TAX PAK

NEWSLETTER BY TOLA ASSOCIATES

TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

JULY
2020

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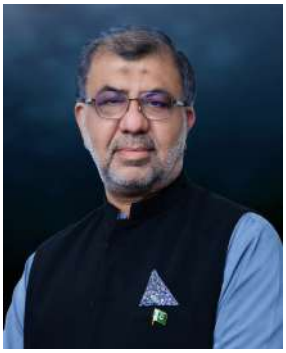

Dear All,

By the grace of Almighty Allah, the number of active Covid-19 cases have dropped significantly, showing positive signs of recovery. We now hope that our economy follows suit.

We welcome you to yet another edition of our TAX PAK Newsletter for the month of July 2020. At the beginning thereof are important Notifications/ circulars passed by the Tax and Corporate Authorities, including but not limited to, the Sindh Revenue Board ("SRB"), Federal Board of Revenue ("FBR") and the Securities and Exchange Commission of Pakistan ("SECP").

Later on, we have discussed a recent verdict passed by the Sindh High Court ("SHC") that pertains to the provisions of the Income Support Levy Act, 2013, wherein, the said Act has been declared ultra vires to the Constitution of Pakistan and has been declared as ineffective. Towards the end, we deliberate upon an important topic from the Sales Tax arena namely "Time and value of Supply", in our topic of the month segment.

You can visit our website www.tolaassociates.com, or download our mobile Application, in order to access previous versions of this newsletter or more of our monthly publications. The aforesaid application can be downloaded from the links below:

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

It is requested that you may circulate this e-copy within your circle(s), as our primary aim is to benefit the masses. Feedback is always welcomed.

Ashfaq Tola - FCA
Editor in Chief

1. NOTIFICATIONS/ CIRCULARS

i. DRAFT AMENDMENTS REGARDING IMPORT RULES UNDER SECTION 148 OF INCOME TAX ORDINANCE, 2001 ("ITO").

The FBR, vide SRO 615 dated 9th July 2020, has made draft amendments to the Income Tax Rules, 2002 ("ITR") by inserting a new Part 1A in Chapter IX, to give effect to the changes made under Section 148 through the Finance Act 2020.

The purpose of this Part is to prescribe Rules for additions, omission, or amendment of entries in the Twelfth Schedule and application of reduced rate on goods falling under Part III of this Schedule which are raw materials.

More specifically, it has laid down the procedure for reclassification of goods in the following instances:

- A capital good has not been classified in Part I.
- A raw material has not been classified in Part II.

The taxpayer can submit an application to reclassify the above to the Committee on Imported goods. These Rules also provide the manner in which FBR will dispose this application after recommendation of the said committee.

ii. SRB – AMENDMENTS IN NOTIFICATION REGARDING CERTAIN DEPUTY COMMISSIONERS TO EXERCISE THE POWERS OF COMMISSIONERS SRB OR COMMISSIONER (APPEALS).

The SRB has made an amendment in its previously issued notification dated 3rd July 2020, vide notification no. SRB-3-4/25/2020 dated 27th July 2020. The previously seated Assistant Commissioner Unit-3, Mr. Raheel Anwar Soomro has been replaced by Mr. Muhammad Ali Mazgani by virtue of the said amendment.

iii. SRB – NOTIFICATION REGARDING POSTINGS OF THE DEPUTY COMMISSIONERS/ASSISTANT COMMISSIONERS, SRB, AND THE UNITS OF SERVICE SECTORS ASSIGNED TO THEM.

The SRB, vide Notification No. SRB-3-4/24/2020, issued a jurisdictional Notification dated 3rd July 2020 in supersession to the Notification No. SRB-3-4/28/2019 issued earlier dated 8th July 2019. The Notification will take effect from 6th July 2020.

iv. SRB - NOTIFICATION REGARDING POSTINGS OF COMMISSIONERS OF SRB AND THEIR JURISDICTIONS

The SRB has, through Notification no. SRB-3-4/23/2020, issued a jurisdictional Notification dated 3rd July 2020. The said notification contains the name of the officer and its related jurisdiction as a Commissioner.

v. SRB - NOTIFICATION REGARDING JURISDICTIONS AND FUNCTIONS OF THE COMMISSIONERATES IN SRB AND UNITS OF THE SERVICES SECTORS UNDER THE SRB COMMISSIONERATES.

