
# Pakistan Tax Bar Association



# Proposals
# Federal Budget
# 2014-15

# C O N T E N T S


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## 1. Broadening of Tax Base

Pakistan Tax Bar Association is of the firm view that the challenge government faces is not how to increase current tax revenues, but how to widen the tax base to prevent tax-revenue erosion in the future. Year after year we keep on talking about the need to broaden the tax net yet we continue to struggle with a shockingly narrow tax base. Although a considerable section of our population pays taxes in our country through withholding tax and indirect taxation. Yet measurement of a true tax base is important because the mobilization of tax revenue has a direct nexus with the number of taxpayers participating actively in the system set up to collect taxes. A countries tax system cannot continue be dependent on adhoc collection of taxes that has often no nexus to the individuals' real income. Since many years, Pakistan's registered tax base has been more or less stable at just around 1% of the total population.

### PROPOSALS

The Federal Board of Revenue (FBR), in the recent past has made result oriented effort in this direction. However, in order to broaden the desired tax base, to minimize the avenues to evade tax, to document the economy, reducing tax burden on the existing taxpayer to create a fairer society and to generate more employment opportunities, following steps are suggested:-

(i) Complete details and data base of all the owners/ holders/allottee of the property (including residential, commercial, industrial), cars, club membership, international traveling, utilities (including residential, commercial and industrial), vehicles, buses, credit cards, investment in fixed deposits, national saving schemes and stocks be prepared and on the basis of that information a complete profile may be generated and effective use such detail & data base.

(ii) National Tax Number should be made mandatory for purchase/sale/transfer of immovable property (no exemption whatsoever), commercial or industrial utilities connections (present or future) Motor Vehicle, Club Membership, Credit Cards, Registration with CDC and Distribution of Profit/Markup exceeding statutory taxable limit.

(iii) Compulsory submission of quarterly statements by the Registrars & Housing Societies for registration/transfer of Immovable Property (Industrial Commercial, Residential & Agricultural) Motor Vehicle Registration Authorities, Clubs (Private & Public), Credit Card issuing authorities, Central Depository Company, National Clearing Company of Pakistan, large scale private hospitals & schools and Financial Institutions distributing profit more than statutory taxable limited or granted commercial loans; should be made mandatory.

(iv) The exemption from taxation as unexplained income under Section 111(4) of the Ordinance to the foreign exchange brought into Pakistan through proper banking channel should be restricted to home remittances by overseas Pakistanis and only for fresh industrial investment.

(v) On the administrative side we note that there is a loss of focus of the board on broadening of tax base, it is our humble view that the job of broadening the tax base has to be a regular

ritual of the tax administration and should not be left to special initiatives only. **One major problem that we have observed in this regard is the duplicity in jurisdictions assigned to field offices where apart from geographical jurisdictions assigned there are simultaneously several sect oral jurisdictions. This in my view allows the potential smart non filer to get away by refusing to comply by challenging jurisdictions on one pretext or the other. In our view A constant drive is essential for tax broadening and every zone should be assigned targets of adding taxpayers in the same manner as is done for tax collection. The jurisdiction in our view should be for some time be reverted strictly to geographical basis to avoid duplication and slippages of potential tax filers.**

(vi) The taxes must be equitable and fair between different classes of society. Filing of Return for all the segments of the society including professionals like lawyers, accountants, doctors, engineer, architects, designers, even managers etc., having income above threshold should be made mandatory.

(vii) Tax credit at the rate of 5% may be provided to those taxpayers whose 80% purchases are from persons who are registered as Sales Tax and Income Tax taxpayers with the Tax Department and reduction of 5% of Tax Liability to all those class of taxpayers who are regular tax complaint since last more than five years .



## 2. Selection of Persons or Class of Persons for Audit *Section 177*

Presently all returns of income filed, qualify for acceptance under the Self Assessment Scheme irrespective of income or loss declared in the return by the taxpayer and deemed to have been assessed under section 120(l)(b) on the day the return is furnished.

Through Finance Act, 2013, explanations were added to Section 177 and 214C whereby it is being stressed that both these sections are independent provisions and that the commissioners are permitted to call for records of the taxpayer and **conduct the audit.**

There is no dispute whatsoever that both section 177 and 214C are independent sections and that the Commissioners are empowered to call for records and books of the taxpayer and to conduct the audit. However, in our humble opinion the Commissioners are not permitted to select cases under both these sections. Pakistan Tax Bar Association has no objection at all to selection of cases in any number by the FBR whether through parametric or random selection basis. We feel strongly that if cases for audit are selected by the Board, the field offices will be under proper monitoring as to the conduct and outcome of these audits.

It is very unfortunate but a reality that the powers to select cases by the Commissioner is being largely abused at the field offices and provides stimulus to corruption which in turn leaves a bad image on the FBR as an institution and also hampers the drive to expand the tax net. Before the introduction of these explanations and a meaningful synchronizing of selection and conduct of audit was achieved through earlier amendments in Section 177 and introduction of Section 214C.

## PROPOSALS

**(i)** It is therefore strongly urged that to enable fair selection and conduct of audit and to get meaningful results in these audits a policy of selection only by the FBR should be adopted to avoid undue litigation and loss of revenue. The selection of cases should be done by the FBR within 30 to 60 days of close of the filing of return so that ample time is available for conduct of audit and any recovery of taxes before the close of the fiscal year.

The Board may issue immediate internal instruction to vacate / withdraw the cases manually selected by the Commissioner Inland Revenue (CIR) for tax year 2011 and 2012 since the Board has already selected cases through parametric selection.

For tax year 2013 the Board should immediately decide the parameters and carry out selection of cases under Section 214C immediately and till such time direct that any cases selected by the CIR be held invalid.

This in our view will help the FBR in achieving the conduct of audit without facing undue litigation. Further, harassment of existing taxpayers in the garb of unchecked notices being issued to the taxpayers for selection of audit by the Field Officers without any criteria or basis shall be stopped.

(ii) That parameters and criteria for selection of audit should be made part of law which are system-based and laid down on the risk assessment principles. We propose the following criteria for selection of cases for audit:-



**Income Tax**

(a) Continuously Declaring Loss for the last three years. For determining amount of loss for the year, charge on account of depreciation and amortization as per sections 22 and 24 of the Income Tax Ordinance, 2001 shall not be accounted for;

(b) Continuously declaring declined Income for three (3) years;

(c) Where there is a consistent decrease in 'Turnover' by over twenty (20) per cent for three (3) consecutive years;

(d) Where there is a consistent decrease in Gross Profit or increase in Gross loss percentage by over five (5) per cent of the previous year's gross profit or gross loss as the case may be for the three (3) consecutive years;

(e) Where 'Debt to Equity' ratio is consistently below 1:4 (Equity: Debit) for a period of three (3) consecutive years;

(f) Where taxpayer in his return of income taken credit of any sum in excess of 30% of

an amount, which if taxed at a rate or rates would have resulted in tax liability equal to the tax payable in respect of transaction related to import and subject to FTR;

(g) Where claim of Profit and Loss expenditure is over 10% increase from the claim of last year in proportion to the turnover of the current year;

(h) Salaries are equal to or more than thirty (30) per cent of the cost of sales/receipts, excluding service sector; and

(i) Capital work-in-progress is declared at over Rs.50 Million.

**Sales Tax**

I. Where taxable supplies is less than previous years by 20% for three consecutive years;

II. Where net tax is less than 5% in comparison of previous years for three consecutive years;

III. Where registered person is claiming refund consecutively for last twelve months;

IV. Where import or export sales figures differ by 20% from the value of export obtained from Custom's Data;



V. Where there is continuous decrease in the output and input tax ratio for last three years;

VI. Input rate of tax is different from the prevailing rate of Sales Tax; and

VII. Where revise returns have filed for consecutive six months.

(iii) In line with the Repealed Ordinance, one year time limit may be fixed for selection of person for audit of their income tax affairs.

(iv) Time limit for completion of audit proceeding be fixed.

## 3. Rationalization of Tax Rates

Corporate taxes are very high in Pakistan as compare to other developing and developed markets. Following is the list of tax rates of few countries around the world:-

| Country/Region | Corporate Tax Rate | Country/Region | Corporate Tax Rate |
|---|---|---|---|
| Australia | 30% | Malaysia | 25% |
| Austria | 25% | Mauritius | 15% |
| Bangladesh | 27.5% | Netherlands | 20/25% |
| China | 25% | New Zealand | 25% |
| Denmark | 25% | Pakistan | * 35% |
| Egypt | 20% | Russia | 20%(13%forSME) |
| Germany | 29.8% | Singapore | 17% |
| Hong Kong | 16.5% | South Africa | 28% |
| India | 33.2175% | Sri Lanka | 35% |
| Indonesia | 25% | Taiwan | 17% |
| Iran | 25% | Thailand | 30% |
| Japan | 40.69% | Turkey | 20% |
| Kazakhstan | 15% | United Kingdom | 20% for annual profit under£300000 and 25% for annualprofit over £ 300000 |
| Macau | 12% | Vietnam | 25% |



**Companies in addition to corporate tax also pay 7% labor levy i.e. 5% WPPF and 2% WWF. This makeseffective tax rate of 42% for public and private companies**

The present Corporate Tax rate of 35 percent is the highest in the entire region. China, which provides reasonable opportunities for the establishment of manufacturing sector, operates with the rate of tax of around 15 to 20 percent. This is effectively a disincentive to multinational groups for locating their manufacturing base in Pakistan. India, Bangladesh, Malaysia and Thailand have also brought down their corporate rate of tax to around 30 percent.

There are, even, cases where the rate has been brought down to 25 to 28 percent. This level is by and large in line with almost all the OECD member countries where the rate of corporate tax is around 28 percent.

Moreover presently rate of taxes on the higher class of income are not as high as should be. The rich are not contributing their due share of taxes for the betterment of the country.

**PROPOSALS**

Therefore, it is strongly recommended to reduce the tax rates reasonably:-

(i) The rate of Income Tax for the corporate sector be reduced by 5%;

(ii) In order to promote listing of companies it is proposed that the corporate tax rate of listed companies should be atleast 5% less than the non-listed companies;

(iii) Rate of income tax on Individuals (including salaried persons) and AOP should be redesigned in a manner that the persons earning lower income should pay lessor tax in comparison to higher tax earner and higher class of income. Moreover, the concept of marginal relief should also be prescribed.

## 4. Multiplicity of taxes



Presently in addition to the corporate tax of 35% of the Company, it is obligatory for them to pay Workers Welfare Fund @ 2% of the taxable income and Workers Profit Participation Fund @ 5% of profit, which result in tax impact of approximately 42%. These are no different to corporate tax and if they are to be accounted for the total tax rate comes to around 42%.

If the corporate sector is to develop, it is essential that these taxes should be eliminated. The WPPF was introduced to benefit the employees. However, with salary increase, most employees are now above the threshold limit and therefore not entitled to any benefit from this levy. Bulk of the deduction goes to the government. Studies shows that around 75% of the total WPPF charge goes to Government and only 25% is being distributed to the eligible employees. It has come to our knowledge there are approximately 40 Billion funds which are still unutilized.

Manufacturing sector in Pakistan plays a vital role especially in terms of improving the employment statistics of the country and directly contributing towards the GDP, faces in addition to normal taxation, taxes on account of WPPF and WWF which resultantly increases their cost of doing business thus making their products less competitive with importers.

See table below where data has been collected from various countries pertaining to their welfare benefit structure and is clear that except for Pakistan all the welfare benefits are calculated by taking salary/wages as a base rather than the profitability of the company.

| Country | * Pakistan | India | ** Korea | ***Singapore | **Indonesia |
|---|---|---|---|---|---|
| Tax rate | 7% | 0% | 3.4% | Various % | 3.7% |

* ***this includes both WPPF and WWF calculated on the taxable income and profits of the company.***

** ***calculated on employee salary.***

*** ***6% above 60 years, 9% between 55-59 years, 13% up-to 54 years (all calculated on base salary).***

This sort of levy further discourages the existing manufacturers to expand their business in Pakistan and at the same time discourages foreign investors in setting up the manufacturing operations.

**PROPOSAL**

It is therefore proposed that WWF & WPPF may be eliminated in its entirety and instead of further burdening the taxpayer with above levies, an Endowment Fund be created out of existing funds available with the Government of Pakistan under these two heads and whatever profit earned from such endowment fund may be utilized for the benefit of the workers. Utilization of WWF and WPPF by the Company through a Fund (just like Provident Fund) for the benefit of their workers to build schools, hospitals etc may be allowed.



