

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ



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by**

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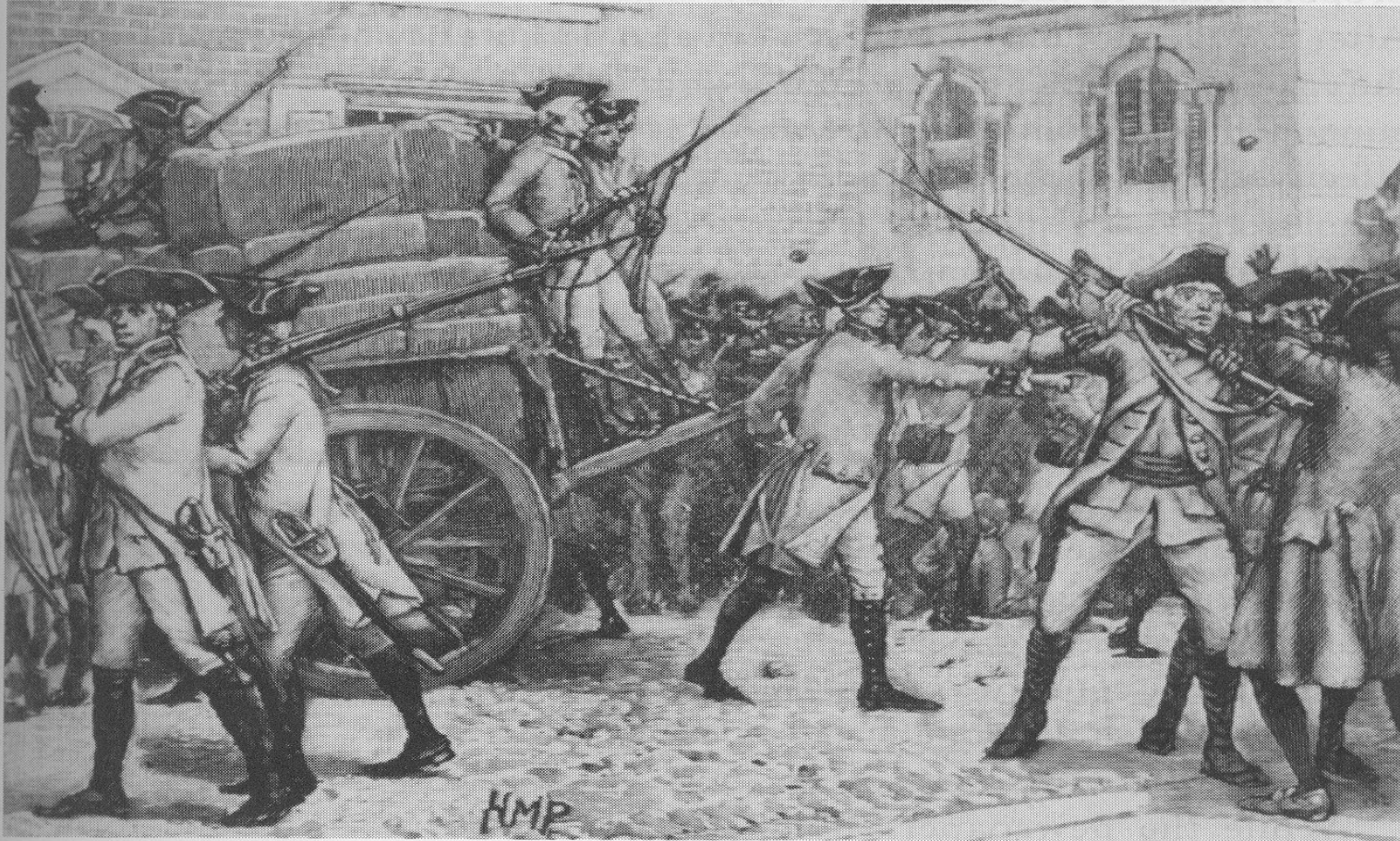
**TO REMOVE CONTRADICTION IN LAW**

**WIRTE-OFF OF IRRECOVERABLE (Non-Performing) LOANS**

Adam Smith, in the eighteenth century, in his classic *The Wealth of Nations* pointed out that, four main objectives should be borne in mind by the State in levying taxes. Firstly, the taxes must be equitable and fair as between the different classes of society. Secondly, the convenience of the taxpayer. Thirdly, economy. The Government must economize and levy only the minimum tax, which is necessary for the national good. Fourthly, certainty and clarity. The laws imposing taxes must be so precisely and clearly worded as to make the taxpayer understand what is the burden he is called upon to bear.

