TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

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TAX PAK

NEWSLETTER BY TOLA ASSOCIATES

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EDITORIAL NOTE

Another monthly issue of Tax Pak, for the month of March 2019 has been issued due to blessings of Almighty Allah, support and appreciation of readers, and commitment and dedication of Tola Associates' team. This is the seventeenth continuous issue. We have covered the Audit Policy 2018 issued by FBR on 4th April 2019, along with connected issues in section of topic of the month.

Another amnesty is also the buzz word these days and is expected to be announced on April 15th, 2019. We will issue a comprehensive commentary on the same like previous year. A snapshot comparison between the scheme of last year and expected scheme of current year has also been prepared by us which may be found through link https://bit.ly/2Vz5lzP

Recently, we have also published a compendious study on statutory stipulations titled" Doing Business in Pakistan" which gives overview of fiscal and other laws guiding investment in Pakistan which may be found through the link https://bit.ly/2UtoR4s

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

Mr. Ashfaq Tola, President Tola Associates attending SAFA meeting of PAIB Committee and Fiscal Laws Committee in Kathmandu, Nepal. Following is a pictorial glimpse of these events.

Attending SAFA meeting of PAIB Committee at Radisson Hotel Kathmandu Nepal

Attending SAFA meeting on Fiscal Laws Committee at Radisson Hotel Kathmandu Nepal

Having dinner with Mr. In-kee-jo President IFAC, Mr. Jafar Hussain President ICAP, and Mr. Abdullah Yusuf

1. NOTIFICATIONS/ CIRCULARS

1. SRO 328(1)/2019 dated 11 March 2019

By virtue of SRO 328(I)/2019, dated 11 March 2019, the Federal Government has amended the Sales Tax Special Procedure (Withholding) Rules, 2007. The Federal Government has inserted a provision that the registered persons purchasing cane molasses from unregistered person shall withhold sales tax at the applicable rate on supplies of molasses from the payment due. The amount of sales tax shall be worked out on basis of gross value of taxable supply. The said withholding tax on molasses will not be claimable as input tax by the withholding agent as input tax.

2. SRO 37(1)/2019 dated 15 March 2019

By virtue of SRO 37(I)/2019, dated 15 March 2019 , the Federal Government has amended the Rule 33(2)(c) of the Federal Excise Act, 2005, that Board may waive the condition of printing code on the packs of cigarettes exported out of Pakistan in case where the importing country has different rules for printing. In addition to that the pack should state that these are not meant for sale in Pakistan.

3. Exemption of sales tax on services to FATA/ PATA from Khyber Pakhtunkhwa Sales Tax on Services Act.

The KPK Government has amended the section 28 of the Khyber Pakhtunkhwa Finance Act,2013 and has granted exemption from the levy of sales tax on services provided or rendered in FATA/PATA provided that the service provider are residents of FATA/PATA, and their business are located in FATA/PATA.

The notification will take effect from the day the Twenty Fifth amendment in the Constitution of Pakistan received assent from the President of Pakistan and will remain in force till June 30, 2023.

4. Further Extension in Filling of Income Tax Returns & Statements up to 30th April 2019

FBR vide Circular No. 3 dated 31st March 2019, has further extended the date of filing of Income Tax Returns under section 114 and statements under section 115 to 30th April 2018 for the following:

- Companies with Special Tax Year & Normal Tax Years
- Salaried persons
- Other Individuals
- Association of persons

2. SRO 584(I)/2017 STRUCK DOWN BY LAHORE HIGH COURT

Through the writ petition **W.P 131563 of 2018** dated 19.03.2019, the petitioners challenged the issuance of SRO 584(I)/2017 dated 01.07.2017 issued by the Board with the approval of Federal Minister-in-charge. The notification amended the SRO 1125(I) 2011 dated 31.12.2011 which, inter alia, imposed further tax on supplies to unregistered persons of items covered under SRO 1125.

Earlier, in light of the decision of M/s Mustafa Impex, Karachi and others vs the Government of Pakistan through Secretary Finance and Others reported **PLD 2016 Supreme Court 808**, the petitioners challenged the amendment made vide Finance Act 2017 whereby powers to levy further tax were devolved to FBR with the approval of federal minister in charge. Powered to levy further tax was previously conferred to the Federal Government, the powers to levy further tax were again conferred to Federal Government vide Finance act, 2018 to give effect decision of Apex Court in **PLD 2016 Supreme Court 808**.

The Constitutionality of the amendment has also been highlighted as a result of Sindh High Court's judgment

CP D-7159 of 2017 whereby it struck down an unconstitutional section 18(3) of the Customs Act,1969. The grounds raised in W.P 131563 of 2018 are similar to that of 18(3) of the Custom Act,1969 whereby Board with the approval of Federal Minister-in-charge was given power to impose regulatory duty on wide range of imports.

