

TAX PAK

NEWSLETTER BY
TOLA ASSOCIATES



AUGUST
2020



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EDITORIAL NOTE

Dear All,

By the grace of Almighty Allah, the number of active Covid-19 cases have dropped significantly, showing positive signs of recovery in COVID-19 cases and economy as well.

We welcome you to yet another edition of our TAX PAK Newsletter for the month of August 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 decision passed by the Federal Tax Ombudsman ("FTO") that bank certificate of foreign remittance is sufficient to claim exemption u/s 111(4) of ITO. Towards the end, we deliberate upon an important topic from the Income Tax arena namely "Recharacterization of Income and deductions", in our topic of the month segment.

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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

A. AMENDMENTS IN INCOME TAX RULES 2002, BANKING COMPANIES REPORTING REQUIREMENT RULES 2010

The FBR vide SRO 773(I)/2020 dated August 24th, 2020, issued amendments in Chapter VIIIA Banking Companies Reporting Requirement Rules 2010 relating to Section 165A of the ITO. The following changes have been made:

- The minimum threshold for reporting monthly deposits has been increased from 1 million to 10 million. Further the Bank will also report Resident/non-resident status and IBAN no. business/profession, address, and Telephone no.
- The minimum threshold for reporting credit card information on payment has been increased from 1 lac to 2 lacs. The bank will also now report information mentioned in previous point.
- The minimum threshold for reporting cash withdrawal information on payment has been changed from fifty thousand per day aggregating one million per month to one million per month with same particulars as above.
- The minimum threshold for reporting profit on debt was Rs 1 million for filers and Rs 5 lac for non-filers, now there is now minimum threshold.

B. AMENDMENTS IN INCOME TAX RULES 2002, COMMON REPORTING STANDARDS

The banks and financial institution are required to provide information regarding non-residents to the FBR u/s 165B for automatic exchange of information under bilateral agreement or multilateral convention. The Rules regarding reporting requirement are provided in Chapter XIIA of Income Tax Rules, 2002 inserted vide SRO 166(I)/2017 dated March 15th, 2017. Now FBR has made amendments in this chapter vide SRO 773(I)/2020 dated August 24th, 2020 as follows:

- Change made in definition of "Controlling person" whereby person who owns 20% or above stake in an entity will be included in definition.

- The FIs are required to keep record of steps undertaken for due diligence procedures for atleast 5 years.
- The date for filling of common reporting standards reports shall be 31st May of each year.
- The common reporting standard reports shall be filed on the AEOI portal on FBR's official website in CRS XML Schema prescribed by the Global Forum of Organization for Economic Cooperation and Development (OECD).
- The FBR or any person authorized can call the record and inspect premises
- The FBR can make compulsory enrolment of FI with AEOI portal on FBR's official website if FI fails to enroll voluntarily.

C. DRAFT INCOME TAX RETURN FORMS FOR SALARIED PERSONS, AOPS, COMPANIES AND BUSINESS INDIVIDUALS FOR TAX YEAR 2020

The FBR vide SRO 745(I)/2020 dated 19th August 2020, has issued draft returns for above persons for Tax Year 2020. On issue of final forms, the taxpayers can submit their online returns for the said tax year.

D. EXEMPTION/REDUCTION OF TAXES FROM IMPORT OF REFINED WHITE SUGAR

Due to continued price increases in local supply of sugar, the Federal Government, vide SRO 750(I)/2020 dated 20th August 2020, has inserted Clause 12G in Part IV of Second Schedule of ITO, whereby the provision of Section 148 shall, in pursuance of the Cabinet Decision in case No. 541/30/2020 dated 4th August 2020, not apply on import by Trading Corporation of Pakistan up to 30,000 metric tons of white sugar having PCT heading 1701.9910, 1701.9920.

For import by others, the FG vide SRO 771(I)/2020 dated 24th August 2020 has reduced the rate u/s 148 to 0.25% in respect of import of white crystalline sugar falling under H.S codes 1701.9910 and 1701.9920 from 25th August 2020 to 15th November 2020. Maximum 300,000 metric tons in manner prescribed by Ministry of Commerce. (Clause 9AA Part II Second Schedule).

Similarly, through SRO 751(I)/2020 dated 20th August 2020, the FG has exempted Sales Tax on import of 300,000 metric ton of white sugar by TCP, and has reduced the rate of sales tax @1% and exemption of minimum value addition tax for others for period from 25th August 2020 to 30th November 2020 vide SRO 770(I)/2020 dated 24th August 2020.

