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A QUALITATIVE DIAGNOSIS OF FACTORS INFLUENCING PRESUMPTIVE TAX COLLECTION IN SRI LANKA

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Abstract

This study aims to explore the factors influencing presumptive tax collection in Sri Lanka. Sri Lanka has a tax to GDP percentage of 7.8% in 2024. Tax revenue increase can be aimed via formal and informal tax collections. Various research identified the mechanisms of improving formal tax collections However hardly any research is done on informal tax collections in Sri Lanka. The researcher identified the gap and analyzed the important factors in this research. An interpretivist paradigm was adopted in this study using a qualitative research approach. Primary data were collected through virtual (On-line) in-depth interviews with 15 participants among tax consultants from the Department of Inland Revenue, tax practitioners, academics and General public in Sri Lanka. Qualitative data were analyzed using thematic analysis. The results of the qualitative analysis of the factors influencing presumptive tax collection in Sri Lanka show the institutional, legal and regulatory framework as well as the governance and political factors, which will help the Department of Inland Revenue and policy makers, formulate policy strategies to promote presumptive tax collection and voluntary tax compliance in Sri Lanka. The research study finds that the government of Sri Lanka improve tax revenue via presumptive taxes of informal activities which has not been considered in the past.

Keywords: Presumptive Tax, Informal Economy, Thematic Analysis

1. Introduction

Government revenue comprises various components. Taxation is an important component of Government revenue. The taxation plays a crucial role in funding public services, infrastructure development and national economic growth by ensuring an efficient and fair taxation system. The Inland Revenue Contribution of Rs. 2.62 trillion to Government revenue collection represents a substantial figure particularly when viewed in the context of the national Gross Domestic Product (GDP) at current market prices which stands Rs. 29.90 trillion. However, the Inland Revenue Contribution of Rs. 2.62 Trillian equates to approximately 8.76% of the Total GDP. Sri Lanka has a large informal economy. This is considered to be a major obstacle in the implementation of income taxes in developing countries (Memon, 2013:40). A lack of appropriate compliance management and a voluntary compliance tradition facilitated the rapid development of the underground economy

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in many developing countries (Engelschalk 2015:277). For many decades, the perilous state of Sri Lanka's public finance has significantly impeded economic growth, hindering the effective delivery of public services and other development outcomes.

