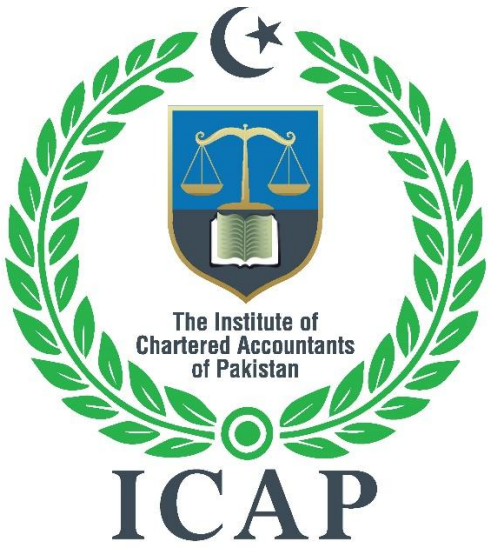
The Institute of
Chartered Accountants
of Pakistan
ICAP

MESSAGE FROM THE PRESIDENT

The Institute of Chartered Accountants of Pakistan continues to play a pivotal role in supporting the development of a fair, transparent, and efficient taxation framework in Pakistan. As President of the Institute, I am pleased to present our Budget Proposals for the Federal and Provincial Budgets 2026–27.

These proposals have been developed through rigorous technical deliberations and professional input from members of the Institute, with a focus on improving the structure and administration of fiscal laws.

The recommendations aim to simplify tax procedures, remove ambiguities in existing provisions, and address structural inefficiencies within the current system. Emphasis has also been placed on enhancing documentation, improving compliance mechanisms, and facilitating taxpayers through clearer and more consistent regulatory practices.

This document is intended to support policymakers by providing practical and implementable suggestions that contribute to a more streamlined and effective taxation system.

I commend the efforts of the respective committees and their conveners for their dedication and valuable contributions in developing these proposals.

We are pleased to present this document to the Ministry of Finance and Economic Affairs, Government of Pakistan, and remain available for any further support in this regard.

Muhammad Samiullah, FCA
President
The Institute of Chartered Accountants of Pakistan

MESSAGE FROM THE CHAIRMAN

On behalf of the Economic Advisory and Fiscal Laws Committee, I am pleased to present the Institute of Chartered Accountants of Pakistan's Budget Proposals for the Federal and Provincial Budgets 2026–27. These proposals are the outcome of detailed technical analysis and the collaborative efforts of the Committee members, focusing on key fiscal challenges and opportunities within the existing taxation framework. Particular emphasis has been placed on rationalizing tax provisions, enhancing administrative efficiency, and promoting greater clarity and consistency in the application of fiscal laws.

The Committee has endeavored to put forward pragmatic and actionable recommendations aimed at strengthening documentation, facilitating compliance, and addressing structural gaps in the current system, with a view to supporting the development of a more coherent, efficient, and responsive tax regime.

I would like to acknowledge the dedication and valuable contributions of the Committee members and conveners, whose expertise has been instrumental in shaping these proposals. I also extend my sincere appreciation to the ICAP members who contributed to this effort, namely Mr. Khalid Mahmood, Mr. Asif Siddiq, Mr. Atiq Ur Rehman, Mr. Rizwan Bashir, and Mr. Habib Fakhruddin, for their valuable input and support.

The Committee remains committed to supporting the Institute and the relevant authorities in advancing meaningful and sustainable fiscal reforms.

Zeeshan Ijaz, FCA
Chairman – Economic Advisory & Fiscal Laws Committee
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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PART-I

FEDERAL TAXATION

DIRECT TAXATION

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DIRECT TAXATION

1.01 SLAB RATES OF TAX FOR SALARIED INDIVIDUALS

HIGH

Over the past few years, tax rates applicable to salaried individuals have 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 six 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 almost no tax planning options.

The salaried tax slabs have been sharply tightened over the past two years, substantially increasing the burden on middle-income earners. The top slab threshold, previously applied above 7 million rupees, has now been reduced to 4.1 million rupees, bringing many mid to upper middle-income individuals into the highest tax bracket. These compressed brackets have raised monthly tax deduction and reduced take-home pay. A review of the slab structure is therefore essential to restore fairness and protect the salaried class.

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 class, especially in low and middle-income brackets.

It is proposed that automatic indexation of salary tax slabs based on the Consumer Price Index (CPI) be introduced so that tax brackets are adjusted annually in line with inflation.

Rationale

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

- Help maintain taxpayers' real disposable income and prevent individuals from being

pushed into higher tax slabs merely due to increases in nominal salaries driven by inflation. Automatic indexation will also bring greater transparency, predictability, and fairness to the tax system, reduce the need for frequent discretionary changes in tax policy, and ensure that the burden of inflation does not result in unintended increases in effective tax rates for salaried individuals.

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

1.02 RATIONALIZATION OF SALARY TAXATION AND EXEMPTION OF EMPLOYMENT-RELATED ALLOWANCES

Income under the head "salary" is currently taxed on a gross basis. While this approach was initially accompanied by reduced tax rates, subsequent increases in tax slabs and rates have not been matched with the restoration of deductible allowances. As a result, salaried individuals are now subject to higher effective taxation without corresponding relief.

The withdrawal of tax credits under Sections 62 and 62A through the Finance Act, 2022 has further exacerbated this burden. These credits previously encouraged savings and financial security through investments in mutual funds, pension funds, and life insurance.

In addition, the rising cost of living—particularly due to increased fuel prices, has significantly elevated essential employment-related expenses such as daily commuting. Despite being a necessary cost incurred for employment, conveyance allowance is currently treated as taxable income, thereby imposing tax on what is effectively a reimbursement of expense rather than discretionary income.

Recommendation

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

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

   Rationalize the existing tax rates applicable to salaried individuals; or

   Reinstate exemptions for common employment-related allowances such as:

   - House rent allowance
   - Utilities allowance
   - Conveyance allowance

2. **Exemption of Conveyance Allowance:**

Specifically exempt conveyance allowance from income tax, either fully or up to 10% of basic salary, to reflect the essential nature of commuting costs.

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

Passive income streams (e.g., bank interest or rental income) should not alter an individual's primary classification as a salaried taxpayer for the purpose of concessional tax treatment.

Rationale

It is inequitable to subject salaried individuals whose incomes are fully documented and taxed at source to elevated tax rates without allowing corresponding exemptions or deductions, particularly when business and professional taxpayers are taxed on net income after expenses.

The proposed measures will:

- Ensure equitable treatment across taxpayer categories
- Align taxation with real disposable income
- Provide relief against rising employment-related costs, particularly commuting
- Promote savings and financial security
- Enhance taxpayer morale and voluntary compliance

1.03 RATIONALIZATION OF SALARY WITHHOLDING TAX MECHANISM UNDER SECTION 149 TO INCORPORATE FULL ADJUSTMENTS OF TAX CREDITS, ALLOWANCES, AND REFUNDS

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 under section 149, which includes tax credits u/s 61 and 63. Further, tax credit under section 63A have been introduced through FA 2025, however, the corresponding amendment has not been made in section 149 to allow adjustment of such tax credit for the purpose of deduction of tax from payment of salary.

Recommendation

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 (at least specific inclusion of section 63A to allow adjustment of tax credit from deduction of salary to align it with the provisions of

section 63A).

- 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.

1.04 SECTION 60D – DEDUCTIBLE ALLOWANCE FOR TUITION FEES

HIGH

The current income eligibility threshold of Rs. 1.5 million under Section 60D significantly limits the number of taxpayers who can avail the tuition fee deduction. Over time, education expenses have risen sharply across schools, colleges, and universities, while the threshold has not kept pace with inflation or changing socioeconomic realities. As a result, a large proportion of low to middle income earners, who increasingly struggle to meet rising education costs, are excluded from this important tax relief measure.

Recommendation

It is recommended to enhance the income eligibility threshold for tuition fee deductions to a more realistic level that reflects current income patterns and education expenses. This may include:

- Increasing the threshold from Rs. 1.5 million to 2.5 million, or
- Indexing the threshold to annual inflation or education cost indicators, ensuring it remains relevant over time.

Rationale

- Such reform would broaden access to tax relief and provide meaningful support to families managing substantial education expenses.
- Tuition fees at most institutions have increased significantly due to inflation, operational expenses, and sector-wide cost adjustments. A stagnant threshold no longer reflects the real cost burden on households.

- Many salaried individuals earning slightly above Rs. 1.5 million fall into the middle-income bracket. Despite not being high earners, their children's education expenses constitute a major portion of household spending. The current rule excludes them entirely from relief they genuinely need.
- Revising the threshold ensures equitable treatment of taxpayers whose income levels have shifted over time due to inflationary pressures, without translating into real increases in their purchasing power.

1.05 TAX REBATE FOR WORKING WOMEN (SALARY INCOME)

HIGH

Women increasingly serve as primary earners but face identical tax burdens despite structural disadvantages.

Recommendation

It is proposed that, in line with the tax rebate available to women enterprises, a similar benefit be extended to salaried women by introducing a tax credit or rebate on income derived under the head "Salary."

Accordingly, a provision may be inserted in the Income Tax Ordinance, 2001 to allow a reasonable tax rebate (e.g., up to 10%–15% of tax payable) to all salaried women, irrespective of profession or sector.

This measure will ensure parity in tax treatment between women engaged in business and those earning through employment.

Rationale

Currently, a 25% tax reduction is available to women enterprises to promote female entrepreneurship and economic participation. However, no corresponding relief exists for salaried women, despite their increasing role as primary earners and contributors to household income.

1.06 TAX REBATE FOR FULL-TIME TEACHERS AND RESEARCHERS – CLAUSE 3A, PART III, SECOND SCHEDULE

HIGH

The 25% tax rebate previously available to full-time teachers and researchers has expired after Tax Year 2025, removing a key incentive that supported academic professionals engaged in teaching and research activities. With rising inflation and increasing competition for skilled educators, the lapse of this rebate weakens the country's ability to attract and retain qualified academic talent.

Recommendation

It is proposed to reinstate the 25% tax rebate for full-time teachers and researchers and to remove any sunset limitation to ensure long-term continuity of this incentive.

Rationale

This proposed measure will:

- Recognize educators as drivers of national development, reinforcing the value of teaching and research professions.
- Help retain and attract academic talent, reducing the brain drain and strengthening educational institutions.
- Support the growth of a knowledge-based economy by incentivizing research, innovation, and high-quality education.

1.07 PROFIT ON DEBT IN CASE OF SENIOR CITIZENS AND WIDOWS

Senior citizens are currently subject to taxation at normal slab rates (up to 49.5% including surcharge) where their profit on debt exceeds Rs. 5 million per annum. Given the prevailing economic conditions and inflationary pressures, this threshold is relatively low and results in a higher tax burden on elderly individuals who primarily rely on fixed income streams such as savings and investments for their livelihood and healthcare.

Recommendation

It is recommended that the threshold for profit on debt income for senior citizens be increased from Rs. 5 million to Rs. 10 million per annum. Furthermore, tax deducted at source at the rate of 20% on such income should be treated as the final discharge of tax liability.

Rationale

This proposal will:

- Provide meaningful financial relief to senior citizens.
- Align taxation with inflation and reduced purchasing power.
- Simplify tax compliance for elderly taxpayers.
- And ensure that individuals dependent on savings are not disproportionately taxed.

1.08 MINIMUM TAX REGIME

The Institute highly appreciates the policy change of moving from Final Tax Regime [FTR] to Global Taxation of Income on net income basis [NTR] subject to Minimum Tax under various provisions of the Income Tax Ordinance, 2001. However, this transition from FTR to

NTR coupled with multiplicity of minimum taxes has brought alongside various legal, factual and computational issues, which need serious consideration. These are enumerated below for reference:

I. 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 take 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.

II. 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); and
- Adopted by most of the Individuals and AOP's even otherwise.

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;
- The applicability of Minimum Tax is with reference to tax payable on the income for the year from such imports. However, 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; and

- 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.

III. 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 outstanding 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.

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

Under the 10th Schedule the rates 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.

V. 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.

Further, 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; multiplied 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.

VI. 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.

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.
- For this purpose, following amendments are proposed in the Ordinance–
  a. Sub-section (7) of section 148 shall be substituted as under –
     "The tax required to be collected under this section shall be adjustable."
  b. Sub-section (7A) of section 148 shall be omitted.
  c. 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."
  d. Sub-section (2B) of the section 152 shall be substituted as under –
     "The tax deductible under sub-section (2A) shall be adjustable."
  e. Proviso to sub-section (2B) of the section 152 shall be omitted.
  f. 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.
  g. 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."
  h. In sub-section (4) of section 153, after the word "minimum", the words and figures "tax under section 113" shall be inserted.
  i. Sub-section (2B) of section 233 shall be omitted.
  j. Sub-section (3) of the section 233 (including the explanation) shall be substituted as under –
     "The tax deductible under this section shall be adjustable."
  k. Sub-section (3) of the section 236CA shall be substituted as under –
     "The tax required to be collected under this section shall be adjustable."
  l. 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, 63, 63A, 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."