E. EXEMPTION OF TAXES FROM IMPORT OF COVID RELATED SUPPLIES

The Federal Government has exempted oxygen gas (PCT Code 2804.4000), Cylinders for oxygen gas (PCT Code 7311.0090), Cryogenic tanks for oxygen gas (PCT Code 7311.0030) from tax u/s 148 for 3 months starting from 23rd June 2020.

The FG has also exempted these items from Sales Tax vide SRO 649(I)/2020 dated 3rd August 2020 for 3 months starting from 23rd June 2020.

F. DRAFT AMENDMENTS IN INCOME TAX RULES- ALTERNATIVE DISPUTE RESOLUTION

The FBR had revamped provisions relating to Alternate Dispute Resolution in Section 134A through FA 2020. Now, to make rules in line with them, draft amendments has been proposed in Rule 231C vide SRO 780(I)/2020 dated 26th August 2020.

G. AUDIT POLICY 2019

The FBRs' Taxpayers Audit Wing has issued Audit Policy 2019 for Tax Year 2018, whereby the FBR will conduct computer ballot by applying Risk Based Parameters for selection of 0.76% of cases for audit out of total filers after exclusions in Income Tax for the tax year 2018. For Sales Tax and FED, the FBR would select 1.67% and 5.65% cases for audit, respectively, after exclusions.

G. 1. Exclusions for Income Tax

- i. All cases already selected for audit by the Commissioner Inland Revenue and Director I&I (IR) under Section 177 and in consequence of action u/s 175 of the ITO for Tax Year 2018.
- ii. All Cases where income chargeable to tax under the head salary and/or pension exceeds 50% of taxable income, except cases having business income.

Directors of companies do not qualify for this exclusion.

- iii. All cases where entire income is covered under Final Tax Regime (FTR).
- iv. All cases where declaration has been made under the Voluntary Declaration of Domestic Assets Act, 2018
- v. All cases where declaration has been made under the Asset Declaration Ordinance, 2019.

G. 2. Exclusions for Sales Tax/ FED

- i. All cases already selected under Section 25 and 38 of Sales Tax Act, 1990 by the Commissioner Inland Revenue or Director I&I (IR) for tax periods corresponding to the accounting period adopted for the purpose of returns of income under the ITO for tax year 2018 provided that where only a part of the said accounting period had been audited already, the relevant authority may select the remaining period for audit.
- ii. Federal, Provincial and Local Governments Departments.
- iii. All cases where declaration has been made under Voluntary Declaration of Domestic Asset Act, 2018. [There is anomaly as no sales tax amnesty was given in 2018]
- iv. All cases where declaration has been made under the Asset Declaration Ordinance, 2019.

H. GREENFIELD INDUSTRIAL UNDERTAKING APPROVAL AND EXEMPTION RULES

The FG provided exemption of Sales Tax on import of plant and machinery classified under chapter 84 and 85 by greenfield industries by inserting entry no. 150 in Sixth Schedule of Sale Tax Act, 1990 vide Finance Supplementary (Second Amendment) Act, 2019. Now to streamline process of obtaining exemption, FBR through SRO 777(I)/2020 dated 25th August 2020 has inserted new Chapter XVII-A in Sales Tax Rules, 2006.

I. COLLECTION OF EXTRA TAX ON ELECTRIC POWER AND NATURAL GAS CONSUMPTION

As per Sales Tax Special Procedure Rules, 2007 Chapter IVA "Special Procedure For Collection And Payment Of Extra Tax On Supplies Of Electric Power And Natural Gas Consumed By Unregistered And Inactive Persons", every person supplying electric power or natural gas, was

required to charge and collect extra tax at the rate notified by the Federal Government, from every consumer having an industrial or commercial connection, where the bill for a month is in excess of rupees fifteen thousand, and the consumer either has not provided his sales tax registration number to the supplier or his name is not shown as active on the Active Taxpayers List (ATL) maintained by the FBR.

This was repealed by Notification SRO 694(I)/2019 dated 29th June 2019. Now FBR has incorporated the provisions in Sales Tax Rules, 2006 by inserting Chapter XVII-B vide SRO 777(I)/2020 dated 25th August 2020.

J. AMENDMENTS IN SALES TAX RULES, 2006

The FBR vide SRO 776(I)/2020 dated 25th August 2020 and SRO 793(I)/2020 dated 27th August 2020 has made following changes:

J. 1. Application for registration-Rule 5

In Form STR-1, which is application for registration, in entry no 23 which requires applicant to provide “Detail of business outlets/branches”, now “Detail of all brands names/trademarks in which dealing” is added.