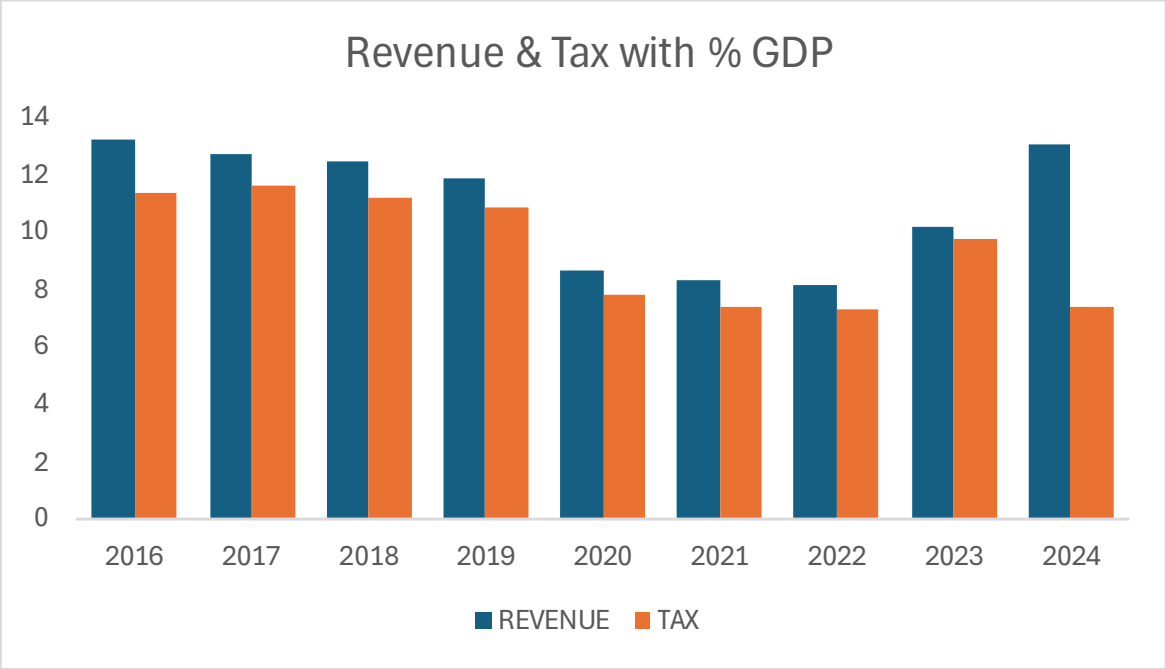


Figure #1 : Sri Lanka revenue & tax with GDP %

In Sri Lanka, like many developing economies, optimizing tax revenue remains a persistent challenge due to structural inefficiencies, tax evasion, a large informal sector, and limited administrative capacity. Despite numerous tax reforms over the years, Sri Lanka continues to face a widening fiscal deficit, exacerbated by economic shocks, political instability, and a shrinking tax base.

In this context, **presumptive taxation** has gained attention as a potential tool to enhance tax compliance and broaden the tax net, particularly by targeting the informal and hard-to-tax sectors. A presumptive tax system estimates tax liability based on indirect indicators such as turnover, assets, or industry norms, rather than actual income, thereby simplifying tax assessment and reducing compliance costs.

The effectiveness and efficiency of presumptive tax methods in optimizing revenue collection remain under-explored in our country. Moreover, balancing equity, simplicity, and revenue sufficiency poses a significant policy challenge.

This research seeks to explore how presumptive taxes can be better designed and implemented to optimize revenue generation in Sri Lanka, with particular emphasis on administrative feasibility, taxpayer compliance, and the socio-economic characteristics of target groups.

1.2 Problem Statement

Sri Lanka faces a persistent challenge in mobilizing sufficient tax revenue to meet its public expenditure needs, especially amidst growing fiscal deficits, mounting debt, and economic instability. Despite many ongoing tax reforms, country's tax-to-GDP ratio remains low compared to regional and global standards, largely due to inefficiencies in tax administration, widespread tax evasion, and the dominance of an informal economy.

Traditional income-based taxation methods have proven inadequate in capturing revenue from small businesses, informal sector operators, and self-employed individuals who often lack proper accounting records. In order to address this issue, presumptive taxation which involves estimating tax liability based on indicators other than actual income has been introduced in many countries to simplify tax compliance and increase revenue from difficult-to-tax groups. While Sri Lanka has made limited use of presumptive tax measures, their scope, design, effectiveness, and impact on revenue generation remain underexplored.

The graph below shows the informal economy sizes of regional countries.

