TOLA ASSOCIATES

TAX & CORPORATE ADVISORS

APRIL 2019

TAX PAK

NEWSLETTER BY TOLA ASSOCIATES

https://goo.gl/LFiWyx

https://goo.gl/QDM4ZM

ADDRESS

408, 4th Floor, Continental Trade Centre,
Clifton Block-8, Karachi

Email: connect@tolaassociates.com

Ph# 35303294-6

Website: www.tolaassociates.com

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CONTRIBUTORS

Mr. Ashfaq Tola - FCA
Editor in Chief

Mr. Muhammad Furqan - ACA - Managing Editor

Mr. Talha Shahid - Editor

Mr. Sameer Ahmed
Designer

EDITORIAL NOTE

Another monthly issue of Tax Pak, for the month of April 2019 is in your hands due to blessings of Almighty Allah, support and appreciation of readers, and commitment and dedication of Tola Associates' team. This is the eighteenth continuous issue. We have covered the important topic of International taxation "Permanent Establishment" in section of topic of the month.

Recently, the ICAP Fiscal Law Committee had a meeting with FBR officials in which proposal for upcoming budget has been discussed and agreed by FBR officials. The recent reshuffle in top tier of FBR and SBP is likely to bring improvement in these institutions and facilitate IMF Pakistan staff level agreement which likely to be reached shortly.

Readers are requested to visit our website www.tolaassociates.com or download our mobile apps from below links to access previous issues and other publications and to stay updated of future notifications.

1. https://goo.gl/QDM4ZM (iOS)
2. https://goo.gl/LFiWyx (Android)

Readers are also requested to circulate this e-copy within their circle, as our primary aim is to benefit the masses. Feedback is always welcomed.

Ashfaq Tola - FCA
Editor in Chief

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Mr. Ashfaq Tola, President Tola Associates attending meeting. Following is a pictorial glimpse of these events.

Chairman Fiscal Law Committee ICAP presenting ICAP Budget Proposal for they year 2019-20 to Dr. Abdul Hafeez Shaikh, Advisor to Prime Minister on Finance, Revenue, and Economic Affairs

President ICAP Mr. Jafar Husain presenting ICAP Budget Proposals to Chairman FBR Dr. Jahanzeb Khan. Also present Mr. Ashfaq Tola Chairman Fiscal Law Committee ICAP and Dr. Hamid Sarwar Ateeq Member IR Policy FBR

With Sheikh Rasheed, Pir Naqeeb ur Rehman, And Sahibzada Hassan Habib ur Rehman

Team ICAP with Chairman FBR and President ICAP after protracted discussions on Budget Proposals

Almighty has added yet another feather in my cap by conferring Honorary Life Membership of Karachi Press Club. Receiving certificate from Raja Kamran and Rizwan Bhatti being son of a former journalist from DAWN, Mr. Yousuf Abdul Karim, I feel honoured and I wish my next generations shall follow our footprints.. Aameen

1. NOTIFICATIONS/ CIRCULARS

1. SRO 438(1)/2019 dated 9 April 2019

The ministry had imposed the conditions by amending Import Policy Order 2016 through SRO 237 (I)/ 2019 issued on February 19, 2019, under which it was made mandatory that the ingredients and details of the products (e.g. nutritional facts, usage instructions etc.) of the food products shall be printed in Urdu and English languages on the consumer packaging, the logo of Halal certification body shall be printed on the consumer packaging, the shipment must be accompanied by a Halal certificate issued by a Halal Certification body, which should be a member of International Halal Accreditation Forum (IHAF) or Standards Metrology Institute for Islamic Countries (SMIIC).

Now by virtue of SRO 438(1)/2019, dated 9 April 2019 the Ministry of Commerce has deferred the implementation of above till 30 June 2019.

2. Amendment in ADRC Rules in Sales Tax Rules vide SRO 488 (I)/2019 dated 25th April 2019 and in FED Rules vide SRO 489(I)/2019 dated 25th April 2019

Before FA 2018, the procedure of settlement of dispute through Alternative Dispute Resolution mechanism was essentially recommendatory in nature. The FBR was not mandatorily required to accept the recommendation of the ADRC.

Consequently, the appellant was not necessarily required to withdraw the appeal filed before an appellate forum for seeking remedy under the ADRC. Through FA 2018, the whole scheme was revamped whereby the whole structure been changed. Firstly, the option of seeking remedy in ADRC shall only be available if the applicant waives his right of appeal in the appellate authorities. Secondly, the recommendations of ADRC will now consequently be binding on both the parties.

