

## **LOSS OF CORPORATE INCOME TAX REVENUE DUE TO TAX EXEMPTIONS: AN ANALYSIS BASED ON TAX RETURNS**

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This paper estimates the potential Corporate Income Tax (CIT) revenue, collectible CIT revenue accounting for tax exemptions granted and the loss of CIT revenue due to tax exemptions based on tax returns of 1,015 companies (a 20% random sample of 5075 companies with consistent information) during the period from 2010/2011 to 2014/2015. The computation was also done by subsamples of small, medium and large scale companies and agricultural, industrial and service companies. The potential CIT revenue was computed by multiplying the total aggregate business profit and income by the marginal CIT rate, and the collectible CIT revenue was computed by subtracting the aggregate business profits and income exempted from the potential CIT revenue. The loss of CIT tax revenue due to tax exemptions is defined as the difference between the potential CIT revenue and the collectible CIT revenue. The estimated loss of CIT revenue due to the exemption of the profit and income of the companies for tax purposes amounted to Rs. 7,231 million and Rs. 9,240 million in the 2010/2011 and 2014/2015 assessment years respectively. The period average loss of CIT revenue due to exemptions amounted to Rs. 8,100 million, which stood as 26% of the potential CIT revenue of the companies in the sample. This indicates that on average a tax loss of Rs. 7.98 million is reported per company due to the CIT exemptions. If the projection is made to the population of 5075 companies in question, the average tax loss due to exemptions amounts to Rs. 40,500 million, which would be about 41% of the average actual CIT revenue collected during the period. Following the same method, the loss of CIT revenue was estimated for small, medium and large scale companies. The loss of CIT revenue due to the exemptions granted for the profit and income earned by 656 small companies, 252 medium companies and 107 large companies in the sample amounted to Rs. 3,311, Rs. 429 and Rs. 5,500 million respectively in the 2014/2015 assessment year. On average, a tax loss of a total of Rs. 8,100 million is reported for the 1,015 companies between the 2010/11 and 2014/15 assessment years. Further, the results reveal that the average of annual tax loss due to exemptions per company is Rs. 2.6 million for medium companies, Rs. 5.5 million for small companies and Rs. 36.5 million for large companies during the period in question. The period average CIT revenue loss due to exemptions given to 14 agricultural companies, 381 industrial companies and 620 service providing companies in the sample was Rs. 15, Rs. 3687 and Rs. 4397 million respectively. The average CIT revenue loss per agricultural, industrial and service company is recorded as Rs. 1.07, Rs. 9.68, and Rs. 7.09 million respectively. The results reveal that service and industrial companies receive larger tax exemptions than agricultural companies. This situation signals the need for immediate policy attention to the tax exemptions.

*Keywords:* Corporate Income Tax, Tax Exemptions, Collectable Tax Revenue