SRI LANKA

TRADE SUMMARY

U.S. goods exports in 2013 were $314 million, up 40.0 percent from the previous year. Corresponding U.S. imports from Sri Lanka were $2.5 billion, up 8.6 percent. The U.S. goods trade deficit with Sri Lanka was $2.1 billion in 2013, up $105 million from 2012. Sri Lanka is currently the 117th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Sri Lanka was $102 million in 2012 (latest data available), up from $94 million in 2011.

IMPORT POLICIES

The government continues to stress the need to promote import substitution policies, which distort the market. Sri Lanka's 2013 and 2014 budgets emphasized the importance of agricultural self-sufficiency and import substitution.

Import Charges

Sri Lanka's main trade policy instrument has been the import tariff. According to the WTO, Sri Lanka's average applied agricultural tariff in 2010 was 25.4 percent, but its bound rates are significantly higher, averaging 50 percent. However, the compounded duty rates for imported agriculture products are routinely between 80 percent and 100 percent of the cost, insurance, and freight (CIF) value. In 2010, Sri Lanka's average applied tariff for nonagricultural goods was 9.2 percent. However, less than 30 percent of Sri Lanka's nonagricultural tariffs are bound under WTO rules.

Sri Lanka's import tariff structure consists of "bands" in which all products covered by a particular band are subject to the same tariff rate. The import tariff structure was simplified in June 2010 by reducing the number of tariff bands from five to four. The current tariff bands are: 0 percent; 7.5 percent; 15 percent; and 25 percent. Tariffs on semi-processed raw material are 7.5 percent, while intermediate product tariffs are 15 percent. Most tariffs on finished products are 25 percent. There continue to be a number of deviations from the four-band tariff policy. Some items are subject to an *ad valorem* or a specific tariff, whichever is higher, and there is intermittent use of exemptions and waivers. Footwear, ceramic products, and agricultural products carry specific tariffs.

In response to large current account deficits in 2011 and 2012, the government took several policy measures to stem import growth. For example, it depreciated the rupee and moved to a flexible exchange rate policy in early 2012. Sri Lanka also increased tariffs on motor vehicles in a bid to curb imports and imposed a 100 percent deposit requirement on motor vehicle imports, requiring importers to pay upfront the full value of motor vehicles at the time of opening letters of credit with commercial banks.

In addition to the import tariff, there are a number of supplementary taxes and levies on imports. Some supplementary taxes on selected products are increased regularly through annual government budgets, most often to protect local industries. For example, the Export Development Board (EDB) levy on biscuits increased from Rs 60 (approximately $0.51) per kg in 2012 to Rs 80 (approximately $0.62) per kg in 2013. The tax was increased further to Rs 100 (approximately $0.76) per kg in 2014. The EDB levy on cheese was increased from Rs 100 (approximately $0.86) per kg in 2012 to Rs 200 (approximately $1.56) per kg in 2013 and to Rs 300 (approximately $2.29) per kg in 2014. The EDB levy on butter and dairy spreads increased from Rs 100 (approximately $0.86) per kg in 2012 to Rs 200 (approximately $1.56) per kg in 2013. The 2014 budget replaced the import tariff and all supplementary taxes on butter and dairy spreads with a special commodity tax of Rs 880 (approximately $6.70) per kg. In general, the frequent changes—mostly upward—of these taxes and other levies have added unpredictability to foreign exporters' and local importers' cost calculations. Affected products from the United States include fruits, processed/packaged foods, and personal care products.

Other charges on imports include:

- An EDB levy, often referred to as a "cess," ranges from 10 percent to 35 percent *ad valorem* on a range of imports identified as "nonessential" or competing with local industries. Most of the items are subject to specific duties as well. Also, when calculating the EDB levy, an imputed profit margin of 10 percent is added onto the import price. In some cases, such as biscuits, chocolates, and soap, the levy is charged not on the import price, but on 65 percent of the maximum retail price. Locally manufactured products are not subject to the EDB levy. The government continues to increase the EDB levy, most recently in November 2013, when it increased the EDB levy on a range of items, including dairy products, meat, fruits, vegetables, and confectionary.
- A Ports and Airports Development Levy of 5 percent is applied on most imports. Locally manufactured products are not subject to the Ports and Airports Development Levy.
- When calculating the Value Added Tax (VAT), an imputed profit margin of 10 percent is added on to the import price. Locally manufactured products are also subject to VAT, but not the imputed profit margin. The current VAT rate is set at 12 percent.
- Excise fees are charged on some products such as aerated water, liquor, beer, motor vehicles, and cigarettes. When calculating the excise fee, an imputed profit margin of 15 percent is added to the import price. The excise fee is applied on the price inclusive of other duties. Locally manufactured products are also subject to excise fees.
- A Nation Building Tax (NBT) of 2 percent is applied on most imports.
- As of November 21, 2011, a Special Commodity Levy (SCL) is charged on some imported food items including oranges, grapes, and apples. The SCL is Rs 65 per kg on oranges, Rs 130 per kg on grapes, and Rs 45 per kg on apples. The items subject to the SCL are exempted from all other taxes.
- In November 2011, the government introduced an all-inclusive tax under the EDB levy on imported textiles not intended for use by the apparel export industry, replacing the import tariff, the EDB Levy, the Ports and Airports Tax, the VAT, and the NBT. Currently, this all-inclusive tax is Rs 100 per kg (approximately $0.95.)
- Apparel imports are subject to a 15 percent import duty, an Rs 75 (approximately $0.57) per unit EDB Levy, a 12 percent VAT, a 5 percent Ports and Airports Levy, and a 2 percent NBT.

