

Pre-Budget Seminar 2019-20

Karachi Tax Bar Association

Federal Sales Tax

06 May 2019

Presented by:

Saud-ul-Hassan
Director - Tax



EY Ford Rhodes
601 Progressive Plaza, Beaumont Road
Karachi 75530, Pakistan
+92 (0)21 3565 7677

Adoption of a Full Fledged VAT

- ▶ Conceptually Value Added Tax (VAT) system is adopted for documentation of economy.
 - ▶ **Presently the ST Act is a blend of numerous:-**
 - ▶ exemptions; zero-rating, subsidized / reduced rates;
 - ▶ fixed tax regimes, extra tax, further tax, value addition tax;
 - ▶ withholding provisions;
 - ▶ various restrictions on claiming input tax; and
 - ▶ various special regimes
- **It is suggested that all the above distortions in VAT system should be removed and a full fledged uniformed VAT regime may be adopted.**
 - This step will provide a level playing field for all registered persons and restore their confidence.
 - Ensure proper documentation of economy and a genuine increase in the tax to GDP ratio.

Rate of Sales Tax

- ▶ **Rate of sales tax on goods is 17% which is at a higher side.**
 - ▶ Coupled with various increasing conditions like Further tax, extra tax, minimum VAT etc and
 - ▶ restrictions on claim of input tax, the sales tax cost (effective rate) is further enhanced.
 - ▶ Such outlook on a tax compliant person promotes tax evasion in the masses.
- ▶ **It is suggested that the tax rate may be brought down to 15% and gradually upto 10%.**
 - ▶ The reduced tax rate will encourage the unregistered persons to get themselves registered.
 - ▶ Resulting in broadening of tax base and documentation of economy and
 - ▶ discourage under invoicing, corruption and smuggling.

Harmonization in Sales Tax on Goods & Services

Presently, the scope of goods and services are not clearly determined under the Federal ST and the respective Provincial sales tax legislation. In certain cases it is overlapping including:

1. **intangible movable goods** (i.e. software and other soft contents);
2. **supply of goods involve reasonable consumption of services** (i.e. restaurants, caterers, toll manufacturing); and
3. **mixed nature of contracts** (i.e. turn-key contracts, civil works).

Resultantly, due to such confusion in scope of goods and services, tax authorities are trying to tax such activities being goods and services simultaneously.

It is suggested that tax authorities should **agree on methods or rules, which covers the grey area** in this regard and taxpayers are certain about an activity that whether the same is to be taxed as goods or services.

Friction Between FBR And Provincial Revenue Authorities.

- Federal and Provincial Revenue Authorities have locked horns over **taxation of services such** as Toll Manufacturing, Franchise Services, Restaurants, etc. and on **Cross Border Services**.
- Extreme unrest and problems amongst the business community. This situation is causing a lot of confusion, harassment and litigation.
- It is suggested that the Federal and Provincial Sales Tax **Authorities should form a fully empowered commission to bring harmony** in the sales tax laws dealing with services, particularly focusing on following:
 - (i) Principle for taxation of services (origin, destination or mix);
 - (ii) Mechanism for adjustment of taxes collected by Authorities, without causing botheration to taxpayers;
 - (iii) Harmonization of Tariff headings and definition / scope of services;

Time of Supply - Advance

Section 2(44) of the ST Act provides that a supply, would be considered to be provided at the **event earlier of-**

- The time at which goods are **delivered or made available** to the recipient of supply, or
- The time when any **payment is received by** the supplier in respect of that supply.

There are neither any procedures for payments of sales tax on advance nor adjustments through returns are prescribed which has resulted in unnecessary problems in payments and adjustment of sales tax on advance

This is also causing discrepancies in CREST system.

There appears to be no revenue-benefit from such exercise.

It is suggested that the previous position for chargeability of sales tax at the time of delivery may be reverted back.

Tax Credit not allowed – SRO 490(I)/2004

The list of taxable purchases against which input tax adjustment is not allowed was enhanced in 2013, (SRO 490(I)/2004) and Section 8(1)(h) to (i) i.e. includes **building materials, office equipment, electrical and gas appliances, wires, cables, etc.**

whereby claim or adjustment of input tax has been restricted by general expressions like-

- **directly used in taxable activity**
- **goods and services acquired for personal or non-business consumption**
- **directly use in the production or manufacture of taxable goods**
- **goods and services not related to the taxable supplies**

It is suggested that the **new list of items increased in SRO 490 should be removed** as the cost of doing business and litigation has been enhanced.

Restrictions on claim of input tax through **general expressions should be removed from section 8(1)**, as it restricts the taxpayers vested right to claim legitimate input tax.