J. 2. Sales Tax Return-Rule 14

As per Rule 14, all registered manufacturers making supply of specified taxable goods shall furnish, in Annex-J of the monthly return, details of such goods manufactured or produced and goods supplied, using the specified units. Now in the specified list “Concentrate” has been added in Rule 14.

Further, new particulars have been added such as NTN, Business name, item code, products detail, value of supplies local and value of supplies export while column regarding monthly installed capacity has been deleted.

J. 3. Electronic filing of Sales Tax Return-Rule 18

A condition has been added in Sub Rule(1) that if a registered person fails to fill-in relevant data or information in any applicable column of the sales tax return or any annexure thereto in his case, such return shall be treated as invalid. An Explanation has also been included whereby the electronic return designed in pursuance to the Change Request Form(s) (CRFs), and finally made available on web portal of the Board shall be deemed as prescribed return.

J. 4. CHANGES IN ALTERNATE DISPUTE RESOLUTION

Through FA 2020, the provisions related to alternate dispute resolution in Sales Tax Act, 1990 were revamped. The same changes now have been made in sales tax rules, 2006 as below:

J. 4.a Application for alternative dispute resolution and appointment of Committee-Rule 65

Rule 65 prescribe procedures for applying for resolution of dispute under Section 47A of Act, now changes have been made whereby Chief Commissioner Inland Revenue having jurisdiction over the case shall be Chairman of committee formed for ADR instead of A retired judge not below the rank of District & Sessions Judge, appointed in a manner as aforesaid. The form of application SRT-27 along with Annexure has also been changed.

J. 4.b Procedure for alternative dispute resolution - Rule 66

As per Rule 66, the Chairperson of the Committee shall be responsible for deciding the procedure to be followed by the Committee including to decide about the place of sitting of the Committee **in consultation with the Chief Commissioner having jurisdiction over the applicant.** Now Chairperson will be the Chief Commissioner himself therefore the clause in bold has been removed.

J. 4.c Decision of Committee -Rule 68

Before Amendment	After Amendment
(1) The Committee shall decide the dispute within one hundred and twenty days from the date of receipt of order of withdrawal from the Board mentioned in sub-rule (5) of rule 65. Decision of majority members of the Committee shall be construed decision of the Committee which shall be communicated by the Committee to the Board, the Commissioner having jurisdiction and the applicant.	(1) The Committee shall decide the dispute within one hundred and twenty days from the date of its appointment by the Board, through consensus. The Committee shall communicate its decision to the Board, the Commissioner having jurisdiction and the applicant.
(2) The decision of the Committee under sub-rule	(2) The decision of the Committee under sub-rule

(1) shall be binding on the Commissioner and the aggrieved person.

(1) shall be binding on the Commissioner **where the aggrieved person, or class of persons, have withdrawn the appeal pending before any appellate authority or the court of law and have communicated the order of withdrawal to the Commissioner:**

Provided that if the order of withdrawal is not communicated to the Commissioner within sixty days of the service of decision of the committee upon the aggrieved person, the decision of the committee shall not be binding on the Commissioner

K. EXTENSION IN FILLING OF ANNEX-H FOR TAX PERIOD JULY 2019 TO FEBRUARY 2020

FBR through letter no. C.No. 9(11) /ST/Mis /Cond/2016/141345-R dated 24th August 2020 has extended time limit up to 19.09.2020 in case of Taxpayers who had filled Annexure-H on or before 20th August 2020 and FBR had ordered them to be reopened. It is further clarified that taxpayers who have not filed Annexure-H at all will be required to follow Rule 39D of Sales Tax Rule, 2006 for filling and processing of refund claims.

L. EXPLANATION OF IMPORTANT AMENDMENTS IN SALES TAX ACT, 1990 AND FED ACT, 2005

The FBR has issued letter no. C.No.2/10-STB/2020(Pt-I)/132927-R dated 6th August 2020 whereby important amendments in Finance Act were explained and illustrated.

M. STANDARD PROCEDURE FOR OVERRULING THE STARR OBJECTIONS ON SALES TAX REFUND CLAIMS

The FBR has issued letter no. C.No.4(1)ST-LP&E/Misc/2019 dated 4th August 2020 to document standard procedure for over ruling the STARR Objections on Sales Tax Refund claims in a single document and to remove gaps,

contradictions and variance which were present in various instructions, guidelines w.e.f. 01-08-2020.

For Refund Claims refused by FASTER/ERS, the Claimant may apply to FBR through concerned Chief Commissioner for reprocessing of the refund claim or revision of Annexure H mentioning reasons therein.