## 5. Revenue Measures/Improvement in Tax to GDP Ratio

(a) From the following statement of sectoral shares in the GDP and Share in Taxes; it will be observed that Government has to show its will to collect tax from all the segment of the economy in accordance with their share in the GDP. It is desirable that PTBA work with Government of Pakistan for increase of tax to GDP ratio:-

| Sectors | 2004-05 | 2008-09 | 2009-10 | 2010-11 | |
|---|---|---|---|---|---|
| | Share in GDP{%) | Share in GDP {%) | Share in GDP {%) | Share in GDP {%) | Tax-to-GDP {%) |
| **Agriculture** | 22.40 | 21.80 | 21.20 | 20.90 | 1.20 |
| **Manufacturing** | 18.30 | 18.20 | 18.60 | 18.70 | 50.80 |
| **Electricity, Gas, Mining &Construction** | 8.00 | 7.10 | 7.90 | 7.10 | 14.00 |

| Sectors | 2004-05 | 2008-09 | 2009-10 | 2010-11 | |
|---|---|---|---|---|---|
| **Transport, Storage &Communication** | 10.40 | 10.20 | 10.10 | 10.00 | 7.60 |
| **Wholesale and Retail Trade** | 18.70 | 16.80 | 17.00 | 18.20 | 6.40 |
| **Finance and Insurance** | 6.00 | 7.70 | 6.90 | 6.90 | 5.00 |
| **Other Services** | 16.20 | 18.20 | 18.30 | 19.20 | 15.00 |
| **Total** | **100** | **100** | **100** | **100** | **100** |
| **GDP for the year in real term** | **4,593,230** | **5,475,716** | **5,681,531** | **5,817,406** | |

It may be noted that while the manufacturing sector contributes

(b) Following exemption available for withholding of tax u/s.148 of the Ordinance may be reviewed and appropriate tax may be levied:-

| Clause | Item |
|---|---|
| 56 of Part IV of 2nd Schedule | Goods classified under Pakistan Customs Tariff falling under Chapter 27. |

(c) A clear distinction should be made between the taxpayer and non-taxpayers by imposing higher rate of taxes. For example the withholding tax under section 231A collected from the existing taxpayer be withdrawn; however from non-taxpayers it should collected @ 1% of the cash amount withdrawn from bank.

(d) Adjustable withholding tax may be imposed on the following transactions:-

(i) **Purchase of Motor-Vehicle.** Advance tax to be collected by the automobile companies;

(ii) **Transfer of Immovable Properties.** Advance tax to be collected by the Registrar and housing societies;

(iii) **Grant of new membership or transfer of membership of Private Clubs.** Advance tax to be collected by the Clubs; and

(iv) **On issuance of Credit Card or renewal of the same.** Advance tax to be collected by the issuing authorities.

(v) **Transfer of properties/plots by the Mukhtarkar, Societies, Local Authorities and Registrar.**

Advance tax to be collected by the transferring authorities.

## 6. Final Tax Regime (FTR)

Tax administrators all over the world and particularly in the developing countries like Pakistan face major problems of non-reporting and under-reporting of income. Government has experimented various liberal Self Assessment Schemes; with the objective of encouraging voluntary compliance encompassing virtually all the taxpayers including limited companies irrespective of income level, but in my humble view the confidence reposed in the taxpayer was not fully responded.

The withholding tax and presumptive tax regime are not new and the earlier was initially introduced in the Income Tax Act, 1922 as Section 18(3BB) and the scope of these provisions were further extended through Income Tax Ordinance, 1979. But from 1980 onward and especially in the last two decades, the Withholding and Presumptive Tax Regime have come into full force with the object to have voluntary compliance and increasing revenue generation at low administrative cost. The law which weaved indirect taxes into direct tax texture has resulted in distortion of principle of taxation of real income and it's taxability on the basis of liability to pay in progressive manner.

Through Finance Act, 2012 positive steps have been taken for opting out of presumptive tax regime in respect of Sale of goods, Import of goods and Export of goods, subject to certain conditions, which is highly appreciated. Similar positive steps are also required to be taken in respect of Execution of Contracts (U/S 153(1)(c)), Brokerage and Commission (U/S 233), Goods Transport Vehicles Plying for Hire (U/S 234) and CNG Stations (U/S 234A).

**Recommendations:**



- As a transitional measure, for all corporate taxpayers current final tax regime should be converted into minimum tax, with facility to carry forward such minimum tax for immediate five succeeding tax years to adjust against tax liability determined on taxable income.

- Alternatively, the corporate sector be given option to opt out from presumptive taxation.

- The benefit of opting out of presumptive tax regime be extended to Execution of Contracts (U/S 153(1)(c)), Brokerage and Commission (U/S 233), Goods Transport Vehicles Plying for Hire (U/S 234) and CNG Stations (U/S 234A) as well.

## 7. Facilitation of taxpayerError! Bookmark not defined.

It is therefore proposed that effective departmental check may be prescribed in the law.

**Toughest mode of recovery of tax & problems in refund of tax**

The Ordinance has been very tough against the taxpayers in case of recovery of tax due from them. There are a number of provisions in the Ordinance whereby the Commissioner has been empowered to proceed to recover the tax due from the taxpayer by one or more of the modes provided therein. The modes operandi for recovery of tax include recovering the tax through attachment and sale of property, rights to arrest of taxpayers and taxpayer detention

in prison for a maximum period of six months, seizure of bank accounts, imposition of penalties and additional tax etc.

The taxpayers feel great disappointment when the department find that the revenue takes appropriate care to safeguard their interests in the Ordinance; on the other hand the taxpayers' interests or rights generally and particularly in respect of obtaining the refund of tax paid in excess to the amount they are chargeable to tax under the Ordinance are not adequately taken care by the department.

**It is proposed that:**

(a) Section 170(4) may suitably be amended in view of the above proposed amendments, particularly substituting the 60 days with 15 days within which the Commissioner shall pass the order, and in case of his failure to pass the order within the stipulated period of 15 days, the refund application be deemed to have been accepted by him.

(b) Provision be made in section 170 (2)(c); whereby the Commissioner may be authorized to admit an application made after the expiry of the stipulated period of 2 years on genuine reason.

**Time limit of filing of Annual Tax Returns**



The due date for filing of income tax returns by salaried individuals by 31 August is too short for compiling the required information and obtaining proof and evidences. Earlier, the deadline was 30 September.

Past experience shows that the Income Tax Return forms etc. are not notified well in time and the e-filing system is also not in place in time. On the other hand our history is that the due date of filing of Income Tax Returns etc. is always extended on one pre-text or other.

The institute feels that delay in finalizing the Income Tax Return forms etc. and extension in due date of filing of Income Tax Returns etc. causes un-necessary burden of last minute rush of work.

## PROPOSAL

Due date for filing of Income Tax Return by salaried individuals, non-salaried individuals and AOP's be aligned to 30 September or 60 days from the date the e-filing system is in place, whichever is later.

**Filing of Monthly Statements of Withholding of Tax**

Every person collecting or deducting tax is required to furnish the monthly statement by 15th day of the month following the month to which in withholding pertains. Moreover, the date for filing of monthly sales tax return is also 15th day of the month.

## PROPOSAL

It is proposed that date for filing of monthly statement under Section 165 be changed to 25th day of the month following the month which in withholding pertains.

**Deductions not allowed**

The Finance Act, 2006 substituted Clause (I) of Section 21 whereby:-

(L) any expenditure for a transaction, paid or payable under a single account head which, in aggregate, exceeds fifty thousand rupees, made other than by a crossed cheque drawn on a bank or by crossed bank draft or crossed pay order or any other crossed banking instrument showing transfer of amount from the business bank account of the taxpayer-Provided that online transfer of payment from the business account of the payer to the business account of payee as well as payments through credit card shall be treated as transactions through the banking channel, subject to the condition that such transactions are verifiable from the bank statements of the respective payer and the payee:



Provided further that this clause shall not apply in the case of-

(a) expenditures not exceeding ten thousand rupees;

(b) expenditures on account of-

- (i) utility bills;
- (ii) freight charges;
- (iii) travel fare;
- (iv) postage; and
- (v) payment of taxes, duties, fee, fines or any other statutory obligation.

## PROPOSALS

The single account limit of PKR 50,000 may be enhanced to 250,000.

The limit of Rs.10,000/- in Section 21(L) and Rs.15,000/- in Section 21(m) be enhanced to Rs.50,000/-and Rs.75,000/- respectively.

**Payments for Goods and Services**

**(a) Time limit for Order u/s.153 and Appeal thereof**

Section 153(4) provides that the Commissioner may, on application made by the recipient of a payment referred to in sub-section (1) and after making such enquiry as the Commissioner thinks fit, may allow in cases where tax deductible under sub-section (1) is adjustable by an order in writing, any person to make the payment (a) without deduction of tax or (b) deduction of tax at reduced rate.

The above provision of law is very positive and encouraging but it would be appropriate if some time limit is fixed for passing an order under this sub- section. It would also be in the interest of justice and equity, if a reasonable opportunity of being heard is granted to the taxpayer before any adverse order is being drawn by the Commissioner.

**PROPOSAL**

(I) Sub-section (4) be substituted with the following:

*"The Commissioner may, on application made by the recipient of a payment referred to in sub-section (1) and after making such enquiry and providing a reasonable opportunity of being heard to the applicant if he thinks fit, may allow in cases where tax deductible under sub-section (1) is adjustable by order in writing within fifteen days from the date of receipt of application, any person to make the payment without deduction of tax or deduction of tax at a reduced rate."*



**(b) Increase in threshold for withholding of tax**

Clause (xii) (a) and (b) of SRO 586(I)/91 dated 30th June, 1991 provides that the provisions of Subsection (4) of section 50 of the Income Tax Ordinance, 1979 (Section 153 of the Income Tax Ordinance, 2001) shall not apply to the following persons receiving payments:-

(i) not exceeding rupees twenty five thousand on account of supply of goods, in a financial year; and

(ii) not exceeding rupees ten thousand on account of services rendered or execution of a contractor, in a financial year.

The above limits of Rs.25,000/- and Rs.10,000/- were fixed almost fifteen years back and require to be enhanced.

**PROPOSAL**

The amount of Rs.25,000/- on account of supply of goods and Rs.10,000/- on account of services rendered or execution of contract may be increase to Rs.200,000/- and Rs.100,000/- respectively.

**(c) Exemption from withholding tax payment covered under the Presumptive Tax Regime**

There are number of services under the Presumptive Tax Regime like Commission earned by the Indenting Commission Agents, Advertising Agents, Yarn Dealers, CNG Stations, etc. On the one hand the taxes deducted on their incomes constitute full and final tax liability and on the other hand their clients while making payments to them are also deducting tax under section 153, which unnecessary creating hardship for them and refund as well.

Keeping in view the similar problem being faced by the travel agent; Clause 43(B) was inserted in Part IV of the Second Schedule by the Finance Act, 2007, which provides that the provisions of clause (a) sub-section (1) of section 153 shall not apply to payments received on sale of air tickets by traveling agents, who have paid withholding tax on their commission income.

**PROPOSAL**



We therefore propose that similar facility should also be allowed to the taxpayers in respect of services rendered by them Indenting Commission Agents, Advertising Agents, Yarn Dealers, CNG Stations, etc.

**Tax Incentive for Handicap Taxpayer**

Clause 1A of Part III of the 2nd Schedule provides that where the taxable income, in a tax year, of a taxpayer aged 60 years of more on the first day of that tax year does not exceed. Seven hundred fifty thousand rupees, his tax liability on such income shall be reduced by 50%.

**PROPOSAL**

We propose that the similar incentive may also be announced for the Handicap taxpayers as well.

**Marginal Relief for Business Individuals**

Currently the benefit of marginal relief is available to the salaried individuals. It provides a great benefit to those who marginally cross the higher tax rate slab.

**PROPOSAL**

It is proposed that this relief may also be provided to the business individuals in order to improve the business activity and level playing field for both business and salaried class individual.

**Payment of Tax Collected or Deducted**

Clause (b) of Rule 43 provides that where the tax has been collected or deducted by a person other than the Federal Government or a Provincial Government, the same shall be paid to the Commissioner by way of credit to the Federal Government by remittance to the Government Treasury or deposit in an authorized branch of the State Bank of Pakistan or the National Bank of Pakistan, within Seven days from the end of each week ending on every Sunday. This provision of law has enhanced the work load of tax collecting agents many fold; who are working for the Government without any remuneration.