1.09 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 sections 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.

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

HIGH

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 two 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.

1.11 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)

1.12 LIMITATION OF EXEMPTION CERTIFICATE AVAILABILITY FOR FTR TAXPAYERS

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 persons 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.

1.13 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.

Recommendation

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 it convenient for the revenue authority by 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.

1.14 SECTION 4C – SUPER TAX ON HIGH EARNING PERSONS

HIGH

Under Section 4C(2)(i), the law provides for inclusion of certain income streams in the computation of Super Tax, stated as:

> "*Profit on debt, dividend, capital gains, brokerage and commission;*"

A close reading of the above clause indicates that due to the absence of the word "and" after "capital gains," the terms "brokerage and commission" appear as two independent categories. Consequently, if this is so interpreted, this extends the scope to include all types of brokerage and commission income, including those not covered under Section 233 (such as foreign indenting commission, petroleum commission, etc.).

Brokerage and commission income is subject to various administrative, selling, and financial expenses. Therefore, applying Super Tax on the gross amount results in inequitable taxation.

Moreover, the net income from brokerage and commission is already included in taxable income and falls under Section 4C(2)(ii), thereby creating the risk of duplication or excessive taxation.

Recommendation

It is recommended that appropriate clarification be introduced by replacing 'brokerage and commission' with the words "net income from brokerage and commission" under section 4C. Further, for 'profit on debt' be replaced with "profit on debt under section 7B", so that only net income from brokerage and commission and Profit on Debt under section 7B is considered for the purpose of clause (i) of sub-section 2 of the section 4C. This will clarify the position and keep these incomes separate from the taxable income covered in clause (ii).

Rationale

This proposal will help in computation of Super tax under section 4C and:

- Ensure that only real income (after expenses) is subject to Super Tax,
- Eliminate any ambiguity in interpretation of the provision,
- Prevent excessive or double taxation, and
- Align the treatment of brokerage and commission income with fundamental taxation principles.
- Keep taxation of profit on debt as per section 7B separate from that taxed on net income basis.

Section 4C currently calculates Super Tax based on total income without allowing adjustment for carried-forward losses. This leads to taxation even where a taxpayer has not earned net profit.

Recommendation

Allow set-off of accumulated business losses under Section 57 while determining income for Section 4C.

Rationale

This ensures Super Tax is imposed on genuine economic surpluses and maintains horizontal equity among sectors with cyclical income patterns

1.15 MARGINAL RELIEF- MARGINAL RELIEF / PROGRESSIVE TAX SYSTEM

HIGH

The absence of marginal relief in the current tax framework leads to disproportionate tax burdens when income marginally exceeds specified thresholds. For instance, under

Section 4C (Super Tax), an income of Rs. 500 million is taxed at 7.5% (Rs. 37.5 million). However, an increase of even Rs. 1 in income results in the application of a higher rate of 10%, increasing the tax liability to Rs. 50 million. This creates an excessive tax burden for a negligible increase in income.

Recommendation

It is recommended that a true progressive tax system be introduced whereby higher tax rates apply only to the incremental portion of income exceeding each threshold, rather than the entire income. This would effectively eliminate sharp tax jumps and ensure smoother tax transitions across income slabs.

Rationale

This proposal will:

- Ensure fairness and equity in taxation,
- Eliminate disproportionate tax spikes on marginal income increases,
- Improve taxpayer confidence and perception of the tax system,
- And align the tax structure with internationally accepted progressive taxation principles.

1.16 ADVANCE TAX – SECTION 147

In case of an individual the threshold for payment of advance tax is latest assessed income of Rs. 1,000,000. This threshold was increased 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. 60,000. 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.

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.

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

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.

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."

1.17 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 was previously available under the law.

Rationale

Taxpayers expecting business losses or those already subjected to tax deduction under other heads, still remain subjected to tax collection at the import stage under section 148, causing unnecessary accumulation of refundable tax. Since this tax will ultimately be claimed as refund through the return of income, it results in avoidable cash-flow blockages for the company. This withholding mechanism strains operational liquidity, particularly during periods of reduced profitability. The resulting delays in refund processing further exacerbate financial pressure. Reintroduction of obtaining exemption from collection of tax at import stage under section 148 is therefore essential to prevent cash-flow disruption, safeguard revenue sustainability and provide support to loss-making businesses in these challenging economic environments.

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

HIGH

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.

Recommendation

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(1) 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.

1.19 ADVANCE TAX ON SALES TO RETAILERS U/S 236H

HIGH

Though difference currently exists between the tax rates applied to Active Taxpayers (ATL) and non-ATL individuals. However, the existing rate structure can further be strengthened for non-filers to make them obliged to enter the documented economy.

Recommendation

It is proposed that the withholding tax rate for non-ATL taxpayers be increased from 2.5% to 3.5%, thereby enhancing the differential between compliant and non-compliant taxpayers.

Rationale

A higher cost of remaining outside the tax net will motivate individuals to register and file returns to avoid additional withholding. As more individuals opt to join the ATL to benefit from lower rates, the documented taxpayer base will naturally expand, supporting long-term tax revenue mobilization.

1.20 ADVANCE TAX ON CASH WITHDRAWAL U/S 231AB

HIGH

The current Rs. 50,000 daily threshold for advance tax on cash withdrawals by the person not on ATL has become outdated due to the inflation and rising transactional needs. This low limit results in frequent tax deductions, even for routine cash requirements of individuals and small businesses.

Recommendation

It is proposed that:

- The threshold be increased to Rs. 75,000 to align with current cash-flow realities.
- While tax rate may be increased to 1.5%.

Rationale

Updating the withdrawal threshold aligns with inflation and reduces unnecessary tax deductions for genuine cash needs, whereas, this will provide compensating effect due to suggested increase in the rate to 1.5% so as to encourage non-ATL persons towards the documented economy.

1.21 CLARIFICATION ON DEFINITION OF CONTRACT

HIGH

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 the 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.

1.22 RATIONALIZATION OF GROSS AMOUNT PAYABLE UNDER SECTION 153(1)

HIGH

Currently, withholding tax under Section 153 is deducted on the gross amount including sales tax, despite sales tax being collected on behalf of the government but does not constitute income or revenue.

This is because under section 153(1), a prescribed person is required to deduct tax at source on the "Gross Amount Payable" at the time of making payment which includes sales tax, if any. Further, clause (v) of section 153(7), also defines turnover as being the gross sales or gross receipts inclusive of sales tax and FED. This results in excessive tax deduction, cash flow strain and particularly harmful in low-margin sectors.

Recommendation

It is proposed to redefine the gross amount payable and exclude Sales Tax, Federal Excise Duty, and other statutory levies collected on behalf of the Government. So that the withholding tax is applied on the net of tax value of goods and services.

Rationale

Redefining "gross amount payable" under Income Tax Ordinance, 2001 to exclude Sales Tax, Federal Excise Duty, and other statutory levies ensures withholding tax is applied only on actual income rather than pass-through amounts, thereby reducing undue cash flow strain, minimizing refunds and compliance burdens, and aligning the tax framework with fundamental taxation principles and international best practices.

1.23 GROUP RELIEF – SECTION 59B

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 needs 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.

1.24 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.

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

HIGH

Under section 92 of the ITO the income of association of persons (AOP) is taxed and amount received by the members is exempt from tax. For the AOPs of professionals which are restricted to be incorporated as a limited liability company, the provisions with respect to their taxation need revision.

Recommendation

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.

1.26 SECTION 153(1)(a) – REGIME FOR AOP/INDIVIDUAL MANUFACTURERS

HIGH

Under the current fiscal regime, corporate manufacturers are allowed to operate under an Adjustable/Normal Tax Regime. However, AOPs and individual manufacturers are excluded from this facility, despite undertaking substantial capital investments and contributing significantly to economic activity. This creates an imbalance in taxation and discourages growth and formalization among non-corporate manufacturers.

Recommendation

It is recommended that the Adjustable/Normal Tax Regime be extended to individual and AOP manufacturers having turnover of Rs. 300 million and above with the condition that they furnish audited financial statements. Such taxpayers should be allowed to avail the same tax treatment as corporate manufacturers.

Rationale

This proposal will:

- Ensure a level playing field between corporate and non-corporate manufacturers.
- Encourage documentation and audit compliance.
- Promote industrial growth among SMEs.
- and incentivize transition towards the formal economy.

1.27 AUTOMATION AND RATIONALIZATION OF REFUND PROCESSING AND ADJUSTMENT MECHANISM

HIGH

Despite efforts by the Federal Board of Revenue to enhance taxpayer confidence, a persistent trust deficit remains. One of the primary contributors to this gap is the delay or non-issuance of legitimate tax refunds. Taxpayers frequently encounter unnecessary procedural hurdles, including repeated physical verification of information that is already available within the FBR's digital systems and can be verified electronically.

In addition, the mechanism for adjustment of refunds against outstanding tax liabilities requires significant improvement. Despite repeated applications, such requests are often not processed in a timely manner. Given that withholding tax data (excluding import-stage taxes) is readily available on the IRIS MIS portal, and supporting documentation for import taxes can be furnished with ease, these delays result in avoidable liquidity constraints and further erode taxpayer confidence.

Furthermore, judicial forums, including the High Courts and the Tax Ombudsman, have consistently emphasized the need for prompt and fair processing of refund claims. However, the lack of effective implementation at the field level continues to hinder resolution.

Recommendation

It is recommended that an automated refund credit system be introduced to streamline both the issuance and adjustment of refunds. 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 timeframe.

Adjustment of verified refunds against outstanding tax liabilities should be made mandatory and should not be subject to administrative discretion.

Rationale

Implementing an automated and integrated refund mechanism will:

- Enhance transparency and reduce administrative burden
- Ensure timely issuance and adjustment of legitimate refunds
- Minimize discretionary delays and procedural inefficiencies
- Improve taxpayer confidence and trust in the tax administration system
- Alleviate cash flow constraints for businesses and individuals, thereby supporting economic activity.

1.28 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.

1.29 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 Tax Laws (Amendment) Act, 2024 and the Income Tax (Amendment) Act, 2026, 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, 114(6), 137, 138 and 140, 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.

4. **Recovery of Tax Demands:** Section 137 requires payment of demand within 30 days from service of notice and upon expiry of said time, Assessing Officer is required to issue Notice u/s 138 setting due date for payment of tax Demand. Thereafter, if Demand remains unpaid, then the Assessing Officer can proceed for recovery measures u/s 140.

There exists an apparent conflict between Section 134A (10) which requires payment of Demand within time decided by the ADRC whereas Section 137 & 138 require recovery of Demand after affording proper time. Superior Courts have repeatedly held that proper time be allowed to taxpayers for recovery of Tax Demands.

It has been noted that the ADRC issue their judgments near to month end and set unrealistic due dates. This creates conflict with other provisions of Income Tax Ordinance besides discrimination between SOE and non-SOE.

In order to remove this discrimination, it is proposed that the time of recovery of demand in case of orders passed by ADRC be aligned with that provided under section 137 and 138 of the Ordinance. The corresponding amendments be made in section 134A (10) to state that demand arisen as a result of ADRC order shall be payable within 30 days from service of such order to the taxpayer.

Further, in sub-section (7) of section 134A, the deemed stay against recovery of tax payable should start from the date of filing of application by the taxpayer for appointment of a committee under section 134A instead of constitution of such committee. Under the existing provision, the constitution of committee takes time during which the taxpayer remains exposed to the recovery of tax payable even it has already applied for the 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

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

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.

Further, like in case of appeal before Commissioner Appeals, a platform for online filing of application for ADRC and proceedings thereon should be introduced.

Rationale

This will result in imparting justice to the SOEs and will reduce the unnecessary disputes.

1.30 ASSESSMENTS & ORDERS SECTION 124 & 124(A)

HIGH

124(1)	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.*

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:

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, 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

it is suggested 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 from sub-sections (1) and (2) of section 124. Such restrictions were introduced to align these provisions with section 126A of the Ordinance through which the jurisdiction of appeal lying with Commissioner Appeals was restricted to 20 million rupees. Although section 126A has been omitted through Finance Act, 2025 and hence the restriction of twenty million rupees for appeal is also no more in the law, but the corresponding amendment in section 124 has not been made to remove the twenty million limits. Therefore, the provisions of section 124 need to be updated and aligned.

1.31 ISSUANCE OF SHOW-CAUSE NOTICES U/S 161

The current practice of issuing Show-Cause Notices under Section 161 of the Income Tax Ordinance, 2001 reflects procedural inconsistencies and often places undue pressure on taxpayers. Taxation Officers, during assessment monitoring, frequently extract figures directly from financial statements (e.g., Profit & Loss accounts) and challenge entire expense amounts without examining the underlying nature of transactions or valid justifications for non-deduction of tax.

