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# TAX PAK

NEWSLETTER BY  
TOLA ASSOCIATES


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## EDITORIAL NOTE

Fifth edition of Tax Pak is in your hands. This month of March is special for us as it marks the first anniversary of Tola Associates. Also, the final version of our mobile application, on both android and IOS platforms, is available and fully operational (previously running as trial version). The application will keep the users updated on latest developments in tax and corporate legislation. The apps may be downloaded through below links:



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

A report has also been prepared on Offshore and Onshore parallel economy and proposed amnesty scheme. The report may be perused via the link <https://goo.gl/D1Wtxi>

I am again grateful to my colleagues in ICAP Council, Teaching Fraternity and Students for their support and commitment. We specially request students to contact us in case of any query whether theoretical or practical. We will do our best to resolve the same at earliest.

Lastly, readers are requested to spread the newsletter to their circles for the benefit of all.

**Ashfaq Tola - FCA**  
Editor in Chief

## 1. PROCEDURE OF APPEALS COMMISSIONER (APPEALS) REVISED UNDER THE INCOME TAX ORDINANCE, 2001, THE SALES TAX ACT, 1990 AND THE FEDERAL EXCISE ACT, 2005

Federal Board of Revenue vide SRO's 277(1)/2018, 278(1)/2018 and 279(1)/2018 dated 05 March 2018 revised the forms of appeals required to be filed before of Commissioner Appeals FBR.

Moreover, it has also been directed that hearing for the stay applications filed before 1pm shall be fixed for next day, while for stay applications filed after 1pm, hearings will be fixed for day following next day, through a proper notice.

## 2. SINDH SALES TAX ON RENTING OF IMMOVEABLE PROPERTY SERVICES

### 1. Introduction

The Sindh Sales Tax on Services (Amendment) Bill, 2018 has been recently passed by Provincial assembly of Sindh whereby the taxability of renting of immovable property services (which was previously declared as illegal by the Hon'ble Sindh High Court vide order dated August 18, 2017) has been attempted to be restored back with effect from July 01, 2015. The said order of SHC has been challenged by SRB authorities before the Hon'ble Supreme Court of Pakistan (SCP).

### 2. Background

The renting of immovable property service was originally brought within the scope of taxable services under the Sindh Sales Tax on Services Act, 2011 (SSTSA) through Sindh Finance Act, 2015 by way of insertion of entry no. 9806.3000 'Renting of Immovable Property Services' in the First and Second Schedules to the SSTSA. The corresponding definitions were inserted by adding sub sections (72B) 'Renting of Immovable Property' and (72C) 'Renting of Immovable Property Services' to the Section 2 of the SSTSA.

The initial applicable rate was the reduced rate of 6% with no input tax admissibility which was later increased to 8% in 2016 and then reduced to 3% in 2017. The recipient of services were held responsible to withhold and deposit the 100% sales tax involved on such services.

The aforesaid insertion was then challenged before the Sindh High Court (SHC) on the following premises:

- The definition of renting of Immovable property Services as defined under 2 (72C) though covered within its scope of services in relation to renting of immovable property. However, the renting of immovable property itself is not covered.
- The renting being provision of right to use an immovable property merely, is not a service.

- The renting of immovable property is not covered within the scope of economic activity as defined under Section 4 of the SSTSA which is the main ingredient as per Section 3 for a service to be taxable under the SSTSA.

The aforesaid deficiency in the definition provided under Section 2(72C) was later removed vide Sindh Sales Tax on Service (Amendment) Ordinance, 2015 as regularized through Sindh Sales Tax on Service (Amendment) Act, 2016. This amendment Act also validated the applicability of the provisions of renting of immovable property through insertion of non-obstante Section 84 to the SSTSA giving overriding effect to such amendment and to the proceedings by officers of SRB for levy, collection, recovery of tax on renting of immovable property, over any judgments of the court and any other law for the time being in force.

In our view, the Amendment Act 2018 may also be challenged before SHC and the litigation may continue till the dispute is finally addressed by SCP.

### **3. AUDIT POLICY 2016 CANNOT BE PUT INTO EFFECT - LHC**

The Honorable Lahore high court has passed a judgement against Audit policy 2016 which was filed by the Treet Corporation Limited (the manufacturers of razors, blades and holders of high stakes in pharmaceuticals) against

Federation of Pakistan and others. The judgement was passed on March 06, 2018 in W.P No.11253 of 2017.

In this judgement, the judge who passed this judgment has once again highlighted the administrative challenges that have rendered the Audit policy 2016 ineffective.

Further, the judge while passing the order has given remarks that the selection of taxpayer under Audit policy 2016 must have parameters based on which the selection of audit is to be made. Furthermore, it was also stated that FBR should follow a certain mechanism for the selection of audit to broaden the tax base and increase confidence of the taxpayer.

Therefore, selection of audit as per Audit policy 2016 cannot be put into effect until the FBR frames risk parameters on the basis of which the selection of audit is to be made and should be set aside unless there is proper mechanism for the selection.

### **4. SHOW CAUSE NOTICE OF WITHHOLDING TAX CANNOT BE ISSUED UNDER SECTION 11(2) OF THE SALES TAX ACT, 1990**

The Appellate Tribunal Inland Revenue(ATIR) Lahore bench, provided a clear interpretation of the Section 11(2) and 11(4A) of the Sales Tax Act,1990 (STA). In the aforesaid order, the officer Inland Revenue issued show cause notice under

Section 11(2) of the STA whereby demand of Rs. 3,887,989/- was adjudged against the taxpayer for short withholding of sales tax for the tax periods of July 2013 to June 2015.