N. KHYBER PAKHTUNKHWA SALES TAX ON SERVICES (WITHHOLDING) REGULATIONS, 2020

The KPRA vide notification no. F-16(4)KPRA/Notification/WH/1394-99 dated 13th August 2020 issued Khyber Pakhtunkhwa Sales Tax on Services (Withholding) Regulations, 2020 w.e.f. 1st September 2020, and Khyber Pakhtunkhwa Sales Tax on Services Special Procedure (Withholding) Regulations, 2015 are now repealed. The changes made are discussed as follows:

- Individual/AOP providing or receiving advertisement services and persons registered with the Authority receiving taxable services from unregistered persons were withholding agents in repealed withholding Rules, now they have been omitted.
- Telecommunication services (excluding such services as are provided or received by Telecom companies to or from each other) shall not be subject to withholding.
- 100% withholding on following:
 - Advertisement services
 - Service provided by Unregistered, inactive, or non-active taxpayers
 - Services rendered to Federal, provincial governments or public sector institutions
 - Services provided in KPK by non-resident
 - Services liable to tax at reduce rate i.e. less than 15%
- In all other cases rate of withholding has been increased from 20% to 50%.
- Clarification is added that no input adjustment will be allowed on reduced rate services.

O. AMENDMENT IN SECOND SCHEDULE OF KPK FINANCE ACT, 2013- REDUCTION IN RATES

The KPK Finance Ministry has made following amendments in Second Schedule of Act vide Notification no. BO(Res-III)FD/2-2/2019-20/Vol-I dated 5th August 2020:

Before Amendment	After Amendment
<p>1. Services provided or rendered by hotels, motels, guest houses, resorts, accommodation-and/or-food service providing farm-houses, motorway-or- highway-side.....</p> <p>Exemptions and reduced tax rates:</p> <p>(iii) In case of restaurants excluding those operating in corporate sector, or as franchises of multinationals, or chains of restaurant businesses, or have registered business or brand names, the rate of tax shall be eight percent (8%) without any input tax adjustment:</p> <p>Provided that in case of traditional type restaurants usually called as dhaba or conventional hut-type or similar other road/street side non-air-conditioned restaurants usually serving limited range of pre- cooked or pre-prepared food items with informal seating environment, the rate of tax shall be two percent (2%) without any input tax adjustment.</p> <p>(iv) In case of traditional accommodation facilities like sarrayae or inns or open air overnight bed provisioning services generally located or available around or in the vicinity of railway stations, bus or wagon stands (stations), the rate of tax shall be two percent (2%) without any input tax adjustment if the charges for overnight stay do not exceed rupees three hundred per bed.</p>	<p>1. Services provided or rendered by hotels, motels, guest houses, resorts, accommodation-and/or-food service providing farm-houses, motorway-or- highway-side.....</p> <p>Exemptions and reduced tax rates:</p> <p>(iii) Services provided or rendered by non-corporate local chains of hotels (including guest houses and lodges etc.) and restaurants shall be charged to tax at the rate of Eight Percent (8%) without input tax adjustment; provided that where in any case of such restaurant, the Restaurant Invoice Management System (RIMS) is installed and working properly on regular basis, the rate of tax shall be further reduced to Five Percent (5%) without any input tax adjustment:</p> <p>Provided that in case of traditional type restaurants usually called as dhabha or conventional hut-type or similar other road or street side non-air-conditioned restaurants, usually serving limited range of pre-cooked or pre-prepared food items with informal seating environment (located or operating anywhere in the tariff areas of the Province), the tax shall be charged and paid at the rate of One Percent (1%)</p> <p>(iv) In case of traditional accommodation facilities like sarrayae or inns or open air overnight bed provisioning services generally located or available around or in the vicinity of railway stations, bus or wagon stands (stations), the rate of tax shall be one percent (1%) without any input tax adjustment if the charges for overnight stay do not exceed rupees three hundred per bed.</p>
<p>2. Services provided or rendered by beauty parlors, beauty clinics, healthcare centers, cosmetic or plastic surgery centers/clinics, hair transplant centers..... "Eight Percent (8%) without input tax adjustment.</p>	<p>2. Services provided or rendered by beauty parlors, beauty clinics, healthcare centers, cosmetic or plastic surgery centers/clinics, hair transplant centers..... "Five Percent (5%) without input tax adjustment.</p>
<p>3. Services provided or rendered by stand-alone or other launderers and dry cleaners including carpet or sofa set or similar furniture items cleaners or washers:</p> <p>Reduced Rate of Tax:</p> <p>The medium sized stand- alone launderers and dry cleaners shall be liable to tax at the rate of eight percent (8%) without input tax adjustment</p>	<p>3. Services provided or rendered by stand-alone or other launderers and dry cleaners including carpet or sofa set or similar furniture items cleaners or washers:</p> <p>Reduced Rate of Tax:</p> <p>Services provided or rendered by medium sized stand-alone or other launderers and dry cleaners including carpet or sofa set or similar furniture items cleaners or washers shall be chargeable to tax at the rate of two percent (2%) without any input tax adjustment</p>

5. Services provided or rendered by persons authorized to transact or deal with business in any manner on behalf of others such as customs agents, shipping agents.....