Tax Credit not allowed

- ▶ Further, following anti-avoidance provisions require reconsideration for withdrawal, after the introduction of STRIVE:
- ▶ **Section 8 (1) (ca)**-----Goods or services in respect of which sales tax has not been deposited in the Government treasury by the respective supplier.
- ▶ **Section 8 (1) (caa)**-----Purchase in respect of which a discrepancy is indicated by CREST or input tax of which is not verifiable in the supply chain
- ▶ **Section 8 (1) (d)**-----Fake invoices
- ▶ **Section 8 (A)**-----Joint and several liability of registered persons in supply chain where tax unpaid
- ▶ **Section 8 (B)**-----Restriction of claiming input tax upto 90% of the output tax – **Specially for manufacturers** during first three years to observe huge input taxes paid of import/purchase of plant and machinery

Extra Tax

- ▶ **Extra tax levied on certain specified goods is not allowed as input tax.**
- ▶ To reduce the cost of doing business, the KTBA recommends that extra tax should not be levied on goods sold to ‘manufacturers’ for their own use.
- ▶ Through the Sales Tax General Order 27 of 2014, the FBR has exempted the supply of parts and accessories to the automobile manufacturers from the levy of extra tax, however, other manufacturers have not been granted similar exemption.
- ▶ The bar recommends that similar exemption should also be extended to all manufacturers who are using goods subject to extra tax as industrial input.

Assessment of Tax

- ▶ Section 25 read with 72B authorises tax officers to conduct detailed audit of a taxpayer once in a year.
- ▶ Any observation and issue highlighted during the audit can be assessed u/s 11 of the ST Act.
- ▶ After conclusion of audit, provision to Section 25 allowed the Commissioner to initiate investigation u/s 38 in case of sufficient information in hand for conduct of tax fraud.
- ▶ In spite of that tax officers often issued Showcause notices u/s 11 directly on frivolous and intangible basis.
- ▶ The Bar proposes that an amendment should be made in section 11 to the effect that no show cause notice shall be issued unless the sufficient information of tax fraud is available with the tax officer.

Registration

- Presently, approval process for sales tax registration takes at least 60 to 120 days to be completed which is so long. considering that making supplies without registration is 'tax fraud'.
- Moreover, in order to obtain sales tax registration, the taxpayer is required to file Form 181 on the IRIS web portal whereby the option of registration for Sales tax is to be selected. After submission of Form 181, the IRIS portal generates Order 181. While the ST Act does refer to form TRF-01 to apply for registration, currently, there is no specific mechanism is available on eFBR sales tax portal which makes the process cumbersome.
- Unnecessary delay in sales tax registration, results in huge losses to the applicant who wants to do business and due to departmental delays, a lot of time is wasted due to which not only genuine taxpayer suffers but FBR is also unable to collect tax.

Registration

- Complicated processes to apply for sales tax registration, results in unnecessary delays which result in losses to the taxpayer who is unable to do business prior to obtaining the registration. Genuine taxpayers suffers and FBR is also unable to collect tax.
- The Bar proposes that the sales tax registration process should be expedited.
- The facility of temporary registration should also be allowed to persons other than manufacturers as they also face same period of delay in registration process.
- The temporary registration should also be extended to manufacturers who already have installed machinery, purchased from local market.
- Moreover, persons who have been given temporary registration should be allowed to make taxable supplies and issue sales tax invoices so that business may be commenced by the person and sales tax is deposited on timely basis.
- Moreover, separate process should be introduced on the eFBR sales tax portal to speed up the registration timeline.
- Speedy process of registration shall result in generating timely revenues for FBR.

De - Registration

- At present finalization of sales tax de-registration process take at least 6 to 10 months and in some cases more than one year.
- Taxpayers suffer from uncertainty, mental torture and suspense about the fate of their cases.
- The process of de-registration should be completed within three months. If the application for de-registration is not disposed of within the prescribed time period then applicant be considered as de-registered automatically.

Revision of Sales Tax Return and Time Limit

- The revision of Sales Tax Return for any error (transposition or otherwise) or omission is subject to the prior approval of the Commissioner Inland Revenue within 120 days of filing of original return.
- It has increased the discretionary powers of the Commissioner Inland Revenue and cause of corrupt practices as permission is not granted for months. Even for minor corrections in the return form, several repeated visits to the tax office are required which are not only cumbersome but are also hectic.
- Provisions for auto revisions, particularly in the regime of e-filing, may be restored where there is no decrease in tax liability and/or increase in refund claim to address the problems faced by genuine taxpayers in simple issues where no issue of tax benefits involves.
- Further, time limit of 120 days for applying revision of return may be deleted as this is against the principles of equity and natural justice.

Thank You