Section 4 (c) of the Sales Tax Act,1990 also contemplates the delegation of legislative power of taxation which is vested in the hands of Federal Government to tax goods at the rate of zero percent. The impugned notification 584(I)/2017 imposed further tax on goods supplied to a person who has not obtained registration. While taking into account the various aspects of controversy at hand and the constitutional structure given by the Supreme Court of Pakistan in the case of Ms. Mustafa Impex, whereby it was held that the mandate to levy tax was given to the Federal Government which could not be delegated to any other institution. Hence, the Sindh High Court struck down section 18(3) of the Custom Act,1969.

The same reasoning as discussed above applies to the amendment made in Section 4 (c) of the Sales Tax Act,1990 having been enacted in contravention of the rule given by the Supreme Court of Pakistan in the case of M/s Mustafa Impex. As the crux of the issue at hand is that if the constitution mandates that the certain act has to performed in a certain manner and the interpretation of the same has been provided by Supreme Court, then nothing short of Constitutional amendment will undo the effect of a judgement of Supreme Court. Hence the amendment in Section 4 (c) of the Sales Tax Act,1990 and issuance of SRO 584(I)/2017 was declared as ultra vires having no legal effect.

Even after this decision by the Lahore High Court, the industry practice is that further tax is still being charged on supplies of items falling under SRO 1125(I)/2011 to unregistered persons out of fear of any adverse potential proceedings by tax authorities.

3. ECONOMIC INDICATORS

- The 3-month, 6-month and 1-year KIBOR rate for the month of February 2019 to 10.71%, 10.85% and 11.42%, respectively, which hiked in March 2019 to 10.84%, 10.89% and 11.48%, respectively.

- The 3-month T-Bills rate for the month February of 2019 was 10.41% which hiked to 10.65% in March 2019; The 6-month T-Bills rate for the month of March 2019 was remain unchanged at 10.50%. The rate for 1 year remained unchanged at 6.97% since October 2018.

- The PSX 100 index at the end of February 2019 was 39,054 points and at the end of March 2019 was 38,649 points while the average index for the month of February 2019 was 40,362.32 points and for the month of March 2019 was 38,687 points possessing a decrease of 3.70%.

- The rate for Crude Oil in the OPEC basket at the end of February 2019 was $ 64.86, whereas, at the end of March 2019 was $ 65.28. The increase in price was 0.65%.

- The rate of Gold per troy ounce in the month of February 2019 was $1322.70 whereas in the month of March 2019 it decreased to $1301.80 per troy ounce by 1.58%.

- The rate of Sugar at end of February 2019 was 0.3431 US$/KG which remain unchanged in the month of March 2019.

- The rate of Palm Oil in the month of February 2019 was 522 US$/MT which fell in the month of March 2019 to 492.72 US$/MT by 5.61%.

- The US$ parity to Chinese Yuan at the end of February 2019 was 6.694 whereas in the month of March 2019 it was 6.71 showing a appreciation of 0.39%.

- The US$ parity to Indian rupee at the end of February 2019 was 71.2085 whereas in the month of March 2019 it was 69.17 showing a depreciation of 2.86%.

- The US$ parity to Bangladesh Takka at the end of February 2019 was 83.5379 whereas at the end of March 2019 it was 84.2455 showing an appreciation of 0.85%.

- The US$ parity to Pakistan Rupee at the end of February 2019 was 139.6655 which increased to 140.1869 at end of March 2019 by 0.45%.

- The volume of imports in March 2019 was aprox 562,291 Million rupees (4,030 million $) while the exports were aprox 293,005 Million rupees (2,100 million $). Exports in July 2018 to March 2019 rose by 1.1% to $ 17,210 million while Imports in July 2018 to March 2019 decrease by 8.3% to $40,660 million.

- The stock of currency in circulation was Rs. 4,388 billion as on June 30th, 2018 which increased by Rs. 334 billion up to March 29th, 2019 to Rs. 4,722 billion.

- The Net Government Sector borrowings at end of June 30th, 2018 were Rs. 10,200 billion which increased by Rs. 743 billion up to March 29th, 2019 to Rs. 10,942 billion. The net government sector borrowings were used for the purpose of budgetary support (Rs. 10,301 billion) and commodity operations (Rs. 654 billion); and supported by others (Rs. -12 billion).

- The credit to private sector at end of June 30th 2018 was Rs. 5,973 billion which rose by Rs. 608 billion up to March 29th, 2019 to Rs. 6,581 billion.

- Workers' remittances for the month of February 2019 and March 2019 were $ 1,576.52 million and $ 1,745.80 million respectively, increase by 10.74%.