Additionally, default surcharges and penalties are often computed for extended periods (up to five years), and notices are issued with limited response time (as short as seven days or less), restricting taxpayers' ability to present a proper defense. These practices deviate from the procedural guidance outlined in relevant FBR circulars and undermine principles of fairness and due process.

Recommendation

It is recommended that strict adherence to prescribed procedures for issuance of notices under Section 161 be ensured, in line with FBR Circular No. C.No. 3(08) SS(A&A)/2023 dated 19-02-2025. Adequate response time (minimum 15–30 days) should be provided, and officers should be required to conduct preliminary verification before issuing notices.

Rationale

Implementing procedural safeguards will:

- Ensure transparency and fairness in tax proceedings,
- Reduce unnecessary litigation and disputes,
- And enhance taxpayer confidence in the taxation system.

1.32 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 are available.

Recommendations

Appropriate provisions be introduced in the Ordinance to cater this anomaly.

1.33 SECTIONS 175 & 177 - ENTRY INTO PREMISES AND AUDIT: PROCEDURAL SAFEGUARDS

MEDIUM

Sections 175 and 177 grant extensive powers to tax authorities to enter business premises and select taxpayers for audit. Their unstructured and discretionary application has led to concerns regarding undue harassment of taxpayers, lack of procedural transparency, and inconsistent enforcement.

Under Section 175, tax authorities may enter and inspect business premises without a clearly defined requirement for advance notice or documented justification, creating risk of unannounced visits and misuse of authority. Under Section 177, audit selection based on Commissioner's discretion in addition to computerized selection which results in the perception of arbitrary or targeted audits and undermines voluntary compliance.

Recommendation

Two targeted amendments are proposed:

1. **Mandatory Notice Requirement under Section 175**

   Insert proviso in Section 175:

   "No entry into business premises shall be made without serving a prior notice of at least forty-eight hours to the taxpayer."

   Exception clause: "Provided that this requirement shall not apply in cases where the Commissioner, based on definite and credible information, has reason to believe that tax fraud or concealment of income is being committed."

2. **Risk-Based Audit Selection under Section 177**

   Amend Section 177 to provide:

   "Selection of cases for audit shall be made exclusively through a transparent, computer-generated risk-based system as prescribed by the Board."

Further add: "The criteria and parameters for such selection shall be documented and made publicly available to the extent consistent with enforcement requirements."

Rationale

The proposed reforms strike a balance between effective tax enforcement and protection of taxpayer rights. Mandatory notice requirement protects legitimate businesses from unnecessary disruption while maintaining enforcement effective in genuine fraud cases. Risk-based audit selection eliminates discretionary selection, enhances transparency and fairness, aligns Pakistan's tax system with international best practices, and encourages voluntary compliance. The Supreme Court of Pakistan has consistently emphasized that exercise of statutory powers must be reasonable, proportionate, and in accordance with due process.

1.34 SERVICE OF NOTICE

MEDIUM

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 physical service 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 the taxpayer 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.

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

MEDIUM

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 which is yet to be prescribed as per section 227E of the Ordinance.

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.

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

HIGH

Penalty is prescribed u/s 182 for non-furnishing of statement u/s 165, 165A, 165B or 165C is Rs.50,000, where tax is deposited within the due date and statement is filed after lapse of 90 days, in all other cases it is Rs. 2,500 for each day of default subject to a minimum penalty of Rs. 10,000.

Furthermore, the proviso under this provision is excessively stringent in situations where no tax was actually required to be deducted or collected. It imposes a minimum penalty even in cases where it is established that no deduction or collection obligation existed during the relevant period.

Recommendation

It is proposed that such exorbitant 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.

The existing Proviso in Serial No. 1A of the Table provided in section 182 should provide that no penalty shall apply in a case where it stands established that no tax was required to be deducted or collected during the relevant period. Or alternatively the word "minimum" used in such proviso be replaced with "maximum" to cap the maximum penalty in such cases to Rs. 10,000.

It is also proposed to insert an Explanation or another 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.

1.37 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.

1.38 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.

Through the Finance Act, 2025, these powers have been expanded to override any decision, order, or judgment issued by any forum, authority, or court. However, the exercise of such condonation powers has been limited to a period of two years, except in cases where a significant loss to the exchequer or to the taxpayer is involved. In such exceptional situations, these powers may be exercised without any time limitation.

Recommendation

Amendments made in Section 214A through Finance Act, 2012 and Finance Act, 2025 should be withdrawn.

The provisions of Section 214A, prior to amendment made through Finance Act, 2012 and Finance Act, 2025, implied that this power cannot be used in a manner detrimental to a taxpayer, however, by virtue of these amendments, 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.

1.39 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:

- Initial Review by Assessing Officer
- Secondary Review by Additional Commissioner
- 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 a much needed additional layer of scrutiny, thereby reducing the incidence of unjustified tax demands.

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

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.

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

- Filing of wealth statement by the resident persons:

    - 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 condition for furnishing wealth statement:

    - Sub-section (1) in its present form effectively 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.

- 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 statement under section 116A 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."

1.42 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.

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 one of 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 especially in view of provisions of section 113 (minimum tax on turnover) and section 113C (alternative corporate tax).

Recommendation

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

1.43 SECTION 111(4A) – UNEXPLAINED INCOME & CREDIT AGAINST INCOME SUBJECT TO FINAL TAX

HIGH

In section 111 – Unexplained income or assets, new sub-section 4A was introduced through the Finance Act, 2022 to provide that where a taxpayer explains the nature and source of an amount by referring to income subject to final tax, credit shall not be allowed in excess of imputable income. However, such excess may be allowed if following two cumulative conditions are satisfied:

(i) the excess amount is reasonably attributable to business activities subject to final tax; and
(ii) the taxpayer furnishes audited financial statements duly certified by a chartered accountant.

Currently, income streams under the Final Tax Regime include export of services, commission / discount on petroleum products, and lease of toll collection rights. In particular, export of services under Section 154A is subject to low final tax rates (0.25% to 1% of export proceeds), resulting in imputable income significantly lower than actual earnings.

In practice, especially in the case of IT exports and IT-enabled services, many service providers are non-corporate taxpayers and freelancers. While they can reasonably demonstrate that excess amounts are attributable to their business activities, they are often unable to meet the requirement of furnishing audited financial statements, primarily due to cost and compliance constraints. This creates unnecessary hardship and restricts legitimate claims.

Recommendation

It is proposed that the requirement of furnishing audited financial statements be made conditional, such that it is mandatory only where the taxpayer's annual revenue exceeds Rs. 10,000,000.

Rationale

This proposal will:

- Reduce undue compliance burden on freelancers and small service exporters,
- Facilitate ease of doing business in the IT and services sector,
- Allow genuine taxpayers to substantiate their income sources without excessive procedural barriers,
- And maintain the integrity of the provision while introducing practical flexibility based on taxpayer size.

1.44 TAX ON DEEMED INCOME – SECTION 7E

HIGH

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.

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 Rs. 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 increased to Rs. 100,000,000. Further this threshold instead be made overall exemption deductible, to arrive at the taxable value of capital assets, resulting into progressive taxation.

Definition and elaboration about Rentable Assets be provided, as land itself does not generate rental income so should not be considered for deemed income.

1.45 SECTION 7F AND INAPPLICABILITY OF SECTION 147(5C) IN THE PRESENCE OF SECTION 7F ON BUILDERS & DEVELOPERS

HIGH

With the introduction of Section 7F through the Finance Act, 2024, a new framework has been established for the taxation of builders and developers. However, the current mechanism has become complex and difficult to administer, leading to uncertainty in determining the applicable tax liability.

Further, through Finance Act, 2023, Section 147(5C) was inserted for advance tax payments based on per square feet/yard of area. Rate given for advance tax calculation was same as already given in Eleventh Schedule of the Ordinance to calculate tax chargeable by taxpayers for projects registered u/s 100D which was final tax regime but required to be paid quarterly as advance payment.

Through finance Act, 2024, section 7F was inserted which was applicable for tax year 2025 onward. Section 7F was inserted for taxation of Builders and Developers by linking taxable income to a fixed percentage of sale value (a form of deemed income basis rather than area-based). Section 147(5C) in its current form creates ambiguity after insertion of section 7F.

Recommendations

To ensure clarity, consistency, and effective implementation of taxation for builders and developers, it is proposed to prescribe comprehensive rules detailing the method, basis, and procedures for computing taxable income and tax under this newly introduced provision of the Ordinance.

It is proposed to amend Section 147(5C) to align advance tax computation with Section 7F (sale-value-based taxation), ensuring consistency and avoiding interpretational issues and also gaps in advance tax collection.

Rationale

The proposed amendment is necessary to remove inconsistency and ambiguity arising from overlapping provisions, ensuring a coherent and aligned advance tax mechanism that reflects the current sale-value-based taxation regime under section 7F and promotes clarity, fairness, and effective tax collection. This will help taxation on this sector across the country consistently.

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

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 behind 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 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 and 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 previously, 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's global income which no one disagrees with, as it is universally accepted. However, after taxing the income generated from the foreign assets, 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, depending on returns received 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 as 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 Rs. 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 investors 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 notified in USD or USD equivalent instead of Rupees. Further, this threshold instead made overall exemption deductible, to arrive at the taxable value of foreign assets, resulting into progressive taxation.

1.47 CAPITAL GAIN ON INHERITED ASSETS

HIGH

Previously, Section 37(4A) of the Income Tax Ordinance, 2001 provided that the Fair Market Value (FMV) at the date of transfer/acquisition shall be treated as the cost of a capital asset in certain cases. Finance Act 2022 omitted this provision.

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.

1.48 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

Considering 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
153(1)(a)	75,000	500,000
153(1)(b)	30,000	250,000

Furthermore, it is proposed that in the first proviso to clause (c) of sub-section (1) of section 21, the word "such" be inserted before the second occurrence of the word "purchases," to provide clarity that the disallowance applies to those purchases on which tax was not deducted at the time of payment.

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. Current threshold for cash salaries is even below the minimum wages prescribed by all the provinces.

1.49 SECTION 21(I) - APPLICABLE ON REVENUE EXPENDITURES AND NOT ON CAPITAL EXPENDITURES

Section 21(I) disallows expenditure paid otherwise than through banking channels (above prescribed limits). It applies to "expenditure" claimed in the Profit & Loss account, so it applies only to revenue expenses and does not extend to capital expenditure (fixed assets).

Section 75A specifically governs mode of payment for capital assets. It explicitly allows cash payments up to Rs. 1,000,000 for other assets and Rs. 5,000,000 for Immoveable property. This is a special provision for transactions of capital assets.

Recommendation

It is proposed to amend Section 21(I) of the Income Tax Ordinance, 2001 by inserting the words "excluding capital expenditure" after the word "expenditure" to clearly restrict the applicability of this clause to revenue expenditures only.

Accordingly, the amended wording will read as:

> *"any expenditure excluding capital expenditure, for a transaction, paid or payable under a single account head which, in aggregate, exceeds two hundred and fifty thousand rupees, made otherwise than through prescribed banking channels…"*

This amendment will explicitly clarify that disallowance under Section 21(I) does not apply to payments made for acquisition or addition of fixed assets, which are separately governed under Section 75A.

Rationale

The proposed clarification is essential to remove interpretational ambiguity and avoid overlap between sections 21(I) and 75A, ensuring that capital expenditures are governed exclusively by their specific provisions and preventing unintended disallowances on legitimate asset acquisitions.

1.50 RESTRICTED VALUE OF PASSENGER TRANSPORT VEHICLE

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. 12,000,000.

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.

Recommendation

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. 12,000,000.

1.51 INITIAL ALLOWANCE U/S 23

The rate of initial allowance on plant and machinery has been reduced to 25% whereas the initial allowance on buildings has been withdrawn.

Recommendation

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, 2014 and 2021.

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.

1.52 AMORTIZATION OF INTANGIBLES U/S 24

The maximum amortization period for intangibles with unascertainable useful life was set at 25 years and has been reduced to 15 years through Finance Act 2025, which is still excessive compared to depreciation allowances on tangible assets.

Recommendations

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. 15 years' period too is quite long as compared to the initial, normal and first year depreciation allowances available on tangible assets.

1.53 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 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.

1.54 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.

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.

Recommendation

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

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 jurisdiction.

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.

1.55 DIVIDEND PAID BY INDEPENDENT POWER PRODUCERS – 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.

Recommendation

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 ……."*

1.56 DIVIDEND PAID BY DEVELOPERS AND ENTERPRISES OF SPECIAL TECHNOLOGY ZONES

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 and employing fulltime fifty (50) persons or more in the tax year."

Rationale

Beyond immediate investment, this exemption serves as a catalyst for long-term economic growth by encouraging the scaling of technology zones. By reducing the effective tax burden on shareholders, the government can stimulate a robust venture capital ecosystem that supports job creation and enhances Pakistan's digital export footprint.

