-TIN holders. This widespread dissatisfaction underscores the perceived inefficiency and inadequacy of government services, highlighting the need for substantial improvements in public sector performance.

The widespread dissatisfaction with government services, as indicated by the National Tax Perception Study, aligns with findings from a recent survey conducted by Peradeniya University³. The survey revealed that many people are frustrated with the conduct of state officers, often needing influence or resorting to bribery to get their work done. Visits to state offices are described as unpleasant, with long

³ <https://www.sundaytimes.lk/240303/news/people-disappointed-with-state-officers-work-wont-happen-without-influence-or-bribery-550578.html>

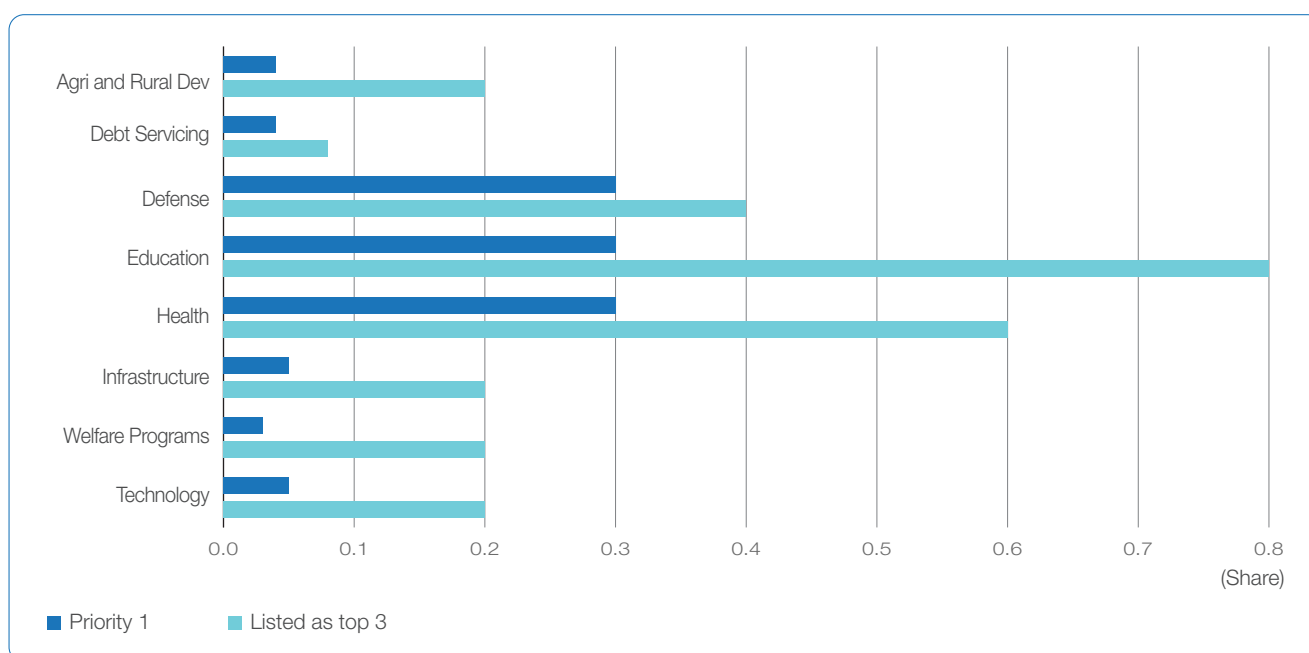


Figure 19: Priority areas for National Budget

waits and multiple visits due to inadequate guidance. Additionally, only 29% of phone calls to government offices were successfully answered, highlighting severe communication issues. These insights underline the inefficiency and inadequacy of public sector performance, necessitating significant reforms to improve service quality and efficiency.

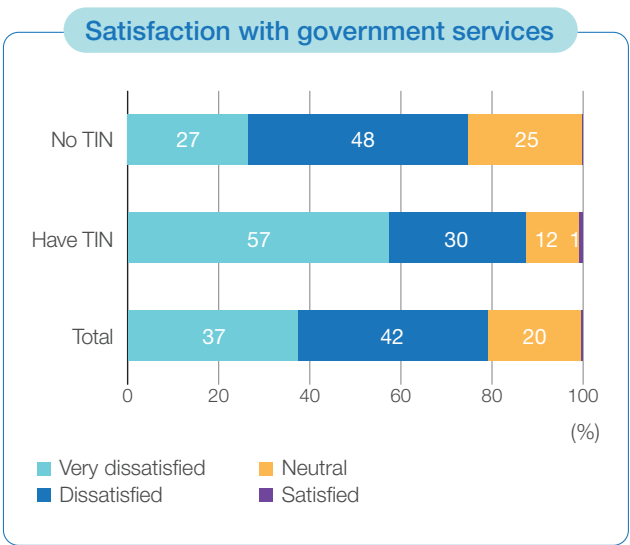


Figure 20: Satisfaction with quality and efficiency of government services

Despite the common consensus that the quality efficiency of government services is inadequate, cutting government spending was the most commonly selected option for addressing the debt crisis with 91% of respondents agreeing that this measure should be implemented (Figure 21). Other popular measures included reducing government employment (80% agreed) and reducing subsidies (68% agreement). This shows that most respondents agree that fiscal consolidation and prudent fiscal management are required to tackle the crisis. However, whether respondents agree with these measures with the implicit understanding that the quality of government services may further deteriorate or with the belief that the efficiency of government spending can be improved so that cuts to spending do not translate to lower quality is unclear. Unsurprisingly, the two least popular options were increasing direct taxes on individuals and increasing indirect domestic taxes.