**PROPOSAL**

It is proposed that the taxpayers be allowed to deposit all withholding taxes collected within seven days of the following month.



## 8. Incentives for the salaried taxpayers

**(i) Post Retirement Medical Fund**

As per the income tax law, many of the retirements benefit plans operated by the company, if approved by the Commissioner income tax are not subject to tax at the hands of the beneficiary i.e, the employee and is an allowable expense for the company who maintains the approved funds.

However Medical plans operational by the company are not approved under the ambit of income tax law and hence companies which provide such essential benefits to their retired employees are not entitled to claim these expenses in their tax returns.

**PROPOSAL**

It is therefore proposed that the plans of the medical benefits may covered under the ambit of income tax law and should be duly approved so as to allow companies to claim their legitimate expenses against their income.

The allow ability of these retirement medical benefit plans will encourage companies to provide benefits to their retired employees which will ultimately benefit both the individual and Governments plans to improve the standard of living of its citizens.

**(ii) Taxation of Notional Income**

Under sub-section (7) of section 13 of the Income Tax Ordinance, 2001 the difference between the benchmark rate and the actual rate of interest charged (where actual rate of interest is less than the benchmark rate) by the employers on concessionary loans provided to the employees is treated as perquisite chargeable to tax.

This is not a significant source of revenue for the Government on the one hand and very rigid piece of legislation on the salaried taxpayer on the other hand who are hard hit by the present economic situation. The taxation of this notional income is highly unjust since it taxes the notional income of the salaried person which is against the basic principle of taxation since this notional income will never ever be received by the taxpayer. Similar notional income in the hands of employees of airline, transport, educational institutions, restaurants, hospitals, clinics etc. is already exempt under clause (53A) of Part I of Second Schedule.

Recommendations:

- The taxation of marginal income on loans obtained from the employer below Benchmark rate should be exempted by making necessary amendments in clause (53A) of the Part I of the Second Schedule and by deleting sub-section (7) of Section 13; or

- Alternatively the minimum threshold of the loan amount on which the provisions of Section 13(7) would not be attracted should be raised to at least Rs.2,500,000 from the existing limit of Rs.500,000.

**(iii) Child education & Medical allowances and Investment allowance**

It is suggested that burden of Salaried Class should be mitigated by offering them above allowances to be offset against their salary income provided documentary evidences containing name, address and National Tax Number of Educational and Medical Institution are provided.

## PROPOSAL

In addition salaried class should also be given adjustment against their tax liability in respect of allowable investment, the limit of which should be enhanced.

**(iv) Taxability of Provident Fund Contribution**

Sub-rule (a) of Rule 3 of the Sixth Schedule provides that any contribution made by an employer to a provident fund in excess of 10% of the salary or Rupees 100,000/-, whichever is low, shall be deemed to be income of the employee.

**PROPOSAL**

We suggest that the deeming of income of an employee may be restricted to 10% of salary only and the restriction of monetary amount of Rs.100,000/- per annum may be removed.

## 9. Amendment of Assessment

Sub-section (5) of section 122 provides that an assessment order in respect of a tax year, or an assessment year, shall only be amended under sub-section (1) and an amended assessment for that year shall only be further amended under sub-section (4) where, on the basis of definite information acquired from an audit or otherwise, the Commissioner is satisfied that-

(i) any income chargeable to tax has escaped assessment; or

(ii) total income has been under-assessed, or assessed at too low a rate, or has been the subject of excessive relief or refund; or

(iii) any amount under a head of income has been misclassified.



Similarly sub-section (5A) of Section 122 provides that Commissioner may amend or further amend, an assessment order, if he considers that assessment order is erroneous in so far it is prejudicial to the interest of revenue. This power to the Commissioner is against the principles of natural justice as if he is examining the tax records to ascertain whether the assessment order completed is prejudicial to the interest of revenue or not, he should examine all the areas once for all and amend the order accordingly and should not be authorized to again amend the same order.

Sub-section (4) also provides that Commissioner may further amend the assessment order as many times as may be necessary within the later of five years after the Commissioner has issued or is treated as having issued the original assessment order to the taxpayer; or One year from the end of financial year in which the Commissioner has issued or is treated as having issued the amended assessment order to the taxpayer. It means that the taxpayer will be at the mercy of revenue officer and his case will not be considered as closed transaction till at least six years from the date of original assessment.

At times of amendment of tax orders, they may be added-backs which may be termed disputed by the taxpayer and this creates a wide gap between the taxpayer and the tax authorities leading to greater fear of the taxman and unnecessary litigation. Further, the re-amending of tax orders by the tax authority creates discomfort with the system and the natural cohesiveness that one should have with tax authorities is severely jolted.

This provision of law is against all the norms of justice, equity and fair play.

**PROPOSALS**

(i) It is proposed that once the assessment is amended it may further be amended only when the department acquires definite information that the income has been concealed or inaccurate particulars of income have been furnished or the assessment is otherwise incorrect.

(ii) That re-opening of the case should be made only by the Chief Commissioner, IRS after giving proper opportunity to the taxpayer of being heard by issuing specific show-cause notice in this regard. It is against the tenets of justice that the same Commissioner of Income Tax who has completed the assessment, re-opens the case for additional assessment.

(iii) Moreover where an assessment is required to be amended under Section 122 (5A) that can be amended only once and thereafter this sub-section cannot be invoked on the similar issue.

(iv) The time period to amend the assessment order should be reduced to 3 years.

## 10. Tax on Inter-Company Dividend

The concept of holding companies has helped many economies of the world to grow. In past couple of years Government has made genuine effort to bring present taxation system in line with the International best practices. This concept is available in Pakistan but has not grown as desired, because of certain issues and anomalies relating to holding company concept under the existing laws and regulations in Pakistan. For example tax on Inter-Company dividend which in fact is double or multiple taxation.



This scenario of double taxation has in fact become a hindrance and deterrent for offering dividends by the company.

Although Clause 103A of Part I of Second Schedule, exempts any income derived from inter-corporate dividend; but the same is available such inter-corporate dividend which are within the group companies entitled to group taxation under Section 59A or Section 59B.

**PROPOSAL**

It is therefore suggested that the tax on inter-company dividend received by the companies be exempted from tax.

## 11. Computation of Capital Gains on Disposal of Securities by the Non-Residents

In Pakistan, there is a technical flaw in the manner of calculation of capital gains especially in the case of investment in shares, where the investment is made in foreign currency. Such a gain is calculated in historical rupee terms.

Due to this reason a tax liability may arise to a non-resident due to devaluation of Pakistani rupee vis-à-vis foreign currency even if the shares are sold at the same value in foreign currency or even at a loss. This manner of calculation of capital gain needs to be corrected.

Capital Gains and losses for non-residents are to be calculated in terms of the currency in which such investment is made. For example, capital gain for investment in shares by a non-resident may be computed in US Dollars term instead of Pakistani Rupee term.

This is an internationally accepted practice as only real income or loss can be taxed. There is no deviation in any tax jurisdiction. It is for this reason that India inserted a proviso in Section 48 of the Indian Income Tax Act, 1961 so that these lacunae in the law may be removed. In Pakistan this issue was never arose in the past, as capital gains were exempt from tax.

The implementation of following proposals will help attract foreign investment into Pakistan as investment would not be exposed to losses stemming from depreciation of Pakistani Rupees.

### PROPOSAL



Therefore to protect foreign investment from sharp depreciation in Pakistan Rupee and to help attract foreign investment it is proposed that a proviso similar to Section 48 of the Indian Income Tax Act, 1961 be inserted in Section 76 of the ITO relating to cost of investment for the purpose of determination of capital gain.

## 12. Alternative Dispute Resolution Committee

Section 134A introduced the above mechanism for the first time through Finance Act, 2004. The original idea of providing taxpayer a forum to resolve tax related disputes and to liquidate arrears of tax was provided in the Sales Tax Law under section 47A through Finance Act, 2003.

Sub-section (4) of section 134A provides that the Federal Board of Revenue may on the recommendation of the ADR committee, comprises of professionals, businessmen and FBR officials pass such order, as it may deem appropriate, within forty five days of the receipt of recommendations of the Committee.

It is provided in sub-section (5) that in case the matter is already subjudice before any authority or tribunal or the court, an agreement made between the aggrieved person and the Board in the light of recommendations of the Committee shall be submitted before that authority, tribunal or the court for consideration and orders as deemed appropriate.

It is provided the taxpayer an easy and efficient dispute resolution mechanism and to liquidate arrears of tax an alternative dispute resolution forum.

The ADRC is an independent body because of the nature of its composition and thus has a very strong element of credibility being trustworthy and totally unbiased.

Since it comprises of officer of Inland Revenue and other experts from public/private sector, they have a thorough understanding of the tax laws and its practicality and therefore the recommendations of the ADRC will have strength and will have to be considered seriously by the Board.

**PROPOSALS**

(i) The recommendation made by the Committee should be accepted in a letter & spirit, unless there is any apparent mistake

(ii) That instead of communicating the agreement to the appellate forum, the appeals filed bythe respective parties should be withdrawn.

(iii) Cogent reasons including dissenting notes by the ADR Member must properly be providedand incorporated in the Order issued by the FBR.

(iv) Proper rules may be framed for formation of the committee, scope of work, conducting ofADR proceedings, stay of matter/demand, disposal of application by the ADR Committee, retention of record, remuneration for members of ADRC and etc.



## 13. Separation of tax judicial system from collection machinery

The present scheme of tax appellate authorities being under the control of the executive side of the tax machinery has been an obvious impediment in providing quick justice to the taxpayers and as such it has been time and again proposed that the judicial side should be made independent of the executive side with no cross border movement from one side to the other; being also a constitutional requirement. This aspect needs immediate attention so that the system be brought in line with the provision of the Constitution of the Islamic Republic of Pakistan. We feel that adjudicating officers may be removed from subordination of FBR. Appellate Forums should work under the respective High Courts instead of FBR.

**PROPOSAL**

It is proposed that the tax judicial system should be given under the control of Member Judicial; who may be a Judge of the High Court or Supreme Court of Pakistan.

## 14. Standard Rate of Sales-tax

**ISSUE:**

- Present rate of Sales Tax @ 16% is too high.
- Narrow Tax Base due to high rate of tax.

**OUTCOME:**

- Induces tax evasion, under invoicing, corruption and smuggling.

### PROPOSAL

- Sales Tax Rate should be brought down to a single digit. However, as a first step **we propose the rate of Sales Tax to be brought down to 10%.**

**BENEFIT:**

- Expansion of tax base, reduction in smuggling and corruption, rise in government revenues and increased competitive edge and promotion of documentation of economy.

## 15. Frequent changes in procedures/policy – (End to SRO culture)

**ISSUE:**

- Conflicting policy statements under the Sales Tax Act, 1990 over past few years and frequent changes in the regime by way of levy of new/additional taxes by issuance of SRO's is complicating the most important tax of the future.

**OUTCOME:**

- **Resulting in**confusion, uncertainty, and fear among the business community, creating a negative business environment.

### PROPOSALS

- All such ad-hoc measures taken without the consulting the stakeholders and Tax Bars should be withdrawn forthwith as levy of taxes without taking them into confidence is against the principles of natural justice.
- Further, KTBA also proposes that any policy measures for levying or changing of existing regime should be taken during the budget only in consultation with all stakeholders.

**BENEFIT:**

- Stable tax regime will ensure better business environment;
- Promote trust between tax collector and taxpayer; and
- Result in generating consistent tax revenues

## 16. Fiction between Federal Board of Revenue and Provincial Revenue Boards

**ISSUE:**

- Federal Board of Revenue and Provincial Revenue Boards (SRB / PRA) have locked horns over various legal and procedural issues, such as cross input adjustment etc.

**OUTCOME:**

- Extreme unrest and problems amongst the business community. Issues like taxation of franchise, advertisement and food sectors are unsettled as yet.

**PROPOSAL**

- We suggest that law should be made crystal clear vis-à-vis services taxation in Sindh and Punjab and all pending matters with SRB / PRA may be settled to safeguard taxpayers interests.



**BENEFIT:**

- Stable tax regime will ensure better business environment;
- Promote trust between FBR / SRB; and
- Result in harmony between Federation and Provinces

## 17. Active Taxpayer List (ATL) - Sales Tax General Order 34 of 2010:

**ISSUE:**

- The mechanism of Active Taxpayers List (ATL) envisaged under Sales Tax General Order No. 34 of 2010 dated September 16, 2010, is in serious conflict with the provisions of the Sales Tax Act, 1990.
- The amendment made vide Sales Tax General Order No. 16 of 2013 dated April 11, 2013, has further complicated the issue wherein if a taxpayer does not file a sales tax return for a single tax period by the end of a calendar month, the taxpayer shall be removed from the list of ATL.