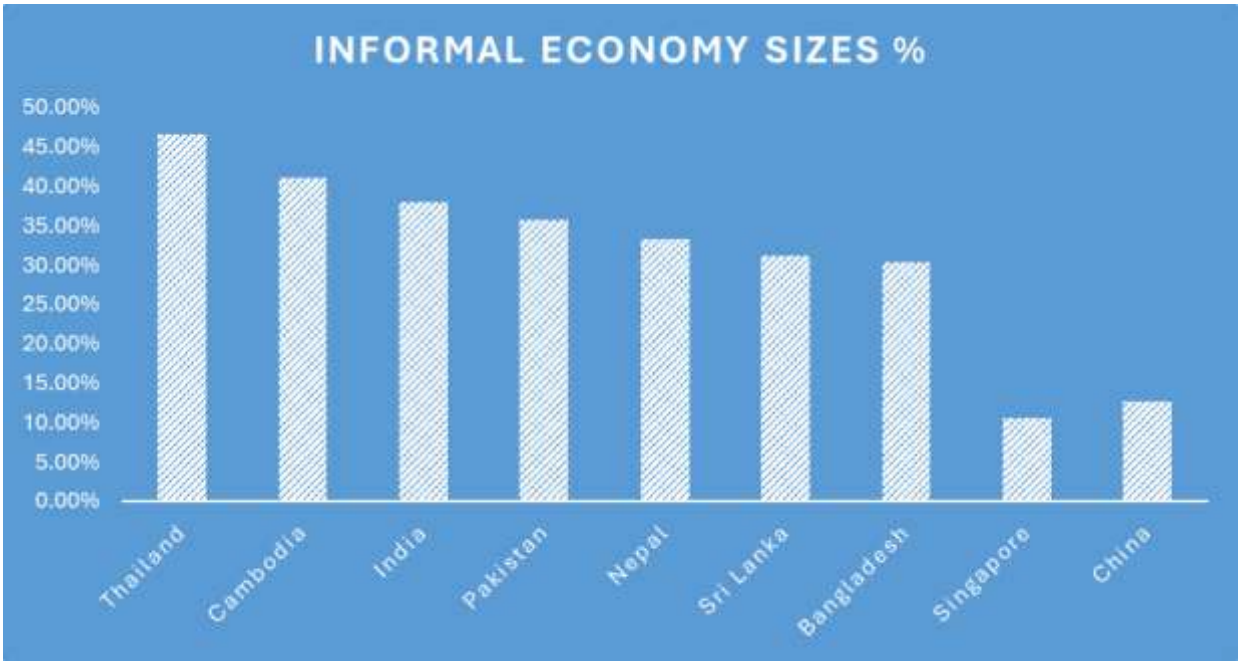


Figure #2: Informal sector percentage of the regional countries

There is limited empirical evidence on how presumptive tax systems can be optimized to suit the Sri Lankan context, particularly in a way that balances revenue generation with fairness, simplicity, and administrative efficiency.

This gap in knowledge poses a significant challenge for policymakers aiming to broaden the tax base, reduce tax evasion, and increase compliance without placing undue burden on small taxpayers. Hence, there is a pressing need to critically examine the role of presumptive taxation in Sri Lanka's revenue system and explore ways in which such mechanisms can be refined and effectively implemented to optimize revenue collection.

1.3 Objectives of the research

While presumptive tax regimes have been widely studied and implemented in various developing countries such as Kenya, Pakistan, and India, **there is a notable lack of academic research and policy analysis specific to Sri Lanka**. Existing literature on Sri Lankan taxation focuses primarily on tax policy, fiscal deficits, VAT and income tax reforms, but offers **limited insights into alternative taxation methods** targeting the informal sector and SMEs.

Moreover, **no comprehensive study currently evaluates the effectiveness of presumptive taxes** in Sri Lanka in terms of revenue yield, compliance behavior, administrative efficiency, and economic equity. The gap also extends to a lack of comparative analysis between Sri Lanka's approach and international best practices, leaving policymakers without a clear framework for improving or scaling up presumptive tax systems. This study aims to fill this gap by exploring the potential of presumptive taxation to optimize revenue generation in Sri Lanka, thereby contributing to both academic literature and practical policymaking in tax administration and reform.

It is further revealed that governments increase their tax revenue through the taxation of the informal economy, (www.Sunday times.lk,14th July 2024) although the revenue yield is very insignificant (Fjeldstad, 2013; Mpapale, 2014).

1.4 Significance of the study

Informal businesses like online, freelance consultants earn higher income which has comparatively high profits. When these businesses are brought into informal businesses a higher amount of tax revenue can be generated. Furthermore, detecting unreported income and activities will not guarantee compliance in the future. Economically, it makes no sense to invest a large amount of resources in moderately small tax revenue. The extant literature shows that most of the income

generated in the informal economy is far below the taxable threshold, which is why this sphere has always been ignored. To ensure the reduction of this sector, there is a need to design a tax system that discourages people from moving into the informal economy.

Various authors have Identified different factors such as the use of cash transactions, lack of proper records, level of illiteracy and political considerations that make it difficult for tax authorities to collect taxes from the informal economy. Without information, identifying potential taxpayers and assessing their tax obligations will be difficult. Close analysis of the extant literature shows that there is no solid research that provides a qualitative analysis of the factors that influence the presumptive tax; thus, this article is aimed at determining the factors influencing presumptive tax collection.

2 Literature Review

This study adopts qualitative research to explore factors that influence presumptive tax collection in Sri Lanka. The central aim is to gain an in depth understanding of attitudes perceptions institutional challenges policy gaps and behavioral dynamics among key stakeholders including tax officials and tax consultants. The qualitative methods are most appropriate as they consist of exploratory nature of the research, understanding the practical challenges in tax collection. It also allows for context sensitive exploration. Since the research has lack of quantitative data and the research priorities understanding why and how behind tax collection challenges rather than measuring the frequency or extent of the issues.