Through a Notification bearing No. SRB-3-4/22/2020, the SRA has issued a jurisdictional Notification dated 3rd July 2020, whereby, Service categories are assigned to various Commissioners.

vi. SRB - NOTIFICATION REGARDING CERTAIN DEPUTY COMMISSIONERS TO EXERCISE THE POWERS OF COMMISSIONERS SRB OR COMMISSIONER (APPEALS)

Vide Notification No. SRB-3-4/21/2020, the SRB has issued a jurisdictional Notification dated 3rd July 2020 in supersession to Notification No. SRB-3-4/25/2019 dated 8th July 2019 and SRB-3-4/35/2019 dated 29th November 2019. The said Notification is to take effect immediately.

vii. SRB - ONLINE SUBMISSION OF THE OPTION/ELECTION FORMS

The SRB, vide Circular No. 04 dated 24th July 2020, has informed that the Manual submission of option/election forms prescribed under the Sindh Sales Tax on Services Act, 2011 is not acceptable anymore via any mode, and therefore the registered person is to submit the form online on SRB portal.

Registered Persons who has submitted the option/election forms manually were needed to submit the form online with the due date being **29th July 2020** which was extended from 21st July 2020 for the people who were facing problems while submitting the forms online. In the future, no manual submission will be treated as Notified by this circular.

viii. SRB - INPUT TAX CREDIT AGAINST INVOICES ISSUED BY FOREIGN SERVICE PROVIDERS NOT HAVING SNTNS

The SRB has through a Circular bearing No. 06, dated 10th July 2020, stated the conditions in which a registered person will be able to claim input tax against invoices received from Non-resident Pakistanis not registered with the SRB.

The conditions are:

a) If the registered person receives the taxable services against an invoice issued by that foreign service provider
b) If the registered person pays consideration to the Foreign Service provider, for the services so received.
c) If the registered person deposits the amount of Sindh sales tax, on such services in Sindh Government's head of account "B-02384" in the prescribed manner.

In case all the conditions above are satisfied, the registered persons would claim the input under Sections 15, 15A and 15B of Sindh Sales Tax on Services Act, 2011 and the Rules thereunder.

ix. CLEARANCE DELAYS ON ACCOUNT OF CHANGES MADE IN SECTION 148 OF INCOME TAX ORDINANCE, 2001.

The FBR, vide Circular No. C. No. 3(24) E&C/2020/Pt, dated 21st July 2020 has clarified the issue of Clearance delays on consignments due to changes made in Section 148 "imports" of the ITO vide Finance Act, 2020.

It has been clarified by the FBR that in case the importer provides satisfactory evidence to the Collector of customs that the rate of Advance Income Tax he has claimed on his goods were allowed in the previous financial year for the same goods, the consignments will be cleared when the importer pays the differential amount of Advance income tax by either a pay order or a bank guarantee.

x. EXTENSION IN DATE FOR ANNEX-H FOR THE TAX PERIOD OF JULY 2019 EXTENSION IN DATE FOR ANNEX-H FOR THE TAX PERIOD OF JULY 2019

The FBR, vide Circular No C. No. 9(11)/ST/Misc/Cond/2016 /110737-R, dated 7th July 2020 had extended the date for filing Annex-H of the Sales tax return for the Tax Period of July, 2019 to January, 2020 till 31 July 2020.

xi. EXTENSION IN DATE OF POS INTEGRATION FOR TIER-1 RETAILERS

The FBR has, through Circular No C. No. 2(1)/ST & FE/Misc/2019/09599-R dated 3rd July 2020, apprised that in order to facilitate the registered retailers of Tier-1, the FBR has extended the time of Point of Sale (POS) integration with the FBR computerized system for efficient reporting of sales to **31st August 2020**. This will be subject to the condition that all Tier-1 Retailers must furnish in writing their willingness to integrate all their POSs to the respective RTO/LTU by 20th August 2020.

