The Institute of Chartered Accountants of Pakistan

ICAP

ICAP PROPOSAL

FOR FEDERAL AND PROVINCIAL BUDGET 2025-26

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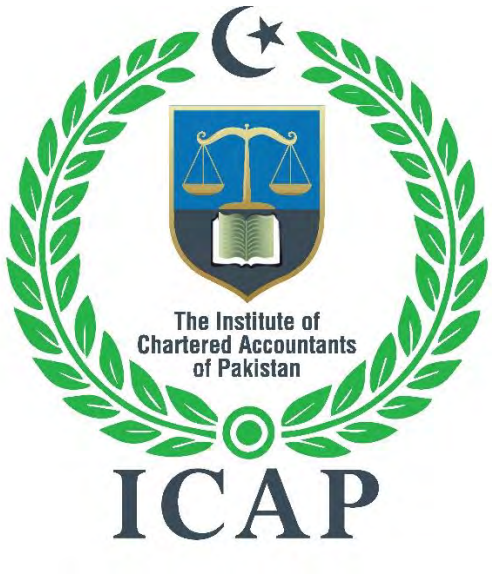
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MESSAGE FROM THE PRESIDENT

As Pakistan stands at a pivotal economic juncture, the imperative to design a progressive, equitable, and growth-oriented fiscal framework has never been more urgent. The Institute of Chartered Accountants of Pakistan (ICAP), in its enduring commitment to national development, is proud to present its tax policy proposals for the Federal and Provincial Budgets 2025–26.

These proposals are the result of rigorous deliberations and insights from Pakistan's leading chartered accountants and tax professionals, deeply rooted in the principles of transparency, inclusivity, and long-term economic resilience. Our focus remains steadfast on broadening the tax base, enhancing compliance, curbing distortions in the system, and advancing fiscal responsibility through a rational and facilitative tax regime.

The persistent reliance on indirect taxation continues to disproportionately affect lower-income segments, impede documentation, and undermine equity. It is imperative that we transition toward a direct, progressive taxation framework that promotes fairness and economic formalization. In this spirit, our proposals seek to support a more predictable, efficient, and sustainable tax structure that fosters trust between the state and its citizens.

I commend the ICAP Committee on Fiscal Laws for their diligence and vision in developing these comprehensive recommendations. Their work reflects ICAP's broader mission—to be a constructive partner to the government and a catalyst for economic reform.

Let us strive collectively for a fiscally empowered, transparent, and just Pakistan.

Saif Ullah, FCA
President
The Institute of Chartered Accountants of Pakistan

MESSAGE FROM THE CHAIRMAN

The Institute of Chartered Accountants of Pakistan (ICAP) remains steadfast in its mission to contribute meaningfully to Pakistan's economic advancement through prudent fiscal recommendations and professional insight. As part of this ongoing commitment, we are pleased to present our proposals for the Federal and Provincial Budgets 2025–26, developed with the objective of fostering a transparent, efficient, and equitable taxation regime.

In the face of mounting fiscal challenges, there is an urgent need to shift from fragmented, short-term fixes toward strategic, systemic reforms. Our proposals focus on broadening the tax base, improving tax administration, addressing structural inefficiencies, and enhancing compliance mechanisms to drive sustainable revenue growth.
We reiterate the critical need to reduce dependence on regressive indirect taxation, which disproportionately burdens vulnerable populations and constrains economic progress. Direct taxation, aligned with the principles of equity and economic justice, must form the cornerstone of our tax policy going forward.

A restructured approach is needed—one that clearly demarcates tax policy from administration, fosters institutional autonomy, and leverages digital tools for effective enforcement and data integration. Equally essential is the harmonization of provincial and ICT sales tax frameworks on services, ensuring consistency, eliminating duplication, and simplifying compliance for nationwide service providers.

We advocate for a "One Nation, One Tax" vision, where unified processes, returns, and regulations guide the indirect taxation system, enhancing transparency and inter-jurisdictional coherence.

I would like to express my heartfelt gratitude to all members of the committee for their invaluable support, with special appreciation for the conveners of the subcommittees: Mr. Kamran Iqbal Butt, Mr. Asif Siddiq, Mr. Haider Ali Patel, Mr. Asif Haroon, Mr. Khalid Mahmood, Mr. Rizwan Bashir, and Mr. Sharif-ud-din Khilji. I am also grateful to Mr. Mansoor Zaighum, Mr. Adil Jillani, Mr. Mohsin Nasrullah, Mr. Aamir Younas, Mr. Mohammed Muzammil, Mr. Raza Toor, and Mr. Yasir Gadit for their dedicated contributions. My sincere thanks also go to Mr. Nafeh Akbar and Mr. Furqan Atique for their valuable assistance throughout the process.

Zeeshan Ijaz, FCA
Chairman – Committee on Fiscal Laws
The Institute of Chartered Accountants of Pakistan

GLOSSARY OF TERMS

BSTSA	Balochistan Sales Tax on Services Act 2015
BSTSR	Balochistan Sales tax on Services Rules 2018
EOBI	Employees' Old-Age Benefits Institution
FEA	Federal Excise Act, 2005
FED	Federal Excise Duty
FER	Federal Excise Rules 2005
ITO	Income Tax Ordinance, 2001
ITR	Income Tax Rules, 2002
KSTSA	Khyber Pakhtunkhwa Sales Tax on Services Act 2013
KPKWTR	Khyber Pakhtunkhwa Sales Tax on Services Special Procedure (Withholding) Regulations 2015
PATR	Punjab (Adjustment of Tax) Rules 2012
PSTSA	Punjab Sales Tax on Services Act 2012
PSTSPR	Punjab Sales Tax on Services (Special Provisions) Rules 2012
PSTWTR	Punjab Sales Tax on Services (Withholding) Rules 2015
SESSI	Sindh Employees' Social Security Institution
SSTSA	Sindh Sales Tax on Services Act 2011
SSTSR	Sindh Sales Tax on Services Rules 2011
SSTWTR	Sindh Sales Tax Special Procedure (Withholding) Rules 2014
STAWTR	Sales Tax Special Procedure (Withholding) Rules 2007
ST/STA	Sales Tax Act 1990
STR	Sales Tax Rules 2006
WPPF	Workers' Profit Participation Fund
WWF	Workers' Welfare Fund
WeBOC	Web Based One Customs

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FEDERAL TAXATION

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FEDERAL TAXATION

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1.01 MINIMUM TAX REGIME

HIGH

The Institute highly appreciates the policy change of moving from Final Tax Regime to Global Taxation of Income subject to Minimum Tax under various provisions of the Income Tax Ordinance, 2001. However, this transition from FTR to MTR coupled with multiplicity of minimum taxes has brought alongside various legal, factual and computational issues, which need serious consideration of the Tax Policy Wing of the Federal Board of Revenue. These are enumerated below for reference:

I. Treatment of Opening and Closing Stocks of imports by other than industrial undertaking

The applicability of Minimum Tax is with reference to tax payable on the income for the year from such imports. However, in almost all cases of other than an industrial undertaking the corresponding income relating to closing stocks of such imported goods does not form part of the current year (the year of import of goods) income and on the other hand the income arising from the opening stock forms part of the current year income (though not imported during the current year). The law is silent as to its treatment and no uniform method to offset the effects of opening and closing stock of such imported goods exists (i.e., matching concept).

II. Comparison of Minimum Tax

It goes without saying that the word "Minimum" when and wherever used postulates that there exists something else to make a comparison with e.g.-

- *For the purpose of minimum tax under Section 113 "tax payable" on taxable income for the tax year is compared with the minimum tax (amount worked out by applying the applicable percentage on the turnover); and*
- *For the purpose of alternative corporate tax under Section 113C "Corporate Tax" is compared with "Alternative Corporate Tax "both defined in section 113C (2)*

Contrary to the foregoing, all the provisions relating to withholding tax being Minimum Tax do not provide for the other component for the purposes of comparison.

The main reason of the deficiency pointed out above is the replacement of the word "Final" with "Minimum", without considering other consequential amendments required. Another reason for this deficiency is that the legislators did not took into consideration the majority of the cases with composite sources of income i.e., both income subject to minimum tax and not subject to minimum tax as well.

III. Problems in following Mercantile System of Accounting

- In case of taxpayers following "mercantile system of accounting" (accrual-based accounting), taxable income is determined irrespective of the fact whether revenue and expenses are received or paid. On the other hand, all the provisions of withholding tax apply at the time of making the payment or clearance of goods, which is Applicable on all Companies;
- Adopted by all Sales Tax Registered Individuals and AOPs (to reconcile sales as per sales tax return and as per income tax return);
- Adopted by most of the Individuals and AOP's even otherwise; and
- Taxable income for the year is determined irrespective of the fact whether revenue and expenses are received or paid. On the other hand, all provisions of withholding tax also apply at the time of making the payment or clearance of goods.

In all such cases, there is every possibility that:

- Taxable income declared for the year is inclusive of income in respect of unrealized revenue (under mercantile system) on which withholding provisions will apply in the following year(s);
- Taxable income declared for the year is exclusive of income in respect of realized revenue relating to preceding year(s) on which withholding provisions will apply in the current year;
- Taxable income declared for the year is exclusive of income in respect of stock-in-hand of un-sold imports on which withholding provisions will apply in current year;
- Taxable income declared for the year is inclusive of income in respect of brought forward stock-in-hand from the previous year of commercial imports on which withholding provisions had applied in preceding year.

IV. Implications of the word "deductible" used in various withholding tax provisions under the Income Tax Ordinance, 2001:

Under almost all withholding tax provisions the time of collection or deduction of tax by the withholding agent is at the time of making the payment, e.g., Section 153(1) reads "…shall, at the time of making the payment, deduct tax from."

Similarly, under various withholding tax provisions the tax collectible or deductible (as stated above) is the minimum tax, e.g., Section 153(3) reads *"The tax deductible under sub-section (1) and under sub-section (2) of this section, on the income of a resident person, shall be minimum tax"*.

Some of the professionals are of the view that the word "deductible" used in provisions declaring tax deducted as minimum tax, e.g., *section 153(3), will cover the entire sales made during a tax year to a withholding agent irrespective of the fact whether payment has been made and tax has been deducted by the withholding agent or not.*

On the other hand some of the professionals are of the view that the word "deductible" used in provisions declaring tax deducted as minimum tax, e.g., section 153(3), should not be read in isolation and should be read in conjunction with the main section dealing with deduction of tax, e.g., section 153(1), which defines the time of deductibility of tax (i.e., at the time of making the payment) and therefore, if the payment has not been made, the tax on such un-paid amount could not be classified as "deductible" for the purpose of provisions declaring tax deducted as minimum tax, e.g., section 153(3).

Precisely, this gives rise to the issue of treatment of un-realized sales of the year out-standing on the last day of tax year (Trade Debtors, who are withholding agents) i.e., whether such out-standing sales, the income of which is reflected in the taxable income of the current tax year and normal tax thereon is being paid will be included in the sales subject to minimum tax or not.

V. Rate of Minimum Tax for persons not appearing in active taxpayers list

Under the 10th Schedule the rate of withholding tax (in particular those falling under final and minimum tax regime) are increased by 100% in case the person is not appearing on the active taxpayers list.

However, after the end of the financial year or after the provisional assessment is made, if the taxpayer furnishes the return of income, the applicable rate of tax, in view of provisions of section 169(4), will be those as applicable to a person appearing on the active taxpayer list and the excess deduction can be claimed as refund.

Contrary to above, in the absence of any provision parallel to section 169(4) for the purposes of minimum tax, the tax deducted or collected in respect of transactions falling under minimum tax regime at 100% higher rates will be the minimum tax. This means that:

- The return forms (in particular "final / fixed / reduced / relevant" and "minimum tax regime") has to also provide for such 100% increased rates; and
- No incentive to taxpayers to become filers.

VI. Attributable Income for the purposes of Minimum Tax [Problems in IRIS]

IRIS calculates attributable Income on transactions subject to Minimum Tax by apportioning the entire cost of sales, administrative expenses, selling expense and financial expenses considering the same as common cost/expenses for different segments of the business in total disregard to the provisions of *section 67 of the Income Tax Ordinance, 2001 read with Rule 13 of the Income Tax Rules, 2002, which provides for apportionment of only common expenditures and not the directly attributable expenses;*

IRIS calculates attributable Income on transactions subject to Minimum Tax by applying Section 67 of the Income Tax Ordinance, 2001 read with Rule 13(2)(a) of the Income Tax Rules, 2002 and completely ignoring the alternate method provided in Rule 13(2)(b) of the Income Tax Rules, 2002.

IRIS calculates attributable Income on transactions subject to Minimum Tax by applying the formula: A/B x C.

Where;

A is the Taxable income from business; divided by

B is the Total Turnover subject to normal tax; multiply by

C is the Turnover of the respective transactions subject to Minimum Tax

The formula is correct, but component B is taken exclusive of Sales Tax and component C is taken inclusive of Sales Tax, hence this needs to be rectified for correct computation of attributable income e.

VII. Multiplicity of Minimum Taxes;

Considering the complex landscape created by multiple minimum tax provisions in the Ordinance, it is proposed to revisit the provisions wherein tax withheld at source under various provisions has been made minimum tax.

It is pertinent to mention that section 113 was already in place charging minimum tax on the income of persons declaring loss or claiming exemptions. The purpose of withholding tax provisions was documentation of economy/transactions to enforce the charging provisions; however, these provisions have wrongly been used as revenue generating measures by treating the tax withheld at source as minimum tax which was either adjustable or final tax previously. Furthermore, there is no provision allowing carry forward of excess tax paid for adjustment in future years like provisions of carry forward in section 113. This has resulted in a parallel tax regime which is not supported by or coherent with the charging provisions of the Ordinance, therefore, treating withholding tax as minimum tax liability is unfair and confiscatory in nature and considering the high rates of withholding, section 113 has effectively been made redundant by treating tax withheld as minimum tax. This view has also been endorsed by the Appellate Tribunal Inland Revenue (ATIR) in ITA no. 1313 dated May 5, 2021, whereby, ATIR declared the minimum tax regime under Section 153 unconstitutional in the presence of Section 113 and non-existence of charging provisions supporting minimum tax regime under various provisions.

Recommendations

- In order to overcome the above issues, and in particular the complexity of multiple minimum taxes the first recommendation is that provisions treating tax withheld as minimum tax be withdrawn.
- However, to safeguard the revenue concern, existing rates of withholding tax be prescribed in section 113 of the Ordinance in respect of transactions subject to withholding tax. For this purpose, following amendments are proposed in the Ordinance–

  a. In section 113 –

     i. In sub-section (1) the words, bracket and figures "(having turnover of hundred million rupees or above in the tax year 2017 or in a subsequent tax year)" appearing twice shall be omitted;

ii. In clause (e) of sub-section (1), the words, bracket and figures "percentage as specified in column (3) of the Table in Division IX of Part I of the First Schedule of the amount representing the person's turnover from all sources for that year" shall be substituted by words, bracket and figures "sum of minimum tax payable as specified in Serial No. 1 to 4 of column (3) of the Table in Division IX of Part I of the First Schedule"

b. Sub-section (7) of section 148 shall be substituted as under –

"The tax required to be collected under this section shall be adjustable."

c. Sub-section (7A) of section 148 shall be omitted.

d. Sub-section (1B) of the section 152 shall be substituted as under –

"The tax deductible under sub-section (1A), (1AA) and (1AAA) shall be adjustable."

e. Sub-section (2B) of the section 152 shall be substituted as under –

"The tax deductible under sub-section (2A) shall be adjustable."

f. Proviso to sub-section (2B) of the section 152 shall be omitted.

g. In sub-section (4A) of section 152, after the word "tax" appearing for second time, the words and figures "under section 113" shall be inserted.

h. Sub-section (3) of the section 153 (, including provisos and explanation) shall be substituted as under –

"The tax deductible under this section shall be adjustable."

i. In sub-section (4) of section 153, after the word "minimum", the words and figures "tax under section 113" shall be inserted.

j. Sub-section (2B) of section 233 shall be omitted.

k. Sub-section (3) of the section 233 (including the explanation) shall be substituted as under –

"The tax deductible under this section shall be adjustable."

l. Sub-section (3) of the section 236CA shall be substituted as under –

"The tax required to be collected under this section shall be adjustable."

m. In Division XI, Part -I, First Schedule the Table should be rationalized:

- Introduce provisions for the purposes of tax collected or deducted as minimum tax similar to section 169(4) dealing with final tax regime and also make corresponding amendments in section 148(7), 152(2B) and 154(5). The draft of which is as under:

"**169A. Tax collected or deducted as a minimum tax. —**

(1) This section shall apply where the tax required to be collected or paid is a minimum tax under sub-section (7) of section 148; or the tax required to be deducted or paid is a minimum tax under sub-sections (1B), and (2B) of section 152, sub-section (3) of section 153, 2nd proviso to sub-section (5) of section 154, sub-section (2B) and (3) of section 233, , proviso to sub-section (2) of section 236C or sub-section (3) of section 236CA.

(2) Where this section applies —

(a) Minimum tax is on the attributable taxable income relating to transactions subject to collection or payment of tax under sub-section (1) of section 148; or minimum tax is on the attributable taxable income relating to transactions subject to deduction or payment of tax under sub-sections (1A), (1AA), (1AAA) and (2A) of section 152, sub-section (1) and (2) of section 153, section 154, sub-sections (1) and (2A) of section 233 or sub-sections (1) and (2) of section 236CA.

(b) "Attributable tax" means amount of tax on attributable taxable income arrived at as under: A / B X C

Where;

A is the amount of tax on taxable income;

B is the amount of taxable income; and

C is the amount of attributable taxable income

(c) "Tax on taxable income" means:

(i) Income tax on taxable income computed by applying the rate or rates of tax specified in Division I or II of Part I of the First Schedule.

(ii) Reduced by adjustment of brought forward minimum tax u/s 113 from earlier years and u/s 113C from earlier years.

(iii) Reduced by tax reduction under sub-clause (2) of clause (1) and clause (6) of Part III of second schedule and tax credits u/s 61, 62, 62A, 63, 64B, 64D, 65E, 65F, 65G and 103; and

(iv) Increased by difference of Minimum Tax Payable for the year u/s 113 or 113C as applicable for the tax year."

(d) "Taxable income" does not include income subject to fixed tax as a separate block, i.e., monetization of conveyance, golden handshake, arrears of salary, capital gains on disposal of securities and capital gains on disposal of immovable property.

(e) "Attributable taxable income" means taxable income apportioned in accordance with section 67 of the Ordinance and related rules under the Income Tax Rules, 2002 in respect of transactions subject to collection or deduction of tax under the Ordinance as minimum tax.

(f) where the attributable tax on the attributable taxable income under the respective provisions referred to in clauses (a) and (b) of sub-section (2) is less then minimum tax collectible or deductible under the said sections, then the minimum tax collectible or deductible under that section shall be the amount of tax payable on such attributable taxable income instead of attributable tax.

(g) where the minimum tax exceeds the attributable tax, the excess amount of tax shall be carried forward for adjustment against tax on taxable income computed by applying the rate or rates of tax specified in Division I or II of Part I of the First Schedule of the subsequent tax year:

Provided that the amount under this clause shall be carried forward and adjusted against tax on taxable income computed as above for five tax years immediately succeeding the tax year for which such excess amount was determined.

(h) Subject to clause (j), there shall be no refund of the tax collected or deducted unless the tax so collected or deducted is in excess of the amount for which the taxpayer is chargeable under this Ordinance.

(i) Where a taxpayer has paid tax in a tax year on a transaction on which tax has been collected or deducted in the following tax year or tax years, such tax collected or deducted in the following tax year or tax years shall be refundable; and tax collectible or deductible has not been collected or deducted, or short collected or deducted, the said non-collection, non-deduction, short collection or short deduction may be recovered u/s 162, and all the provisions of this Ordinance shall apply accordingly.

(j) Where all the income derived by a person in a tax year is subject to minimum tax under the provisions referred to in sub-section (1), the person shall be required to furnish a return of income u/s114 for the year.

(k) Where the tax collected or deducted is minimum tax under any provision of this Ordinance and hundred percent higher tax rate has been prescribed for the said tax under the Tenth Schedule, the minimum tax shall be the tax rate prescribed in the First Schedule and the excess tax collected or deducted under the Tenth Schedule specified for persons not appearing in the active taxpayers' list shall not be minimum tax, in case the return is filed before finalization of assessment as provided in Rule 4 of the Tenth Schedule.

This section shall be deemed to have been inserted with effect from July 01, 2019."

1.02 REPLACING WITHHOLDING TAX REGIME WITH ADJUSTABLE ADVANCE TAX REGIME FOR LISTED COMPANIES

HIGH

The corporate sector taxpayers are compliant taxpayers and contribute significantly to the tax revenue, but they are still exposed to several challenges including very stringent and cumbersome ever-expanding withholding tax regime and facing difficulties in getting credit of withholding taxes due to non-availability of CPRs or late or non-deposit of withholding tax by the withholding agents or their non-verification in the FBR's electronic database.

As a first step, the FBR should seriously consider lifting the burden of withholding taxes and substituting it with payment of monthly advance tax in case of listed companies. Accordingly, it is proposed that instead of exposing the listed companies to a large number of withholding taxes on their income and expenditure, amend Section 147 of the ITO for the listed companies to make them pay the advance tax on a monthly basis, instead of quarterly.

Rationale

Implementation of this proposal will lift a significant burden from the listed companies and make the life of FBR officials easier as they would be getting the payment of taxes on a monthly basis directly from the taxpayers instead of through withholding agents. It would also substantially reduce the unnecessary documentation and hassle of verification and risk of withholding agents committing frauds. It will also improve the cash flow of the companies and minimize the exposure of tax refunds.

1.03 WITHDRAWAL OF ALTERNATIVE CORPORATE TAX (ACT) U/S 113C

HIGH

Whilst there is already a minimum tax regime which imposes tax on the gross turnover u/s 113, alongside minimum tax regime for supplies, services, etc. under various section of the Ordinance, and ACT, which actually operates as alternative minimum tax regime, for the corporate sector (with exceptions), has rendered the computation of income and tax liability very complex for the corporate sector. It is also noted that the ACT rate, which was fixed at 17% by the Finance Act, 2014 (i.e., 50% of the corporate tax rate then applicable) remained unchanged whereas the rate of corporate tax has reduced from 34% to 29%, and in case of small companies, the rate was reduced from 25% to 20% in 2024. On the other hand, the rate of minimum tax u/s 113 is increased from 0.5% to *1.25%*.

In addition to the above, an important thing to note is that an exception provided in sub-section (8) of section 113C states that it would not be applicable on any receipts subject to minimum tax under any of the provisions of the Ordinance. This effectively makes ACT redundant and only results in taxing anomalies created due to various accounting treatments under IFRS which otherwise would not have been taxable.

Considering the above, it is strongly proposed that the ACT should be withdrawn; or the rate be revised downward to 50% of the current normal corporate rate of tax applicable to the companies.

Rationale

The minimum tax regime of ACT at such a high rate in the presence of two more Minimum Tax Regimes is highly unreasonable and discriminatory. Only one type of Minimum Tax Regime should be applicable on the taxpayer.

1.04 SLAB RATES OF TAX FOR SALARIED INDIVIDUALS

HIGH

Over the past few years, tax rates applicable to salaried individuals have been increased significantly, resulting in a higher tax burden. Additionally, the minimum taxable threshold for salary income remains fixed at Rs. 600,000 per annum, a limit that has not been revised for the past two years. During this period, inflation has risen sharply, eroding the real purchasing power of salaried individuals.

Resultantly, many low-to middle income earners are now being pushed into the taxable bracket, despite facing rising living costs. Moreover, the current threshold fails to account for inflationary pressures and increasing basic expenses such as housing, utilities, transportation, and education. The combined effect is a disproportionate tax burden on salaried individuals, particularly those with fixed incomes and limited tax planning options.

Recommendation:

It is recommended that the minimum taxable threshold for salaried individuals is revised upward to Rs.1,200,000 from Rs.600,000 to reflect current inflationary trends, thereby ensuring that only individuals with reasonable disposable income are brought into the tax net.

Simultaneously, a review of the existing tax slab rates should be undertaken to ease the burden on salaried classes, especially in low and middle-income brackets.

Rationale:

Adjusting the threshold and rationalizing tax rates in line with inflation will:

- Promote equity and fairness in taxation,
- Help maintain the real income and consumption capacity of salaried individuals,
- And foster voluntary compliance by ensuring that taxation does not become excessively burdensome on the formally employed sector.

1.05 SALARY U/S 12

HIGH

Income under the head "salary" is currently taxed on the gross amount. This policy was introduced by bringing down the corresponding rates of tax for each income slab. However, gradually the income slabs as well as rates of tax were enhanced without restoring the deductible allowances when income from salary was taxed at higher rates.

The withdrawal of tax credits under Sections 62 and 62A through the Finance Act, 2022 has further increased the effective tax burden on salaried individuals. These credits previously provided relief for investments in mutual funds, pension funds, and life insurance, which served as important tools for promoting savings and financial security among middle- and upper-middle-income earners.

Recommendation

To address the growing tax burden on salaried individuals, it is proposed that:

1. **Tax Rates Rationalization or Restoration of Exemptions:**

   Either rationalize the existing tax rates applicable to salaried individuals, or reinstate exemptions for common employment-related allowances such as:

   - House rent allowance,
   - Interest on house financing,
   - Utilities,
   - Conveyance.

   These exemptions were historically available and served to offset living costs borne by employees.

2. **Consider Passive Income in Context:**

   In many cases, income from other sources (e.g., bank interest or rental income) is passive in nature and does not alter the individual's primary status as a salaried taxpayer. Such passive

income should not disqualify individuals from accessing the concessional tax regime intended for salaried earners.

Rationale

It is inequitable to subject salaried individuals—especially those in higher income brackets—to elevated tax rates without corresponding exemptions or deductions, particularly when business and professional taxpayers are taxed on net income after deducting expenses. Salaried persons, whose incomes are fully documented and taxed at source, face a disproportionate tax burden under the current regime. A fairer approach is needed to ensure horizontal equity across taxpayer categories and to maintain taxpayer morale and compliance.

1.06 DEDUCTION OF TAX FROM PAYMENT OF SALARY U/S149

HIGH

The employer is entitled to make certain adjustments from the average rate of tax for the purposes of deducting tax from payment of salary, which includes tax credits u/s 61, 62 and 63.

It is proposed to rewrite this section to provide full coverage to the following provisions of the ITO for computation of withholding tax due from salary by the employer in each tax year:

- Allow adjustment of "Deductible allowances" available under Part IX of Chapter III of the ITO.
- Allow adjustment of "Tax credits" available under Part X of Chapter III, read with Second Schedule, of the ITO.
- Allow adjustment of tax collected at source as is adjustable under the ITO; and
- Allow application of average rate of tax of preceding three tax years for determination of withholding tax on payments received by an employee under sub-clause (iii) of clause (e) of sub-section (2) of section 12 of the ITO.
- Allow adjustment of "tax refund" claimed by the employee in the return of income of previous years, if the employee has submitted the refund application but has been pending with the tax authorities for more than six months without issuance of refund.

Rationale

The amendments are necessary to ensure that the employees are allowed full adjustments of all withholding taxes deducted or collected and tax credits and the employees do not suffer tax in excess of what is due.

It will provide relief to compliant taxpayers who are adversely impacted by delays in refund processing and will also improve cash flow for salaried individuals and reduce dependency on prolonged administrative processes. Moreover, it will incentivize tax compliance by trust in the efficiency and fairness of the tax system.

1.07 TAXATION OF AOPs OF PROFESSIONALS U/S 92 & 93

HIGH

The income of association of persons (AOP) of the professionals, which are prohibited from incorporating as a limited company, should not be taxed in hands of the AOP and instead share of each partner / member be taxed in his/her hands equated with salary income or rate applicable for business individuals for the purposes of determining the tax liability.

For this purpose, sub-section (2), (3), (4) and (5) of u/s 92 and u/s 93 of the ITO omitted by Finance Act, 2007 should be restored.

Alternately if this is not possible, then rate of tax of AOP prohibited from converting into a company may be equated with the rate of tax applicable to corporate sector i.e., 29%. This will provide alignment of the tax rate with that of the company and provide a level playing field for such AOPs having limitation in forming themselves into a company.

Rationale

Professionals like Architects, Accountants, Advocates etc., are not allowed by their respective governing statues to form a limited liability company. Thus, the professionals have no alternative but to join hands in the status of an AOP. This brings the AOP of professionals at a disadvantageous

position in respect of effective tax rate as compared with a company, since member's salary is not a deductible expenditure, whereas in case of a company, director's remuneration is a deductible expenditure, and such remuneration is taxed at rates applicable to a salaried individual. Further, where the members of such AOP have no other taxable income, they are deprived of all deductible allowances and tax credits available under the ITO.

1.08 GREENFIELD INDUSTRIES

HIGH

Through the Tax Laws (Second Amendment) Ordinance, 2019, the term Greenfield industries was defined in the Income Tax and Sales Tax laws.

To promote industrialization of the existing goods and services being produced in Pakistan in underdeveloped areas, the Institute is of the view that the condition No. "(iv)" of the definition of Greenfield industry may be removed. The condition states that technology to be used for such projects should be which is not previously used in Pakistan. However, this may be subjected to condition that if one such greenfield project has been established in an area, thereafter, similar industry would not qualify for greenfield status for that particular area.

Rationale

The aim to introduce benefits to Greenfield industries was to promote industrialization by providing exemption from minimum turnover tax due to initial years' losses and heavy depreciation. In the presence of existing condition it appears not be possible for the government to attract investment in existing industries where total local demand is not being met or where potential to export surplus production exists.

1.09 EXEMPTION AGAINST WITHHOLDING TAX U/S 148

HIGH

Currently, there is no provision in the law to seek exemption from collection of tax at import stage u/s 148 of the Ordinance.

Recommendation

It is recommended to restore availability of exemption certificate from collection of tax u/s 148 of the Ordinance as previously available under the law.

Rationale

Taxpayers anticipating business loss will be unnecessary subjected to collection of tax at import stage u/s 148 which will eventually be claimed as tax refundable in the return of total income.

1.10 STRENGTHENING THE ALTERNATIVE DISPUTE RESOLUTION COMMITTEE (ADRC) FRAMEWORK UNDER THE INCOME TAX ORDINANCE, 2001

HIGH

The Alternative Dispute Resolution Committee (ADRC) mechanism, established under section 134A of the Ordinance, serves as a pivotal platform for the expeditious and amicable resolution of tax disputes. Amendments, notably through the Finance Act, 2023, have expanded the scope and binding nature of ADRC decisions, particularly mandating State-Owned Enterprises (SOEs) to resolve disputes via this mechanism.

(A) Corresponding amendments in the Ordinance

The absence of explicit provision for passing the order for giving effect to the decisions of the Alternative Dispute Resolution Committee (ADRC) in key provisions of the Ordinance—namely Sections 124, 221, and 114(6)—the overall effectiveness become restrictive. To address this shortcoming and enhance the utility of the ADRC framework, it is imperative that suitable amendments be introduced in the corresponding provisions of the Ordinance.

Recommendations

Appropriate provisions in the following sections of the Ordinance be introduced:

1. **Implementation of ADRC Decisions**: Currently, there is no explicit provision mandating the issuance of orders giving effect to ADRC decisions, unlike the clear directives for appellate orders provided for under Section 124. In such respect, the words "Alternative Dispute Resolution Committee" be inserted in section 124 wherever necessary.

2. **Rectification of Errors in ADRC Orders**: The Ordinance lacks specific provisions allowing for the rectification of mistakes in ADRC decisions, leading to potential injustices and prolonged disputes. In such respect, the words "Alternative Dispute Resolution Committee" be inserted in section 221 wherever necessary, allowing the rectification of ADRC orders.

3. **Revision of Tax Returns Post-ADRC Decisions**: While Section 114(6)(c) permits revision of tax returns following appellate decisions, it does not explicitly extend this facility to outcomes from the ADRC, limiting taxpayers' ability to align their returns accordingly. In such respect, the reference of section 134A be inserted with other sections in section 114(6)(c), allowing the revision of return following the orders of ADRC.

Rationale

Implementing these recommendations will fortify the ADRC mechanism, ensuring that it functions as an effective, fair, and integral component of the tax dispute resolution system.

(B) Extending the scope of ADRC and Right of appeal to SOE's before appellate forums

State-Owned Enterprises (SOEs) are currently not granted the right of appeal to the Appellate Tribunal, resulting in a discriminatory limitation on their access to appellate remedies.

Furthermore, under Section 134A(6) of the Ordinance, decisions of the ADRC are not treated as binding precedents for the same issue in different tax years involving SOEs. This restriction leads to repetitive litigation, causing unnecessary expenditure of time and resources for both the taxpayers and the tax administration.

Recommendation

Appropriate amendments should be introduced in Sections 131 and 134A of the Ordinance to explicitly allow State-Owned Enterprises (SOEs) the right of appeal before the Appellate Tribunal. The current limitation, which excludes SOEs from accessing this appellate forum, creates a disparity in legal recourse that should be rectified to ensure equitable treatment.

Additionally, the scope of disputes that may be referred to the Alternative Dispute Resolution Committee (ADRC) should be expanded to explicitly include questions of law. This would enable ADRC to adjudicate legal matters involving SOEs, enhancing the utility and effectiveness of the mechanism.

Moreover, where a question of law has been amicably decided by the ADRC in the case of an SOE, such a decision should be binding on both the tax department and the ADRC for other assessment years of the same SOE. This approach will promote consistency, reduce repetitive litigation, and minimize the administrative burden and costs incurred by both SOEs and government authorities in resolving recurring legal issues.

Rationale

This will result in imparting justice to the SOEs and will end the limitation of right of appeal. Further, this will reduce the unnecessary disputes.

1.11 AUTOMITIC ISSUANCE OF REFUNDS UNDER SECTION 170

HIGH

Despite efforts by the Federal Board of Revenue (FBR) to enhance taxpayer confidence, trust deficit still persists. One of the key contributors to this gap is the delay or non-issuance of legitimate tax refunds. Taxpayers frequently face unnecessary hurdles, including repeated physical verification of information that already exists in the FBR's online records and can be verified digitally.

Recommendation

It is recommended that an automated refund credit system be introduced to streamline the refund process. Under this system:

- Refunds that are fully verifiable through the FBR's existing digital records should be processed and credited to the taxpayer's account within six months, without requiring manual intervention.
- Refunds requiring additional evidence or documentation may continue to be processed manually, but within a clearly defined and reasonable timeline of six months of the application.

Rationale

Implementing an automated refund mechanism will enhance transparency, reduce administrative burden, and improve taxpayer confidence. It will also help alleviate cash flow constraints for businesses and individuals, thereby stimulating economic activity and contributing to a more efficient tax ecosystem.

1.12 CAPACITY BUILDING OF REVENUE AUTHORITIES

HIGH

The tax laws applicable in Pakistan are inherently complex and require thorough understanding for accurate interpretation and application across a range of scenarios. Effective administration of such laws necessitates a workforce with specialized knowledge in tax, accounting, and auditing standards. However, shortcomings in training and recruitment practices have led to inconsistencies and inefficiencies in the enforcement and interpretation of tax provisions.

Recommendation

1. **Recruitment of Qualified Personnel:**

   The Federal Board of Revenue (FBR) should ensure that it recruits individuals with appropriate educational backgrounds and professional qualifications in taxation, accounting, and auditing, to enhance the competence and reliability of tax administration.
2. **Structured Training for New Recruits:**

   It is recommended that all new employees or officers undergo a mandatory six-month structured training program before being assigned operational responsibilities. This will ensure that they are adequately prepared to handle real-world tax scenarios with the required legal and technical acumen.

3. **Continuous Professional Development for Existing Staff:**

   FBR should establish a continuous training framework to keep existing staff updated on:
   - Amendments to tax laws and procedural rules,
   - New policy developments and legal interpretations,
   - Technological enhancements within the tax administration system.

   These trainings should be conducted on a regular basis to ensure alignment with current legal and administrative standards.

Rationale

Implementing these recommendations will:

- Strengthen the accuracy and consistency of tax assessments,
- Improve compliance and taxpayer confidence through well-informed interactions with FBR staff, and
- Ensure that tax officers are equipped to handle complex legal matters and evolving tax policy challenges effectively.

1.13 FULL ACCESS TO WITHHOLDING DATA TO TAXPAYER ON REAL TIME BASIS

MEDIUM

A positive step has been taken by FBR by implementation of MIS-Information Center in 'IRIS', where in a taxpayer can view income tax paid by way of collection or deduction at source. However, the scope of this Information Center needs to be expanded to the entire withholding tax regime so that the taxpayer can reconcile its position on real time basis.

Through MIS, taxpayer is able to check various taxes deposited in their name in real sense. Further, any lapse on part of withholding agent can also be pursued by the taxpayer without any issue of its verification and availability of tax credit.

1.14 DEFINITION OF PERMANENT ESTABLISHMENT U/S 2(41)

LOW

U/s 2(41) (d), furnishing of services, including consultancy services by any person through employees or other personnel engaged by the person for such purpose is considered to be Permanent Establishment. However, minimum threshold of presence of employees or other personnel in Pakistan is not provided.

It is proposed to amend the definition to provide that, in case of services, a PE shall be established where the stay of employees or other personnel engaged exceeds 90 days in a tax year.

Rationale

The absence of minimum threshold for services give rise to a situation where services provided for even a day in Pakistan could give rise to a PE situation thereby disentitling the non-resident from fixed taxation envisaged in section 6 at the rate of 15%.

1.15 WITHHOLDING TAX ON PRIZES U/S156

MEDIUM

Withholding tax @ 20% is required to be withheld from prizes offered by companies for promotion of sales.

The term Prize should be distinguished from normal trade schemes which are offered by manufacturing & trading companies to their distributors and dealers as per the business norms. The following explanation should be added under Sec 156:

"The term Prize means winning by chance and does not include:

- *free samples,*
- *promotional giveaways of petty amounts, and*
- *payments either in cash or in kind to any person on achieving sales target.*

The explanation shall be deemed always to have been so added and shall have effect accordingly."

Rationale

The tax authorities tend to treat the normal trade schemes like post sales discounts, free issues, promotional giveaways and target incentives as 'prize', and accordingly demand 20% withholding tax.

1.16 AMORTIZATION OF INTANGIBLES U/S 24

MEDIUM

The maximum amortization period of intangibles having unascertainable life for tax purposes be restored to 10 years.

Rationale

Intangibles are significant business assets both for manufacturing and service sectors of the economy. 25 years' period too is quite long as compared to the initial, normal and first year

depreciation allowances available on tangible assets.

1.17 TAX ON SURPLUS FUND OF NON-PROFIT ORGANIZATION U/S 100C

MEDIUM

Currently, sub-section (5) of section 100C of the ITO provides that surplus funds of non-profit organization shall be taxed at a rate of ten percent. Moreover, surplus funds u/s 100C (6) have been defined as funds or monies:

i. not spent on charitable and welfare activities during the tax year;

ii. received during the tax year as donations, voluntary contributions, subscriptions and other incomes;

iii. which are more than twenty-five percent of the total receipts of the non-profit organization received during the tax year; and

iv. are not part of restricted funds.

faMost of the non-profit organizations establish and run welfare related projects such as schools, clinics, vocational training centers etc. and for the purpose, huge capital expenditures are required to be incurred to develop the infrastructure, construct buildings, provide equipment etc.