Various researches conducted in Sri Lanka and South Asia mainly covered on formalization of informal businesses in Sri Lanka (De Mel, Mckenzie woodruff, 2012), Informal sector and the economy in Sri Lanka (S.M.P Senanayake et el, 2015), Taxation underground economy and economic performance (Sineth Kannangara et el, 2024), Informal employment or informal firms Regulatory enforcement and the transformation of the informal sector (Sanjay Jain;2024). The research area of Presumptive taxation which mainly targets informal businesses are not catered in Sri Lanka and South Asia.

2.1 Presumptive Taxation

The presumptive tax system, which involves collecting taxes from the informal economy, does not provide a summary of different taxes collected from different informal economic activities. All the taxes collected from various informal activities are collectively classified as “presumptive taxes”. This means that there is a lack of essential information for comparison purposes, and this lack of information will lead to misappropriation of funds because of the absence of taxpayer information.

Tax authorities implemented the presumptive tax system due to a lack of 'costless information for one of the parties.

The presumptive tax systems are commended for their simplicity to facilitate administration. However, Tax officials worldwide face major challenges in taxing the informal economy (IMF, 1996). Such challenges include complexity in terms of rules and tax bases, tax uncertainty, scope (too wide or narrow) and lack of data and analysis

A Large economy is often considered to be a major obstacle in the implementation of income taxes in developing countries (Memon. 2013) and a lack of appropriate compliance and a voluntary compliance tradition facilitated the rapid development of the underground economy in many developing countries (Engelschalk 2015) The idea that small businesses have a greater opportunity for tax evasion than formal business is also well documented (Ogembo 2018)

The rationale behind the use of presumptive tax systems is to reduce taxpayers' compliance costs and administration costs of compliance, enhance enforcement management, and facilitate transition from informal to formal activities (Pashev 2006)

It is prudent that revenue authorities should be familiar with these challenges when designing informal tax policies (OECD, 2020). Fjeldstad (2013) and TRA (2010) observe that the challenges associated with the taxation of the informal economy should be examined from a compliance perspective. There are factors that drive/foster tax compliance and tax law applicable to both informal and formal economies (Fjeldstad, 2013). In other words, the literature identifies three areas that influence taxpayer behavior: tax policy, tax administration and independence of the tax system.

Three main types of presumptive tax system have been identified from the findings about the presumptive tax system from 20 articles selected analyzed for the purpose of this study: (1) lump-sum tax systems, under this initial type of lump sum tax systems by introduce a separate tax law This method can be adopted for lump-sum license fee and patent by paying a fixed amount If any businesses where income cannot be assessed properly this method should be adopted (2) Turn over/Gross income tax system, under this method income tax businesses like mobile sellers and pavements sellers by charging different rates to different business activity and (3) Third party tax reporting Systems Finally the third party reporting should be used for which business records are not usually available **(1.3)** Under the lump-sum tax system taxpayers pay a fixed amount per period (quarterly, semi-annually, or annually) based on an individual's profession or trade. The Gross income or turnover based tax systems can be structured in different ways. One alternative is to apply the same tax rate to all businesses subject to the tax irrespective of business activity. A second alternative is to divide the small business community into a number of business segments with different tax rates for individual segments. This takes into account the different profit margins in business segments. The third alternative is to introduce a progressive tax on gross income where different tax rates are applicable to different levels of gross income. The third type is the third party reporting system which is evaluated against the characteristics of taxpayers

targeted, thresh holds in place and time frame of use. Since small business records are usually not available, the demand for third party information to reconstruct small business income has gradually increased.

3 Methodology

Many prior studies on taxation in informal economies have applied quantitative methods and very little attention has been given to stakeholders' perceptions of the determinants of presumptive taxes, which has been identified as a significant gap in literature.

This article adopts qualitative research and exploratory research design to understand the factors that affect the collection of presumptive taxes in Sri Lanka. The qualitative research approach attempts to gather non-numerical data in the form of interviews. **Primary Data obtained from semi-structured interviews** with government officials and experts. These data were analyzed by grouping into different themes or sub themes (thematic analysis) (Braun & Clark 2021). This approach provides insight and understanding of the phenomenon and provides room for data triangulation. In this study the researcher has selected a population comprises senior officials of the Department of Inland Revenue of Sri Lanka including Senior Deputy Commissioners, Commissioners and Assistant Commissioners. In addition, Tax Consultants have also been interviewed actively/directly involved in the process.