1.57 WITHHOLDING TAX ON PRIZES U/S156

HIGH

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

Recommendation

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 issue of samples, promotional giveaways and target incentives as 'prize', and accordingly demand 20% withholding tax.

1.58 REDUCTION IN WITHHOILDING TAX RATES

HIGH

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.

Recommendation

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

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

HIGH

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 MIS report available on IRIS does not capture the advance tax collected under various provisions of the Ordinance such as advance tax collected under section 235, 236 etc. Therefore, 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.

Recommendation

Integrate MIS so it captures all taxes deducted and collected at source, enabling automated verification of the taxes.

Rationale

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.

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

HIGH

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.*

Most 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.

Recommendations

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.

1.61 REINTRODUCTION OF TAX CREDIT FOR EMPLOYING FRESH GRADUATES – SECTION 64C

Section 64C, which previously provided a tax credit to employers hiring fresh graduates, was omitted through the Finance Act, 2021. Its removal reduced incentives for businesses

to onboard young talent, despite rising youth unemployment and the growing need for industry-relevant skill development.

Recommendation

It is proposed to reintroduce Section 64C, allowing a tax credit for businesses that employ fresh graduates from Higher Education Commission (HEC) recognized institutions. This incentive would encourage organizations to create more entry-level opportunities and invest in workforce development.

Rationale

This proposed measure will:

- Address youth unemployment,
- Encourage skill development and documentation, and
- Strengthens academia-industry linkages.

1.62 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 cumbrous, 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 non-profit 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 avoidable 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.

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

The availability of a tax credit under section 100C for Government grants and foreign grants is restricted to persons specified in sub-section 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.

1.64 SME SIMPLIFICATION – REVISION OF SMALL COMPANY THRESHOLD

The turnover threshold for classification as a “Small Company” has not been updated in line with inflationary factor.

Recommendation

It is proposed that the definition of "Small Company" be amended to increase the annual turnover threshold from Rs. 250 million to Rs. 400 million.

Rationale

The existing turnover threshold of Rs. 250 million has become outdated due to inflationary factors and the natural growth in nominal revenues over time. As a result, many small businesses are effectively excluded from the Small Company regime despite no significant change in their real economic size.

1.65 DOUBLE TAXATION ON SPECIE DIVIDEND

Under the current law, the gross amount of specie dividend is 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 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.

1.66 STATUS OF LIMITED LIABILITY PARTNERSHIP

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).*

1.67 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

This exemption will encourage the development of organized agricultural infrastructure, leading to better resource management and sustainable farming practices. Corporate farming ventures provide a formal platform for significant CAPEX in irrigation and soil health, which are currently unfeasible for small-scale, fragmented landholders.

1.68 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.

Recommendation

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.

1.69 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.

Recommendations

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.

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

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

> *"(1) 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.*
>
> *(2) 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.*
>
> *……..*
>
> *(5) 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.

1.71 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	**Clause (126EA) (b), Part I, 2nd Sch.** zone Enterprises as defined in the Special Technology Zones Authority Act, 2021	No provision in the Income Tax Ordinance, 2001 granting exemption from:

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;	(XVII of 2021) for a period of ten years from the date of issuance of license by the Special Technology Zone Authority; and **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	a. Withholding taxes (except u/s 148 on import of capital equipment); b. Capital gain tax; c. Withholding tax on dividend; and d. Minimum taxes other than under section 113.

	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;	

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 the aforesaid date shall be for the next five years.	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 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	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 30, 2020, is missing in the Ordinance. c. Exemption from minimum taxes including on turnover, not provided in Income Tax Ordinance, 2001

	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.	

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.

1.72 TAXATION OF CRYPTO

HIGH

Crypto, as a decentralized digital currency, is gaining traction globally and in Pakistan, offering potential benefits and challenges. The rising use of crypto in Pakistan necessitates a formal regulatory and taxation framework to prevent financial instability and illicit activities. This proposal seeks to regulate crypto transactions, generate government revenue, and ensure transparency within the digital financial ecosystem.

Recommendation

It is proposed that a comprehensive taxation and regulatory framework for crypto assets be introduced under the Income Tax Ordinance, 2001, recognizing crypto as a distinct and emerging class of digital assets.

Rationale

Crypto assets represent a rapidly growing and largely undocumented segment of economic activity in Pakistan. At present, the absence of a clear legal and taxation framework has resulted in this sector remaining an untapped source of revenue, with minimal contribution to the national exchequer despite increasing adoption.

The lack of regulation also poses risks related to tax evasion, money laundering, and capital flight, while creating uncertainty for legitimate investors and businesses operating in this space.

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

HIGH

It is estimated that half of the remittances inflows are charged at a 1% tax rate while the other half (being PSEB registered) pay 0.25% both under 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 m
○ Non-PSEB registered companies Tax (1% tax):	US$20m
Total:	**US$ 25 m**

Recommendation

The current FTR for IT & ITeS Exporters registered with PSEB @ 0.25% is valid till June 2026, however this restriction is not relevant in other cases whether FTR is @1%.

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

Extending 0.25% FTR for entities registered with PSEB for 10 years in the Finance Bill 2026 will provide long term predictability and semblance of stability to the industry and therefore facilitate high quality growth to this sector at reduced tax rate of 0.25%.

1.74 DISTINCTION BETWEEN FREELANCERS AND REMOTE WORKERS

HIGH

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

The definitions of freelancers and remote workers be included in the Finance Bill 2026 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/ not entitled to structured employment benefits such as health insurance or pensions, and is 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

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 introduction of these 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.
- The prevalence of remote work arrangements, coupled with 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.

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

HIGH

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.

Recommendation

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.

Rationale

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 those other countries provided to their technological 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.

1.76 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.

Recommendation

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.

Rationale

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.

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

In order to expand IT sector in Pakistan, establishing new ventures and then converting them into companies should be facilitated. Also, capital gain on first-time sale of shares of such IT companies may please be considered for granting exemption.

Recommendation

Capital gain on disposal of shares of start-up companies and export-oriented IT & ITeS companies should be exempted through the insertion of the appropriate clause in Part I of the Second Schedule while withholding tax exemption should 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.

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

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.

Recommendation

Tax on dividend paid by start-up companies and export-oriented IT & ITeS companies to their shareholders should be exempted while withholding tax exemption should also be given.

Tax on dividends discourages corporatization primarily due to the double taxation effect it creates.

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.

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

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.

Recommendation

Exporters of IT & IT enabled Services were eligible for 100% tax credit under section 65F, therefore, exemption from levy of super tax under section 4C for the tax year 2022 may please 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.

1.80 PROPOSED CHANGE IN STARTUP DEFINITION

Current definitions by SECP & FBR are not harmonized, keeping startups separate from tax incentives. Currently, the differences between the afore-mentioned definitions are as follows:

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)

Recommendation

Section 2(62A) of the Income Tax Ordinance, 2001 should be amended to align the definition of startups with the Companies Act, 2017.

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.

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

HIGH

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.

Recommendation

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.

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

Clarification to be made for avoidance of ambiguity.

Recommendation

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. Removing the ambiguity surrounding the 'actual buyer' will foster a more transparent tax environment for foreign suppliers. This amendment ensures that the act of selling goods to Pakistan does not create a taxable presence for the seller, thereby encouraging a seamless flow of essential imports and technology transfer.

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

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.

Recommendation

It was observed that 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 as having a PE as per newly inserted clause (g) of Section 2(41).

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.

Rationale

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

1.84 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 20% /

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.

1.85 REPRESENTATIVE U/S 172

LOW

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.

Recommendation

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.

1.86 FOREIGN DIRECT INVESTMENT ("FDI")

HIGH

Foreign direct investment in Pakistan is not increasing much and requires immediate attention.

Recommendation

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 Pakistani 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.

1.87 TRANSFER PRICING ECOSYSTEM NEEDS EXPANSION IN PAKISTAN

HIGH

Pakistan's transfer pricing framework has been gradually aligned with OECD guidelines through provisions relating to Master File, Local File, and Country-by-Country Reporting (CbCR). However, key mechanisms such as Advance Pricing Agreements (APAs), Safe Harbor Rules, and specific guidance on Cost Contribution Arrangement /Cost Sharing Arrangements (CCAs/CSAs) remain limited, resulting in non-availability of agreed mechanisms otherwise available in global best practices under the OECD guidelines for avoidance of interpretation and disputes and also reduction of administrative.

Recommendation

It is proposed that the transfer pricing framework in Pakistan be strengthened through the following measures:

a. Introduction of Advance Pricing Agreement (APA) regime through legislative amendments, including unilateral, bilateral, and multilateral APAs, integrated with Mutual Agreement Procedures (MAPs);
b. Issuance of comprehensive rules for Cost Contribution Arrangements (CCAs) and Cost Sharing Arrangements (CSAs) to provide clarity on intra-group cost allocations;
c. Introduction of Safe Harbor Rules for specified transactions and sectors to reduce compliance burden and provide certainty to taxpayers;
d. Strengthening and streamlining of three-tiered documentation requirements (Master File, Local File, and CbCR) with clear thresholds and reduced compliance burden for smaller entities;
e. Capacity building within tax authorities to effectively administer complex transfer pricing mechanisms.

Rationale

The absence of certainty-driven mechanisms increases the risk of disputes, double taxation, and compliance costs for taxpayers.

The proposed measures will:

- Provide upfront certainty and reduce litigation through APAs;
- Simplify compliance and administration via Safe Harbors;
- Ensure clarity in intra-group arrangements through CCA/CSA guidance;
- Maintain transparency while avoiding excessive compliance burden.
- Overall, these reforms will align Pakistan with global best practices, improve investor confidence, and promote a predictable and efficient tax environment.

1.88 TEMPORARY (SHORT TERM) REGISTRATION UNDER INCOME TAX ORDINANCE

HIGH

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 served 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.

Recommendation

To address these challenges effectively, it is proposed to introduce 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.

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

HIGH

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).

Recommendation

It is proposed that 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.

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

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.

Recommendation

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.

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

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.

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

Recommendation

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.

Rationale

This is for the avoidance of unnecessarily extending the scope of Pakistan source income and also resident individuals in Pakistan being considered representatives of non-residents due to business connections.

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

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.

Recommendation

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.

Rationale

This will help simplification of taxation of these non-residents and avoidance of challenge from the field officers.

1.93 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 discharged 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 organization 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.

Recommendation

It is proposed to 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.

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 on Active Taxpayers List at about 189 K in April 2026 (210 K in April 2025) when compared with taxpayers for income tax of over 7.3 million in April 2026 (over 6.7million in April 2026), we find that there is reduction in sales tax ATL while increase in income tax ATL. 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.

Recommendation

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, SRB & 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, in certain cases 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.

Recommendation

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

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.

Recommendation

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.

Recommendation

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*".

Recommendation

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.

Recommendation

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 as well as Digital Invoicing 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 INPUT TAX CREDIT ON BUILDING MATERIALS – SECTION 8(1)(h)

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.

Recommendation

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.

2.08 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.

Recommendation

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.

2.09 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.

Recommendation

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 through filing of special annexure in monthly Sales Tax Return by the taxpayer. Hence, in this way, the requirement for approval can 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.

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

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.

Recommendation

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.

2.11 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.

Recommendation

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.

2.12 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.

Recommendation

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.

2.13 ANNEXURE H - FASTER SYSTEM FOR SALES TAX REFUND PROCESSING

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.

Recommendation

The FASTER system should be upgraded to allow for the inclusion of brought-forward input balances, provide an option for consolidated annual Annexure-H filing, and incorporate a dedicated mechanism for adjusting carry-forward balances.

Rationale

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

2.14 SERVICE OF ORDERS & DECISION U/S 56 OF STA

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.

Recommendation

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 physical delivery of notices and orders (as was done prior to introduction of electronic delivery) along with sending text messages on registered mobile number of tax taxpayers.

"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. Further, an intimation regarding the notices, orders, etc. shall also be sent in form of text messages on registered mobile number of the taxpayers.

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.

2.15 CONDONATION OF TIME LIMIT U/S 74 OF STA

MEDIUM

In terms of Section 74 of the STA read with notification SRO 1444(I)/2024 dated 12-09-2024), the Commissioner and the Board are allowed to condone a lapse of one year and more (maximum two years in aggregate and further by committee of members) 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.

Recommendation

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 responding to taxpayers' genuine issues.

2.16 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.

Recommendation

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.

2.17 SHOW CAUSE NOTICES U/S 11E OF STA

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.

Recommendation

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 or refund 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.

2.18 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.

Recommendation

It is proposed to insert a proviso in Section 11F of the STA as follows:

"Provided that, at the time of recovery of tax under this section, 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.

2.19 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.

Recommendation

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.

2.20 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.

Recommendation

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.