2. CORPORATE NOTIFICATIONS / CIRCULARS

➢ PREAMBLE

The SECP is the financial regulator for the corporate sector in Pakistan. It was formed on January 1st, 1990, succeeding to the previously established Corporate Law Authority or CLA. Being an independent agency, it performs all three functions; legislative, judicial, and executive. The SECP generally promotes a free market model, through its law, that requires that ALL MATERIAL facts be disclosed and that investors be free to choose whether to purchase a security, rather than government officials reviewing each security offering and determining whether the offering had sufficient MERIT before allowing the public to purchase such security.

As mentioned above, having legislative power but being non-political, the presence of non-elected representative poses a risk of isolation, lack of accountability and a lack of transparency in the decision making process as decision makers do not have a strong incentive to consider full ramifications of a decision before they make it. To mitigate this risk, the SECP does not adopt a rule without seeking objections/comments from the public with regards to any necessary amendments that have, or are to be made, in the draft legislation(s) before its implementation.

i. CORPORATE RESTRUCTURING COMPANIES (AMENDMENT) ORDINANCE, 2020.

The Government of Pakistan made amendments in the Corporate Restructuring Act, 2016 vide the Corporate

Restructuring Companies (Amendment) Ordinance, 2020, which was promulgated on 7th July 2020 and was published in the Gazette of Pakistan on the same day.

The amendment mainly included the provisions of Companies Act, 2017 which were inserted in the Corporate Restructuring Act, 2016.

ii. ALTERATION IN THE THIRD SCHEDULE TO THE COMPANIES ACT, 2017.

The SECP, vide SRO 614 dated 6th July 2020, made alterations to the Third Schedule of the Companies Act, 2017.

The Third Schedule of the Companies Act, 2017 provides classification of companies for the purpose of allocating applicable accounting frameworks and the relevant schedules of the Companies Act, 2017. Now, all the companies producing and selling sugar have been brought under the ambit of the third schedule.

iii. SRO 613 (DATED 7TH JULY 2020) - AMENDMENTS IN THE NON-BANKING FINANCE COMPANIES AND NOTIFIED ENTITIES REGULATIONS, 2008

Through the captioned SRO, the SECP has made amendments in the Non-Banking Finance Companies and Notified Entities Regulations, 2008 [NBFC & NE Reg. 2008].

The SECP has brought Exchange Traded Funds (ETF) under the ambit of [NBFC & NE Reg. 2008].

iv. SRO 582 (DATED 29TH JUNE 2020) – AMENDMENTS IN THE CREDIT RATING COMPANIES REGULATION, 2016

The SECP, has through the captioned SRO, made amendments in the Credit Rating Companies Regulation, 2016.

In the said SRO, certain additions were made in Regulation no. 2, wherein, the scope of "Private ratings", "Solicited ratings" and "Un-Solicited ratings" were added.

Other important additions were the eligibility of professional qualifications such as CA, CFA, ACCA and CMA under the head of "Competence and Capability" in Annexure C of the aforementioned regulation.

3. SINDH HIGH COURT HELD INCOME SUPPORT LEVY 2013 ULTRA VIRES TO THE CONSTITUTION

Income Support Levy (hereafter "ISL") was levied through the Income Support Levy Act 2013, enacted through the Finance Act 2013. As per its preamble, its purpose was to provide for financial resources for running an income support fund for economically distressed persons and their families. A levy @ 0.5% of net immovable assets held as at 30th June, was charged on all individuals having net moveable wealth more than Rs 1 million. However, it was repealed through the Finance Act 2014. Although the levy for TY 2014 and the pursuit thereof was maintained by the FBR issuing demand notices to the concerned individuals. In response, 576 taxpayers filed a Constitution Petition before Sindh High Court ("SHC") to declare the levy as Ultra Vires to the Constitution of Pakistan, 1973 ("Constitution"). The case was decided in and as a combined judgment in C.P. No. D-3757/2013.