The researcher has sought views from the informal economic sector associates, academics and other Government officials to establish the factors leading to poor revenue performance from the informal economy. The participants were chosen based a purposive study on the field they were expertise and their experience in tax policy as well as informal economic issues. A total of 15 participants were interviewed for this research study. The rationale for selecting 15 participants in this study was that it is in line with the guidelines for a qualitative sample of 15 for suggested by Guest et al. (2020). The researcher assumed that interviewing 15 participants would enable the researcher to study a saturation level which is a key ingredient in qualitative research (Mason, 2010). This allowed the researcher to manage complexity of the analytic task (Vasileiou et al., 2018 p, 2). The interviews of 15 participants revealed diverse opinions of which all significant issues were identified.

3.1 Data Collection

The primary data were collected through direct interviews to elicit detailed information on the factors influencing presumptive tax collection Sri Lanka. Initially an interview guideline was developed along with a questionnaire based on documentary analysis. Policy documents**,** official documents, were examined to guide the sampling procedure, structured interview questions and clarify any discrepancies that may be found (Saleheem, 2013). To understand the underlying issues that restrict the officials of department of Inland Revenue from effectively collecting presumptive taxes from informal economies, unstructured interviews with relevant stakeholders are integral to the success of this research. Here samples mainly consist of sector associates' academics, Staff of Inland revenue department and tax consultants. As the research, it uses persuasive and stratified sampling to ensure representations from all key stakeholders. In addition, samples selected from each group based on their relevance and experience with presumptive tax system.

The interviews serve as a reliable source of data about 1) the operation of the informal economy. The data collection process lasted approximately three months and was conducted during the latter part of December 2024, and the beginning of January 2025. The interviews were conducted in both English and Sinhala. All the questions were asked by the researcher, and the responses were given in Sinhala. The researcher clarified as and when required. The responses were written in English and checked with the interviewee for accuracy.

An in-depth literature review was used as a secondary source of data. A literature review involves the collection of data through the perusal of publicly available documents such as government circulars, press statements, magazines, media reports, journals and government publications. Document analysis enabled the researcher to understand the contemporary tax framework of informal economy, identify the participants and gain knowledge of the phenomenon in the digital era. Document analysis was used in conjunction with interviews as the means of triangulation to provide a confluence of evidence that affords credibility (Bowen, 2009, p. 28)

To reduce potential bias, the researcher combined the findings from interviews and documentary reviews.

3.2 Data Analysis

Thematic Analysis is a widely used method for analyzing qualitative data obtained from sources like interviews, focus group discussions, or text data, to identify, analyze, and report patterns (or "themes") within the data. It is particularly useful for understanding people's experiences, perceptions, or behaviors. Thematic analysis is flexible, allowing researchers to use both inductive approaches (where themes are derived directly from the data) or deductive approaches (where themes are driven by pre-existing theories or concepts

The analysis begins with data familiarization by researcher. The answers provided by interviewees are examined in depth to gain an understanding of the content. This is followed by generating the initial coding process. The next stage would be searching for themes: grouping related initial codes into potential themes. As a result, thematic analysis was adopted in this research.

Interviewee	Designation	
T1	Assistant Tax commissioner	Inland Revenue Department – Colombo
T2	Commissioner	Inland Revenue Department – Colombo
T3	Deputy Tax Commissioner	Corporate Unit – Inland Revenue Department Colombo
T4	Deputy Tax Commissioner	Recovery Regional Department – IRD -Dambulla
T5	Commissioner	Special Investigation Unit – IRD Colombo
T6	Commissioner	IRD – Colombo. – Involved in Research & Development
T7	Tax commissioner	Inland Revenue Department - Jaffna
T8	Assistant Tax Commissioner	Inland Revenue Department – Jaffna