Such capital expenditure is incurred over a period and cannot be expended in one fiscal year. Further, to incur such expenditure, as and when required, cash is to be retained in respect of projects, which are to be completed over a period exceeding one year.

It is proposed to abolish sub-section (5) and (6) of section 100C of the ITO as it is directly causing hindrance to the welfare activities involving capital expenditure to be incurred over a period exceeding one year.

Alternatively, the limit of spending in a year on charitable and welfare activities from receipts during that year currently set at minimum 75% of such receipts may be analyzed over a reasonable period (at least three years), to account for expenditures which are inevitably spread over a period exceeding one year.

Surplus funds may be calculated after taking impact of revenue expenditure as well as capital expenditure incurred during the year.

The proposed recommendation is being suggested to ensure the smooth functioning of welfare projects that are specially meant for the benefit of the deprived members of the society.

Rationale

There is a dire need in the society for charitable and welfare related projects specially in the education, health and social sector for uplifting of the under-privileged class dominating the population. The prevailing provision is imposing restriction and hindering the smooth functioning of such welfare projects.

1.18 ASSESSMENTS & ORDERS SECTION 124 & 124(A)

MEDIUM

The following provisions of law are prescribed for giving effect to the findings/direction/decision of various appellate forums where an appeal filed by a taxpayer against any order passed by the tax authorities:

124(2)	For direction of giving effect	*Where, in consequence of, or to give effect to, any finding or direction in any order made under Part III of this Chapter by the Commissioner (Appeals), if the value of assessment or, as the case may be, refund of the tax does not exceed twenty million rupees, Appellate Tribunal, High Court, or Supreme Court an assessment order or amended assessment order is to be issued to any person, the Commissioner shall issue the order within two years from the end of the financial year.*

124(2)	For set aside issue	*Where, by an order made under Part III of this Chapter by the Appellate Tribunal, High Court, or Supreme Court, an assessment order is set aside [wholly or partly,] and the Commissioner [or Commissioner (Appeals), as the case may be,] if the value of the assessment or, as the case may be, refund of the tax does not exceed twenty million rupees, is directed to pass a new assessment order, the Commissioner or Commissioner (Appeals), as the case may be, shall pass the new order within one year from the end of the financial year.*
124 (4)	In case of direct relief	*Where direct relief is provided in an order u/s 129 or 132, the Commissioner shall issue appeal effect orders within two months of the date the Commissioner is served with the Order.*
124A (2)	Case where decision is reversed by the Superior Court	*In case the decision of High Court or the Appellate Tribunal, referred to in sub-section (1), is reversed or modified, the Commissioner may, notwithstanding the expiry of period of limitation prescribed for making any assessment or order, within a period of one year from the date of receipt of decision, modify the assessment or order in which the said decision was applied so that it conforms to the final decision.*

In practice, the FBR officials do not issue the appeal effect orders based on the refundable position. Therefore, if the taxpayer has completed the above-mentioned period, the taxpayer therefore, is not able to receive the appeal effect order. The said refund accordingly is not available for adjustments in the subsequent year's tax liability, nor the taxpayer is able to claim the refund through refund application in the FBR web portal.

In addition to the above, the FBR web portal does not provide option for filing of appeal effect application. Therefore, the officer is not bound to respond to the queries raised within the stipulated time.

Recommendation

The institute suggests that the FBR web portal should provide the facilities of online filing of the appeal effect applications. It is further suggested that the taxpayer should be allowed to file the appeal effect applications along with the revised working which is based on the order passed by the Appellate and higher authorities. If the concerned officer has not initiated any actions with the given time against the provided relief by the Appellate and higher authorities on completion of the statutory time limit, then the submitted revised working by the taxpayer will be considered deemed to be accepted. It is also recommended that restriction about value of assessment refund of the tax to twenty million rupees for passing of the appeal effect order should be removed.

1.19 CERTIFICATE OF COLLECTION / DEDUCTION OF TAX – U/S 164

MEDIUM

The Institute fully appreciates and endorses the need for submissions of the challans as evidence of tax paid. However, keeping in view the prevailing ground realities, it is very difficult for the taxpayers to obtain copies of challans from the withholding agents in many cases and in particular where the tax withheld is paid through book entry or through a single consolidated challan without the details of the persons from whom it has been collected or deducted e.g., tax collected or deducted from dividend, profit on debt, export realizations, petroleum products, cash withdrawal from a bank, issuance of instruments, sale of securities (NCCPL), registration of motor vehicle, gas consumption by CNG stations, electricity consumption, telephone usage, domestic and international air tickets, etc. and tax collected or deducted by Governments under various provisions. Accordingly, the Institute is of the view, that until each and every withholding agent complies with his obligation of providing the challans of tax collected or deducted at source, any other equivalent document or certificate of tax collected or deducted should be acceptable as evidence of tax paid by way of collection or deduction of tax at source.

Sub-section (1) of section 164 requires that the withholding agent has to provide copies of the challan (CPR) or any other equivalent document along with a certificate of the amount of tax collected or deducted.

Sub-section (2) of section 164 requires furnishing of copies of challan (CPR) along with the return of income as evidence of tax paid by way of collection or deduction at source but does not provide for acceptance of 'any other equivalent document'. The term 'any other equivalent document' used is sub-section (1), is neither defined nor explained.

It is proposed to consider the following amendments to address this issue:

- The term 'any other equivalent document' used in section 164(1) should be defined or explained, which may include electricity bills, telephone bills, airline tickets, bank statements, etc.;
- In section 164(2), the words 'any other equivalent document' be added as evidence of tax payment to be furnished along with the return; and
- A proviso be added u/s 164(2), whereby only a certificate of collection or deduction of tax would also be acceptable as evidence of tax payment, where the withholding agent does not separately identify the person from whom tax has been collected or deducted in the respective tax deposit challan (CPR) or the tax is deposited through internal government adjustments.

In addition, a new clause should be inserted in Part IV of Second Schedule as follows:

"Section 164 shall not apply in the case of following withholding agents:

- Electricity distribution companies;
- Telecommunication companies;
- Airlines; and
- Local, statutory and other government bodies.

The certificate issued by the above companies or bodies or their agents mentioning the amount of tax collected shall be treated as sufficient evidence."

Rationale

This may result in resolving dispute with tax authorities and restricting disallowance of credit for taxes deducted at source.

Various withholding agents including but not limited to electricity distribution companies, telecommunication companies, airlines and other government and local bodies do not provide copies of challans to the taxpayers, as their customer base is too high.

1.20 OFFENCES AND PENALTIES - NON-FURNISHING OF STATEMENT WITHIN THE DUE DATE U/S 182

MEDIUM

Penalty for non-furnishing of statement u/s 165, 165A or 165B (where tax is not deposited within the due date and statement is filed after lapse of 90 days) is prescribed u/s 182 as Rs. 2,500 for each day of default subject to a minimum penalty of Rs. 10,000.

Recommendation

It is proposed that such exuberant penalty should be reduced to Rs. 500 per day subject to a maximum penalty of Rs. 50,000; and in case of continuation of default after the imposition of first penalty a further penalty of Rs. 1,000 per day.

It is also proposed to insert an Explanation or Proviso stating that no penalty shall apply in a case where there was nothing to report in the statement u/s 165.

Rationale

The present quantum of penalty is too harsh and highly unreasonable. In many cases, practically, the quantum of penalty exceeds the actual tax liability itself.

1.21 GROUP RELIEF – SECTION 59B

MEDIUM

Section 59B seeks to provide group relief in the form of adjustment of losses between holding and subsidiary or subsidiary-to-subsidiary if they fulfil the minimum holding criteria. The required holding is 55%, if one of the companies in the group is a listed company and 75% if none of the companies in

the group is listed company.

The law further prescribes certain conditions that the group companies have to fulfil in case they avail the facility of group relief. The conditions are set out in subsection (2) of Section 59B. One of the conditions under sub-section 2(c) of Section 59B is as follows:

"…. holding company, being a private limited company with seventy-five percent of ownership of share capital gets itself listed within three years from the year in which loss is claimed."

Similarly, sub-section (1A) restricts the admissibility of loss of the subsidiary company to the percentage of shareholding in the subsidiary, which need to be revisited in view of provision of sub-section (6).

Recommendation

It is proposed that clause (c) of sub-section (2) of Section 59B be substituted as follows:

"At least one of the companies of the group shall get itself listed within three years from the year in which loss is claimed if all companies of the group including the holding company are private limited companies."

It is proposed to delete sub-section (1A) as sub-section (6) puts a condition on the loss acquiring company to transfer cash equal to the amount of tax payable on profits to be set off against the acquired loss to the loss surrendering company.

Rationale

This would bring the condition in line with other condition of minimum holding discussed above where a higher holding is only required if none of the companies in a group is a listed company.

Further, the requirement to list the holding company is against the principle of group formation and consolidation as a group may not like to keep its investments in a listed company due to the risk of hostile takeovers etc. as in such an event the group may lose control on its entire entities within the group.

Restricting the availability of loss to the percentage of shareholding, when cash equal to the amount of tax payable on the profit to be set off against such loss, is unjustified.

1.22 CONSISTENCY IN THE APPLICATION OF CARRY FORWARD OF TAX U/S 113 AND U/S 113C.

MEDIUM

Minimum tax is applicable if a company earns lesser profit/ incurs losses in any tax year. It should be noted that Business losses are allowed to be carried forward for a period of six years against the Business Income and such adjustment of losses in subsequent years results in reduction of taxable income.

Companies, who adjust their losses in subsequent years are currently not able to recover the Minimum Tax paid in the year of loss as the adjustment period for business loss is six years whereas the minimum tax u/s 113 cannot be carried forward for more than three years.

Recommendation

To bring consistency in the treatment of carry forward of excess taxes paid in earlier years, similar to carry forward of business losses, minimum tax u/s 113 should also be allowed to be carried forward for six years.

1.23 DOUBLE TAXATION ON SPECIE DIVIDEND

MEDIUM

Under the current law, the gross amount of specie dividend is first taxed u/s 5 of the Income Tax Ordinance. However, at the time of disposal of the shares received as dividend in specie, the cost of shares is taken as zero in accordance with Rule 13P (v) of the Income Tax Rules, 2002. This means that the same amount is taxed again u/s 37A of the Income Tax Ordinance, 2001, which results in double taxation.

Recommendation

It is recommended that the cost base of the shares received as dividend in specie should be the value on which tax has been collected u/s 150 of the Income Tax Ordinance.

Rationale

This would ensure that the amount received as dividend in specie is not taxed twice, and the taxpayer is not unfairly burdened with double taxation.

1.24 CAPITAL VALUE TAX ON FOREIGN ASSETS – SECTION 8 OF THE FINANCE ACT, 2022

MEDIUM

Background

Capital Value Tax was at first introduced through the Finance Act, 1989 for the first time in history of Pakistan. The purpose and rational for bringing this tax in Pakistan were to tax assets which were created from untaxed money specially in relation to acquisition of properties and vehicles. In addition to the above, if we think it out loud, the other possible coherent reason could be to tax idle investment which do not contribute to the gross domestic product.

The above understanding is based on the budget speech of Mr. Ihsan ul Haq Piracha while presenting the Federal Budget for year 1989-90. He categorically stated that this tax would only be levied on persons who are not registered with authority. However, as is evident from our history defeating the very purpose of any law in Pakistan is a practice which we diligently follow. Therefore, the tax was levied on the sale, transfer, or gift of immovable property, such as land or buildings irrespective of the fact that such person is either making such investment from taxed money or not. Nevertheless, in the larger interest of Pakistan and to boost the economy, the alternative rational as stated above could still be pretty much relevant.

Whether right or wrong, whatever the consequences it carried, CVT after remaining in force for quite some time was abolished.

Reintroduction of CVT through Finance Act 2022

The Finance Act, 2022 again introduced CVT but this time on a resident person in Pakistan on his entire foreign assets. This time around, the purpose and intent bringing back CVT, as we understand should have been the same. However, the demographics under which we (Pakistan) operate in comparison to 1989-90 have shifted substantially.

Time and again, it has been emphasized, to increase the tax net rather than taxing the taxpayers who fortunately or unfortunately are under the garb of the taxation system. But due to fact that the registered taxpayers are an easy target for revenue, the Government has always placed reliance on such easy money.

Issues and impact:

(a) **Flight of Capital** – The above taxation has witnessed adverse impact on flight of capital from Pakistan. There are no two views that our economy has reached the brink of collapse and requires concerted efforts to rebuilt from whatever we are left with. In this backdrop taxing declared foreign assets of residents is proving to be a nail in the coffin.

(b) **Drainage of entrepreneurial capital** – Many of these residents have decided and have left Pakistan or are spending major time abroad to become non-resident, depriving Pakistan of their availability for venturing in business. This is a very dangerous trend that's developing which could have a far-reaching impact.

(c) **Applicable to Foreign resident expatriates as well –** Also it is attracted to resident expatriates (who become resident by virtue of employment exercised in Pakistan) as well which seems totally ridiculous that why should a foreign national who is here for working on projects etc. be required to pay CVT on his assets in his home country or elsewhere, while he is in Pakistan. This anomaly has been shared with FBR in last budget, but this has not so far been rectified and in such cases the burden of this tax is shifted to local industry who require their services thus increasing cost of doing business in Pakistan.

(d) **Double taxation** – On one hand we are taxing a resident person global income which no one disagrees with, as it is universally accepted. However, after taxing the income generated from the foreign asset i.e., rental income from immovable property, profit on debt (interest) on placements in bonds and bank account etc. and capital gains on portfolio investments, etc., the CVT law forces the resident to pay tax on the basis of value of asset at 1%. This 1 % tax on asset value effectively means that you are again charging the income at anything ranging from 20% to 505%, depending on returns received for e.g., the average rental return of investment ranges around 5% so 1% CVT means you are further taxing income at 20%. Similarly deposits in foreign currency hardly earn a good return abroad which would be a low as 0% or up to 3% to 4% (depending on the jurisdiction and earning interest rates). Effectively this means double taxation.

Under section 7E of the Income Tax Ordinance, 2001 (tax on deemed income), the immovable properties from which rental is being derived and tax thereon is paid have been exempted or excluded from the preview of the levy for the simple reason that income derived from immovable property is being taxed. The same logic evenly applies in respect of foreign assets generating income and being subject to income tax under the principles of taxation of global income.

(e) **Deduction of liabilities –** Immovable property outside Pakistan, is generally acquired under a mortgage arrangement. However, section 8 of the Finance Act, 2022 relating to levy of Capital Value Tax only take into consideration the assets without deduction of liability.

(f) **Threshold verses basic exemption** – In case of foreign assets, there is no exemption except a threshold of Rs. 100,000,000 for levy of CVT. Where the value of the foreign assets does not exceed Rs. 100,000,000 the liability of CVT is Rs. Nil and the moment the value of foreign assets exceeds Rs. 100,000,000, even by a Re. 1, it attracts CVT of Rs. 1,000,000, which on the face appears to be irrational.

Recommendations

In this background, it is necessary that immediate remedial measures are taken including:

- We have no choice but to abolish CVT on resident's foreign assets and instead focus on broadening of tax base. CVT collected is a few billion rupees while its repercussions are depriving Pakistan of not only valuable capital but also is draining our entrepreneurial capital. One must understand that local investment in business is a must to show strength to foreign investors. Further reliance on local investor is far better than focusing on FDI as the latter has negative pressure on our reserve, in shape of payouts in FX to foreign investors as has been recently witnessed. A balance is therefore required between the two.

OR Alternatively:

- CVT on foreign assets should be restricted to resident citizens of Pakistan;
- Section 8 of the Finance Act, 2022 be amended to impose CVT on the "net value of assets" instead of "value of assets", thereby allowing deduction of liabilities from the value of the assets;
- Foreign assets, the income of which is chargeable to tax should be granted exemption or excluded from the levy of CVT; and
- The threshold of the taxability of foreign assets of Rs. 100,000,000 be instead made overall exemption deductible, to arrive at the taxable value of foreign assets, resulting into progressive taxation.

1.25 WEALTH STATEMENT AND RECONCILIATION THEREOF – SECTION 116 AND FOREIGN INCOME AND ASSETS STATEMENT – SECTION 116A

- Sub-section (1) of section 116 empowers the Commissioner to require from any person being an individual to furnish wealth statement;

- On the other hand, sub-section (2) of section 116 requires that every resident individual has to un-conditionally furnish wealth statement along with the return of income; and
- Proviso to sub-section (2) of section 116 requires that all the members of an AOP have also to furnish the Wealth Statement along with the return of income of the AOP.

After removal of conditions for furnishing wealth statement from sub-section (2):

- Sub-section (1) in its present form appears to be redundant;
- Proviso to sub-section (2) is also redundant since every resident individual is required to furnish wealth statement along with the return of income.

A non-resident individual is not required to furnish his/her wealth statement along with the Income Tax Return. We understand that by non-furnishing of wealth statement by non-resident individuals the assets acquired in Pakistan, either from Pakistan Sources Income or Foreign Source Income brought into Pakistan, remain un-recorded in the tax records at the relevant time. After lapse of limitation to amend an assessment, even if un-earthed could not be called in question.

Another issue is with regard to declaration of assets and liabilities of the person's spouse, minor children or other dependents, where such persons are independent taxpayers and are separately filing wealth statement along with their own income tax return.

A resident person having foreign assets, liabilities or income and expenses is required to declare the same in the wealth statement to be furnished under section 116 and related sub-forms of the income tax return under section 114. The same information at the cost of duplication is again furnished under the foreign income and assets statement under section 116A.

Recommendations

- The Commissioner's powers to call for the wealth statement should only be restricted where it is not furnished along with the return;
- Obligation of AOP to furnish wealth statement of members be dispensed with;
- Non-resident individuals should be required to file wealth statement and re-conciliation thereof only to the extent of assets and liabilities held or owed in Pakistan and inflows and outflows in Pakistan;
- Assets and liabilities of the person's spouse, minor children or other dependents, where such persons are independent taxpayers need not to be declared;
- Duplication of furnishing of foreign income and foreign assets be dispensed with.

The draft of the suggested substitution of sub-section (1) and (2) of section 116 is as under:

"116. Wealth statement. - (1) Every taxpayer, being an individual, filing a return of income for any tax year shall furnish statements (hereinafter referred to as "wealth statement", "wealth reconciliation statement" and "annual personal expenditure statement") in the prescribed form and verified in the prescribed manner giving particulars of-

(a) the person's total assets and liabilities as on the last day of the corresponding tax year;

(b) the total assets and liabilities of the person's spouse, minor children and other dependents, where such spouse, minor or dependent have not furnished their return of income, as on the last day of the corresponding tax year;

(c) any assets transferred by the person to any other person during the corresponding tax year and the consideration for the transfer;

(d) the total expenditures incurred by the person, and the person's spouse, minor children and other dependents, where such persons have not furnished their return of income, during the corresponding tax year and the details of such expenditures; and

(e) the reconciliation statement of wealth

Provided that:

(a) in case of resident individual, the wealth statement and wealth reconciliation statement shall comprise of both local and foreign assets, liabilities, transfers, expenditures, inflows and outflows; and

(b) in case of non-resident individual, the wealth statement and wealth reconciliation statement shall comprise of only local assets, liabilities, transfers, expenditures, inflows and outflows;

(2) Where a person fails to furnish the statements as required under sub-section (1), the Commissioner may, by notice in writing, require any person being an individual to furnish, on the date specified in the notice, a "wealth statement", "wealth reconciliation statement" and annual personal expenditure statement") in the prescribed form and verified in the prescribed manner."

1.26 ADVANCE TAX – SECTION 147

a. In case of an individual the threshold for payment of advance tax is latest assessed income of Rs. 1,000,000. This threshold was fixed by Finance Act, 2017, when the tax payable on such threshold was Rs. 69,500. By the passage of time tax rates have been reduced and today the tax payable is of Rs. 55,425. Thus technically, instead of enhancing the threshold the same has been reduced, thereby increasing the number of individual taxpayers to pay advance tax as required by section 147.

It has been observed that proceedings for default in payment of advance tax, which could be 100% automated, has gone on the back burner with the increase in number of persons required to make payment of advance tax.

Recommendations

The threshold of Rs. 1,000,000 needs to be increased to at least Rs. 3,000,000. The outcome of this increase in threshold will be reduction in number of individuals required to pay advance tax, which will ensure proper monitoring and proceedings for non-compliance.

b. In case of an individual income from salary subject to deduction of tax under section 149 is excluded for the purposes of payment of advance tax and accordingly, tax deducted under section 149 is not taken into consideration for calculating the installment due. Sub-section (4B) of section 147 prescribes the formula for calculation of each installment of advance tax. The component A and B of the formula read as under:

"A is the tax assessed to the taxpayer for the latest tax year or latest assessment year under the repealed Ordinance; and

"B is the tax paid in the quarter for which a tax credit is allowed under section 168, other than tax deducted under section 149.

In component B tax deducted under section 149 is excluded while in the component A full amount of tax assessed for the latest year is to be taken, which is inclusive of tax on salary.

Recommendations

In component A, proportionate tax assessed for the latest year on taxable income excluding salary income should be taken instead of full amount of the tax assessed for the latest year.

"C A taxpayer is entitled to adjust all adjustable withholding taxes paid from the gross installment of advance tax due to arrive at the net installment due. The component D of sub-section (4) and component B of sub-section (4B) of section 147 reads as under:

"D is the tax paid in the quarter for which a tax credit is allowed under section 168."

"B is the tax paid in the quarter for which a tax credit is allowed under section 168, other than tax deducted under section 149."

It has been observed in many cases that the amount of adjustable withholding tax (component D and B) is more than the installment due and hence that particular installment stands overpaid.

If we go by the strict language of the component D and B the excess payment of earlier installment cannot be carried forward and adjusted in the following installment, which we understand is not the intention of overall scheme of payment of advance tax. The rational of payment of advance tax under section 147 is 'pay as you earn' the liability of the annual income tax for the ensuing year.

Recommendations

The wording of the aforesaid components D and B be appropriately amended to adjust the overpaid installment in the next quarter.

The drafts of the suggested substitutions are as under:

Component D of sub-section (4):

"D is the tax paid in the quarter or excess paid in the previous quarter or quarters, for which a tax credit is allowed under section 168."

Component A of sub-section (4B):

"A is the proportionate tax assessed on the taxable income excluding income under the head salary subject to deduction of tax under section 149, for the latest tax year or latest assessment year under the repealed Ordinance; and

Component B of sub-section (4B):

"B is the tax paid in the quarter or excess paid in the previous quarter or quarters, for which a tax credit is allowed under section 168, other than tax deducted under section 149."

1.27 SUPER TAX ON HIGH EARNING PERSONS – SECTION 4C

MEDIUM

Litigation on the constitutionality and justification otherwise is pending before the Supreme Court of Pakistan and as per varying orders of the High Courts the recovery of this tax imposed through Finance, Act, 2022 is jeopardized. We had a lot of debate on this issue and now it is high time to find alternate means to generate revenue from high earning persons. The consensus was to make it simple, straight forward and litigation free, even at the cost of losing some revenue on Dividend, Capital Gains, Profit on debt, imputable income and brought forward business losses, depreciation losses and amortization losses.

Recommendations

Section 4C be omitted; and

Alternatively, clause (i) sub-section (2) of section 4C includes separately profit on debt, capital gains and brokerage and commission in the income for the purpose of levy of super tax under section 4C.

Profit on debt and capital gains are chargeable both under the normal tax regime as well as final tax regime depending upon its nature and applicable conditions.

However, brokerage and commission, after amendment in section 233 by Finance Act, 2019 is only chargeable under normal tax regime.

Recommendations

Clause (i) of sub-section 2 of section 4C be amended to exclude the words "brokerage and commission" and a condition be inserted for profit on debt, dividend and capital gains if chargeable under final or fixed tax regime.

1.28 TAX ON DEEMED INCOME – SECTION 7E

MEDIUM

a. The law is silent as to deduction of liabilities relating to or incurred in relation to capital assets (as defined in section 7E) for the purposes of determining the market value of the specified capital assets and the resultant deemed income.

b. In case of capital assets (as defined in section 7E), after excluding certain exemptions, there is a threshold of Rs. 25,000,000 of the value of capital assets. Where the value of the capital assets (after excluding exemptions) does not exceed Rs. 25,000,000 the liability of tax under section 7E is Rs. Nil and the moment the value of capital assets exceeds Rs. 25,000,000, even by Re. 1, it attracts tax under section 7E of Rs. 250,000, which on the face appears to be irrational.

Recommendations

Section 7E be amended to calculate deemed income of the specified capital assets based on the "net value of capital assets" instead of "value of capital assets", thereby allowing deduction of liabilities from the value of the assets;

The threshold of the taxability of capital assets of Rs. 25,000,000 be instead made overall exemption deductible, to arrive at the taxable value of capital assets, resulting into progressive taxation.

1.29 BROUGHT FORWARD UNABSORBED DEPRECIATION – SECTION 57(4)

Restricting the set off of brought forward unabsorbed (i) depreciation loss; (ii) initial allowance; (iii) accelerated depreciation to alternate energy projects; and (iv) amortization of intangibles, to 50% of the business income was introduced by Finance Act, 2018. To date neither the Board has issued any clarification circular nor does the return filing system "Iris" support the calculation of such restriction.

We understand that this substitution through Finance Act, 2018 was made to generate some quick revenue to meet the budget targets or to target some specific case or cases. This is a one the amendments distorting the decades old taxation system. We also understand that this amendment, since its introduction has never been implemented in its true letter-and-spirit being of no major revenue impact in view of provisions of section 113 (minimum tax on turnover) and section 113C (alternative corporate tax).

Recommendations

Undo the substitution of Section 57(4) and related amendments made through Finance Act, 2018.

1.30 FINAL TAX REGIME

Subject to our reservations for improvement in the Minimum Tax Regime, we acknowledge a positive step of moving away from Final Tax Regime leading to non-documentation. However, tax collected / deducted, on the following transactions continue to be covered under final tax regime needs to be brought into Minimum Tax Regime:

- Commission/discount on petroleum products – Section 156A
- Lease of rights to collect tolls – Section 236A (3)

1.31 TAXATION OF PROFIT ON DEBT (OTHER THAN FROM FOREIGN CURRENCY ACCOUNTS AND ON SPECIFIED INVESTMENTS MADE FROM SPECIFIED ACCOUNTS) IN THE HANDS OF NON-RESIDENT INDIVIDUALS

Residential status of an individual is determined for each tax year and may vary from resident to non-resident or vice-versa every year and such determination can only be made after the close of the corresponding income year. There is no mechanism in place whereby a resident person paying profit on debt to an individual can determine whether such individual will be a resident or non-resident for the relevant tax year, at the time of such payment, and accordingly it could not be determined whether income tax (WHT) is to be withheld will be under section 151 or 152(2).

Generally, in above situation the tax is deducted under section 151 at the rate of 15% and the profit on debt is chargeable under section 7B, which section applies both to a resident and non-resident person. However, after the close of the year if the person is a non-resident the profit on debt is actually chargeable under sub-section (2) of section 152 and the rate of deduction of tax is 10% read with Clause (5A) of Part II of 2nd Schedule.

Profit on debt from investments in specified instruments through specified accounts covered under proviso to clause (5A), clauses (5AA) and (5AB) are subject to final tax and all other, mainly accounts

and deposit with financial institutions etc., where the deposit or investment are not through specified accounts fall under normal regime and also attracts the provisions of Avoidance of Double Tax Treaties.

Recommendations

Appropriate provisions need to incorporate, that tax deducted under section 151 from a non-resident shall for all purposes be treated as tax deducted under sub-section (2) of section 152.

1.32 REINSTATING GROUP TAXATION BENEFITS:

Clause 103A of the Part 1 of the 2nd Schedule of the Income Tax Ordinance, 2001, introduced via the Finance Act, 2007, initially provided exemption on income derived from inter-corporate dividends within group companies eligible for Group Taxation under Section 59AA or Group Relief under Section 59B aiming to foster corporatization in Pakistan. However, subsequent amendments, particularly through the Finance Act, 2016 and Finance Supplementary (Second Amendment) Act, 2019 led to the omission and then reintroduction of such exemption for entities eligible for Group Relief under Section 59B.

However, the Finance Act, 2021, omitted clause 103C for companies eligible for group relief under Section 59B, subjecting multi-layered groups to multiple taxation on dividend income within the group. Moreover, if companies opt to reverse the group formations, it may lead to substantial capital gain taxes.

Recommendations

It is proposed to reinstate Clause 103C for companies entitled to group relief.

Rationale:

Restoring Clause 103C will uphold the intended benefits of fostering corporatization, while preventing multiple taxation within group structures, aligning with the legislative intent of promoting fair and efficient taxation practices.

1.33 RESTRICTED VALUE OF PASSENGER TRANSPORT VEHICLE

a. Through Finance Act, 2022 the restricted value of passenger transport vehicle for the purposes of depreciation was enhanced to Rs. 7,500,000 from Rs. 2,500,000. Keeping in view the current market prices, this needs to further revise, upwards to Rs. 10,000,000.

b. Further, for the purpose of lease rental deductions the corresponding restriction of principal amount of lease under proviso to clause (b) of sub-section (1) of section 28 remained unchanged at Rs. 2,500,000, which also needs to be brought at par with restricted value for depreciation purposes.

Recommendations

It is proposed to bring both similar deductions at par by enhancing the limit of restricted value of passenger transport vehicle under clause (a) of sub-section (13) of section 22 and clause (b) of sub-section (1) of section 28 to Rs. 10,000,000.

1.34 REDUCTION IN WITHHOILDING TAX RATES

MEDIUM

The current withholding tax rates, in particular for income covered under the final tax regime or subject to minimum tax are being enhanced year by year, being the easiest way to generate revenue, without considering the impact and capacity of businesses to bear this tax burden. A brief study of the impact of such high rate of withholding tax, applying corporate rate of tax of 29% is as under:

Turnover	WHT rate	Imputable Income	Percentage of Taxable Income
10,000,000	5%	1,724,138	17.24%
10,000,000	6%	2,068,966	20.68%
10,000,000	7%	2,413,793	24.13%
10,000,000	8%	2,758,621	27.59%
10,000,000	9%	3,103,448	31.03%
10,000,000	10%	3,448,176	34.48%
10,000,000	11%	3,793,103	37.93%
10,000,000	12%	4,137,931	41.38%

The percentage of taxable income further aggravates when applying rates for small company, non-corporate taxpayers and taxpayers with higher rates of sales tax and also collecting advance tax.

Recommendations

It is proposed to examine this aspect of the high rates of withholding tax and appropriate remedial measures are taken.

1.35 CLARIFICATION ON DEFINITION OF CONTRACT

MEDIUM

Sub-section 1 of section 153 states that *"Every prescribed person making a payment in full or part including a payment by way of advance to a resident person*

(c) on the execution of a contract, including contract signed by a sportsperson but not including a contract for the sale of goods or rendering of or providing of services".

Clause (c) of sub-section 3 of section 113 states that *"turnover means:*

(c) the gross receipts from the execution of contracts; except covered by final discharge of tax liability for which tax is separately paid or payable".

Similarly section 153(7)(v)(c) states *"Turnover" means the gross receipts from the execution of contracts.*

Whereas the term contract though mentioned in both sections referred above, but it is not defined in section 2 therefore ambiguity exists as to the definition of contract.

Recommendation

It is recommended to define the term "Contract" in Income Tax Ordinance 2001.

Rationale

By defining the term "contract" in the Income Tax Ordinance 2001 is to establish a clear legal framework that enhances tax administration and compliance. A precise definition of "contract" will provide clarity on the scope and application of tax laws to contractual transactions, thereby reducing ambiguity and potential disputes between taxpayers and tax authorities. By explicitly delineating what constitutes a contract for taxation purposes, the Ordinance will facilitate accurate assessment and reporting of income derived from contractual agreements. This clarity will improve tax compliance and enforcement efforts, leading to greater fairness and efficiency in the tax system.

1.36 CAPITAL GAIN ON INHERITED ASSETS

MEDIUM

Finance Act 2022 omitted sub-section 4A of section 37 of Income Tax Ordinance 2001. Sub-section 4A before omission stated:

"*(4A) Where the capital asset becomes the property of the person*

(a) under a gift from a relative as defined in sub section (5) of section 85, bequest or will;

(b) by succession, inheritance or devolution;

(c) a distribution of assets on dissolution of an association of persons; or

(d) on distribution of assets on liquidation of a company,

the fair market value of the asset, on the date of its transfer or acquisition by the person shall be treated to be the cost of the asset;

Provided that, if the capital asset acquired through gift is disposed of within two years of acquisition and the Commissioner is satisfied that such gift arrangement is a part of tax avoidance scheme, then the provisions of sub-section (3) of section 79 shall apply for the purpose of determining the cost of asset in the hands of recipient of the gift."

The purpose of omission of aforementioned section was apparently to prohibit misuse of above provision for avoidance of tax through gifts however inherited assets have also been hit by the omission of above provision. The omission of above provision means that the cost of inherited asset in the hands of successor becomes the cost incurred by the predecessor which may result in exorbitant taxable gain in the hands of successor effectively taxing inheritance in the hands of successor.

Recommendation

Section 37(4A) may be reinstated only to the extent of inherited property;

OR alternatively:

In case of inherited assets, the holding period to be counted from the date of purchase by the deceased.

Rationale

The omission of section 37(4A) imposes disproportionate tax liabilities on recipients of inheritance. Such an approach overlooks the intrinsic value of inherited assets and unfairly subjects recipients to tax obligations based on the entire proceeds of disposal.

1.37 REMOTE WORKERS EMPLOYED BY FOREIGN COMPANIES

MEDIUM

The income of Remote workers working under an employment contract with foreign companies fall within the definition of salary provided under section 12 read with section 101(1) however, they frequently utilize section 154A to circumvent taxation on their salary. This phenomenon has resulted in a significant shift of essential resources from domestic Pakistani enterprises to international counterparts, which opt to engage remote workers instead of maintaining local offices. This practice, inherently unlawful, persists due to the absence of robust regulatory oversight, placing local Pakistani enterprises at a disadvantage. Particularly advantageous for high-income bracket individuals, this tax avoidance strategy significantly undermines the competitiveness of local companies.

Recommendation

It is recommended to introduce clear definition of "remote worker" within Income Tax Ordinance 2001 to facilitate accurate classification and taxation of individuals engaged in remote work arrangements and FBR to take necessary steps to ensure that such remote workers are appropriately taxed as salaried individuals while their employers shall also be penalized for breach of Pakistan tax, corporate and labour laws.

Rationale

The prevalence of remote work arrangements, coupled with tax avoidance tactics misusing the facility of section 154A, has resulted in a detrimental outflow of resources from local Pakistani enterprises to international entities. By establishing a formal definition of remote workers and instituting measures to tax their income, the proposed regulatory framework aims to restore fairness and equity in taxation. This initiative will safeguard the interests of local companies, promote compliance with tax regulations, and foster a level playing field in the business environment. Ultimately, these measures are crucial for preserving the integrity of the tax system and supporting the growth of domestic enterprises in Pakistan.

1.38 TAX CREDITS U/S 100C FOR GOVERNMENT GRANTS TO SEMI-GOVERNMENT BODIES

MEDIUM

The availability of a tax credit under section 100C for Government grants and foreign grants is restricted to persons specified in subsection 2 of said section, subject to approval by the Commissioner Inland Revenue (CIR) as per section 2(36). However, semi-government bodies or body corporates, not mentioned in section 100C (2) lack eligibility for approval under section 2(36). Consequently, grants received by such entities will be liable to taxation, potentially undermining the intended purpose of the grants, which are typically allocated for operating expenses but may effectively be repaid to the government in the form of taxes.

Recommendation

It is recommended to introduce an exemption clause within the Second Schedule to address the taxation dilemma faced by semi-government bodies and body corporates receiving government grants. This exemption would ensure that grants intended for operational purposes are not subjected to taxation, thereby preserving the financial viability of these institutions and preventing the inadvertent return of grant funds to the government through tax obligations.

Rationale

The current taxation framework places semi-government bodies and body corporates at a disadvantage by subjecting government grants received by them to taxation. This undermines the purpose of such grants, which are typically allocated for essential operational expenses. By introducing an exemption clause, these entities would be relieved from tax obligations on government grants, ensuring that the intended financial support is utilized effectively for its designated purposes. This measure not only safeguards the financial sustainability of semi-government bodies and body corporates but also promotes the efficient allocation of government funds towards key societal objectives.

1.39 LIMITATION OF EXEMPTION CERTIFICATE AVAILABILITY FOR FTR TAXPAYERS

MEDIUM

In cases with 100% FTR income, as in case of export of services, tax is collected or deducted not only under the relevant provision, but also adjustable taxes under various provisions of the Ordinance, which ultimately results into tax refundable.

The current provisions of section 159 do not provide for issuance of exemption certificate to persons whose income falls under the Final Tax Regime (FTR). Consequently, this restriction results in the accumulation of refunds for such taxpayers under adjustable tax provisions.

Recommendation

It is recommended that section 159 be amended to provide for issuance of exemption certificates to personal falling under 100% Final Tax Regime in respect all adjustable taxes.

Rationale

The modification of section 159 to extend exemption certificate availability to persons under the FTR aligns with principles of fairness and efficiency in taxation.

1.40 TAXABLE AMOUNTS THRASHOLD FOR INDIVIDUALS AND AOPs

MEDIUM

The existing taxable amounts subject to 0% tax rate under Division 1 of Part I of the First Schedule require reconsideration. Currently set at Rs. 600,000 for both salaried and non-salaried individuals, these thresholds may no longer adequately reflect prevailing economic conditions or ensure equitable taxation.

Recommendation

It is recommended to increase the taxable amounts chargeable at a 0% tax rate from Rs. 600,000 to Rs. 1,200,000 for salaried individuals and from Rs. 600,000 to Rs. 750,000 for non-salaried individuals. This adjustment aims to provide relief to taxpayers by allowing a higher threshold of income to be taxed at a 0% rate, thus reducing the tax burden on low-income individuals and promoting fairness in taxation.

Rationale

The proposed adjustment of taxable amounts at the 0% tax rate seeks to enhance equity in taxation and alleviate tax burdens on low-income individuals. By raising the thresholds, more individuals will benefit from the 0% tax rate on a larger portion of their income. This measure is essential for ensuring that tax policies are responsive to the needs of taxpayers and reflective of prevailing economic realities. Additionally, it demonstrates the government's commitment to promoting social justice and supporting the financial well-being of its citizens by implementing measures that provide meaningful relief to those with lower incomes.