1. GROUNDS TAKEN BY THE PETITIONERS

The grounds taken are divided in 2 categories:

1.1 The challenge of Vires to the Constitution

The Petitioners contended that ISL is not a tax, therefore, it cannot be levied through a Money Bill in terms of Article 73 of the Constitution. It may be noted here that according to Article 73, Money bills must be placed only before the National Assembly and can be passed while bypassing the Senate. The Senate can give only recommendations, however the same are not binding. Since ISL will not be deposited in the Federal Consolidated Fund, it is for a special purpose and not for a general purpose as tax is. Therefore, it needs to be approved through both National Assembly and the Senate in terms of Article 70 rand 78 of the Constitution. It may originate from any house in respect of any matter in the Federal Legislative List. If passed by both houses, it shall be presented to the President for his assent, and then the revenue so collected shall go to the Federal Consolidated Fund of Public Account, from where, it is distributed amongst the provinces as per their respective share, and is to be utilized for general public purposes.

The Petitioners further contended that even if it is treated as tax, it is discriminatory as it creates unreasonable classification between the individuals having same net moveable assets exceeding Rs 1 million, however, only existing taxpayers who are required to file wealth statement under Section 116 of ITO are charged the levy, and the individuals not required to file wealth statement i.e. non taxpayers are excluded from levy. Hence, it is a violation of the fundamental rights of citizens to be given equal treatment under Article 25 of the Constitution.

1.2 Notices issued AFTER the ISL was repealed, were illegal and without lawful jurisdiction.

The Petitioners contended that the ISL was repealed through Clause 10 of the Finance Act, 2014 without any saving or validation clause in the Finance Act 2014, therefore, no proceedings can be initiated, nor any order can be passed after the repeal of ISL. The normal effect of repealing a law is to wipe it out from the law book as it never been passed or existed. Since no proceedings or notices were issued, or order made, during which the ISL was in-field, the notices issued after being it repealed are illegal.

2. REBUTTAL BY DEPARTMENT/FEDERATION

2.1 The challenge of Vires to the Constitution

The counsel representing the Federation contended that ISL is a tax, as it has all elements of tax, and therefore it could be imposed through the Money Bill. As per Article 260, an Act of Majlis-e-Shoora (Parliament) means an Act passed by Majlis-e-Shoora OR National Assembly, therefore, Petitioners argument are not valid. With regards to the question that whether a Bill is a Money bill or not, the decision of Speaker of National Assembly shall be final. Moreover, as per Entry 250 in the Fourth Schedule of the Federal Legislative List, the Federation is competent to levy taxes on Capital Value of moveable assets, which may be generally or for a specific purpose. Hence, no distinction of tax or fee can be made in case of ISL being a capital tax. Further, as per Article 260 of the Constitution, a tax includes any tax or duty, whether general, local, or special, hence a special purpose tax is valid.

ISL is not discriminatory, because is liable to be recovered from all persons having moveable assets in excess of Rs. 1 Million.

2.2 Notices issued AFTER repeal of ISL, being illegal and without lawful jurisdiction

The Federation contended that if no saving or validation is provided in the repealing statute, then Section 6 of General Clauses Act, 1897 comes in to play which explains the effect of repealing of an enactment in such circumstances. Moreover, as per Section 6(c), unless a different intention appears, repeal of an enactment shall not affect any right, privilege, obligation or liability, acquired, accrued or incurred under the repealed enactment, whereas, Section 6(e) provides that the repeal does not affect any investigation, legal proceedings or remedy in respect of any such right, privilege, obligation, liability, penalty or forfeiture acquired, accrued or incurred under the repealed law.

Since the levy has been accrued before the repealing of the ISL, therefore, such obligation will remain in-field, and can be recovered through proceedings conducted after being repealed.