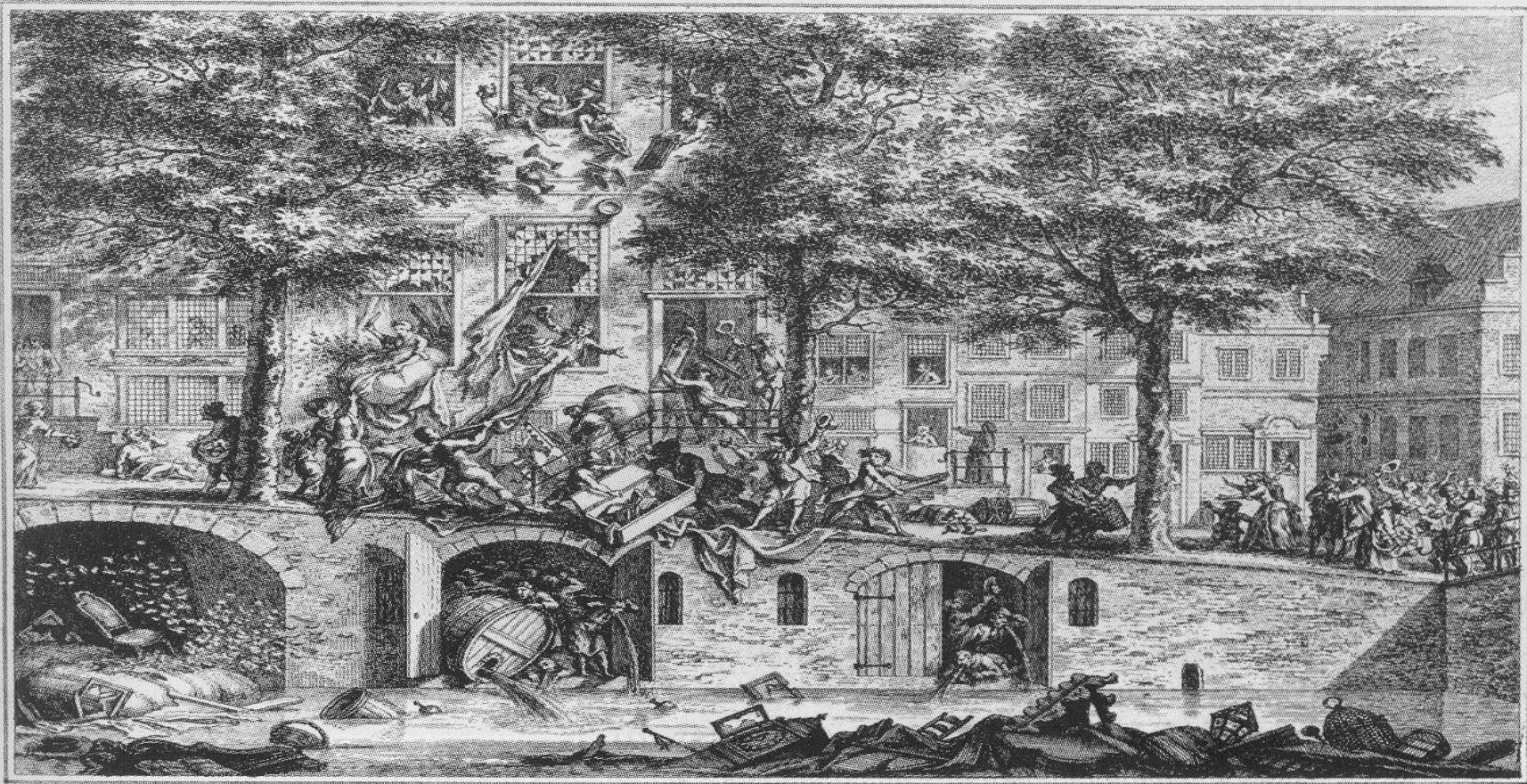
Social justice is beyond doubt the most important goal of taxation, particularly under developed countries. The main problem facing the under developed countries is to reconcile the objective of social justice with the need of providing the fiscal stimulus to promote economic goals.