- It is in direct conflict with the provisions of law and it also contravenes the dictum of Superior Courts vis-à-vis right of adjustment of input tax.

**OUTCOME:**

- Unnecessary hurdle for the genuine taxpayers who for some reason are unable to furnish their return.

**PROPOSAL**

- Thorough review of the Sales Tax General Order be made in consultation with the Karachi Tax Bar Association and appropriate amendments / modifications made therein.

## 18. Provision of rectification, appeal effect and consequential relief

**ISSUE:**

- Under the Sales Tax Act, 1990, there is no provision for rectification of mistakes and discrepancies, appeal effect and consequential relief in case of reduction of tax demand at appellate stage which creates hardship for the taxpayers and causes multiple litigations.



**OUTCOME:**

- Due to the non-availability of the provisions for above situations under the sales tax statute, the issues are not attaining finality.

**PROPOSAL**

- It is proposed that relevant provisions for rectification, appeal effect and consequential relief as provided under the Income Tax Ordinance should be introduced in the Sales Tax Law.

**BENEFIT:**

- Relief to the taxpayers.

## 19. Joint and several liability of registered persons in supply chain where tax unpaid

**ISSUE:**

- According to this section, a registered person receiving a taxable supply from another registered person can be held jointly and severally liable to pay tax if the tax from such supply, its previous supply or subsequent supply would go unpaid.

**OUTCOME:**

- Payment / deposit of sales tax in the Government Treasury is the responsibility of supplier (seller) U/s. 3 of the Sales Tax Act, 1990. However, at present, virtually all offices of FBR is using this section as a tool to recover the tax not deposited by the supplier (seller) from the customers (buyers) and consequently treating the taxpayers (buyers) as accused person and lodging FIRs against them causing harassment.

### PROPOSAL

- Suitable amendment should be made in section 8A i.e. where a buyer (customer) has paid the invoice amount together with amount of sales tax through the banking channel in compliance of section 73, he should not be held responsible for the default of the seller (supplier). This is also in conformity with section 21 of the Sales Tax Act, 1990.

**BENEFIT:**



- Payment of sales tax will be ensured by the person evading it.

## 20. Adjustable Input Tax

**ISSUE:**

- Section 8B restricts adjustment of input tax in excess of 90% of output tax for a tax period from the registered person.

**OUTCOME:**

- It unnecessarily creates cash flow problems for the registered person.

### PROPOSAL

- Mandatory restriction of input tax and thereby creating tax liability is against the business practice and may be removed in the forthcoming budget.

**BENEFIT:**

- Relief to the taxpayers.

# PROPOSALS FOR LEGAL AMENDMENTS FOR REMOVAL OF HARDSHIP/ ANOMALIES



# FOR THE FEDERAL BUDGET

# 2014-15

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# LEGAL AMENDMENTS
## DIRECT TAX

### 1. Amalgamation *Clause (1A) of Section 2*

Clause (1A) of Section 2 provides that **"Amalgamation"** means the merger of one or more banking companies or non-banking financial institutions, or insurance companies, or companies owning and managing industrial undertakings or companies engaged in providing services and not being a trading company or companies **in either case at least one of them being a public company,** or a company incorporated under any law, other than Companies Ordinance, 1984 (XLVII of 1984), for the time being in force, (the company or companies which so merge being referred to as the "Amalgamating Company" or companies and the company with which they merge or which is formed as a result of merger, as the **"Amalgamated Company")** in such manner that.

**PROPOSAL**

The condition of at least one of them being a public company be removed.

### 2. Employment *Clause (22) of Section 2*

The definition under section 2(22) of **"Employment"** includes-



(a) A directorship or any other office involved in the management of a company;

(b) A position entitling the holder to a fixed or ascertainable remuneration;

(c) The holding or acting in any public office.

It is the general norm that director is mostly involved in the total affairs of the company and he only takes the remuneration from the company when it becomes profit venture. For having the relation of Employee and Employer it is important to have contractual relationship of employment for remuneration.

Further, more under the aforesaid definition of "employment", any person holding a position entitling the said person to a fixed or ascertainable remuneration could be classified as an employee irrespective of whether or not there is an employer / employee relationship. For example the consultants who are working for a fixed or ascertainable remuneration could not be termed as employee.

**PROPOSAL**

It is proposed that sub-section 2(22) be substituted with the following:-

"Employment" includes a directorship or any other office involved in the management of a company entitling the individual to a fixed or ascertainable remuneration from a Company.

## 3. Permanent Establishment

*Section 2(41)(f)*

**ISSUE:**

The definition of permanent establishment as stated in Sub clause (f) of clause 41of Section 2 as under:

> "(f) any substantial equipment installed, or other asset or property capable of activity giving rise to income".

**PROPOSAL**

Since, the industrial growth has been promised by the government. It would be appropriate that a minimum period of suitable time be included in Sub-Clause (f). The specification of minimum period is also necessary to time bound the Taxpayers in order to promote the industrialization in true sense and to ensure the actual investment of capital in the country. Therefore, it is suggested that the minimum period of 90 days be allowed for the injection and investment of capital by the permanent establishment to install the equipment and machinery.



## 4. Tax on Dividend

*Section 5 read with Section 8 & Division III of Part I of the First Schedule*

Sub-Section (1) of Section (5) provides that a tax shall be **imposed** at the rate of 10% to the gross amount of the dividend, on every person who receives a dividend from a Company or treated as dividend under Clause (19) of Section 2.

Prior to the insertion of proviso by the Finance Act, 2007, Section 8 of the Ordinance provided that the tax imposed under Section 5 shall be final tax on the amount in respect of which the tax is imposed and the liability of a person under Section 5 shall be discharged to the extent that the tax payable has been deducted at source at the rate of 10% on dividend received from a Company. However, the following proviso was inserted by the Finance Act, 2007 in Section 8 of the Ordinance:-

> **"Provided that the provision of this Section shall not apply to dividend received by a Company"**

We understand the above proviso was inserted with the intention to exclude Company as recipient of the dividend from the Final Tax Regime. However, we feel that due to ambiguity in law the purpose has not been achieved clearly. On the one hand Section 5 provides that the tax shall be imposed on the gross amount of Dividend, (which means tax payable on such income) and on the other hand the Companies have been excluded from the operation of Section 8, which provides finality to the dividend income.

**PROPOSAL**

We propose that in Sub-Section (1) of Section 5 and in Section 8 the word "Imposed" be substituted with word "Collected"

## 5. Taxability of employees contribute to provident fund

*(Section 12, Sixth Schedule Part I Rules 3)*

**ISSUE:**

The above rule to the ordinance, before an amendment by finance Act 2008 was provided that the contribution made by any employer in excess of 1/10 of the salary was deemed to be income in the hands of an employee. Finance Act, 2008 bought an amendment in the said rule that Rs.100,000/- should compare with the 1/10 of the salary and the lower of the two should be tax in the hands of an employee.

By virtue of the above amendment the high on net salaried taxpayers suffers a lot due to the fact that the Rs.100,000/-always be lower than 1/10 of their salary. Therefore, all the contribution made by the employer in addition to Rs.100.000/- is taxable in their hands.



**PROPOSAL**

It is proposed that this additional burden on the salaried class may be withdrawn. Especially in view of the fact where the provident fund is approved by the Income Tax authorities and the amount representing the accumulated balance is exempt from Tax.

## 6. Stock-in-Trade

*Section 35*

Under this section, the concept of determination of the cost of stock in trade disposed of has been introduced. Generally in the cases of companies, the valuation has to be mandatory made on the basis of International Accounting Standards.

**PROPOSAL**

It is therefore, proposed that in Section 35, wherever word "person" has been used, words "other than companies" may be inserted.

## 7. Long-Term Contracts

*Section 36(2)*

The provision of sub-section (2) of Section 36, requires that contract revenue be recognized as

income of tax year in which the work is performed and correspondingly, contract costs be recognized as an expense in the tax year in which the work to which they relate is performed. It is important to note that under subsection (2) of this Section, for the purposes of determining income on incomplete long-term contracts, the percentage of completion shall be determined by the ratio which the contract costs incurred up-to the end of the tax year has with the estimated total cost as "determined at the commencement of the contract". I feel that considering contract costs as a variable "at the commencement of the contract" for estimating the stage of completion is not appropriate, given the practical considerations whereby with the ongoing progress of the contract, it is invariably desirable to re-estimate the entire costs of the contract until its completion. This is necessary so as to have a more fair estimate of the completion achieved and hence a proper determination of percentage of completion of the contract. This principle is duly recognized in IAS-11 which should be allowed to be observed.

**PROPOSAL**

That the word "commencement of the contract" in sub-section (2) of section 36 of the Ordinance may be substituted with the words "commencement of the year".

## 8. Disposal of Asset between Wholly-Owned Companies

*Section 97*

Section 97 provides that where a resident company disposes of an asset to another resident company, no gain or loss shall be taken to arise on the disposal if the both the companies belong to **a wholly-owned group** of resident companies at the time of the disposal.



**PROPOSAL**

We propose that a "wholly-owned group" be defined as companies having 90%% or more share holding in the company.

## 9. Change in Control of an Entity

Section 98(1)(b)

Sub-section (1) of section 98 provides that when there is a change in fifty percent or more of the underlying ownership of an entity, any loss incurred for a tax year before the change shall not be allowed as a deduction in a tax year after the change unless the entity:

(a) Continues to conduct the same business after the change as it conducted before the change until the loss has been fully set-off

(b) Does not, until the loss has been fully set-off, engage in any new business or investment after the change where the principal purpose of the entity or the beneficial owner of the entity is to utilize the loss so as to reduce the income tax payable on the income arising from the new business or investment.

The second condition practically restricts the new management of the entity to make any further investment or enter into new business to generate income from the investment/business. Generally it is observed that when the original management was unable to make a profit out of the business then such circumstances may lead to shifting of hands. Therefore, barring the new management to make further investment or enter into new business is highly unreasonable.

**PROPOSAL**

It is proposed that provisions of Section 98(1 )(b) be deleted.

## 10. Geographical source of Income

*Section 101(3)*

**Business income of a non-resident person**

Sub-Section(3) of section 101 provides that business income of a non-resident person shall be Pakistan source income to the extend to which it is directly or indirectly attributable to:-

(a) a permanent establishment of the non-resident person in Pakistan;

(b) sales in Pakistan of goods or merchandise of the same or similar kind as those sold by the person through a permanent establishment in Pakistan;

(c) other business activities carried on in Pakistan of the same or similar kind as those effected by the non-resident through a permanent establishment in Pakistan; or

(d) any business connection in Pakistan

On perusal of above it is transpired that in the presence of PE criteria the existence of clause (d) i.e. any business connection in Pakistan becomes superfluous and irrelevant.

**PROPOSAL**

Clause (d) in sub-section (3) of section 101 may be deleted.

## 11. Foreign Losses

*Section 104*

Section 104 is somewhat similar to the principles laid down in section 56 and 57. Its provides that deductible expenses incurred to earn foreign sources income can be deducted only against foreign source income and loss of foreign source income can be set-off and carry forward against foreign source income only.
In principle the business loss arises locally or incurred to earn foreign source income should be allowed to set-off against income earned during the tax year and if not fully set-off the same may be allowed to carry forward.

**PROPOSALS**

It is proposed that Section 104 of the Ordinance be deleted.

## 12. Commissioner Empowered to Re-Characterize Income & Deductions

*Section 109*

Under section 109 Commissioner has been empowered to re-characterize a transaction or an element of a transaction or disregard a transaction devoid of economic substance or re-characterize a transaction where form and substance are incompatible. The aforesaid measures could be invoked where the Commissioner may have reasons to believe that such transaction was done in pursuance of a tax avoidance scheme.

In sub-section (2) of section 109 the definition of tax avoidance scheme caters such transaction of which the main purpose is to avoid or reduce tax. The courts have held that only such transaction can be disregarded which have no commercial purpose. Further, courts have also held that circumventing provisions of law using legal method is permissible and tax avoidance carries different meaning in tax laws. Therefore, a transaction, which has commercial purposes beside any objective to avoid or reduce tax, should not be treated as tax avoidance scheme.