The FBR has now issued SRO 488 (I)/2019 dated 25th April 2019 whereby it made amendments in Chapter X of Sales Tax Rule 2006 in Rule 63 to 69 and in FED Rules vide SRO 489(I)/2019 dated 25th April 2019 to make Rules in line with changes brought about by FA 2018.

3. Maintenance in Petroleum Rates from 1st May to 4th May 2019 vide SRO 499(I)/2019 dated 30 April 2019 and Increase in prices vide SRO 507(I)/2019 dated 4th May 2019

The Federal Government [FG] has now partially increased prices on recommendations by OGRA and after decision by ECC of Cabinet w.e.f. 5th May 2019 by increasing Sales Tax rates on petroleum products vide SRO 507(I)/2019 dated 4th May 2019. OGRA had earlier recommended in its summary to Ministry of Finance, a hike of Rs4.89 per litre in diesel prices, Rs7.46 in kerosene oil, Rs14.37 in petrol and Rs6.40 in light diesel price which was managed earlier by government by decreasing the rates of sales tax from 1st May 2019 to 4th May 2019 vide SRO 499(I)/2019 dated 30th April 2019.

As per latest SRO, the sales tax on petrol now stands at 12%, HSD at 17%, LDO at 17% and Kerosene 17%. We understand that the new rate of sales tax on motor spirit is lower than the standard sales tax rates under FBR, SRB & PRA, hence the issue of inadmissibility of input tax by respective authorities may arise.

A comparison of Sales Tax rates of petroleum products from August 2017 to April 2019 can be found below:

Date	SRO	Effective from	Products ST rate %				
			MS	HSD	LDO	HOBC	Kerosene
31/7/17	713	Aug 01 17	23.5	40	0	17	0
5/8/2017	757	Aug 06, 17	20.5	35.5	0	17	0
31/8/17	867	Aug 31, 17	17	30	0	17	0
30/9/17	984	Oct 01, 17	17	31	0	17	0
31/12/17	1331	Jan 01, 18	17	25.5	6	17	6
31/1/18	98	Feb 01, 18	17	25.5	7.5	17	7
28/2/18	265	Mar 01, 18	17	25.5	17	17	17
31/3/18	414	Apr 01, 18	21.5	27.5	16.5	17	17
30/4/18	560	May 01, 18	15	27.5	11.5	17	12
31/5/18	663	Jun 01, 18	7	17	1	17	7
11/6/18	729	Jun 12, 18	12	24	9	17	12
30/6/18	830	Jun 30, 18	17	31	17	17	17
1/8/18	993	Aug 01, 18	9.5	22	1	17	6
30/9/18	1167	Sep 30, 18	4.5	17.5	0	17	1.5
31/10/18	1308	Nov 01, 18	4.5	12	0	17	1.5
30/11/18	1461	Nov 30, 18	8	13	0.5	17	2
31/12/18	1574	Dec 31, 18	17	17	17	17	17
30/04/19	499	May 01, 19	2	13	9	17	8
04/05/19	507	May 05, 19	12	17	17	17	17

MS	=	Motor Spirit (Petrol)
HSD	=	High Speed Diesel
LDO	=	Light Diesel Oil
HOBC	=	High Octane Blending Component

2. LAHORE HIGH COURT [LHC] - NO SALES TAX RECOVERY WITHOUT REGISTRATION

In case of M/s S.K. Steel Casting Gujranwala [STR No. 54 of 2016] the taxpayer was reportedly liable to be registered under sales tax, 1990[STA] for Tax Years 2010, 2011 and 2012 as electricity bills were above minimum threshold of Rs 700,000 but did not get registration. A Show Cause Notice [SCN] was issued, which followed Order-in-Original [OIO] requiring to pay sales tax relating to period prior to registration along with default surcharge [DS]. The taxpayer preferred an appeal to Commissioner Inland Revenue [CIRA] who upheld the officer's order. The taxpayer preferred second appeal to Appellate Tribunal [ATIR] which set aside orders passed by below forums on ratio that OIO was finalized without registration or compulsory registration. The Department preferred a Reference in LHC on grounds that 1) person liable to be registered is also included in the definition of the registered person under section 2(25) of STA, hence it is deemed registered person and liable as registered person prior to registration 2) The ATIR did not consider all relevant provisions of STA and rules viz. combined reading of overall scheme of STA was ignored, while deciding the case.