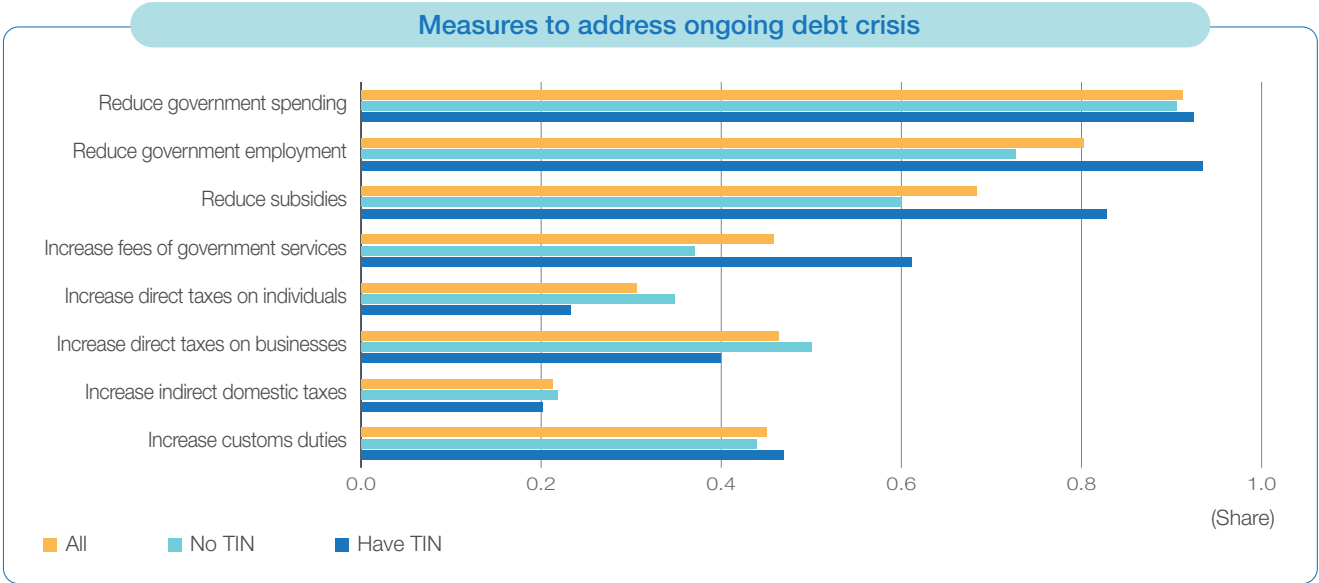


Figure 21: Measures to address ongoing debt crisis

There are some interesting differences between the responses from TIN holders and the rest. TIN holders were much more likely than the others to support reducing government employment and subsidies and increase fees for government services. Those without a TIN, on the other hand, were more likely to recommend increasing direct taxes on individuals and businesses. The latter is intuitive given that the TIN holders are primarily composed of payers of direct taxes and already report facing a heavy tax burden. When it comes to preferences for cutting government employment and subsidies and increasing fees for government services, it is possible that the TIN holders (the majority of whom are above the income tax threshold) perceive these expenditures to be wasteful as they are not the direct beneficiaries of this spending. Subsequently, they are less hesitant to recommend cutting these expenses. For instance, government health and education services tend to be more utilized by poorer households that cannot afford private sector alternatives.

4. Trust in tax institutions

The willingness to pay taxes is influenced not just by satisfaction with the public goods and services received but also trust in the government (Castaneda, 2024). This section focuses specifically on tax-related institutions in the country, examining the perceived role of an administrator as well as the level of trust in these institutions.

Expected Responsibilities of Tax Administrators

Respondents emphasized several key responsibilities for tax administrators (Figure 22). A significant portion of TIN holders highlighted the importance of creating awareness about tax obligations (over 60%), assisting taxpayers in calculating taxes and ensuring compliance with legislation (62%), and implementing tax laws and regulations (64%). These responsibilities reflect a strong public demand for educational initiatives, accessible support services, and effective enforcement mechanisms. Also notable is that whereas TIN holders were more likely to consider taxpayer assistance and awareness creation on tax obligation to be the main responsibilities of the tax administration, those without a TIN were more likely to suggest that the tax administrator’s main responsibility is to collect as much tax as possible. This points again to the social contract and knowledge of tax concepts in general where those who are more engaged with the tax system are more likely to see a productive role while those who are not are more likely to consider the concept of taxation to be unfair.

Although fewer respondents mentioned these aspects, transparency and accountability, minimizing tax evasion and fraud, and involvement in tax policy formulation were also cited as important. These expectations, cited by about 25% of respondents, highlight areas where improvements could significantly enhance the perceived fairness and effectiveness of the tax system. (More on these suggestions are discussed in the next sections.)

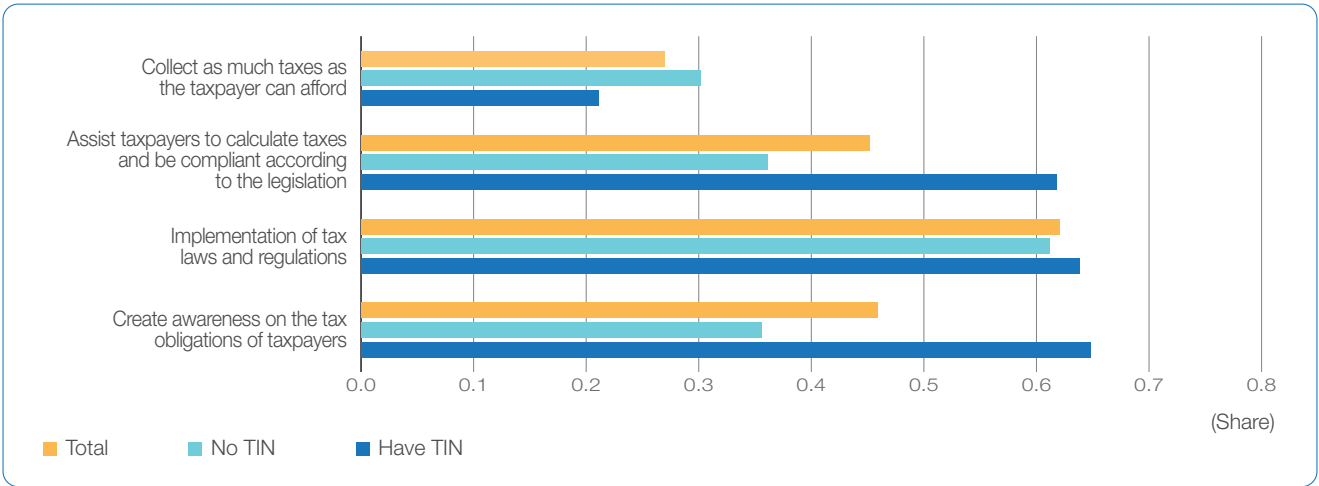


Figure 22: Responsibilities of tax administrator

Trust Levels in Tax Institutions

The Ministry of Finance (MoF) and the Inland Revenue Department (IRD) were widely recognized as the primary institutions responsible for tax policy formulation, with approximately 75% of respondents identifying the MoF and 42% identifying the IRD. Trust in tax institutions varied significantly across institutions, with the IRD garnering the highest level of trust (40%) followed by the MoF (35%) (Figure 23). However, the share of respondents who distrusted a given institution outweighed the share trusting it across the board, with the Cabinet of Ministers and President’s Office generating the largest shares of distrusting respondents (at 80% and 72%, respectively). It is noteworthy that these results suggest that while respondents are more likely to trust the bureaucracy and the system, they are less likely to trust their political representatives. One potential explanation of the distrust was captured in a separate question which revealed that 84% (93%) of respondents (TIN holders) agreed that corruption affects their willingness to pay taxes. This widespread distrust underscores the need for institutional reforms to enhance transparency, accountability, and public confidence.

Insights from KIIs: It was noted that, when questioned about how digitalization could be used to improve the tax system, several respondents mentioned that it would be useful for minimizing the role of human intervention in the taxpaying process, thereby minimising corrupt practices. The following excerpts underscore the perception about the prevalence of widespread corruption in the tax system.

