TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

TAX PAK

NEWSLETTER BY TOLA ASSOCIATES

NOVEMBER

2021

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ADDRESS

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

Email: connect@tolaassociates.com Ph# 35303294-6

Website: www.tolaassociates.com

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CONTRIBUTORS

Mr. Ashfaq Tola - FCA
Editor in Chief

Mr. Muhammad Furqan - ACA - Managing Editor

Mr. Muhammad Amayed Tola - Contributor

Mr. Talha Shahid - Contributor

Mr. Haseeb Naushad
Designer

EDITORIAL NOTE

Greetings everyone! Hope this monthly issue of TAXPAK finds you in good spirits and immaculate health! Although by now you already know, but nonetheless, I will still briefly state that the purpose of this newsletter is to provide a monthly update on the ongoing legal and administrative developments that take place within the field of taxation in Pakistan. Alhamdulillah, so far, we have been successful in our mission to educate about, and keep the public-at-large updated of, these developments on a monthly basis.

Moving on to the content of this letter, I would like to apprise the reader of what information you can expect in this document. This newsletter contains an elaboration of important notifications and circulars issued by the Federal Board of Revenue and its provincial counterparts. Moreover, notifications from the corporate regulatory body i.e. SECP are also discussed. Furthermore, keeping in mind the aforementioned stated purpose of this document, a recent judgment passed by Sindh High Court on Sections 170 and 221 of the Income Tax Ordinance, 2001 ("ITO") pertaining to "Refund" and "Rectification of mistakes". The said judgment contains a discussion regarding adjustment of WWF liability against the Income tax refunds.

Lastly, this newsletter is concluded with our Topic of the month which for this month happens to be "Fair Value Framework in GAAP and ITO, 2001". The said topic will be of interest to the people involved in the profession of Accounts and Taxation as well.

All our readers are requested to visit our website www.tolaassociates.com, or download our mobile application from the links mentioned below, in order to access previously published editions of this monthly issue along with other publications, and to stay updated of future notifications.

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

Lastly, we request our readers 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

1. NOTIFICATIONS/ CIRCULARS

1. EXTENSION IN DEADLINE STIPULATED UNDER SECTION 21(la) OF THE INCOME TAX ORDINANCE, 2001

The FBR has issued Circular No.9, dated November 01, 2021 whereby the deadline for digital payments to be made by the Corporate Sector has been extended upto November 30, 2021.

2. COMPLIANCE OF THE ORDER PASSED BY THE APPELLATE TRIBUNAL - IR (HQ) ISLAMABAD

The FBR has issued Letter No. C.No.3(3) PA&ATIR-Lit/2021, dated November 10, 2021 in which an Order of the ATIR, dated November 01, 2021 has been cited. In the said Order, the ATIR has shown concern for causing delay by the appellate authorities in the disposal of a huge number of cases and in sitting tight over stay applications filed by the taxpayers, which has compelled the taxpayers to initiate filing writ petitions or appeals to get orders for extension in their stay. In this regard FBR directed its officers that prompt disposal of stay applications may kindly be ensured in pursuance of this Order.

3. CHANGE IN THE RATE OF SALES TAX ON PETROLEUM PRODUCTS

The FBR has issued SRO No. 1450(I)/2021, dated 11th November 2021 for the change of rate of sales taxes for petroleum products w.e.f. 5th November 2021. They have amended the table that was present in SRO No. 57(I)/2016, dated 29th January 2016, and substituted it with the following table:

S.No	Description	PCT Heading	Current Rate	Previous Rate
1	MS (Petrol)	2710.1210	1.43% ad valorem	6.84% ad valorem
2	High Speed Diesel Oil	2710.1931	6.75% ad valorem	10.32% ad valorem
3	Kerosene	2710.1911	6.70% ad valorem	6.70% ad valorem
4	Light Diesel Oil	2710.1921	0.20% ad valorem	0.20% ad valorem

4. CHANGE IN VALUE OF SUPPLY OF STEEL PRODUCTS

Pursuant to the powers provided in second proviso to Section 2(46) of the Sales Tax Act, 1990 ("STA") the FBR has revised Minimum Value of Supply of Steel Products by amending its previously issued SRO bearing No. 985(I)/2021 that was dated 4th August 2021. This amendment has been done through SRO No. 1465(I)/2021 dated 15th November 2021, through which the following table has been added in place of the table present in the previous table:

S.No	Goods	Current Value	Previous Value (SRO 985 dated 4th August 2021
1	Steel bars and other long profiles	Rs 153,000 Per Metric Ton	Rs 140,000 Per Metric Ton
2	Steel Billets	Rs 131,000 Per Metric Ton	Rs 125,000 Per Metric Ton
3	Steel ingots/bala	Rs 126,000 Per Metric Ton	Rs 120,000 Per Metric Ton
4	Ship Plates	Rs 126,000 Per Metric Ton	Rs 120,000 Per Metric Ton
5	Other re-rollable iron and steel scrap	Rs 119,000 per metric Ton	Rs 118,000 Per Metric Ton

It may be noted that in case the value of supply of the goods specified in this Notification is higher than the values fixed herein, the value of goods shall be the value at which the supply is made.

5. EXEMPTION OF SALES TAX ON IMPORT OF EDIBLE FRUITS FROM AFGHANISTAN

The FBR, vide SRO 1501(I)/2021, dated 22nd November 2021, has exempted import of edible fruits from Afghanistan from sales tax, except for apples (PCT 0808.1000) w.e.f. 15th September 2021.

6. VALUE OF SUPPLY TO CNG CONSUMERS

As per the powers provided in second proviso to Section 2(46) of the STA,the FBR vide SRO 1464(I)/2021, dated

15th November 2021, has revised the Minimum Value of Supply for charging of Sales Tax. The revised values are be as follows:

S.No	Description	Current Value	Previous Value (SRO 690 dated 29th June 2019
1	For Region-I	Rs 128.11 per Kg	Rs 69.57 per Kg
2	For Region-II	Rs 134.57 per Kg	Rs 74.04 per Kg

7. SALES TAX ON THE SERVICES PROVIDED IN THE MATTER OF MANUFACTURING OR PROCESSING FOR OTHERS ON TOLL BASIS (TARIFF HEADING 9830.0000)- SRB CLARIFICATION

The SRB has issued a Letter bearing No. SRB/TP/22/2021/35436 ("recent letter"), dated 2nd November 2021, whereby it is noted that a Letter C.No. 1(106) STM/2017/180608-R, dated 28th October 2021, signed by Second Secretary(ST-L&P), FBR has gone viral on social and print media. The letter issued by the SRB highlights that the FBR did not endorse the said letter that had previously gone viral on social and print media, to any of the Provincial Revenue Authorities (PRAs), including the SRB. It is also pertinent to note that the services provided in relation to the manufacturing for others on toll basis are taxable under:

a. Tariff heading 9830.0000 of Second Schedule of Sindh Sales Tax on Services Act 2011

b. Tariff heading 9868.0000 read with Sr.No. 37 of Punjab Sales Tax On Services Act 2012

c. Tariff Heading 9840.000 read with S.No. 12 of the Second Schedule to the KP Finance Act 2013

d. Tariff Heading 9816.000 of the Second Schedule to the Balochistan Sales Tax on Services Act 2015

As per the recent letter, none of the Provincial Authorities have issued any such exemption notification to justify FBR's stance that "Provinces shall not collect tax on toll manufacturing which will rest with FBR". Moreover, as per the same letter, The Provincial Authorities during their meeting in Islamabad on 30th October 2021 expressed their concern and dismay on the FBR letter dated 28th October 2021 which has not been issued in line with the jointly concurred letter of the Provinces bearing No. SRB/TP/22/2021/19109, dated 18th September 2021 and its enclosures issued by SRB addressed to the Chairman FBR.

Furthermore, the recent letter further goes onto state that the in NTC meeting held on 16.09.2021, it was agreed that Provinces shall not levy/collect sales tax on toll manufacturing services and the Federation shall, likewise, not levy/collect sales tax on the food /beverages served in hotels & restaurants located in Provinces. In other words, the decision had an element of quid pro quo. However, as per the recent letter, the FBR's letter does not mention the agreed decision about the non-levy of federal sales tax on the food/beverages served in Provincial Jurisdictions. The Provincial Authorities in the aforesaid meeting of 30th October 2021 also resolved that SRB may communicate to FBR the joint views and concerns of the PRAs and request FBR to withdraw its aforesaid letter immediately under intimation to all concerned.

Nevertheless, as per the recent letter, the Provincial Authorities also resolved that the Provinces shall continue to levy and collect the sales tax on the services provided in the matters of manufacturing for others on toll basis in accordance with respective Provincial laws and rules until the decision about the non-levy of federal sales tax on the food/beverages served in hotels & restaurants located in Provinces is simultaneously and explicitly endorsed by FBR.