- Foreign exchange balance at end of March 29th, 2019 (Provisional) and March 1st, 2019 (Provisional) were $ 17,397.6 million (SBP: $10,492.0 million, Commercial Banks: $6,905.6 million) and $ 14,956 million (SBP: $8,116.5 million, Commercial Banks: $6,839.7 million) respectively showing a increase of 16.33%.

4. TOPIC OF THE MONTH

- AUDIT POLICY 2018

1. FOREWARD:

FBR has released Audit Policy 2018 on 4th April 2019 for selection of Audit cases under Income Tax, Sales Tax [ST] and Federal Excise Duty [FED] for Tax Year 2017. According to the policy, FBR would do parametric selection by running Data analytics on available population based upon identified risk parameters. This strategy ensures that only non-compliant taxpayers are selected for audit and minimizes the chance of selection of tax compliant taxpayers. As per policy, FBR would conduct computer ballot on parametric basis for selection of 2.3% of cases for audit out of total filers after exclusions in Income tax for tax year 2017. For Sales Tax and FED, FBR is to select 2.5% and 7.7% cases for audit, respectively, out of total filers after exclusions for tax periods July 2016 to June 2017.

Accordingly, FBR has selected 10,982 cases out of 477,374 income tax cases (2.3-%) as against 9.5 % in last year. In sales tax FBR has selected 3,126 cases out of total 124,004 sales tax cases (2.5%) as against 7.5% in last year, and in FED, 56 cases are selected out of total 725 cases (8.3%) as against 8.6% in last year.

The taxpayers who have been audited in Income Tax in any of the preceding three (Tax Years i.e. 2016, 2015, and/ or 2014); all cases where entire income is covered under Final Tax regime, and salaried individuals are excluded from this year's ballot. Similarly, taxpayers who have been selected for audit under Audit Policy

2017 for sales tax and FED have been excluded from this year's ballot.

2. SELF ASSESSMENT SCHEME U/S 120 OF ITO [SCHEME]

The universal acceptance of returns scheme is provided u/s 120 of the Income Tax Ordinance, 2001 [ITO], whereby all the returns filed on the due date are considered as assessment orders of the taxpayers issued by the Commissioner relieving them from the hassle of obtaining assessment orders from the department.

Hence the law requires intelligence-based tax information system that alone can help attain better voluntary compliance. Tax evaders and avoiders should be tackled by gathering information. The return filers should not be compelled to provide evidence against themselves.

However, Finance Act, 2005 creates some departure from scheme by inserting sub-section (1A) authorizing the Commissioner to even select a completed assessment for audit u/s 177. Later Finance Act, 2010 went a step further by providing that, "he may conduct audit of tax affairs of a person". This is against the established principle that an order which has attained finality cannot be disturbed or unsettled by fishing inquiry through audit. Earlier, once assessment u/s 120(a) was treated to have been made only section 122 could be invoked to amend the assessment, if so, allowed by law.

3. SECTION 214C - AUDIT SELECTION

Under Scheme, to ensure compliance of tax laws, promote tax culture and discourage the practice of giving false declaration with impunity, selecting tax payers for audit becomes essential practice. A certain percentage of returns filed is selected for tax audit on the basis of risk assessment to verify the accuracy and correctness of income tax return. Through section 214C, which was inserted in 2010, FBR has been empowered to select persons or classes of persons for audit through random or parametric computer ballot. Audit in such cases shall be conducted in accordance with the provisions of section177 of ITO.

3.1 The Power of Commissioner to Select for Audit is Independent of FBR's power

The divergent views emerged on selection of cases u/s 177 by FBR and Commissioner- Lahore High Court and Peshawar High Court held that in the presence of section 214C, the Commissioner cannot select a case u/s 177. The Islamabad High Court held that powers u/s 177 and 214C are Independent. Through Finance Act 2013, amendments were made in law to nullify the judgment of Lahore and Peshawar High Courts.

3.2 Lahore High Court observations on Audit Policy 2015

The Lahore High Court (LHC) in W.P No. 32597 of 2015, observed as follows:

- FBR should improve its taxpayers' auditing procedure to get them rid of random selections.
- A taxpayer selected and audited for the preceding tax year should not be selected and audited without giving reasons for such selection.
- If audit is not completed within the given timeframe, the selection shall be deemed to have been dropped.
- Persons selected for audit should be made part of FBR Act, 2007 under which any person aggrieved by any action done or taken for the enforcement of fiscal laws or due to any act of maladministration, corruption and mis-behavior by any officer of the board might prefer representation to the FBR chairman for grievance.

These directions/observations had far reaching effect on Audit Policies announced afterwards as well as current audit policy of 2018.