“In customs it’s almost a norm”

“This is one of the biggest concerns and issues faced by most of the importers. The best option would be to eliminate and put a full stop, but I’m not sure whether it’s possible.”

“It is happening from top to bottom across the country”

Reasons provided by interviewees for corruption to prevail included assessors being given high targets resulting in indiscriminate allegations being made against organizations and the cost of paying a bribe being lower than the tax obligation. Accordingly, suggestions to tackle corruption include regular rotation of staff, enhanced use

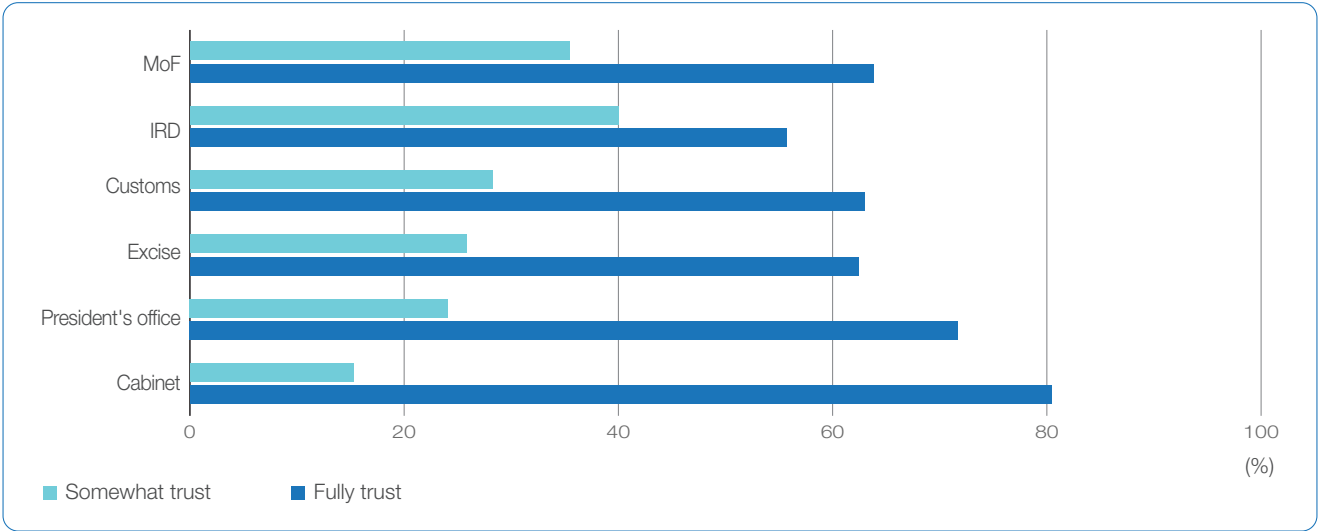


Figure 23: Trust in tax-related institutions

of digital services and simplification of the tax code to minimise human intervention and subjective interpretation and following a zero-tolerance policy with more severe penalties (e.g. termination of employment and publicizing names of corrupt officials in the event of being found guilty).

5. Satisfaction with services provided by the IRD

This section focuses specifically on the experiences of respondents with utilizing services provided by the Inland Revenue Department starting from the sources of tax-related information.

Sources of tax-related information

Despite the majority of those who reported having used IRD services doing so to obtain help with TIN or VAT registration, nearly two-thirds of TIN holders reported getting their tax information from tax professionals, while just less than half reported using government websites (Figure 24). Moreover, when asked how easy it is to access information about the rights, benefits and responsibilities of the taxpayer, nearly half reported that it was not at all easy. This highlights the heightened administrative costs of tax compliance, even among individual income taxpayers. Among those without the TIN, the most common sources of tax-related information were social media and news underscoring the need for accessible, reliable online resources and journalism.

Insights from KIs: The sources of tax-related information were similar in the KIs too, with respondents following the IRD website, news, and tax consultants or accountancy firms to stay informed about changes to tax laws and regulations. The responses suggest that the use of external services such as tax consultancies and attending tax seminars were required due to the complexity of the system and ad-hoc nature of some policy changes.

“It’s true that individual companies often rely on their tax consultants to navigate tax matters, and these consultants also keep an eye on developments in tax regulations and practices. However, this process tends to be informal, with companies informally sharing insights and updates among themselves.

What’s lacking is a more structured and predictable approach. The current situation feels too ad hoc, with new regulations seemingly appearing out of nowhere. While we’re vigilant and monitor these changes, the challenge lies in the unpredictability and randomness of these developments.” - Apparel industry

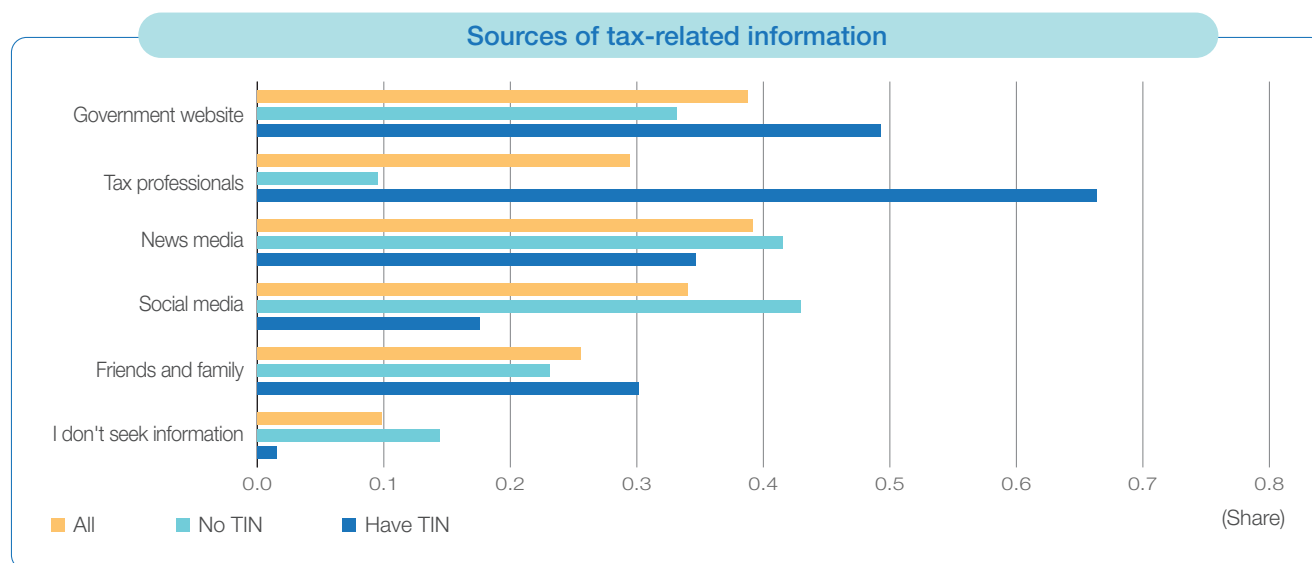


Figure 24: Sources of tax-related information

“News alerts from “ADA Derena” and having teams to scramble around, attempting to decipher recent rulings such as the recent VAT amendment, determining what is applicable and what exceptions exist. There is a pressing need for this process to be conducted in an orderly manner.” - Automotive industry

The KIs also show that a majority of respondents were not satisfied with the government’s communication regarding tax-related matters. However, among those who elaborated further on this, it appears that the lack of satisfaction was less with the communications related to tax administration and more related to lack of communications on the usage of tax money.