The learned bench of the ATIR contended that the insertion of Section 11(4A) through Finance Act 2016 clearly shows that liability to withhold sales tax was of the withholding agent. Therefore, it was imperative for the Officer Inland Revenue to first assess and determine the amount of default on part of the withholding agent and only after establishing that the withholding agent never deducted withholding tax can proceed in the matter.

Therefore, a show cause notice cannot be issued under Section 11(2) of the STA without first determining the amount in default on part of the withholding agent and proceeding under Section 11(4A) of the STA.

## 5. TOPIC OF THE MONTH

### NATIONAL FINANCE COMMISSION AWARD (NFC AWARD)

#### What is NFC Award ?

The NFC award is the distribution of financial resources among the province of Pakistan on annual basis.

Taxes are pooled and distributed: Certain type of taxes are collected in each province and redistributed according to the NFC formula. Taxes included in the pool are:

- i. Income taxes
- ii. General Sales Tax
- iii. Wealth Tax
- iv. Capital gains tax
- v. Custom Duties

#### Background of NFC Award

After the separation of East-Pakistan resulting end of war with India in 1971, Prime Minister Zulfikar Ali Bhutto's government formed the commission under Chief Justice Hamoodur Rahman to investigate and study the loss of East Pakistan. While many factors had pointed out by the commission, generally marking the political, economic, ideological and geophysical reasons but the one emphasized the "Distribution of Resources" between each contingent. Controversially, the economic distribution of financials funds, grants, and resources were based on GNP performances and tax collection. The issue of population growth was never calculated and even raised by any civil servant or bureaucrat, since many had realized that if such factors determined, it would have resulted in greater share of East-Pakistan from the Federal Divisible Pool or in Federal Budget for East and West Pakistan.

Efforts were applied to end the economic disparity and depression among federal government and provincial governments of Pakistan by the lawmakers. While drafting the new Constitution in 1973, the issue of financial



distributions, economic equality, and economic justice was specifically mentioned in separate chapter of the Constitution. Article 160 of the Constitution of Pakistan, laid the foundation and philosophical existence of the National Finance Commission (NFC) and provides the logical framework of (NFC), in 1973. The Constitution was unanimously approved by all the major political parties in the country, and successfully promulgated the constitution in 1973. During the fiscal period from 1973 to 1974, Zulfikar Ali Bhutto and his government collaborated with the provincial governments of four provinces and successfully enacted the first financial award under NFC program; the first award proved to be success after it had produced a positive conclusive results in 1974.

In 1997, changes in NFC formulation was carried out by Prime Minister Nawaz Sharif after including the custom duties taxes with the award. Before 1991, the custom duties taxes revenue had been awarded to federal government while the revenue of Worker Welfare Fund (WWF) remain in the four provinces where they are collected. The principality of 1991 NFC Award specifies that 63.12% of collected revenue of taxes were directed to the federal government and 37% distributed to the four provinces. Prime Minister Sharif was widely given credit for achieving a consensus on formulating the 7th NFC Award with some positive recommendations. Earlier in 1991, the financial resources were vertically distributed at a fixed ratio of 20:80 among



federal and provincial governments.

Majority of the taxation and revenues are collected from Punjab and Sindh provinces of Pakistan. Almost all custom duties are collected at the Port of Karachi. Based on the formula determined in 1997, the taxation revenue collected from four provinces are: 65% from Sindh; 25% from Punjab; 7.01% from Khyber-Pakhtunkhwa; and only 3.09% from the largest province, Balochistan.

There is a constitutional obligation that the NFC Award cannot be announced if the four provinces have failed to develop consensus. Minor changes in NFC formulations were carried out by Finance minister Shaukat Aziz in 2001, allocating 50% of revenue to the four provinces against the prevailing formula of 62.89% as of 1995 NFC calculations. In 2005, President Pervez Musharraf finalizes the formula and enacted the award under the NFC program by the ratio of 52:48 among federal government and provincial governments.

The NFC program is viewed a step forward towards decentralization and establishment of fiscal federalism to promote equality

accountability, cost effectiveness, and opportunities for empowering and serving the poorest people in four provinces.

## Controversy in Sales Tax

A peep into the revenue distribution history of the subcontinent reveals that sales tax was exclusive domain of the provincial government before 1947. It was in 1974 NFC award that the sales tax was completely federalized. It declared the population as the only criterion for revenue distribution.

## Provincial Autonomy in Pakistan

The 18th amendment to Pakistan constitution became law after the country's President signed it on April 2010. The historic accomplishment was achieved after many rounds of discussion and compromises. Through the 18th amendment the concurrent legislative list containing subjects where Federal Government and the four provinces had shared jurisdiction prior to the 18th amendment was abolished.

Under the 18th amendment the following matters are moved to PART-1 (Federal Jurisdiction) from PART-II (where Council of Common Interest advises)

- Electricity
- Major Ports
- Census
- National Planning and economic

coordination

- Legal , medical and other professions
- Standards in institution for higher education and research, scientific and technical institutions.

Other than some jurisdictions from Concurrent Legislative list and Part-1 of the Federal Legislative list that have been moved to Part-II of the Federal Legislative list, the concurrent list is abolished and the Provinces regained jurisdiction on the following matters

- Sales Tax on Services
- Duties in respect to succession of property
- Estate Duty in respect of property.

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