Conceptually there is nothing wrong with these provisions as the objective is to forestall "tax avoidance schemes". This provision has even declared "tax avoidance" as illegitimate and forbidden. Not only the taxpayers have been deprived of a lawful right, but the taxation officers have been given unqualified powers to declare whatever they may conceive and label it as a "tax avoidance scheme." Although this concept has recently been introduced in the number of countries of the world like UK in the year 2000 and is still in it's infancy. We feel that in Pakistan this discretionary power may be misused.



### PROPOSAL

Amendment is needed to attract provisions to such transaction only, which has no commercial purpose and value.

## 13. Un-explained investment, etc deemed to be income

*Section 111(3) and 111(4)*

Sub-section (2) of Section 13 of the Repealed Ordinance provided that where the value of any investment or article referred to in clause (aa),(b),(c) or (d), or the amount of expenditure referred to in clause (e) of sub-section (1) is, in the opinion of the Deputy Commissioner, too low, **the Deputy Commissioner after giving a reasonable opportunity to the assessee of being heard may determine a reasonable value or the amount thereof,** as the case may be, and all the provisions of sub-section (1) shall have effect accordingly.

In the Repealed Ordinance the Revenue Officer was bound to provide a reasonable opportunity to

the assessee of being heard before making addition of any value or the amount thereof whereas sub-section (3) of section 111 which is corresponding section of the Repealed Ordinance authorizes the Commissioner to include the difference in the person's income chargeable to tax without providing him a reasonable opportunity of being heard while making addition of any amount thereof. We feel this is against the all norms of natural justice.

Sub-Section (4) of Section 111 provides that any amount of foreign exchange remitted from outside Pakistan through normal banking channel that is encashed into rupees by a scheduled bank and a certificate from such bank is produced to that effect. In my humble view this is licence to whiten the future black money and play an active role in defiting the Government's effort to bring the tax evaders into the tax net.

**PROPOSAL**

(i) After the words "the Commissioner may," the words "after giving to the taxpayer areasonable opportunity of being heard and "may be inserted.

(ii) The exemption from taxation as unexplained income under Section 111(4) of the Ordinance to the foreign exchange brought into Pakistan through proper banking channel should be restricted to home remittances by overseas Pakistanis and only for fresh industrial investment.



## 14. Revision by the Commissioner

Section 122A

Section 122A provides that the Commissioner may *suo moto* carry out a revision of any proceeding under the Ordinance in which an order has been passed by any officer of Inland Revenue. A taxpayer should also be given a right to approach the Commissioner for the revision of assessment to seek a redress of his grievance by the Commissioner as was available u/s.138 of the Repealed Ordinance.

**PROPOSAL**

We propose that such option may also be allowed to the taxpayer upon his request to the Commissioner.

*Section 122-B*

## 15. Revision by Chief Commissioner

**ISSUE:**

No provision is availablefor Chief Commissioner to call for revision of audit cases on an application filed by the taxpayers.

**PROPOSAL**

Section 122-B should be revised so as to give powers to the Chief Commissioner for the revision of

cases selected for Audit U/S 177.

## 16. Appeal to the Commissioner

*Section 127*

Sub-Section (1) of section 127 provides that any person dissatisfied with any order passed by a Commissioner or a Taxation Officer under various specified sections/ provision of law of the Ordinance holding a person to be personally liable to pay an amount of tax, or an order declaring a person to be the representative of a non-resident person, except a provisional assessment under Section 122C or an order giving effect to any finding or directions in any order made under this part by the Commissioner (Appeals), Appellate Tribunal, High Court of Supreme Court or an order refusing to rectify the mistake, either in full or in part as claimed by the tax payer or an order having the effect or enhancing the assessment or reducing a refund or otherwise increasing the liability of the person, may prefer an appeal to the Commissioner (Appeals) against the orders.

Weare the view that every citizen of Pakistan has inherent right to file appeal before appropriate appellate forum on any order, judgment, decree or sentence of the assessing authority, as such insertion of various sections/clauses rendered superfluous.

### PROPOSAL



The sub-section (1) of section 127 be substituted with the following clause:-

> "Any person dissatisfied with any order passed by a Commissioner or a Taxation Officer under this Ordinance including provisional assessment holding a person to be personally liable to pay an amount of tax, or an order declaring a person to be the representative of a non-resident person, or an order giving effect to any finding or directions in any order made under this Part by the Commissioner (Appeals), Appellate Tribunal, High Court or Supreme Court or an order refusing to rectify the mistake, either in full or in part as claimed by the tax payer or an order having the effect or enhancing the assessment or reducing a refund or otherwise increasing the liability of the person, may prefer an appeal to the Commissioner (Appeals) against the orders".

## 17. Disposal of cases at appellate forum Commissioner Inland Revenue (Appeals)

*Section 129*

**ISSUE:**

Upto the Tax year 2005, the Commissioner of Income Tax (Appeals) [CIR(A)] had the power to set aside the orders framed by the assessing officers. Vide finance At 2005, the power to set aside has been divested and therefore, the CIR(A) would be able only to modify, confirm or annul the

assessment after making the inquiries or examining the books of accounts.

It has been noticed that to give relief, the CIR(A)is required to examine the evidences. However, due to paucity of time and with the shortage of staff posted with the CIR(A) it is not possible for the CIR(A), to verify and dispose of the cases in all respect judicially and on equitable basis.

**PROPOSAL**

It is proposed that this power to set aside the appeal should be re-introduced in the law.

## 18. Appointment of the Appellate Tribunal Member *Section 130*

Sub-section (3) of section 130 interalia provides for appointment of an Advocate of High Court as a Judicial member of the Tribunal.

**PROPOSAL**

We propose that the Fellow Chartered Accountants, Fellow Cost and Management Accountants and Advocates having experience of Ten (10) years may be allowed to be appointed as Accountant Member.



## 19. Appellate Tribunal Inland Revenue *Section 132(2)*

**ISSUE:**

Sub-Section 2 of Section 132 states as under:

> "(2) The Appellate Tribunal shall offered an opportunity of being heard to the parties to the appeal and, in case of default by any of the party on the date of hearing, the tribunal may if it deem fit, dismiss the appeal in default, or may proceed ex parte to decide the appeal on the basis of the available record". (underline ours)

In view of the above, we understand that the power to dismiss the appeal is unjustified in view of the fact that ATIR is the last fact finding authority and accordingly the decision of ATIR in respect of the facts is final.

**PROPOSAL**

It is therefore, proposed that the said Sub-section (2) may accordingly be amended as under:

> *"The Appellate Tribunal shall afford an opportunity of being heard to the parties and in case of failure to attend the appeal by the person filing the appeal, the tribunal may proceed ex-parte to decide appeal on the basis of the available records"*

The condition of dismissal of appeal should be eliminated from the above provision in order to provide the taxpayer an opportunity to get justice even in the ex parte decision.

In our considered opinion, the language used in Sub-section (2) is defective and needs suitable amendments as it cannot be presumed that legislature intended to cause injustice.

## 20. Reference to the High Court

*Section 133*

Prior to substitution of section 136 of the Repealed Ordinance in the year 2000 the taxpayer or commissioner was allowed to file appeal directly to the High Court against the order of the Income Tax Appellate Tribunal (ITAT). However, now they both are required to apply to ITAT to refer to the High Court any question of law arising out of order of the ITAT. This is creating delay in finalization of pending issues and causing additional cost to the taxpayer.



It was therefore proposed that the provisions prior to amendment made in the year 2000 in the Repealed Ordinance for Direct Appeal to the High Court may be restored. The Finance Act, 2005 extended these facilities of Direct Reference to the High Court to the taxpayers.

However, the proviso inserted in sub-section (6) of above section, whereby the honourable High Court may make an order authorizing the Commissioner to postpone the refund until the disposal of the appeal by the Supreme Court, provided the application is made by the Commissioner with 30 days of the receipt of judgment of High Court which resulted in a tax refund; has nullified the effect of such a positive amendment made in the Ordinance.

**PROPOSAL**

The words "the disposal of the appeal by the supreme court" be substituted with "the period of six months from date of receipt of High Court Order".

## 21. Stay of demand

*Section 137*

**ISSUE:**

The provision of above section provides that, any demand created as a result of an assessment or an amended assessment order or any other order issued by the Commissioner IR, the resultant demand shall be payable within 15 days from the date of service of the notice. Before the amendment vide Finance Act, 2008, the time period for the payment of tax was 30 days. This reduction of time period as a result of an amended order causing hardship and now becoming a basis of harassment to the taxpayer from the tax authorities.

This would become more serious when the demands are un-realistic and frivolous for which the taxpayers have to suffer.

**PROPOSAL**

Automatic stay of demand upto 85% for first stage of appeal and 50% till the ATIR stage of appeal be provided as was provided in the repealed Income Tax Ordinance, 1979.

## 22. Collection of tax in the case of Private Companies and AOP

*Section 139(1)*



Sub-Section (1) of Section 139 provides that notwithstanding anything in the Companies Ordinance, 1984 (XLVII of 1984), where any tax payable by a private Company (including a private Company that has been wound-up or gone into liquidation) in respect of any tax year cannot be recovered from the Company, every person who was, at any time in that tax year:-

(a) a director of the Company, other than an employed director; or

(b) a shareholder in the Company owning not less than ten percent of the paid-up capital of the Company.

shall be jointly and severally liable for payment of the tax due by the Company.

We feel that in case of limited liability companies the above provision of law is neither in line with the provisions of the Companies Ordinance, 1984 nor the international norms in this regard.

**PROPOSAL**

We propose that every shareholder should be made responsible to pay the tax payable in accordance with his percentage of shareholding in the Company and to the maximum of his share capital in the Company.

## 23. Imports

*Section 148 (4A), 159*

The Finance Act, 2008 omitted Sub-Section (4A) of Section 148; whereby the CIT was authorized toissue tax exemption certificate at a reduced rate of 0.5% to any person other than those covered under the Presumptive Tax Regime, if the CIT is satisfied that such person is not likely to pay any tax other than tax under Section 113.

Sub-Section (7) of Section 148 provides that the tax collected under this section shall be a final tax,except as provided under sub-section (8) [Import of Edible Oil and Packing material] on the income of the importer arising from the imports subject to Sub-Section (1) and this Sub-Section shall not apply in the case of import of:-

(a) Raw material, plant, machinery, equipment and parts by an industrial undertaking for itsown use;

(b) .....

(c) .....

(d) .....

The above withdrawal has created problems and hardship to the many genuine taxpayers who are not industrial undertaking; for example:-



- The tax would be deducted on import of ATM machines by the Banks and such withholding tax would be considered as final liability.

- Import of machinery by the Contractor for performance of his contract. His receipts from contracts are subject to final tax and are no more liable to pay any extra tax. However, the tax so deducted at import stage would be additional levy.

- The tax deducted in the case of taxpayers who are not industrial undertaking and are also not liable to pay any tax due to depreciation or brought forward losses etc.

Although the Finance Act, 2007 vide substituted sub-section (2) expanded the powers of FBR and allowed it to exempt person, classes of persons, goods or classes of goods from withholding taxunder this Ordinance but for all practical purpose it is a cumbersome and long awaited process forthe taxpayer to obtain exemption certificate.

### PROPOSAL

Powers may please be delegated to the respective Chief Commissioner of RTO(s) and LTU(s) for issuance of exemption certificates in the hardship cases as explained above and make appropriate amendments in the law to authorize Commissioner of Income Tax, Inland Revenue to issue exemption certificate in cases where 100% income is covered under the Presumptive Tax Regime.

## 24. Withholding of Tax on Payment of Profit on Loan from Directors/Associates

*Section 151(1)*

Sub-section (1) of section 151 provides that different classes of taxpayers paying profit on debts shall deduct tax at the prescribed rates except on profit on loan obtained under agreement between borrower and a banking company or a development finance institution.

We all are fully aware that, it is also a general norm that companies grant loans to their sister concerns and subsidiaries. In past question of withholding of tax on such loans was raised and it had already been settled and appropriate amendment was also made in the law to exclude such companies from preview of withholding provisions. However, few of our members have informed us that their clients' have received notices from the Taxation Officers (TO); wherein they have inadvertently contended that taxpayers are liable to withheld tax under Section 151 of the Income Tax Ordinance, 2001 (the Ordinance) on payment of Profit/Interest on Loan obtained from Directors/Associates.