Reduced Rate of Tax:

All services of this entry other than business support services and labour or manpower supply services shall be charged to tax at the rate of Eight Percent (8%) without any input tax adjustment.

8. Services provided or rendered in matters of sale, purchase, rent or hire (other than rent-a-car) under any kind or type of arrangements

Reduced Rate of Tax:

Tax shall be charged at the rate of five percent (5%) without any input tax adjustment in case of property dealers, property agents and realtors, dealers of second hand goods of all categories including second hand automobiles and all renting services covered in this entry.

9. Services provided by specialized workshops or undertakings:

.....

Five Percent (5%) without any input tax adjustment in all cases except industrial workshops and authorized automobile dealers' workshops where the tax shall be charged at the rate of Ten Percent (10%) without input tax adjustment.

13. Services provided by persons engaged in contractual execution or performance of works (including repair

"Fifteen Percent (15%)

15. Digital or IT-based services in whatever form or manner or under whatever arrangement

Five Percent (5%)

17. Airport services (including passenger facilitation, car parking, cargo handling, cargo warehousing.....

Fifteen Percent (15%)

5. Services provided or rendered by persons authorized to transact or deal with business in any manner on behalf of others such as customs agents, shipping agents.....

Reduced Rate of Tax:

(i) All services of this entry other than business support services and labour or manpower supply services shall be charged to tax at the rate of Eight Percent (8%) without any input tax adjustment.

(ii) Business support services and labor or manpower supply services shall be charged to tax at the rate of five percent (5%) without any input tax adjustment.

8. Services provided or rendered in matters of sale, purchase, rent or hire (other than rent-a-car) under any kind or type of arrangements

Reduced Rate of Tax:

All services covered in this entry except services (whole range) of authorized automobile (all categories of automobiles) dealers shall be chargeable to tax at the rate of two percent (2%) without any input tax adjustment.

9. Services provided by specialized workshops or undertakings:

.....

(i) Five Percent (5%) without any input tax adjustment in case of industrial workshops,

(ii) Two Percent (2%) without any input tax adjustment in case of all categories or types of workshops,

(iii) Two Percent (2%) without any input tax adjustment in case of standalone car wash (car wash station) services, and

(iv) Ten Percent (10%) without any input tax adjustment in case of authorized automobile dealers' workshops (whole range of their workshop services including car wash etc.

13. Services provided by persons engaged in contractual execution or performance of works (including repair

Five Percent (5%) without any input tax adjustment

15. Digital or IT-based services in whatever form or manner or under whatever arrangement

Two Percent (2%) without any input tax adjustment

17. Airport services (including passenger facilitation, car parking, cargo handling, cargo warehousing.....

Ten Percent (10%) without any input tax adjustment.