For instance, in current Audit policy the basis for selection is parametric although Section 214C has provided power to FBR to select cases both on random or parametric basis. ***The current drop in percentage of audit cases selected also might be due to above guidelines by FBR.***

3.3 Random vs Parametric Selection of Audit

In the past for the purpose of audit, selection of cases was mostly made through random ballot which entails the chance of selecting already compliant taxpayers thus overburdening them with audit procedures and department's exploitations. This leads to litigations in Superior Courts, and as discussed in previous sections the Superior Courts had issued guidelines in this regard. This had enforced FBR to issue 'Audit Policy 2016' for Tax Year 2015 and onwards to focus on parametric and risk-based selection as against random or general selection. This approach minimizes the chances of selection of already tax compliant tax payers resulting in saving scarce resources and building confidence of the taxpayers in the Audit System.

3.4 The Audit Parameters in selection

The Audit policy 2018 is prepared on same lines as previous policies with respect to parametric selection. The parameters for Income Tax cases selection has been kept confidential in view of subsection (1A) of Section 214C in previous as well as current policy. However, the parameters for ST and FED cases have been disclosed in previous as well as current Audit policy. There are some changes made in parameters for ST & FED in current policy presented below:

- Previously the threshold for decline of supplies was at 10% over last year for selection of audit. Now, no percentage as benchmark is mentioned in audit policy.

- Previously the threshold for decline in ratio of taxable supplies to total supplies was set at 10% over last year for selection of audit. Now, no percentange as benchmark is mentioned in audit policy.

- Previously the limit for reduction in sales at 10% to avoid selection of audit. Now, no percentage as benchmark is mentioned in audit policy.

- Previously the limit for manufacturers for value addition was set at 10% to avoid selection of audit. Now, no percentage as benchmark is mentioned in audit policy.

- The parameters omitted are follows:
  - (i) non-filers, nil filer or null-filers for more than 6 months in the year in case the Registered Person is showing any turnover in income tax return of the corresponding period,
  - (ii) where more than 30% purchases were from unregistered persons,
  - (iii) Where more than 30% sales were to un-registered persons,
  - (iv) Increase in carry forward of input tax by margin of 10%.

- New Parameters inserted are as follows:
  - (i) Difference in declared value of sales as compared to declared turnover in Income Tax Return.
  - (ii) Declared sales are less than imports.
  - (iii) Decrease in payment of tax as compared to corresponding months of previous year.
  - (iv) Increase in refund claimed as compared to corresponding months of previous year.
  - (v) Unclaimed purchase to declared purchased ratio is high.
  - (vi) Utilities to sales ratio is high.
  - (vii) Discrepancy identified by CREST.

3.5 Audit Selection only once in 3 Years

Through FA 2018, clause 105 in Part IV of Second Schedule was added in ITO whereby the selection of audit under section 214C has been restricted once in three years, however, the Commissioner have the powers to select the case for audit under section 177 for any tax year for preceeding six years but after seeking approval of the Board.

In Sales Tax the authorized officer of Inland Revenue could conduct audit of the records of the registered person once in a year. Through FA 2018, a new proviso was inserted u/s 25(2) whereby it was clarified that routine audit of sales tax records shall be conducted only once in in every three years. Yet this immunity from audit may not apply for investigative audit initiated under the provisions of Section 38 of Act. Similar, amendment was also made in section 46 of Federal Excise Act, 2005.

4. DIFFERENCE BETWEEN AUDIT 177 AND 214C

The scope of section 214C is clearly different from section 177. Under Section 214C the FBR has the power of selection by taking a holistic view whereas under section 177(1) the Commissioner is empowered to call for the record either after selection of persons for audit by the FBR or at his own notion by examining each case and recording reasons thereof for the purpose of audit. Commissioners also have the mandate to select taxpayers for audit of their Income Tax affairs under section 177 of the Income Tax Ordinance, 2001 after recording reasons in writing for the same and these reasons have to be communicated to the taxpayer. Whereas in case of selection of a case by the Board under Section 214C, the Commissioner is not required to record and communicate the reasons for calling of record for the purpose of audit.

5. PROBLEMS IN AUDIT ADMINISTRATION

FBR has been facing difficulties in carrying out audit due to shortage of staff in the machinery. This means that the revenue collection mechanism of the government is not only slow but also results in a number of cases of audit piling up with no timeline of when the cases will be resolved. One of the basic reasons why employees are not able to deliver what the job requires is due to lack of skills. This means that the hiring process must be more vigilant in order to ensure that deserving people get the jobs and there is a smooth running of the revenue collection process. These issues have also been highlighted in various proposals for restructuring of FBR and need urgent decisions from present government.

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