3. DECISION OF THE SHC

3.1 The challenge of Vires to the Constitution

The SHC observed that the distinction between "tax" and "fee" primarily lies in the fact that a tax is levied as a part of common burden while a fee is paid for a special benefit or privilege, and it is clear from budget speech of the Finance Minister that the receipts under this head will be credited to Income Support Programme of the Government. The preamble also shows that the special purpose is to provide financial assistance and other social protection and safety measures to economically distressed persons and their families through a levy to be called Income Support Levy, and also to provide for financial resources for running an income support fund for economically distressed persons and their families. Furthermore, in the charging section the word used is 'levy' not tax. Therefore, the ISL is a fee and not a tax. In

light thereof, it cannot be levied through a Money Bill under Article 73 of the Constitution.

With regard to the stance on discrimination by the levy, the SHC observed that the concept of absolute authority by rulers on their subjects, without having any representation of the people in such legislation, is no more available under the Modern Democratic System of Governments, which are run by the elective representatives of the people under their respective Constitutions. The Legislature can classify persons or property for imposing different tax rates, but it should not result in an inequality amongst same class of persons or property. If there is such an inequality, then it is liable to be struck down on account of an infringement of the fundamental right(s) relating to equality. Nevertheless, the ISL is discriminatory in nature as it creates an unreasonable classification within the same class, and hence it is ultra vires to the Constitution.

3.2 Notices issued AFTER repeal of ISL, being illegal and without lawful jurisdiction

The SHC disagreed with arguments of Federation and held that before a proper assessment is made and a charge created, the levy cannot become payable on an accrual basis only. Since prior to the repealing of ISL, no notices were issued, nor were there any assessment proceedings pending, the General Clauses Act 1897 will not apply where no saving clause is provided in the FA 2014, and accordingly all notices or orders are without jurisdiction or lawful authority.

4. TOPIC OF THE MONTH

- TIME AND VALUE OF SUPPLY

➢ PREAMBLE

This time we conclude our newsletter with a key concept within Sales Tax that is "Time and value of Supply". As we can adjudge from the name of the topic, that we have two conceptual products of Supply, i.e. the Time of supply and the value of supply, for the purpose of sales tax applicability. In this segment, it will be our aim to discuss the definition, concept, and technicalities present while evaluating the Time of Supply and Value of supply for the purposes of Sales tax chargeability, under Section 3 of the STA.

1. TIME OF SUPPLY

This concept is very important as it determines as to when the sales tax incidence arises. The concept of Time of Supply is categorized between services and goods. Goods are further sub-categorized into supply of goods under a hire-purchase agreement and supply of goods other than those under a hire-purchase agreement.

Supply of goods other than a hire-purchase agreement are taxable:

- At the time when goods are delivered and are available to the recipient; or
- At the time when the payment is received by the supplier of goods

whichever is earlier.

It means that an advance against supply is subject to sales tax at the time of payment of advance. Therefore, invoices also need to be issued in respect of advances received.

Here it is worthwhile to mention that a security deposit does not come under the ambit of advance, and that there is no sales tax incidence on the receiving of a security deposit.

Supply of goods made under a hire-purchase agreement are taxable when the hire-purchase agreement is entered into, i.e. the time of supply is the date of agreement and an advance in this case is not subject to sales tax.

In case of supply to an associated person, the time at which goods are made available to the associated person shall be treated to be the time of supply, and any advance will not be subject to sales tax.

In case of rendering of services, the services will be taxable at the time when the services are rendered or provided. It is worthwhile that after the enactment of

various provincial sales tax laws on services, only the services provided in the Islamabad Capital Territory come within the purview of the FBR.

The confusion arises in cases where a part payment is being made against the supply of goods and services. For the purposes of clarity, the partial payment made against supply of goods and services in a tax period will be chargeable to tax for the same tax period in which the partial amount is received.

For example, some goods were supplied by a manufacturer to its consumer for Rs. 8000 including 17% Sales Tax in the month of March 2020, while the consumer has paid 50% of the amount in February 2020. In such a case, the amount to be included in the in Annex-C of Sales Tax return for the month of February in terms of the abovementioned particular good would be Rs. 4000 x 17% i.e. Rs. 680.