1.41 HARMONIZING EXEMPTION CLAUSES OF INCOME TAX ORDINANCE 2001 VIZ-A-VIZ SPECIAL TECHNOLOGY ZONES AUTHORITY ACT 2021 AND SPECIAL ECONOMIC ZONES AUTHOURITY ACT, 2012

MEDIUM

Misalignment has been identified between the clauses outlined in the Income Tax Ordinance, conferring tax exemptions for zone enterprises and zone developers, and the corresponding provisions in Section 20 and 21 of the Special Technology Zones Authority Act, 2021 and Section 37 of the Special Economic Zone Authority Act, 2012. This lack of alignment may result in confusion regarding the interpretation and application of tax exemption provisions, necessitating harmonization to ensure consistency and clarity. A comparative analysis is as under:

STZ Act, 2021	Income Tax Ordinance, 2001	Remarks
Section 20(1)(a) – Zone Developer Exemption from **all taxes** under the Income Tax Ordinance, 2001 including tax on profits and gains, income tax, turnover tax, withholding tax, capital gains tax, income tax on dividend income and withholding tax on dividend;	**Clause (126EA) (a), Part I, 2nd Sch.** Profits and gains derived by – a. zone developer as defined in the Special Technology Zones Authority Act, 2021 (XVII of 2021) from development and operations of the zones for a period of ten years starting from the date of signing of the development agreement;	No provision in the Income Tax Ordinance, 2001 granting exemption from: a. Withholding taxes; b. Capital gain tax; c. Income tax on dividend; d. Withholding tax on dividend; and e. Minimum taxes other than under section 113.
Section 21(1)(a) – Zone Enterprises Exemption from **all taxes** under the Income Tax Ordinance, 2001 including tax on profits and gains, income tax, turnover tax, withholding tax, capital gains tax, income tax on	**Clause (126EA) (b), Part I, 2nd Sch.** a. zone Enterprises as defined in the Special Technology Zones Authority Act, 2021 (XVII of 2021) for a period of ten years from the date of issuance of license by the Special Technology Zone Authority; and	No provision in the Income Tax Ordinance, 2001 granting exemption from: a. Withholding taxes (except u/s 148 on import of capital equipment); b. Capital gain tax; c. Withholding tax on

STZ Act, 2021	Income Tax Ordinance, 2001	Remarks
dividend income and withholding tax on dividend;	**Clause (103D), Part I, 2nd Sch.** Dividend income and long-term capital gains of any venture capital fund from investments in zone enterprises as defined in the Special Technology Zones Authority Act, 2021 (XVII of 2021) for a period of ten years commencing from issuance of license by the Authority to the zone enterprise. **Clause (60DA), Part IV, 2nd Sch.** The provisions of section 148 shall not apply to the import of the capital equipment as defined in Special Technology Zones Authority Act, 2021 (XVII of 2021). (a) Zone developers as defined in Special Technology Zones Authority Act, 2021 (XVII of 2021) for consumption in the special technology zones for the period of ten years commencing from the date of signing the development agreement; (b) Zone enterprises as defined in Special Technology Zones Authority Act, 2021 (XVII of 2021) for a period of ten years from the date of issuance of license by the Special Technology Zone Authority; and **Clause (11A) (xliii), Part IV, 2nd Sch.** **(**Minimum Tax U/S 113) Persons qualifying for exemption under clause (126EA) of Part I of this Schedule;	dividend; and d. Minimum taxes other than under section 113.

SEZ Act, 2012	Income Tax Ordinance, 2001	Remarks
Section 37(b) exemption from **all taxes** on income for enterprises commencing commercial production by the thirtieth June 2020, in the SEZs for the next ten years; provided that exemption from all taxes on income for those zone enterprises or firms which commence commercial production after	**Clause (126E), Part I, 2nd Sch.** Income derived by a zone enterprise as defined in the Special Economic Zones Act, 2012 (XX of 2012) for a period of ten years starting from the date the developer certifies that the zone enterprise has commenced commercial operation and for a period of ten years to a developer of zone starting from the date of signing of the development agreement in the special	a. The condition commencing commercial production on or before June 30, 2020, to qualify for exemption of ten years is missing in the Income tax Ordinance, 2001 b. The extended exemption for five years, where commercial production is commenced after June

SEZ Act, 2012	Income Tax Ordinance, 2001	Remarks
the aforesaid date shall be for the next five years.	economic zone as announced by the Federal Government: Provided that this clause shall also apply to a co-developer as defined in Special Economic Zone Rules, 2013 subject to the condition that a certificate has been furnished— (a) by the developer that he has not claimed exemption under this clause and has relinquished his claim in favor of the co-developer; and (b) by the Special Economic Zone Authority validating that the developer has not claimed exemption under this clause and has relinquished claim in favor of the co-developer.	30, 2020, is missing in the Ordinance. c. Exemption from minimum taxes including on turnover, not provided in Income Tax Ordinance, 2001

Recommendation

It is recommended to harmonize the clauses specified in the Income Tax Ordinance with the corresponding provisions outlined in Section 20 and 21 of the Special Technology Zones Authority Act, 2021 and Section 37 of the Special Economic Zone Authority Act, 2012.

Rationale

Harmonizing the clauses between the Income Tax Ordinance and the Special Technology Zones Authority Act is crucial to enhance clarity and promote compliance in taxation. Consistency in clauses across legislative instruments reduces the risk of misinterpretation and ensures that taxpayers, regulatory authorities, and other stakeholders have a clear understanding of their rights and obligations. This measure fosters confidence in the tax system, facilitates smooth implementation of tax policies, and supports the objectives of promoting investment, innovation, and economic development within designated zones.

1.42 STATUS OF LIMITED LIABILITY PARTNERSHIP

MEDIUM

Limited Liability Partnership (LLP) is not defined in the Ordinance resulting in different classification as company or association of persons (AOP).

Recommendations

Limited Liability Partnership be defined with clarity as to its status as Company by inserting clause (vc) in section 80(2)(b)

"*(vc) a limited liability partnership as defined in the Limited Liability Partnership Act, 2017 (XV of. 2017)*"

OR

Inserting the words and figures "a *limited liability partnership as defined in the Limited Liability Partnership Act, 2017 (XV of. 2017)" in clause (a) of section 80(2)(a).*

1.43 DIVIDEND PAID BY INDEPENDENT POWER PRODUERS – CLAUSE (a) OF DIVISION III OF PART I AND CLAUSE (a) OF DIVISION I OF PART III OF THE FIRST SCHEDULE

MEDIUM

Current wording implies that the dividend is pass through item of IPP's to the power purchaser whereas in reality it is the tax on such dividend paid.

Recommendations

In clause (a) of Division III of Part I of First Schedule and clause (a) of Division I of Part III of First Schedule, after the word "such" the words "tax on" may be added.

The amended clauses will read as under:

"*7.5% in case of dividend paid by Independent Power Producers where such* ***tax on*** *dividend is a pass-through item under an Implementation Agreement or ……..*"

1.44 DIVIDEND PAID BY DEVELOPERS AND ENTERPRISES OF SPECIAL TECHNOLOGY ZONES

MEDIUM

It is a fact that material investment is required for capex in Special Technology Zones for establishing technology infrastructure, which is consistent with the Government's initiative for establishment of technology exporting entities and facilitate investment in such projects.

Since the income of developers and enterprise of Special Technology Zones are exempt, the dividend income from such entities in the hands of the investors/shareholders will be taxable @ 25% other than by Venture Capital Funds [as defined in the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003] which are exempt for 10 years.

Recommendations

To grant exemption of tax on dividend income received from zone developers or zone enterprises of Special Technology Zones having export proceeds exceeding USD 500,000 (suggested) and employing more than 50 (suggested) person;

Alternatively, reduced rate of tax of 7.5% on dividend income received from zone developers or zone enterprises of Special Technology Zones having export proceeds exceeding USD 500,000 (suggested) and employing more than 50 (suggested) persons be provided in clause (a) of Division III of Part I of First Schedule and clause (a) of Division I of Part III of First Schedule, by inserting clause (e) as under:

> "*(e) 7.5% in case of person receiving dividend from Zone Developer or Zone Enterprise eligible for exemption under clauses (126EA) of Part I of Second Schedule and having export proceeds exceeding USD 500,000 (suggested) and employing fulltime 50 (suggested) persons or more in the tax year.*"

Rationale:

To promote investment and in particular foreign direct investment.

1.45 CORPORATE FARMING

MEDIUM

Currently, the land holdings in Pakistan have shrunk to such level that farming is becoming cost inefficient and in case of corporate farming, the transfer of agricultural land, held for over 6 years, to a company incorporated for corporate farming venture attracts capital gains tax under section 37(1A) and withholding tax under section 236C and 236K.

Recommendations

An exemption be allowed on capital gains to land owner on transfer of land to a company incorporated for corporate farming venture as well as exemption from withholding tax under section 236C and 236K subject to the condition that the land is transferred as consideration in kind against

issuance of shares, which are held for at least five years and such company carries on the business of corporate farming on such land for five subsequent tax years.

Rationale:

To incentivize corporate farming and promote investment.

1.46 RECOVERY OF TAX NOT DEDUCTED OR COLLECTED; OR NOT DEPOSITED – SECTION 161

Tax recovered from a person for default in collecting or deducting tax; or not depositing the tax collected or deducted is being currently deposited in the name of the defaulter. As a result, the person from whom such tax was to be collected, deducted or deposited can't claim the credit of the same and on the other hand the defaulter is unable to recover the same from person from whom such tax was to be collected or deducted.

This is an apparent anomaly and requires to be redressed, particularly in cases where complete details of the persons from such tax were to be deducted, collected or deposited.

Recommendations

Appropriate provisions be introduced in the Ordinance.

1.47 TAX EXEMPTION FOR NON-PROFIT ORGANIZATIONS U/S 2 (36) & RULE 213

Non-Profit Organizations (NPOs) play a pivotal role in delivering essential services across Pakistan, including education, health, and social welfare. To avail tax exemptions, NPOs must obtain approval under Section 2(36) of the Income Tax Ordinance, 2001, following procedures outlined in Rule 213 of the Income Tax Rules, 2002. However, the current approval process can be protracted, leading to operational delays and financial uncertainties for these organizations. Therefore, the costs, both in terms of money and time, required for approvals should be minimized to encourage a culture of charity. However, in some instances, departments resort to coercive measures against these organizations to meet their ambitious targets.

Recommendations

Appropriate provisions be introduced in the Ordinance. In this respect, following insertion may be made after first proviso of 100C(4)(e)

> *"Provided also that where the Commissioner has not made an order of approval in writing, for approval of nonprofit organization, before the expiration of six months from the date when the application of approval along with annexures is submitted online, the approval required under respective rule shall be deemed to have been granted by the Commissioner."*

Rationale

Implementing this deemed approval mechanism will enhance efficiency by encouraging timely decision-making by tax authorities, reducing unnecessary delays. It will provide certainty to NPOs, allowing for clearer financial planning and uninterrupted operations. Moreover, it will promote philanthropy by minimizing hurdles, thereby fostering a more conducive environment for charitable activities. This amendment aligns with the government's commitment to support the non-profit sector and acknowledges the vital contributions of NPOs to national development.

1.48 MONETARY LIMITS UNDER SECTION 21(c), 21(l) AND 21(m) OF THE INCOME TAX ORDINANCE, 2001

Sections 21(c), 21(l), and 21(m) of the Income Tax Ordinance, 2001, impose monetary thresholds on deductible business expenditures to promote transparency and curb tax evasion. However, these thresholds are currently set at Rs. 25,000 for single transaction in Section 21(l)(a) and Rs. 32,000 for Section 21(m). Given the significant inflationary trends and currency depreciation in recent years,

these static limits have become increasingly restrictive, making the compliance with these provisions challenging for taxpayers dealing with routine business expenses.

Recommendations

In light of the prevailing economic conditions and inflation impacts over the last few years, it is recommended to revise the monetary thresholds under the aforementioned sections to more realistic levels that reflect current market realities. The proposed adjustments are as follows:

Section	Existing limit	Suggested limit
21(l) proviso (a)	25,000	75,000
21(m)	32,000	50,000
21(c):		
153(1)(a)	75,000	500,000
153(1)(b)	30,000	250,000

Rationale

These revisions of limits aim to align tax regulations with the current economic landscape, thereby facilitating compliance and reducing the administrative burden on taxpayers. Further, the proposed adjustments also consider the impact of inflation and currency depreciation on business expenses, ensuring that the thresholds remain relevant and effective.

1.49 REVIEW OF EX-PARTE ORDERS UNDER SECTIONS 161, 121 AND 174 OF THE INCOME TAX ORDINANCE, 2001

Ex-parte orders under Sections 161, 121, and 174 of the Income Tax Ordinance, 2001, are frequently issued by the tax department without proper service of notice, leading to significant challenges for taxpayers. Such orders often result in substantial and unjustified tax demands, adversely affecting the financial stability of individuals and businesses. The absence of a structured mechanism for oversight and approval of these orders exacerbates the issue.

Recommendations

It is recommended to establish a hierarchical review mechanism for ex-parte orders, ensuring that all such orders are subject to oversight by higher authorities. Specifically, the following steps are proposed:

1. Initial Review by Assessing Officer
2. Secondary Review by Additional Commissioner
3. Final Approval for any ex-parte order by the Commissioner

Rationale

This review process is already in place for refund cases and has proven effective. Implementing a similar mechanism for ex-parte orders will provide an additional layer of scrutiny, thereby reducing the incidence of unjustified tax demands.

1.50 SERVICE OF NOTICE

Effective communication between the Federal Board of Revenue (FBR) and taxpayers is crucial for ensuring compliance and upholding taxpayers' rights. Currently, the FBR predominantly relies on electronic means, such as emails and the IRIS portal, to serve notices. However, this approach has led to instances where taxpayers, remain unaware of notices due to limited access to electronic communication channels. Consequently, ex-parte orders are passed without providing taxpayers a fair opportunity to respond, undermining the principles of natural justice.

Recommendations

To address these concerns and ensure that taxpayers are aware of proceedings before any order is passed against them, it is recommended that the FBR makes the personal service of at least one notice (physical service), ideally issuance of show cause notice should be mandatory upon the officer in respect of any proceedings against the taxpayer before passing of an ex-parte order so that he/she may be aware of it.

By implementing the above, the FBR can enhance the likelihood that taxpayers receive and acknowledge notice at any stage of proceeding so that the onus is shifted upon the taxpayer, thereby reducing the incidence of ex-parte assessments and promoting fairness in tax proceedings.

Rationale

Relying solely on electronic means for serving notices has proven insufficient, particularly for non-resident taxpayers or those with limited access to digital communication. Adopting a comprehensive approach, as permitted under Section 218, ensures that notices are more effectively communicated.

1.51 IMPLEMENTATION OF E-HEARING OPTIONS UNDER SECTION 227(E) OF THE INCOME TAX ORDINANCE, 2001

The Federal Board of Revenue (FBR) introduced the electronic hearing (e-hearing) system in 2021 to streamline and enhance the efficiency and accessibility of tax audit and assessment processes. While the initiative aimed to simplify tax proceedings, it has not been effectively implemented due to the non-availability of the required mechanisms.

Recommendations

It is recommended that the e-hearing facility be made available at various stages of the tax process i.e., at the assessment level, before the Commissioner (Appeals) and at the Appellate Tribunal level, at the discretion of the taxpayer. This will allow taxpayers to choose the mode of hearing most convenient for them.

Rationale

Making e-hearing facilities available at these stages will enhance taxpayer convenience, particularly for those who face logistical challenges in attending in-person hearings. It will reduce administrative burdens by streamlining processes and minimizing delays. It will also align tax procedures with modern technological practices, creating a more efficient, transparent, and accessible tax system.

1.52 FILING OF WEALTH STATEMENT BY NON-RESIDENTS IN CASE OF LOCAL ASSETS

Currently, non-resident individuals are not obligated to file a wealth statement along with their return of income. This exemption has led to the non-declaration of local assets held by non-residents, resulting in gaps in asset transparency and potential tax base erosion.

Recommendation

It is recommended that the declaration of local assets be made mandatory for non-residents through appropriate amendments to Section 116 of the Income Tax Ordinance. This will ensure that all taxpayers, regardless of residency status, disclose their Pakistan-based assets in a consistent and transparent manner.

Rationale

Mandating the declaration of local assets by non-residents will promote greater transparency, improve asset tracking, and support the integrity of the tax system. It will also help mitigate the risk of asset concealment and ensure equitable tax compliance across all categories of taxpayers.

1.53 SYSTEM GENERATED NOTICES ISSUED UNDER SECTION 114(4)

MEDIUM

Currently, it is a common practice that whenever a person gets registration with the Federal Board of Revenue (FBR), a system-generated notice under Section 114(4) of the Ordinance is automatically issued for preceding tax years. As per the law, the taxpayer is required either to file income tax returns in response to the notice or to provide a justification for the non-filing. However, a significant number of taxpayers are not computer literate and rely heavily on their tax consultants. It is impractical for consultants to check each taxpayer's IRIS login individually. As a result, many cases proceed to assessment under Section 121 without proper compliance, often due to legal deficiencies on the part of the department and unawareness to the taxpayer. These assessments are frequently annulled or remanded by appellate forums, leading to a waste of time and resources for both the authorities and taxpayers.

Recommendation

It is recommended that notices under Section 114(4) should not be system-generated. Instead, they should be issued following a reasonable inquiry by the assessing officer. The issuance of such notices should be preceded by a proper show-cause notice, and the taxpayer must be served in accordance with legal procedures, including dispatch of notices via registered post or courier. Only those cases should proceed to assessment under Section 121 where the assessing officer can substantiate the proceedings at the appellate level.

Rationale

This approach will help avoid unnecessary remands, reduce the burden on appellate forums, and prevent the accumulation of unrealized tax demands that remain stuck in litigation without contributing to government revenue.

1.54 ISSUANCE OF GENERIC NOTICES WITHOUT INDUSTRY-SPECIFIC UNDERSTANDING

MEDIUM

A common practice within the Federal Board of Revenue (FBR) is the issuance of generic notices for audits or information collection without adequate consideration of the nature of the taxpayer's business or the specific areas where potential revenue leakages are most likely. This broad approach often leads to the issuance of unfocused information requests and arbitrary disallowances of expenses, many of which are ultimately annulled by appellate forums due to lack of proper justification or comprehension of industry-specific practices.

Recommendation

Instead of issuing generic notices and collecting information across all heads of income, a more targeted approach should be adopted. Information should be gathered under Section 176 of the Income Tax Ordinance after conducting a thorough preliminary review. Only in cases where discrepancies or indications of tax leakage are identified should the case be selected for audit and further proceedings.

Rationale

This approach will result in more meaningful audits, reduce unnecessary litigation, and improve the overall efficiency and credibility of the tax assessment process.

1.55 INITIAL ALLOWANCE U/S 23

LOW

It is proposed that the Initial Depreciation Allowance rate be restored to 50% for Plant, Machinery & Equipment and 25% for Buildings as was the case prior to the Finance Act 2013 and 2014 respectively.

Rationale

This incentive is a major investment driver and motivates investments in different sectors of the economy. The benefits of accelerated depreciation are merely a timing difference whereby providing relief to the investor by paying less tax in the initial period of investments.

1.56 ADDITIONAL PAYMENT FOR DELAYED REFUNDS U/S 171

LOW

U/s 170(4) of the ITO, the Commissioner on receipt of a refund application may serve an order within 60 days. Section 171(1) provides that the refund may be paid within three months of the due date, which has been explained to be the date of order u/s 170.

Recommendations

- It is suggested that where the refund order is not passed by the Commissioner within 60 days, it shall be deemed to have passed on the 60th day; and
- Accordingly, the additional payment for delayed refunds to also commence from the 61st day of filing of refund application.

Rationale

In order to remove anomaly in the law.

1.57 CONDONING OF TIME LIMIT BY THE BOARD U/S 214A

LOW

The Federal Board of Revenue (FBR) is empowered to condone the time or period specified under any of the provisions of the ITO or rules made thereunder within which any application is to be made or any act or thing is to be done, in any case or class of cases and permit such application to be made or such act or thing to be done within such time or period as it may consider appropriate. The scope of exemption was extended by introducing an explanation in Section 214A vide Finance Act, 2012 by way of which the scope to grant condonation was extended to cover the defaults of the officials of Inland Revenue for non-fulfillment of their official duties within the prescribed time.

Recommendation

Amendments made in Section 214A through Finance Act, 2012 should be withdrawn.

The provisions of Section 214A, prior to amendment made through Finance Act, 2012, implied that this power cannot be used in a manner detrimental to a taxpayer. However, by virtue of the amendment made through Finance Act, 2012 it has been specifically provided that this power to condone the time or period of an act or thing to be done by any of the Income Tax Authorities can also be condoned.

Rationale

This amendment is highly prejudicial to the interest of taxpayers and indirectly gives a blanket power to the FBR to override the statutory time limit or period of any act or thing to be done by the Income Tax Authorities. This provision is also unconstitutional as it gives power to an administrative body to nullify the time limitation provided to the income tax authorities under the ITO to act or do things within the timeline provided in the ITO.

1.58 POWERS OF DIRECTOR GENERAL (INTELLIGENCE & INVESTIGATION) SECTION 230 READ WITH SRO 115(I)/2015.

LOW

The Federal Board of Revenue vide S.R.O.272 (I)/2021 dated 02 March 2021 conferred upon the Directorate General (Intelligence and Investigation), Inland Revenue, the powers of the Chief Commissioner/Commissioner:

- to exercise powers and perform functions u/s 174, 175, 176, 177 (other than power to initiate audit), 178, 179, 180, 181, 182, Part III, Part XI of Chapter X, Sections 205 and 221; and
- to investigate Suspicious Transactions Reports (STRs) or other assets of persons or classes of

persons impounded by any department or agency of the Federal or Provincial government and prepare/transmit reports to respective RTOs or LTOs for the purpose of application of Section 111 and for taking appropriate action under the ITO.

Recommendation

The law should be amended so that the authority of Director General Intelligence and Investigation is exercised only to investigate Suspicious Transactions Reports (STRs), or other assets of persons or classes of persons impounded by any department or agency of the Federal or Provincial government and prepare / transmit reports to respective RTOs or LTOs for the purpose of application of Section 111 and for taking appropriate action under the ITO.

Rationale

The creation of parallel authorities for the purpose of sections 174, 175, 176, 177, 178, 179, 180, 181, 182, Part III, Part XI of Chapter X, Sections 205 and 221 is causing problems to the taxpayers.

1.59 EXEMPTION OF INCOME OF WPPF & WWF – SECTION 54

Income of the Workers' Profit Participation Fund and Workers Welfare Fund is exempt under the WPP Fund Act and WWF Ordinance respectively, and the same was accepted under the ITO by virtue of proviso to Section 54 of the ITO as it stood before an amendment brought in through the Finance Act, 2008. However, through the Finance Act, 2008 the proviso to Section 54 of the ITO was omitted.

As a result, exemption provided to the income of the WPP Fund under the WPP Act and WWF under the WWF Ordinance lost its applicability, which appears contrary to the entire scheme.

Additionally, WWF/WPPF paid to provincial authorities is allowed as deductible allowance u/s 60A and 60B of the Income Tax Ordinance, 2001. A proviso has also been inserted which disallows payment of WWF/WPPF to provinces by a trans-provincial establishment.

Recommendation

A corresponding amendment should be made giving exemption to the income of WPP Fund established under the WPPF Act or under any provincial WPPF Act and WWF established under the WWF Ordinance, 1971 or under any provincial WPPF and WWF Acts. Accordingly, it is proposed that the following sub-clause be inserted in Clause (66) of Part I of Second Schedule to the ITO.

"Workers Participation Fund established under the Companies Profits (Workers Participation) Act, 1968 or under any provincial WPPF Act and Workers Welfare Fund established under the Workers Welfare Fund Ordinance, 1971 or under any provincial WWF Act."

Clarity should be provided in the law regarding a trans-provincial establishment i.e., basis to determine if an establishment is trans-provincial or otherwise such as based on manufacturing premises, sales offices etc.

Rationale

The amendment in Section 54 of the ITO had jeopardized a number of entities, which were exempt from income tax under various statutes other than the Income tax law. Accordingly, certain sub-clauses were inserted in Clause (66) of Part I of the Second Schedule to the ITO granting exemption from Income Tax to entities, which were enjoying such exemptions under their respective statutes after the proviso to Section 54 of the ITO, was withdrawn. However, due to an oversight, the exemption of income of WPPF and WWF could not find a place in Clause (66) of Part I of the Second Schedule.

1.60 EXPRESSION 'ANY BUSINESS CONNECTION' U/S 101(3)(d)

The words 'any business connection' have very broader meaning. The same has been used liberally by tax authorities even for activities carried out by independent third parties including but not limited to distributors and other intermediaries, in the ordinary course of their own business, outside Pakistan. This results in unnecessarily extending the scope of Pakistan source income.

Recommendation

It is proposed that clause (d) in sub-section (3) of Section 101 be omitted or clarity provided so as to prevent its misinterpretation.

Rationale

The concept of 'any business connection' is no more applicable internationally due to the usage of the term 'permanent establishment', which is understood internationally in the context of Double Taxation Treaties and their commentaries.

1.61 FOREIGN TAX CREDIT U/S 103(7)

LOW

A credit is allowed u/s 103(7) only if the foreign income tax is paid within two years after the end of the tax year in which the foreign income to which the tax relates was derived by the resident taxpayer.

This sub-section should be omitted. Alternatively, the period of two years should be increased to at least five years.

Where a taxpayer adopts accrual basis of accounting, the foreign source income is offered to tax in the year in which it becomes due. However, receipt of the income in some cases is delayed beyond the time period of two years due to procedural limitations and regulations imposed by the remitting country. The taxpayer in this case is unable to claim foreign tax credit (usually withheld by the remitting country in the year of payment) on the income already taxed two years ago.

Rationale

In many countries, assessment of the income and tax liability takes a long time and the tax paid on completion of such assessments cannot be claimed due to the limitation of two years from the end of tax year. In particular, this problem is very common in case of resident taxpayers deriving foreign source income from Azad Kashmir, which for taxation purposes is treated as a foreign country.

Further, where a taxpayer adopts accrual basis of accounting, the foreign source income is offered to tax in the year in which it becomes due. However, actual receipt of the income and deduction of tax in some cases is delayed beyond the time period of two years and, as a result, the taxpayer is unable to claim foreign tax credit on income already taxed on accrual basis of accounting.

1.62 CAPITAL GAIN ON DISPOSAL OF ASSET UNDER A SCHEME OF ARRANGEMENT AND RECONSTRUCTION

LOW

Presently, the sub-sections (1), (2) and (5) of section 97A of the Income Tax Ordinance 2001 (the "Ordinance") are read as follows:

i *No gain or loss shall be taken to arise on disposal of asset from one company (hereinafter referred to as the "transferor") to another company (hereinafter referred to as the "transferee") by virtue of operation of a Scheme of Arrangement and Reconstruction u/s 282L and 284 to 287 of the Companies Act, 2017 (XIX of 2017) or section 48 of the Banking Companies Ordinance, 1962 (LVII of 1962), if the following conditions are satisfied, namely:*
   - *(a) the transferee must undertake to discharge any liability in respect of the asset acquired;*
   - *(b) any liability in respect of the asset must not exceed the transferor's cost of the asset at the time of the disposal;*
   - *(c) the transferee must not be exempt from tax for the tax year in which the disposal takes place; and*
   - *(d) scheme is approved by the High Court, State Bank of Pakistan or Securities and Exchange Commission of Pakistan, as the case may be, on or after first day of July 2007.*

ii *No gain or loss shall be taken to arise on issue, cancellation, exchange or receipt of shares as a result of Scheme of Arrangement and Reconstruction u/s 282L and 284 to 287 of the Companies Act, 2017 (XIX of 2017) or section 48 of the Banking Companies Ordinance, 1962 (LVII of 1962) and approved by:*
   - *(a) the High Court;*
   - *(b) State Bank of Pakistan; or*

(c) Securities and Exchange Commission of Pakistan, as the case may be, on or after the first day of July 2007.

iii Where sub-section (2) applies and the shares issued vested by virtue of the Scheme of Arrangement and Reconstruction u/s 282L and 284 to 287 of the Companies Act, 2017 (XIX of 2017) or section 48 of the Banking Companies Ordinance, 1962 (LVII of 1962) and approved by the High Court or State Bank of Pakistan or Securities and Exchange Commission of Pakistan as the case may be, are disposed of the cost of shares shall be the cost prior to the operation of the said scheme.

Recommendations

i. The existing reference to sections 282L of the Companies Act 2017 should be replaced with 'section 282L of the repealed Companies Ordinance 1984';

ii. The existing reference to section 284 to 287 of the Companies Act 2017 should be replaced with 'sections 279-282 of the Companies Act 2017';

iii. Section 284 of the Companies Act 2017 should remain part of section 97A of the Income Tax Ordinance 2001; and

iv. Section 97A should be amended to account for the effect of section 284 of the Companies Act 2017, where under, the requirement of approval of the Scheme of Arrangement and Reconstruction by the High Court or Securities and Exchange Commission of Pakistan has been waived off for amalgamation of (i) wholly owned subsidiaries in holding company; and (ii) two or more companies, each of which is directly or indirectly wholly owned by the same person.

Rationale

Companies Ordinance 1984 was repealed by the Parliament in 2017 vide Companies Act 2017 and reference to the Companies Ordinance 1984 was substituted with Companies Act 2017 vide Finance Act 2020. However, for the following reasons, further amendments to section 97A, as proposed above, are need of the hour to correctly and appropriately account for the provisions of the Companies Act 2017:

1. According to section 509 (Repeal and Savings) of the Companies Act 2017, the Companies Ordinance 1984 has been repealed except for Part VIIIA consisting of sections 282A to 282N (that includes section 282L); and the provisions of the said Part VIIIA along with all related or connected provisions of the repealed Companies Ordinance 1984 will be applicable mutatis mutandis to Non-Banking Finance Companies in a manner as if the Companies Ordinance 1984 has not been repealed;

2. Section 279 to 282 of the Companies Act, 2017 are the provisions corresponding to sections 284 to 287 of the repealed Companies Ordinance 1984;

3. Provisions of section 284 of the Companies Act 2017 were introduced for the first time under the Companies Act, 2017 and there were no corresponding provisions under the repealed Companies Ordinance 1984; and

4. Moreover, section 284 of the Companies Act 2017 has waived off the requirement of approval of the Scheme of Arrangement and Reconstruction by the High Court or Securities and Exchange Commission of Pakistan for amalgamation of (i) wholly owned subsidiaries in the holding company; and (ii) two or more companies, each of which is, directly or indirectly, wholly owned by the same person.

In view of the foregoing reasons, the afore-mentioned changes have been proposed to amend the section 97A of the Income Tax Ordinance, 2001 to correctly and appropriately account for the changes introduced under the Companies Act 2017.

DIRECT TAXATION
TAXATION OF NON-RESIDENTS

1.63 FOREIGN DIRECT INVESTMENT ("FDI")

MEDIUM

A separate Schedule for FDI in export-oriented manufacturing industries, be introduced for extending concessions and protections and prescribing qualifying criteria for FDIs. Related provisions may also be introduced in other relevant statues. The concession, protections and conditions may include:

a) Consistency in income tax regime, for at least next ten years, from the year of commencement of operations of the industry established under the scheme;
b) Conditions of minimum limit of investment, creation of specified number / percentage of employments for Pakistan nationals, specified percentage of transfer of technology within a specified number of years of operations.

Rationale

Encouraging FDI is required under current situation, which may help in reviving economic activities in the Country.

1.64 DEFINITION OF PERMANENT ESTABLISHMENT U/S 2(41) (d)

MEDIUM

Furnishing of services, including consultancy services by any person through employees or other personnel engaged in Pakistan by the person for such purpose is considered as having a Permanent Establishment ("PE") in Pakistan. Ironically, no minimum threshold of physical presence of the employees or other personnel in Pakistan is provided in Law.

It is proposed to amend clause (d) to provide that a PE shall be established where the stay of the employees or other personnel exceeds 90 days in a tax year.

Rationale

The absence of minimum threshold of stay of employees or other personnel for services could trigger a PE situation even with one-day presence in Pakistan, which cannot be the intention of legislature.

1.65 DEFINITION OF PERMANENT ESTABLISHMENT U/S 2(41) (g) - EXPLANATION B

MEDIUM

Explanation B at the end of sub-clause (g) in Section 2(41) should be amended to insert the words "other than the actual buyer of the goods imported" immediately after the words "any other person".

Rationale

These amendments are more of clarifying nature to remove ambiguity.

1.66 EXPRESSION 'ANY BUSINESS CONNECTION' U/S 101(3) (d) AND 172(3)(b)

MEDIUM

The words 'any business connection' has very broader meaning. The same has been used liberally by tax authorities even for activities carried out by independent third parties including but not limited to distributors and other intermediaries, in the ordinary course of their own business, outside Pakistan. This results in unnecessarily extending the scope of Pakistan source income.

This may also lead to resident individuals in Pakistan being considered representatives of non-residents due to business connections.

It is proposed that clause (d) in sub-section (3) of Section 101 and clause (b) in sub-section (3) of Section 172 be omitted for clarity and preventing its misinterpretation.

1.67 INDIRECT TRANSFER OF ASSETS OUTSIDE PAKISTAN U/S 101A

MEDIUM

The Finance Act, 2018 introduced section 101A primarily to tax gain arising on indirect transfer of assets outside Pakistan through non-resident holding company structures. A mechanism for collection of advance tax was also introduced within this section at the higher of 10% of the Fair Market Value (FMV) of the transferred assets or 20% of the gain arising on such transfer.

This section does not provide an option for seeking tax exemption or lower rate taxation certificate from the Commissioner by the Resident Company or the Seller where it can be demonstrated that the actual tax on capital gains arising on such transaction is less than 10% of FMV or where the Seller is covered under the provision of Double Taxation Agreement (DTA).

It is proposed either to amend this section to empower the Commissioner to issue a tax exemption or a lower rate of tax certificate; or extend the application of section 159 to section 101A.

Rationale

Advance tax under this section, in some cases, could result in a much higher incidence of tax if compared with normal Capital Gains Tax rate on direct disposal transactions. Furthermore, in certain cases, the alienator may be genuinely covered under the DTA which allows total exemption from, or a lower rate, tax in Pakistan.

1.68 SEEKING WEALTH STATEMENT BY THE COMMISSIONER U/S 116(1)

MEDIUM

Under sub-section (2) of section 116, only residents are required to file wealth statement. However, sub-section (1) of section 116 authorizes the Commissioner to seek wealth statement from any person being an individual, which may include non-resident individual. Since non-resident is not required to file his return on world income basis, the extension of this sub-section to non-resident individual does not seem appropriate. It is therefore proposed as under:

Wealth statement of non-residents be made mandatory for only their assets and liabilities in Pakistan;

Additionally, if a taxpayer declares himself a non-resident than there is no requirement to file wealth statement. However, the form of electronic return still requires filling out wealth statement which is against the law. Therefore necessary correction is required in the Tax return form for individuals on the IRIS portal.

Rationale

This amendment is necessary to prevent the risk of it being used to seek wealth statement from a non-resident who is not liable to be taxed on world income basis.

1.69 RESTORATION OF FINAL TAX REGIME U/S 152(1AA) & 152 (1AAA) read with Section 152(1B)

LOW

Taxation of income of non-residents from insurance and re-insurance premiums u/s 152(1AA) and advertisements relaying from outside Pakistan u/s 152(1AAA) read with section 152(1B) has been moved from final tax to minimum tax regime by the Finance Act, 2021, perhaps, without realizing that it would increase the complexity level for determination of taxable income arising from such transactions in Pakistan.

Rationale

Considering that the non-residents are less likely to have taxable income that will be subject to tax more than the minimum tax, thereby field officers would challenge such tax declarations. Accordingly, it is strongly suggested to withdraw the minimum tax regime and restore the final tax regime retrospectively.

1.70 BUSINESS INCOME OF A NON-RESIDENT PERSON U/S 152

MEDIUM

The Finance Act 2018 introduced amendments in sections 2(41), 101(3) and 152(7) to tax supply of goods by a non-resident under an overall arrangement for the supply of goods, installation, construction, assembly, commission, guarantees or supervisory activities ("Cohesive Business Operations") even if the supply is made outside of Pakistan and the importer on record is the purchaser.

These amendments were made to stop Base Erosion and Profit Shifting (BEPS) by an artificial use of permanent establishment and misuse of bilateral treaties.

Primarily, taxing supply of goods from outside Pakistan is contrary to the principles of international taxation. The jurisdiction to tax such supply of goods should remain with the country from where the supply originated.

These amendments are more likely to have following ramifications:

a) it is detrimental to the overall strategy of winning foreign investments in Pakistan as under these amendments, tax is more likely to be levied in Pakistan on supply of plant machinery and equipment by the offshore suppliers;

b) non-residents would be hesitant in accepting projects in Pakistan unless the tax is borne by the recipient of goods or services in Pakistan;

c) the cost of doing business in Pakistan is more likely to increase if the offshore supplier of goods and services require grossing up of the price to neutralize the risk of tax levied in Pakistan on such goods and services; and

d) the non-residents may not be able to claim credit for taxes paid in Pakistan on such supplies taxed in the home jurisdiction.

It was observed the field officers in several cases challenge the automatic withholding tax exemption available to the non-residents where they implied that the supplies made by the non-resident was a part of EPCC contract and alleged that the activities were performed by the associate or PE of the non-resident in Pakistan. Using this provision, the field officers try to recover the withholding tax u/s 152(4B) as well as treating the non-resident having a PE as per newly inserted clause (g) of Section 2(41).

Rationale

The amendments were introduced to implement the recommendations of BEPS Action Plan 7. However, the scope of BEPS Action Plan 7 is to ensure taxation of artificial splitting of contracts or transactions, and not to tax offshore supplies altogether. Hence, the amendments in sections 101(3), 152(7) and the explanation in section 2(41) are beyond the scope covered by Action Plan 7 and should be modified to prevent taxation of offshore supplies. The field force may examine the EPCC contracts to determine arm's length price of the offshore supply and onshore services u/s 108 and 109, and challenge if there is a pricing issue for onshore services.

Further, misuse of these provisions could result in increasing the cost of doing business in Pakistan and impacting the foreign investments.

1.71 PAYMENTS TO NON-RESIDENTS U/S 152

MEDIUM

There is a requirement to serve a notice to the Commissioner by a person making payment to a non-resident without deduction of tax. The Commissioner is mandated to pass an order within 30 days of the service of such notice either concurring with the payer; or directing the payer to make payment after deducting tax under sub-section (2) of Section 152, read with DTA. However, the law is silent on allowing any extension in the time for passing of the order; or whether an order shall be deemed to have been passed on the expiry of 30 days. In the absence of an order of the Commissioner, the payers are reluctant to take the risk of making payment without deduction of tax on the expiry of 30 days for two major reasons:

a) Risk of recovery of un-deducted tax u/s 161 of the Ordinance; and

b) the Banks insist on production of an order of the Commissioner to remit the payment to the non-resident outside Pakistan.

To address this issue, it is strongly recommended that a sub-section be inserted providing that the Commissioner shall be deemed to have concurred with the notice served by the payer if the order is not passed within 30 days. The electronic system may also provide for issue of deemed order automatically.

Rationale

Timely payments to non-residents are critical for business. Accordingly, 30 days' time allowed for passing of the order without a provision of deemed order on expiry of 30 days is quite repressive from business perspective. The Finance Act, 2021 has already inserted provisos in section 159 for automatic issue of exemption certificate in case of a company if the certificate requested is not issued within 15 days.