18. Dryport services including operation of a dryport and other services provided at or in respect of dryport such as inward/outward transportation/movement of goods, Fifteen Percent (15%)	18. Dryport services including operation of a dryport and other services provided at or in respect of dryport such as inward/outward transportation/movement of goods, Ten Percent (10%) without any input tax adjustment
20. Cinematographic production, photographic services, recording services and telecasting or broadcasting Ten Percent (10%) without any input tax adjustment	20. Cinematographic production, photographic services, recording services and telecasting or broadcasting Two Percent (2%) without any input tax adjustment
21. Event management services whether covering all or any of the processes like planning, budgeting, scheduling Fifteen Percent (15%)	21. Event management services whether covering all or any of the processes like planning, budgeting, scheduling Eight Percent (8%) without any input tax adjustment.
25. Services provided or rendered by call centers (by whatever name called) engaged in mediating business..... Five Percent (5%) without any tax adjustment	25. Services provided or rendered by call centers (by whatever name called) engaged in mediating business..... Two Percent (2%) without any tax adjustment
26. Storage and warehousing services including public bounded warehouses, cold storages and yards or places Fifteen Percent (15%)	26. Storage and warehousing services including public bounded warehouses, cold storages and yards or places Five Percent (5%) without any input tax adjustment.
32. Valuation or assessment services including competency and eligibility testing services and services Fifteen Percent (15%)	32. Valuation or assessment services including competency and eligibility testing services and services Five Percent (5%)
33. Services provided for inland carriage of goods by air, railways or otherwise against freight or carriage charge.	33. Services provided for inland carriage of goods by air, railways or otherwise against freight or carriage charge: Provided that the following services of Pakistan Railways whether falling under this Serial No. or elsewhere in this Schedule, shall be liable to tax at the rate of two percent (2%) without any input tax adjustment: (i) courier services in relation to the speedy, fast, quick, or urgent mail, parcel or cargo services provided; and (ii) services provided for inland carriage of goods against freight or carriage cargo
34. Services provided or rendered by under writers including sponsorship services. Fifteen Percent (15%)	34. Services provided or rendered by under writers including sponsorship services. Two Percent (2%) without any input tax adjustment
35. Services provided or rendered by indenters and similar intermediaries. Fifteen Percent (15%)	35. Services provided or rendered by indenters and similar intermediaries. Two Percent (2%) without any input tax adjustment
36. Services provided or rendered by auctioneers Fifteen Percent (15%)	36. Services provided or rendered by auctioneers Two Percent (2%) without any input tax adjustment
39. Services provided or rendered in respect of quality assurance, quality control, quality inspection	39. Services provided or rendered in respect of quality assurance, quality control, quality inspection

Fifteen Percent (15%) 42. Online Market Place (OMP) including online platform or portal services.....	Two Percent (2%) without any input tax adjustment 42. Online Market Place (OMP) including online platform or portal services.....
Five Percent (5%) without any input tax adjustment 44. Services relating to or in respect of the installation, erection, commissioning, or other permanent structure affixed/linked/tied placement	Two Percent (2%) without any input tax adjustment 44. Services relating to or in respect of the installation, erection, commissioning, or other permanent structure affixed/linked/tied placement
Fifteen Percent (15%)	Two Percent (2%) without any input tax adjustment

2. CORPORATE NOTIFICATIONS / CIRCULARS

A. AMENDMENTS IN PRIVATE FUNDS REGULATIONS, 2015

The SECP in exercise of power in Section 282B of the Companies Ordinance, 1984 vide SRO 545(I)/2020 dated 10th June 2020, has made certain amendment in the Private Funds Regulations, 2015 which were previously published as draft vide SRO 1214(I)/2019 dated 8th October 2019.

The amendments mainly relate to:

- Insertion/amendment of definition of 'Angel Fund,' 'Angel Investor,' 'Eligible Investor,' Hedge Fund, Impact Fund, Infrastructure Fund, Private Equity and Venture Capital Fund, Small and Medium Enterprise Fund, and Venture Capital Fund;
- Prohibition to engage in business of private equity and venture capital fund management service without registration;
- Role of private management company;
- Minimum investment in private fund;
- Investment conditions and restrictions;
- Contents of placement memorandum;
- Private fund valuation and pricing;

B. DELEGATION OF POWERS – INSURANCE

The SECP vide SRO 744(I)/2020 dated 17th August 2020 has delegated its various powers under Companies Act, 2017, Insurance Ordinance, 2000 (XXXIX of 2000), Takaful Rules, 2012, Companies (further issue of shares) Regulations, 2018, Listed Companies (Buy-Back of Shares) Regulations, 2019 to Commissioner (Market Development Policy and Regulation Department - Insurance Division) and

Commissioner (Supervision Department – Insurance Division).

3. FTO ISSUED RECOMMENDATIONS THAT BANK CERTIFICATE OF FOREIGN REMITTANCE IS SUFFICIENT TO CLAIM EXEMPTION U/S 111(4) OF INCOME TAX ORDINANCE, 2001[ITO]

Section 111 of ITO empowers Commissioner to include any unexplained income or concealed asset of a person to its income chargeable to tax. An exception to this is provided in case of foreign remittances u/s 111(4) whereby if a person brought into Pakistan, undisclosed foreign exchange remittances through proper banking channel the tax authorities could not include such in taxable income. In the instant case, the taxpayer was selected for audit of tax year 2016 through balloting u/s 214C, and intimation was issued u/s 177 of ITO vide letter dated 12.06.2018. In the meanwhile, taxpayer availed amnesty under Voluntary Declaration of Domestic Assets Act, 2018 and declared undisclosed income and assets amounting Rs 4.526 million on 31.07.2018. However, Department disregard the amnesty and continued audit proceedings against assets declared in amnesty and foreign remittance of Rs 30 million declared in return of tax year 2016. The taxpayer, felt aggrieved, preferred a complaint with FTO vide Compliant no. 1239/GWL/IT/2018. The FTO issued findings/recommendations dated 13.11.2018 that FBR directs the Commissioner-IR, Zone-II, Gujranwala to consider while finalizing the audit proceedings for tax year 2016, declaration of assets dated 31.07.2018 filed by the taxpayer.

