PROPOSALS FOR BUDGET 2026

Research Publications and Resources

Reduce tax on EPF returns from 14% to 10%

Abstract — In September 2023, Sri Lanka became the only country to restructure local currency debt by exclusively targeting retirement savings funds, excluding all others. This move was justified by claims that retirement savings were receiving preferential tax treatment. However, our analysis shows that retirement funds face adverse, not preferential, tax treatment. This proposal is to reduce the tax on EPF savings returns from the current 14% to 10%, which would reduce the financial burden on contributors while being fiscally sustainable through offsetting revenue-generating measures.

Overview — The EPF, established in 1958, was originally a tax-free savings instrument—no tax on the savings, returns to investment of the savings, or withdrawal of the funds upon retirement. In 1989, the government introduced a 10% tax on investment returns, which was increased to 14% in 2018.

By 14% the EPF bears a significantly higher tax burden relative to financial institutions because it is effectively taxed on most of its gross income, whereas financial institutions are taxed mainly on net income, even at a higher tax rate. By contrast, based on Central Bank data, the banking sector paid, on average, only 8.0% of its gross income in VAT, SSCL, and corporate income tax combined, during the 2018-22 period examined.

Over 90% of active EPF members earn less than LKR 100,000 per month (Refer Annex 01). These contributors, who fall below the taxable income threshold and are not liable to pay income taxes, still face a 14% tax on their EPF savings returns. This creates a stark inequity, as these savings returns would have been entirely tax-exempt if saved privately. The current taxation policy disproportionately penalises low-income earners, undermining the intended purpose of retirement savings.

Cost - Reducing the tax on EPF investment returns from 14% to 10% will result in an **estimated revenue loss of LKR 15.7 billion.** However, this cost can be offset by complementary revenue-generating measures, such as increasing the withholding tax rate and correcting the flaws in cigarette taxation. This ensures fiscal sustainability while improving equity in retirement savings taxation.

Supporting reading/reference material

- Retirement Funds Face Regressive Taxation in Sri Lanka – [available here]

Annex 01: Breakdown of EPF member accounts

Monthly Income (LKR)	Number of Currently contributing EPF account holders end of Sept 2024	% of EPF Member Accounts
Upto 100,000	2,024,569	91.6%
100,000 - 141,667	65,656	3.0%
141,667 - 183,333	39,695	1.8%
183,333 - 225,000	26,119	1.2%
225,000 - 266,667	13,920	0.6%
266,667 - 308,333	9,138	0.4%
308,333 - 350,000	6,609	0.3%
350,000 - 391,667	4,362	0.2%
391,667 - 433,333	3,413	0.2%
More than 433,333	16,066	0.7%
Total	**2,209,547**	**100.0%**

Source: Information obtained through a Right to Information request made by Verité Research