1.72 REPRESENTATIVE U/S 172

Clause (a) of sub-section (3) of section172 provides that a person who is employed by, or on behalf of, the non-resident person may be declared a representative of the non-resident for tax purposes.

It is proposed that clause (a) of sub-section (3) of section 172 should either be deleted or modified to restrict it to an employee who is an associate of, or beneficially connected with, the non-resident person.

Rationale

This amendment is necessary to prevent the paid employee of the non-resident facing the unnecessary brunt of the tax authorities on tax matters related to a non-resident employer.

1.73 SUPER TAX UNDER SECTION 4C OF THE ORDINANCE IN ADVANCE UNDER SECTION 147 OF THE ORDINANCE BY NON-RESIDENT

Till tax year 2023, super tax was required to be discharge alongwith the return of income. Subsequently section 4C(5A) of the Ordinance was inserted vide Finance Act, 2023 whereby super tax is required to be discharged in advance in terms of the provisions of section 147 of the Ordinance and accordingly sub-section 4AA of section 147 of the Ordinance has also been inserted.

Generally, the Pakistan source income of the FIIs is comprising of Dividend Income [FTR income], Capital Gains and Interest Income.

With refence to the discharge of advance tax on Capital Gains, National Clearing Company Pakistan Limited [NCCPL] is authorized to compute and collect tax under section 4C at the rates specified in Division IIB of Part I of the First Schedule of the Ordinance.

However, payment of advance tax on income other than Capital Gains i.e. Dividend Income and Interest Income or any other income, poses significant administrative burdens and compliance challenges for non-resident taxpayers.

The primary challenge faced by non-residents is the need to project their total income accurately from different heads to determine whether it falls under the threshold for the levy of Super Tax. This necessitates detailed tax projections and calculations, which can be complex and time-consuming, particularly in an environment of uncertainty regarding dividend distributions and other income realizations.

It is proposed that provide an exemption for non-residents, particularly FIIs, from the requirement to discharge Super Tax in advance under Section 147 of the Ordinance.

Rationale:

Exempting non-residents would alleviate administrative burdens and compliance challenges, allowing them to focus on investment activities without undue tax-related complexities.

By exempting non-residents from advance tax discharge requirements, Pakistan can enhance its attractiveness as a destination for foreign investment. Simplifying tax compliance procedures fosters a more investor-friendly environment, encouraging greater capital inflows and supporting economic growth.

1.74 TEMPORARY (SHORT TERM) REGISTRATION UNDER INCOME TAX ORDINANCE

The current tax registration framework poses significant challenges for non-residents, particularly institutional investors have registered in Pakistan for investment purposes with the intention of capitalizing the investment opportunities for few years, considering volatility of economic condition of Pakistani market.

When non-resident institutional investors withdraw their investments and close operations if the Pakistani market becomes economically unviable. Despite filing notice for discontinuation of business, different notices are being serving to the fund and on some instances ex-party orders; leading to legal complications upon their return after a few years. This situation restrains them from investing in Pakistan in the future.

To address these challenges effectively, it is propose the introduction of a provision allowing for registration for a specific number of years under certain conditions.

Rationale:

This provision would offer foreign investors and professionals a favorable tax situation in Pakistan. It would facilitate ease of compliance and encourage continued engagement in the Pakistani market, ultimately fostering a more conducive environment for investment and economic growth.

DIRECT TAXATION
TAXATION OF IT BUSINESS

1.75 EXTENSION OF FINAL TAX REGIME (FTR) ON IT EXPORT INCOME TILL JUNE 2035.

HIGH

It is estimated that half of the remittances inflows are changed at a 1% tax rate while the other half (being PSEB registered) pay 0.25% FTR. If exports are estimated to be US$ 4 billion this year, the total collection of taxes is approximately

PSEB registered companies Tax (0.25% tax): US$ 5 million

Non-PSEB registered companies Tax (1% tax): US$20m

Total: US$ 25 m

PSEB predicts, in line with extensive discussions with the industry that the increase in remittances and economic activity driven by the FTR extension is likely to more than offset the direct tax revenue foregone. The duration of the FTR extension is as important as the FTR itself. In fact the industry has stated in numerous interactions that the FTR may not be brought to zero instead, it should be extended to at least 10 years to provide a semblance of stability to the industry.

The long term stability in policy could potentially deliver a 20% increase in additional remittances inflow into Pakistan.

Rationale:

The current FTR for IT & ITeS Exporters is valid till June 2026 which provides for 0.25% FTR for entities registered with PSEB and 1% for entities not registered with PSEB.

Extending 0.25% FTR for entities registered with PSEB and 1% for non-PSEB registered IT/ITeS entities for 10 years in the Finance Bill 2025 would provide long term predictability and semblance of stability to the industry and therefore facilitate high quality growth.

1.76 EXEMPTION OF WHT ON EXPORTERS' SPECIAL FOREIGN CURRENCY ACCOUNTS (ESFCA'S) INTERNATIONAL TRANSACTIONS

HIGH

The exact data pertaining to ESFCA WHT collection is available with FBR and hence can provide a potential loss of revenue if the exemption is implemented.

In line with informal discussions, it has transpired that ESFCAs are likely not being used extensively for international transactions and perhaps just 1% of the deposits in ESFCAs are currently being utilized by the account holders for international transactions. One of the reasons frequently cited by IT companies is transaction charges on ESFCA transactions.

There are approximately 35,000+ ESFCA accounts as reported by SBP. Eliminating WHT on ESFCA transactions would incentivize exporters to utilize these accounts, potentially increasing the remittances inflow.

According to internet-based search, the removal of WHT generally tends to enhance business confidence, improve banking system usage, and stimulate economic activities, which, in the context of Pakistan, would facilitate IT exporters, thus in turn enhancing IT exports which are estimated at an additional USD 300–400 Mn per year.

Rationale:

Payments made from ESFCA be exempted from 5% withholding tax and any other additional charges or taxes till June 2035.
The exemptions should apply to all categories of IT services to prevent ambiguity in implementation and foster consistent growth and investment in all segments of the digital economy.

This would help build confidence of IT Industry and make remitting to Pakistan more attractive due to lower cost for making payments abroad.

1.77 DISTINCTION BETWEEN FREELANCERS AND REMOTE WORKERS

HIGH

The definitions of freelancers and remote workers be included in the Finance Bill 2025 for ensuring clear distinction between the two categories of IT workforce. The definition proposed is as follows:

1.1 Freelancer (Independent Contractor)

A freelancer is a self-employed individual who provides services to multiple clients without a long-term employment contract. They manage their taxes, typically paying 1% on remittances (0.25% if PSEB registered), and are not entitled to structured employment benefits such as health insurance or pensions. They must be registered with Pakistan Software Export Board (PSEB) in order to be categorized as a freelancer.

OR

For the purpose of section 154A of Income Tax Ordinance (ITO) 2001, freelancer means an individual fulfilling all the following conditions:

1. The individual is engaged in the export of services;

2. The individual export services to one or more foreign clients through online freelancing platforms and/or social media platforms with gross annual receipts up to US$ 18,000. For export receipts exceeding US$18,000, the freelancer must have three or more clients and must register with PSEB.

3. Freelancers with one client must provide an affidavit to PSEB stating that he/she is not an employee of the client.

Provided that an individual shall still be deemed to be a freelancer and neither of the conditions related to minimum clients and maximum gross annual receipts mentioned at serial # 2 & 3 respectively shall apply in any of the following cases:

a. The individual pays taxable salaries to at least three employees and such employees are duly registered with EOBI;

b. The individual is engaged as consultant for export of services by a foreign government or a company owned by foreign government or United Nations or any entity of United Nations

1.2 Remote Worker

A remote worker is a formally employed individual who works remotely for only a single foreign or domestic company under a permanent contractual basis. They need to pay taxes as regular employees.

OR

For the purpose of section 154A [ITO 2001], Remote worker means an individual, other than a freelancer as defined in section 2(20) [ITO 2001], who receives income from salary through an employment contract with a foreign entity while the employment is exercised in Pakistan.

Explanation:

For the removal of doubt, it is clarified that the definition of remote worker is inserted for the purpose of clarification only and the insertion of this definition shall not be construed as creation of a new category of taxpayers. It is clarified that Remote workers shall be deemed to have always been included in the definition of employee as provided under clause 20 of section 2 [ITO 2001] and the salary income of remote worker from employment exercised in Pakistan, albeit with a foreign employer, shall be deemed to have always been subject to tax as Pakistan source salary income under section 12 read with sub-section 1 of section 101 [ITO 2001].

Note: Any disputes arising from interpretations of these definitions will be referred to a PSEB committee for resolution, whose decisions shall be final and binding.

The definitions would be useful for undertaking evidence-based fiscal and policy measures in-line with reported data. In addition, SBP would be able to develop dedicated banking code to determine remittances inflow from freelancers and remote workers separately.

Rationale:

This will result in accurate tracking of remittance inflows, facilitating targeted fiscal policies and improved data-driven decision-making for the IT workforce.

1.78 EXEMPTION ON CAPITAL GAINS ON DISPOSAL OF SHARES OF START-UPS AND EXPORT ORIENTED IT COMPANIES

HIGH

Capital gain on disposal of shares of start-up companies and export-oriented IT & ITeS companies shall be exempted through the insertion of the appropriate clause in Part I of the Second Schedule while withholding tax exemption shall also be given through the insertion of the appropriate clause in Part IV of Second Schedule.
These changes would encourage corporatization and attract investors towards the IT sector. Exemption from capital gains tax encourages corporatization by making it more financially attractive for businesses to operate as corporations. Additionally, when capital gains from the sale of shares are tax-exempt, investors are more likely to invest in corporate entities profits.
Capital gains tax exemption can lead to increased investment in start-ups and innovative sectors, fostering a more dynamic, tech eco system for the country.

Rationale:

Exempting capital gains tax and withholding tax on shares of start-ups and export-oriented IT/ITeS firms will incentivize corporatization, attract investment, and stimulate growth and innovation in Pakistan's tech ecosystem.

1.79 EXEMPTION ON DIVIDEND PAID BY START-UPS AND EXPORT ORIENTED IT COMPANIES

MEDIUM

Tax on dividend paid by start-up companies and export-oriented IT & ITeS companies to their shareholders shall be exempted while withholding tax exemption shall also be given.
Tax on dividends discourages corporatization primarily due to the double taxation effect it creates Corporations are taxed on their profits, and then shareholders face additional taxes on the dividends they receive. As a result, businesses may opt to remain unincorporated or choose simpler business structures to avoid this tax burden.

Rationale:

Exempting dividends and withholding tax for start-ups and export-oriented IT & ITeS companies will eliminate double taxation, encourage corporatization, and promote growth by making corporate structures more financially attractive.

1.80 SUPER TAX CLARIFICATION FOR EXPORTERS OF IT AND IT-ENABLED SERVICES FOR THE TAX YEAR 2022

MEDIUM

There is a need for additional clarification in section 4C stating that super tax is not applicable on exporters of IT and IT-enabled services for the tax year 2022 because these exporters were eligible for a 100% tax credit under section 65F of the Income Tax Ordinance, 2001. Exporters of IT & IT enabled Services were eligible for 100% tax credit under section 65F. The same exemption can also be extended to PSEB-registered entities.

Rationale:

Clarifying the exemption of super tax for IT and IT-enabled services exporters eligible for 100% tax credit under section 65F, and extending it to PSEB-registered entities, will provide tax certainty and strengthen support for the export-oriented IT sector.

1.81 PROPOSED CHANGE IN STARTUP DEFINITION

MEDIUM

FBR should amend Section 2(62A) of the Income Tax Ordinance (ITO), 2001 to align the definition of startups with the Companies Act, 2017. Current definitions by SECP & FBR are not harmonized, keeping startups separate from tax incentives. Currently, the differences between the afore-mentioned definitions are as following.

Sr #	SECP	FBR
1.	A company that is not more than 10 years of existence	A company that commenced after 1st July 2012
2.	Turnover not greater than Rs. 500 million in any of the financial years since incorporation	Turnover of less than Rs. 100 million in each of the last five tax years
3.	Working towards the innovation, development or improvement of products or processes or services or is a scalable business model with a high potential of employment generation or wealth creation	Offer technology driven products or services to any sector of the economy provided that the person is registered with and duly certified by the Pakistan Software Export Board (PSEB)

Rationale:

There will be harmony between benefits for startups under Companies Act and Income Tax Ordinance. Reduced transaction costs for startups due to compliance with different laws and their requirements under Companies Act 2017 & ITO, 2001.

Around 200–300 additional startups annually could qualify for FBR's tax exemptions if aligned with SECP's broader definition.

1.82 REMOVE INCONSISTENCY IN THE PAYROLL TAXATION BETWEEN EMPLOYEES AND REMOTE WORKERS

It is recommended to formally define remote workers within the Income Tax Ordinance (2001). Under the proposed definition, individuals earning more than PKR 2.5 million annually through foreign remittances or serving fewer than three international clients would be classified as remote workers and taxed similarly to salaried individuals in Pakistan. This income bracket represents the top 5% of earners, and it is essential that all high-income individuals contribute fairly to the national economy. The proposed reform would broaden the tax base and enhance fiscal equity.

Introducing a clear legal classification for remote workers would provide much-needed clarity for both taxpayers and tax authorities. Given that the IT sector is heavily reliant on human capital, the current inconsistencies in labor market taxation place local companies at a competitive disadvantage. It is currently more cost-effective for international companies to hire Pakistani professionals remotely than it is for local firms to employ the same talent domestically. These disparities hinder the competitiveness of local businesses and contribute to the outflow of potential export revenue.

1.83 ENSURE CONTINUITY IN TAX POLICY FOR THE IT/ITES SECTOR

Consistency in tax policy is critical for fostering long-term growth in the IT sector, which is still in its early development stage. The industry's export potential is closely tied to the strength of the local IT market. Recent growth has been exceptional, and both foreign and domestic investors have begun to recognize the sector's promise. At a recent investment forum, over USD 700 million in agreements were signed—underscoring growing investor confidence.

To sustain this momentum, stability in tax and fiscal policies is essential. Abrupt or frequent changes—whether related to export taxation, local withholding, or other direct or indirect taxes—create uncertainty and discourage investment. Such unpredictability may force investors to reconsider their commitments, putting at risk the substantial progress achieved through joint efforts of both the public and private sectors.

The total exports of the IT sector now stand at approximately USD 4.0 billion. To reach its full potential, the industry requires the same level of support and nurturing that other countries provided to their technology sectors during formative stages. Any additional or unplanned tax burdens could undermine investor confidence and jeopardize billions in investments already made in branding, skills development, and infrastructure.

Disrupting the current tax framework could also derail broader national initiatives—such as "Tech Destination Pakistan," skill enhancement programs, and 5G infrastructure development—led by various government institutions. A stable and predictable tax environment is, therefore, not just beneficial but necessary for preserving and building on the progress made so far.

1.84 ENSURE REGULATORY SUPPORT AND END HARASSMENT OF IT COMPANIES

The international repatriation of capital must be fully digitized without delay to facilitate the inflow of investment and enable local companies to compete on a level playing field with their global counterparts. In today's economy, ease of doing business is not a luxury—it is a necessity. Streamlining financial processes and removing operational bottlenecks are critical steps in attracting both foreign and domestic investment.

Unfortunately, recent practices by various government departments—including EOBI and tax authorities at all levels—have led to undue harassment of IT companies through arbitrary closures and questionable legal notices. This hostile environment severely undermines business confidence.

The sealing or shutting down of IT businesses such as call centers, BPOs, and tech firms causes irreversible financial damage. It creates a risk perception so severe that even local companies may consider relocating operations abroad, resulting in loss of jobs, revenue, and export potential.

This pattern of harassment must end immediately. It is imperative that protections be enacted through legislation to safeguard IT businesses from such actions. Moreover, outdated labor laws and the EOBI Act must be re-evaluated in the context of the digital economy. Until such reforms are implemented, the IT sector should be granted exemptions from policies that hinder its growth and competitiveness.

INDIRECT TAXATION
KEY RECOMMENDATIONS
SALES TAX

2.01 REDUCED RATE OF SALES TAX

HIGH

Currently, Standard sales tax rate is 18% which is high thereby leading to lower level of registered person of about 210 K when compared with taxpayers for income tax of over 6.7million. Moreover, Tier 1 (subject to certain value addition) retailers engaged in the business of finished fabric, and locally manufactured finished articles of textile, textile made-ups, leather and artificial leather are allowed reduced sales tax rate of 15%, if their sales transactions are integrated with the FBR system. Unfortunately, several income taxpayers are not willing to register owing to high rate and even retailers are not interested in implementing the POS integration with FBR.

It is proposed that the Government should seriously consider taking following steps to achieve implementation of POS system by retailers:

a) consider reduction in the standard sales tax rate and reduce rate for Tier 1 Retailers; and

b) consider extending the reduced rate to all retailers.

c) The prize scheme should be restarted so that end consumer may be encouraged to buy from Tier 1 retailers.

d) Like PST & ICT, there should be reduced sales tax rate, if consumer makes payment via debit/credit cards to restaurants.

Rationale

Tier 1 retailers are significant players, and it is necessary to build their confidence in the tax system and convince them to achieve full implementation of POS system. Reporting of increased turnover due to integration will also lead to increased income tax, which can be partly offset by effects of sales tax rate reduction.

2.02 BAR CODE ON ALL NOTICES AND ORDERS – ST SECTION 56(2)

HIGH

Currently, the requisition, notices and orders are issued without system generated Bar Code, whereas this system is implemented by the FBR in case of income tax with effect from July 1, 2015, read with recent direction dated January 28, 2021, which also appears to be for Sales Tax.

Although after FTO instruction, FBR has issued instructions to field formation, however, it is proposed to insert the following proviso in section 56(2) of the STA so that every taxation officer and registered person all over Pakistan are aware of the same:

"Provided that the notice, order or requisition served as mentioned in clauses (a) to (d) above shall be valid only if the said notice, order or requisition bears system generated bar code on them duly verifiable from the FBR's database."

Rationale

Implementation of bar code system will strengthen the controls over the issue and delivery, of notices and orders.

2.03 RATIONALISATION IN TIME LIMIT FOR COMPLIANCES – SECTIONS 7, 9, 66 & 73

MEDIUM

The time period specified in various sections and rules requires rationalizations to facilitate compliances by the taxpayers.

Moreover, such powers are being used by Commissioners Inland Revenue to allow condonation to tax officers to perform tax assessment for time barred cases, which is against the spirit of these sections.

Powers of condonation should be allowed to be used rationally with specific restrictions on condonation for tax assessment of time barred cases.

It is proposed to rationalize the time period provided in the following sections:

i. Time period for claiming of input tax u/s 7 should be increased from 6 months to 1 year.

ii. Time period for filing of refund claim u/s 66 should be increased from 1 year to 2 years.

iii. Time limit of 180 days for payment of input tax u/s 73 should be either withdrawn as under STRIVE it is now allowed when the sales tax is paid by the seller; or the time limit be increased to at least 1 year.

iv. Time limit for issuing debit / credit notes u/s 9, as provided under the rules, should be increased from 180 days to 1 year.

Rationale

The implementation of this proposal will not only facilitate taxpayers but will also reduce the burden of seeking approvals for condonations and related workload of both taxpayers and tax collectors.

2.04 ADVANCE RULING FOR SALES TAX

HIGH

Currently, there is no provision in the STA which allows a person to seek advance ruling on any sales tax matter from the FBR, as it is allowed to a non-resident in case of income tax u/s 206A of the ITO.

It is proposed to insert a new section in the STA to allow a person to obtain an advance ruling on matter from the FBR.

Rationale

Advance Ruling should be able to assist local as well as foreign investors.

2.05 JOINT AND SEVERAL LIABILITY OF REGISTERED PERSONS IN SUPPLY CHAIN WHERE TAX IS UNPAID U/S 8A

HIGH

Section 8A stipulates joint responsibility of buyer and seller of goods in case all of the tax payable in respect of that supply or any previous or subsequent supply of the goods supplied would go unpaid.

Section 8A states "*Where a registered person receiving a taxable supply from another registered person is in the knowledge or has reasonable grounds to suspect that some or all of the tax payable in respect of that supply or any previous or subsequent supply of the goods supplied would go unpaid, of which the burden to prove shall be on the department, such person as well as the person making the taxable supply shall be jointly and severally liable for payment of such unpaid amount of tax*".

It is proposed to remove the text from the section, or any previous or subsequent supply of the goods supplied" as this condition has made irrational burden on bonafide buyer.

Rationale

The existing provisions makes Taxpayers responsible for the wrong doings of any party in the entire supply chain which is not justified and tantamount to give unnecessary powers to the Tax Authorities.

2.06 ADJUSTABLE INPUT TAX – SECTION 8B

LOW

Section 8B restricts the claim of input tax up to 90% of the output tax and requires mandatory payment of 10%. The relief earlier provided to Listed Public Limited Companies under Finance Act, 2021 has been withdrawn under Finance Act,2022. This requirement is now again applicable on all listed and unlisted companies.

It is proposed to delete Section 8B as a mandatory payment of at least 10% of the output tax for all listed and unlisted companies.

Rationale

Principle of 90% adjustment of input tax was introduced to encourage sales tax registered taxpayers for accurate declaration of sales and purchase transactions in sales tax returns, enabling them to claim legitimate input tax. After introduction of STRIVE System by FBR, input tax is allowed to the registered taxpayers where supplies have been declared in sales tax return and related sales tax liability has been deposited. Hence, the principle of 90% adjustment of input tax has become redundant after introduction of STRIVE System.

Furthermore, any provision deferring the claim of legitimate input tax / refunds of a registered person is not justifiable in any fiscal law as it poses serious liquidity problems for the taxpayers, especially Listed and Unlisted companies, which are more compliant than other type of the taxpayers. It will also reduce the refund piling up issue for the government.

2.07 ADJUSTMENT OF PRIOR PERIOD REFUND CLAIMS AGAINST SUBSEQUENT LIABILITIES – SECTION 10

HIGH

Section 7 of STA allows taxpayer to adjust input tax paid on purchases from their output tax liability within six months. Section 10 of STA allows taxpayer to file refund claims in case input tax paid on purchases exceeds output tax on account of zero-rated local supplies or export, while for non-zero-rated cases the Rule 34 of STR allows selected category of taxpayers to claim refunds instead of carry forward of unadjusted input tax.

Further, Section 10 of STA requires payment of refund claims within 45 days of the filing. However, practically refund claims are neither processed nor paid within the prescribed time.

It is proposed to address this issue by inserting a proviso or sub-section in Sections 7, 10 and 66 of STA to allow taxpayers to adjust refund claims against any subsequent tax liability in any of the following three situations:

(i) where the refund application is filed but the processing did not commence; or

(ii) where the application is processed and the registered person has complied with all the requirements of the Tax Department, but the refund payment order (RPO) has not been issued; or

(iii) where the RPO has been issued, but the Refund Cheque is neither received, nor credited into account of the taxpayer.

Rationale

Timely refund of sales tax has always been a painful and disturbing issue for the taxpayers from liquidity perspective and it would be a welcome move if the refunds are allowed within a reasonable time whether in cash or through adjustment against any existing or future tax liability to Government under any fiscal laws.

2.08 REFUND / INPUT TAX CREDIT NOT ALLOWED U/S 21(3)

HIGH

Under sub-section (3) of Section 21, the invoices issued by a person during the suspension of his registration shall not be entertained for claiming sales tax refund or input tax credit. Further, once such person is blacklisted, the refund or input tax credit claimed against the invoices issued by him, whether pre or post blacklisting, shall be rejected through a self-speaking appealable order and after affording an opportunity of being heard to such person.

It is proposed to rationalize the provisions of Section 21(3) to create an exception to allow input tax in the following situations:

a) where the buyer holds valid tax invoice;

b) where the supplier's name was appearing in the Active Taxpayers' List at the time when purchases were made;

c) where purchase relates to the date prior to the date of suspension and blacklisting; and

d) where the payments were made through banking channel in compliance with Section 73 of the STA.

Rationale

Refund/Input tax is only claimable by buyer once the same is deposited into the Government treasury by the supplier, therefore, there is no justification for disallowance of input tax adjustment claimed by the buyer in respect of period prior to blacklisting / suspension and that too for non-compliance of the supplier without knowledge of buyer at the time of execution of transaction. A registered person should not be deprived of his legitimate right of input tax relating to period before suspension or blacklisting of supplier if the transaction is falling in the ambit of abovementioned situations. The principle of natural justice demands that a taxpayer should not be penalized for a non-compliance of another taxpayer.

2.09 SERVICE OF ORDERS & DECISIONU/S 56 OF STA

HIGH

The Finance Act 2017 inserted clause (d) in Subsection (1) section 56 of STA whereby the service of notice and order are treated as properly served if they are served electronically through email or to the e-folder maintained for each taxpayer on IRIS.

This was not a welcome provision as the taxpayers have been finding it difficult to switch over to the changed system from the traditional service of notice as fully elaborated in these sections. Accordingly, it became a point of dispute in appeal that notices sent, or order served electronically did not reach the taxpayer mainly for the following reasons:

a) it was not practically possible for most of the taxpayers to visit e-folder every day or

b) in various cases, the email address provided belongs to senior personnel who may not regularly check their emails.

c) technical issues such as spam filters or email delivery errors further accelerated the problem, leading to instances where notices or orders were not found in inbox of the taxpayers despite, being sent electronically by the department.

Considering the above, and for the Rationale provided below, it is proposed that electronic service of notice may be declared mandatory, but until such time, the taxpayers are well conversant with the computers and developed the skills and habits to visit electronic sites regularly, the following proviso should be inserted to provide for simultaneous delivery of notices and orders as was done prior to introduction of electronic delivery.

"Provided that the service of notices, orders, etc. referred to in clause "d" shall be treated as validly served if the same has been duly served under any of the clauses "a" to "c" above.

Rationale

Most of the taxpayers may not have been using computers or have expertise to use email either due to lack of skills or absence of internet. Therefore, until taxpayers develop the necessary skills and habits to navigate electronic platforms regularly, it is imperative to maintain provisions for simultaneous delivery of notices through courier. This approach ensures equitable access to information and upholds principles of fairness and accessibility in the tax administration process.

2.10 INADMISSIBLE INPUT TAX U/S 73

HIGH

Section 73 puts a time limit of 180 days for the buyer to make the payment to the suppler, failing which the input tax of buyer becomes inadmissible. It appears to be a harsh proposition considering the fact

that related sales tax is already paid by the supplier into government treasury at the time of issuing tax invoice.

In case of receivable and payable balance from the same party, section 73 allows settlement on net payment basis, subject to approval from the Commissioner. However, seeking approval from the Commissioner for each settlement is a cumbersome exercise. It is proposed to allow constructive payment on the basis of intimation to the Commissioner only and requirement for approval should be abolished.

Rationale

The practice of offsetting receivable and payable balances with the same party is a routine aspect of business operations, and as such, it should be facilitated without necessitating explicit approval from the Commissioner. This approach has already been acknowledged in the Income Tax through Circular No. 1 of 2009, where such offsetting is permitted without any additional conditions. Recognizing this established practice in the context of sales tax regulations would not only align with industry norms but also promote consistency and coherence within tax laws. By leveraging existing precedents and facilitating seamless offsetting procedures, businesses can operate more efficiently and effectively, fostering a conducive environment for economic growth and compliance.

2.11 CONDONATION OF TIME LIMIT U/S 74 OF STA

MEDIUM

In terms of Section 74 of the STA read with notifications SRO 394(I)/2009 (as amended vide SRO 1444(I)/2024) and 395(I)/2009 respectively, the Commissioner and the Board are allowed to condone a lapse of one year and more in any compliance related issue respectively, where any timeline has been prescribed under any provision of the law.

However, e-FBR web portal does not allow automatic adjustment of purchase invoices or debit / credit notes where manual condonation has been granted by the Commissioner or the Board, as the case may be. Further, there is no procedure for e-filing of Condonation Applications. The taxpayer has to file manual applications and physically follow-up with the Tax Officers for processing.

Furthermore, there is no prescribed time limit to decide condonation applications or filing of review applications where the application is rejected by the Commissioner.

It is proposed to insert a provision within the STA to address the following:

i. Introducing a detailed mechanism for e-filing of Condonation Applications and approval may be laid down by the Board;

ii. Approval of Condonation Application, should automatically be uploaded and available on STRIVE system;

iii. Where the Condonation Application is rejected by the Commissioner, it should be subject to review by the Chief Commissioner or the Board, as the case may be; and

iv. Timeline should be provided for deciding the Condonation Application or the Review Application, failing which the Condonation or the Review Application, as the case may be, shall be deemed to have been treated as approved. The timeline provided shall exclude the additional time requested by the taxpayer to provide any additional information, explanation, or evidence required by the Commissioner, the Chief Commissioner, or the Board, as the case may be.

Rationale

The above changes are necessary to make the process efficient, prevent unreasonable delays, and ensure proper transparency and accountability of the FBR officials in attending to taxpayers' genuine issues.

2.12 EXTRA TAX ON ELECTRIC / GAS BILLS

HIGH

In terms of S.R.O. 1222(I)/2021, every electric power and gas distribution company / organization supplying electricity or gas to commercial & industrial consumers are required to charge and collect extra tax @ 17% for unregistered industrial consumers and ranging from 5%-17% for unregistered commercial consumers based on amount of bill.

It is proposed to make reasonable amendments in the SRO 1222(I)/2021 to make changes to prevent burdening the taxpayers with extra tax by the Utility companies considering the following practical issues being faced by them.

Rationale

- Majority of electricity connections / accounts are maintained in the name of a person who possesses the ownership of commercial / industrial property. Therefore, particulars of the consumers available on sales tax registration certificate / upon FBR portal do not match with the name of the account holders;
- Banks, Insurance companies, Telecommunication companies, Large Multinationals, and other similar organizations operate through numerous business locations, manufacturing premises, facilitation offices, distribution & warehouses, which, in most cases, are not in the name of such organizations. Further, sales tax registration particulars on FBR Portal do not reflect all such business places from which business operations are carried out. If the procedures envisaged in SRO are followed, extra tax would be charged and collected from registered persons in respect of all of their electric connections, which are not in the name of such registered persons;

  Furthermore, updating these particulars (e.g., business locations) on FBR database may take considerable time and Banks, Insurance companies, Telecommunication companies, and Large Multinationals that are already registered for sales tax, will have to bear extra tax on all such electricity and gas connections just because data is not updated;
- Institutions owned by Federal and Provincial governments, defense organizations, social sector institutions, and various other service providers are either not required to obtain sales tax registration numbers or are registered under the Provincial Laws. Hence, they neither possess any sales tax registration number nor are required to obtain any registration under the STA. However, most of the aforementioned organizations or institutions are commercial consumers, and, by virtue of the SRO, they are unnecessarily suffering extra tax; and
- Cottage Industry, retailers, hospitals, various agencies, diplomatic missions, privileged persons, and organizations have been specifically exempted under the Sixth Schedule to the STA and are not required to obtain registration. However, most of the aforesaid organizations or institutions are commercial consumers, and, by virtue of SRO, they are unnecessarily suffering extra tax.

2.13 ADJUSTMENT OF SALES TAX REFUNDS WITH INCOME TAX, SALES TAX & FED LIABILITY AND VICE VERSA

HIGH

It has been seen that a registered person's cash flows are tied up with the Inland Revenue in the form of sales tax refunds and, at the same time, the taxpayer is required to pay advance income tax at the time of assessment of his income tax liability. Sales tax refund processing mechanism is also cumbersome and requires extensive efforts to get it processed from the department. Tax refunds, particularly sales tax refunds, represent a significant portion of a taxpayer's cash flow.

It is proposed to introduce enabling provisions in the STA for adjustment of sales tax refunds against sales tax, FED, and income tax payable and vice versa.

It is also proposed to incorporate in the Law the existing mechanism for refund adjustment as laid down in FBR's Circular letters dated 20 December 1999 and C.No.3(6) ST-L&P/2002 dated 24 April 2007.

Rationale

These changes are necessary to prevent accumulation of refunds and address the cash flow issues

faced by the taxpayers enabling them to focus on their business operations and growth initiatives.

2.14 NON-AVAILABILITY OF INPUT TAX PAID THROUGH BILLS OF ADDITIONAL DUTY (BoAD) U/S 7(2)(ii)

LOW

The registered persons are currently unable to claim adjustment of sales tax paid through Bills of Additional Duty (BoAD) in Annexure B of the sales tax return as the same is not uploaded automatically in Annexure B of sales tax return on FBR portal; and manual entry is also not allowed in the Annexure. The BoAD is generally issued in the following situations:

- Where additional duty is paid due to difference in currency exchange rate or weight of the consignment, etc.; and
- Where the imported raw material could not be used in manufacturing items of export within the prescribed time limit provided under sales tax SRO 492 dated June 13, 2009, and customs SRO 490 dated June 18, 2001 read with EFS SRO 957 of 2021.

It is proposed to address this important issue by uploading the BoAD document on the FBR's e-filing system portal as it is done in case of duties paid through GDs.

Rationale

It is a genuine issue and its redressed is necessary to allow the taxpayers to claim sales tax which is actually paid to the customs authorities.

2.15 INPUT TAX CREDIT ON BUILDING MATERIALS – SECTION 8(1)(h)

MEDIUM

In terms of Section 8(1)(h), input tax paid on acquiring building materials is not allowed except for those used directly in the production or manufacture of taxable goods. The department generally disallows input tax paid on building materials even in cases of construction of projects assisting the taxable activity.

It is proposed to relax the restriction and allow input tax on building materials especially in case of construction of projects assisting the taxable activity.

Rationale

Removal of restriction is in line with generally accepted VAT principles worldwide and will reduce the cost of doing business and is more likely to boost the investment in projects with corresponding increase in revenue generation for the Government.

Further in case of disallowance of input tax on building materials, the registered taxpayers prefer to procure materials from unregistered persons to mitigate 18% sales tax cost with only 5% sales tax withholding resulting in loss to national exchequer as well.

2.16 SHOW CAUSE NOTICES U/S 11E OF STA

MEDIUM

It has been observed that show cause notices are invariably issued to taxpayers' u/s 11 of the STA on frivolous and intangible basis without having definite information. This leads to passing of illegal and unsustainable assessment orders.

In order to address this issue, the aforesaid sections should be amended to the effect that unless definite information of any tax evasion, illegal input tax adjustment or refund is available with the tax officer, show cause notice should not be issued. Further, term "definite information" should be defined on the suggested lines in STA:

"Definite information includes relevant substantial evidence about sales or purchases of any goods and rendering or acquiring of services on which applicable sales tax is not paid or illegal input tax adjustment orrefund has been claimed."

Order for assessment of tax based on definite information will surely help in passing of legally sustainable order, in addition to saving time of both the taxpayers and tax collectors.

2.17 DISCHARGE OF LIABILITY AT SUBSEQUENT STAGE – SECTION 11F

LOW

The Sales Tax law requires certain taxpayers to withhold certain amount of sales tax from the recipient and deposit the same to the credit of the recipient. In case of default, the tax authorities can recover the amount of sales tax not withheld from the withholding agent.

Based on the judgements of the Superior Courts, it is now a settled principle of law that if any liability for tax is not deducted but is subsequently discharged by the person from whom tax was deductible, then the same cannot be recovered from the taxpayer again, as it would be tantamount to double taxation. However, such a provision is not part of section 11F of the STA.

It is proposed to insert a proviso in Section 11 as follows:

"Provided that, at the time of recovery of tax under sub-section (4A) it is established that the tax that was to be deducted from the payment made to another person has meanwhile been paid by that person, no recovery shall be made from the person who had failed to deduct the tax but the said person shall be liable to pay default surcharge as per section 34 of the Act from the date he failed to deduct the tax to the date the tax was paid."

Provided further that the default surcharge, for delay in payment of sales tax, will be recoverable from the person who has failed to pay or deduct or deducted but not deposit the sales tax."

Rationale

The proposed amendment is similar to Section 161 (1B) of the ITO.

2.18 CERTIFICATE BY AUDITORS – SECTION 22

MEDIUM

As per sub-section 4 of section 22, registered persons whose accounts are subject to audit under the Companies Ordinance, 1984 (XLVII of 1984) shall be required to submit a copy of annual audited accounts along with a special certificate by the auditors certifying the payment of tax due has been discharged by the registered person.

It is proposed to either delete the requirement of submitting a special certificate by the auditors or it may be modified to provide for issue of a certificate in consultation with ICAP.

Rationale

Issue of a certificate in the manner requested under the STA is not within the mandate of auditors' role as external auditors under the Companies Act, 2017.

2.19 MULTIPLE AUDITS – U/S 25, 38 AND 72B

HIGH

Section 25 and Section 38 empower the tax authorities to conduct sales tax Audit / Investigation. Section 72B empowers the Board to select persons or classes of persons for audit of tax affairs through computer ballot. Section 38 empowers the tax department to conduct investigation of registered persons without any time limitation and allied framework.

Each year companies are served notices, requiring producing large volume of data and reconciliations, which is against the concept of universal self-assessment. Thereby, companies incur huge administrative, tax consultants and legal costs for every audited year.

It is proposed that no audit should be initiated unless specific scope, guidelines and mechanism of Investigation is available in the law to bring clarity vis-à-vis risk-based sample driven audit. Likewise, if detailed investigation of a registered person has already been conducted u/s 38, there should be no need to conduct audit u/s 25 and u/s 72B or assessments u/s 11D, 11E and 11F of that person again in order to save taxpayers from double jeopardy. The previous limitation of conducting tax audit once in three years should be restored.

Alternatively, Section 38 be amended to include time limitation of six years, in line with record keeping requirements in Section 24 of STA.

Rationale

Multiple audits and assessments of sales tax record of the same tax period without any incontrovertible evidence of tax fraud or wrongdoing are a burdensome and unproductive exercise both for the taxpayers and tax collectors.

2.20 POWER TO ARREST U/S 37A

MEDIUM

Presently, Inland Revenue Officers are authorized to execute arrest of any person if that officer on the basis of material evidence has reason to believe that such person has committed a tax fraud or any offence warranting prosecution under STA. Moreover, the powers given to officers also include powers to arrest any director of the company if the officer has reasons to believe that such director or officer is personally responsible for actions of the company contributing to tax fraud.

It is proposed that this Section should only be applicable where the tax fraud has already been established at independent appellate forum. Alternatively, the amendment to be made in Section 37A in line with the amendment made in Section 8A through Finance Act 2015 and the burden to prove the allegations should be on the tax department.

Rationale

Such an open-ended power could lead to harassment of genuine taxpayer.

2.21 POSTING OF INLAND REVENUE OFFICER TO PREMISES OF REGISTERED PERSON SECTION 40B

MEDIUM

Section 40B authorizes the FBR to post officer of Inland Revenue to the premises of registered person or class of such persons, to monitor production, sales of taxable goods and the stocks position.

There is a general perception that this provision leads to misuse of power or authority and undue harassment by the tax authorities and is voiced as a main concern of various trade bodies.

It is proposed to prescribe a detailed and transparent mechanism for compliance by the Officer before exercising such power.