T9	Commissioner	Transfer Pricing – IRD – Colombo
T10	Deputy tax Commissioner	IRD – Badulla
C1	Tax Consultant / Lecturer	Tax Consultant of an Audit Firm – Colombo
C2	Tax Consultant	Freelance Tax Consultant – Colombo
C3	Tax Consultant	Tax Consultant of an Audit Firm – Jaffna
C4	Tax Consultant	Tax Consultant – Australia
C5	Chartered Accountant (Passed Finalist)	Audit Trainee of a Audit Firm

Table # 1. Theme Summary

Theme	Subtheme	Participant supporting (n)	Participant Role	Data Sources
Institutional factors	Organizational Capacity	N=9	IRD Staff 6 Consultant 3	Interviews, IR Annual Repor
Institutional Factors	Financial Capacity	N=7	IRD Staff 5 Consultant 2	Interviews
Intuitional Factors	Commitment and Support	N=8	IRD Staff 5 Consultant 3	Interviews
Governance	Cooperation - Stakeholder	N=10	IRD Staff 6 Consultant 4	Interviews
Governance	Political Interference	N=15	IRD Staff 10 Consultant 4 Audit Trainee 1	Interviews, Bu Speeches
Governance	Policy Consistency	N=12	IRD Staff 8 Consultant 4	Interviews
Legal framework	Enforcement	N=8	IRD Staff 6 Consultant 2	Inland Revenu Act
Legal Framework	Quality of Service	N=15	IRD Staff 10 Consultant 4 Audit Trainee 1	Interviews
Legal Framework	Presumptive Tax Structure	N=5	IRD Staff 7	Interviews

The researcher systematically identifies interesting patterns in the data. The researcher label segments of the data with short, descriptive codes that capture key ideas, concepts and themes. Which are categorized and elaborated below:4

4.Research Results

Theme 1. Institutional Factors affecting Presumptive Tax Collection

Participants consistently identified intuitional constraints within the Department of Inland Revenue (IRD) as a major influence on presumptive tax collection. Three sub themes emerged as follows

1.1 Organizational Capacity

1.2 Financial Capacity

1.3 Commitment and support.

1.1 Organizational Capacity

Several participants (n=9) perceived that organizational weaknesses within the IRD hinder effective tax administration. These weaknesses were described in terms of politicization, lack of transparency and staff capacity issues, including corruption and weak internal controls

Participant **A participant (T1)** emphasized the importance of information sharing and digitalization across state institutions:

"The information should be shared by various stakeholders in order to tax accurately. The digitalization of many state sector organizations provides automatic transfers of information".

Similarly, another **participant (T2)** perceived digitalization as reducing unethical practices within IRD:

"The digitalization helped the Department of Inland Revenue to revenue mobilization in Sri Lanka. As it was initially constrained by lack of agreed procedures, possible misuse and other illicit activities. However, digitalization has eliminated unethical activities illicit activities etc. to a greater extent".

However, other participants highlighted unintended institutional consequences of administrative restructuring. For example, **Participant (T3)** observed that responsibilities for managing certain informal economic actors, such as street Vendors, had shifted away from the IRD to divisional secretariats, which was perceived to reduce the department's direct engagement with the informal economy

Concerns were also raised about the inclusiveness of administrative requirements. One **consultant (C1)** noted that mandatary tax file registration for individuals above 18 years of age was perceived as overly rigid, particularly for those without income or with disabilities.

Overall, participants viewed organizational capacity as closely linked to the department's ability to mobilize revenue, with digitalization perceived as strengthening administrative reach while human resource limitations constraint enforcement.

1.2 Financial Capacity

Participants (n=7) frequently linked weak presumptive tax collection to financial constraints within the IRD, particularly staff shortages and limited training resources.

One **interviewee (T3)** reported that insufficient staffing affected follow up actions on assessments

"Following up of notice of assessments issued, on timely basis by the department of Inland Revenue has not been made due to short age of staff.

Another **Interviewee (T4)** similarly perceived ineffective resource deployment and inadequate training as limiting tax collection efforts, especially within the informal economy**.**

Several respondents expressed the view that the IRD underestimates the revenue potential of the informal economy. Participants suggested that some informal operators, including private practitioners, earn incomes comparable to or higher than those in the formal sector but remain insufficiently assessed.

Overall participants perceived that limited financial capacity restricts the department's ability to recruit skilled staff, conduct research, and engage effectively with informal actors.