The LHC observed that before declaring a person liable to be registered, the well-established principle of natural justice i.e. audi alteram partem (no one should be condemned unheard), is to be observed before issuing SCN. Further, definition clauses in statute are of declaratory nature; and while the definitions are to be read to interpret various provisions of Act, they cannot override a main provision of statute if contents of provision of Act indicates otherwise. It is well settled principle that tax cannot be charged and levied unless it falls squarely within the purview of charging provisions. The LHC upheld ATIR order that no SCN could be issued before registration or compulsory registration; and modified ATIR order u/s 47(5) of STA by holding that legislature intends combined reading in applying the provisions of STA and this means that where a person is liable to be registered, the department is required to a) first register that person b) then charge sales tax from it and c) may proceed against person regarding prior to registration contravention of provisions of STA.

3. ECONOMIC INDICATORS

- The 3-month, 6-month and 1-year KIBOR rate for the month of March 2019 to 10.84%, 10.89% and

11.48%, respectively, which hiked in April 2019 to 11.12%, 11.25% and 11.66%, respectively.

- The 3-month T-Bills rate for the month March of 2019 was 10.65% which hiked to 11.05% in April 2019; The 6-month T-Bills rate for the month of March 2019 was 10.50% rises to 10.92% in April. The rate for 1 year remained unchanged at 6.97% since October 2018.

- The PSX 100 index at the end of March 2019 was 38,649 points and at the end of April 2019 was 36,784 points while the average index for the month of March 2019 was 38,687 points and for the month of April 2019 was 37,159 points possessing a decrease of 4.39%.

- The rate for Crude Oil in the OPEC basket at the end of March 2019 was $ 65.28, whereas, at the end of April 2019 was $ 70.57. The increase in price was 8.11%

- The rate of Gold per troy ounce in the month of March 2019 was $1301.80 whereas in the month of March 2019 it decreased to $1,288.60 per troy ounce by 1.01%.

- The rate of Sugar at end of March 2019 was 0.3431 US$/KG which slightly decreased to 0.3330 US$/KG in the month of April 2019.

- The rate of Palm Oil in the month of March 2019 was 492.72 US$/MT which rises in the month of April 2019 to 509.9 US$/MT by 3.486%.

- The US$ parity to Chinese Yuan at the end of March 2019 was 6.71 whereas in the month of April 2019 it was 6.7338 showing a slight change of 0.35%.

- The US$ parity to Indian rupee at the end of March 2019 was 69.5509 whereas in the month of April 2019 it was 69.556.

- The US$ parity to Bangladesh Takka at the end of March 2019 was 84.2455 whereas at the end of April 2019 it was 82.84 showing a change of -1.66%.

- The US$ parity to Pakistan Rupee at the end of March 2019 was 140.1869 which change to 141.59 at end of April 2019 by 1.00%.

- The stock of currency in circulation was Rs. 4,388 billion as on June 30th, 2018 which increased by Rs. 427 billion up to May 3rd, 2019 to Rs. 4,816 billion.

- The Net Government Sector borrowings at end of June 30th, 2018 were Rs. 10,199 billion which increased by Rs. 950 billion up to May 3rd, 2019 to Rs. 11,150 billion. The net government sector borrowings were used for the purpose of budgetary support (Rs. 10,508 billion) and commodity operations (Rs. 653 billion); and supported by others (Rs. -11 billion).

- The credit to private sector at end of June 30th, 2018 was Rs. 5,973 billion which rose by Rs. 587 billion up to May 3rd, 2019 to Rs. 6,560 billion.

- Foreign exchange balance at end of May 3rd 2019 (Provisional) and March 29th, 2019 (Provisional) were $ 15,972.6 million (SBP: $8,984.1 million, Commercial Banks: $6,988.5 million) and $ 17,397.6 million (SBP: $10,492.0 million, Commercial Banks: $6,905.6 million) respectively showing a decrease of 8.92%.

- Workers' remittances for the month of March and April 2019 were $ 1,746 million and $ 1,779 respectively, an increase of only 1.9%.