2.21 POWER TO ARREST U/S 37A AND 38B (TOTALLY AMENDED AS MAJOR CHANGES LAST YEAR)

HIGH

Sections 37A and 37B of the STA have been added which authorize the Inland Revenue officers to arrest individuals involved in suspected tax fraud or prosecutable offences, subject to prior approval of the Commissioner. For offences involving a company, the CEO, practically CFO, and responsible directors may also be arrested, without absolving the company of its tax liabilities. All arrests must follow the Criminal Procedure Code, unless inconsistent with the Act. Additionally, with the Commissioner's approval, an officer not below Assistant Commissioner may arrest any person who abets tax fraud or related offences.

Recommendation

These sections must be abolished immediately for strengthening taxpayers' confidence in justice system.

Rationale

Such an open-ended power could lead an environment of fear for businesses and leaves taxpayers vulnerable to harassment.

2.22 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.

Recommendation

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.

2.23 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.

Recommendation

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).

2.24 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.

Recommendation

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.

2.25 INVENTORY RECORD FOR GOODS DESTROYED – RULE 23

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.

Recommendation

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.

2.26 INITIATION OF RECOVERY ACTION - RULE 71

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.

Recommendations

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

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

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

2.27 SALES TAX WITHHOLDING – ELEVENTH SCHEDULE

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.

Recommendation

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 IMPROVEMENTS/AMENDMENTS IN SALES TAX RETURN

Several Changes are made on FST return on IRIS, without taking the stakeholders in in loop leads to 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.

Recommendation

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.

2.29 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.

Recommendation

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.

2.30 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.

Recommendation

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.

2.31 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.

Recommendation

Reinsert Clause 6A of the Fifth Schedule to the Sales Tax Act, 1990, to restore zero-rating on the supply of capital goods to Export Processing Zones, thereby aligning sales tax policy with existing customs laws and international export standards.

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

MEDIUM

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.

Recommendation

Reinstating the exemptions under Serial Nos. 149 and 150 of the Sixth Schedule and withdrawing Minimum Value Addition Tax on plant and machinery imports for manufacturers will unlock critical cash flows and encourage industrial expansion without causing any net loss to permanent revenue

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

MEDIUM

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,

Recommendation

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.

2.34 INVOICE INTEGRATION

MEDIUM

FBR through various Sales Tax General Orders issued from time-to-time notified list of persons required to integrate their POS with the FBR's System, non-compliance to which results in disallowance of 60% of the input tax claimed and imposition of penalties.

The taxpayers who did not meet the criteria for Tier-1 Retailer had to file application before the Concerned Commissioner for exclusion from the list, and the Concerned Commissioner would make a decision in this regard in accordance with the procedure laid down in STGO 17 of 2022, dated 13.05.2022.

Later on, FBR through its S.R.O no. 709(I)/2025 dated 22-04-2025 have now required all Corporate and Non-Corporate taxpayers registered for sales tax to electronically integrate their hardware and software systems with the Federal Board of Revenue's (FBR) computerized system through a licensed integrator and to issue electronic invoices, in accordance with the rules contained in Chapter XIV of the Sales Tax Rules, 2006.

Recommendation

A notification or clarification should be issued by the FBR to determine whether integration (Digital Invoicing) carried out in compliance with S.R.O. No. 709(I)/2025 is sufficient for the purpose of the aforesaid removal of disallowance under Section 8B(6) of the Sales Tax Act, 1990, or whether the taxpayer is still required to specifically integrate its system with the FBR POS system as stipulated under Sales Tax General Order No. 01 of 2024 dated April 23, 2024, or to file an application before the concerned Commissioner for exclusion from the list.

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.

Recommendation

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.

Recommendation

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.

Recommendation

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.

Recommendation

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.

Recommendation

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.

Recommendation

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 along with sending text messages on registered mobile number of tax taxpayers.

Recommendation

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. Further, an intimation regarding the notices, orders, etc. shall also be sent in form of text messages on registered mobile number of the taxpayers.

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.

Recommendation

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.

Recommendation

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.

KEY RECOMMENDATIONS CUSTOM ACT

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.

Recommendations

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.

4.2 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.

Recommendation

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 ad hoc 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.

4.3 REDUCTION OF IMPORT DUTIES ON IT EQUIPMENT

Recommendation

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.

PART-II

SALES TAX ON SERVICES

REFERENCE INDEX

KEY RECOMMENDATIONS

ISLAMABAD CAPITAL TERRITORY (ICT) SALES TAX ON SERVICES

5.1 SALES TAX ON SERVICES OF ACCOUNTANTS AND AUDITORS

HIGH

At present, services provided by accountants and auditors in ICT are subject to a sales tax rate of 15%, which is the highest in the country compared to the rates applicable in any of the provinces.

Recommendation

It is recommended that the sales tax rate on these services be reduced to 5% across ICT, without the facility of input tax adjustment.

Rationale

Accounting and auditing firms, as well as individual practitioners operating in ICT, face significant competitive pressure due to the comparatively higher sales tax rate of 15%. This disparity is particularly detrimental to new firms seeking to establish their practices in ICT, as it places them at a disadvantage compared to counterparts in neighboring provincial jurisdictions of Punjab and KPK where tax rate of 5% is attracted.

In the longer term, reducing the rate would prove beneficial for revenue generation, as it would encourage business activity to remain within ICT rather than shifting to provinces, thereby potentially increasing overall tax collection.

PROVINCIAL SALES TAX ON SERVICES
SINDH SALES TAX ON SERVICES

6.1 STATUTORY INPUT RIGHT

LOW

Recommendation

It is proposed that input tax adjustment be reaffirmed as a statutory right. All caps (such as the 90% rule) should be removed to ensure the tax functions as a true value-added tax.

Rationale

A true VAT taxes only value addition. Removing caps restores neutrality, improves cash flow, and reduces compliance burdens.

6.2 OPERATIONALIZE THE NSTR

LOW

Recommendation

The National Sales Tax Return portal should be fully operationalized with automatic inter-treasury transfers to allow a single return for all jurisdictions.

Rationale

A single return reduces compliance costs for multi-provincial businesses and facilitates seamless input tax adjustments across provinces.

6.3 PLACE OF SUPPLY RULE

LOW

Recommendation

The "Place of Provision of Services Rules" should be embedded directly into the primary Acts rather than left to subordinate notifications, providing better legal certainty for trans-provincial businesses.

Rationale

Statutory rules are more stable and legally certain than notifications, reducing disputes over jurisdiction.

6.4 NEGATIVE LIST TRANSITION (SINDH FINANCE ACT, 2025)

Recommendation

Sindh has shifted to a "Negative List" regime, redefining "service" under Section 2(79) to include any activity or advantage provided for consideration, and has adopted the UN Central Product Classification (CPC) system. It is proposed that Sindh expressly incorporate the "principal supply" test into the SSTSA to prevent arbitrary classification of bundled services by tax officers.

Rationale

The principal supply test provides objective criteria for bundled services, reducing disputes and ensuring consistent treatment.

PUNJAB SALES TAX ON SERVICES

7.1 DEFINITION OF "SERVICE", "TAXABLE SERVICE" AND "ECONOMIC ACTIVITY"

Sections 2(38), 3 and 6 define "service", "taxable service" and "economic activity" in exceptionally broad and open-ended terms, treating virtually every activity that is not goods as a service and including one-time, incidental and ancillary activities within "economic activity". This creates serious uncertainty. The absence of statutory guidance on bundled or composite transactions leads to frequent disputes, retrospective demands, and inconsistent classifications by the Authority.

Recommendation

It is proposed that the Act expressly incorporate statutory principles such as the dominant-nature test or principal-supply test for bundled and composite supplies. Clarifying provisions should also be added for reimbursements, incidental supplies, and mixed contracts to provide certainty and prevent arbitrary classification.

Rationale

Certainty in classification reduces litigation and promotes voluntary compliance. A clear statutory framework for bundled supplies aligns with international VAT best practices.

7.2 EXCESSIVE DELEGATION THROUGH NOTIFICATIONS

Sections 5, 10 and 12 allow fundamental elements of tax policy – taxable services, rates, thresholds and exemptions – to be altered through notifications. This over-reliance on delegated legislation reduces parliamentary oversight, creates uncertainty, and exposes taxpayers to frequent and abrupt policy changes.

Recommendation

It is proposed that major policy decisions affecting tax incidence and scope be embedded in the Act itself. Notifications should be limited to procedural matters and be subject to sunset clauses and mandatory impact assessments.

Rationale

Legislative oversight ensures democratic accountability and predictability. Limiting delegated powers protects taxpayers from arbitrary or frequent changes.

7.3 RESTRICTION OF INPUT TAX CREDIT AND VAT NEUTRALITY

Sections 16, 16A, 16B and 16C regulate input tax adjustment but, taken together, weaken the basic VAT principle of tax neutrality. Although section 16 appears to allow deduction of input tax, this right is largely restricted by later provisions through strict procedures, broad disallowances and adjustment limits. Section 16A denies credit for mere payment-mode defects, section 16B disallows credit even where buyers are compliant but suppliers are not, and section 16C caps adjustment regardless of actual tax paid. Collectively, these provisions increase complexity, block working capital, cause tax cascading and excessive litigation.

Recommendation

It is recommended that the regime be simplified and realigned with VAT fundamentals by reaffirming input tax adjustment as a statutory right where tax is actually borne and inputs are used in taxable services. Disallowances should be limited to genuine fraud or abuse, procedural lapses made regularizable, supplier non-compliance not defeat a bona fide buyer's credit, and the adjustment cap repealed or narrowly targeted with efficient refund mechanisms.

Rationale

A true VAT taxes only value addition, not compliance imperfections. Restoring neutrality improves cash flow, reduces litigation, and encourages formalization.

7.4 NEED FOR STATUTORY CLARIFICATION BETWEEN ASSESSMENT (SECTION 24) AND RECOVERY (SECTION 52)

Sections 24 and 52 suffer from structural overlap and ambiguity because both deal with unpaid, short-paid or escaped tax without clearly defining their functional boundaries. Section 24 is intended as a quasi-judicial assessment provision, while section 52 is styled as a recovery provision – yet section 52 itself authorizes show-cause notices and determination of tax not levied, effectively functioning as a parallel assessment mechanism. This has allowed recovery proceedings to be initiated before tax liability is finally assessed, leading to coercive enforcement, duplication, and violation of due process.

Recommendation

It is proposed that the law be clarified to expressly separate determination from recovery: section 24 should be the exclusive provision for assessment (including escaped assessment and wrong refunds), and section 52 limited strictly to recovery of tax already determined, admitted, or finalized. A clear sequencing clause should be inserted so that section 52 may be invoked only after liability under section 24 has attained finality, except for admitted tax or narrowly defined fraud cases with safeguards.

Rationale

Due process requires that tax be determined before recovery. Separation of functions prevents coercive enforcement without a final liability order and reduces litigation.

7.5 CONCENTRATION OF DISCRETIONARY AND ADJUDICATORY POWERS

Sections 39 to 41 and section 60 confer expansive discretionary powers on tax officers relating to jurisdiction, adjudication, reassignment of cases, and enforcement. These provisions lack sufficient procedural safeguards, resulting in inconsistent enforcement and erosion of taxpayer confidence.

Recommendation

It is proposed that the Act require reasoned written orders, mandatory opportunity of hearing, and internal independent review before exercising significant discretionary or adjudicatory powers, except in clearly defined fraud cases.

Rationale

Procedural safeguards ensure fairness, reduce arbitrariness, and build trust in the tax administration.

7.6 DISPROPORTIONATE PENALTIES

Section 48 prescribes high and often automatic penalties for a wide range of defaults, including purely procedural lapses. The absence of proportionality or differentiation between minor non-compliance and serious evasion creates undue hardship, particularly for small and medium businesses.

Recommendation

It is recommended that a graduated penalty regime be introduced, including warnings for first-time defaults and mitigation where no revenue loss occurs. A statutory proportionality principle should be expressly incorporated.

Rationale

Proportionate penalties encourage compliance without destroying businesses. Differentiating minor errors from fraud is consistent with natural justice.

7.7 SEALING OF PREMISES AND DIGITAL SURVEILLANCE

Sections 59A and 59B empower the Authority to seal business premises and impose extensive electronic monitoring, including electronic invoicing and video surveillance, with limited statutory safeguards for necessity, proportionality, and data protection.

Recommendation

It is proposed that the Act require prior hearing (except in fraud cases), limit sealing to last-resort situations, and incorporate explicit data-protection principles such as purpose limitation, data minimization, and independent oversight of surveillance mechanisms.

Rationale

Intrusive enforcement measures must be proportionate and subject to checks to prevent abuse and protect taxpayer rights.

7.8 APPEALS AND ALTERNATE DISPUTE RESOLUTION

Sections 63 to 67 establish appellate forums that remain institutionally linked to the tax administration, while section 69 provides for ADR without clear binding effect. This undermines perceived independence and contributes to prolonged litigation. Further, the ADR mechanism has not been implemented.