## Stamp Duty



*British soldiers forcefully clearing the way for a transport of packages of stamps in New York in 1765.*

## *Farming out Taxes*



HET PLUNDEREN VAN HET HUIS VAN A. M. VAN ARSSEN,  
op de Cingel bij de Huiszittensteeg te Amsterdam, op Dingsdag den 25<sup>en</sup> Junij A<sup>o</sup> 1748.

*The years 1747 and 1748 saw revolts against the tax farmers in the Republic of the United Netherlands. The result was the abolition of the practice of farming out taxes. The cartoon shows an angry crowd pillaging the house of an Amsterdam mayor who was being held responsible.*

## *Distributing the Tax Burden*



*During the Ancien Régime in France, the taille, which was primarily a real estate tax, was an annual direct tax on capital. The first class (the clergy) and the second class (the nobility) were exempt from this tax because of an argument dating back to the Middle Ages. The reasoning was that the religious served their country with their prayers and charitable works and the knights defended their country with their blood. However, this had been an outdated representation of reality for centuries. The cartoon illustrates the opinion of the third class (farmers and citizens).*

# INVESTMENT AND SAVINGS

**Tax credit for enlistment of companies in stock exchange**

**Section 65C (1)**

The Finance Bill seeks to amend sub-section (1) in order to enhance tax credit for a company which opts for enlistment in any registered stock exchange as an incentive for enlistment, from 5% to 15% of the tax payable for the tax year, in which the said company is enlisted.

## **Tax Credit for 100% equity investment**

## **Section 65D**

**The Finance Bill seeks to insert new section 65D to provide tax credit of 100% of the tax liability to a company, which establishes a manufacturing industrial undertaking in Pakistan or invest in the purchase and installation of Plant and machinery for the purpose of balancing, modernization and replacement (BMR) of plant and machinery already installed therein .**

**The tax credit shall be allowed for a period of 5 years from the date of commencement of commercial production or 1st July 2011, which ever comes later. However, the tax credit shall be available only to those industrial undertakings which are funded by 100% own equity.**

# PROVISIONAL ASSESSMENTS

Through the Finance Act 2010, a concept of provisional assessment under section 122C was introduced, whereby, if a person does not file his tax return, the Officer Inland Revenue shall provisionally assess the taxable income of any person on the basis of available information or material and to the best of his judgment.

Such provisional assessment is treated as final assessment, if the taxpayer fails to submit his tax return, wealth statement, wealth reconciliation and source of acquisition of assets to the Officer Inland Revenue within the period of 60 days.

## PROVISIONAL ASSESSMENTS

However, the corresponding modification was not made in the definition of assessment at that time. Now the Finance Bill seeks to insert appropriate wording in the definition of “Assessment” provided in section 2(5) of the Ordinance.

Similarly, under Section 137(2) which relates to “Due date for payment of tax”; the Finance Bill also proposes that the tax liability u/s 122C shall be immediately payable after the lapse of 60 days of service of order u/s 122C and notice thereof.

Now it has also been expressly proposed in Section 127(1); that the Provisional Order u/s 122C would not appealable u/s 127(1) of the Ordinance.

# **BROADENING OF TAX BASE**

**Presently the Federal Board of Revenue is making efforts to broaden the tax base of the country to avoid suffering of existing taxpayers due to high rates of taxation, improper documentation of economy and to bring equity in the taxation laws for every citizen. In this regard following steps have been proposed by the Finance Bill to initiate the process of broadening :-**

## **Filing of return by electricity connection holders**

**Section 114(1)(b)(viii)**

The Finance Bill proposes that the connection holders of commercial and industrial electric connections will now require to file return of income, if their annual electricity bill exceeds rupees one million.

## **Filing of statements**

**Section 165**

Statements of withholding of tax at source has once again been made mandatory on monthly basis i.e. by the 15th of every month for taxes withheld in the preceding month.

In order to generate information for the data warehouse, it is also proposed to mention the CNICs and NTN of individual payee along with his name and addresses.

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Presently as per serial No.1 column 3 of this section penalty can be levied for default committed by the taxpayers in furnishing of Return of Income under section 114, Statement in lieu of Return of Income under section 115, Wealth Statement within due date equal to 0.1% of the tax payable for each day of default, which should not be less than rupees five thousand, but maximum penalty shall not exceed 25% of the tax payable. As we all know that we have always calculated such penalty on the basis of admitted tax liability as per Return of income or statements u/s 115 or 165 of the Ordinance.