Rationale

Such an open-ended power could lead to the harassment of the genuine taxpayers if they are applied without following a well-documented procedure and defining the time limit / number of days of posting of Inland Revenue Officer should also be mentioned in this section which should correspond to the production or volume of sales.

2.22 LIABILITY FOR PAYMENT OF TAX U/S 58

MEDIUM

Where any private company is wound up, then following persons are jointly and severally liable for payment of outstanding tax:

i. Director

ii. Shareholder, owning not less than ten per cent of the paid-up capital.

This section neither defines director nor provides the extent to which the outstanding liability could be recovered from the directors and shareholders. For instance, under the Companies Act, 2017, director could be a nominee director or independent director or an employee director with or without shares. Similarly, whether it would be justified to recover tax exceeding the percentage of shareholding of the shareholders.

It is proposed to insert the following further provisions in this section:

i. Define director as "Director to exclude employee director, nominee director and independent director";

ii. The shareholders and directors cum shareholders owning not less than ten per cent of the paid-up capital shall be liable to payment of outstanding tax not exceeding the percentage of their holding in the company.

Rationale

It is not just and equitable to make recoveries from employee director, nominee director and independent director. Moreover, recoveries of outstanding tax from those shareholders who own more than 10% of the paid-up capital to the extent of their ownership in the company may be reasonable (in line with section 139 of ITO).

2.23 BUSINESS BANK ACCOUNTS U/S 73 & STR-1

HIGH

Section 73(1) require that the payment against invoice should be made directly from the bank account of buyer to bank account of supplier.

In the era of technology, many online marketplaces and payment gateways are conducting transactions on behalf of supplier, and they collect money on behalf of the supplier and thereafter transfer the same to supplier. Therefore, when buyer make payment to online marketplace, the input tax claim will not be available to buyer due to non-transfer in supplier account.

It is proposed insert following proviso in section 73(1):

> *"Provided that if the buyer purchased goods through online marketplace and made directly in account of online marketplace and / or payment gateways on behalf of supplier, it shall be treated as the buyer has made payment directly in the bank account of supplier.*

Further, Explanation to Section 73 of STA defines 'Business Bank Account' to mean a bank account utilized by registered person declared to Commissioner through Form STR-1 or change in particulars in registration database.

Currently, the Form STR-1 (taxpayer registration form) does not exist online as the e-FBR website portal automatically re-directs to IRIS web portal (used for filing of Income Tax and sales tax returns). Thus, the change in particulars application is submitted on IRIS portal via "181 (Form of Registration filed for modification -Income Tax)". This Form is not covered under the Sales Tax Act.

Owing to non-availability of Form STR-1 on e-FBR portal, reference to Form STR-1 in Section 73 should be replaced with Form "181 (Form of Registration)" which, at present, is applicable to Income Tax (pursuant to Section 181 of ITO). Moreover, title of said Form be changed to "181-73 - Form of Registration / Modification (Income Tax, Sales Tax and FED)".

Rationale

Many technology businesses are facing difficulty as most of the buyers are reluctant in making payment to online marketplace and / or payment gateways due to disallowance of input tax.

It is a glitch to be addressed for the taxpayer's facing difficulty in adding business bank account or a change in business bank account.

2.24 INVENTORY RECORD FOR GOODS DESTROYED – RULE 23

LOW

Rule 23 of the STR requires that when goods are returned by the buyer being unfit for consumption, the same is required to be destroyed by the supplier after obtaining permission from the Collector of Sales Tax having jurisdiction. Practically speaking, the tax department may not have the capacity and human resource having specialized skills required to decide the application for approval for destruction.

It is proposed to amend the rule to provide for engaging independent verifier (to be appointed by the Collector) to work with the tax team to physically inspect the goods and carry out other procedures to decide the application and arrange the destruction of such goods under the supervision of the representatives from the tax department, taxpayer, and independent verifier. The rule should also prescribe the qualification of "independent verifier".

Rationale

Implementation of the above proposal would certainly ease out the process of approval and destruction of goods unfit for consumption.

2.25 INITIATION OF RECOVERY ACTION - RULE 71

HIGH

i. Rule 71 of STR require that on expiry of 30 days from the date on which the Government dues are adjudged, the referring authority shall deduct the amount from any money owing to the person from whom such amount is recoverable, and which may be at the disposal or in the control of such officer.

Rule 201B of the Income Tax Rules requires that prior approval of the Chief Commissioner shall be obtained who shall satisfy himself as to the service of order and that no refund due to the defaulter is available for adjustment against the tax demand. He shall also satisfy himself that no application for rectification or appeal effect which is likely to result in creation of refund is pending hearing before the Commissioner.

It has been noted that Sales Tax Orders passed by taxation officers generally contain factual inaccuracies leading to determination of incorrect Tax Demand on which taxpayers apply for rectifications. However, Taxation Officers proceed to initiate recovery proceedings, without passing self-speaking Order on the rectification applications.

It is proposed to amend Sales Tax to add similar provision (in line with relief already available under Income Tax Rules 201B)

ii. Rule 71 of STR provides that the proceedings for recovery of tax demand may be initiated after 30 days from the date on which the Government dues are adjudged (date of order). The date of order is generally misinterpreted as the date mentioned on the order, whereas legally an order is treated as order on the date it is served on the taxpayer.

It is proposed to amend the rule to substitute the words "date on which the Government dues are adjudged" with the words "date of service of the order".

Rationale

Prevent unnecessary litigation and hassle to taxpayer and taxation officer. Prevent misinterpretation and harmonize it with Section 45B of the STA.

2.26 UNDUE RESTRICTIONS OVER EXPORTS TO AFGHANISTAN

MEDIUM

As per SRO 190 dated April 2, 2002 (read with SRO dated February 14, 2012 and SRO 691 dated June 29, 2019), zero rating on Exports u/s 4 of the STA is not applicable in respect of supply of certain categories of goods, exported by air or via land route to Afghanistan and through Afghanistan to Central Asian Republics. Categories of goods specified in SRO 190 (as amended) have been reproduced below for ready reference:

i. items other than PVC and PMC materials (PCT Code 39.01 to 39.14) as are manufactured in the Export Processing Zones or in manufacturing bonds;

ii. exported, other than against irrevocable letters of credit, or advance payment, in convertible foreign currency;

iii. exported without fulfilling the conditions prescribed in paragraphs 8, 12B, entry 9 of the Schedule I and Schedule IV to the Export Policy and Procedure Order, 2000; and

iv. specified in the list below, namely: -

(a) cigar, cheroots, cigarillos, and cigarettes of tobacco or of tobacco substitutes;

(b) dyes and chemicals;

(c) yarn all types;

(d) polyester metalized film;

(e) ball bearings;

(f) vegetable ghee and cooking oil (if exported from Export Processing Zones or manufacturing bonds); and

(g) all petroleum products whether imported or produced locally (unless there is a Government-to-Government contract done through oil marketing companies only). Unquote

Similar restrictions on exports to Afghanistan and through Afghanistan to Central Asian Republic as specified in clause (a), (b) and (d) above are also part of the Export Policy Order, 2016 issued vide SRO 344 dated April 18, 2016.

It is proposed to revisit and relax the restrictions on zero rating facility on all items, as per SRO 190 dated April 2, 2002, and SRO 344 dated April 18, 2016, in order to increase overall exports and to prevent other countries like India to capture the market in Afghanistan. The following restrictions may be considered:

- restriction on exports via manufacturing bond be removed and only conditions relating to exports against irrevocable letters of credit, or advance payment, in convertible foreign currency should remain intact owing to the fact that goods manufactured through the manufacturing bond facility are subject to strict scrutiny of the Customs authority;
- for export, other than through manufacturing bond, of goods specified in clause "(d)" of SRO 190 as well as items specified in Schedule III of the Exports Policy Order, 2016, exporters should be made liable to comply with the following conditions:
  i. export transactions must be executed against irrevocable letters of credit, or advance payment, in convertible foreign currency;
  ii. zero rating be allowed only in case of exports by manufacturers from Pakistan to manufacturers in Afghanistan;
  iii. where the proof that goods exported have reached Afghanistan has been verified on the basis of a copy of import clearance documents by Afghan Customs Authorities; and
  iv. exports should only be routed through authorized export land routes i.e., Torkham, Chaman, Ghulam Khan and Qamar Uddin Karez (when it becomes operational).

Rationale

We understand that goods manufactured in manufacturing bonds are subject to strict scrutiny by the Customs authorities from import until the final exports stage in accordance with the procedure given in Customs SRO 450 dated June 18, 2001. Therefore, goods manufactured in the manufacturing bonds are less prone to be used for unscrupulous activities.

We also understand that restrictions under SRO 190 and SRO 344 were imposed to prevent misuse of zero-rating benefits by traders by exporting goods to Afghanistan and thereafter re-importing the same via unlawful means. We believe that a blanket restriction, on all goods manufactured in the manufacturing bond as well as on specific items, instead of bringing the desired results, has dented our Exports market, and has also helped the other countries like India, to increase their exports to Afghanistan, which otherwise would have been supplied from Pakistan.

These suggestions, if implemented in true spirit, will not only increase the overall Exports and Foreign Exchange reserves but will also encourage documented sectors thereby resulting in a major barrier for operations of undocumented sector.

2.27 SALES TAX WITHHOLDING – ELEVENTH SCHEDULE

MEDIUM

Sales Tax is to be withheld at the time of payment to unregistered person and inactive registered person without any threshold.

In most of the cases, withholding tax from unregistered persons is being shown in bulk in the return. It is proposed to require the registered persons to identify the person from whom sales tax is withheld while depositing the sales tax withholding so that the same could be used for broadening of the tax base.

Until June 2019, 1% Sales Tax was to be withheld on payment to unregistered person however said rate was increased to 5% vide Finance Act 2019 and now, Sales Tax withholding agents are required to deduct Sales Tax @ 5% of gross value of supplies from persons other than Active taxpayers. The rate of 5% is additional burden on registered taxpayers as unregistered suppliers include said impact in their Selling Prices and thus this needs to be rationalized. Further lower withholding rates be prescribed for withholding agents who declare registration number of unregistered supplier.

Since essence of withholding regime is to be broadening of tax base thus it is proposed that Rate of Sales Tax withholding be brought down from existing 5% to 1% for those suppliers who provide CNIC to the buyer and buyers declare CNIC of the supplier in monthly sales tax return (and does not declare the same as bulk unregistered sales).

Rule 150ZZI (2) of STR requires that sales tax is to be withheld at the time of payment. However, Rule 150ZZI (5) inadvertently requires deposit of sales tax withheld by 15th of the month following the month during which the purchase has been made.

It is proposed that sub-Rule (5) be amended in line with sub-Rule (2) to bring consistency.

Records of CNIC and business name of unregistered or inactive suppliers with FBR (as supplied by several registered person) will enable it to identify potential taxpayers and take focused measures to bring them into the tax net.

Rationale

It will also support ease of doing business, particularly in small transactions, especially when sales to unregistered person.

Moreover, enabling FBR to broaden the tax base on unregistered economic activity.

2.28 ANNEXURE H - FASTER SYSTEM FOR SALES TAX REFUND PROCESSING

LOW

From July 1, 2019, FBR has implemented systems for expeditious processing of sales tax refunds, for which taxpayers are required to file Annexure H of the sales tax return. However, the registered persons have been facing following challenges in filing of Annexure H:

- For the first time, Annexure H can only be filed if there is no brought forward sales tax input balance appearing in the sales tax return. In case, sales tax brought forward balance [carried forward from prior months] is appearing in sales tax return portal and Annexure H was not submitted in prior months, registered exporter will not be able to file Annexure H from now onwards. In case a person has not claimed sales tax refund in prior periods but wants to file refund claim from now onwards, he should be given an option to file Annexure H [while carrying forward earlier months' balance];
- In case any taxpayer does not want to carry out cumbersome exercise of filing Annexure H on a monthly basis, then such taxpayers should also be given an option to file Annexure H on an annual basis covering the data from July to June each year; and
- Taxpayers dealing in exports as well as local supplies are usually required to pay minimum sales tax @ 10% u/s 8B of the Sales Tax Act unless export value is 50% or more of the total sales. However, Annexure H does not provide any option to incorporate / fit in carry forward balance relating to amount paid u/s 8B. This issue should properly be addressed.

Rationale

Unless the above shortcomings are addressed the objective of faster processing of sales tax refund cannot be achieved.

2.29 IMPROVEMENTS / AMENDMENTS IN SALES TAX RETURN

During January to May 2025, Affidavit & several new annexures have been introduced in the sales tax return, significantly increasing the complexity of compliance. While the objective is to enhance transparency and documentation, the frequent and uncoordinated changes have created practical challenges for taxpayers and consultants.

It is proposed that any further improvements or amendments in the sales tax return filing process be implemented in a phased manner, after proper stakeholder consultation and awareness campaigns.

Moreover, qualified accountant cum tax specialist be involved to design in the design and development of such changes to ensure technical accuracy and alignment with practical reporting requirements.

Rationale:

A gradual and consultative rollout will allow taxpayers and the IRIS system to adjust effectively, reduce the compliance burden, and improve the accuracy and coverage of tax filings. Inclusion of accounting professionals cum tax professionals in the development process will ensure the changes are technically sound and practically implementable.

2.30 RESTRORATION OF ZERO-RATING ON LOCAL SUPPLIES UNDER EFS

Through the Finance Act 2024, the Federal Government has omitted the following Serial Number 21 of Fifth Schedule to the Sales Tax Act, 1990 whereby zero-rating facility on local supplies under Export Facilitation Scheme [EFS] has been done away with:
"Local supplies of commodities, raw materials, components, parts and plant and machinery to registered exporters authorized under Export Facilitation Scheme, 2021 notified by the Board with such conditions, limitations and restrictions as specified therein."
Consequently, local supplies to exporters are chargeable to sales tax at the rate of 18% whereas there is an exemption from sales tax at import stage due to corresponding entry in the Sixth Schedule of the Sales Tax Act 1990.

Removal of zero-rating sales tax has a disadvantage to domestic manufacturers of intermediate inputs, as exporters who can import without sales tax would prefer to import it instead of buying it locally, paying sales tax and wait for sales tax refunds thereon. It is strongly recommended to restore the zero-rating facility for local supplies under EFS to promote local manufacturing and exports which will help to reduce the imports.

Moreover, EFS related Customs Rule 880 (1) specify Exports to acquire input goods without payment of customs duty, Federal excise duty, sales tax, or withholding tax except (a) procurement of local input goods shall be allowed on payment of leviable sales tax (b) duty and taxes paid goods from the domestic market against sales tax invoice. This leads to sale tax payment for indirect Exporter and then claim refund by Direct Exporter OR Direct Export prefer to Import directly or buy Locally from Commercial Importer. Hence, Local supply by Indirect exporter be Zero rated

Rationale

Ease of doing Business by avoid cash flow issue for Exporter, save Department refund processing hassle and save foreign exchange.

2.31 ABOLISH SALES TAX ON SUPPLY OF CAPITAL GOODS TO EXPORT PROCESSING ZONES [EPZ]

MEDIUM

Through Finance Act 2022, clause 6A of 5th Schedule has been deleted whereby sales tax zero rating on supply of capital goods to persons in EPZ has been abolished and consequently, such supply has been subjected to sales tax @ 18%. On the other hand, as per the customs law, supply to EPZ is still considered as exports and is subject to zero rating of sales tax. It is proposed to be reintroduced zero rating.

Rationale

EPZs are zones dedicated only for exports. Considering that exports are zero rated, therefore, levy of sales tax on capital goods meant for use in exports will unnecessarily hurt exports and will create bottlenecks in investments for export promotion and jobs generation.

2.32 AVOIDANCE OF INVESTMENT TAXATION NOT GENERATING PERMANENT REVENUE

With the omission of Serial Nos 149 & 150 of the Sixth Schedule by the Finance (Supplementary) Act, 2022, Import of Plant and Machinery has been subjected to sales tax at the rate of 18% and 3% Minimum Value Addition Tax (MVAT) [except imported for setting up of a Special Economic Zone (SEZ) by zone developers and for installation in that zone by zone enterprises, on one-time basis and for assembly/ manufacturing of electric vehicles]. Moreover, MVAT is being collected at import stage on import of plant and machinery [except chapter 84 and 85]. Sales tax as well as MVAT on import of the Plant & Machinery for Green Field and SEZ base project as well as existing industries be exempted.

Rationale

Although the sales tax collected on import of Plant & Machinery is adjustable, even though it utilizes significant cash flows owing to huge investment. Further, the concept of MVAT is principally applicable for any item imported by commercial importers for subsequent sales in same condition and therefore, the said levy of 3% should not be applied to manufacturers. Both the exemptions will promote investment, ease of doing business and create jobs.

2.33 DOUBLE TAXATION OF SOFTWARES AS GOODS AND SERVICES

The double taxation issue arises because federal authorities treat software as goods subject to sales tax, while provincial authorities treat it as a service, also subject to sales tax,

To address this, a proposed modification in the Sixth Schedule of the Sales Tax Act 1990, specifically Table 1, serial #41, may be made as following.

41	Computer software in any form whether supplied or installed online, through a hard drive, cloud or any other medium	Respective headings

Rationale

This modification would resolve the issue of double taxation by harmonizing federal and provincial tax approaches, ensuring software is not taxed both as a good and a service.

INDIRECT TAXATION
KEY RECOMMENDATIONS
FEDERAL EXISE DUTY

3.01 ADVANCE RULING FOR FEDERAL EXCISE

HIGH

Currently, there is no provision in the FEA which allows a person to seek advance ruling on any federal excise matter from the FBR, as it is allowed to a non-resident in case of income tax u/s 206A of the ITO.

It is proposed to insert a new section in the FEA to allow a person to obtain an advance ruling on matter from the FBR.

Rationale

Advance Ruling should be able to assist local as well as foreign investors.

3.02 ADJUSTMENT OF SALES TAX AND FED REFUNDS WITH INCOME TAX, SALES TAX & FED LIABILITY AND VICE VERSA

HIGH

It has been seen that a registered person's cash flows are tied up with the Inland Revenue in the form of sales tax and FED refunds and, at the same time, the taxpayer is required to pay income tax at the time of assessment of his income tax liability. Tax refunds, particularly sales tax and FED refunds, represent a significant portion of a taxpayer's cash flow.

It is proposed to introduce enabling provisions in the FEA for adjustment of sales tax and FED refunds against sales tax, FED, and income tax payable and vice versa.

It is also proposed to incorporate in the Law the existing mechanism for refund adjustment as laid down in FBR's Circular letters dated 20 December 1999 and C.No.3(6) ST-L&P/2002 dated 24 April 2007.

Rationale

These changes are necessary to prevent accumulation of refunds and address the cash flow issues faced by the taxpayers enabling them to focus on their business operations and growth initiatives.

3.03 FED ON FRANCHISE SERVICES

LOW

Adjustment of sales tax levied whether under Federal sales tax law or Provincial laws suffered by a taxpayer on acquiring goods or services is not available against specified dutiable goods and services on which FED is not collected in the sales tax mode.

It is proposed that franchise services should be subject to FED in the Sales Tax mode so that same can be claimed as Input Tax.

Alternatively, considering that franchise is also subject to sales tax in provinces, it is proposed to delete franchise services from FEA and shift it to ICT (Tax on Services) Ordinance, 2001 along with the revised definition of franchise as proposed above.

Rationale

The implementation of the proposal would put to rest ongoing tax controversies.

3.04 ADJUSTMENT OF EXCISE DUTY U/S 6 AND RULE 13

HIGH

Currently, Federal Excise Duty (FED) on purchases is adjustable on payment basis rather than on accrual basis. Moreover, there is also a condition for adjustment that sales proceeds of goods including related FED are received through banking channels.

Section 6 read with Rule 13 specifically mention that the adjustment of duty of excise is allowable, only if it is paid on purchase of dutiable goods, which are used directly in manufacture or production of dutiable goods only.

This means that FED paid on acquisition of dutiable services may not be adjusted against supply of dutiable goods and further no adjustment of duty whether paid on dutiable goods or services is at all available against rendering of dutiable services.

It is proposed to make the following changes:

i. Adjustment of FED should be allowed on accrual basis i.e., in the month in which purchase is made, in the same manner as it is allowed under the STA; and

ii. Cross adjustment of FED on acquisition of dutiable goods or services should be available for adjustment against both dutiable goods and services charged or levied by registered person on supply, or rendering, of such goods or services.

Rationale

The proposed changes are necessary for addressing the cash flow problem and the cost of doing business for the registered person. By aligning FED adjustment provisions with those of the STA and allowing for cross-adjustment between goods and services, businesses can better manage their tax obligations and operational costs.

3.05 CONDONATION OF TIME LIMIT U/S 43 OF FEA

MEDIUM

In terms of Section 43 of FEA read with notifications SRO 394(I)/2009 (as amended vide SRO 1444(I)/2024) and 395(I)/2009 respectively, the Commissioner and the Board are allowed to condone a lapse of one year and more in any compliance related issue respectively, where any timeline has been prescribed under any provision of the law.

However, e-FBR web portal does not allow automatic adjustment of purchase invoices or debit / credit notes where manual condonation has been granted by the Commissioner or the Board, as the case may be. Further, there is no procedure for e-filing of Condonation Applications. The taxpayer has to file manual applications and physically follow-up with the Tax Officers for processing.

Furthermore, there is no prescribed time limit to decide condonation applications or filing of review applications where the application is rejected by the Commissioner.

It is proposed to insert a provision within the FEA to address the following:

i. Introducing a detailed mechanism for e-filing of Condonation Applications and approval may be laid down by the Board;

ii. Approval of Condonation Application, should automatically be uploaded and available on STRIVE system;

iii. Where the Condonation Application is rejected by the Commissioner, it should be subject to review by the Chief Commissioner or the Board, as the case may be; and

iv. Timeline should be provided for deciding the Condonation Application or the Review Application, failing which the Condonation or the Review Application, as the case may be, shall be deemed to have been treated as approved. The timeline provided shall exclude the additional time requested by the taxpayer to provide any additional information, explanation, or evidence required by the Commissioner, the Chief Commissioner, or the Board, as the case may be.

Rationale

The above changes are necessary to make the process efficient, prevent unreasonable delays, and ensure proper transparency and accountability of the FBR officials in attending to taxpayers' genuine issues.

3.06 BAR CODE ON ALL NOTICES AND ORDERS –FED 47(2)

HIGH

Currently, the requisition, notices and orders are issued without system generated Bar Code, whereas this system is implemented by the FBR in case of income tax with effect from July 1, 2015, read with recent direction dated January 28, 2021, which also appears to be for FED.

Although after FTO instruction, FBR has issued instructions to field formation, however, it is proposed to insert the following proviso in 47(2) of the FEA so that every taxation officer and registered person all over Pakistan are aware of the same:

"Provided that the notice, order or requisition served as mentioned in clauses (a) to (d) above shall be valid only if the said notice, order or requisition bears system generated bar code on them duly verifiable from the FBR's database."

Rationale

Implementation of bar code system will strengthen the controls over the issue and delivery, of notices and orders.

3.07 SERVICE OF ORDERS & DECISION U/S 47 OF FEA

HIGH

The Finance Act 2017 inserted clause (d) in sub-section (2) of Section 47 of FEA, whereby the service of notice and order are treated as properly served if they are served electronically through email or to the e-folder maintained for each taxpayer on IRIS.

This was not a welcome provision as the taxpayers have been finding it difficult to switch over to the changed system from the traditional service of notice as fully elaborated in these sections. Accordingly, it became a point of dispute in appeal that notices sent, or order served electronically did not reach the taxpayer mainly for the following reasons:

a) it was not practically possible for most of the taxpayers to visit e-folder every day or

b) in various cases, the email address provided belongs to senior personnel who may not regularly check their emails.

c) Technical issues such as spam filters or email delivery errors further accelerated the problem, leading to instances where notices or orders were not found in inbox of the taxpayers despite, being sent electronically by the department.

Considering the above, and for the Rationale provided below, it is proposed that electronic service of notice may be declared mandatory, but until such time, the taxpayers are well conversant with the computers and developed the skills and habits to visit electronic sites regularly, the following proviso should be inserted to provide for simultaneous delivery of notices and orders as was done prior to introduction of electronic delivery.

"Provided that the service of notices, orders, etc. referred to in clause "d" shall be treated as validly served if the same has been duly served under any of the clauses "a" to "c" above.

Rationale

Most of the taxpayers may not have been using computers or have expertise to use email either due to lack of skills or absence of internet. Therefore, until taxpayers develop the necessary skills and habits to navigate electronic platforms regularly, it is imperative to maintain provisions for simultaneous delivery of notices through courier. This approach ensures equitable access to information and upholds principles of fairness and accessibility in the tax administration process.

3.08 DEBIT AND CREDIT NOTES - RULE 14 A OF FEA

LOW

Rule 14A allows issuance of debit or credit notes for dutiable goods and making corresponding adjustment in return where the amount mentioned in the tax invoice needs to be modified. However, said facility has not been extended to dutiable services.

It is proposed to amend the rule to extend the application of Rule 14A to excisable services.

Rationale

Proposed amendment would facilitate the taxpayer for issuance of debit / credit notes relating to FED on services.

3.09 INITIATION OF RECOVERY ACTION - RULE 60

MEDIUM

Rule 60 of FER require that on expiry of 30 days from the date on which the Government dues are adjudged, the referring authority shall deduct the amount from any money owing to the person from whom such amount is recoverable, and which may be at the disposal or in the control of such officer.

Rule 201B of the Income Tax Rules requires that prior approval of the Chief Commissioner shall be obtained who shall satisfy himself as to the service of order and that no refund due to the defaulter is available for adjustment against the tax demand. He shall also satisfy himself that no application for rectification or appeal effect which is likely to result in creation of refund is pending hearing before the Commissioner.

It has been noted that Federal Excise Orders passed by taxation officers generally contain factual inaccuracies leading to determination of incorrect Tax Demand on which taxpayers apply for rectifications. However, Taxation Officers proceed to initiate recovery proceedings, without passing self-speaking Order on the rectification applications.

It is proposed to amend Federal Excise Rules to add similar provision (in line with relief already available under Income Tax Rules 201B)

Rationale

Prevent unnecessary litigation and hassle to taxpayer and taxation officer. Prevent misinterpretation and harmonize it with Section 45B of the STA.

INDIRECT TAXATION
KEY RECOMMENDATIONS
CUSTOM

4.01 AFGHAN TRANSIT TRADE

MEDIUM

Smuggling through Afghan Transit Trade has always been the biggest threat for economic growth and this menace has affected all sectors of the economy. Smuggled goods through the borders of Iran, China, India, and the Afghan Transit Trade form a chunk of the informal economy which is costing the national exchequer in billions.

Markets across the country are flooded with smuggled goods and local industries are struggling for survival as smuggled goods are not only easily available everywhere but are also attracting the buyers who prefer foreign merchandise.

In order to allow industry to fairly compete with unscrupulous imports and Government to benefit from increased revenue, it is proposed to implement the following protocols:

i. Scanners be installed at Pak Afghan Borders at Turkham and Chaman as it is presently working at Port Qasim (ICG3) Karachi for USA exports, in order to check/verify contents of each and every container to cross verify that the same have been delivered to Afghan Border without its misuse. The scanning machines and its tracking/integration should be initiated right from import gate to Pak border to Afghanistan border;

ii. Scanning image of import should be compared with the scanning image of goods delivered to Afghan border, until then entry should remain open for scrutiny;

iii. Afghan importers should also file the entry in the WeBOC system of Afghanistan (which Pakistan is helping to develop) and then Pakistan should have access to the Afghan WeBOC system to mark the cleared container green in the Afghan WeBOC. The containers not yet cleared; or in transit; or if not cleared after 7 days of being released from Pakistan port, should be marked red (for the risk of being misused);

iv. Pakistan Customs should collect duties on behalf of Afghan government at the time of entry via Pak port and the said amount be handed over to Afghan government once the said consignment is cleared / entered into Afghanistan;

v. Pakistan government should collect 18% sales tax as "commitment fee for safe transit into Afghanistan" on all imports under ATT citing past data of rise in ATT on high tariff items and the same amount should then be refunded on clearance of goods into Afghanistan, just as it is done with our exporters; and

vi. Income Tax / Sales Tax registration number of Importer under ATT should be submitted in the Afghan transit trade entry filed in port of import at Karachi and the same should be verified online with Afghanistan's tax registration system. Data base of imports value per year under each registration number be maintained. Moreover, importer should be made liable to submit copy of Afghan sales tax return with Pak customs at end of the year to monitor that such importer is declaring these imports in his Afghan import in order to enable him to qualify for next year under ATT. In order to circumvent this, traders may close old company and form a new company but then Pakistan will have a data base of how many companies did that. Incase Afghan Government says that Income Tax / Sales Tax registration number is not allotted to importers then they should be allowed specified timelines to create such system and allot registration number.

Rationale

Improved protocol for Afghan transit trade is necessary to curb smuggling, illegal trade, and fake imports & exports.

6.02 CPEC AND THE MENACE OF SMUGGLING / ILLEGAL TRADE

MEDIUM

China Pakistan Economic Corridor (CPEC) is a journey towards economic regionalization in the globalized world. This will deepen and broaden economic links between Pakistan and China and will surely leave a positive impact on other countries in the region. However, this also carries the risk similar to Afghan Transit Trade.

The success of CPEC is directly proportional to three factors vis-a-vis. (a) security arrangements, (b) infrastructural development and (c) smooth e-based Customs operations. Whereas a number of initiatives are being taken and also proposed to be taken, on two fronts vis-a-vis. security and infrastructure, but Customs operations, have hitherto been given little attention. In order to ensure that the foreign trade conducted through CPEC is free from menace of smuggling or illegal trade, it is proposed to take the following steps:

- Scanners be installed at Pak China Borders and at Gwadar / Karachi Port in order to check / verify contents of each and every container to cross verify that the same have been exported / imported without its misuse;
- Scanning image of exports from China border should be compared with scanning image of goods delivered from Gwadar / Karachi port and vice versa for imports until then entry should remain open for scrutiny;
- Chinese exporters / importers should also file the entry in the WeBOC system of China, and Pakistan should have access to the China WeBOC system to mark the cleared container green in the WeBOC. Entry to remain open until the same is verified by actual export / import routed through Gwadar / Karachi. The containers not yet cleared; or in transit; or if not cleared after 7 days of being released from Pakistan port; should be marked red (for the risk of being misused). In such cases, show cause notices be sent to exporters / importers, as the case may be, for further inquiry;
- In case of exports, goods should only be allowed in containers loaded in China and evidence of shipping line booking and Bill of Lading be obtained as proper evidence; and
- There should also be a set up for custom offices after every 200 km intervals along the routes of CPEC to ensure effective monitoring of transit trade flows;

In order to ensure swift and smooth monitoring, e-tagging should be installed on vehicles carrying cargo, some further measures are:

- When a vehicle crosses the designated customs office at the pre-marked route, the data of cargo movement should automatically enter the system showing location and brief description of goods, etc.;
- The online movement of the cargo should be viewed by both customs offices at port of entry and exit. The containers carrying cargo be sealed and de-sealed by customs at entry and exit points respectively. This will ensure safety of the cargo and avoiding en-route pilferage;
- Both Governments must agree to strengthen customs controls at the border and to establish "Electronic Data Interchange" (EDI) linkage between Pakistan and China on "Real Time Basis" to ensure reconciliation of export/ import data of cargo routed through CPEC route; and
- In case of imports, evidence of payment of goods by Chinese importer to their suppliers and submission of bank guarantee equivalent to government levies to be collected on China imports by Pakistan Customs before release.

Transit cargo will be transported from and to China, which needs Customs facilitation as well as

monitoring both en-route and entry/exit stations to avoid menace like presently being faced in case of Afghan Transit Trade.

CPEC also envisages establishment of export processing zones, special economic zones, and free zones. This requires Customs facilitation to ensure swift clearances of goods without any pilferages. More importantly, the duty/tax free goods will be transported across Pakistan, which needs en-route monitoring so that the same are not pilfered, jeopardizing the very essence of CPEC. Moreover, any smuggling/pilferage of Chinese goods en-route will have direct and serious repercussions on Pakistani industry and duty paid goods.

Rationale

A case in hand is Afghan Transit trade cargo. It used to suffer from different infirmities, which kept on hindering its smooth operations. These issues ranged from misdeclarations, delays, isolated and partial-monitoring, en-route pilferages, smuggling etc. A number of adhoc arrangements such as verifications of cross border certificates, random examinations at port of entry and enhancement of anti-smuggling operations etc. were made, but desired results could not be achieved.

6.03 REDUCTION OF IMPORT DUTIES ON IT EQUIPMENT

Reduction of Import Duties on IT equipment would support the growth of local freelancers and ICT industry and in general, the growth of tech eco system in Pakistan through reduced costs, in particular for freelancers and small businesses. Additionally, 200 -300K freelancers will be facilitated by having access to IT Equipment with potential to increase USD 50-100 million.

Rationale

To support the Digitalization of Pakistan, the sales tax rate on laptops, computers, and other IT equipment should be reduced from 10% to 0%.

This would lower the cost of acquiring essential technology, benefiting freelancers and small businesses that form the backbone of the digital economy. Moreover, exempting tax on IT equipment would encourage investment, innovation, and competitiveness in the sector, helping Pakistan leverage its growing IT export potential.

Currently, exemptions are available for certain machinery and plant imports under the Sixth Schedule, but IT equipment remains taxable, which creates a cost barrier for the sector. Therefore, revising the Sixth Schedule to include IT hardware would harmonize tax policy with economic development goals and support the digital transformation agenda in Pakistan

PROVINCIAL TAXATION

PART-II
PROVINCIAL SALES TAX

REFERENCE INDEX

PROVINCIAL SALES TAX ON SERVICES
SINDH SALES TAX ON SERVICES

1.01 APPOINTMENT OF OMBUDSMAN

LOW

SSTSA law envisages (Section 65A) the concept of Ombudsman; however, the Government has not yet implemented it despite considerable lapse of time. It is proposed that the Government should appoint an Ombudsman and frame relevant rules.

Rationale

Appointment of Ombudsman will bring a check over maladministration and abuse of authority by the tax administration.

1.02 DELEGATION OF POWERS

LOW

SECTION 36(1)(A)

The Board is empowered to appoint a Deputy Commissioner to exercise the powers of Commissioner (Appeals). It is proposed to delete this provision.

Rationale

It undermines the quasi-judicial function and weakens the judicial process when a junior ranked officer is allowed to assume the powers of a quasi-judicial authority.

1.03 INCONSISTENCES IN PROVINCIAL SALES TAX REGIMES: THE NEED FOR UNIFORM

ZERO RATING OF EXPORT OF SERVICES

LOW

Unlike other provinces, the Sindh Revenue Board does not generally allow zero-rating on the export of services under the SSTSA, except in limited cases i.e., software and IT services and Accountants & auditors' services etc. As such, the export of services other than those explicitly exempted remains subject to sales tax in Sindh. In contrast, other provincial tax statutes explicitly provide zero-rating for export of services:

This divergence in the treatment of export of services leads to a lack of harmonization across provincial jurisdictions and creates commercial disadvantages for service providers operating from Sindh. The absence of a uniform zero-rating regime in Sindh for all export of services hampers the competitiveness of Sindh-based exporters.

Rationale

Extending zero-rating uniformly to all export of services across all provinces including Sindh would foster greater interprovincial tax harmonization and better safeguard the economic and constitutional rights of taxpayers.

1.04 SALES TAX AT REDUCED RATE & ITS ADMISSIBILITY AS INPUT TAX

HIGH

Currently, certain services are chargeable to sales tax at a reduced rate subject to certain restrictions, limitations and conditions (including inadmissibility of related input tax credit / adjustment) and in some cases option is also provided to pay tax at standard rate. Similarly, where a reduced rate is applied on services, there is a restriction on adjustment of such input tax by the person receiving such services.

It is proposed that-

i. an option for general rate taxation be extended to all services for the province of Sindh like option has been provided under section 10A of PSTSA, section 16D of BSTSA and under section 18 of KSTSA. Under these provisions of said laws, a registered person providing services chargeable at a reduced rate of tax can opt to pay sales tax at the standard rate and take input tax adjustment after taking approval from the authority; and
ii. services procured at reduced rate of sales tax should be available as adjustable input tax if the recipient of service is liable to sales tax at normal rate on his services or on sale of goods under the Federal Law.

Rationale

It is just and equitable and in line with the true spirit of Law and Justice. Moreover, it will ensure uniformity in application and enforcement across all provinces.

PUNJAB SALES TAX ON SERVICES

1.05 TAXATION THROUGH REPRESENTATION

LOW

The Tax Administration heavily relies on notifications issued for enforcement of law, but they are not formally placed before the Provincial Assembly as per requirements of section 5(3) of the PSTSA. Further, certain reduced rate notifications are issued on yearly basis instead of amending the governing law.

It is proposed that the notifications issued should be tabled before the assembly as required u/s 5(3) of the PSTSA. Further, instead of repeating notifications each year, the governing law should be amended.

1.06 RESTRICTION ON INPUT TAX ON VEHICLES

LOW

SERVICES U/S 16B OF PSTSA

The other three Provinces (excluding PSTSA) do allow the input tax on vehicles if directly used and consumed in the economic activity of a registered person, which is also aligned with the principles decided by the higher Courts. A comparative statement analysis below spells out the details:

Balochistan Sales Tax 16B(1)(g)	Sindh Sales Tax 15(A)(1)(g)	Punjab Sales Tax 16B(1)(i)	KPK Sales Tax Section 17(1)(g)
The Input tax credit not allowed on goods and services acquired for personal or non-business consumption, excluding the following ones directly used and consumed in the economic activity of a registered person in provision of the services paying sales tax at a rate not less than 15% ad valorem such as – Vehicles classified under chap 87 of the first schedule to the Custom Act 1969 and part (including batteries and tyres and tubes of such vehicles …….	*the Input tax credit not allowed on the following goods and services, excluding the ones directly used and consumed in the economic activity of a registered person in provision of the services paying sales tax at a rate not less than 15% ad valorem such as – Vehicles classified under chap 87 of the first schedule to the Custom Act 1969 and part (including batteries and tyres and tubes of such vehicles …….*	*the Input tax credit not allowed on vehicles including three and two Wheelers*	*the Input tax credit not allowed on the following goods or services, excluding the one directly used and consumed in the economic activity of a registered person in provision of the services paying sales tax Vehicles classified under chap 87 of the first schedule to the Custom Act 1969 and part (including batteries and tyres and tubes of such vehicles …….*

It is proposed that necessary amendments should be incorporated so that distortion among the provinces can be avoided. There are various businesses where vehicles are essentially required to transport the goods and disallowance of input sales tax would increase unnecessary cost of doing business.

Rationale

This proposed amendment will align and harmonize the chargeability of services amongst all the Provincial Sales Tax laws and would avoid discrimination.

1.07 RESTRICTION ON ADJUSTMENT OF INPUT TAX IN EXCESS OF 90% OF OUTPUT TAX

MEDIUM

Section 16C was inserted in PSTSA through Finance Act, 2020 through which restriction was imposed on adjustment of input tax in excess of 90% of output sales tax.