Import Licenses

Sri Lanka requires import licenses for over 400 items at the 6-digit level of the Harmonized Tariff System, mostly for health, environment, and national security reasons. Importers must pay a fee equal to 0.222 percent of the import price with a minimum fee of Rs 1,000 (approximately $7.60) to receive an import license.

GOVERNMENT PROCUREMENT

Government procurement of most goods and services is primarily undertaken through a public tender process. Some tenders are open only to registered suppliers. Procurement may also be undertaken outside the normal competitive tender process. The government publicly subscribes to principles of international competitive bidding, but charges of corruption and unfair awards are common. In 2006, Sri Lanka published guidelines and a procurement manual to improve the public procurement process. However, in early 2008, the government disbanded the National Procurement Agency, which it had established in 2004, and shifted its functions to a unit in the Ministry of Finance. A special cabinet-appointed review committee reviews unsolicited development proposals, and this committee has considered the most important infrastructure projects and investment proposals, which occur outside the tender process. These moves have raised concerns about the government's commitment to improve the transparency of procurements.

Sri Lanka is not a signatory to the WTO Agreement on Government Procurement and has indicated it has no plans to join despite its status as an observer to the WTO Committee on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

Although intellectual property rights (IPR) enforcement has improved in Sri Lanka, counterfeit goods continue to be widely available. Local agents of well-known U.S. and other international companies representing recording, software, movie, clothing, and consumer product industries continue to complain that lack of IPR protection is damaging their businesses. Piracy of sound recordings and software is widespread, making it difficult for the legitimate industries to protect their market and realize their potential in Sri Lanka. According to a recent industry-commissioned study, the rate of software piracy in Sri Lanka was 84 percent and the value of pirated software was $86 million in 2011. With respect to the government sector, the government of Sri Lanka published a policy in 2010 requiring all government ministries and departments to use only licensed software, specifying that licenses can be for either proprietary software or for open source software. This has enabled government organizations to legalize the software they use. However, the government has yet to put systems in place to monitor compliance with this policy.

Redress through the courts for IPR infringement is often a frustrating and time-consuming process. While police can initiate action against counterfeiting and piracy without complaints by rights holders, they rarely do so. In the apparel, software, tobacco, and electronics sectors, however, rights holders have had some successes in combating trademark counterfeiting through the courts.

SERVICES BARRIERS

Insurance

Sri Lanka does not allow the cross-border supply of insurance, with the exception of health and travel insurance. In order to provide all other insurance services to resident Sri Lankans, insurance companies must be incorporated in Sri Lanka. Branch offices are not permitted. The Sri Lankan government requires all insurance companies to reinsure 20 percent of their insurance business with a state-run insurance fund. (The government also requires insurance companies, both local and foreign, to list on the Colombo Stock Exchange by 2016). However, the government is in the process of developing regulations to exempt foreign-owned companies from this listing requirement.

Broadcasting

The government imposes taxes on foreign movies, programs, and commercials to be shown on television, ranging from Rs 25,000 (approximately $190) for an imported English-language movie to Rs 90,000 (approximately $690) per half hour of a foreign-language program dubbed in the local language, Sinhala. Foreign television commercials are taxed at Rs 500,000 (approximately $3,820) per year, and rates for non-English foreign programming are even higher. Government approval is required for all foreign films and programs shown on television.

INVESTMENT BARRIERS

Although Sri Lanka welcomes foreign investment, there are restrictions in a wide range of sectors. For example, foreign investment is not permitted in certain types of money lending activities, in the coastal fishing sector, and in retail trade for investments of less than $2 million (or $150,000 in the case of international brands and franchises). In other sectors, foreign investment is subject to case-by-case screening and approval when foreign equity exceeds 40 percent. These sectors include shipping and travel agencies, freight forwarding, mass communications, deep-sea fishing, timber industries, mining and primary processing of natural resources, and the cultivation and primary processing of certain agriculture commodities. Foreign equity restrictions also apply in the air transportation, coastal shipping, lotteries, and gem mining sectors, as well as in sensitive industries such as military hardware.

Sri Lanka prohibits the sale of public and private lands to foreigners despite the fact that there is no current basis in law for this prohibition. Any investment with over 25 percent foreign equity is treated as "foreign" for the purpose of these measures. The measures do not apply to the purchase of condominium properties above the fourth floor of a building. The government also imposes a 15 percent tax on land and property leased to foreign investors (waived for leases of condominium properties above the third floor of a building); the tax for the entirety of the lease period is due at the time the lease is signed. Although these measures are not yet reflected in current law, the government has instructed land registries to begin enforcing these policies in advance of amendments to the existing law.

In November 2011, the government approved a new law, the Revival of Underperforming Enterprises and Underutilized Assets Act, which allows for the nationalization of assets belonging to 37 companies deemed by the government to be underperforming and not meeting lease conditions. Although many of the companies were defunct, several were operating businesses, including one that was owned by a prominent member of the opposition. The measure was passed under procedures that limited Parliamentary debate to one day. While the Central Bank noted that the enactment of the law was a "one-off" measure, the government subsequently announced plans to retake 25,000 hectares of tea plantation leased land that was not being fully utilized and to acquire abandoned private paddy land. The law significantly increases investor uncertainty regarding property rights in Sri Lanka.

OTHER BARRIERS

Public sector corruption, including bribery of public officials, remains a significant challenge for U.S. firms operating in Sri Lanka. While the country has generally adequate laws and regulations to combat corruption, enforcement is weak and inconsistent. U.S. firms identify corruption as a constraint on foreign investment. In particular, U.S. industry has expressed concern about corruption in large projects and with respect to government procurement.