In this regard, before we submit our view; it would be pertinent to reproduce below the provisions of Section 151 of the Ordinance -

**Section 151 of the Income Tax Ordinance, 2001**

Where-



a banking company, financial institution, a company referred to in sub-clauses (i) and (ii) of clause (b) of Sub-Section (2) of Section 80, or finance society pays any profit on any bond, certificate, debenture, security or instrument of any kind (other than a loan agreement between a borrower and a banking company or a development finance institution) to any person other than financial institutionthe payer of the profit shall deduct tax at the rate specified in Division I or Part III of the First Schedule from the gross amount of the yield or profit paid as reduced by the amount of Zakat, if any, paid by the recipient under the Zakat and Ushr Ordinance, 1980 (XVII of 1980), at the time the profit is paid to the recipient.

(2) This section shall not apply to any profit on debt that is subject to Sub-Section (2) of Section 152.

(3) Tax deducted under this section shall be a final tax on the profit on debt arising to a taxpayer other than a Company from transactions referred to in Clauses (a), (b) and (d) of Sub-Section (1).

On perusal of above provisions it would be revealed –

- a banking company, a financial institution, a company referred to in sub-clauses (i) and (ii) of clause (b) of sub-section (2) of section 80 of the Ordinance; and

- the payer of profit on payment of profit on bonds, certificates, debentures, securities or instruments of any kind (other than a loan agreement between a borrower and banking company or a development finance institution) to any person other than financial institution;

shall deduct tax at the specified rate and tax so deducted shall be final tax on the profit on debt arising to a taxpayer other than a Company

On further examination of above provision your good-self will observe that the words ***"or instruments of any kind"*** are preceded by bonds, certificates, debentures, securities, which all are negotiable and transferable instruments in nature by mere delivery or endorsement. According to general words used thereafter only refer to an instrument of the same class and color, but of different nomenclature. As such, I am of the opinion that keeping in view the doctrine of ***Ejusdem Generis,*** the tax is deductible under section 151(1) (d) of the Ordinance on income generated from the negotiable instruments of like nature as required by it and not on the instrument of any other kind having no nexus with the financial instruments referred in the section 151(1) (d) of the Ordinance.

It is also submitted that enactment of above provisions of law on theprofits/interest on directors/ associate loans will cause lot of revenue loss to the exchequer, because presently such income is being taxed under the normal law (maximum rate of tax is 25%); whereas the withholding of tax under the above provision of law is deductible at the rate of 10% of the yield or profit paid.

Keeping in view the above provisions of law, decisions of the superior courts and our submissions, it is clear beyond any doubt that the provisions of section 151 is applicable only to the negotiable instruments issued by a banking company, a financial institution, a company referred to in sub-clauses (i) and (ii) of clause (b) of sub-section (2) of section 80 of the Ordinance and not applicable to the payments made for interest/profits on loans from directors/ associates.



**PROPOSAL**

In order to clarify further appropriate amendments may please be made to exclude payments made for interest/profits on loans from directors/associates.

## 25. Exemption or lower rate certificate

*Section 159*

**ISSUE:**

The above provisions of the Ordinance, state that the Commissioner shall provide an exemption certificate to the taxpayer without mentioning any time limit for the issuance of such exemption certificate. It is the common observation of the taxpayer that it takes 3 to 6 weeks on average to get the certificate from the tax authorities. By that time a considerable amount of tax deducted from the payments received by the taxpayer.
It is also observed that the application of the exemption certificate rejected by the Commissioner without assigning any cogent reason.

**PROPOSAL**

It is therefore, proposed that a statutory time limit of "7 days" may be provided in the provisions of the above section so that if any delay arises, it should be on some reasonable grounds.

It is also proposed that a right of appeal be provided to challenge any frivolous refusal of application by the Commissioner as in a past.

## 26. Refunds

*Section 170*

**ISSUE:**

Under the provisions of section 170 of the ordinance, the time limit for the application for the claim of refund is two years from the date of assessment order or the date on which the tax was paid, whichever is later.

We understand that with the introduction of the concept of self-assessment under the provisions of the ordinance, refund is a vested right of the taxpayer. The conditions of restricting the time limit of filing the vested rights are unconstitutional, un-called for and prejudicial to the interest of the taxpayers.

It is also observed that time limit for the issuance of refund by the Commissioner is 60 days from the receipt of the refund application.



**PROPOSAL**

It is therefore, proposed that the provisions related to the time limit constraints for filing of refund application be deleted. In this respect, clause (c) of sub-section (2) of section 170 of the ordinance should be deleted.

In cases where refund is not issued within the specified period of time provided in the ordinance, it is therefore, proposed that the proviso shall be inserted which provides that *the application shall deem to have been accepted after the expiry of said period of 60 days for the issuance of the refund by the Commissioner.*

## 27. Rationalization of Additional Payment for delayed Refund and Default Surcharge

*Sections 171 and 205*

**171. Additional Payment for delayed refund**

Where a refund due to a taxpayer is not paid within three months of the date on which it becomes due, the Commissioner shall pay to the taxpayer a further amount by way of compensation at the rate of KIBOR per annum of the amount of the refund computed for the

period commencing at the end of the three month period and ending on the date of which it was paid.

**205. Default Surcharge**

A person who fails to pay:-

(a) any tax, excluding the advance tax under Section 147 and default surcharge under this section;

(b) any penalty; or

(c) any amount referred to in Section 140-141,

on or before the due date for payment shall be liable for default surcharge at a rate equal to KIBOR plus three percent per quarter on the tax, penalty or other amount unpaid computed for the period commencing on the date on which the tax, penalty or other amount was due and ending on the date on which it was paid.

**PROPOSAL**

The rate of Default Surcharge and compensation for delayed refund be rationalized or should be at par.



## 28. Power to enter and search premises *Section 175*

Section 175 provides that in order to enforce any provision of this Ordinance (including for the purpose of making an audit of a taxpayer or a survey of persons liable to tax), the Commissioner or any officer authorized in writing by the Commissioner for the purposes of this section:-

(a) shall, at a times and without prior notice, have full and free access to any premises, place, accounts, documents or computer;

(b) may stamp, or make an extract or copy of any accounts, documents or computer-stored information to which access is obtained under clause (a);

(c) may impound any accounts or documents and retain them for so long as maybe necessary for examination or for the purposes of prosecution;

(d) may, where a hard copy or computer disk of information stored on a computer is not made available, impound and retain the computer for as long as is necessary to copy the information required; and

(e) may make an inventory of any articles found in any premises or place to which access is obtained under clause (a).

The provision is very harsh in nature. It also provides for action to be initiated by the Commissioner without prior notice, which does not meet the principle of natural justice.

**PROPOSAL**

Appropriate amendment be made in this section as to ensure that before any action under this section is taken by the Commissioner he should issue a show cause or prior notice which is properly and duly served on the taxpayer and the access does not extend to entering residential premises.

## 29. Notice to obtain Information or Evidence

*Section 176*

Under section 176 the Commissioner can call for any information from any person. By virtue of this section, where a hard copy or computer disk of information stored on a computer is not made available to the Commissioner, he has the power to require production of the computer on which the information is stored and impound and retain the computer for as long as is necessary to copy the information required. We are afraid of misuse of such powers in its application, in reality.

**PROPOSAL**



This provision of law may be reviewed for reduction of discretionary powers.

## 30. Penalties for Non-Filling of Return of Income and Statements u/s.114(4), 115,116 and 165

*Section 182(1)*

Section 182(1) substituted through Finance Act, 2010 and explanation has been inserted through Finance Act, 2011, whereby penalties for non/late filling of return of income, statement of final tax, wealth statement its reconciliation and withholding statement specified under aforesaid section are very harsh and excessive.

Generally the main reason for levying penalties on commitment of offences is only to educate the taxpayers and create deterrence; so that they may file the return/statement within stipulated time. The intention of legislature has never to create huge demands or to achieve revenue target through such penalties. The quantum of penalties raised through substitution of section 182(1) read with the explanation is very harsh and unfair. It is also unjustifiable and illogical to impose such huge penalties; which may create harassment among the taxpayers rather to facilitate them.

**PROPOSAL**

The Finance Act, 2011, an explanation has been inserted whereby for the purpose of this entry, it has been declared that the expression “tax payable” means tax chargeable on the taxable income on the basis of assessment made or treated to have been made under section 120, 121, 122 or 122C of

the Ordinance.

At the outset, the prescription of above penalty for default in submission of withholding tax statement is not relevant as the same is not related to tax on taxable income.

Consequent to insertion of the said explanation, it has been noted that the tax authorities have invariably started levying penalty for a single day of default on the basis of tax payable in the return without taking into account the taxes already paid/ deducted. Further, the tax authorities are now imposing this penalty for prior years/ periods as well, which is against the established principle that any amendments putting additional burden can operate only prospectively. This situation is causing a serious hardship to the taxpayers, as now due to this explanation, the tax authorities are using the explanation as tax collection avenue instead of a deterrent.

Logically, imposing of penalty should have been restricted to the extent of short tax paid with the return, as was held by the appellate authorities before insertion of the said explanation, and if there was no tax payable then token amount of penalty should have been imposed, as was the cause before substitution of section 182 of the Ordinance.

**PROPOSAL**

It is, therefore proposed that:-

(a) Minimum penalty of Rs.5,000/- shall be levied if any person without reasonable excuse fails infiling the return of income u/s.114 and statement under section 115(4), thereafter an additionalpenalty higher of 0.1% per day of tax payable u/s.137(1) of the Ordinance or Rs.500/- per dayduring which the default continues. The maximum penalty should not exceed 25% of tax payablealong with return/statement.



(b) Minimum penalty of Rs.2,000/- shall be levied if any person without reasonable excuse fails infiling the wealth statement / reconciliation u/s.116 and withholding statement u/s.165, thereafteran additional penalty of Rs.200/- per day during which the default continues. The maximumpenalty should not exceed 25% of tax payable under Section 137(1) or Rs.25,000/, whichever ishigher.

## 31. Advance Ruling *Section 206A*

Advance rulings facilitate investors in general and foreign investor in particular to know their tax liability in advance and to plan their business and investment strategies, for helping economy. Advance rulings also share the burden of judiciary and restrict revenue officials from using discretionary and injudicious powers. There are number of countries where this practice is being followed successfully.

Government deserves lot of appreciation for introduction of such provisions in the law, which is in line with international practice, but the same facilitate only to the foreign investors:-

**PROPOSALS**

It should also be clarified that the Advance Ruling will be valid even where the non-residenttaxpayer after obtaining the ruling becomes resident.

## 32. Appearance before the authorities *Section 223(2)*

It is proposed that the Income Tax Practitioner (ITP) provide in Clause (f) of sub-section (2) of Section 223 may be replaced with the Federal Tax Practitioners (FTP), since all the taxes have integrated and one window is being implemented for all the Federal taxes, so that the person can also represent before all the tax authorities working under the FBR.

## 33. Withholding tax on Cash withdrawals from bank *Section 231A*

There are number of tax payers covered under the Presumptive Tax Regime. Any tax paid or deducted other than PTR is refundable to them. It is the general policy of the Government that the tax which ultimately is to be refunded should not be collected. With this idea number of items have also been made zero rated in the Sales Tax Act in order to save the exporters from hassle of firstly paying and then claiming refunds.



Section 231A was introduced in the year 2005 for deduction of tax by the banks from cash withdrawals exceeding Rs.25,000/-. From 1st July 2006 the position was further changed and ceiling of Rs.25,000/- was changed to daily basis rather than each transaction base. Exemption is given to certain categories but the tax payers covered under PTR especially exporters are not exempted even the Commissioner is not authorized to issue exemption certificate to such taxpayers. This is a futile exercise of paying tax and then refunding the same which create various problems.

Moreover, this provision was introduced with following two objectives in mind:-

(i) To broaden the tax net by bringing new taxpayers with the help of the information collected frombanks;
(ii) To make clear difference between the taxpayers and non-taxpayers.

**PROPOSALS**

It is therefore proposed that:

(a) Minimum exemption level should be increased Rs.100,000/- (One Lac) per day as Rs.25,000/-is too meager to meet the day to day expense and creating great hardship to the genuine businessmen.
(b) Tax at the rate of 0.2% of the cash amount withdrawn should not be collected from account

holder who are existing taxpayers; however in case of non-taxpayers the same should be collected at the rate of 1.0%.

(c) Effective law may be framed required bankers to provide tax deduction certificates on deduction made on day-by-day basis.