Recommendation

It is proposed that the institutional independence of appellate authorities be strengthened through independent appointments and security of tenure. ADR outcomes should be binding except in fraud cases, with clear timelines for implementation. The ADR mechanism as provided in federal tax laws (income tax and sales tax) should be adopted

and implemented to reduce tax litigation and speed up tax recovery.

Rationale

Independent appellate forums and binding ADR reduce pendency, lower litigation costs, and improve taxpayer confidence.

7.9 ENFORCEMENT-CENTRIC DESIGN OF THE ACT

Taken collectively, the charging provisions, penalties, enforcement powers, and recovery mechanisms reveal an enforcement-centric legislative design that prioritizes coercion over facilitation. This undermines voluntary compliance, investor confidence, and long-term revenue sustainability.

Recommendation

It is proposed that the Act be recalibrated toward a compliance-driven model by codifying taxpayer rights, reducing unchecked discretion, strengthening certainty, and fostering a cooperative relationship between taxpayers and the Authority.

Rationale

A cooperative, compliance-focused regime yields higher voluntary compliance and sustainable revenues than a purely coercive approach.

7.10 RATE OF SALES TAX

Currently the standard rate of sales tax is 15% in all provinces except Punjab, where it is 16%. This creates discrimination and needs correction.

Recommendation

It is recommended to amend the second schedule of the Punjab Sales Tax on Services Act 2012 to revise the general rate for sales tax to 15% instead of 16%.

Rationale

Uniform rates across provinces eliminate competitive distortions and align Punjab with the rest of the country.

BALOCHISTAN SALES TAX ON SERVICES

8.1 PHASED BLOCKCHAIN REGISTRIES FOR INTER-PROVINCIAL SETTLEMENT

MEDIUM

Recommendation

It is proposed to enable phased blockchain registries for inter-provincial settlement (similar to the Brazilian market). Smart contracts should be used to automate the "Place of Supply" logic. When a service is billed, the contract automatically settles the input tax adjustment across provincial borders in real-time, eliminating current manual reconciliation delays that block business liquidity.

Rationale

Blockchain-based automation reduces disputes, accelerates cross-provincial adjustments, and improves cash flow for businesses.

8.2 INCENTIVE-DRIVEN TAX BASE / DOCUMENTATION CASHBACK

Recommendation

Instead of using coercion or penalties for digital payments, it is proposed that the government offer a direct tax refund (cashback) to consumers who pay via digital platforms (Raast/Cards). A portion of the provincial sales tax collected can be credited back to the consumer's wallet automatically, creating a self-enforcing documentation cycle where citizens demand tax invoices for their own benefit.

Rationale

Positive incentives are more effective and less regressive than penalties. Cashback encourages digital payments and voluntary invoice seeking, broadening the tax base sustainably.

PART-III

HARMONIZATION OF TAX LAWS

REFERENCE INDEX

HARMONIZATION OF TAX LAWS

9.1 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.

9.2 INTEGRATION OF TAXATION AUTHORITIES FOR ONE-WINDOW SOLUTION

HIGH

Recommendation

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 for organizations.

It is also proposed that company registration with the SECP, FBR and all provincial tax authorities also be integrated into a one window solution. This would significantly reduce time required for registration and commencement of business by substituting registration requirements with multiple authorities. Furthermore, it would also ensure that all companies are automatically registered with all tax authorities, in turn increasing transactional visibility for enforcement authorities.

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.

9.3 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.

Recommendation

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.

9.4 EXPANDING THE SCOPE OF PLACE OF PROVISION OF SERVICE RULES

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.

Recommendation

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, in turn improving ease of doing business.

9.5 ZERO RATING OF EXPORT OF SERVICES

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.

Recommendation

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.

In Punjab it is advisable that export of services be made zero rated through amendments in the Act itself rather than the rules. The language would also need to be made unambiguous as under the existing provisions the zero-tax rate is allowed to services delivered or used outside Pakistan however no clarity has been provided on what would constitute "delivered or used outside Pakistan"

Rationale

This measure will help in promoting export of services and can be instrumental in enabling the government to increase its foreign exchange reserves and reduce Current account deficit.

9.6 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.

Furthermore, the changes to withholding rules of Punjab Sales tax brought about in 2025 have contributed to ambiguity. It is recommended that the language of Rule 5 of the Punjab Sales Tax on Services (Withholding) Rules, 2015 be revisited to add more clarity.

Secondly, *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	20% for registered persons; 100% for unregistered persons
Punjab	Other than Active Companies 100%; For Active Companies 20%, except for advertisement services; Telecommunication, banking and insurance companies to withhold 80% except on advertisement services.
KPK	Other than Active Persons 100%; For Active persons 50%
Balochistan	20% for registered persons; 100% for unregistered persons

Recommendation

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

The proposal aims to avoid unwarranted administrative and operational issues as well as to minimize cost. 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. This will also reduce the sales tax withholding related litigation.

9.7 CLASSIFICATION OF TAXABLE SERVICES RULES

The Provincial and ICT tax laws have not addressed the following:

I. classification of services that simultaneously falls under more than one 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. Importance of having clear and unambiguous classification of services has become more importance especially since all four provinces has amended their respective Acts to introduce negative list of services. Clarity would help taxpayers ascertain if their services are exempt, higher rated or reduced rated.

A line of demarcation also 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.

Recommendation

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.

The 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.

9.8 H.S CODES / TARIFF HEADINGS TO VARIOUS SERVICES IN FIRST SCHEDULE

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.

Recommendation

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 in sales tax laws and promote uniform tax positions across provinces.

9.9 SALES TAX ON SERVICES OF ACCOUNTANTS AND AUDITORS, AND CREDIT RATING SERVICES

Currently, the services of accountants and auditors, and credit rating services are subject to varied rates under the Provincial Sales Tax laws in the following manner:

Provincial Law	*Applicable Rate*
Sindh Sales Tax	*8% without input tax adjustment*
Punjab Sales Tax	*5% without input tax adjustment*
KPK Sales Tax	*5% without input tax adjustment*
Balochistan Sales Tax laws	*8% without input tax adjustment.*
Islamabad Sales Tax laws	*15%*
Provincial Law	***Applicable Rate***
Sindh Sales Tax	*15%*
Punjab Sales Tax	*16%.*
KPK Sales Tax	*10%, without input tax adjustment, for services rendered by non-corporate special agencies*
Balochistan Sales Tax laws	*15%*
Islamabad Sales Tax laws	*15%*

Recommendation

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.

9.10 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*

Recommendation

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.

9.11 ISSUE OF TAXATION OF DISTRIBUTORS

Recent amendments introduced through the respective provincial Finance Acts, 2025–26 across all provinces have fundamentally altered the scope of provincial sales tax on services. Previously, only services expressly listed in the relevant schedules were taxable. The schedules now instead specify exempt services or those subject to reduced or higher rates, effectively broadening the tax base to cover all services unless specifically excluded.

In this context, "Supply Chain Management or Distribution (including delivery) Services" continue to be treated as taxable services under all provincial laws. Since the Mubashir Traders Judgment, provincial revenue authorities, particularly the Sindh Revenue Board, have increasingly initiated enforcement actions, including issuance of registration notices to distributors.

This has created significant uncertainty, as prevailing industry practices treat distribution arrangements as trading activities involving transfer of title in goods, rather than the provision of services.

Recommendation

It is therefore proposed that:

(i) a clear and uniform definition of "Supply Chain Management or Distribution (including delivery) Services" be introduced under provincial sales tax laws, in consultation with federal and provincial authorities; and

(ii) the levy of sales tax be expressly restricted to arrangements where no transfer of title in goods occurs, thereby excluding pure trading transactions from the ambit of services taxation.

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.

9.12 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.

Recommendation

A uniform definition of "Value of taxable service" needs to be drafted.

Rationale

To avoid unnecessary litigation.

9.13 ONLINE INTEGRATION AND REAL-TIME REPORTING OF SALES

Various provisions relating to real-time reporting of sales and receipts under different tax statutes (including sales tax, provincial and income tax laws) are not aligned in terms of

scope, implementation mechanisms, and reporting formats.

Recommendation

It is recommended that a unified and synchronized framework for real-time reporting of sales and receipts be introduced across all federal and provincial tax laws.

Rationale

A harmonized real-time reporting regime will eliminate inconsistencies across tax laws, reduce compliance burden for taxpayers, and improve data accuracy and transparency.

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	90% 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 per recipient	All payments above 50,000 per recipient
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 15% allowed	N/A	Up to 15% allowed
Input tax adjustment under reverse charge	Disallowed	Disallowed	Allowed	N/A	N/A
Assessment Proceedings and Records					

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. 100 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 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	Interbank+3 %	Interbank+3 %	24% p.a.	12% p.a

	plus 3% p.a, whichever is higher				
Others					
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

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% Company, 100% others	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	-

Sales Tax Withholding Requirements
Annexure-II

PART-V

BROADENING OF TAX BASE

REFERENCE INDEX

BROADENING OF TAX BASE

10. 1 BROADER CHALLENGES & PROPOSED SOLUTIONS

Pakistan's population is estimated at approximately 255–256 million. Despite this, only about 5.9 million individuals filed income tax returns for the tax year 2024–25. 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.

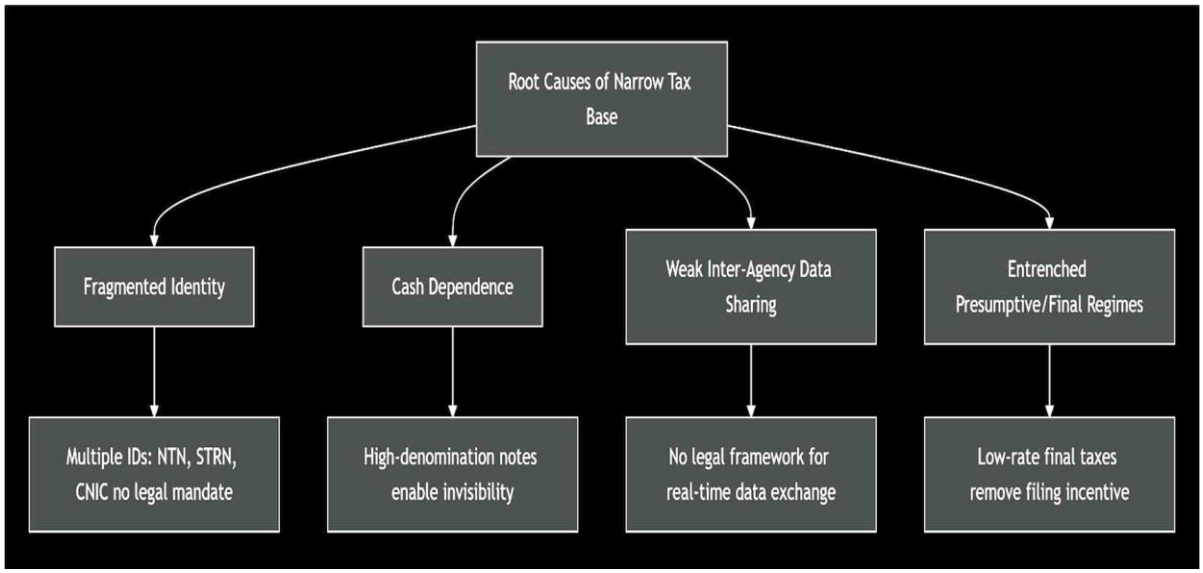
10.2 THE DIAGNOSTIC: WHY PAKISTAN'S TAX BASE REMAINS NARROW

Before prescribing solutions, it is essential to understand the structural drivers of tax base narrowness.

Key Indicators of the Tax Gap

Indicator	Current Estimate	Benchmark (Comparable Economies)
Tax-to-GDP Ratio	<10%	15–18% (South Asia average, excl. Pakistan)
Active Income Tax Filers	~3.2 million	<5% of labor force
Registered Retail Outlets	<200,000	Out of ~3.5 million total
Real Estate Tax Contribution	<0.5% of GDP	2–3% of GDP in documented economies
Cash in Circulation (as % of GDP)	>25%	<10% (digital economies)

Structural Root Causes



Recommendation

Piecemeal reforms have failed. A systemic, integrated overhaul is required.

10.3 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.

10.4 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.

10.5 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.

10.6 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.

10.7 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.

10.8 FIXED INCOME TAX REGIME FOR SMALL RETAILERS

MEDIUM

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.

10.9 CAPACITY BUILDING OF REVENUE AUTHORITIES

HIGH

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.

10.10 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.

10.11 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 PKR 600,000 is to be treated as below taxable limit thus annual income above this limit (which arrives at PKR 50,000 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.

10.12 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.

10.13 WITHDRAWAL OF TOTAL EXEMPTIONS FROM TAX

MEDIUM

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.

10.14 TAX ON INCOME OF SOCIAL AND SPORTS CLUBS

MEDIUM

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.