1.3 Commitment and Support

Participants (n=8) including all consultants highlighted perceived weaknesses in institutional commitment and frontline motivation. These were attributed to limited incentives, unclear implementation processes, and inconsistent political backing.

On **participant (T6)** described selective targeting of informal businesses that operate from fixed locations, such as payment vendors, noting that licensing requirements were were increasingly used as mechanism for tax collection.

Others linked compliance behavior of perceptions of fairness and government effectiveness. As on Consultant (C2) explained :

"Once the government is perceived to be inefficient and has no capacity to collect taxes from the informal economy, then very few informal economy operators are to comply."

Although respondents acknowledged recent efforts to broaden the tax base, they generally perceived limited institutional commitment to sustaining compliance across the informal economy

Theme 2: Governance Factors Influencing Presumptive Tax Compliance

Governance-related issues emerged as a central theme shaping presumptive tax compliance. Participants identified the following critical factors:

- Cooperation/synergies with other stakeholders ·
- Policy consistency ·
- Political legitimacy and interference.

2.1 Cooperation with Key Stakeholders

Many participants (n=10) perceived weak cooperation between Ministry of finance and the IRD. This was described as leading to administrative delays and policy decisions made without adequate consultation such as the setting of presumptive tax rates.

Participants suggested that these coordination gaps undermine confidence in tax administration and complicate engagement with informal economic actors. It is vital that the coordination among stakeholders will help to effectively tax the informal sector.

2.2 Policy Consistency

Policy inconsistency was widely perceived (n=12) as discouraging compliance. One **participant (T7)** linked frequent policy changes and unclear directives to resistance among taxpayers:

"Poor knowledge of tax policies and the adverse commands contributed to resistance by taxpayers".

Participants further perceived politically motivated tax deductions, including tax reductions, weakened enforcement creditability and encouraged informality. Normally taxes should not be used as political weapons to capture power in a country.

2.3 Political legitimacy and interference

Political interference was consistently reported by all participants (n=15)as a barrier to effective tax collection. Some participants claimed that politicians discouraged tax payment among supporters for electoral reasons.

One **participant (C3)** argued that transparency and visible government accountability were necessary to gain taxpayer cooperation. Others expressed distrust in political leadership, citing perceived misuse of public funds and weak service delivery as reasons for noncompliance.

Participants (n=10) generally agreed that when government legitimacy is questioned, compliance with tax obligations declines.

Theme 3: Legal and Regulatory Framework

Participants identified legal and regulatory conditions as shaping both enforcement capacity and taxpayer behavior. Three subthemes emerged:

- Enforcement of rules and regulations ·
- Quality of delivery service
- The structure of the Presumptive tax system.

3.1 Enforcement of Rules and Regulations

Participants widely perceived (n=8) enforcement mechanisms as inconsistent and selectively applied. Some suggested institutional reforms, such as specialized courts, to expedite tax cases.

One **Interviewee (T4)** described the current enforcement system as follows:

"There should be a special court system formed in order to deal with pending cases to expedite the assessments". This will enable all the pending assessments to be clear within the time bar period

Views diverged on the use of law enforcement agencies in tax collection. While some participants justified police involvement due to safety concerns, others viewed coercive enforcement as undermining trust and long-term compliance

Several respondents noted that weak deterrence and lack of accountability reduce the effectiveness of existing sanctions

3.2 Quality of Service Delivery

All participants (n=15) linked voluntary compliance to perceptions of service delivery. Poor infrastructure, health services, and public utilities were repeatedly cited as reasons for reluctance to pay taxes.

Participants mentioned that tax service quality is often considered to be the availability of public goods and services (service delivery), while the tax structure focuses on the tax base, tax rates and compliance measures.

One **participants, (T7), mentioned:**

"*Tax service quality has a positive impact on voluntary compliance among informal economy operators". In Sri Lanka, people in the informal economy do not see the value of paying taxes due to poor service delivery in towns and cities*.

As another **participant's** response to the above**,**

"*Informal economy taxpayers can comply with presumptive taxes only when they are satisfied with the way in which public funds are used to provide essential social services".*

- A tax official selected as one of the respondents supported the opinion

"Informal economy operators are willing to comply voluntarily but are demanding tangible benefits (payoff rule) from taxes paid. When taxpayers see state-of-the-art infrastructure services such as health care facilities, good schools, clean water and other social amenities, they are motivated to fulfil their tax obligations. Therefore, the government should commit itself to providing tangible services".