The taxpayer considered FTO recommendations incomplete, as Commissioner-IR subsequently issued

notices u/s 176 to banks to confirm authentication of bank certificates of foreign remittances over and above amount declared in amnesty i.e. Rs. 25.474 million and filed Review Petition under Section 14(8) of FTO Ordinance 2000, under which the Federal Tax Ombudsman shall have the power to review any finding communicated or recommendation made, or any order passed by him.

1. GROUNDS TAKEN BY THE PETITIONERS

The Complainant taxpayer had sought to review of findings on the basis of following grounds:

1.1 No verification of Bank Certificates is required u/s 111(4) of ITO

The taxpayer argue that it has furnished proper bank certificates of scheduled bank as required u/s 111(4)(a) of ITO regarding receipt of foreign remittances through exchange company of Dubai and ACIR Audit Unit-8, Gujranwala has un-necessarily issued notices to the bank for verification which tantamount to harassment. Therefore, it was prayed to restrain ACIR, Audit Unit-8, Zone, Gujranwala from issuance of illegal notices causing harassment and recommend action against the official(s) of Department.

1.2 No verification of Bank Certificates is required when amnesty has been availed

The taxpayer has further contended that as voluntary declaration of domestic assets was filed by it, it provides immunity from all proceedings under ITO, therefore audit proceedings u/s 177 should be dropped.

2. REBUTTAL BY DEPARTMENT/FEDERATION

2.1 No verification of Bank Certificates is required u/s 111(4) of ITO

The Department contended that bank certificates furnished as evidence of foreign remittance did not fulfill the requirement of Section 111(4) of ITO, therefore notice issued to bank u/s 176 of ITO to confirm foreign remittance in the name of the taxpayer.

2.2 No verification of Bank Certificates is required when amnesty has been availed

The department contended that foreign remittance claimed to be received was Rs 30 million and amnesty was

availed for Rs. 4.526 million. Therefore the foreign remittance over and above amnesty i.e. Rs 25.474 million was sought to be verified and hence there is no illegality in issuance of notices and department is authorized to check its taxability in view of provision of Section 111(4) of ITO.

3. DECISION OF FTO

The FTO noted that the condition of Section 111(4) for exemption that 'receipt of foreign remittance through normal banking channel' has been fulfilled or not will be determined by the State Bank of Pakistan. Therefore, a letter was written to SBP to confirm whether exemption was available to taxpayer or not. In this regard SBP describes the procedure for foreign remittance through different channels that will be eligible to exemption as follows:

- **Channel 1** - Remittances through Schedule Banks: Foreign Currency is surrendered to the bank located in the country where the remitter resides and same is paid in Pakistan after conversion into Pak Rupee by the bank. The remittance received through this procedure will constitute "foreign exchange remitted from outside Pakistan through normal banking channels" as required in Section 111(4) of ITO.
- **Channel 2** - Remittance through Foreign Exchange Companies: Foreign currency is surrendered to the bank located in the country where remitter resides and same is paid in Pakistan after conversion into Pak Rupees by the bank. The SBP noted that the overseas remitter books the home remittance transaction and foreign currency is converted into PKR at the offered exchange rate by overseas Money Service bureaus (MSB) / Exchange Companies (EC) at the time of booking of remittance. The MSB/EC sends advice/instructions to Pakistani Banks through email with which it maintains a pre-funded Non-Resident Pak Rupee Account (NRPKR) and in some cases Foreign Currency Account (FFCA) for execution of home remittance transactions. Upon receiving instructions, domestic bank transfers the sum, as mentioned in the MSB's/EC advice/ instructions by debiting MSB's/EC's NRPKR/FCA, to the beneficiary's account immediately,

Subsequently, Pakistani Bank receives foreign exchange proceeds through SWIFT to replenish NRPKR/FCA of the MSBs/ECs. The remittances received through MSBs/ECs also constitute to be “foreign exchange remitted from outside Pakistan through normal banking channel as stipulated in Section 111(4) of ITO.