10.15 MEASURE FOR CURBING MASSIVE UNDER-INVOICING

MEDIUM

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.

10.16 FILING OF "NIL" INCOME TAX RETURN TO GAIN ACTIVE STATUS

MEDIUM

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.

10.17 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.

10.18 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.

10.19 DISALLOWANCE OF INPUT FOR NON-INTEGRATED RETAILERS

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.

10.20 ENHANCEMENT OF SALES TAX RATE FOR TIER-2 RETAILERS

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.

10.21 DEVELOPMENT OF DATA SCIENCES AND DATA ANALYTICS DEPARTMENT AND USE OF TECHNOLOGY

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.

10.22 MANDATORY INTEGRATION OF POINT OF SALE (POS) SYSTEMS

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.

10.23 MANDATORY NTN REGISTRATION OF INFORMAL SECTOR

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.

10.24 REGULAR AND TARGETED SURVEYS OF VARIOUS MARKET SECTORS

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.

10.25 MANDATORY REGISTRATION OF NPO'S OPERATING IN PAKISTAN

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.

10.26 COLLABORATION WITH PROVINCES REGARDING PROPERTY OWNERSHIP

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.

10.27 COMPREHENSIVE SURVEY OF BUSINESS OPERATING WITHOUT REGISTRATION

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.

10.28 STRICT PENAL ACTION AGAINST TAX DEFAULTERS

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.

10.29 BANKING TRANSACTIONS ABOVE 3 MILLION

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.

10.30 NO BUSINESS / TRADEMARK REGISTRATION WITHOUT REGISTRATION WITH FBR

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.

10.31 FOREIGN NATIONALS IN PAKISTAN

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 is 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.

10.32 ROYALTY PAYMENTS TO LOCAL RESIDENTS

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.

10.33 WITHHOLDING TAX ON LEASE RENTALS

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.

10.34 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.

10.35 POS INTEGRATION COMPULSORY FOR WHOLESALER, DEALERS, DISTRIBUTORS, AND RETAILERS

MEDIUM

Strategic Rationale

Pakistan has an estimated 3.5 million retail outlets, wholesalers, dealers, and distributors. Fewer than 200,000 are registered with any tax authority. The gap between actual sales and reported sales is estimated to be in the trillions of rupees annually.

Compulsory Point of Sale (POS) integration means that every sale above a certain threshold is recorded electronically, timestamped, linked to the seller's CNIC/NTN, and transmitted in real time (or near real time) to FBR's centralized system.

Technical Specifications for POS Systems

Requirement	Description
Real-time or near-real-time	Invoice data transmitted to FBR within 24 hours; large-volume taxpayers may be required to transmit within 1 hour
Tamper-proof	POS software must be approved by FBR; hardware security modules prevent invoice manipulation

Unique invoice numbering	Sequential, system-generated, cannot be skipped or duplicated
Mandatory fields	Seller CNIC/NTN, buyer CNIC (for B2B or above Rs. 100,000 B2C), date/time, line items, quantity, unit price, tax amount, total
Offline mode	In case of internet disruption, invoices stored locally and synced when connection restored; local storage tamper-evident
Integration with payment systems	Link to digital payment rails (Raast, credit/debit cards, QR codes) for automatic reconciliation

Incentives for Early POS Adoption

Incentive	Eligible Taxpayers
Reduced income tax rate (2 percentage points lower) for first 3 years	All retailers installing POS within Year 1
Fast-track VAT refunds (processed within 15 days)	POS-compliant retailers
Audit protection (no full-scope audit for 3 years)	Retailers with >95% invoice transmission rate
Input tax credit on POS hardware and software	All registered taxpayers
Public recognition (digital badge, government procurement preference)	Top 100 POS-compliant retailers per district

Penalties for Non-Compliance (After Grace Period)

Violation	Penalty
No POS installation after mandatory deadline	Daily fine of Rs. 5,000; business closure order after 90 days
Manipulation of POS (invoice skipping, deletion)	Minimum penalty of Rs. 500,000 or 200% of suppressed tax, whichever is higher; criminal prosecution for fraud
Failure to transmit invoices	Suspension of input tax credit for 6 months
Two or more violations	Name published on FBR website as non-compliant; banking transactions restricted

10.36 ADDRESSING IMPLEMENTATION CHALLENGES

Challenge 1: Cost of POS hardware for small retailers

Solution: FBR to empanel low-cost POS providers (mobile phone-based POS apps for

micro-retailers); government subsidy covering 50% of hardware cost for first 500,000 retailers; leasing options through partner banks.

Challenge 2: Internet connectivity in remote areas

Solution: Offline-first POS with sync-on-connectivity; SBP to prioritize branchless banking agents in unconnected areas; pilot with USSD-based POS (feature phone compatible).

Challenge 3: Resistance from wholesalers accustomed to cash-only trade

Solution: Phased mandate (wholesalers get 18 months); peer pressure through district chambers (chamber rankings include POS adoption rates); linking trade licenses to POS compliance after Year 2.

10.37 INTRODUCE SIMPLE TAX LAWS FOR SMALL AND MEDIUM INCOME TAXPAYERS

MEDIUM

The Problem of Complexity

Pakistan's Income Tax Ordinance 2001 has been amended over 50 times. The Sales Tax Act 1990 is similarly convoluted. A small trader or freelancer cannot reasonably be expected to navigate:

- Multiple return forms (income tax, sales tax, provincial sales tax/service tax)
- Dozens of schedules and annexures
- Complex depreciation, amortization, and inventory rules
- Withholding tax adjustments and final tax regimes

The result is either:

- Reliance on expensive tax consultants (cost prohibitive for small businesses)
- Non-compliance (simpler to stay undocumented)
- Errors that trigger penalties (further alienating taxpayers)

10.38 PROPOSED SIMPLIFIED REGIME FOR SMALL AND MEDIUM TAXPAYERS

Feature	Micro (Turnover < Rs. 10M)	Small (Rs. 10M–50M)	Medium (Rs. 50M–250M)
Return form	Single page (presumptive)	3 pages (simplified)	5 pages (standard)
Audit requirement	None	Random 1%	Risk-based
Record keeping	Basic cash book + sales summary	Cash book + purchase invoices + bank statements	Full books but simplified formats
Tax rate	0.25%–1% of turnover (presumptive)	10%–15% of adjusted profit	Standard corporate /individual rates

Withholding tax	Exempted (no deduction at source)	Reduced rates (50% of standard)	Standard rates but adjustable
Input tax credit (sales tax)	Not applicable	Full credit on documented purchases	

10.39 LESS DEPENDENCE ON WITHHOLDING AND ADVANCE TAXES

MEDIUM

Pakistan has one of the world's most extensive withholding tax regimes. Over 80% of income tax is collected at source through withholding agents (employers, banks, contractors, importers, etc.). While this improves collection, it has severe side effects:

- Cash flow burden on businesses (tax deducted before income is realized)
- Complexity (dozens of withholding sections with different rates and thresholds)
- False sense of compliance (withholding is treated as final tax, discouraging return filing)
- Inequity (salaried class bears disproportionate burden; business income escapes)

Proposed Reforms:

Reform Measure	Rationale	Timeline
Reduce number of withholding sections to 15 core sections	Simplify compliance for deductors	Year 1–2
Raise thresholds for withholding (e.g., cash withdrawal from Rs. 50,000 to Rs. 200,000)	Reduce burden on small transactions	Year 1
Convert withholding from final tax to adjustable advance tax for most sectors	Incentivize return filing to claim credit	Year 2–3
Phase out final tax regime (FTR) for all except genuinely micro-operators	Ensure all income is declared and aggregated	Year 3–5
Reduce advance tax installments from quarterly to semi-annual for small businesses	Improve cash flow	Year 1
Salaried individuals: Advance tax collected through employer but no separate advance installments	Maintain simplicity	Immediate

10.40 AIM TO REDUCE FACE-TO-FACE CONTACT BETWEEN TAXPAYERS AND TAX COLLECTORS, ESPECIALLY IN SALES TAX

MEDIUM

The Problem with Face-to-Face Contact

Pakistan's tax administration has historically been characterized by:

- Discretionary powers of tax officers (assessment, audit selection, penalty imposition)
- Rent-seeking opportunities (taxpayer pays bribe to reduce assessment or avoid audit)
- Harassment (officers demand "tea money" or "travel expenses" for routine processing)
- Inefficiency (physical file movement across desks takes weeks or months)

The COVID-19 pandemic demonstrated that much of this face-to-face contact is unnecessary. FBR's Iris portal allowed many transactions to move online, but the default culture remains manual.

Proposed Re-engineering by Function

Function	Current (Manual)	Proposed (Re-engineered)
Registration	Visit FBR office; submit physical forms; officer approval required	Online application; automatic approval within 24 hours for CNIC-verified applicants; physical visit only for biometric verification (once)
Refund processing	Physical verifications; multiple departments involvement; weeks or months	Online claim; AI verification against input tax records; automatic approval for low-risk (under Rs. 1 million); payment within 15 days
Audit selection	Officer discretion (often based on personal knowledge or bribe)	AI risk scoring; no human intervention in selection; officer only sees assigned cases after selection
Audit conduct	Physical visit to taxpayer premises; demands for documents	Desktop audit (e-records); physical visit only for high-risk cases and with prior judicial approval
Assessment order	Drafted by officer; signed by superior	Algorithmic draft based on data; officer reviews and confirms (reduced discretion)
Appeals	Physical file movement across desks	Digital case file; accessible to taxpayer and all appellate authorities
Grievance	Visit commissioner's office; written application	Online portal with tracking; service level guarantees (e.g., response within 7 days)

Specific Re-engineering for Sales Tax

Sales tax (VAT/GST) is particularly problematic because:

- It involves monthly returns (versus annual for income tax)
- Input-output adjustments require matching thousands of invoices
- Fraudulent input claims are common (fake invoices, missing traders)

Proposed Reforms for Sales Tax

Reform	Description
Mandatory e-invoicing	All B2B invoices above Rs. 100,000 must be transmitted to FBR in real time; buyer and seller both receive confirmation
Automated input-output matching	System matches buyer's input claims with seller's output declarations; mismatches flagged automatically
Pre-populated sales tax returns	70% of return fields auto-filled from e-invoice and import data; taxpayer only confirms or adds missing B2C sales
Risk-based verification	Low-risk taxpayers (e.g., POS-compliant retailers) receive automatic input credit without manual review
Reduced filing frequency	Small taxpayers (turnover < Rs. 50M) file quarterly instead of monthly
Single sales tax return	Harmonized federal and provincial sales tax return (one form, one filing, revenue split algorithmically)

10.41 UNIVERSAL ECONOMIC IDENTITY: THE CNIC-LED SINGLE PROFILE

Replace all fragmented tax identifiers (NTN, STRN) for individuals with the Computerized National Identity Card (CNIC) as the mandatory, universal economic identifier across all federal, provincial, and local transactions.

Establish a National Single Economic Profile Registry that aggregates, in real time, every economic activity linked to a CNIC through an Integrated Risk Management System (IRMS) using artificial intelligence and data analytics.

All material transactions must be automatically tagged to CNIC:

- Banking: All account activity, profit withholding, cash withdrawals above threshold.
- Assets: Property purchase/sale, vehicle registration, share/CDS accounts, mutual funds.
- Trade: Import/export declarations.
- Utilities: Commercial electricity, gas, broadband connections.
- Government payments: Withholding taxes (salary, dividend), professional fees, local government levies.
- Digital economy: Social media monetization, e-commerce platforms.

Within 3–5 years, the majority of individual taxpayers should receive a pre-filled annual return based on third-party data (banks, employers, property registrars). The taxpayer only confirms or corrects — not constructs from scratch.

International Precedent: India's ITR pre-filling (over 70 million auto-populated returns); Chile's SII model.

Legal and Privacy Framework Required

- Legal Mandate: Amend Income Tax Ordinance 2001 to designate CNIC as universal economic identifier.
- Data Sharing Law: Enact inter-agency framework with defined access controls, audit trails, judicial oversight.

Privacy Safeguards: Access limited to tax authorities; data not monetized; citizens can view their profile on request.

10.42 TRANSACTION TRACEABILITY: MANDATING THE DOCUMENTED ECONOMY

MEDIUM

A tax base cannot be broadened if most transactions remain invisible. This proposal establishes a clear, phased mandate: no material transaction without traceability.

Threshold-Based Digital Payment Mandate

Transaction Type	Threshold	Effective Date
B2B (manufacturers, importers, large distributors)	≥ Rs. 200,000	Year 1
B2C (retailers service providers)	≥ Rs. 100,000	Year 2
High-value assets (property, vehicles, commodities)	≥ Rs. 1 million	Immediate upon policy adoption

Consumer Incentive: VAT rebate on digital payments at point of sale (modelled on Uruguay's successful retail digitization program).