“What taxpayer must do is clear what government intends to do is not clear at all or is not known”

KIs were also asked to comment on the extent media coverage has influenced perceptions of the new tax policies. While most agreed that media coverage has a significant influence on public perception, several highlighted issues surrounding political biases among media outlets resulting on one-sided reporting sometimes demoralising the taxpayer, and insufficient understanding of taxation and the tax system among journalists. In fact, many of the respondents felt that the negative portrayals of taxes by journalists were misleading and inaccurate and suggested that journalists be more educated on tax related matters given their social responsibility to inform and educate the public.

“Public and media coverage are not focused on depicting a clear and a fair picture on the whole tax story. Taxes are being portrayed as something evil. It should not be the case.”

“The media highlights the negatives such as the number of firms avoiding paying taxes, which creates a negative opinion with the public. However, the media does not have a proper understanding on taxation. Although the media highlights the amount

of taxes to be collected, they don’t mention about the number of disputes. The IRD has not collected the tax probably because companies have gone through the dispute process, and maybe they appeal for the courts process. Giving a one-sided picture show that the journalists are weak in terms of their financial understanding. Educating the journalists and making them understand the economics better will make a more informed story.”

“Media plays a big role. They have a responsibility to HL (highlight) any wrong doing or investigative reporting. Media must carry a balanced view as perceptions are formed by ordinary folk.”

“Media needs to do more in terms of investigative journalism and hold govt/ administration accountable for tax leakages. Eg high profile cases with large values involved should automatically also result in tax audits.”

“There as a sentiment that was created which questioned the reason of paying taxes when it only goes to politicians. They have played a huge role in demoralising the taxpayer.”

Given that the majority on non-tax payers rely on the media for their information on taxation, an emerging narrative from the KIs is that the media can play a key role in raising awareness on the citizens’ rights and responsibilities related to taxation and improving tax morale while also holding the government accountable for their utilization of tax revenues through responsible investigative journalism.

Experiences with IRD Services

Among the respondents, 115 reported having used IRD services, with TIN holders more likely to utilize these services. The usage of IRD services, including online resources, increased with familiarity with the tax filing process (Figure 25), and more than half (55%) of those who had used IRD services reported doing so for the purpose for TIN or VAT registration.

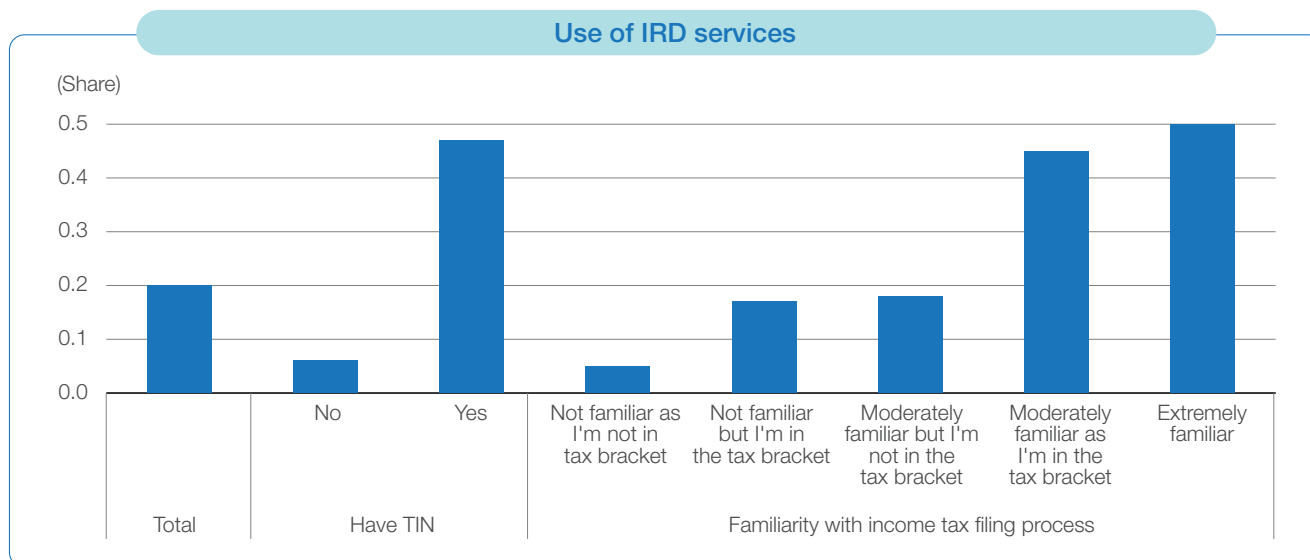


Figure 25: Use of IRD services

Respondents who had used IRD services generally reported positive experiences with registering for TIN and filing and paying taxes (Figure 26). However, negative reviews outweighed positives for services related to requesting refunds, lodging appeals or objections, and checking tax balances. When it came to challenges faced when interacting with the IRD, the

most common issues raised were difficulty in reaching the hotline (35.8%) and lack of user-friendliness of the website (32%) (Figure 27). These challenges underscore the need for better communication channels and more accessible online services to improve taxpayer experiences.