The restriction of adjustment of input sales tax is proposed to be removed as it unnecessarily blocks the genuine input sales tax of registered persons. If such provision is not possible to be removed, then the threshold of 90% should be relaxed for businesses which have low margins. Authority has powers to issue notification for exclusion of persons or class of persons.

Rationale

For business which are operated on thin / low profit margins suffers liquidity problem which would discourage the documentation of taxpayers. The removal of such restriction would not result in any revenue loss to the exchequer. The relaxation of 90% threshold would ease the liquidity of businesses which have low operating margins.

1.08 INPUT TAX ADJUSTMENT ON FRANCHISE SERVICES

MEDIUM

Under the VAT law, input tax paid by service recipient under the reverse charge basis is available as input tax. There seems to be no specific bar on such adjustment under PST law and related rules. It is also understood that Punjab Revenue Authority (PRA) allows such input tax adjustment on case-to-case basis. There is however a misunderstanding on interpretation of Rule 6 of the Punjab Sales Tax on Services (Adjustment of Tax) Rules, 2012 and Rule 61 of the Punjab Sales Tax on Services (Specific Provisions) Rules, 2012 which provides non-adjustment on certain other grounds, but such rules are understood as bar on input tax adjustment on reverse charge basis. Since Sindh Revenue Board (SRB) has issued a Circular No.6/2020 dated July 10, 2020 allowing the input tax adjustment on reverse charge basis, the issue of input tax adjustment on reverse charge basis has been resolved / clarified.

In order to remove the misunderstanding on this matter, PRA may modify Rule 6 and 61 or issue a clarification in line with SRB.

Rationale

To align the law in line with sales tax principles and with other service tax laws.

KHYBER PAKHTUNKHWA SALES TAX ON SERVICES

1.09 TAXABILITY OF SERVICES BY CERTAIN PROFESSIONAL

HIGH

Serial number 19 of Second Schedule to the KPSTSA provide that certain services by professionals operating other than as corporate entities are taxable at reduced rate of 5%, whereas such services provided by corporate entities are taxable at standard rate of 15%. Similar, reduced rates are proposed for non-corporate entities under Sr. No. 5 and 8 of Second Schedule.

It is proposed that a uniform tax rate be adopted for all such professional services irrespective of status of service provider.

Rationale

Concessional rate for unincorporated entities would discourage the corporatization of businesses. Therefore, a uniform rate of sales tax would encourage corporatization.

1.10 PROCEDURE FOR ELECTRONIC INVOICING, MAINTENANCE OF RECORDS ETC

MEDIUM

No procedure or software has been prescribed by the Authority u/s 35(4) of the Act for electronic invoicing or billing, maintenance of records, filing of tax returns, and for any other matter by a registered person or class of such persons.

It is proposed that the Authority must prescribe the procedure or software for electronic invoicing, billing, filing of returns, etc. To enforce these measures effectively, a reward system for the customers to be introduced in the form of certain percentage of tax refunds, prize draws etc.

Rationale

The use of technological means would not only broaden the tax base but would also provide an efficient tool of compliance.

1.11 SPECIAL PROCEDURAL RULES ON APPOINTMENT OF ELECTRONIC INTERMEDIARY

MEDIUM

As per section 80 (6) of the Act, the Authority may prescribe rules for the conduct and transaction of business of e-intermediaries, however no such rules have been prescribed to date. Hence, it appears that this provision has not been enforced effectively thus far.

It is proposed that the Authority should issue special procedure / rules regarding appointment, and suspension and cancellation of appointment of e-intermediary.

Rationale

The introduction of rules in this respect would enhance transparency and professionalism.

BALOCHISTAN SALES TAX ON SERVICES

1.12 MEDICAL & HEALTH SERVICES

MEDIUM

Under Balochistan Sales Tax Laws, Sales Tax is charged on health care facilities. It is proposed that medical and health related services should not be chargeable to Sales Tax.

Rationale

This will bring harmony amongst all the Provincial Sales Tax laws and reduce the cost of medical treatment.

ISLAMABAD SALES TAX ON SERVICES

1.13 ENACTMENT OF INDEPENDENT SALES TAX ON SERVICES LAW

HIGH

The scope of Islamabad Capital Territory (tax on services) Ordinance, 2001 (ICT STO) was expanded by substituting the Schedule of services on the lines it is done by other provinces. However, nothing was done to make it a totally independent legislation. It continued to rely on the provisions of the Sales Tax Act, 1990 for their application as if it is a sales tax levied under the STA. Since the ICT STO is enforced by the FBR through its enforcement team in the field offices, who are responsible for enforcement of STA, they invariably apply the provisions of STA as if the entire law was applicable for charging and recovering sales tax on services.

After having extended the scope of ICT STO to bring in the ambit of tax almost all kinds of services that are taxable under the Provincial Sales Tax Laws, it has become extremely necessary to convert it into a full-fledged independent law on the lines it is done by the provinces, and while doing so, cognizance should be taken of the fact that these laws are to be harmonized with the provincial sales tax laws and the rules framed thereunder.

Rationale

Mutatis Mutandis application of the provisions of the STA (which applies to goods) related to certain matters including any other allied and ancillary matters related thereto, without identifying the sections, rules, orders, notifications etc. promotes ambiguity and makes it difficult for both the taxpayers and the tax collectors to follow the law. Following expansion of the list of services in the Schedule of Services, ICT STO has become a very active law and cannot be applied properly an effectively if they continue to be enforced through the unclear application of STA.

HARMONIZATION OF TAX LAWS

PART-III
HARMONIZATION OF TAX LAWS

REFERENCE INDEX

1 HARMONIZATION OF TAX LAWS

PRELIMINARY COMMENTS

Post 18th Amendment to the constitution of Pakistan, the power to levy sales tax on services is vested in the provinces, which poses serious challenges for taxpayers in ensuring simultaneous compliance with all provincial sales tax laws. Accordingly, this calls for urgent resolution for harmonization of tax portals and legal provisions of all provincial sales tax laws. This move should not be interpreted as centralization, rather it should be seen strictly from the perspective of bringing uniformity in the sales tax legislations of the Provinces and ICT and their similar application across the Provinces & ICT. These proposals are intended to create common standards across the Provinces and ICT. It does not mean to encroach upon the powers of enacting laws and regulations from the provinces. Since most of the major service providers operate across the country and are bound by the laws of the respective provinces to ensure compliance with all those laws therefore the need for increased harmonization of Provincial and ICT sales tax on services laws has become crucial. The principal areas which are conflicting or raise serious concerns are:

- Jurisdiction;
- Inconsistency in rates of tax;
- Reverse charge mechanism;
- Uneven penalty and default surcharge;
- Incidence of tax;
- Admissibility of common input;
- Filling of Multiple Tax Returns;
- Inter-province transactions; and
- Tax classification issues including HS Codes/ Tariff headings and inconsistency in definitions etc.

We have chalked out a brief comparison of major legal provisions to illustrate similarities and differences existing in relation to common subjects within the federal and provincial sales tax laws in **Annexure-I** to this document.

Keeping in mind the prevailing difference the following measures may be considered to achieve Harmonization:

1.01 INTEGRATION OF TAXATION AUTHORITIES FOR ONE-WINDOW SOLUTION

HIGH

We strongly recommend integration of federal and provincial revenue authorities across the country in such a way that provides one window solution to the taxpayers without undermining the existence and independence of each authority. One window solution should, inter alia, achieve replicating single sales tax return for all other taxpayers as is currently applicable to telecom sector, E&P (Oil & Gas) Companies and Microfinance Banks.

As soon as the above proposal is made effective this would eliminate undue compliance pressure of filing monthly tax return in each province and ICT totaling to five monthly and 60 returns annually in number of organizations.

Furthermore, it is imperative to introduce proper amendments in provincial laws to provide legal framework for smooth implementation of single tax return. Changes in laws are required to provide clarity regarding issues mentioned below inter alia.

Whether sales tax is to be paid on the basis of origin or destination principle in case of inter-province transactions other than those five service sectors for which the place of provision of service rules have been notified.

How, extension of time for filing return, revision of return, and penalty for late filing is to be catered.

Rationale

This will put taxpayers at ease by simplifying the sales tax return filing process and will be a right step towards ease of doing business.

1.02 INCONSISTENT CONCEPT OF REVERSE CHARGE IN PROVINCES

MEDIUM

The concept of reverse charge is used in many countries to exempt the exporters of services from registering themselves in the country of the importer.

The provincial sales tax laws of Pakistan also have Reverse Charge provisions which bound the recipient of services to pay tax on services which originate from outside the province or outside Pakistan. Since the inter-province transactions are not zero-rated or exempt in the jurisdiction of origin, such transactions are also taxed in the province of the service provider. This tantamount to double taxation which is not the spirit of tax statute. For practical purposes taxpayers are managing this challenge by either availing legal cover from courts to avoid dual chargeability of sales tax on their services or obtaining registration in the province of their customer to charge sales tax accordingly.

It is highly advisable that the reverse charge should be restricted to such cases where service provider is located outside Pakistan. Further, the recipient of services paying sales tax under reverse charge mechanism should be allowed adjustments of same as input tax.

Rationale

The above measure will prevent taxpayers rendering services in more than one province from double taxation. Further, the adjustment of tax paid under reverse charge mode, as input tax would help in reduction of cost and will promote ease of doing business.

1.03 EXPANDING THE SCOPE OF PLACE OF PROVISION OF SERVICE RULES

MEDIUM

The federal government to the extent of ICT and all other provincial governments have notified place of provision of service rules for the following specified services:

a) Advertisement
b) Advertising agents
c) Electric power transmission services
d) Insurance
e) Insurance Agents
f) Franchise
g) Transportation or Carriage of goods

The said rules have provided guidelines with regards to ascertainment of origination, termination, and execution of services for chargeability of sales tax. This action can be termed as a right step towards addressing disparities resulting from principles of origin and reverse charge. However, there are several other taxable services which could not form part of these rules.

It is therefore proposed to expand the scope of these rules to cover all taxable services for bringing harmony in chargeability of sales tax in respect of services expanding beyond territory of a province.

Rationale

This would bring more clarity regarding chargeability of sales tax and can minimize legal disputes.

1.04 ZERO RATING OF EXPORT OF SERVICES

MEDIUM

Despite government's major focus on boosting exports necessary measures are pending for allowing zero rating of export of services to foreign countries. The provincial statutes lack agile zero-rating provisions as they are not at par with tax provisions applicable to export of goods under the Federal Sales Tax Act and export of services under ICT (Sales Tax on Services) laws. In Punjab, zero rating on export of service is allowed subject to stringent conditions, and in Sindh, it is allowed merely to Accountants & Auditors, Software Consultants and call centres.

It is advisable that zero rating of export of services should be allowed by all provinces on all types of services with lenient conditions in order to promote export of services in the international market, and the laws in this respect be harmonized with the Federal Sales Tax Act and ICT (Sales Tax on Services) Laws.

Rationale

This measure will help in promoting export of services and can be instrumental in enabling the government to increase its foreign reserves and reduce Current account deficit.

1.05 SALES TAX WITHHOLDING

HIGH

Unlike Punjab, other provincial sales tax withholding rules require withholding of sales tax against services received from active/registered persons. This adds on to administrative work and obstructs ease of doing business.

For ready reference a comparison has been drawn for sales tax withholding requirements of federal and provincial statutes at **Annexure-II** to this document.

It is advised that sales tax withholding should not be made applicable in cases where services are received from corporate or non-corporate registered persons who are active for sales tax purposes. Where a service is rendered by an unregistered person to the registered service recipient, the liability to pay the tax practically falls upon the person receiving the service in almost all cases. The whole amount of sales tax is required to be withheld from the payment made to the unregistered person.

For harmonization it is recommended that either the rate of withholding tax in provinces for unregistered service providers may be reduced to 5% in line with the Federal Sales Tax Withholding Rates or input tax adjustment may be allowed to the person receiving such service.

Rationale

To avoid unwarranted administrative and operational issues as well as to minimize cost. This will also reduce the sales tax withholding related litigation.

1.06 CLASSIFICATION OF TAXABLE SERVICES RULES

MEDIUM

The Provincial and ICT tax laws have not addressed the following:

(i) classification of services that simultaneously falls under more than one taxable service categories;

(ii) classification and separation of a service component from a goods component within the same transaction; and

(iii) classification of multiple or composite services.

The need for these rules has never been as crucial as it is now in view of judgement of the honorable Sindh High Court in case of Messrs. M. Mubashir trader which was lately upheld by Supreme Court of Pakistan. A line of demarcation needs to be drawn between the goods component involved in a manufacturer and dealer/distributor relation which will attract sales tax on goods and the service component which will invoke services sales tax.

Taxpayers should not be left at disposal of tax authorities rather, the definitions of taxable supplies/ services available in relevant statutes should be amended to eliminate all possibilities of dual taxation on a single transaction.

Also, it has been observed that services like supply chain management or distribution (including delivery) services inserted through Finance Act, 2016 are also covered under business support services as 'Managing distribution and logistics'. Renting of immovable property services through Finance Act, 2015 are also covered under business support services as 'Infrastructural support services'.

The above confusions and ambiguities can be addressed by introduction of classification of services rules. The Classification rules play a vital role and are generally crucial in the following situations:

- Applicability of different tax rates, or where one of the possible headings is not taxable;
- Availability of exemption when one of the possible headings is exempt from tax;
- Mode and manner of taxation of transactions involving composite arrangement i.e., goods and service component; and
- Determination of date from which the tax is to be levied where a service falls under two headings, one attracts tax from an earlier date.

Moreover, a guideline can also be issued by provincial tax authorities for educating taxpayers.

Rationale

These steps will eliminate confusion and will augment ease of doing business.

1.07 H.S CODES / TARIFF HEADINGS TO VARIOUS SERVICES IN FIRST SCHEDULE MEDIUM

Several categories of services mentioned in the First Schedule are without H.S Code/ Tariff Headings. Likewise, different categories of services fall under different HS code in different provinces. It is recommended that proper tariff codes should be assigned to such services and in case of discrepancies in alike services across provinces uniformity should be ensured.

Rationale

It will bring clarity and uniform tax positions across provinces.

1.08 DEFINITION OF TAXABLE SERVICES

MEDIUM

Unlike Sales Tax laws relating to Sindh and Punjab, the definitions of taxable services given under KPK Act are limited to certain services only.

It is suggested that all services covered under First Schedule to the Sales Tax on Services Acts, should be defined and such definition should be in conformity with definitions in other provincial laws.

Rationale

This will promote harmonization and uniform tax treatment across provinces.

1.09 SALES TAX ON SERVICES OF ACCOUNTANTS AND AUDITORS

HIGH

Currently, the services of accountants and auditors are subject to varied rates under the Provincial Sales Tax laws in the following manner:

Provincial Law	*Standard Rate of Tax*	*Reduced Rate*
Sindh Sales Tax	*15%*	*8% without input tax adjustment*
Punjab Sales Tax	*16%*	*5% without input tax adjustment*
KPK Sales Tax	*15%*	*5% without input tax adjustment*
Balochistan Sales Tax laws	*15%*	*6% subject to a condition*
Islamabad Sales Tax laws	*15%*	*Not available*

It is proposed that the rate of tax in all the territories should be aligned.

Rationale

There should be harmonization between all the provinces and such rate of tax should be reduced to 5% under all the jurisdictions to promote the regulatory culture and to reduce the cost of compliance.

1.10 TIME LIMITATION FOR ASSESSMENT & RETENTION OF RECORDS

U/s 24(2) & 32(1) OF PSTA; SECTIONS 23(2) & 27(1) OF SSTA; SECTION 27(5) & 36(1) OF KPSTA, SECTION 24(2) & 32(1) OF BSTA & SECTION 11E, 11G & 24 of STA

The period for retention of records and time limitation for assessment of tax are not aligned and consistent under the Provincial and Federal Sales Tax laws, as tabulated below:

Sales Tax Law	Records Retention Period	Time limitation for assessment	Order Issuance
Federal Sales Tax	*6 years*	*5 years*	*120+90 days*
Sindh Sales Tax	*10 years for periods till 30 June 2025* *6 years for periods after 1 July 2025*	*8 years for periods till 30 June 2025* *5 years for periods after 1 July 2025*	*180+60 days*
Punjab Sales Tax	*8 years for periods before July 2022* *6 years for periods after July 2022*	*8 years for periods before July 2022* *5 years for periods after July 2022*	*1 year*
KPK Sales Tax	*5 years*	*5 years*	*120+60*
Balochistan Sales Tax	*10 years*	*8 years*	*180+60*

It is proposed that the time period for retention of records and assessment of tax should be rationalized and fixed at 6 years in all provinces as is applicable under the STA and ITO.

Rationale

Longer period of retention and assessment is not only burdensome, but also creates uncertainty for the taxpayers for assessment as well as results in additional cost for retaining information / documents for such extended period of time. Moreover, the period of assessment / retention of information should be curtailed in a phased manner.

1.11 ISSUE OF TAXATION OF DISTRIBUTORS

All the provincial sales tax laws (except for KPK) have a taxable entry of 'Supply Chain Management or Distribution (including delivery) Services'. Sindh Revenue Board initiated the enforcement under the said category of services and passed the orders to compulsorily register few distributors. The matter was litigated and after the complete round of litigation finally decided against the taxpayers by the Supreme Court of Pakistan. Resultantly, provincial sales tax authorities (especially SRB) have started issuing notices to distributors to get them registered. This situation has created a chaotic situation as the distribution model in industry operates as

trading of goods instead of services.

It is proposed that definition of 'supply chain management or distribution (including delivery) services' needs to be defined under the provincial sales tax laws and with the consensus among federal and provincial authorities, scope of such services should be restricted to the transactions executed without transfer of title of goods.

Rationale

Multiple taxation on single economic activity of trading of goods is resulting in more difficulties in doing the businesses besides affecting the VAT system of the country as a whole.

1.12 100% SALES TAX WITHHOLDING FROM CERTAIN SERVICE PROVIDERS

Withholding Rules provides various conditions and scenarios for withholding the provincial sales tax. These rules are very complex and unharmonized which complicate the compliance for the taxpayers. Following table summarizes the general withholding provisions:

Law	Applicability of Sales Tax Withholding on
Sindh	Other than Active Persons and certain specified services
Punjab	Other than Active Companies
KPK	Other than Active Persons
Balochistan	Other than Registered Persons and certain specified services

It proposed that withholding should not be applicable in case of active taxpayers and all the provincial sales tax laws should be harmonized in this respect.

Rationale

Such amendment is necessary to remove undue hardship being faced by such registered taxpayers who are not able adjust their input tax. The complexity and variation in withholding rules also complicate the assessment process where substantial time is consumed by the assessing officers to verify the withholding.

1.13 STREAMLINING OF THE DEFINITION OF VALUE OF TAXABLE SERVICE

PRA and SRB have attempted to bring in to the scope of taxable services the entire consideration received by the service providers regardless of the nature of same. Though the Courts have ruled out the possibility of taxing certain components of considerations which does not constitute a taxable service such as reimbursable costs for HR and security service providers, but provincial sales tax authorities continue to tax same by amending the wording of definitions of respective act. A uniform definition of "Value of taxable service" needs to be drafted.

Rationale

To avoid unnecessary litigation.

Contrast of legal provisions
Annexure-I

Description	FBR/ICT	PRA	SRB	KPRA	BRA
Input Tax Adjustments					
Extent of input tax adjustment	90% of output tax	90% of output tax	100% allowed	100% allowed	100% allowed
Input tax on fixed assets purchase	100% allowed	100% allowed	In 12 equal monthly installments	100% allowed	In 12 equal monthly installments
Payment through banking channel	Payments exceeding 50,000	Payment to single party for more than 50,000 in a tax period	All payments	All payments above 50,000	All payments above 50,000
Input tax claim against credit purchases	Payment should be within 180 days of invoice	Payment should be within 180 days of invoice	Payment should be within 180 days of invoice	N/A	Payment should be within 180 days of invoice
Limit on input tax adjustment rate	N/A	N/A	Up to 13% allowed	N/A	Up to 15% allowed
Input tax adjustment under reverse charge	Disallowed	Disallowed	Allowed	N/A	N/A

Assessment Proceedings and Records					
Description	**FBR/ICT**	**PRA**	**SRB**	**KPRA**	**BRA**
Assessment proceedings	5 years	Up to 8 years for periods earlier than July 2022 Up to 5 years for period after July 2022	8 years for periods till 30 June 2025 5 years for periods after 1 July 2025	Up to 5 years	Up to 8 years
Assessment Order	120+90 days of show cause notice	Within 1 year of show cause	180+60 days of show cause	120+60	180+60 days of show cause
Records	6 years	8 years for earlier than July 2022 6 years for periods after July 2022	10 years for periods till 30 June 2025 6 years for periods after 1 July 2025	5 years	10 years

Penalties and default surcharge					
Default in filing sales tax return within due date	Rs. 10,000 for default exceeding 10 days, otherwise Rs. 200 per day	Rs. 10,000 for default up to 15 days, after that additional Rs.200 per day	Rs. 10,000 per month or proportionately on no. of days if default extending beyond 10 days, otherwise Rs. 300 per day	Rs. 9,000 per month or proportionately on no. of days if default extending beyond 10 days, otherwise Rs. 300 per day	Rs. 10,000 for default up to 15 days, after that additional Rs.200 per day
Failure to deposit the amount of the tax due	Higher of Rs. 10,000 and 5% of payable tax, but in case of payment within 10 days Rs. 500 per day.	Higher of Rs. 10,000 and 5% of payable tax, but in case of payment within 10 days Rs. 500 per day.	Higher of Rs. 10,000 p.m. or proportionately on no. of days and 5% of payable tax (for >3 days default).	Higher of Rs. 10,000 and 5% of payable tax.	Higher of Rs. 10,000 and 5% of payable tax, but in case of payment within 10 days Rs. 500 per day.
Default surcharge	12% p.a or KIBOR plus 3% p.a, whichever is higher	Interbank+3%	Interbank+3%	24% p.a.	12% p.a

Others

Description	FBR/ICT	PRA	SRB	KPRA	BRA
Definitions	N/A	Separate Definition rules	Section 2	No definitions	Section 2
Appeals					
Commissioner Appeals:					
Commissioner Appeals- Appeal	30 days	30 days	30 days	30 days	30 days
Commissioner Appeals- Stay	30 days	60 days	180 days	60 days	60 days
Commissioner Appeals- Decision	120+60 days	120+60 days	180+60 days	120+60 days	120+60 days
Appellate Tribunal:					
Appellate Tribunal- Appeal	30 days	60 days	60 days	60 days	40 days
Appellate Tribunal- Stay	90 days	90 days	90 days	6 months	90 days
Appellate Tribunal- Decision	90 days	6 months	6 months	6 months	6 months

Sales Tax Withholding Requirements **Annexure-II**

Categories of suppliers/service providers	FBR	PRA	SRB	KPRA	BRA
Unregistered or in-active	5% of gross value	100% of applicable sales tax	100% as per tax fraction	100% of applicable sales tax	100% of applicable sales tax
Advertisement services	100% sales tax	100% of sales tax	100% of sales tax	100% of sales tax	100% of sales tax
Certain specified goods/services	80% of sales tax	-	100% of sales tax	-	100% of sales tax
Registered active person	0% with exceptions	-	20% of sales tax	50% of sales tax	20% of sales tax
Registered active person- Corporate	-	0%	-	-	-
Registered active person- Other than Corporate	-	100% of sales tax	-	-	-
Reduced rate services	-	-	-	100% of sales tax	-

EASE OF DOING BUSINESS

PART-IV
EASE OF DOING BUSINESS (EODB)

REFERENCE INDEX

EASE OF DOING BUSINESS (EODB)

Pakistan's ranking of 108 out of 190 in the World Bank's Ease of Doing Business index (2021) underscores persistent structural barriers that deter investment and slow economic growth. Despite efforts at modernization, the business environment remains burdened by complex, inconsistent, and frequently changing regulations—particularly in taxation, where overlapping federal and provincial regimes continue to create inefficiencies, increase compliance costs, and cause jurisdictional disputes.

Key obstacles include:

- A large undocumented and informal economy
- Inconsistent enforcement and lack of harmonization between tax authorities
- Frequent and unpredictable amendments to tax laws
- Fragmented indirect tax regimes across provinces
- Bureaucratic red tape, arbitrary powers, and limited automation
- Delays in dispute resolution, tax refunds, and return revisions
- Onerous compliance requirements for small businesses and formal sector companies

While broader reforms—such as improved infrastructure, digital government services, and trade facilitation—are essential, this document focuses specifically on fiscal and tax administration reforms at both federal and provincial levels to improve Ease of Doing Business (EoDB) across Pakistan.

Reform Objectives

These proposals are designed to:

- Streamline tax administration through digitization and automation
- Ensure consistency and predictability in fiscal policies
- Eliminate unnecessary and overlapping tax burdens
- Harmonize federal and provincial tax laws and filing systems
- Introduce uniform treatment across jurisdictions for service providers and manufacturers
- Protect businesses from arbitrary enforcement actions and coercive recovery measures
- Encourage corporatization, equity investment, and documentation of the economy
- Support small and medium enterprises (SMEs), technology zones, and exporters through targeted incentives

Key Reform Areas

Federal Tax Reforms

1. Complete automation of tax processes – e-filing, e-notices, reconciliation
2. Consistency in fiscal laws and procedures – simplification of overlapping tax regimes
3. Reduction in effective direct tax rates – abolishing minimum, alternate, and super taxes
4. Improved tax recovery and refund mechanisms – ensuring timely and fair enforcement
5. Rapid tax dispute resolution – with independent and efficient appellate forums
6. Independent and transparent tax administration – with governance reform and autonomy
7. Streamlining of withholding tax management – reducing duplication and ensuring real-time access to data
8. Monitoring of withholding tax (Section 161) – with clear timelines and protection against harassment
9. Coordination between federal and provincial tax authorities – single-window tax collection and jurisdiction resolution
10. Automated transfer of sales tax drawbacks – to active taxpayers
11. Revival of the POS Prize Scheme – to drive invoice-based consumer transactions
12. Incentives for Special Technology Zones – including exemption alignment across tax laws
13. Reform of Sections 161 and 165 – to rationalize WHT obligations and credit mechanisms
14. Rationalization of the "prescribed person" definition under Section 153 – to support small corporations
15. Dividend tax reforms (Section 150) – to remove double taxation and incentivize reinvestment
16. Industry rebate and origin verification framework – to promote local sourcing and reduce import dependency

Provincial Tax Reforms

1. Uniform rules on input tax adjustment – including longer pre-commencement periods and harmonized treatment of 'extra/further' taxes
2. Recognition of Value Addition Tax paid at import stage – as input tax for service providers
3. Elimination of joint and several liability without evidence of collusion – aligned with federal provisions

4. Assessment order amendments – with Commissioner oversight and defined triggers
5. Audit reforms – including selection by Commissioners only, mandatory justification, and a 6-month time limit
6. Removal of audit certification requirements by statutory auditors – to align with legal audit scope
7. Return revision rights – without prior approval within 120 days, with deemed approval mechanism
8. Limiting excessive information requests – to prevent fishing inquiries
9. Exemption for nonprofit entities – from provincial sales tax
10. E-hearing expansion – from Commissioner Appeals to Appellate Tribunals
11. Minimum taxable threshold for small service providers – with uniform rules across provinces
12. Taxation of e-commerce/digital services – with coordinated framework and single return
13. POS integration across tax authorities – for real-time cross-jurisdictional compliance
14. Automatic stay of tax recovery on appeal – without upfront tax payments or with reduced percentage
15. Refund of excess input tax – aligned with federal laws and best practices
16. Recognition of cost reimbursements (e.g., salaries) – in line with court judgments
17. Withdrawal of sales tax on renting of immovable property – as per superior court rulings
18. Barcoding of notices and orders – to enhance authenticity and prevent abuse
19. Advance publication of draft SROs – with stakeholder consultation
20. Rectification of any mistake apparent from record – not limited to clerical errors
21. Establishment of Advance Ruling authorities – for pre-transaction certainty
22. Reduced tax rate for digital payments – to incentivize formal economy participation

Adopting these comprehensive federal and provincial reforms will significantly improve Pakistan's investment climate, reduce compliance costs, increase tax documentation, and create a predictable, fair, and efficient tax system. Most importantly, they will align the country's fiscal environment with global best practices—an essential step toward long-term economic stability and growth.

EASE OF DOING BUSINESS – FEDERAL TAXES

1.01 COMPLETE AUTOMATION OF TAX PROCESSES - DIGITILIZATION

HIGH

The Federal Board of Revenue ("FBR") has progressed over the years in implementing Information Technology ("IT") in income tax administration. However, use of IT for sales tax and integration with provincial sales tax authorities' data is still behind the desired level. There is a need to achieve complete automation of IT Processes, as early as possible. The use of IT in the sales tax processes, can ensure completeness of indirect tax revenue collections and ensures effective monitoring of compliance. IT further helps the tax administration in efficiently processing tax returns, tax assessments and tax refunds. It also supports and provides an effective tool for the following:

i. Conducting audit of tax administration covering its functions of tax assessment, tax collection, and effective use of IT for broadening of tax base; and

ii. Creating and maintaining a computerized folder of each taxpayer's complete tax record including but not limited to:

   (a) Activities of taxpayer, which can assist in determination of taxable income;

   (b) Appeals to Appellate Tribunal Inland Revenue and related orders;

   (c) Refunds outstanding and refunds issued; and

The taxpayers are required to file quarterly withholding statement u/s 165(1), annual withholding tax statement u/s 165(6) and another annual withholding tax statement u/s 165(7). It is proposed to omit submission of unnecessary duplicate information by the taxpayer, when the information required can be captured through effective use of IT.

Based on the information of the taxpayer transactions available on IT systems, efforts are required to modify the system to prepare pre-populated Income Tax Returns available to the taxpayer at the close of the Tax Year thereby facilitating tax compliance and ensuring completeness and transparency.

1.02 CONSISTENCY IN FISCAL LAWS AND PROCEDURES

HIGH

FBR with the objective to enhance tax revenue over the years, enhanced the complexity of tax laws and procedures through continuous amendments in fiscal laws by introducing several final, minimum, alternate, and super tax regimes along with several exceptions which further added to the confusion. Similarly, many withholding taxes were introduced by the name of "Transitional Advance Tax Provisions – Chapter XII". This, at times, becomes more vulnerable as field officers of the revenue authorities make different interpretations which opens the doors for long drawn litigations giving rise to exorbitant increase in "cost of doing business". Above all, predictability of the laws has always been questionable, and that prevented the taxpayers from making long-term business plans.

Interaction with revenue authorities in multiple tax jurisdictions without harmonization of goods and services tax laws of the federal and provincial governments results in tax disputes which adds significantly to the cost of doing business.

A concerted effort is needed for bringing all revenue authorities together on the agenda of reformation and harmonization of goods and services tax laws of the federal and provincial governments. Similarly, it is strongly recommended to reform the existing tax framework to make it less complex and easy to comply.

These measures may include:

i. Consistency / freezing of laws for a segment of business for an appropriate period;
ii. Harmonization in rates of indirect taxes on goods and services across the country;
iii. Single tax collecting platform for federal and provincial indirect taxes;
iv. True enforcement of Self-assessment scheme;

v. Commissioner's open-ended power to select cases for audit should be restricted only to cases where the Commissioner has definite information that the taxpayer has either committed fraud or has made false declaration;

vi. Efficient completion of assessments where cases are selected for tax audits under an automated and transparent selection process;

vii. Automatic transfer of tax refunds to designated bank account of the taxpayer;

viii. Reduction in number of tax payments and their filing requirements; and

ix. Workers related federal and provincial taxes and levies namely Employees old-age pension benefits, social security, surplus (un-distributable) workers profit participation fund and workers' welfare fund should be deposited in designated banks and financial institutions using one consolidated payment document.

1.03 REDCUTION IN EFFECTIVE DIRECT TAX RATES

HIGH

The key findings of a report on "Corporate Tax Rates around the World, 2023" published by "Tax Foundation" on December 12, 2023, based on the data of 225 countries are as follows:

- Most countries are constantly reduced corporate tax rates since 1980, but has leveled off in recent years;
- Forty-one countries have corporate tax rates of below 25 percent, one hundred and twenty have rates above 20 percent and below 30 percent;
- Average corporate income tax rate across 225 countries is 22.27 percent;
- Asia has the lowest regional average rate of 19.80 percent;
- Only three countries impose a corporate tax rate of greater than 35 percent;
- OECD Pillar Two agreement has guided certain low tax jurisdiction to impose / improve corporate tax rate;
- Corporate tax rates between 20 percent and 25 percent have become the most common;
- All regions saw a net decline in average statutory rates between 1980 and 2023; and
- Most countries have agreed to implement global minimum tax rate of 15 percent, as proposed by Pillar Two Agreement initiated by OECD, over the years.

Corporate tax rates in some of related jurisdictions are as follows:

- Sri Lanka 30 percent
- Turkey 25 percent
- Republic of Korea 26.5 percent
- Bangladesh 27.5 percent
- China 25 percent
- Indonesia 22 percent
- India 30 percent

Although corporate tax rate of 29 percent imposed in Pakistan is considered for the purposes of the study, but study does not capture the levy of super tax, Alternate Corporate Tax and Minimum Tax regimes, which converts the corporate tax regime in Pakistan, as one of the most aggressive.

In addition, the tax laws are amended to curtail the admissibility of expenditure and making harsh assessments to snatch away the relief, if any, extended by any provision. Significant negative amendments introduced overtime are: (a) eliminating or significantly reducing the initial depreciation on tangible assets; (b) increasing the maximum period for amortization of intangibles from 10 to 25 years; (c) reduce depreciable value of motor vehicles used for business; (d) restrictions on admissibility of sales promotion and advertisements.

It is strongly recommended to initiate following steps for smooth operation of the businesses, particularly for the startups and MNCs set up through foreign investments:

i. Super tax regime be abolished;

ii. Alternate Corporate Tax regime be abolished;
iii. Minimum tax regime based on turnover be abolished otherwise Maximum rate of taxation should also be defined;
iv. A gradual decrease in corporate tax of 29 percent be introduced;
v. Tax rates for non-corporate sector, which includes salaried and business individuals, SMEs and AoPs should be reduced, and it should not, by any means, be more than the rates prescribed for small companies.
vi. vi. Surcharge on income exceeding Rs.10 million applicable on Individuals & AOP shall be abolished.

The aforesaid proposals if implemented can revive the economy of the country and bring prosperity and ultimately increase the tax revenue for the Government, provided effective implementation of tax laws is ensured.

vii. The burden of lack of capacity of regulators in implementing fiscal laws should not be passed to the taxpayers, resulting in contraction of economy.

1.04 TAX RECOVERY AND TAX REFUND MECHANISM

HIGH

Current tax recovery mechanism fully provides for all imaginable recovery options. What it lacks is its fair application particularly in cases where harsh tax assessments are framed and are being challenged at appellate forums. Whilst it is hoped that with the setting up of independent and transparent tax administration manned by competent staff would result in fair taxation, it is strongly recommended to make amendments in the tax recovery provisions for introducing mandatory approval mechanism before initiating any coercive recovery option, such as attachment of bank account, arrest or appointment of receivers. Such approval should be sanctioned only in cases where tax dispute resolution options are exhausted or there is a high risk of the taxpayer absconding or leaving country. This is necessary as uncontrolled use of such powers, could financially and operationally cripple the taxpayer and the economy.

Current tax refund mechanism is highly inefficient, and, in cases where the amount of refund is substantially higher, it is usually withheld deliberately for one reason or the other. Denying, or delayed processing of, assessed tax refunds has significantly distorted the business-friendly image of Pakistan. The Finance Act, 2019 has tried to address this issue by introducing refund bonds for the settlement of long outstanding income tax refunds. These refund bonds carry a simple interest of 10%, which is payable along with principal amount of refunds on attaining maturity period of three years. However, it did not auger well as such bonds are neither traded freely in the market nor eagerly discounted by the banks.

It is strongly recommended to initiate following steps for addressing the refund issues:

i. Processing of refunds should be entrusted to a separate wing, and such process should be completed within a maximum period of 90 days reckoning from the date of filing of the application;
ii. Amendment should be made in the FTO Ordinance to allow the FTO to accept cases of refund disputes for issuing an order binding on the tax authorities; and
iii. Delayed payment of refund should be eligible for a return at monthly KIBOR plus 3% per annum.

1.05 RAPID TAX DISPUTE RESOLUTION

MEDIUM

Tax disputes could arise between the tax administration and the taxpayers both under local tax laws and tax treaties. Currently available options for dispute resolution are; (a) appellate forum starting from Commissioner Appeal (which is a part of tax administration) to the Appellate Tribunal (which is a quasi-judicial forum) where disputes covering matters both on fact and law are decided; (b) High Courts and Supreme Court (which are independent) but where only point of law arising from the order of the Appellate Tribunal is decided and (c) alternate dispute resolution, where a dispute resolution committee decides issues other than point of law provided the taxpayer is willing to withdraw appeal on the disputes pending resolution at the appellate forum or in courts. Continuous

amendments in Alternate Dispute Resolution mechanism could not gain confidence amongst taxpayers.

Current dispute resolution options are a lengthy exercise and most of the disputes remain undecided for longer period. In several cases, particularly in case of MNCs (where huge foreign investments are at stake), the cases remain undecided for five or more years. Absence of rapid dispute resolution mechanism becomes not only a costly affair, but also works as an obstacle in routine operation of the businesses, particularly where the disputed tax is either recovered through coercive measures including attachment of bank accounts.

It is strongly recommended to take the following steps for providing rapid resolution of the tax disputes:

i. The appellate forum of Commissioner Appeals be completely abolished;
ii. Tribunal should be strengthened and be made totally independent. The accountant member if selected from amongst the officials of the tax department, should first relinquish his right to join back the department;
iii. Tribunals benches be made operational throughout the country, to facilitate taxpayers;
iv. First appeal be adjudicated by two members bench of the Tribunal and Second appeal by a full bench comprising three or more members of the Tribunal;
v. A separate bench should be set up in all high courts for hearing of tax cases only;
vi. An independent permanent body for Alternate Dispute Resolution be set up, and they should be given full powers to decide all kinds of dispute and making its decision binding on the tax administration;
vii. It is strongly recommended that the Appellate Tribunal Inland Revenue should be brought under the under administrative control of Islamabad High Court; and
viii. In order to build the confidence of the taxpayers in the appeal system, it is also recommended to publish all judgments of the appellate forums.
ix. The amendments introduced through the Tax Laws (Amendment) Act, 2024 further complicates the situation for the taxpayers and was implemented only to facilitate tax recovery, which in most of the cases was incorrectly levied to create tax demands, rather than to facilitate the taxpayers and to correct the gaps in the system. It has the potential to fully jeopardize the tax appellate structure.

1.06 INDEPENDENT AND TRANSPARENT TAX ADMINISTRATION

Tax Administration plays an important role in enforcing tax laws to collect tax for the governments for their use for the social uplifting of the general public including the taxpayers and for creating infrastructure for long-term economic development. It is therefore necessary that the Tax Administration should not only be efficient but also be fairly independent – having either detached from, or less control of the government.