- The volume of imports in April 2019 was approx. 670,895 Million rupees (4,753 million $) while the exports were approx. 295,541 Million rupees (2,094 million $). Exports in July 2018 to April 2019 decrease by 0.12% to $ 19,169 million over the same period last year, while Imports in July 2018 to April 2019 decrease by 7.88% to $45,471 million over same period last year.

4. NATIONAL ACCOUNTS COMMITTEE - PROVISIONAL PERFORMANCE

The Gross Domestic Product (GDP) according to the Official Provisional results provided for a growth, was almost half of the annual target of 6.2 %, due to a negligible growth in agriculture and industrial sectors as well as the devaluation of rupees in terms of Us Dollars.

The economy slipped from USD 313 billion to USD 280 billion, reflected by the fact that the production cost of all goods and services produced in a year grew at a rate of 3.29 %, during fiscal year 2018-19 ending on 30 June 2019, according to the National Accounts Committee (NAC).

The growth was mainly derived from a less job intensive sector namely service sector, which contributed as much as 87 % to the total national output for the outgoing fiscal year.

The NAC revised economic growth upward for the last year's PMLN government from 5.2 % to 5.53 %, which was revised by the current PTI government to 5.2 % for the fiscal year 2018-19 claiming that the PLMN government manipulated the growth rate, which claim is proven wrong.

The Government's indecisiveness and inconsistent economic policies served the lowest GPD of 3.29 % in none years, which further lead to the unceremonious removal of former finance minister Asad Umar.

Looking at the conditions and the upcoming economic challenges, Pakistan is set to enter an International Monetary fund (IMF) program.

The prospects for higher economic growth in the next two years are also very low although a 3.3 % growth rate is largely in line with the projections of international financial institutions that had predicted a 2.9 % to 3.9 % growth rate, with IMF projecting a lowest rate of 2.9 %.

The service sector witnessed 87 % growth, with electricity generation and gas distribution sector outperforming their growth by 40.5 % against their set target of 10% for the outgoing fiscal year, whereas the agricultural and industrial sector contributed only 5% and 9 % respectively while having weightage of about 19.27 % and 20.8 % on the economy.

Advisor to the Prime Minister on Finance Dr Abdul Hafeez Sheikh will formally announce a provisional growth rate of 3.3 % on 10 June with the release of the Economic survey of Pakistan 2018-19.

Due to the missed targets and improper policies by the present government the Agriculture sector witnessed a growth of only 0.85 % this fiscal year. The production of major crops declined by 4.4 % while other crops declined by 6.6 %. In particular cotton production declined by 17.5 %, rice production by 3.3 %, sugarcane by 19.4 %, maize by 7 % and wheat by 0.5 %.

In addition, Cotton grew by 2 %, Livestock by 4 % and fishing by 0.8 % while none achieved their targeted growth.

The targets were severely missed by the government in terms of industry sector as against a target of 7.6 % the output in the industrial sector stood at 1.4 % only. The output of large scale contracted to 0.3 % while on the small-scale manufacturing featured growth by 8.2 %.

In addition, the slaughtering sub sector grew by 3.5 %, electricity generation and distribution by 40.5 % and mining by negative 2 % against the targets of 10 % and 3.6 % respectively. The constructive sector also witnessed negative growth of 7.5 %.

The service sector which accounted for growth by 4.7 % also missed its target as its targeted growth was around 6.5 %. The financial services sector witnessed a decent growth on behalf of heavy government borrowing as well as an increase in money supply.

In addition, the wholesale and retail trade grew by 3.1

% against target of 7.8 % while finance and insurance sector grew by 5.1 % against the target of 7.5 %.

5. TOPIC OF THE MONTH

- PERMANENT ESTABLISHMENT

Permanent Establishment (**PE**) is a term used for a place of business in another country by companies which tend to operate in those countries in addition to its resident country and tend to avoid double taxation on its profits. Companies which operate PE are relieved from taxation on its profits on its residence country but are rather taxed in the country in which it has PE. PE in definition means a **fixed** place of business through which a business activity of an enterprise is **wholly or partly** carried on.

The Place of business in a PE shall be fixed viz it must be established at a distinct place with a certain degree of permanence. It also includes any premises, facilities or installations used for carrying on the business of the enterprise. The place of business may be situated in the business facilities of another enterprise for e.g. A Inc. a foreign company is in the practice of using the ware-house facilities in Pakistan of B Ltd, a Pakistani company, for the purpose of distribution of goods all over Pakistan. In this case A Inc. will be considered to have a place of business in Pakistan.