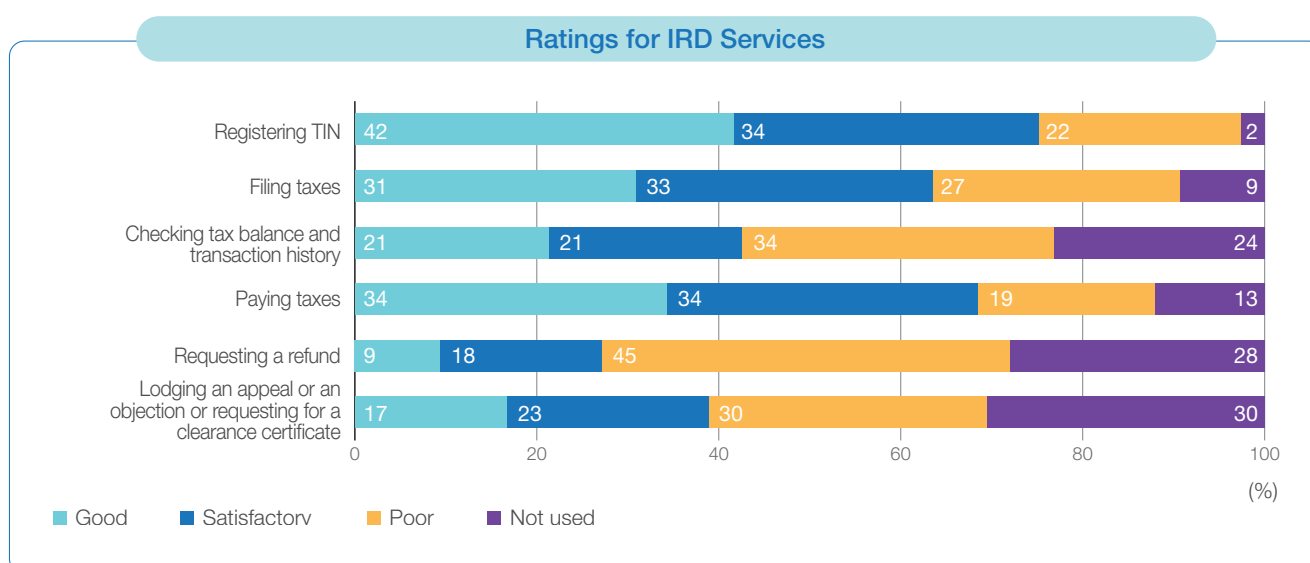


Figure 26: Ratings for IRD services

When asked specifically about interactions with IRD officials, approximately 35% of respondents who had used IRD assistance reported that they were not satisfied with their interactions, indicating a need for improvements in these specific service areas to enhance overall satisfaction (Figure 28).

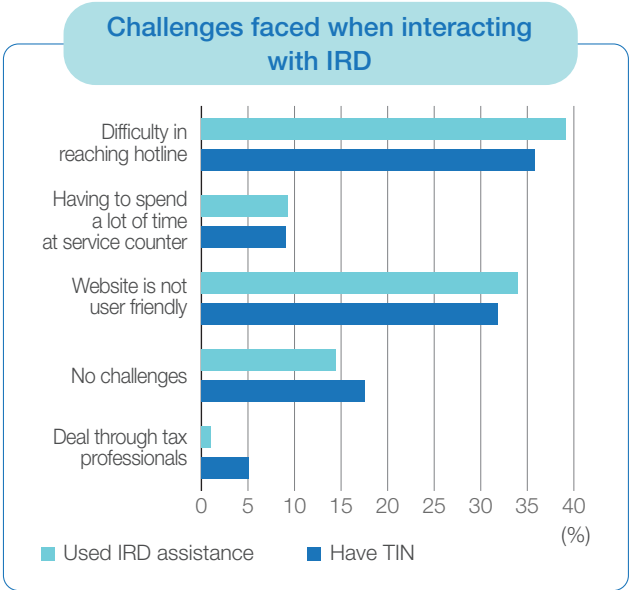


Figure 27: Challenges faced when interacting with IRD

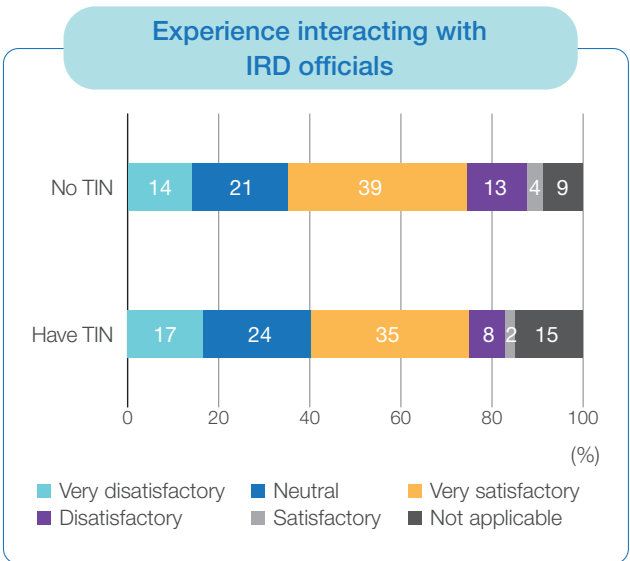


Figure 28: Experience interacting with IRD officials

Insights from KIs: Experiences of interacting with IRD officials were further explored in the KIs. When asked about their experience with tax audits, 27 reported having experienced a tax audit among whom very few reported positive experiences. There were several comments relating to lack of satisfaction with their interactions with the official in-charge including refusal to discuss assessments or hear justifications, lack of sector-specific knowledge, and attitudinal issues. Some respondents also reported that incorrect information was provided in some cases when help was sought from the IRD or that auditors had insufficient knowledge about ERP systems.

“IRD interprets in their own way and doesn’t consider what the business has to say, which is very unfair.” - Finance sector

“It was really an unhappy experience. There were no independent opinions/ decision from the senior Officials and it was solely a decision of the IRD Officer to raise the assessment. If the Officer is not correct, no Officer in the higher level in the hierarchy to correct the same. The assessed value is also not reasonable and it was an arbitrary amount. Assessment was with the IRD Officer when we were at the interviews to discuss the tax concerns.” - Finance sector

“looked upon as an ace fraudster simply wanting to dupe the tax authorities.” - Hospitality sector

SUGGESTIONS FOR IMPROVEMENT BY RESPONDENTS

The survey and KIs, while collecting perceptions and satisfaction relating to taxation in Sri Lanka, also provided respondents an opportunity to provide suggestions on various aspects of the same. These ranged from the more general suggestions on how tax policy at large could be improved to more specific suggestions on how the IRD could improve its services and makes its information more accessible. This section presents these suggestions.

Improvements to tax policy

In terms of suggestions to improve tax policy in Sri Lanka in general, a majority of survey respondents (79%) emphasized the enhanced transparency and communication (Figure 29). More than 50% also highlighted the need to simplify the tax process (52%) and for further digitization (51%). TIN holders were also overwhelmingly more likely (63% vs 14% among those without the TIN) to suggest increasing the taxpayer base. Respondents were also allowed to supply their own suggestions which included the provision of taxpayer rewards and incentives and the imposition of more fair tax rates and threshold. As one might expect, both these categories of responses were from TIN holders – given their more extensive interaction with the system, they are more forthcoming on ways to improve the system.

Given concerns about policy inconsistency in the Sri Lankan context, when asked how much notice should be provided before making a change to tax policy, the consensus (close to 50%) was that at least a year's notice should be given, though there were a sizeable share of respondents, mainly among the TIN holders (35%), who felt that 3 months was also sufficient time.