**The Finance Bill now proposes to insert explanation in sub-section (1) in column 3, whereby penalty can be worked out on the basis of tax payable on assessment order passed under section 121, 122 or 122C or assessment treated to have been made under section 120 of the Ordinance, and/or Wealth Reconciliation under section 116 and Withholding Statement under section 165.**

# WITHHOLDING OF TAXES

**Payments for goods and services**

**Section 153**

**Section 153 deals with deduction and collection of tax at source on sale of goods, rendering of services, execution of contracts and payments made by Exporter or Export House against stitching, dying, printing, embroidery, washing, sizing and weaving (specified services).**

Section 153 has undergone a lot of changes and amendments since the promulgation of Income Tax Ordinance, 2001. In view of the above, the Bill seeks to replace existing Section 153 with the newly drafted Section 153. The significant changes are highlighted below:-

- (i) Tax deduction on services rendered by private limited companies has been clearly stated as minimum tax.
- (ii) Definition of Turnover has now been provided for the purposes of AOPs & Individual as withholding agent

The tax deducted under this section on the income of a resident person or permanent establishment of a non-resident person, shall be:-

- (a) a final tax on payments received on account of supply of goods, except on,
  - (i) payments received on account of supply of goods in respect of a company being a manufacturer of such goods; or
  - (ii) payments received on account of sale of goods by a public company listed on a registered stock exchange in Pakistan;

- (b) a minimum tax on payments received on account of for the rendering of or providing of services ;
- (c) a final tax on the payments received on account of the execution of a contract, other than a contract for the sale of goods or the rendering of or providing of services, except on payments received by a public company listed on a registered stock exchange in Pakistan on account of execution of contracts; and
- (d) a final tax on payments made by Exporter or Export House against stitching, dying, printing, embroidery, washing, sizing and weaving (specified services).

## **Advance tax at the time of sale by auction**

## **Section 236A**

Section 236A provides that advance income tax at the time of sale by public auction of any property or goods including property or goods confiscated is collected at the rate of 5% of the gross sale. The Finance Bill now proposes to also include those transactions for sale of goods made through “auction by a tender” as well.

## **Cash withdrawal from a Bank**

## **Section 231A, Division VI of Part IV**

The Finance Bill seeks to reduce the rate of adjustable withholding tax on cash withdrawal from Bank from the existing 0.3% to 0.2%. This step has been taken to reduce the cash money in circulation and to encourage individuals to conduct transaction through bank. However, we feel this half hearted effort would not bring any significant results.

## **TAXATION OF BANKING COMPANIES**

### **Rule 1(c), Rule 6 of Seventh Schedule**

Presently Rule 1(c) of Seventh Schedule provides that the Income, profits and gains of a banking company shall be taken to be the balance of the income, from all sources before tax, disclosed in the annual accounts required to be furnished to the State Bank of Pakistan subject to the provisions for advances and off balance sheet items shall be allowed up to a maximum of 1% of total advances; and provisions for advances and off-balance sheet items shall be allowed at 5% of total advances for consumers and small and medium enterprises (SMEs) (as defined under the State Bank Prudential Regulations) provided a certificate from the external auditor is furnished by the banking company to the effect that such provisions are based upon and are in line with the Prudential Regulations.

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## **Rule 1(c), Rule 6 of Seventh Schedule**

**Provisioning in excess of 1% would be allowed to be carried over to succeeding years, provided that if provisioning is less than 1% of the advances, then actual provisioning for the year shall be allowed.**

**The above rule was substituted by the Finance Act, 2009 and further insertion was made by the Finance Act, 2010; whereby a bank can carry over the provision in excess of 1% of total advances; however there was an anomaly in respect of carry over of provisions of 5% of total advances for consumers and Small and Medium Enterprises (SMEs). The Finance Bill now seeks to amend the proviso according to changes made in sub-rule (c) to clarify the position and remove anomaly.**

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## **Rule 1(c), Rule 6 of Seventh Schedule**

**Rule (6) of the Seventh Schedule provides that the income under the head Dividend shall be taxed at the rate of ten per cent.**

**The Finance Bill seeks to enhance the rate of tax on a banking company on Dividend received from its asset management company and such dividend shall be taxed at the rate of 20%.**

# UNIFORMITY OF LAW

## Profit on debt

**Section 151(3), Clause (5A) of Part II of IInd Schedule**

Presently profits on debt, except the profit earned on securities of Federal Government, Provincial Government and Local Government; arising to a taxpayer other than a company are final tax on such profits.