Phased Restriction of High-Denomination Currency (Rs. 5,000 Note)

Measure	Timeline
Restrict use in property, vehicle, B2B settlements	Immediate
Progressively reduce issuance volume	0–36 months
Full withdrawal (subject to digital infrastructure readiness)	After 36 months

Rationale

High-denomination notes are the primary instrument for undocumented wholesale trade, property deals, and informal lending. Restriction — not abrupt withdrawal — is the practical path.

10.43 SECTOR-SPECIFIC TAX GAP ANALYTICS: EVIDENCE-BASED POLICY

MEDIUM

Generic enforcement notices have failed. The future is sector-specific, data-driven tax gap analysis.
Annual Pakistan Tax Gap Report

Lead Institutions: FBR Policy Wing (primary), PBS (GDP/sector data), SBP (transaction flows), Pakistan Single Window (trade data).

Coverage (initial 10 sectors):

- Real estate
- Wholesale trade
- Retail trade
- Construction
- Transport & logistics
- Professional services (medical, legal, architecture)
- Agriculture processing
- Manufacturing (sub-sectors)
- Services (general)
- E-commerce/digital economy

Policy Mechanism

1. Quantify expected tax contribution per sector (benchmarked against GDP share).
2. Calculate actual collection.
3. Formally present gap to sector chambers.
4. Assign accountability for taxpayer base expansion (not revenue collection).
5. Launch evidence-based compliance drives

International Reference: UK HMRC's annual Tax Gap publication; South Africa SARS econometric sector models.

10.44 TRANSITION FROM PRESUMPTIVE TO DOCUMENTED COMPLIANCE

MEDIUM

Pakistan's Final Tax Regimes (FTR) and presumptive schemes, while administratively simple, have become structural traps that discourage full documentation.
Core Transition Principle

No reversion. Any taxpayer entering the documented regime cannot revert to presumptive. Each step is a permanent progression.
Transition Timeline

Period	Action
Year 1–2	Enhanced incentives for voluntary converters (lower effective rates, priority banking, procurement access)
Year 3–4	Tighten presumptive thresholds; reduce FTR coverage scope

Year 5	Presumptive regimes only for genuinely micro-scale operators (below defined turnover floor); all others fully documented with IFRS/IAS compliant financial statements (SMEs excepted)

Simplification for Micro and Small Businesses

Introduce a **single-page tax return** for micro and small businesses (modelled on India's ITR-4 Sugam and UK Self-Assessment Short Return). Complexity is a primary driver of non-compliance among small traders.

10.45 ESTABLISHMENT AND REVIVAL OF BTB ZONE TO TRACK AND INCREASE THE TAX NET

MEDIUM

Rationale and Strategic Importance

Pakistan's tax-to-GDP ratio has remained stubbornly below 10% for over a decade. The primary constraint is not the statutory tax rates but the structural inability to identify, register, and track economic participants. The **Broadening the Tax Base (BTB) Zone** is proposed as a dedicated, semi-autonomous unit within the Federal Board of Revenue (FBR) with a singular mandate: **expand the documented economy by bringing invisible transactors into the tax net**.

Unlike traditional revenue collection units that are evaluated on how much money they extract from existing taxpayers, the BTB Zone will be evaluated on:

- Net increase in active filers (by district and sector)
- Reduction in sector-specific tax gaps
- Number of previously unregistered entities brought into formal compliance
- Increase in documented transactions as a percentage of estimated economic activity

10.46 ACTIVELY USE CNIC-LINKED DATABASE (NADRA) TO BRIDGE INFORMATION GAPS THE CORE INSIGHT

MEDIUM

Pakistan possesses one of the world's most sophisticated national identity systems through NADRA, with over 120 million CNICs issued. However, this asset remains largely disconnected from tax administration. The proposal is to legally mandate that every material economic transaction be tagged to the CNIC of the beneficial owner or authorized representative.

Practical Mechanisms for Bridging Information Gaps

Information Gap	Current Problem	CNIC-Linked Solution

High spender, low filer	Individual lives in expensive house, drives luxury car, children in elite schools — but files nil return	AI compares property value, vehicle engine capacity, utility consumption, school fee patterns against declared income
Benami (proxy) holdings	Property or business registered in name of low-income employee or domestic worker	Transaction trail (bank, utility, insurance) reveals true beneficial owner through lifestyle patterns
Undisclosed business income	Professional (doctor, lawyer, architect) receives fees in cash, deposits small amounts	AI flags mismatch between professional qualification, client volume estimates (from chamber data), and bank deposits
Suppressed sales (retail)	Retailer shows minimal sales on tax return but has high electricity bill (AC, lighting, freezers)	Utility consumption normalized against declared turnover — outlier detection triggers notice or POS mandate

Integration with Banking Records

Current State: Banks report withholding tax on profit and cash withdrawals above Rs. 50,000. However, FBR does not receive full account statements or transaction-level data for non-withholding purposes.

Proposed Enhancement: All banks will provide, on a monthly basis, a digital extract of all transactions (credits and debits) for every account linked to a CNIC, above a threshold of Rs. 10,000 per transaction. This data will be ingested into the AI engine to:

- Identify business income deposited into personal accounts
- Detect circular transactions designed to inflate turnover artificially
- Match interest/profit income reported by banks with taxpayer declarations

Integration with Property Registration

Current State: Property registrations are handled by provincial authorities (Board of Revenue in each province). Valuation is often based on outdated FBR circle rates that are 30–70% below market value. Many transactions are registered at undervalued rates to minimize taxes.

Proposed Enhancement:

- Mandatory CNIC of buyer, seller, and both witnesses for every property transaction
- Real-time data feed from provincial e-stamp paper systems and sub-registrar offices to FBR

- Market value determination through AI models that use:

- Recent registered transactions in the same locality
- Online real estate platform listings (Zameen.com, Graana.com)
- Satellite imagery of property size and improvements
  - Any transaction registered at less than 85% of AI-determined market value triggers automatic notice

10.47 INSTITUTIONALIZING DISTRICT CHAMBERS AS TAX INTERMEDIARIES

The FBR cannot alone reach every trader. District Chambers of Commerce must be transformed from reactive pressure groups into structured compliance partners.
Institutional Design

Component	Description
Tax Facilitation Desk	Co-staffed by FBR and provincial revenue authorities (PRA/SRB/BRA/KPRA/ICT) at each District Chamber
Data Sharing (Anonymized)	Chambers receive sector-disaggregated tax data for their district, enabling peer accountability
Co-signed Targets	Chambers co-sign district-level compliance improvement targets (registered taxpayers, documented transactions)
Digital Dashboard	Real-time, visible to both FBR and Chamber, tracking progress

Accountability Mechanism

Chambers are evaluated annually on:
- Net increase in registered taxpayers (by district)
- Increase in documented transaction volumes
- Audit outcomes

Formal national ranking and public disclosure. Defunct, politically captured trade bodies should be de-recognized.

International Reference: Turkey's TOBB protocol with Revenue Administration; Rwanda's District Revenue Committees (contributed to tax-to-GDP rise from 12% to >16%).

10.48 PERFORMANCE METRICS: REFRAMING FBR'S SCORECARD

MEDIUM

Current FBR performance targets are denominated entirely in **revenue collection** — a single metric that drives perverse incentives (harassing compliant taxpayers is easier than expanding the base).

Proposed Balanced Scorecard for FBR

Metric	Type
Net increase in active return filers (individual, AOP, corporate) by district	Primary
Reduction in tax gap per sector (as published in Annual Tax Gap Report)	Primary
Increase in documented transactions as % of total economic activity	Primary
New taxpayer registrations by district (benchmarked against economic activity)	Secondary
Revenue collection (retained but de-emphasized)	Secondary

10.49 CONCLUSION

From Infrastructure to Implementation Pakistan already possesses approximately 80% of the required institutional building blocks:

- NADRA – Universal identity and biometric infrastructure.
- SBP – Raast instant payment system (P2P, P2M).
- Pakistan Single Window – Trade data integration.
- FBR – Existing withholding data streams (salary, bank profit, imports, cash withdrawals).
- SECP – Beneficial ownership registry linked to CNIC.

The missing elements are not technological — they are policy integration, legal mandate, and sustained political will to sequence and see through a multi-year transition.

This framework is designed to be:

- **Mutually reinforcing** – CNIC enables traceability; traceability enables gap analytics; analytics enables evidence-based enforcement; enforcement plus incentives expands the base.
- **Equitable** – The salaried class receives visible relief; the informal sector receives a pathway, not a penalty.

- **Irreversible** – The no-reversion principle ensures that each compliance step is permanent.

The objective is not a higher tax rate on those already paying. The objective is a fair and proportionate contribution from all who participate in Pakistan's economy.

Economic Advisory and Fiscal Law Committee

Mr. Zeeshan Ijaz, FCA-Chairman – Economic Advisory & Fiscal Law Committee

Special Acknowledgments:

Task Forces of the Committee

Taskforce	Convener	Co- Convener
Direct Taxation	Mr. Khalid Mahmood, FCA	Mr. Faisal Iqbal Khawaja, FCA
Indirect Taxes	Mr. Asif Siddiq, FCA	Mr. Hasnain Adam Ali, FCA
Provincial Taxes	Mr. Atiq Ur Rehman, ACA	Mr. Aqal Sardar, ACA
Harmonization of Taxes	Mr. Habib Fakhruddin, FCA	Mr. Mohammed Muzammil, ACA
Broadening of Tax Base	Mr. Rizwan Bashir, FCA	Mr. Mohsin Nasrullah, FCA

Members for Structuring Task Forces

Sub - Committee Responsible for Structuring Task Forces
Mr. Aamir Younas, FCA
Mr. Muhammad Furqan Atique, ACA
Mr. Sheikh Moeen Ahmed, ACA
Mr. Ahmed Jabbar, FCA
Mr. Atiq Ur Rehman, ACA
Mr. Taiyab Shahid, FCA
Mr. Dawood Ahmed, FCA

Other Members on the Committee

Ms. Syeda Arj Naz, ACA

Mr. Abbas Hasan Naqvi, FCA

Mr. Adeel Kaiser, FCA

Syed Ahmad Husain Naqvi, ACA

Mr. Ahmad Suleman, ACA

Mr. Ahmed Arslan, ACA

Mr. Amir Waheed Ahmed, FCA

Ms. Ammara Shamim, ACA

Mr. Aneel Peter, FCA

Mr. Mohammad Moin Khan FCA

Mr. Aqeel Alam, FCA

Mr. Asad Feroze, FCA

Mr. Asif Haroon, FCA

Mr. Asjad Wasi, ACA

Mr. Dawood Khan, FCA

Mr. Faisal Ali Butt, FCA

Mr. Deepak Kumar, ACA

Mr. Ghulam Abbas, FCA

Hafiza Hira Rauf, ACA

Hafiz Khalil Ahmad Hashmi, FCA

Mr. Hamid Raza, FCA

Mr. Inam-Ullah, FCA

Mr. Jackson Wilson, FCA

Mr. Jehan Zeb Khan, ACA

Mr. Kamran Iqbal Butt, FCA

Ms. Khushboo Mushtaq, ACA

Mr. Majid Ali, ACA

Syed Kumail Mohammad, ACA

Mr. Laeeq Ahmed Rana, FCA

Ms. Habiba Fatima, ACA

Mr. Majid Mahmood, FCA

Mr. Mansoor Ahmad Siddiqui, FCA

Mr. Mohammed Ahmed Bharamchari, FCA

Mr. Mohammed Asif Mehdi Rizvi, FCA

Ms. Ramia Kiran, ACA

Mr. Muhammad Ali, ACA

Mr. Mubashir Hussain, ACA

Mr. Muhammad Adil Jillani, FCA

Mr. Muhammad Awais, FCA

Syed Muhammad Fahad Sajid, ACA

Mr. Muhammad Saad, ACA

Mr. Muhammad Mubashar Bashir, FCA

Mr. Muhammad Raza Toor, FCA

Mr. Mustafa Kamal, FCA

Mr. Muhammad Safder, FCA

Mr. Muhammad Taiyab, FCA

Mr. Najeeb Taher Moochhala, FCA

Mr. Nabeel Shaikh, FCA

Mr. Nafeh Akbar, FCA

Mr. Raheel Rehman, FCA

Mr. Nosherwan Ali Abbas Khawaja, FCA

Mr. Owais Ahmed, FCA

Ms. Rizwana, ACA

Mr. Rashid Ibrahim, FCA

Mr. Saad Uz Zaman, FCA

Mr. Sajid Hussain, FCA

Mr. Saad Manzoor Bhatti, ACA

Mr. Saqib Rafique, FCA

Mr. Shamail Shahid, FCA

Mr. Sajjad Iftikhar, FCA

Mr. Tahir Sharif, FCA

Dr. Vaqar Ahmed

Mr. Sohail Ahmed Nisar, FCA

Mr. Zeshan Chishti, ACA

Mr. Zohaib Salim, ACA

Mr. Mansoor Zaigham, FCA

Mr. Haider Ali Patel, FCA