## INDIRECT TAXES

### 1. Blacklisting and suspension of registration

**ISSUE:**

- The law provided under sub-section (2) and (3) of 21 of the Sales Tax Act, 1990 with regard to black-listing and suspension of registration of the taxpayerread-with Rule 12 of Sales Tax Rules, 2006 and clause (N) of Sales Tax General Order 3 of 2004 dated June 12, 2004, is not followed by the Department in latter and spirit.
- No opportunity of hearing is provided.
- No order is passed by the Department.

**OUTCOME:**

- Department rather completing formal conditions as required under the law, is using this section to block the taxpayers on whims and fancies causing unnecessary hardships to the taxpayers.

### PROPOSALS

- This law applied in latter and spirit.



- Any such suspension or blacklisting outside the ambit of detailed modalities as provided in terms of Section 21 read-with Rule 12 of Sales Tax Rules, 2006 and Sales Tax General Order No. 3 of 2004 should immediately be stopped.
- Further, wherever the proceeding of suspension or black listing is initiated, it should be done within the time frame provided in Section 21.
- Fair opportunity of being heard should be provided to the taxpayers.

**BENEFIT:**

- It will restore confidence of the genuine taxpayers on taxation system.

### 2. One sales tax registration for two or more business:

**ISSUE:**

- After amendment in Sales Tax Act, 1990, through Finance Act, 2008, FBR has directed to cancel multiple registrations under single proprietorship.

**OUTCOME:**

- Proprietor having two businesses is faced with the dilemma to show its entire sales under one business, which is creating hardship for his customers in their respective returns.

**PROPOSAL**

- FBR to issue necessary instructions to incorporate multiple business feature in its web-portal for facilitation of the taxpayers.

**BENEFIT:**

- Better documentation of economy and proper maintenance of records of taxpayer.

## 3. Cottage Industry

*Section 2 (5ab)*

**ISSUE:**

- Limit of cottage industry is Rs.5 (M) with limit of utility Rs.0.7 (M) is outdated in view of consistent inflation, devaluation of Pakistan Rupee and increasing trend of cost of doing business.



**OUTCOME:**

- High inflation and increasing trends of utility is now becoming unbearable.

**PROPOSAL**

- Exemption limit for Cottage Industry needs to be increased from Rs.5 (M) to Rs.10 (M) and the utility limit should be increased from Rs.0.7 (M) to Rs.1.2 (M) in order to counter the increase in inflation and utilities tariff and devaluation of currency.

**BENEFIT:**

- More taxes shall be collected from Cottage Industry.

## 4. Tax Fraud – section 2(37) and power to arrest & prosecute

*Section 37A*

**ISSUE:**

- Under Sub-Section (37) of Section 2 of the Sales Tax Act, 1990, the burden of proof to prove innocence is laid upon the accused whereas U/s. 37A, the accused is provided with no opportunity of hearing to provide his innocence before he can be accused, arrested and prosecuted.

**OUTCOME:**

- No opportunity of being heard is provided. This is against the principles of natural justice which is the basic right of every taxpayer.

### PROPOSAL

- Section 37A be amended as follows:

- The words "and after giving him an opportunity of hearing, to confront the evidence", should be inserted after the word "evidence" in sub section (1) of Section 37A.

- Furthermore, the responsibility of proving the guilt of accused should primarily lie on the Department.



**BENEFIT:**

- Simplification of Sales Tax Law and curtailing discretionary powers of tax officials.

## 5. Determination of tax liability (input adjustment)

*Section 7*

**ISSUE:**

- Sales Tax Department has started putting certain sales tax registered person under the list of suspicious supplier and is disallowing input adjustment in case purchases are made from these suppliers.

**OUTCOME:**

- It creates an unnecessary hardship for a registered person because he is penalized for the fault of the department although he has lawfully purchased an item with sales tax payment and has also made payment through banking channel.

### PROPOSAL

- Since the registered person has a valid sales tax invoice, therefore, Department should not disallow input adjustments.

**BENEFIT:**

- Taxpayer shall not be penalized due to administrative problems of FBR.

## 6. Tax credit not allowed

*Section 8(1)(A)*

**ISSUE:**

- The Department sometimes is not allowing inputadjustment of ancillary items under the provision of section 8(1)(a) that are related and used in the production process for making taxable supply.

**OUTCOME:**

- Unnecessary hardship is caused to the taxpayers on such disallowance of input tax and the taxpayer has to approach the appellate forum causing wastage of time.

**PROPOSAL**



- Discretionary authority vested with the Department be withdrawn and only those items be disallowed which are specifically stated through SRO or under the law.

**BENEFIT:**

- Taxpayer shall be able to adjust input tax paid on ancillary purchases used for production process for making taxable supply.

## 7. Tax credit not allowed

*Section 8(1)(CA) AND 8(1)(D)*

**ISSUE:**

- The goods in respect of which sales tax has not been deposited in the Government Treasury by the respective supplier (seller) is not allowed as per section 8(1)(ca). Input is also not allowed in case of Fake Invoice is issued as per section 8(1)(d).

**OUTCOME:**

- Punishment to genuine taxpayer (purchaser) who has paid the amount of sales tax to his supplier (seller). It is the responsibility of the supplier to make the payment of sales tax in the Government treasury and it is not possible for a purchaser to ensure that his supplier has deposited the amount or not.
- At the time of issuance of invoice, the seller appears as Active Taxpayer on the web portal of FBR and the purchaser do not have any other option to check the authenticity of the supplier (seller).

## PROPOSAL

- Instead of outright rejecting the input tax, the Department must fulfill its responsibility i.e. to initiate recovery action against the supplier (seller) U/s. 11 of the Sales Tax Act, 1990 and **FBR's responsibility should not be imposed on the taxpayer (buyer) if he has fulfilled the provisions of Section 73**.

**BENEFIT:**

- Genuine taxpayers will be able to claim the input tax duly paid.

## 8. Sales Tax Refund



*Section 10*

**ISSUE:**

- Refund under Chapter V, Rule 33 of the Sales Tax Rules, 2006 is allowed to the claimants to the extent of the input tax paid on Purchases or imports that are actually consumed in the manufacture of goods which have been exported or supplied at the rate of zero percent.

**OUTCOME:**

- Further blocking of the funds in addition to Section 8B and SRO 98, it will be very cumbersome for the taxpayers to get the amount input tax paid on the basis of consumption in the manufacturing of goods exported or supplied at zero rates.

## PROPOSAL

- Requirements under rule 33 of above rules be done away with.

**BENEFIT:**

- Relief to the taxpayers.

## 9. Recovery of short paid amount

*Section 11A*

**ISSUE:**

- The payment of tax less than the tax indicated in the return can be recovered from registered person without giving him a show cause notice as per S. 11A.

**OUTCOME:**

- Violation of principles of natural justice.

**PROPOSAL**

- No action should be taken without issuance of show cause notice.

**BENEFIT:**

- Restoration of confidence of taxpayers.

## 10. Registration

*Section 14*

**ISSUE:**



- At presentsales tax registration process involves at least 60 to 120 days and this time varies according to category of registration requested-for.
- Practicallyfollowing steps are taken after submission of application online and documents of documents through courier to Islamabad:
    - FBR marks it to Collectorate for physical verification in virtually all cases.
    - After physical verification, the concerned Collectorate present report to registration wing of FBR.
    - After receipt of report FBR issue registration certificate to taxpayer.

**OUTCOME:**

- 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.

**PROPOSAL**

- Time limitation as provided in the Sales Tax Rules, 2006, i.e. 15 days, be implemented in latter and spirit.
- Alternatively, FBR should issue a temporary registration number immediately after expiration of 15 days of filing of application, enabling the applicant to initiate his business operation.
- **WE AT KTBA proposes that** basic documents i.e. CNIC, NTN, Chamber / association's membership and bank certificate should be sufficient to verify the genuineness of taxpayers.

**BENEFIT:**

- Speedy process of registration shall result in generating timely revenues for FBR.

## 11. De-registration

*Section 21*

**ISSUE:**

- At present finalization of sales tax de-registration process take at least 6 to 10 months and in some cases more than one year.



**OUTCOME:**

- Taxpayers suffer from uncertainty, mental torture and suspense about the fate of their cases.

**PROPOSAL**

- Time limitation as provided in the Sales Tax Rules, 2006, i.e. 3 months, be implemented in latter and spirit to finalize the process of de-registration.
- If the application for de-registration is not disposed of within the prescribed time period then applicant be considered as de-registered automatically.

**BENEFIT:**

- Taxpayer shall be saved from unnecessary hardships.

## 12. Records

*Section 22*

**ISSUE:**

- During the audit exercise, sometimes the tax authorities call for documents like Audited Accounts, Cost Audit Report, Minutes of BOD, Income Tax Records, etc. which are not prescribed records in section 22 of the Sales Tax Act, 1990.

**OUTCOME:**

- Taxpayers suffer from unnecessary consumption of time and no fruitful objective is achieved besides this being against the law.

### PROPOSAL

- The FBR and Federation of Pakistan Chamber of Commerce & Industry (FPCCI) have already agreed upon records which may be sought by the tax administration during the course of tax audit. This agreement was also made public vide FBR's letter dated 17 November 2001. It is suggested that the suitable amendments may be made in section 22 of the Act by incorporating the above FBR letter as part of the statute.

**BENEFIT:**



- Less cost of compliance and book keeping for taxpayer.

## 13. Multiple Sales Tax Audit

*Section 25*

**ISSUE:**

- As per Section 25 of the Sales Tax Act, 1990, there can only be one audit per year on defined parameters i.e. selection of taxpayers through computer ballot U/s. 72B.
- Multiple audits are conducted under different names, i.e., investigative audit, desk audit, audit for abnormal profile, etc. without following agreed / defined parameters and specified time frame.
- Audit observations are also not submitted within the prescribed time limit.

**OUTCOME:**

- Multiple and prolonged audits are unnecessary and a source of harassment.
- Many officers use audit notices for their ulterior motives.

### PROPOSALS

- There should be a single comprehensive annual audit within fixed parameters by only one agency and be completed within specified time frame once the taxpayer is selected for audit through computer ballot by the FBR alone.
- There should be no authority to re-audit once an audit has been finalized.
- Provisions relating to audit in Sales Tax Act should be implemented in letter and spirit since the prime sufferers are small businesses, punitive clauses should be inserted in tax laws for sales tax officials violating the law.
- On the basis of audit report, if show cause notice is issued, proper opportunity be provided to the registered person to challenge the audit report and no order be passed on the basis of oral request of any person unless the same has been duly recorded on the relevant file.
- If the audit observation is not submitted within 60 days, it will deem to be treated that no contravention/short payment/non-payment has been detected.
- 100% sales to unregistered persons be exempted from audit as full amount of tax has been paid to the government.

**BENEFIT:**

- Savings in time and inconvenience resulting from multiple audits.
- Introduce transparency in audit selection and discourages use of discretionary powers.



## 14. Simplification of Sales Tax Return Form

*Section 26*

**ISSUE:**

- The existing sales tax return contains complicated and un necessary annexure), which are time consuming and requirement of proper staff.

**OUTCOME:**

- The forms such as annex ‘F’ and annex ‘H’ are simply not so relevant or of commensurate advantage and dire need of the Department particularly after introduction of electronic regime.

## PROPOSAL

- Condition for filing un necessary annexure should be curtailed at maximum level to achieve simplification, such details if essentially requires can be made part of annual return.

**BENEFIT:**

- Less cost of compliance and book keeping for taxpayer.

## 15. Revision of sales tax return and time limit

*Sub-section (3) of Section 26*

**ISSUE:**

- 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.

**OUTCOME:**

- 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.

### PROPOSALS

- 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.



**BENEFIT:**

- Less cost of compliance and hassle free business operation for taxpayer.
- Reduction in unnecessary visits to the tax office and end to corrupt practices.

## 16. Time Limitation

*Section 8, 10 & 73*

**ISSUE:**

- Time limit for issuance of Debit & Credit Notes U/s.9 - 80 days
- Time limit for submission of refund claim U/s.10 - 120 days
- Time limit for compliance of proof U/s 73 - 180 days

**OUTCOME:**

- Causes unnecessary hassle and botheration to the taxpayers.

**PROPOSAL**

- Time limitation in all above situations should be extended till one year as no revenue loss is involved in simplification of sale tax law.

**BENEFIT:**

- With extended time periods interaction of taxpayers will reduce with tax collectors. The simplification will increase faith on taxation system and will facilitate the taxpayers.

## 17. Penalties

*Section 33*

**ISSUE:**

- Penalties for non-compliance of section 73 against zero rated supplies are harsh.

**OUTCOME:**

- Taxpayers are unnecessarily being penalized where no loss of revenue is involved.