- **Channel 3:** In case of Money transfer Operators (MTOs) such as Western Union, Money Gram or Ria Finance, all of the above also have pre-funded accounts with banks in Pakistan. Beneficiaries have liberty to pick their transactions from any authorized agent against code provided to the remitter at the time of booking of remittance. The MTOs replenish their pre-funded account with the foreign exchange proceeds of the paying financial institution. The remittances received through MTOs also constitute to be “foreign exchange remitted from outside Pakistan through normal banking channel as stipulated in Section 111(4) of ITO.

The FTO accepted the plea of complainant and issued directions that the Commissioner IR consider Foreign Remittance over and above declared under amnesty i.e. Rs 25.474 million **in accordance with clarification issued by SBP.**

4. TOPIC OF THE MONTH

- RECHARACTERIZATION OF INCOME AND DEDUCTIONS

➤ PREAMBLE

This time we conclude our newsletter with a key concept within Income Tax that is “Recharacterization Of Income and Deductions”. The concept of “Substance over form” is a very basic accounting principle used in the preparation of financial statements if effectively applied then the financial statements will depict the overall financial reality of the entity (economic substance) rather than the legal form of transaction (form). For e.g. in International Financial Reporting Standards (IFRS) an application of this concept is provided in IAS 17 Lease (Now IFRS 16) in which

standard requires financial statements to consider the substance of lease arrangements when determining type of lease i.e. operating lease or fiancé lease for accounting purpose.

This concept is also equally applicable in Pakistani Income Tax laws whereby the charge of tax is based on substance rather than its form. This principle is derived through provisions of Section 109 of Income Tax Ordinance, 2001 under which an income or deduction could be “recharacterized” by the tax authority for purpose of taxation.

1. EXPLANATION OF PROVISIONS OF SECTION 109

- (a) The Commissioner may-
 - i. recharacterized a transaction that does not have substantial effect;
 - ii. disregard a transaction that does not have substantial economic effect;
 - iii. recharacterize a transaction where the form of the transaction does not reflect the substance; or
 - iv. disregard any entity or a corporate structure that does not have an economic or commercial substance or was created as part of the **tax avoidance scheme.**
- (b) “tax avoidance scheme” means any transaction where one of the main purposes in entering into the transaction is the avoidance or reduction of tax liability i.e. reduction, avoidance or deferral of tax or increase in tax refund **including the effect of tax treaty.**

The procedure commonly followed by Tax authorities is to bifurcate a transaction in which independent activities with non-tax objectives are combined with an unrelated item having only tax-avoidance objectives in order to disallow those tax-motivated benefits.

➤ Examples of substance over form may be:

- If a person brings contribution in a private company, it could be viewed as either as a loan/debt to the business with business claiming deduction of interest or as an investment/equity in the business. If in reality it is equity, but the business claim it was debt, then the tax authorities may recharacterized for tax purposes the debt as equity and disallow interest expense claimed as deduction.

- If a person disposes off a few immovable properties during a year and he declares capital gain on such disposals to be exempt due to the reason that holding period was more than the period for exemption specified under section 37 of ITO, the Commissioner may recharacterize such capital gain as other income or business income citing reason that the activity of disposing off multiple properties are in nature business/trade.
- If a private company claims expenses that are not incurred for business purposes for e.g. personal expenses of directors such as private foreign tours, or the company pays for expenses of loss making associated companies and claim such expenses from its own profits, the Commissioner may recharacterize such expenses as non-business expenses and may disallow them.

Conceptually there is nothing wrong with these provisions as the objective is to mitigate “tax avoidance schemes”. But tax avoidance is one’s legal right as held in a number of cases of courts. Tax avoidance through legitimate means (tax planning) is different from tax evasion. This provision has even declared “tax avoidance” as illegitimate and forbidden. Not only the taxpayers have been deprived of a lawful right, but the taxation officers have been given unqualified powers to declare whatever they may conceive as a “tax avoidance scheme”.

2. RELATION WITH AGREEMENTS FOR THE AVOIDANCE OF DOUBLE TAXATION AND PREVENTION OF FISCAL EVASION- SECTION 107

Before FA 2018, as per Section 107(2), provisions of any tax treaty entered between Government of Pakistan and Government of another country which is notified by the official gazette overrides provisions of the Ordinance including Section 109. Which means if transaction was conducted by non-resident which was Pakistan source income, but it was not reported on substance basis, but reported as per treaty provisions, Commissioner could not recharacterized it u/s 109.

Through FA 2018, the amendment was made in Section 107(2) whereby the aforesaid relief is now subject to anti

avoidance measures specified under section 109 of the Ordinance which can be taken by Commissioner. This however has chance to be misinterpreted by Department and may result in disregard of tax treaties by mere allegation of anti-avoidance scheme.

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