Participants emphasized that informal operators were more willing to comply when they perceived tangible benefits from tax payments. Conversely, perceptions of corruption and misappropriation of public funds discourage compliance.

3.3 Presumptive Tax Structure

The tax system structure emerged as a key determinant of the existing tax compliance status within the informal economy. Therefore, based on the assessment, the paper identifies tax rates, penalties, and the complexity of the tax system as the key elements of the tax system.

One commissioner (T7) emphasized that Tax structure should be simplified:

"Taxpayers find it difficult to compute their tax liability, there are various tax sections, subsections provisions and schedules which taxpayers cannot understand; as a result, they should talk to tax consultants which will be an additional cost."

Similarly, presumptive tax noncompliance is influenced by the complexity of the tax system.

One **participant (T9)** stated the following:

"The presumptive tax is based on an estimation of tax liability. Owing to their failure to understand the criteria for estimation and computation, taxpayers may decide not to comply or end up bribing tax officials to avoid paying more"

The complexity and perceived unfairness of the presumptive tax system emered as significant concerns. Participants reported difficulty understanding the tax provisions and calculating liabilities, often resulting in reliance on consultants or noncompliance**.**

Several respondents (n=7) argued that estimated tax bases and high tax rates were inappropriate for low-income informal operators. Ambiguities within tax policy documents were perceived as enabling discretionary enforcement and avoidance

5. Discussion

The results revealed that legal and regulatory factors, institutional factors and governance significantly influence presumptive tax collection. Therefore, to improve the revenue from tax collection the policy makers should implement required legal and regulatory framework, proper institutional requirements and proper governance

The first is institutional factors that influence voluntary compliance of paying presumptive tax This study establishes that a lack of capacity (both human and financial resources) and commitment and support have significantly contributed to poor presumptive tax collection. The Inland Revenue Department of Sri Lanka is understaffed and does not have a budget mobilized tax revenue from the informal economy in Sri Lanka. As the article stated in World bank, 2005 version, The widespread lack of awareness among SMEs suggests a structural communication failure within the tax administration. While presumptive taxes are designed to simplify compliance in order eliminate the lack awareness the SMEs, this benefit is nullified if target groups are not effectively reached. This raises questions about whether simplification alone is sufficient without parallel investments in outreach and trust-building. The resource constraints, which represent barriers to the full roll-out of a presumptive tax regime in Sri Lanka.

The second factor of collection of presumptive tax revenue is credit for governance. According to the empirical findings, policy inconsistency and political illegitimacy and interference are associated with tax revenue collection inefficiency. The participants' responses revealed that political interference and policy inconsistency lead to inefficient presumptive tax revenue collection. The third factor is related to legal and regulatory frameworks, that is, the enforcement of rules and regulations, the quality of services and the

presumptive tax structure significantly impact presumptive tax collection. Policymakers face a trade-off between increasing revenue through presumptive taxes and maintaining fairness. A flat presumptive rate may boost administrative simplicity, but it risks being regressive, placing a disproportionate burden on micro-enterprises while allowing relatively larger informal firms to underpay. This raises the issue of whether a tiered presumptive tax, though more complex, could better align with equity goals.

6 Conclusion

This study has explored the key factors that influence the effectiveness of presumptive tax collection in Sri Lanka through qualitative methods (interviews, focus groups, document review). Several interrelated issues have emerged. This article concludes that the constant low tax revenue from the presumptive tax system in Sri Lanka is affected by several factors, such as institutional factors, lack of legal and regulatory frameworks, and governance and political factors.

However informal economy remains a potential revenue base in Sri Lanka. This article has established that taxing the informal sector is beneficial. However, it is a daunting task due to lack of administration capacity, complicated laws and rates and transparency and accountability. In addition, innovative methodologies should be adopted like gamification, conducting awareness programs to increase taxpayers' Further knowledge, develop mechanisms to capture online businesses and so on.

This study recommends that the government should develop a proper tax system and phase out cash in the payment system and involve e-transactions to ensure the traceability of all financial transactions in real time. Furthermore, the government should invest in public infrastructure, like hospital services, facilities, roads and hospitals, among others, to gain citizenry trust.

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