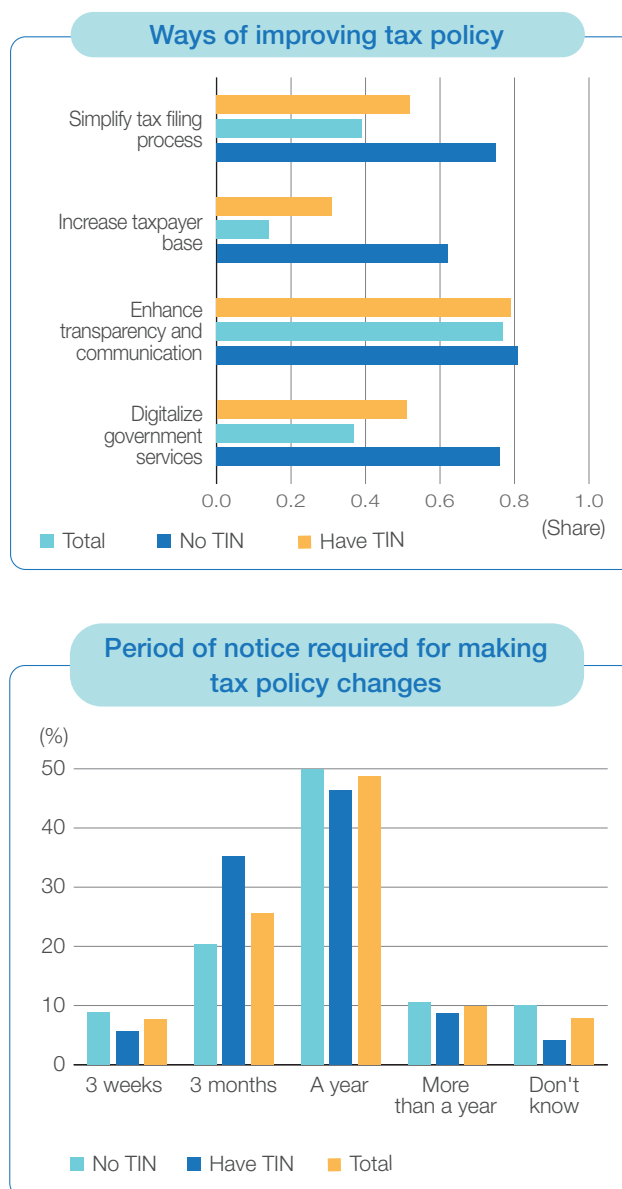


Figure 29: Improving Tax Policy and Notice Period for Policy Changes

Insights from KIs: The KIs were also provided an opportunity to elaborate on how Sri Lanka's tax policy could be improved. Key suggestions emerging from this can be broadly classified into the themes provided in the survey though some additional considerations were highlighted. The most common themes raised by the KIs were the need to further widen the tax base and simplify the tax system by further leveraging digital technologies, enhance transparency and communication and maintaining policy consistency. Specific suggestions are summarized thematically below:

1. Widening the tax base: reducing tax rates to encourage compliance, linking databases such as the banking system, Department of Motor Vehicles and the Land Registry to track high value transactions and identify high wealth individuals while making the TIN mandatory for services such as opening of bank accounts or motor vehicle registration, encouraging cashless transactions to discourage informal sector transactions, reducing tax exemptions and concessions, higher penalties for tax evasion
2. Simplify the tax system: use of digitization to fast-track tax filing and returns, incorporating systems that automatically track taxable activities minimizing the need for extensive manual interventions (e.g. land, vehicle and banking transactions), centralise revenue collection at all levels and facilitate easy online payments for all taxes and fines (e.g. police fines)
3. Improving the tax mix: reducing dependency on trade taxes and VAT and moving towards higher taxes on profits and income so that taxes can be used to reallocate resources equitably
4. Enhanced transparency and communication: consulting stakeholders in the policy formulation process, requiring taxes to be passed by parliament rather than allowing ministerial discretion, move towards digitization to minimize human intervention and corrupt practices in the process

5. Maintaining policy consistency: conducting thorough macroeconomic analyses and consultations with the industry to help reduce the need to make frequent changes, providing notice of 6 months-1 year before enacting tax reforms (though longer periods ranging from 2-5 years were suggested by those working in sectors like construction where investment and project durations are longer)

Improvements to IRD services

Given that the most significant issues related to using IRD services included difficulty in reaching the hotline and the user-friendliness of the website, most survey respondents who had used IRD services suggested enhancing the user-friendliness of the IRD website (73% of those who had used IRD services) and making more information available online (71%) (Figure 30). The introduction of mobile apps for easier access to services (50%), better ways to connect to the hotline (46%), and more service counters to reduce waiting times (31%) were also recommended. These suggestions clearly highlight the importance of leveraging digital solutions and enhancing service accessibility to meet taxpayer needs. Interestingly, better customer service was less of a priority among the provided options.

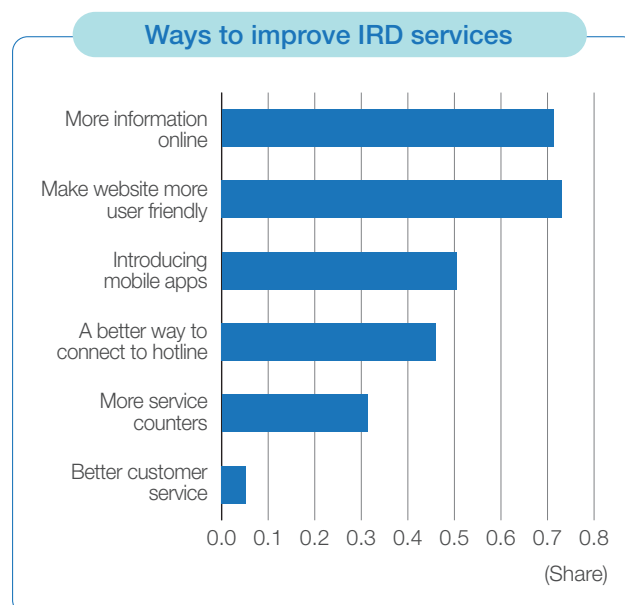


Figure 30: Ways to improve IRD services

Insights from KIIs: The KIIs provided an opportunity for interviewees to provide more detailed feedback on improving aspects of the services provided by the IRD including registering to pay taxes, filing returns, requests for information, settling appeals and conducting assessments. Again, many of the suggestions revolved around digitalization, though other comments also focused on the services provided by the IRD staff as well. The suggestions are summarized by function below:

- Registering: outsource the registration process, digitise entire process, ensure the cyber security of the system
- Filing returns: improve capacity of the system to avoid system crashing especially close to quarter end, digitise entire process to discourage face to face interactions, simplify the system by improving the RAMIS, interlinked systems (e.g. bank accounts) that may allow auto-filling of certain fields, development of mobile apps for tax filing
- Information requests: develop a mechanism (e.g. a token system) that tracks requests to ensure they are cleared within a certain set number of days so that time taken to resolve issues is reduced
- Settling appeals: enable proactive discussions with an online help desk to settle appeals (ensure that authorised persons are given access as help desk will have confidential information)
- Assessments: assessments should be raised with a sound rationale and should be reasonable (“stop opening up old files simply because they need to increase revenue collection”), allowing the taxpayer the right to explain or provide additional information where necessary
- Other: zero-tolerance approach to corruption with punishments for corrupt officials, IRD to adopt common policies for interpretations of various tax laws, avoid two tax regimes within a single tax year, improve attitudes of staff (“friendly customer service”)

“Simplify the way of filing taxes. It is difficult currently since there are withholding taxes involved. People might say that they don’t want to pay taxes as it is cumbersome.