It is our understanding that a proposal was already under active consideration of the government to convert the FBR into an autonomous body on lines similar to SBP and SECP. Whilst this is indeed a welcome step, it is proposed to consider the following minimum steps for functioning of an effective independent and transparent tax administration till such a decision is implemented:

i. Tax Policy should be transferred to Ministry of Finance and Ministry of Law and Justice. All amendments in fiscal laws should be the responsibility and routed through the two Ministries;
ii. The FBR Act and related rules and regulations should be amended appropriately for improving the governance structure and making it highly autonomous, transparent and subject to accountability by independent external auditors, in addition to the office of the Auditor General of Pakistan;
iii. FBR should operate and work with a corporate governance structure with a Board of Directors, vested with powers similar to the Boards of Public listed companies. Fifty percent of the Board members including Chairman FBR may be nominated by the government (Ministries of Finance, Law, and Commerce) and, the remaining fifty percent should be nominated by the established

trade and professional bodies like OICCI, PBC and ICAP;

iv. FBR should be headed by an experienced qualified professional, who should be assisted by qualified and trained professionals having established knowledge and experience of accounting, taxation, law, IT, economy and business administration. For this purpose, full autonomy be given for remunerating the hired personnel and elevating and incentivizing them based on performance evaluated using a balance score card; and

v. An Internal Audit Department should be set up for conducting effective internal audits of FBR affairs and directly reporting to a Committee of Board members comprising government and non-government members.

vi. Imposing widespread taxes that are difficult to administer defeats the purpose of taxation. Therefore, the practicality of implementation must be a central concern when designing any tax. Moreover, the success of tax administration lies not just in the amount collected, but in the fairness of the collection process. A just system ensures all stakeholders contribute equitably, rather than unfairly targeting the poor and salaried while failing to collect from entrepreneurs and businesses. Consequently, tax administrators must adopt rational and equitable methods.

1.07 STREAMLINING OF WITHHOLDING TAX MANAGEMENT

The largest part of the annual tax collection is currently made through withholding tax regime. It would be justified to consider it as the backbone of current tax collection system. However, there is still so much to be done for gathering of withholding tax data and its use both for the benefit of tax collectors and taxpayers. Accordingly, it is strongly recommended to streamline the withholding tax management by taking the following minimum steps:

i. Implementation of Automatic issuance of tax exemption certificates;

ii. Ensure gathering of accurate withholding tax data of each taxpayer from the withholding agents including those who are currently not providing such data, i.e., utilities, financial institutions, telecommunication sector, AGPR, airlines etc.;

iii. Provide access to withholding tax data to the taxpayers on a real-time basis;

iv. Where the withholding agents, i.e., governments, utilities, financial institutions, airlines, who do not provide Computerized Payment Receipt (CPR), a certificate of tax withheld or collected issued by such withholding agents should be accepted as valid evidence of tax withheld or collected for admissibility for tax adjustment including refunds;

v. Withholding tax deducted or collected by the withholding agents represents tax of the persons from whom tax is deducted or collected. There is a provision for recovery of un-deducted or un-collected tax from the withholding agents (section 161) where default committed by the withholding agent in this respect surfaces through a monitoring exercise. There is also a provision (section 162) which prevents recovery of such tax from the withholding agent where the tax is paid by the actual taxpayer. The tax collector usually proceeds against the withholding agent and penalize him by recovering the un-deducted or un-collected tax as revenue measure, instead of first ensuring that the payments to the recipient that escaped tax deduction or collection have been offered to tax by the actual taxpayer in his tax declaration;

vi. Due date of payment of withholding tax deducted or collected by the withholding agent should be uniformly applied on a monthly basis for all withholding agents; and

vii. The requirement of filing statement of taxes withheld by the withholding agent can also be withdrawn, as FBR could use its IT resources to generate such statement based on the information provided in the CPR.

1.08 COORDINATION BETWEEN FEDERAL AND PROVINCIAL TAX AUTHORITIES

The amendments in the Constitution of Pakistan provided substantial fiscal and legal autonomy to the provinces for raising finance and enacting new laws. Following enactment and implementation of the service tax laws and labor welfare laws by the provinces, the businessmen, who have businesses located in more than one tax jurisdiction being Trans Provincial Companies ("TPCs"), are

facing jurisdictional challenges and duplicate taxation leading to tax disputes. This is causing financial and operational hardships as number of challenges overtime has increased substantially.

It is strongly recommended to establish (preferably within FBR) a permanent cell or directorate which should be equally represented by nominees of the federal and provincial tax authorities to provide a common platform to the taxpayers for resolving jurisdictional issues and preventing duplicate taxation. The cell should also be responsible to address and allocate the tax deposited by the taxpayer in one jurisdiction, to the other jurisdiction, if so, decided by the cell, without the involvement and penalizing taxpayer.

As an alternative it is recommended that one authority be empowered to collect all types of federal and provincial taxes for onward transmission to respective revenue authorities within the country without burdening the business entities and the provincial taxes should be consolidated specially the labor levies e.g., EOBI, SESSI, WPPF, WWF etc.

Special attention may need to be given to tax implication arising on emerging e-business models and asset free web service providers who act as coordinator between supplier and buyer. Mechanism for sales tax and income tax application for such models should be placed for revenue generation.

1.09 MONITORING OF WITHHOLDING TAX U/S 161

In most of the notices for monitoring of withholding taxes, figures are taken from the financial statements and withholding agent is required to reconcile those figures with the payments. This lengthy exercise involves lot of time and resources of the taxpayers.

As per provision of Section 174 of the ITO, a taxpayer is required to maintain accounts and documents for six years after the end of tax year to which they relate. Since no time limit is prescribed in Section 161 of the ITO for monitoring of withholding tax, the taxpayers are receiving notices for the period beyond six tax years for which they are not obliged to maintain / retain records, which create hardship to the taxpayers furthermore, the field officers force recovery from the withholding agent despite the fact that the person from whom tax was to be withheld has already discharged his tax liability.

Since the taxpayers are filing withholding tax statements, same data should be used for monitoring, and notices should only be issued in case of material differences. Moreover, monitoring of one year should be carried out at one time and a time limit be provided in Section 161 of the ITO for monitoring of withholding taxes. It is recommended that time limit of 5 years should specifically be provided under the Income Tax Ordinance, 2001 for carrying out exercise of monitoring of withholding taxes.

Although section 161(1B) exists, application of section 162 of the ITO should be mandatory for field officers before invoking section 161 of the ITO. Following amendments in section 161(1) of the ITO are proposed:

"The person shall be personally liable to pay the amount of tax to the Commissioner who may pass an order within a period of five years from the end of the financial year in which the payment was made, after ensuring that provisions of sub-section (1B) are not met."

Monitoring of withholding taxes is to be used as deterrent and not as revenue measure. This kind of exercise also results in harassment and unethical practices, which can be avoided.

1.10 AUTOMATED TRASNFER OF SALES TAX DRAW BACK TO THE ACTIVE TAXPAYERS

The 5% draw back of the sales tax of Tier-1 retailers must be directly credited to the bank accounts of the Active Taxpayers to encourage all the shoppers to add invoices in the system. Simultaneously FBR must develop a system of automatically matching the invoices and report the variances. Any non-compliance shall be strictly punishable.

1.11 RESTORATION OF FBR PRIZE SCHEME SHOPPERS OF POS TIER-1 RETAILERS

LOW

FBR launched an appreciable prize scheme for the shoppers from POS-integrated Tier-1 retail outlets. Thousands of prizes worth hundreds of thousands of rupees were distributed among the shoppers through a computerized ballot, who opted to shop from POS integrated retail outlets spread all across the country. The scheme was much appreciated, as it increased compliance, however the scheme is currently suspended, and it is suggested that FBR should relaunch the scheme as it results in the culture of demanding sales tax invoices from retailers.

1.12 INCENTIVES FOR SPECIAL TECHNOLOGY ZONES

HIGH

The Special Technology Zones Authority (the Authority) was established to develop Pakistan's scientific and technological ecosystem through technology zones and acceleration of technology development in the country. The Authority brings together technology, industry, academia and Government services for national socioeconomic development and lays the foundation of Pakistan's knowledge economy of the future. Target technologies for promotion are primarily Biotech, Chemical technologies, Aggrotech, Fintech, Robotics, Nanotech, Edtech, etc.

Various tax incentives were extended by STZA to Zone Enterprises and Developers including exemptions from Income Tax, Sales Tax, Customs Duty, Property Tax and ease of maintaining of foreign currency accounts.

For effective implementation of incentives, relevant insertions were made in corresponding laws. However, certain amendments to the relevant laws were, inadvertently, missed which are proposed for incorporation in fiscal laws for harmonization with Incentives offered by the STZA Act:

(a) **Income Tax Withholding** - Since profits and gains derived by Zone Enterprises and Developers are exempt pursuant to Clause 126EA of Part I of the Second Schedule to the ITO'2001, therefore such entities should also be exempt from Withholding Income Tax. However, there is no specific provision in the ITO'2001 that allows an exemption to Zone Enterprises and Developers from the application of withholding provisions in respect of their receipts and expenditure. Resultantly, corresponding disclosures are needed under the provisions of Division II or III of Part V of Chapter X (i.e., from section 148 to section 158) and Chapter XII (i.e., from section 231AB to section 236Z) to grant exemption from Withholding Income Taxes to Zone Enterprises and Developers.

(b) **Sales Tax on services under Federal Excise Act, 2005, Islamabad Capital Territory (Tax on Services) Ordinance, 2001 & Provincial Sales Tax Acts** – Although section 21 of the STZA Act provides for exemptions from sales tax under the Sales Tax Act, 1990, no exemption is available either in the Federal or in the Provincial sales tax laws on services rendered. Accordingly, related additional disclosures are needed in the STZA Act for allowing sales tax exemptions on services in the Islamabad Capital Territory and Provinces to Zone Enterprises and Developers. In addition, similar corresponding disclosures are needed in the Federal Excise Act, 2005, the Islamabad Capital Territory (Tax on Services) Ordinance, 2001 and the Provincial Sales Tax Acts.

(c) **Sales Tax on supply of goods under the Sales Tax Act, 1990** - Corresponding disclosures to the extent of supply of goods and related services are needed in the Sales Tax Act, 1990 in line with section 21 of the STZA Act, providing requisite exemptions from sales tax to Zone Enterprises and Developers under the Sales Tax Act, 1990.

1.13 CHANGES IN WITHHOLDING TAX REGIME

HIGH

Credit of tax recovered under section 161:

Income Tax recovered by invoking section 161 from the withholding agent goes into the collection of FBR but:

- Credit of same is not available to the withholdee;

- Nor the withholding agent could recover the same from the withholdee, which is in total disregard to the provisions of section 161(2).

In view of decisions of the appellate forums including High Courts and Supreme Court that the tax officials have to identify the person from whom tax has not been deducted or collected in their orders under section 161. This makes it possible that the demand under section 161 should be deposited by the withholding agent in the same manner as he deposits the tax collected or deducted and the than the tax paid u/s 161 will be available to the withholdee for availing credit and in return the withholding agent could also recover the same from the withholdee.

Withholding Statements under section 165:

Section 165 and Rule 44, requiring furnishing of withholding statements are only in respect of transactions subject to WHT. On the other hand the data, details and information, to be provided in these statements are re-production of data, details and information already available and submitted in the withholding tax challans. Thus duplication of information and waste of resources on both sides.

In fact, the provisions of section 165 and Rule 44, needs to be otherwise for providing data, details and information about the transactions on which WHT has not been collected or deducted with reasons thereof. This will ensure a smooth process of monitoring and collection of tax not collected or deducted, by scrutiny of such statements.

Even, if some data, details or information currently required in the statements but missing in WHT Challan, could be incorporated in the Challan.

Exemption from withholding taxes:

- To obtain and retain the records of WHT is a nightmare for the withholdee's;
- On the other hand to collect or deduct tax on certain transaction is equally not possible for a withholding agent e.g., cash counter transaction, various port handling charges, …..
- In many cases on the one hand the withholdee is a collecting agent and on the same transaction the withholding agent is required to deduct tax e.g., Mobile Bills, Phone Bills, Internet Bills, …… And that too of petty amounts.

To coup with the above difficulties it is proposed that:

- At least following be exempt from withholding tax, other than final and minimum tax:
  - Petrol Pumps – Their taxation is already 100% covered u/s 156A, leaving no justification for further deduction of WHT from their sales u/s 153.
  - CNG Stations – Their taxation is already 100% covered u/s 234A, leaving no justification for further deduction of WHT from their sales u/s 153;
  - Mobile phone operators from their sales/services u/s 153
  - Landline phone operators from their sales/services u/s 153
  - Internet service providers from their sales/services u/s 153
  - Persons appearing on active taxpayer list from collection of tax from:
    - Mobile Bills U/S 236
    - Telephone Bills U/S 236
    - With token tax of vehicles U/S 234;
    - On purchase and/or registration of vehicles U/S 231B;

1.14 RATIONALIZING THE DEFINITION OF "PRESCRIBED PERSON" IN SECTION 153 TO PROMOTE CORPORATE FORMALIZATION

Section 153 of the Income Tax Ordinance, 2001 governs the withholding of income tax on payments made for the sale of goods, rendering of services, and execution of contracts. The withholding obligations, however, do not apply uniformly across all business structures. Instead, they

disproportionately burden companies through the definition of "prescribed person" under Clause (I) of Sub-Section (7) of Section 153, while exempting or limiting the scope for AOPs and sole proprietors, especially those operating outside the documented or registered economy.

A. Current Definition of "Prescribed Person" Under Section 153(7)(I)

As per the law, the following are treated as "prescribed persons" required to deduct withholding tax:

- Companies;
- AOPs whose turnover in any of the preceding two years exceeds Rs. 100 million;
- Individuals (sole proprietors) only if:
  a. Turnover in any of the preceding two years exceeds Rs. 100 million, and
  b. They are registered under the Sales Tax Act, 1990.

This definition means that all companies—regardless of size, turnover, or activity—are mandatorily required to act as withholding agents, while non-corporate entities can avoid this obligation by staying below the turnover threshold or remaining unregistered for sales tax.

B. Negative Impact on Ease of Doing Business and Corporate Growth

Unfair Compliance Burden on Companies:

- Micro and small companies (with even minimal turnover) are treated the same as large enterprises.
- Forced withholding, filing of monthly statements under Section 165, and audit exposure are all triggered—regardless of profitability or business activity.

Incentivizing Informality:

AOPs and sole proprietors can legally avoid compliance by keeping turnover below Rs. 100 million or not registering for sales tax. This creates a disincentive to incorporate, as incorporation brings with it an automatic and disproportionate tax burden.

C. Proposed Fiscal Reforms

To promote fairness, reduce the compliance gap, and encourage corporatization, the following reforms are proposed:

- Introduce Turnover-Based Threshold for Companies as Withholding Agents. Amend the definition of "prescribed person" in Section 153(7)(I)(i) to read:

"A company, other than a company whose turnover in any of the preceding two tax years does not exceed Rs. 100 million."

This would align the compliance obligation for companies with that of AOPs and individuals, providing relief to small corporate entities and startups.

Conclusion:

The current definition of "prescribed person" under Section 153(7)(I) creates a structural bias against corporate taxpayers, especially small companies, by enforcing uniform withholding responsibilities irrespective of size. Aligning these rules with those for AOPs and sole proprietors would level the playing field, reduce unnecessary compliance costs, and encourage businesses to transition into the documented corporate sector—thereby achieving a more robust and equitable tax base.

1.15 Reforming Section 150: Withholding Tax on Dividends to Encourage Investment and Corporate Growth

Section 150 of the Income Tax Ordinance, 2001 imposes a withholding tax on the gross amount of dividends paid by companies to shareholders. While aimed at ensuring tax collection, the current

structure under this section creates inefficiencies and discourages equity investments, particularly from foreign investors and within group companies. From an Ease of Doing Business perspective, it introduces an added layer of taxation on already taxed corporate profits and complicates inter-corporate transactions.

A. Key Issues in the Current Framework:

- Double Taxation of Profits:
  i. Companies pay corporate tax on profits, and then dividend distribution is taxed again at 15% under Section 150.
  ii. This leads to an effective tax burden exceeding 40%, discouraging reinvestment through equity financing.
- Deterrent for Foreign Investment:
  i. Non-resident shareholders are subject to 15% WHT unless they apply for DTA-based reduction.
  ii. The current DTA relief process is manual, time-consuming, and lacks transparency.
- Intercorporate Dividend Tax:
  Dividends from wholly-owned or majority-owned subsidiaries to holding companies are taxed again, creating disincentives for group-based business structures.

B. Proposed Fiscal Reforms:

- Exemption for Intercorporate Dividends:
  i. Amend Section 150 to exempt dividends paid by a subsidiary to its holding company if the holding company owns at least 50% of the shares and both entities are on the ATL.
  ii. This reform will support group structuring, reduce tax redundancy, and promote reinvestment.
- Reduced WHT Rate for ATL Shareholders:
  Reduce the withholding tax rate from 15% to 10% on dividends paid to domestic shareholders listed on the Active Taxpayer List (ATL), especially where the distributing company has no outstanding tax dues.
- Streamlined DTA Claim Process for Non-Residents:
  i. Establish an online DTA self-declaration system linked to Section 107, enabling non-residents to apply for treaty benefits and receive reduced WHT rates in real time.
  ii. Issue prescribed forms through FBR's portal with QR-code verification for compliance.

Conclusion:
Reforming Section 150 to reduce redundancy, simplify compliance for foreign investors, and eliminate structural biases in dividend taxation will ease the cost of capital, support corporate reinvestment, and make Pakistan's business environment more attractive to both local and international investors.

1.16 Proposal for promoting local industry through industry rebate and origin verification in Pakistan

Introduction
This proposal aims to accelerate the growth of Pakistan's local industries by implementing a targeted rebate system based on the percentage of local content in products procured and produced domestically. Inspired by successful models in the GCC countries, this approach will incentivize companies to prioritize local sourcing, thereby stimulating economic growth, creating employment opportunities, and increasing government revenues.

Objectives

- Encourage local sourcing: Promote procurement from local markets with at least 70-80% local content.
- Ensure transparency: Develop a robust origin certification and reporting system to verify local content.
- Provide financial incentives: Offer rebates based on the percentage of local procurement and manufacturing.
- Support local industries: Stimulate growth in raw material suppliers and related sectors.
- Generate employment: Create new jobs across multiple industries.
- Enhance government revenue: Increase tax collection through expanded industrial activity.

Impact Assessment & Expected Benefits

Scenario	Local Sourcing & Procurement Content	Total Market & Procurement Value	Estimated Economic Impact
Baseline	30%	$1 Billion	Current industry status, limited growth
Proposed	70-80%	$2.5 Billion	150% growth in local market activity and industry size

Economic Advantage

Job creation: Approximately 15,000 new jobs for every 10% increase in local procurement.
Tax revenue: An additional PKR 50- billion annually.
GDP growth: Potential 1-2% increase over 3-5 years, significantly boosting national economic indicators.

Rebate Slabs & Incentives

Slab / (Objectives)	Local Content & Procurement Percentage	Rebate Rate	Approximate Financial Benefit
Slab 1 (Encourage initial shift towards local sourcing)	60%	5-7%	Moderate incentive to promote local procurement
Slab 2 (Drive higher local procurement levels)	70%	10-12%	Stronger incentive to boost local market activity
Slab 3 (Achieve full utilization of local content)	80%	15-20%	Maximize local sourcing and industry growth

Rebate Calculation Formula

The rebate amount can be calculated using the following formula:
Rebate Amount = Procurement & Production Value × ((Local Content Percentage − Minimum Threshold) / 100) × Rebate Rate
Example:
Procurement & Production Value: USD 1,000,000
Local Content Percentage: 75%
Minimum Threshold: 60%
Rebate Rate: 15%

Calculation:

Rebate = USD 1,000,000 × ((75 − 60) / 100) × 0.15
Rebate = USD 1,000,000 × 0.15 × 0.15
Rebate = USD 22,500
This calculation incentivizes companies to increase their local procurement and production beyond the threshold, fostering growth of the local market.

Focus on Local Market Procurement & Its Impacts

Rather than primarily emphasizing exports, this proposal centers on encouraging procurement from local markets. The key benefits include:
Increased Local Demand: Higher purchases from local suppliers stimulate domestic industries.
Cost Savings: Reduced reliance on imports can lower costs and improve margins for local suppliers. At national level, it may tend to decrease the imports in the long term.
Development of Supply Chains: Strengthening local supply networks enhances resilience.
Financial Incentives: Companies sourcing domestically will be eligible for rebates, making local procurement more attractive.
Employment Opportunities: Increased local procurement leads to job creation in procurement, logistics, and manufacturing sectors.
Trade Balance Improvement: Reduced import dependency helps improve the trade deficit.

Expected Benefits of Local Procurement

- Elevated purchasing from domestic suppliers.

- Growth of local raw material industries.
- Creation of new jobs.
- Greater economic resilience and reduced import dependence

Origin Certification & Reporting System

To ensure transparency and compliance, the following steps will be implemented:

- Origin Certification: Suppliers will provide official documents verifying local sourcing.
- Documentation: Purchase invoices, bills, and certification certificates will be maintained.
- Verification: An independent agency will audit and verify the authenticity of local content claims.
- Certification Number: Each verified claim will be assigned a unique, traceable certification number.

This system will facilitate smooth rebate claims, build stakeholder trust, and ensure genuine local procurement effort.

Multiplier Effect on Exports

Once the local industries are strengthened through increased procurement and investment, a positive multiplier effect on exports will naturally follow. As domestic manufacturers expand and improve quality standards to meet both local and international demands, they will become more competitive in global markets. This enhanced competitiveness can lead to increased export volumes, opening new avenues for foreign exchange earnings. Moreover, a robust local industrial base will attract foreign direct investment (FDI) and foster technological advancements, further boosting export capacity. The combined effect of a thriving local industry and improved export performance will create a sustainable cycle of economic growth, employment generation, and increased national revenue, reinforcing Pakistan's position in the global marketplace.

Conclusion

Implementing a structured rebate program centered on local procurement, supported by a reliable origin certification system, will significantly enhance Pakistan's industrial growth. It will create employment, increase government revenues, and promote sustainable economic development.

Please note that due to limited statistical data availability, fictitious figures/suppositions are taken to elicit the impact on economy.

We seek government support to integrate these policies into the national industrial strategy and to develop the necessary infrastructure for effective implementation.

Next Steps

- Finalize detailed policy thresholds, rebate rates, and certification procedures.
- Develop an electronic platform for origin reporting and verification.
- Train auditors and inspectors for compliance.
- Launch pilot programs to evaluate effectiveness before a full-scale rollout.

Please note that due to limited statistical data availability, fictitious figures are taken for the impact on economy.

EASE OF DOING BUSINESS (EODB) – PROVINCIAL TAXES

2.01 ISSUES RELATING TO INPUT TAX ADJUSTMENT

i) TIME LIMIT TO CLAIM INPUT TAX BEFORE COMMENCEMENT OF BUSINESS

MEDIUM

SECTION 15A(1)(I) OF THE SINDH SALES TAX ON SERVICES ACT, 2011 ['SSTSA']; SECTION 16B(1)(I) OF BALOCHISTAN SALES TAX ON SERVICES ACT, 2015 ['BSTSA']; SECTION 17(1)(i) OF KHYBER PAKHTUNKHWA SALES TAX ON SERVICES ACT, 2022 ['KSTSA']

Currently, input tax is not allowed on goods or services procured or received by a registered person during a period exceeding six months prior to date of commencement of the provision of taxable services by him.

It is proposed that in case of large projects, where the installation and commissioning into service takes longer, the time limit for claiming input tax be allowed from the date of commencement of project to the date of commissioning into service.

Rationale

Bar on admissibility of input tax borne by the taxpayer prior to six months preceding the commencement of provision of taxable services is not justifiable in case of large projects having longer set up time with no visibility of subsequent taxation of their services.

ii) INPUT TAX ADJUSTMENTS

MEDIUM

SECTION 15A OF SSTSA; SECTION 16B OF SECTION 16(1) OF PUNJAB SALES TAX ON SERVICES ACT, 2012 ['PSTSA']; SECTION 16B OF THE BSTSA & SECTION 17 OF THE KSTSA

A registered service provider has been prevented from claiming or deducting input tax paid on the goods or services including but not limited to goods and services subject to tax at fixed or specified rate, sales tax paid on building material, office equipment etc. Similarly, 'further tax', 'extra tax' and value addition tax levied under the Sales Tax Act, 1990 ['STA'] is also barred from adjustment under the provincial sales tax laws.

It is proposed that the aforesaid provisions relating to input tax adjustment should be harmonized and revamped. In most of the cases, 'further tax' and 'extra' tax is charged under STA for the reason that the recipient of supplies (being a service provider) is not a registered / active person under STA. Since 'further tax' and 'extra tax' is levied merely due to procedural limitation that service provider is not registered / Active under STA; such taxes should be allowed as input tax adjustment.

Rationale

This will bring harmony between the federal and provincial tax laws as well as reduce the cost of doing business. The harmony among the sales tax statutes would reduce the litigation. The harmonization would enhance the application of Value Addition Tax ['VAT'] regime which ultimately eliminate cascading effect.

iii) VALUE ADDITION TAX AT IMPORT STAGE

MEDIUM

SECTION 15A(1)(D) OF SSTSA; SECTION 16B(1)(R) OF PSTSA; Section 17(1)(E) OF KSTSA. & SECTION 16B(1)(D) OF BSTSA

The existing provisions of laws restrict or disallow the input tax claim on value addition tax paid on import of goods (used for rendering of services) under the STA or sales tax paid on taxable goods. Under the STA, the levy of Minimum Value Addition tax ['MVAT'] has been exempted for registered service providers. However, because of the wording of the law, it seems that service providers are

subject to MVAT in certain situations.

Whilst we consider that harmonization of sales tax laws across provinces is more likely to address the above issues, meanwhile, it is proposed to withdraw the provision restricting admissibility of minimum value addition tax paid on goods at import stage where the goods are consumed or used in the process of rendering of services.

Rationale

It is unjust to put a restriction on input tax as it is against the true spirit of Law & Justice and also increases the cost of doing business.

2.02 JOINT AND SEVERAL LIABILITY OF REGISTERED PERSONS IN SUPPLY CHAIN WHERE TAX IS UNPAID

LOW

SECTION 18 OF SSTSA; SECTION 19 OF PSTSA; SECTION 22 OF KSTSA; SECTION 19 OF BSTSA

The Provincial Statutes stipulate that where a registered person, receiving a taxable service from another registered person, is in the knowledge of, or has reasonable grounds to suspect, that some or all of the tax payable in respect of that taxable service or any previous or subsequent taxable service provided would go unpaid, both the recipient and provider of the taxable service shall be jointly and severally liable for payment of such unpaid tax.

These provisions are against the basic rights of genuine taxpayers who are held responsible for any non-compliance or tax evasion by another person. It is proposed that the provision should be aligned with Section 8A of STA where the burden of proof that the service provider and service recipient acted in connivance rests upon the tax authorities.

Rationale

This will bring harmony between the federal and provincial sales tax laws. This would protect the genuine taxpayers and would also restrain the assessing officer from using the power hastily without carrying out proper enquiry.

2.03 ASSESSMENT OF TAX

LOW

SECTION 23(5) OF SSTSA; SECTION 24(5) OF PSTSA, SECTION 24 (5) OF BSTSA & SECTION 27(8) OF KSTSA

Currently, the law provides that any assessment order can be amended by directly issuing a show cause notice by the tax officer on the basis of any subsequent information, etc.

It is proposed to shift the power of amendment of an assessment order to the Commissioner or with the approval of Commissioner or Board, as the case may be, with the condition that proceedings shall be initiated based on possession of some definite information (which should be explicitly mentioned in the notice) and a show cause notice should be issued only when there is a substantial evidence available with the officer that warrants reopening or amendment of an assessment order.

Rationale

This is necessary to introduce transparency in the system and provide justice to the taxpayer and save precious time of both the department and the taxpayer. This will also result in reducing the cost of doing business.

2.04 AUDIT

LOW

SECTION 28 OF SSTSA; SECTION 33 OF PSTSA, SECTION 33 OF BSTSA & SECTION 37 OF KSTSA

Under Provincial Sales Tax laws, any officer not below the rank of Audit Officer may initiate audit proceedings on its own without assigning any reason. It is proposed that in line with established good practices self-assessment scheme is required to be introduced in true spirit and additionally, the power to select a case for audit should be vested in officers not below the rank of Commissioner.

Further, it should be mandatory to record the cogent reasons for selection of cases for audit as well.

Further, currently laws do not prescribe any timelines for completion of audit, it is proposed that a timeline of six months for completing the audit proceedings should be prescribed under the law. However, for complex audits or under compelling circumstances a provision allowing for extension of this time by the Commissioner after recording reasons in writing may also be incorporated.

Rationale

Core feature of any self-assessment scheme in tax law is that the sanctity of declarations by taxpayers are acknowledged to the maximum possible level and which can only be audited under certain special circumstances (e.g. apparent misdeclaration, definite information which is inconsistent with the declaration etc.). Further segregation of powers to select audit from conducting authority will bring transparency in the process.

Further defined timelines will ensure that audits are conducted efficiently and concluded within reasonable time facilitating timely resolution of disputes and collection of revenue.

2.05 CERTIFICATE BY THE AUDITORS

LOW

SECTION 31(5) OF PSSTA; SECTION 35(5) OF KSTSA; SECTION 31(5) OF BSTSA

The registered service providers, whose accounts are subject to audit under the Companies Act 2017, are required to submit a copy of the annual audited accounts along with a certificate by the auditors certifying the payment of the tax due and any deficiency in the tax paid by the registered person.

As per section 26(5) SSTA, requirement of certification from the auditor has been removed which is in line with the legal framework of the auditor of the audited financial statements. Similar amendments are required in other provincial laws.

Rationale

With the current scope of statutory audit, the auditor is not obliged to certify the payment of the sales tax due and any deficiency therein. There are provisions available in the sales tax laws which allow the revenue authorities to appoint independent auditors to conduct sales tax audits.

2.06 RETURN REVISION

LOW

SECTION 35(6) OF PSTSA; SECTION 39(6) OF KSTSA; SECTION 30(6) OF SSTSA & SECTION 35(6) OF BSTSA

Currently, under SSTSA, a return can be revised by a taxpayer within 120 days of filing of original return without seeking permission from the commissioner. However, under other provincial sales tax laws, prior permission is required to be sought from the commissioner and there is no time limit provided for passing of an order on an application filed by the taxpayers' seeking approval for filing of revised return. This causes delay in passing of the revision order and also delay in filing of subsequent returns, and subsequent removal of name of taxpayers from the list of active taxpayers.

It is proposed that conditions for seeking the permission should be abolished in all other provinces and taxpayers should be allowed to revise the return within 120 days of filing of the original return. Condition for seeking the permission should be applied where return is required to be revised after elapse of 120 days of filing of original return and specific timelines should be prescribed in the laws wherein the order needs to be passed and if no such order is passed within such timelines on the application, then the same should be considered as deemed approved.

Rationale

Relaxation in revision of return would ease the compliance as taxpayers may correct inadvertent mistakes or errors in the returns. Similarly, fixation of timeline for passing of revision order would greatly help in preventing delays in filing of subsequent returns.

2.07 OBLIGATION TO PRODUCE DOCUMENTS AND PROVIDE INFORMATION

MEDIUM

SECTION 52(1) OF SSTSA; SECTION 57 OF PSTSA, SECTION 57(1) OF BSTSA & SECTION 61 OF KSTSA

The tax officer is empowered to solicit any information or record from any person without specifying any reason and without specifying the reference of any case being investigated by him.

It is proposed that the scope of above referred sections should be restricted to specific parties and transactions already identified by the tax authorities. Powers to seek unrestricted information is tantamount to an act of fishing and roving which practice is deprecated by superior courts.

Rationale

This will put a restriction on fishing enquiries and unnecessary probe into the tax affairs of a person.

2.08 TAX EXEMPTIONS OR ZERO RATING FOR CHARITY

LOW

Currently, the provincial sales tax statutes do not have any provision to allow zero-rating, concession or exemption from payment of sales tax to persons engaged in running charity, social welfare organizations, trusts, hospitals, schools and similar nonprofit organizations.

In line with the Government's overall policy for health and well-being of the citizens of Pakistan, it is suggested that the services provided or rendered to nonprofit organizations should be zero-rated or exempted under the provincial sales tax laws. The said relief should at least be provided to the organization which have already been exempted by the Federal Government, subject to certain conditions. On similar basis, exemption can be provided by the provincial sales tax authorities.

Rationale

This will enable the social sector to spend more on the social welfare activities instead of spending on the taxes which increases the cost of services/facilities to the general public.

2.09 E-HEARING AT THE LEVEL OF COMMISSIONER APPEALS / APPELLATE TRIBUNAL

MEDIUM

RULE 10 OF PUNJAB SALES TAX ON SERVICES RULES (ADJUDICATION AND APPEALS) RULES, 2012 ['PSTAAR']; RULE 157 OF BALOCHISTAN SALES TAX ON SERVICE RULES ['BSTSR'] & RULE 57H OF SINDH SALES TAX ON SERVICES RULES ['SSTSR']AND RULE 32 OF KYBER PAKHTOONKHAWA SALES TAX ON SERVICES (REGISTRATION) REGULATION ['KPSTSR']

The facility for e-hearing of appeals is currently available for appeals filed to Commissioner Appeals. Similar e-hearing facility should be extended for hearing before the Appellate Tribunal.

Rationale

This will not only make the appeal process efficient and less costly, but also greatly help in deciding appeals expeditiously.

2.10 MINIMUM THRESHOLD FOR REGISTRATION

LOW

Currently, the provincial sales tax laws do not prescribe a minimum taxable threshold for small service providers. This issue has been partly addressed by issuing Notifications by Sindh. For instance, construction services, workshops for electric or electronic equipment and automobile washing services where annual turnover does not exceed Rs. 4 million in a financial year and auto-workshop services whose turnover does not exceed Rs. 4 million in a financial year, are exempt from the chargeability of Sindh Sales Tax. Punjab has also prescribed a minimum threshold for restaurant services coupled with other conditions. Other provinces have not aligned their laws in this regard. It is proposed to introduce a uniform minimum taxable threshold for small service providers by all provinces within the statute, rather than through Notifications. The threshold can be defined considering the threshold prescribed for exempt income under the Income Tax Ordinance, 2001 which would rationalize the scheme of exemption. The minimum threshold can also be coupled with

other conditions for instance, installation of digital payment systems.

It is proposed to introduce a uniform minimum taxable threshold for small service providers by all provinces within the statute, rather than through Notifications.

Rationale

This is necessary to provide relief to small service providers across the provinces and to achieve harmonization. Furthermore, exemption will enable the department to put focus on big revenue streams. It would also help to enhance documentation of the economy whilst providing concession / relief to small businesses.

2.11 SALES TAX ON SERVICES RELATING TO E-COMMERCE / E-BUSINESS OR DIGITAL ECONOMY

MEDIUM

E-commerce or E-business is getting momentum and such activities are conducted throughout Pakistan using a digital platform located either outside Pakistan or in one of the provinces in Pakistan, but taxation of their services may not be fully captured. A question also arises with reference to determination of place of such businesses, its jurisdiction and allocation of revenue.

It is proposed that the provincial revenue authorities should get together and agree to the following steps for introducing provisions for taxation of services under e-commerce or e-business:

a) a detailed mechanism for capturing such services in the tax net by the province in which digital platform is located for services provided from within Pakistan and through banks and financial institutions for services rendered from digital platform located outside Pakistan;
b) fair allocation of tax so collected among the provinces based on a formula; and
c) filing of a single return by the service providers located in Pakistan in line with the newly introduced sales tax return by FBR.

Rationale

Unless the Provinces agree to be together on capturing such services and the distribution formula based on a single return filed by the service providers, the services provided through digital platform from within and outside Pakistan may largely remain untaxed by creating confusion whether they are taxable by provincial or federal tax authorities.

2.12 INTEGRATION OF POS SYSTEM AMONG THE TAX AUTHORITIES

HIGH

Currently FBR and provincial sales tax authorities have implemented Point of Sale (POS) system on specified categories of taxpayers. Such POS systems are operated in isolation by each province & FBR and not integrated through a common platform / application.

FBR and provinces should coordinate to introduce a single POS network to record sales for both income tax and sales tax purposes. This may not only result in expansion of the tax base but would also result in ease of doing business, simplicity and consistency in taxation laws. Similarly, the scope of POS should be extended to other services to capture the taxable services.

Rationale

Synchronization of the POS system would enable the tax authorities to track the potential tax revenue. It will also be cost effective as data redundancy would be minimized. Extending the scope of POS would capture the potential tax revenue using technology.

2.13 AUTOMATIC STAY FOR RECOVERY OF TAX ARREARS

MEDIUM

SECTION 70 OF PSTSA; SECTION 66 OF SSTSA & SECTION 72(1) OF BSTSA

The current law requires for deposit of 10% (under the PSTSA and SSTSA) and 25% (under the BSTSA) of the disputed demand for automatic stay against recovery of the remaining tax demand (90% or 75%, as the case may be) until the appeal is decided by the Appellate Commissioner. However, it

does not provide any mechanism for refund of the tax deposited if the demand is extinguished or curtailed to below 10% or 25% (as the case may be).

It is proposed to delete this condition and allow automatic stay without any payment of disputed tax until the appeal is decided by an independent appellate authority. Alternatively, the condition for payment of disputed tax demand should be relaxed to 10% for automatic stay against recovery of balance tax demand till the decision of the Appellate Tribunal. Furthermore, there is no such provision available in the KSTSA, therefore, the same should also be introduced to safeguard the interest of the registered person.

Rationale

The payment of tax demand during pendency of appeal causes grave hardships to the taxpayers and it is contrary to legal judgments where it is held that the disputed tax demand should not be recovered unless it has been reviewed by at least one independent forum. Furthermore, if an appellant deposits partial demand (i.e. 10% or 25% as the case may be) and subsequently the issue is decided in his favor and demand is extinguished, the mechanism of refund should be introduced so that the amount deposited can be refunded.

2.14 REFUND OF EXCESS INPUT TAX

HIGH

RULE 23A OF SSTSR; RULE 29 OF BSTSR; SECTION 19 OF KPSTSA AND SECTION 16 & Rule 3 OF PSTSA & THE PUNJAB SALES TAX ON SERVICES (REFUND) RULES, 2019 ['PSTSRR';]

The existing law does not cater for refunds arising from the following situations:

a) *excess input tax not adjusted against tax liabilities of twelve consecutive months [other than Sindh]; and*
b) *tax withheld in excess of net tax liability for the relevant tax period and remained unadjusted against tax liabilities of twelve consecutive months.*

It is proposed to align the refund related provisions with those applicable in case of sales tax on goods under the STA.

Rationale

This amendment is necessary for adoption of best practices and harmonization of sales tax laws.

2.15 REIMBURSEMENT OF EXPENSES / COST

HIGH

The provincial sales tax laws do not provide the concept of reimbursement of expenses / cost. In the absence of provisions of reimbursement, the charge of sales tax becomes abnormally high. The concept of reimbursement should be introduced in the provincial sales tax laws.