However, the profits earned on securities issued by the Federal Government, a Provincial Government or a Local Government is taxable at the normal rate.

## **Profit on debt**

## **Section 151(3), Clause (5A) of Part II of IInd Schedule**

Therefore, in order to encourage investment in Government Securities (Treasury Bills and Pakistan Investment Bonds) and to provide equal treatment, the Finance Bill proposes to treat tax deduced under Section 151(3) at the rate of 10% of the yield or profit also on such securities as final tax on such yield or profits.

Similar amendment has also been proposed in Clause (5A) of Part II of the Second Schedule to the Ordinance for the Non-Resident person.

# **SCOPE OF UNEXPLAINED INCOME ENLARGED**

## **Unexplained income or assets**

## **Section 111**

**At present the Commissioner shall invoke section 111 on the amount credited in the book of accounts, any investment or valuable article owned by the taxpayer or taxpayer has incurred any expenditure, but fails to explain the same or his explanation is not satisfactory in the opinion of Commissioner. Now the Finance Bill 2011 proposes to enlarge the scope of this section to include the amount of suppressed production or sales and item of receipts liable to tax in whole or in part.**

# **REMOVE CONTRADICTION IN LAW**

## **Disposal of appeals by the Appellate Tribunal      Section 132**

**Section 132 provides that the Appellate Tribunal shall afford an opportunity of being heard to the parties to the appeal and in case of default by any of the party on the date of hearing, the Tribunal may if deem fit, dismiss the appeal in default or may proceed ex-part to decide the appeal on the basis of available record.**

**The Finance Bill now proposes to done away with the powers of ATIR to dismiss the appeal in case of default by any of the party to the appeal. The ATIR now in the case of default by any of the party may proceed to decide the appeal on merit on the basis of the available record.**

## **Advance tax paid by the taxpayer**

## **Section 147**

**Capital gain tax was levied vide Finance Act, 2010, wherein quarterly advance tax payment is required to be made within 7 days of the end of each quarter, which later found to be inadequate, especially in the cases of non-resident investors. In order to remove this hardship and to bring it at par with other provisions of payment of advance tax, it has been proposed to extend the 7 days period to 21 days.**

## **WRITE-OFF OF IRRECOVERABLE (Non-Performing) LOANS**

### **Section 18(1)(d)**

Section 18(1)(d) of the Ordinance provides that the fair market value of any benefit or perquisite, whether convertible into money or not, derived by a person in the course of, or by virtue of, a past, present, or prospective business relationship shall be chargeable to tax under the head Income from Business.

The Finance Bill now seeks to insert explanation in the above clause to expand the scope of word “Benefit” to the income or profit derived by way of waiver of profit on debt or the debt itself under the State Bank of Pakistan, Banking Policy Department, Circular No.29 of 2002 or in any other scheme issued by the State Bank of Pakistan.

## **Section 18(1)(d)**

**In this regard it is pertinent to point out that the State Bank of Pakistan issued guidelines on write-off of irrecoverable (Non-Performing) loans and advances including interest/mark-up and other perforce charges charged to the borrower's account or markup receivable (hereinafter referred as "loans"), vide Circular No.29 OF 2002 dated 15-10-2002.**

**The tax department assumed jurisdiction in various cases under sub-sections (5) and (5A) of Section 34 (unpaid amount of expenditure already charged or unpaid trading liability) and Section 70 (Recouped Expenditure) of the Ordinance and taxed the benefit of write-off of such loans. However, on the request of FPCCI and affected parties the Government inserted following Clause (3A) to Part IV of the Second Schedule to the Ordinance, which was withdrawn by the Finance Act, 2008:-**

*“(3A) The provisions of sub-sections (5) and (5A) of Section 34 and Section 70 shall not apply to any benefit derived by way of waiver of profit on debt or the debt itself under the State Bank of Pakistan, Banking Policy Department’s Circular NO.29 of 2002, dated the 15th October, 2002, to the extent not set-off against the losses under Part VIII OF Chapter III”*

**Thank you  
&  
God bless you all.**