Although there are tax consultants emerging recently for personal income tax, the process should be simplified more.”

ASYCUDA and RAMIS – suggestions from KIIs

RAMIS: The Revenue Administration Management Information System (RAMIS) in Sri Lanka is a digital platform designed to enhance the efficiency and transparency of tax administration. Developed by the Department of Inland Revenue, RAMIS integrates various functions such as taxpayer registration, tax return processing, payments, assessments, refunds, and the handling of appeals and objections. By automating these processes, RAMIS aims to reduce the complexity for both taxpayers and employees, thereby increasing compliance and revenue collection. The system also offers e-services, allowing taxpayers to access information and perform transactions anytime and anywhere, which aims to reduce the administrative burden and improving service delivery.

ASYCUDA: The Automated System for Customs Data (ASYCUDA) is an integrated customs management system developed by the United Nations Conference on Trade and Development (UNCTAD). It aims to facilitate international trade by streamlining customs processes, enhancing the accuracy of customs data, and improving the efficiency of customs operations. ASYCUDA supports various customs procedures including declarations, cargo tracking, and e-payments, thereby reducing the time and cost associated with customs clearance.

Not many respondents had interacted with the Asycuda system but the few who had raised many concerns about the functionality of the system and provided several suggestions. These include: lack of access to timely data (*“waiting until the 20th of the following month to access export information online is archaic, especially when considering that it’s a simple matter of overall numbers, not company-specific data. Why isn’t this information readily available to the public through a dedicated portal?”*),

- Linking the system with other board agencies to minimise the amount of information that has to be entered by the taxpayer (e.g. Registrar of Companies)
- Enhancing the capacity of the system to handle larger volumes of e-commerce transactions and improving the functionality of the system (e.g. enable API integrations)
- Eliminating the requirement to provide hard copies of documentation (*“The need to provide hard copies despite online submission of customs entries on ASYCUDA is ludicrous and patent corruption”*)

Many more respondents were familiar with RAMIS. Similar problems as those reported for Asycuda, including the tendency of the system to crash when overloaded and conflicts between the system and officials were raised. Specific comments relating to the RAMIS include:

- Lack of a user-friendly interface: improvements could include differentiating mandatory and optional fields, allowing corrections to input errors (*“the system does not facilitate to correct the data in the system in case of input errors and hence the Officers cannot clear the incorrect outstanding balances in the system.”*), Redesigning the interface to reduce crowding and make it more compatible for use on mobile devices, improving knowledge about the system among some tax officials
- Limited functionality: dispute resolution process is difficult and a refund mechanism is lacking
- Conflicts between the system and officials: for instance, one KI mentioned instances where the system is tampered with to necessitate in-person meetings leading to corrupt practices. Another highlighted how the irresponsible and arbitrary decisions on the part of tax assessors also undermines the online system.

“Senior workers purposely alter the system so that it doesn’t work so that they can meet the taxpayer in person with the intention of bribes.”

“Assessors who are solely focused on meeting targets and send out letters without proper logic or accountability undermine the integrity of the tax assessment process. This approach places unnecessary burden and costs on organizations, forcing them to prove their innocence even when unjustly accused. Assessors must be held accountable for their actions. Whatever the cost that has been incurred if the assessor has not done his job, the assessor should be paying entire penalty. It’s essential to mandate in their job descriptions the responsibility to conduct assessments accurately and fairly, with penalties for negligence or abuse of authority. This is one of the reasons for the failure of RAMIS.”

Improving accessibility of tax-related information

Given the common perceptions about complexity of the tax system and lack of understanding of the tax system, respondents of the survey were also asked to provide suggestions on how to improve the accessibility and quality of tax-related information in an

open-ended question. The responses provided can be broadly grouped into 6 categories: awareness raising (mentioned by 23% of respondents), provision of more information (8%), simplification and usability of the system (12%), transparency (6%), service delivery (5%), and digitization (4%). Specific suggestions under these themes are summarized in Table 2.

Table 2: Suggestions on improving tax-related information

Awareness raising	Digitization of systems	Providing more information	Enhanced transparency	Service improvements	Simplification/usability of the system
Use of mass media (e.g. tv ads, press briefings) and social media	AI assistant	Explanatory videos, online tutorials	Information on how, where, to what extent taxes are used	Online tax calculator	Use NIC as TIN
Incorporate into education system (e.g. add to DP education platform)	Fully automated system minimizing people involvement	Provision of information in all languages	Introduction of block chain/ cryptocurrency	Industry specific support	
Awareness sessions	Mobile app	Email query system	Regular updates on collection values	Email/SMS reminders and notifications to registered taxpayers	
Using celebrities to talk about taxes		Employing easy language		Tax officer visits to customers	
Knowledge drive at offices		Updating with latest information		More lines and trained people to answer queries	
		Online knowledge base		Develop tax service provider professional service, tax advisory counter	
		FAQs		Call back options for call-centers	
				Facilitate tax payment through fund transfers	
				Dedicated hotline for high tax-payers	

As Table 2 shows, awareness raising and the provision of more information were significant areas highlighted by over 20% of respondents. Suggestions under these two themes included using mass media (such as TV ads, press briefings, and social media) to educate the public about tax obligations. Incorporating tax education into the formal education system and conducting awareness sessions/workshops were also suggested. To ensure accessibility, it was recommended that information be provided in all three languages employing easy-to-understand language, with regular updates to keep taxpayers informed. Possible modes of sharing information included short video tutorials or a Frequently Asked Questions (FAQ) page on the website.

Digitization of systems emerged as another prominent theme. Suggestions here included the development of AI assistants (e.g. chatbots), fully automated systems to minimize human involvement, and mobile apps for easy access to services. These digital solutions aim to streamline tax processes, reduce administrative burdens, and improve taxpayer experiences. Enhanced transparency was also a key focus, with respondents suggesting regular updates on tax collection values, the introduction of blockchain technology for secure and transparent transactions, and clear information on how and where taxes are used. These measures are intended to build trust in the tax system and ensure accountability in the use of tax revenues.

Service quality improvements were highlighted, with recommendations for an online tax calculator, industry-specific support, and email/SMS reminders and notifications for registered taxpayers. Developing a professional tax advisory service and providing a dedicated hotline for high taxpayers were also suggested to offer personalized and efficient support.