Moreover, where any part payment is made in respect of any exempt supply, it shall be accounted for in the tax period in which the exemption is withdrawn.

For example, an item is exempt in June 2020 but is taxable in July 2020. Such items were delivered in July 2020, but the advance was received in June 2020. In such a case time of supply will be July 2020, i.e. the period in which exemption was withdrawn.

The rules related to advance payments are contained in Sales Tax General Order 1 of 2006, which are now incorporated as Rule 160 of Sales Tax Rule 2006 through Finance Act 2019. The salient features are as follows:

i. Payment of Tax: A registered person shall charge sales tax against any advance received and the same will be included in the output tax of the tax period in which such advance is received by him.
ii. Tax Invoice: A registered person is required to issue a serially numbered "**Advance Payment Receipt**" which shall be treated as tax invoice. Tax invoice against such advance may be issued at the time of actual delivery of goods. No tax shall be charged at the time of actual delivery on such advance. However, the registered person will mention the advance payment receipt number and the date in such invoice for the purposes of cross-referencing.
iii. Adjustment of advance: Where a registered person has deposited the tax on advance and such supply or part is cancelled or its value is changed. The registered person may issue a credit note and make adjustment correspondingly.

Where a registered person has deposited tax on advance then the time limit for the issuance of debit and credit note shall not apply as per ST General Order 1 of 2006.

2. VALUE OF SUPPLY

The Value of supply is the amount on which the Sales Tax is chargeable. While determining the value of supply, the consideration received against the goods supplied, including all the Federal and Provincial Duties and Taxes, constitute the value of supply on which Sales Tax is applicable.

For imported goods, the value of supply will be determined by including the customs and excise duty levied thereon.

For Example, the value of raw material imported is Rs. 1000, customs duty 20%, FED 10%, Sales Tax 17% and advance income tax is 5.5%. The amount of sales tax in this case would be:

Rs.1000 + custom duty Rs.200=Rs.1200/-

Rs.1200 + FED Rs. 120=Rs1320/-

Sales tax is Rs. 1,320 x 17% = Rs. 224

Advance income tax is 5.5% x (1320+224) =Rs.85

The trade discount shall be excluded if the tax invoice shows discounted price and the amount of discount is in conformity with the normal business practice. Items present in the 3rd schedule of the STA will not be allowed for trade discount as the manufacturer has to charge sales tax on the recommended retail price instead of his own value of supply. Early payment

discount is not deducted from value of supply as invoice does not show the discount in such cases.

As far as credit supplies are concerned, any markup charged on the credit supplies should not be a part of Value of supply for the purpose of charging tax as per Clause 5 of General Order 3 of 2004.

In general practice, where consideration against supply is partly received in kind or no consideration is received or where the supply is made on installment basis, the value of supply would be adjudged on the basis on the open market price of the supply.

In case, where the supplies are made by a principle to a vendor in terms of raw material or semi-manufactured goods i.e. toll manufacturing. The vendor will use the conversion cost of the raw material or semi-manufactured goods into finished goods as value of supply for the purpose of charging sales tax. In case where the vendor has bought tax-paid raw material or semi-manufactured goods, he will be able to claim tax credit for the same.

If there is reason to believe that the value of supply is under declared in the tax invoice, the Value of supply will be determined by the Valuation Committee comprising representatives of trade and the sales tax department of the Federal Board of Revenue ("FBR").

In case of supply between associated persons, the value as in normal case (i.e. consideration in money including all Federal and Provincial duties which the supplier receives in respect of the supply) excluding amount of Sales Tax; or open market price excluding sales tax, whichever is higher, will be value of the supply.

The Value of supply of electric and gas distribution company will be total amount billed including price of electricity or gas charges, rent, commission, and all local, provincial, and federal duties and taxes but excluding late payment surcharge and sales tax.

DISCLAIMER

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