A certain amount of space withheld by a business for a business activity is sufficient to constitute a place of business, with no litigation required to occupy a place and thus illegal occupation could also constitute PE. For e.g. Mr. A has a warehouse which is kept under lock for a number of years. Mr. A was out of Pakistan for 5 years. During this period, B Inc. a foreign company is in the practice of using such warehouse illegally for the purpose of storing the goods and distributing the same all over Pakistan. Although they are not the legal owners of the place, they are considered to have a place of business in Pakistan.

As a matter of understanding, presence of an enterprise at a particular location merely does not necessarily mean that that location is at disposal of that enterprise e.g. Mr. B is a salesman of A Inc. a foreign company. He is in the practice of regularly visiting C Ltd, its customer in Pakistan for the purpose of securing order on behalf of A Inc. Mr. B doesn't operate from any enterprise in Pakistan. In this case, although the salesman is regularly visiting C. Ltd, its premises are not at the disposal of the enterprise for which the salesman is working and therefore do not constitute a place of business through which the business of that enterprise is carried on. However, Mr. B may constitute an agent PE for A. Inc in Pakistan.

The main purpose to form a PE is to avoid double taxation on its profit by the country in which it has acquired PE and are also required to abide by the taxation rules and regulations of that country.

If the non-resident enterprise does not have a Permanent Establishment, then its profits can be taxed only in the country of residence. However, where the enterprise operates through a PE in the country of source, the profits attributable to the operations carried on by the PE may be taxed by the country where the PE is located. It is also noteworthy to mention that PE is one of the largest contributors to global international tax litigation and continues to be a grey area.

1. PERMANENT ESTABLISHMENT UNDER INCOME TAX ORDINANCE, 2001

a. Definition

The term Permanent Establishment has an exhaustive meaning under Section 41 of the Income Tax Ordi-nance, 2001 as a fixed place of business through which the business activity of the person is wholly or partly carried on. As defined above a PE includes; a place of management, a mine, oil or gas well, an agricultural property or a building site, assembly or installation project. Any installed equipment, asset or property placed on a geographical site and is capable to generate income shall be a part of permanent establishment.

Under the ordinance, a person acting on behalf of a foreign company in Pakistan can be referred to as an agent of the PE. Furthermore, the characteristic of the place of business defined in the Ordinance is classified as fixed and is to be maintained by the non-resident person operating in Pakistan through such PE.

b. Taxability

The taxability of a Permanent Establishment is defined under Section 105 of the Income Tax Ordinance, 2001. Under this Ordinance, a permanent establishment income is chargeable to tax under the head "Income from Business". As tax chargeability is performed under the Ordinance, provisions from the Ordinance will be applied in the taxability of income for the respective permanent establishment. All the deductions subject to this Ordinance will apply on the respective permanent establishment other than its expenses towards its head office or any other related permanent establishment.

2. PERMANENT ESTABLISHMENT / DOUBLE TAXATION TREATIES (ARTICLE 5)

a. Model Definition

Permanent Establishment as defined under the treaties is in coherence with the Income Tax Ordinance, 2001.

The definition in the treaties additionally includes a management of a business to be treated as a permanent establishment as well.

Further it provides that if a resident company of a contracting state has a subsidiary or permanent establishment in other contracting states, the parent or resident company of the contracting state cannot be titled as a permanent establishment itself.

To elaborate the above, if a resident company of USA has a subsidiary or permanent establishment in Pakistan, the parent or resident company of USA cannot be titled as a permanent establishment for the purpose of Pakistan's taxation.

b. Taxability Model

The taxability under the treaty is in accordance with the definition of taxability provided under the Income Tax Ordinance, 2001 and that profit/income of the permanent establishment are to be taxed according to the Ordinance as well as all the provisions, rules and regulations are to be applied.

TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

OFFICES IN PAKISTAN

Karachi Address:
Office no. 408, 4th Floor, CTC Building, Clifton Block-8, Karachi
Tel #: +92 21-3530 3294-6

Islamabad Address:
144, 1st Floor, Street No.82
Sector E-11 / 2 FECHS
Islamabad 44000,
Tel #: +92 51-835 1551

Lahore Address:
202-E, 2nd Floor, Sadiq Plaza
69-The Mall Road, Lahore
Tel #: +92 42-3628 0403

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