In addition to the above, labor and manpower services and security services are performed through a reimbursement model under which salaries are reimbursed on a cost to cost basis which are clearly identifiable in a transaction. The Supreme Court of Pakistan has also upheld the earlier decision of Sindh High Court wherein it was held that sales tax cannot be levied on the portion of salary being reimbursed as per actual cost. Laws should be amended to incorporate the effect of decisions of superior courts which would not only help to enhance compliance level but would also reduce the litigation.

Rationale

The concept of reimbursement would reflect the economic rationale of a transaction whilst encouraging the services provider to obtain registration. The introduction of specific provisions of reimbursement would not result in loss to the exchequer.

2.16 RENTING OF IMMOVABLE PROPERTY

LOW

The concept of sales tax on renting of immovable property is available under SSTSA & BSTSA. In Sindh, the levy of sales tax on renting of immovable property remained a matter of dispute The Supreme Court of Pakistan has also subsequently decided in favor of taxpayers.

The levy of sales tax should be removed in the light of the decision of superior courts.

2.17 BAR CODE ON ALL NOTICES AND ORDERS

LOW

Currently, the requisition, notices and orders are issued without system generated Bar Codes, whereas this system is implemented by the FBR in case of income tax with effect from July 1, 2015 read with direction dated January 28, 2021 which appears to be for Sales Tax and FED too.

It is proposed that necessary amendments should be made in the respective provincial sales tax laws and Islamabad Capital Territory (Tax on Services) Ordinance, 2001 ['ICT'] for mandatory barcoding on service of requisition, notice and order.

Rationale

Implementation of the bar code system will strengthen the controls over the issue, delivery and action on the requisition, notices and orders, both by the tax collectors and taxpayers.

2.18 ISSUE OF DRAFT SROs

LOW

Currently, the SRO / Notifications under the Provincial Sales Tax laws are issued without publication of draft for comments of the stakeholders. Similarly, the SROs / Notifications are published after the effective date and not uploaded on web-portals timely which result in practical impediment to comply with the said SROs / Notifications.

It is proposed to introduce new sections in the Provincial Sales Tax on Services laws as well as under the Islamabad (ICT) Sales Tax on Services laws for publication of draft SROs for comments of stakeholders before their implementation.

It is also proposed that once the SRO / Notification is finalized, it is immediately uploaded on the web-portal whilst simultaneously publishing the same in official gazette.

Rationale

The issue of SROs without publication of drafts for seeking comments is against best practices. Similarly, delayed publication of SRO / Notifications creates practical difficulty in compliance.

2.19 RECTIFICATION OF MISTAKE/ CORRECTION OF CLERICAL ERRORS

LOW

Presently all provincial laws envisage a provision whereby errors of only clerical or arithmetical nature could be corrected by tax officers. It is recommended that such provisions be substituted with a comprehensive provision aligning it with para-Materia provision of Sales Tax Act, 1990 whereby any mistake apparent from record can be rectified by the concerned tax officers.

Rationale

It will reduce the tax litigation burden on taxpayers as well as department.

2.20 ADVANCE RULING AUTHORITY

LOW

Realizing the complexity and dynamic nature of modern economic transactions where businesses face uncertainty regarding the tax implications on their economic activity various countries around the globe have incorporated the concept of "Advance Ruling" in indirect tax laws. Advance rulings offer a preemptive resolution to these uncertainties, providing taxpayers with clarity and legal

certainty about the tax treatment of prospective transactions.

It is proposed that in line with the global best practices comprehensive enabling provision be introduced in all the provincial laws for empowering respective tax authorities to issue "advance ruling" to taxpayers.

Rationale

This will not only enhance compliance and reduce disputes between taxpayers and tax authorities but also facilitate international trade by offering predictable fiscal outcomes.

2.21 REDUCE RATE OF 5% WHERE PAYMENT IS RECEIVED THROUGH CREDIT OR DEBIT CARD TO PROMOTE DOCUMENTATION OF ECONOMY

The Punjab Revenue Authority charge/collect sales tax at reduced rate of 5% from restaurants if payment is made through debit or credit card (Entry # 11 of Second Schedule of Punjab Sales Tax on Service Act, 2012). Similar benefit is available under S.No.1 of Table I of the ICT and Rule 42(b) of the SSTSR.

It is proposed to add similar provisions in other provincial sales tax laws to promote documentation of the economy which will also improve tax collection.

Rationale

The incentive of payment through digital means would enable the tax authorities to capture the data of transactions efficiently. Furthermore, implementing a reduced rate would alleviate the concerns of tax-compliant businesses regarding price competitiveness compared to non-compliant businesses.

BROADENING OF TAX BASE

PART-V
BROADENING OF TAX BASE

REFERENCE INDEX

BROADENING OF TAX BASE

As of 2025, Pakistan's population is estimated at approximately 255 million. Despite this, only about 4.9 million individuals filed income tax returns for the tax year 2024. This low compliance rate is attributed to factors such as a significant trust deficit between taxpayers and tax authorities, ineffective utilization of resources by tax collectors, and a lack of political will to broaden the tax base.

In an effort to modernize the tax system, the Federal Board of Revenue (FBR) has initiated steps to transition from manual record-keeping to automation. This shift has resulted in the accumulation of substantial data. However, the FBR has faced challenges in effectively leveraging this data to increase the number of income tax return filers and, consequently, tax revenues. A significant hurdle identified is the insufficient focus on enhancing the competence and capacity of field officers, which hampers the effective utilization of available data.

Historically, efforts to widen the tax base have been limited. Instead of expanding the taxpayer pool, authorities have often increased the tax burden on existing compliant taxpayers. This approach includes raising tax rates on the same taxable activities and imposing restrictions on the deductibility of legitimate expenditures, often under the guise of audits. Such policies have led to increased pressure on law-abiding taxpayers and have, in some cases, incentivized tax avoidance practices.

To address these challenges, the following measures are proposed:

Data Analysis of High Value Transactions: Assign dedicated personnel to analyze information related to the acquisition and sale of properties, vehicles, and the development of high-value real estate projects. This analysis should be conducted in collaboration with the revenue department, leveraging the mandatory use of Computerized National Identity Cards (CNICs) in major transactions.

Banking Transaction Monitoring: Establish specialized teams, potentially comprising newly inducted or outsourced finance professionals, to scrutinize banking transactions of individuals with significant financial activities. This initiative aims to identify tax evaders through the detection of substantial payments and receipts.

Lifestyle Audits: Implement measures to identify individuals engaging in high-expenditure lifestyles, such as membership in exclusive clubs, enrollment of children in expensive educational institutions, and utilization of premium medical facilities. These individuals should be brought into the tax net through targeted outreach and compliance initiatives.

Additionally, to foster a culture of compliance and reduce the trust deficit, the following strategies are recommended:

Incentivization: Offer incentives to both existing and new taxpayers to encourage timely and accurate tax filings.

Digital Engagement: Develop and enhance online platforms to facilitate efficient and effective communication between taxpayers and tax authorities.

Public Awareness Campaigns: Launch media campaigns to educate the public about the importance of tax compliance and the benefits of a broadened tax base.

Anti-Corruption Measures: Implement stringent measures to eradicate malpractices within the tax collection system, thereby enhancing the credibility of the FBR and building public trust.

By adopting these measures, the FBR can work towards increasing the number of taxpayers, enhancing revenue collection, and restoring public confidence in the tax system.

1.01 REACTIVATION OF BROADENING OF TAX BASE DIRECTORATE

HIGH

The Directorate General of Broadening of Tax Base, established under section 230D of the Income Tax Ordinance, 2001, remains largely non-operational in practice. It is crucial to reactivate this Directorate by introducing innovative measures, including outsourcing specific investigative functions to specialized external agencies or organizations operating in Pakistan.

To facilitate this, the Federal Board of Revenue (FBR) should invite proposals from interested and qualified agencies to conduct taxpayer identification activities. These agencies must demonstrate their methodologies for effectively identifying new potential taxpayers who have taxable income but are currently outside the tax net. Such agencies should receive remuneration directly linked to the number of new taxpayers identified and the additional revenue collected. This approach not only boosts revenue collection but also prevents increased fixed administrative costs, thus avoiding additional burdens on the national exchequer. Outsourcing this function will also relieve the overstretched FBR personnel, allowing them to focus better on core administrative duties.

Additionally, the Directorate General of Broadening of Tax Base should proactively acquire and analyze extensive financial and non-financial data already available with various national and provincial authorities. These datasets include, but are not limited to:

- Withholding tax information provided by banks, including data on cash withdrawals exceeding specified limits and credit card transactions.
- Withholding tax data collected from mobile phone users.
- Data related to withholding tax on electricity bills.
- Information on bank account holders, covering import/export transactions and profit distributions.
- Property registration and real estate transaction records, including data related to construction activities.
- Vehicle registration details and related financial transactions.

To operationalize the use of this data effectively, the FBR should empower the Directorate General by developing a structured mechanism for assessing non-filers based on collected information. The suggested framework includes:

- Defining clear criteria for identifying potential taxpayers who have not yet filed returns.
- Conducting provisional assessments of identified non-filers.
- Forwarding these cases to the relevant tax commissioner for further processing.
- Ensuring an opportunity for the non-filers to present their case and provide required documentation.
- Completing assessments using the best available information if responses or supporting documents are not received.
- Issuing compulsory National Tax Numbers (NTNs) to eligible non-filers in line with Section 114 of the Income Tax Ordinance, 2001.

This comprehensive approach will significantly enhance the effectiveness of the Directorate General, enabling efficient utilization of existing data, expanding the taxpayer base, and contributing positively to overall tax compliance and revenue collection.

1.02 REAL-TIME REPORTING OF SOCIETIES / BUILDERS FOR PROPERTY SALE / TRANSFER

HIGH

It is proposed that housing societies/developers/builders engaged in selling of plots, building unit should integrate their systems with FBR on same mechanism as POS integration and share real time transfer of file/plot/building/building unit. etc. Such information should be transferred to Broadening of Tax Base department so as to analyze the information and crossmatch the same with wealth statements and tax returns of buyers and sellers. Further FBR should modify its tax returns and wealth statements format to allow for standardized property declaration mechanism to ease matching of the property details for the field officers and calculation of capital gains.

1.03 NATIONAL TAX NUMBER REQUIREMENT FOR CERTAIN SERVICES / FACILITIES FROM GOVERNMENT / SEMI GOVERNMENT / PRIVATE ORGANIZATION

HIGH

It is proposed that compulsory NTN be issued to persons using following facilities if they are non-filer in accordance with Income Tax Ordinance, 2001 and such services should not be provided unless they become filer:

- Issuance/renewal of passport;
- Commercial/industrial electricity, gas and water connection;
- Three phase residential electricity connection;
- Sale and purchase of vehicle/motor bike;
- Transfer/purchase of properties;
- Foreign travel; and
- Membership of renowned clubs.

Exceptions may be given to:

- Non-residents not required to file return u/s 114 of Income Tax Ordinance, 2001;
- Education/medical purposes;
- Dependent ladies/ widows;
- Pensioners; and
- Persons under 21 years of age, in these cases tax return of sponsor is required.

1.04 WHISTLE BLOWING

MEDIUM

The Whistle Blower protection concept was initially introduced through Whistle Blower Protection and Vigilance Commission Act, 2019 published on November 01, 2019. But there have been no fruitful results due to deficit of trust.

Therefore, it is proposed to reinforce the concept that if any person comes forward and provides any information with respect to tax evasion/inconsistency/tax fraud then complete anonymity should be granted to that person. No information should be available to any field officer of FBR relating to the whistle blower. Whistle Blower should be considered for reasonable reward from the tax recovered by directly crediting into his/her bank account. FBR should also incorporate this feature in Tax Asaan App for use.

1.05 REFUNDS TO SALARIED INDIVIDUAL

MEDIUM

It is proposed that refunds created for salaried individuals below or equal to the amount of Rs. 300,000/- should be directly credited to their bank accounts without any application for refunds, on

basis of refund showing in annual tax return provided that such refund amount is readily verifiable, and taxpayer is provided option to upload evidence of taxes paid. The timeframe for the refund is proposed to be six months from the date of filing of tax returns.

1.06 FIXED INCOME TAX REGIME FOR SMALL RETAILERS

The retail sector in Pakistan has been amongst the fastest growing markets, contributing almost 20% to the national GDP. It is the third largest sector of the country and the second highest employer, employing 15% of the labor force. Pakistan has millions of retailers, majority of which represents the FMCG trade and other general trade channels, including but not limited to kiryanas, general stores, medical stores, supermarkets, hypermarkets, etc. With the fifth highest population in the world, there is massive potential in the market due to ever-increasing consumerism. Sales in the retail sector in Pakistan have nearly doubled in the last 10 years.

There should be categorization of small retailers on the basis of location and area. FBR has already started working on tapping tier 1 retailers and furthermore, in recent development a fixed income tax regime has been introduced for small retailers called Tajir Dost (Special) Procedure, 2024. However, the manner for calculation of monthly advance tax under these procedures are yet to be prescribed by FBR. It is proposed that such manner for calculation should be prescribed earliest so that fixed income tax regime can be implemented in its true spirit.

1.07 CAPACITY BUILDING OF REVENUE AUTHORITIES

Tax Laws applicable in Pakistan are complex in nature and require a detailed study and understanding before application in different scenarios, therefore, it requires qualified persons with an aptitude to understand and comprehend such laws. Hence, FBR should ensure that it employs persons with relevant knowledge of tax, accounting and auditing laws/rules to ensure the accuracy and completeness of the system.

Furthermore, FBR should train its new employees/officers for a period of six months before assigning them any specific tasks to ensure that they have relevant knowledge and experience to meet the requirements of specific scenarios.

In addition, FBR should plan and implement trainings of existing employees to ensure that they are updated about any amendments or changes in requirements/laws/rules so that they respond accordingly.

1.08 MEDIA CAMPAIGNS AND INCENTIVES TO TAXPAYERS/FILERS

One of the reasons for low number of tax returns filers is the working style of the tax authorities towards the existing taxpayers due to which people prefer to remaining non filer even by paying higher taxes which is evident from insubstantial increase in the number for filers after introducing the concept of non-filers and active taxpayers. The following measures need to be taken:

- Implementation of self-assessment scheme in the true spirit;
- Selection for audit should be through "risk based automated tools";
- Rationalizing the existing tax rates; and

Previously, media campaigns have been conducted by FBR to raise awareness on tax return filing, which have been effective to significant level. Furthermore, engagement of people in POS prize scheme has also proved to be fruitful.

It is suggested that media campaigns should be conducted which are not limited to tax return filing but also broadening the tax base. These campaigns should focus on tax facilitation/incentives that shall be provided to existing and new taxpayers.

The incentives shall be as follows;

- Recognition for high taxpayers (Top 100 to 1000);

  - Representation at certain public offices/ committees;
  - Priority at Airports, Public Amenities, Healthcare and Govt. Offices; and
- Reintroduction of tax rebate on stock exchange listing from 20% to 30%. Pakistan has high tax rates; thus, taxpayers may be incentivized by lowering the tax rates;
- Improved and effective tax facilitation centers at every tax office to help support filing of tax returns;
- Simplified tax guidelines and assistance through qualified staff;
- Encourage interaction and improve the trust deficit;
- Tax incentive for newly registered taxpayers – reduced tax for first 3 to 5 years (like small companies and start-ups);
- Filers should be given priority treatment at various infrastructural facilities e.g., at NADRA, schools, excise and taxation (when registering motor vehicles), courts of law, banks, hospitals, airports etc.;
- Incentive for compliant taxpayers and professionals (Doctors, Engineers, Lawyers, Chartered Accountants) for reduction in tax rates; and
- Some benefits like free medical, education for children, insurance or other privileges must be associated with the payment of taxes for the filers.

On top of this, Government can also incentivize the existing taxpayers with following small benefits by categorizing them on the basis of annual tax paid during the last three years:

- Preferred treatments in the Government owned hospitals and offices;
- Discounted toll tax on the roads and discount at air tickets;
- Discount to the children in Government schools, colleges and universities; and
- Unemployment allowance for six months; and
- Higher insurance coverage limits through Sehat Card etc.

1.09 ALIGNING ALL RETAIL SHOPS WITH QR-CODES TO FACILITATE CASHLESS PAYMENTS

HIGH

Cash transactions are causing hardship in documentation of the economy. Income Tax law provides that annual income below PKR600,000 is to be treated as below taxable limit thus annual income above this limit (which arrives at PKR50,000 per month) is effectively taxable and every business unit in Pakistan squarely falls within this ambit. Thus, cashless sales should be introduced through enablement of QR-codes of each outlet to facilitate buyers too. Such outlets can initially be facilitated with the confirmation they will not be asked by the FBR to display NTN certificates, or they will be absolved from probe by FBR for initial two – three years.

Facilitation through cashless transactions for both buyers and sellers will increase documentation. Adoption of this proposal can help in even capturing the lower strata of the economy to increase documentation. The customer making digital payments may be incentivized by charging reduced sales tax similar to the success achieved by charging reduced rate of sales tax introduced for restaurants by PRA and ICT.

1.10 WIDENING OF TAX ON INCOME FROM PROPERTY

HIGH

There is a strong perception that income from property is not fully tapped due to lack of monitoring. It is suggested to take the following steps for expanding the tax base under the head income from property:

- For preventing escape of taxation on rent from immovable property, every tenant, by statute, should be required to file a copy of the lease agreement to the FBR or any other designated office to ensure that tax return is filed by the lessors and tax thereon is paid; and

- Data should also be collected from the police stations, development authorities or municipal administration of the rented-out properties (both commercial and residential) subject to property tax.

1.11 WITHDRAWAL OF TOTAL EXEMPTIONS FROM TAX

Second Schedule to the ITO has provisions that gives a message that the government is not impartial in levying tax on all sectors of the economy or sections of the society. It demonstrates partiality by providing tax concessions and exemptions to those in power or holds high profile positions in the government thereby giving a message that the tax policy is tilted towards elites including landlords or wealthy. The classic example is of exemptions available to agricultural income and the perquisites given to certain high level officials.

The Government should seriously consider withdrawal of all unwarranted and discriminatory tax exemptions/ concessions provided in the Second Schedule to the ITO as without it broadening of tax base will remain a dream. This should be done proactively rather than on the behest of IMF.

1.12 TAX ON INCOME OF SOCIAL AND SPORTS CLUBS

Some social and sports clubs in Pakistan are not paying taxes and claiming tax exemption on the basis of doctrine of mutuality. It is proposed that FBR should incorporate special tax provisions dealing with tax mechanism for such clubs. These clubs may be treated as "Company" for taxation purposes. It is further proposed that these clubs are made liable to send new members list each year with their spending to FBR so that FBR can verify whether such members hold NTN and whether their declared assets are in line with their spending.

1.13 MEASURE FOR CURBING MASSIVE UNDER-INVOICING

In some cases, massive under-invoicing by commercial importers is discouraging domestic industry. It is proposed that FBR should conduct an inquiry against under invoicing in some specific products and if FBR consider that there are reasons to believe that commercial importers are carrying out under invoicing then FBR should be empowered to publicly disclose such values for effectively addressing this menace. The public disclosure will discourage commercial importers to under-declare the value of consignments for evading government revenues.

It is further proposed that FBR should have powers to auction such goods (which appear to be under invoiced) to local manufacturers by adding a premium of 20% to 30% with such sale proceeds (including premium) going to importer. This will also add as a measure to discourage under invoicing.

1.14 FILING OF "NIL" INCOME TAX RETURN TO GAIN ACTIVE STATUS

Some Individuals, AOPs, and companies file NIL income tax returns to gain active status so as to avoid extra withholding tax. It is proposed that FBR should carries out an exercise to identify such income tax returns (with a threshold of deduction of Rs. 20,000 withholding taxes in a tax year) so as to identify potential tax evaders. The Zero-income filers should also be evaluated in terms of asset purchased.

Furthermore, the stop-filers take benefits and then exits the tax net. There is no such automated mechanism to force stop-filers to remain in the tax net. It is suggested that the benefits of filer, availed before becoming stop-filer should be reversed and penalty should be imposed. Also, the procedure of exiting the tax net should be made difficult. This change will help in reducing the numbers of stop-filers and bound the filer to stays in tax net.

1.15 UTILIZATION OF SWAPS FOR APPLICATION OF DIGITAL INVOICING AND INTEGRATTION OF POS WITH MANUFACTURERS

HIGH

FBR has been taking measures for implementation of Digital Invoicing such as in case of Tier-1 retailers raising such invoice through Point of Sale ["POS"]. Existing business process does not cover issuance of digital invoices through SWAPS. The business process under consideration starts with the responsibilities of withholding agents/SWAPS agents resulting in real-time payment of withholding taxes to FBR and respective payment to the SWAPS beneficiary. The system also facilitates auto-population of withholding tax statements for SWAPS agents, auto loading of tax deductions in the income tax returns of SWAPS beneficiary and sales tax returns for SWAPS agents.

SWAPS is currently under designing, testing and implementation stage. This system should also include a module for SWAPS beneficiary to raise digital invoices. Once these invoices are generated through SWAPS, their settlement would become more easier for the SWAPS agents as the data would already be entered through digital invoice. At initial stage, this may not be made mandatory to avoid resistance/ chocking of SWAPS. However, sales tax registered persons/ persons on ATL should be encouraged or enforced to issue digital invoices through SWAPS. The proposed change will help documentation of complete cycle from invoice generation to its settlement and receipt of applicable taxes.

Furthermore, development and deployment of a scheme similar to POS in the entire supply chain to capture and document it all the way from manufacture and import to the retail stage was earlier proposed and is under consideration. It is suggested that in addition to the Tier-1 retailers, initially, POS should be integrated with the manufacturers and commercial importers to capture the undocumented players of immediate supply chain. Issuance of invoices by manufacturers and commercial importers with QR-code on products and invoices will capture the transaction at initiation stage helping in tracking it at later stages. This will help in documenting the supply chain and tax evasions.

1.16 USE OF QR-CODE TECHNOLOGY AND DOCUMENTATION OF POLYPROPYLENE BAGS ECONOMY

HIGH

POS has been integrated with the Tier-1 retailers however, it has been observed that in most cases these retailers are using dual system for the purpose of invoicing but with no check and balance of their wrongdoing.
It is suggested to implement QR-Code technology such as Track and Trace System already introduced. The printing of QR-code on the products along with digital invoices generated through POS will help reducing this utilization of dual system of invoicing by the retailers. In addition to this, buyers should also be encouraged through incentivizing either through attractive prize scheme or preferably awarding credit points on purchasing the QR-coded products. These credit points should be made utilizable by the buyers in their next purchase transactions similar to credit cards. Further, steps for creating public awareness should be taken such as advertisement through digital means and display of posters at retail shops should be mandated. This proposal will help in reducing the tax evasions with the help in documentation at retail stage.

Furthermore, polypropylene bags are an environment friendly and recyclable industrial packaging, around 2.5 billion bags are produced each year in Pakistan for the industrial sectors covering sugar, wheat, wheat flour, rice, pulses, feeds, fertilizers, chemicals etc. Measures have not been taken to document such sector.

It is suggested to use the polypropylene bags with factory printed QR-codes (instead of separately affixing detachable QR-code stickers, on each bag manually) under the Track and Trace System having tacked serial numbers along with the digital invoices discussed under (1.15) above. This will document the industrial products and 60% of the national economy that is currently outside the tax net and will help in increasing the tax revenue.

1.17 DISALLOWANCE OF INPUT FOR NON-INTEGRATED RETAILERS

HIGH

Retailers which are not integrated are getting benefit of inputs. It is suggested that such retailers should not be allowed to claim inputs. It will attract more retailers to get registered for Tier-1 and simultaneously minimize the chances of errors and human intervention in submitting the sales record to FBR.

1.18 ENHANCEMENT OF SALES TAX RATE FOR TIER-2 RETAILERS

HIGH

Relaxing provisions for Tier-2 retailers in textile and leather industry are causing them to remain unintegrated. Difference of Sales Tax rate between Tier-1 and Tier-2 is dropped down to 3% from 5%. It should be increased to at least 5% as it was in TY 2022/23. Such step will increase number of retailers in Tier-1 which allows FBR to fetch sales records systematically and increased documentation.

1.19 DEVELOPMENT OF DATA SCIENCES AND DATA ANALYTICS DEPARTMENT AND USE OF TECHNOLOGY

HIGH

Accurate and analyzed actionable information not readily available. FBR has sufficient data however, such data is in raw form and no steps are being taken to utilize it purposefully. Data Analytics and Data Science department should be set up immediately to help analyze and utilize the data efficiently. It will help in utilizing the data more efficiently and allows the authorities to take informed decisions.

Further, Artificial Intelligence / Machine Learning Tools and software should be studied to see which are the best suited for our environment to help identify tax evaders and tax fraud. It will help in identifying & catching the tax evaders more efficiently.

Also, it is proposed to completely automate the audit procedure as much as possible and minimize human discretion and interaction. Currently, audit process is completely unautomated, and the officers are conducting audit of tax affairs of the taxpayers manually which does not seem fair and human discretion is causing negative effects and a bad image for the FBR. Such change will reduce this human discretion and interaction resulting in more accurate audits and eventually build stakeholders trust on FBR.

1.20 MANDATORY INTEGRATION OF POINT OF SALE (POS) SYSTEMS

MEDIUM

Mandatory integration of Point of Sale (POS) systems with the Federal Board of Revenue (FBR) should be expanded to cover additional sectors that engage significantly in cash-based and high-value transactions but currently remain largely undocumented. The sectors recommended for immediate mandatory POS integration include:

- Marriage/banquet halls
- All brand retail stores
- Hardware stores
- Furniture showrooms
- Medical and Dental service providers
- Electric stores
- Electronic stores

Moreover, it is proposed that a flat rate of 5% sales tax be applied uniformly on all transactions reported through POS-integrated systems, without allowing any input tax adjustments or refund claims against these sales.

Implementing POS integration in these sectors will effectively capture their economic activities, shifting their substantial cash transactions into the formal, documented economy. Real-time sales reporting through POS will ensure transparency and accuracy in the calculation and payment of

sales tax, ultimately enhancing revenue collection and improving compliance for income tax purposes.

This measure aligns closely with the FBR's broader strategic objective of promoting a fully digitalized and documented economic framework. Additionally, disallowing input tax adjustments on these transactions eliminates the potential for fraudulent or inflated input tax claims, thereby addressing a critical source of revenue leakage within the current taxation system.

1.21 MANDATORY NTN REGISTRATION OF INFORMAL SECTOR

MEDIUM

It is proposed that bulk suppliers operating within traditionally informal sectors, including suppliers of vegetables, fresh chicken, mutton, and fish, be systematically integrated into the income tax framework. This integration should encompass mandatory National Tax Number (NTN) registration, compulsory filing of income tax returns under Section 114 of the Income Tax Ordinance, 2001, and inclusion within the withholding tax mechanism as defined in Section 153, wherever applicable.

These specific sectors conduct substantial cash transactions daily and represent considerable economic turnover. Capturing even a modest proportion of these suppliers within the documented economy can yield significant revenue enhancement without placing additional burdens on existing compliant taxpayers.

Broadening the tax base through these measures ensures fairer distribution of tax responsibilities and supports long-term, sustainable revenue growth, rather than resorting to repeated rate increases on already compliant sectors. Furthermore, the expanding use of digital invoicing, electronic payment solutions, and Point-of-Sale (POS) systems creates a practical framework for effectively monitoring and documenting transactions between bulk suppliers and retailers. This technology-driven approach will facilitate compliance and minimize disruption, ultimately promoting a transparent, equitable, and sustainable taxation environment.

1.22 REGULAR AND TARGETED SURVEYS OF VARIOUS MARKET SECTORS

MEDIUM

It is proposed that the Federal Board of Revenue (FBR) undertake systematic and targeted surveys across key market sectors, including wholesale, retail, and various service segments, to verify the tax registration (filer) status of businesses and accurately assess their actual turnover and income levels. Currently, a significant number of businesses either remain unregistered or consistently misreport their income. Regular physical surveys and robust data collection efforts can identify discrepancies between declared incomes and actual business activities. These surveys will enable the FBR to gain precise insights into sectoral economic contributions, facilitating improved revenue estimation, effective budgetary planning, and more informed policy-making.

Utilizing verified ground-level data will significantly strengthen the enforcement mechanism, allowing the FBR to confidently issue notices under Sections 114(4) and 122(5A) of the Income Tax Ordinance, 2001. Such evidence-based enforcement will enhance compliance, ensure fairness, and solidify the legal foundation of tax collection efforts, ultimately fostering greater transparency and accountability within Pakistan's taxation framework.

1.23 MANDATORY REGISTRATION OF NPO'S OPERATING IN PAKISTAN

MEDIUM

It is proposed that all Non-Profit Organizations (NPOs) operating in Pakistan—irrespective of their size, scope, nature of activities, or claimed tax-exempt status—be required to register with the Federal Board of Revenue (FBR) and submit annual income tax returns.

At present, numerous unregistered entities solicit public donations, manage substantial financial transactions, and operate outside the purview of regulatory oversight, without making any contribution to the national exchequer. Requiring universal registration and annual tax filings will ensure greater transparency and accountability, particularly in the use of public funds and donations.

Moreover, this mandatory framework will assist in identifying entities misrepresenting themselves as NPOs while engaging primarily in commercial or profit-oriented activities. Such regulation will safeguard genuine charitable work and curb potential abuse.

Aligning NPOs' reporting requirements with Sections 114 and 100C of the Income Tax Ordinance, 2001, will enable the FBR to accurately assess eligibility for tax exemptions and ensure compliance with tax regulations. This measure will promote responsible stewardship of donated funds, enhance public confidence, and support the integrity and fairness of Pakistan's taxation and regulatory environment.

1.24 COLLABORATION WITH PROVINCES REGARDING PROPERTY OWNERSHIP

MEDIUM

It is proposed that the Federal Board of Revenue (FBR) establish formal collaboration with provincial Excise and Taxation departments, as well as Cantonment Boards, to effectively access and leverage comprehensive data on property ownership, rental values, and property tax assessments.

Currently, numerous individuals owning high-value residential properties—particularly in major urban centers and cantonment areas—either remain entirely outside the tax net or significantly underreport their rental income. By obtaining and analyzing property records and official rental valuations, the FBR can efficiently cross-check reported rental income under Section 15 of the Income Tax Ordinance, 2001, against realistic market values.

This strategic collaboration would significantly enhance tax compliance and revenue collection, without creating new tax burdens. Instead, it ensures fairness by accurately capturing existing taxable incomes that currently evade detection. This data-driven approach will promote transparency, reduce tax evasion, and strengthen the overall integrity and effectiveness of Pakistan's taxation system.

1.25 COMPREHENSIVE SURVEY OF BUSINESS OPERATING WITHOUT REGISTRATION

MEDIUM

It is proposed that the Federal Board of Revenue (FBR) undertake comprehensive, targeted surveys of major commercial plazas and shopping centers in urban areas nationwide, aiming to identify and document businesses operating without registration under the income tax and sales tax frameworks.

Currently, a considerable number of shopkeepers and service providers carry out substantial commercial transactions and generate significant rental incomes in prominent plazas without possessing mandatory National Tax Numbers (NTNs), Sales Tax Registration Numbers (STRNs), or fulfilling essential filing requirements. Additionally, many such businesses informally collect sales tax from customers but fail to remit these taxes to the government, resulting in considerable revenue leakage.

Conducting detailed surveys of these commercial hubs will allow FBR to pinpoint unregistered and under-reporting businesses, particularly within key urban retail markets that have high business turnover. By systematically gathering and analyzing this data, the FBR can effectively enforce compliance under the Income Tax Ordinance, 2001 (Section 114) and the Sales Tax Act, 1990 (Sections 3 and 14). This enforcement strategy will drive mandatory registration, accurate reporting, and timely filing of returns.

Such proactive measures will significantly broaden the documented economy, enhance tax collection efficiency, and ensure equitable tax contributions from all business sectors without imposing additional burdens on already compliant entities.

1.26 STRICT PENAL ACTION AGAINST TAX DEFAULTERS

MEDIUM

It is recommended that the Federal Board of Revenue (FBR) rigorously adopt and consistently implement a policy of strict enforcement and exemplary penal action against tax defaulters, non-filers, and individuals involved in concealment of income or assets, as outlined under the Income Tax Ordinance, 2001.

Although the current tax laws contain comprehensive provisions for penalties and prosecution—specifically under Sections 114(1) (return filing), 111 (concealment of assets), and Sections 192 and 192A (prosecution and penalties)—enforcement has historically remained inadequate. The absence of visible, high-profile actions against major tax evaders in recent years has significantly weakened the overall credibility and effectiveness of Pakistan's taxation system.

Consistent and visible enforcement actions send a clear message that tax compliance is mandatory for everyone, thereby reinforcing public trust in the fairness of the system. The effective prosecution

of even a small number of high-profile cases, accompanied by substantial penalties under Sections 192 and 192A, can serve as powerful deterrents, discouraging thousands of potential tax evaders and non-filers from violating the law.

Implementing stringent enforcement measures will notably increase compliance pressures, particularly within sectors known for significant tax evasion, such as real estate, wholesale trading, and service industries. This proactive approach will encourage greater registration and timely filing of returns, ultimately strengthening tax compliance and enhancing revenue collection through increased transparency and accountability.

1.27 BANKING TRANSACTIONS ABOVE 3 MILLION

MEDIUM

It is proposed that any banking transaction exceeding Rs. 3 million conducted through personal accounts should undergo mandatory due diligence by banks and relevant regulatory authorities, except where such transactions are demonstrably linked to verified business dealings or documented asset purchases.

Implementing this measure will effectively discourage the misuse of personal bank accounts for undisclosed business activities, promoting greater financial transparency and accountability. Enhanced scrutiny of high-value transactions, particularly those involving foreign income or significant cash flows, will substantially reduce avenues for revenue leakage and tax evasion.

This approach ensures that large transactions are properly monitored and documented, facilitating the identification of taxable income and preventing misuse of personal accounts to conceal business activities or assets. Ultimately, this policy will reinforce trust in the financial system, support fair taxation, and contribute positively to broader national efforts aimed at enhancing financial integrity and transparency.

1.28 NO BUSINESS / TRADEMARK REGISTRATION WITHOUT REGISTRATION WITH FBR

MEDIUM

It is recommended that registration of any business or trademark with governmental bodies—including the Securities and Exchange Commission of Pakistan (SECP) and the Intellectual Property Organization (IPO)—be made conditional upon providing proof of sales tax registration with the Federal Board of Revenue (FBR) or relevant provincial sales tax authorities.

Implementing this measure will ensure comprehensive compliance, compelling all commercial entities, including small and medium-sized enterprises, to operate within the formal and documented taxation framework. Mandatory linkage of business and trademark registrations with sales tax registration will create a seamless integration, ensuring automatic enrollment into the sales tax regime.

Such proactive enforcement will significantly enhance financial oversight and transparency, effectively curbing unregistered commercial activities and tax evasion. Additionally, this initiative will substantially expand the documented economy, promote fair competition, and strengthen the national tax base, ultimately contributing to improved revenue generation and economic stability.

1.29 FOREIGN NATIONALS IN PAKISTAN

MEDIUM

It is proposed that any foreign national residing in Pakistan for more than 183 days within a tax year be legally required to declare their source of income in Pakistan and comply with local tax laws, including the filing of income tax returns under Section 114 of the Income Tax Ordinance, 2001.

Currently, it is estimated that over one million foreign individuals are working in Pakistan—many employed by multinational corporations, foreign-funded projects, or local enterprises. However, only a small fraction of these individuals are registered with the Federal Board of Revenue (FBR) or contribute to the national tax pool.

Stricter enforcement of tax residency rules is essential to ensure that all qualifying foreign residents are taxed fairly and equitably. This includes mandating the declaration of Pakistani-sourced income and subjecting them to the same obligations as local residents. Doing so will:

- Prevent tax evasion and underreporting by foreign employees.
- Ensure equitable tax contributions from all income earners in Pakistan.

- Enhance revenue collection without imposing additional burdens on already compliant taxpayers.
- Promote transparency and accountability within sectors employing foreign talent.

This policy would bring Pakistan in line with international standards on the taxation of resident foreign nationals and reinforce the principle that all residents—regardless of nationality—must contribute their fair share to the economy

1.30 ROYALTY PAYMENTS TO LOCAL RESIDENTS

MEDIUM

It is proposed that a withholding tax (WHT) mechanism be introduced on royalty payments made to resident individuals and entities, at a prescribed rate, consistent with the existing WHT framework applicable to payments made to non-residents.
Currently, royalty payments to non-residents are subject to WHT; however, no such mechanism exists for local recipients, creating a disparity in tax treatment. By extending WHT to resident royalty recipients, the tax regime will achieve greater equity, ensuring that both local and foreign recipients of royalty income are treated uniformly under the law.
Royalty income is often underreported due to its intangible nature and reliance on self-declaration. Implementing WHT on such payments will:

- Ensure tax collection occurs at the source, reducing reliance on post-facto declarations.
- Minimize opportunities for tax evasion and income concealment.
- Enhance compliance by shifting responsibility for initial tax deduction to the paying party.
- Broaden the tax base by capturing income that may otherwise go unreported.

This measure will strengthen revenue collection, promote fairness in the taxation of intellectual property and licensing income, and align Pakistan's tax practices with international norms.

1.31 WITHHOLDING TAX ON LEASE RENTALS

MEDIUM

It is proposed that withholding tax (WHT) be imposed on payments made for the lease or rental of land and buildings, as well as plant, property, and machinery (PPM), at a prescribed rate under the Income Tax Ordinance, 2001.
Currently, lease transactions involving PPM—despite involving high-value contracts—largely fall outside the scope of the withholding tax regime. As a result, many lessors underreport or fail to declare their full rental income, leading to significant revenue leakages.
Bringing such transactions under the WHT framework will:

- Ensure upfront tax collection at the time of payment, reducing the risk of non-compliance and income concealment.
- Improve transparency and documentation of leasing transactions, especially in industrial and commercial sectors.
- Shift the compliance responsibility to lessees, streamlining tax administration and simplifying enforcement for the Federal Board of Revenue (FBR).
- Align leasing income treatment with the broader objective of documenting all significant financial activities.

This measure will significantly broaden the tax base and promote greater fairness in the taxation of passive income, while also strengthening the overall integrity of Pakistan's tax system.

1.32 BROADENING OF TAX BASE UNDER PROVINCIAL LAWS

HIGH

Information collected for potential unregistered taxpayers operating in the economy is not being systematically reviewed. The existing provisions of law have not provided any mechanism for systematic utilization of such information to broaden the tax net. This can be a regressive tool in the longer run where only existing registered persons would be subject to revenue target and

compliance of law.

It is proposed that a proper mechanism be introduced in law to bring in to the tax net the potential unregistered persons whose information is available in the shape of NTN/CNIC through sales tax withholding provisions as well as through filing of sales tax returns by the registered persons requiring full disclosure of information of unregistered persons.

Rationale
This step would greatly assist in broadening the tax base and reducing disparity in the economy.

COMMITTEE ON FISCAL LAWS (COFL) 2024-2025

Zeeshan Ijaz — Chairman – Committee on Fiscal Laws

Coordination Task Force

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