**PROPOSAL**



- Penalty for non-compliance of section 73 against zero rated supplies be done away with.

**BENEFIT:**

- Encouragement to export sector by removal of unnecessary penalties.

## 18. General penalties and default surcharge

*Section 33 & 34*

**ISSUE:**

- The use of word “shall” in section 33 and 34.

**OUTCOME:**

- Due to the word “shall” under section 33 and 34; any kind of delay in payment will automatically attract penalty/additional tax.

**PROPOSAL**

- The word “shall” be substituted with the word “may”.

**BENEFIT:**

- The Adjudicating officermay have the authority of waiving penalty/additional tax in case if delay is genuine and beyond the control of the registered person.

## 19. Power to call information

*Section 38A & 38B*

**ISSUE:**

- The Commissioner has been given blanket permission to require any person, including a banking company to furnish information or statement in connection with any investigation.

**OUTCOME:**

- Discourage faith of depositors in banking companies.

**PROPOSAL**



- The power given be withdrawn. Moreover, the Lahore High Court has already given its decision against the SBP’s BPRD Circular No.22 dated 30-6-2003 seeking information regarding financial matters of accounts holders.

**BENEFIT:**

- Maintenance of Account holders trust on banks.

## 20. Posting of sales tax officer

*Section 40B*

**ISSUE:**

- A Sales Tax Officer may be posted to the premises of a registered person to monitor his business activities.

**OUTCOME:**

- This is against the government policy to minimize direct contact between a tax collector and tax payer as it may be resulted in corruption and tax evasion.

- It totally negates the concept of self assessment, which forms the basis of whole sales tax scheme.
- It is revival of supervised clearance scheme of central excise in Sales Tax Act.

**PROPOSAL**

- The provision be removed from the statute.

**BENEFIT:**

- Minimize chances of corruption and direct contact between tax collector and payer.

## 21. Power of adjudication *Section 45*

**ISSUE:**

- Omission of Section 45 has resulted in abolition of separate and independent adjudication system under the Sales Tax Act, 1990, which has created problems for the registered persons in obtaining impartial assessment orders pertaining to sales tax liability and disputed matters of sales tax.



**OUTCOME:**

- This existing scenario is against the basic maxim of law that no one can be a judge of his own cause.
- Under the existing system, the taxpayers are left on the mercy of the auditors in the absence of appropriate check and balance system.

**PROPOSAL**

- Provision ofSection 45 may be restored, in order to provide separate powers of adjudication from executive, as applicable in Customs.

**BENEFIT:**

- The discretionary powers of audit officers shall be curtailed and will bring transparency in system, eliminate imbalance between taxation officer and taxpayer.

## 22. Alternative Dispute Resolution Committee (ADRC) *Section 47A*

**ISSUE:**

ADRC forum provides the taxpayer an easy and efficient dispute resolution mechanism to resolve tax related disputes and to liquidate arrears of tax It is an independent body because of the nature of its composition (IR officials and other experts from public and private sectors) and thus has a very strong element of credibility being trustworthy and totally unbiased.

### PROPOSAL

- The recommendation made by the Committee should be accepted in a letter & spirit, unless there is any apparent mistake.
- That instead of communicating the agreement to the appellate forum, the appeals filed by the respective parties should be withdrawn.
- Cogent reasons including dissenting notes by the ADR Member must properly be provided and incorporated in the Order issued by the FBR.
- Proper rules may be framed for formation of the committee, scope of work, conducting of ADR proceedings, stay of matter/demand, disposal of application by the ADR Committee, retention of record, remuneration for members of ADRC and etc.



**BENEFIT:**

- Efficient use of ADRC will generate more taxes to the Government exchequer.

## 23. Recovery of Arrears *Section 48*

**ISSUE:**

- It gives overwhelming powers to tax officials for recovery of arrears but fails to include clauses that restrain the authorities from committing excesses. For pending matters, even involving minor liability, undue pressure is imposed on taxpayers by exercising section 48.

**OUTCOME:**

- For recovery of tax, penalty or any other demand raised, the officer of Inland Revenue has the same powers which under the Code of Civil Procedure 1908 (V of 1908), a Civil Court has for the purpose of recovery of an amount due under a decree.

**PROPOSAL**

- All cases should be decided as per the strict interpretation of law. Section 48 should not be exercised unless the case under litigation has undergone two appellate proceedings. Thereafter, a stage wise partial recovery of the principal amount involved can be considered.

**BENEFIT:**

- Taxpayers will be saved from the possibility of undue harassment and misuse of law.

## 24. Action against Tax Officer

**ISSUE:**

- Different time limits and specific provisions are provided under sales tax act which intact the right of tax payer, however normally no importance given to such provisions by tax officers.

**OUTCOME:**

- Non-compliance of act by tax officer causes mistrust, loss in faith of law and shakes confidence of investors/tax payers.



**PROPOSAL**

- A new section 67-A be inserted in sales tax act, 1990 which should provide appropriate action against non-compliance or late compliance, to fix the responsibility and to place proper check and balance.

**BENEFIT:**

- Recourse to seek justice would be available to the taxpayer.

## 25. Sales tax on information technology @ 16%

**ISSUE:**

- Sales tax exemption on Information Technology i.e. Computer Hardware & Computer Software is withdrawn.

**OUTCOME:**

- Making computer a taxable item will badly damage the scope of education, literacy and employment for masses.

## PROPOSAL

- 16% GST on Information technology may be exempted.

**BENEFIT:**

- Hardware and software are an integral part of IT and it can help in increased economic activity.

## 26. Charitable Institutions / Non-Profit Organization

**ISSUE:**

- Unlike Income Tax Law, there is no concept of allowing exemption / zero-rating of sales tax for charitable institutions under the Sales Tax law except the following exemption available under clause 52A of Sixth Schedule to the Sales Tax Act 1990:

> ***"52A. Goods supplied to hospitals run by the Federal or Provincial Governments or charitable operating hospitals of fifty beds or more or the teaching hospitals of statutory universities of two hundred or more beds."***



**OUTCOME:**

- None of the charitable institutions, except some hospitals falls within the ambit of aforesaid clause 52A.

## PROPOSAL

- Following amendment is suggested to provide zero-rating for charitable institutions that are considered and recognized as non-profit organizations under the Income Tax law:

In the Fifth Schedule, the following entry shall be inserted:

| Serial No. | Description |
|---|---|
| (1) | (2) |
| 2A. | Supplies to a non-profit organization as defined in Section 2 (36) of Income Tax Ordinance 2001 |

**BENEFIT:**

- Charitable institutions / Non-profit organizations will be saved from undergoing unnecessary hardships.

## 27. Issues related to Refunds

**ISSUE:**

**RELATED TO STARR AND DOCUMENTATION**

- At present, huge genuine export and non export refunds are blocked with the department resulting in liquidity problems for the taxpayer and resultant litigation. The following are the core issues in refunds:

- For refunds not replicated over STARR, the department desires the refund claimant (buyer) to furnish seller's returns, accounts, statements, etc.. This requirement does not find place in Rule 38 of Sales Tax Rules 2006

- In the absence of any legal support, the seller declines to share / furnish his returns and other statutory declarations with the buyer (refund claimant)

- In certain cases, the department directly contacts the respective supplier to verify the genuineness of the refund claim; however in other cases, the onus of verification is transferred upon the refund claimant

- The Large Taxpayers' Unit (LTU) Karachi has recently discontinued manual over ruling of STARR objections



**PROPOSAL**

- To streamline the entire refund verification and sanctioning process, it is proposed that a comprehensive refund mechanism may be put in place for the whole country in the light of the Section 10 and Sales Tax Rules 2006. Further, Rule 38 may be amended to include list of supplier's documents for cross verification of payment of output tax by seller and the Commissioner LTU, Karachi may be directed to follow the procedure of manual over-ruling as practiced in rest of Pakistan.

**ISSUE:**

**TIME LIMIT OF 60 DAYS WHICH HAS BEEN EXTENDED TO 120 DAYS**

- Rule 28 of the Sales Tax Rules, 2006 provide that no refund claim shall be entertained if the claimant fails to furnish the claim on the prescribed software (RCPS) along-with the supportive documents within one hundred twenty days of filing of return.

- It will be appreciated by the Board that due to number of genuine and practical problem it is very difficult for a registered person to submit all supportive documents along with the information on the prescribed software (RCPS) within the prescribed period of one hundred and twenty days.

- It will be pertinent to mention here that the aforesaid software itself has so many in built checks that it's a Herculean task for a registered person to submit his refund claim within the prescribed time limit.

- Furthermore, neither section 10 nor any other section in the Sales Tax Act, 1990 empowers the Federal Board of Revenue to put any time limit on the registered person for submission of documents.

**OUTCOME:**

- As it is registered person's money that at the disposal of the Department, therefore, if the taxpayer files his supportive documents late, then he is not causing any revenue loss to the government exchequer.

- As a matter of fact by filing the documents late the registered person is giving an opportunity to the Government to use his money without any interest.

- Moreover, there is not a single registered who would deliberately delay the submission of supportive documents as he will be interested in getting his money back as soon as possible; its only due to some genuine and unavoidable circumstances he has to delay the submission of supportive documents.

**PROPOSAL**



- It is, therefore, requested to kindly remove the un-necessary limitation of one hundred and twenty days on filing of his supportive documents. However, as no transaction can be left open for unlimited period, therefore, it is proposed that the time limit of one hundred of twenty days may be increased to one year to bring it in line with the time limit already allowed for filing refund claim under section 66 of the Sales Tax Act, 1990.

## 28. Adjustment of sales tax refund with income tax liability

**ISSUE:**

- It has been seen that on number of occasion registered person's funds are stuck with the Inland Revenue in the form of sales tax refund and at the same time the taxpayer is required to pay income tax at the time on assessment of his income tax liability. Resultantly, the taxpayer has to bear the burden of making payment of income tax liability whereas his own money is lying idly with the Inland Revenue.

**PROPOSAL**

- Board vide letter C.No. 3(70)STM/99 dated: 20th December 1999 has already devised a procedure of inter-tax refund / adjustment; but both sales tax and income tax department are not

following the above said procedure for the reason best known to them. It is, therefore, proposed that a very simple and unambiguous procedure may be notified for adjustment sales tax refund with the income tax liabilities in order to alleviate the unnecessary cash flow problems faced by the registered persons.

## 29. Refund on Building Materials, Steel, Etc

**17.5**

After the suppression of SRO 578(I)/98 dated 12 June 1998 through SRO 490(I)/2004 dated 12 June 2004, sales tax paid on building materials has become eligible for refund / adjustment purposes. However, the Regional Tax Office, Karachi has placed certain other conditions attached to the refund claim such as filing of Approved Building Plan, BOQ, Counter Confirmation from respective Trade Association, etc. Such requirements are not spelled out either in the statute or the rules.

### PROPOSAL

In line with the statute and the related judgments of the superior courts, it is proposed that the relevant Standing Order issued by RTO, Karachi may be withdrawn and refunds may be allowed on building materials without any exception.

**17.6 Refunds under Section 66**



**Legal Position:**

> "No refund of tax claimed to have been **paid** or over paid through inadvertence, error or misconception shall be allowed, unless the claim is made within one year of the date of payment…"

**Departmental Interpretation**

> "No refund of tax **claimed** shall be allowed, unless the claim is made within one year of the date of payment…"

### PROPOSAL

In line with an identical case law pronounced by the High Court, the FBR should clarify that where the tax claimed as refund was not paid due to inadvertence, error or misconception, the time limit of one year will not be applicable. Accordingly, all claims not falling under the above should be admissible and entertained without any time limit. The Supreme Court has already held that no limitation of time can be placed upon filing and sanctioning refunds.

### 17.7 Accounting for Refunds

In recent cases, the tax authorities have started rejecting refund claims where such claims were not booked as receivable in the taxpayers' audited accounts. In support of such contention, the tax authorities contend that non recording of refund as receivable from government tantamount that the sum of claimed was charged off in cost of sales; thus becoming part of selling price which was ultimately recovered from the customers. Therefore, such claims were rejected under Section 3B of the Act.

## PROPOSAL

The explicit provisions of the Act make no distinction between corporate and non-corporate taxpayers. In quite a few cases, because of the contingent nature of refunds due to interpretational/ legal issues and in line with internationally accepted and practiced accounting convention, the taxpayer could not book it as receivable in the accounts. It is, therefore, suggested that refund cases may be examined only in the light of documents prescribed under section 22 of the Act.

**END**