Simplifying the tax system was seen as essential for enhancing compliance and reducing administrative complexity by many respondents though there were very few specific suggestions as to how this could be achieved. These included using the National Identity Card (NIC) as the Taxpayer Identification Number (TIN) to simplify registration and tax processes and revamping the website to make it more user friendly and easy to navigate.

While many of the respondents did provide suggestions for improvement, it is noteworthy that less than a quarter of respondents were aware of existing channels to provide feedback on the tax system, suggesting a need for better communication and promotion of feedback mechanisms to ensure taxpayers can voice their concerns and suggestions effectively.

Improving tax morale: suggestions from KIs

Improving tax morale among the public is essential for enhancing compliance and the overall effectiveness of the tax system. The KIs were asked to comment on how they felt that tax morale could be improved in the Sri Lankan context. Their suggestions are listed below:

Greater Transparency: The most common response was the need for greater transparency in tax collection and utilization. This includes regularly publishing data on whether revenue collection targets are met, how tax revenues are spent, and the avenues of expenditure. Transparency in the provision of tax concessions and the achievement of agreed development impacts was also emphasized.

Higher Accountability: There was a strong call for higher accountability for government expenditures to minimize wasteful expenditures. Ensuring that taxpayers' money is used efficiently and for the intended purposes would help build trust in the tax system and the government.

Elimination of Corruption: Eliminating corruption within the tax administration and the broader government framework was seen as crucial. Corruption not only reduces the effectiveness of tax collection but also erodes public trust, making it more challenging to encourage voluntary compliance.

Equal Treatment of Taxpayers: Ensuring equal treatment of all taxpayers, from ordinary citizens to top-level officials, whether in government or otherwise, was highlighted as necessary. Perceptions of favouritism or unequal treatment can undermine the legitimacy of the tax system.

Widening the Tax Net: Efforts to widen the tax net were encouraged. This includes identifying new areas of taxable income and ensuring that all economic activities contribute fairly to the tax revenue. Highlighting and implementing these efforts would demonstrate the government's commitment to a fair and inclusive tax system.

Incorporating Tax Education: Incorporating tax education into school curricula, using mass media, and other public forums was suggested to raise awareness about tax obligations and the benefits of paying taxes. Educating the public from a young age about the importance of taxes in funding public services and infrastructure can help build a culture of compliance.

The suggestions provided by respondents on various aspects of the tax system in Sri Lanka, if implemented, could significantly streamline tax processes, improve taxpayer relations, and ultimately lead to a more robust and equitable tax system. The results also showcase how certain measures could help address multiple issues within the system – for instance, digitalization would be instrumental for simplifying the system, minimising tax evasion and reducing corruption).

In conclusion, while the key informants highlighted several limitations and challenges within the current tax policy and administration, their insights also provided a roadmap for potential improvements. By considering these issues and leveraging technological advancements, it is envisaged that the tax system in Sri Lanka can be reformed to better meet the needs of all stakeholders.

CONCLUSION AND RECOMMENDATIONS

The National Tax Perception Study – Sri Lanka 2024 provides a comprehensive analysis of public perceptions and experiences with the tax system, identifying critical areas for policy intervention and reform. The study reveals significant gaps in knowledge and varying perceptions of the tax system among different segments of the population. Addressing these disparities is crucial for enhancing tax compliance, improving public trust, and fostering a more equitable and efficient tax system in Sri Lanka. By understanding and addressing the concerns and suggestions of taxpayers, policymakers can implement reforms that not only increase revenue but also strengthen the social contract between the government and its citizens.

Key Recommendations:

• Increase Tax Education and TIN Registration:

- Why it's important: There is a significant knowledge gap about tax concepts and the tax system among those without a Taxpayer Identification Number (TIN). By increasing TIN registration and tax education, particularly among younger workers, self-employed individuals, and government employees, the government can foster a more informed taxpayer base. This will lead to better compliance and a stronger understanding of the tax system's benefits and obligations.
- Action Steps:
 - » Prioritize initiatives to increase TIN registration and tax education.
 - » Launch educational campaigns and simplify the tax registration process.

• Enhance Transparency and Consistency in Tax Policy:

- Why it's important: Perceived complexity and lack of transparency in the tax system erode public trust and hinder compliance. By simplifying tax procedures and ensuring tax policies are stable and predictable, the government can build trust and reduce the perceived burden of compliance. Engaging in broader stakeholder consultations will ensure policies are fair and well-communicated.

• Action Steps:

- » Simplify tax procedures.
- » Ensure stability and predictability in tax policies.
- » Engage in stakeholder consultations.
- » Provide clear, timely communication about tax changes.
- » Implement institutional reforms for transparency and accountability.

• Improve Public Sector Performance:

- Why it's important: There is widespread dissatisfaction with the efficiency and quality of government services. Improving public sector performance can enhance the public's perception of value for their tax contributions, which is crucial for increasing willingness to comply with tax obligations.
- Action Steps:
 - » Implement performance management systems.
 - » Increase accountability in public service delivery.
 - » Enhance the quality and efficiency of government services.

• Leverage Digitization:

- Why it's important: Investing in digital infrastructure can streamline tax processes, making them more efficient and user-friendly. Digital solutions can minimize corruption, reduce errors, and increase compliance by providing accessible and transparent tax services.
- Action Steps:
 - » Invest in digital infrastructure.
 - » Link databases across institutions.
 - » Develop mobile apps and online platforms.
 - » Mandate the use of TIN for various transactions.
 - » Promote cashless transactions to enhance transparency.

- **Ensure Fair and Consistent Tax Policies:**

- Why it's important: Addressing sector-specific needs and avoiding politically motivated tax concessions can ensure a balanced and equitable tax system. Simplifying the tax code and designing policies with long-term revenue targets in mind will create a stable environment that supports economic growth.
- Action Steps:
 - » Address sector-specific needs.
 - » Avoid politically motivated tax concessions.
 - » Simplify the tax code.
 - » Ensure tax policies are designed with long-term revenue targets.
 - » Critically examine tax exemptions and reliefs.

- **Enhance Communication and Public Relations:**

- Why it's important: Effective communication between revenue institutions and citizens is crucial for building trust and ensuring taxpayers feel valued and informed. Clear and consistent communication can enhance public understanding and support for tax policies.
- Action Steps:
 - » Orient revenue institutions' communications to view citizens as entitled users of government services.
 - » Ensure consistent and effective communication between revenue institutions and citizens.

In conclusion, the National Tax Perception Study – Sri Lanka 2024 underscores the urgent need for comprehensive tax reforms to address the challenges identified by taxpayers. By implementing the recommendations outlined above, policymakers can create a tax system that is more transparent, efficient, and fair. These measures will not only enhance compliance and revenue collection but also build public trust and support for the government's fiscal policies. A well-managed and equitable tax system is essential for sustainable economic development, fostering national prosperity, resilience, and overall well-being, ultimately benefiting all citizens of Sri Lanka.

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