2. CORPORATE NOTIFICATIONS / CIRCULARS

1. AMENDMENTS TO THE ASSOCIATIONS WITH CHARITABLE AND NOT FOR PROFIT OBJECTS REGULATIONS, 2018

The SECP has, through SRO 1416, dated 2nd November 2021, made amendments to the Associations with Charitable and Not for Profit Objects Regulations, 2018.

The amendments are made in regulation 10 sub-regulation 2 pertaining to **"Solvency and financial soundness".** The said amendments were placed on their website on 8th November 2021.

The amendments can be further accessed by clicking on the link given below.
Amendments to the Associations with Charitable and Not For Profit Objects Regulations, 2018.

2. AMENDMENT IN THE COMPANIES (FURTHER ISSUE OF SHARES) REGULATIONS, 2020.

The SECP, through SRO 1461, dated 10th November 2021, has made amendments in the Companies (Further Issue of Shares) Regulations, 2020.

The amendments have been made in the Regulation 6 of the Companies (Further Issue of Shares) Regulations, 2020. Moreover, a Chapter VIA pertaining to **"Registration and Valuation"** has been added to the said Regulations. This chapter consists of two sections; (a) Section 8A pertaining to **"Registered Valuers";** and (b) Section 8B **"Qualification and Experience for Valuation".**

The aforesaid amendments were placed on their website on 15th November 2021. The amendments can be further accessed by clicking on the link given below.
Amendment in the Companies (Further Issue of Shares) Regulations, 2020.

3. AMENDMENTS IN THE LISTED COMPANIES (BUY BACK OF SHARES) REGULATIONS, 2019.

The SECP, vide SRO 1494, dated 16th November 2021, has made amendments in the Listed Companies (Buy Back of Shares) Regulations, 2019.

The amendments made incorporate the provisions relating to **"Special Purpose Acquisition Company (SPAC)**" in the aforementioned Regulations. The said amendments were placed on their website on 22nd November 2021.

3. NOTICES UNDER SECTION 221 CANNOT BE INVOKED TO QUESTION REFUNDS – SINDH HIGH COURT

➢ PREAMBLE:

This segment pertains to the case titled **"OBS Pakistan (Pvt.) Ltd versus Federation of Pakistan & Others"** which consisted of 72 other petitioners as well. This judgment, passed by the Sindh High Court ("SHC") revolved around a Circular issued by the FBR pertaining to the Workers Welfare Fund Liability and its adjustment against outstanding income tax refunds of the taxpayers. A more detailed overview is given herein below.

FACTS OF THE CASE AND THE LEGAL PROVISIONS RELATING THERETO

As per a Circular released/published by the FBR bearing No.4 (33)-Rev.Bud./99, dated 17.02.2000, the taxpayers had been allowed to adjust any WWF liability against the outstanding tax refund/credit on the basis that it is earlier considered tax. The Supreme Court of Pakistan, in Workers Welfare Funds v. East Pakistan Chrome Tannery & others, reported as PLD 2017 SC 28 held that payment to WWF is not a tax but instead it is a fee. Accordingly, the FBR issued Circular No. C.No.1 (10)ST-LP&E/2020/66012.R dated 25th May, 2021 stating that the WWF is not a tax, and therefore, under Section 170(3) of the Income Tax Ordinance 2001 ("ITO 2001") the taxpayer's WWF liability could not be adjusted against unpaid outstanding income tax refunds. Officers were thus directed that WWF may not be adjusted against the tax liability. The tax officers issued notices under Section 221(2) of the ITO 2001, to rectify the taxpayer's returns which are a deemed assessment order u/s 120 of the ITO 2001, in which taxpayers have made adjustments of the WWF liability with refunds of prior years. In some cases, the deemed assessment was also amended u/s 122 for previous periods 2014 to 2016.

As per Section 221 of the ITO 'Rectification of Mistakes', the Commissioner, the Commissioner (Appeals) or the Appellate Tribunal may amend any order passed by him to rectify any mistake apparent from the record on his or its own motion or any mistake brought to his or its notice by a taxpayer or, in the case of the Commissioner (Appeals) or the Appellate Tribunal, the Commissioner.

Feeling aggrieved with the notices issued u/s 221 of the ITO 2001, the taxpayers preferred an appeal to the Sindh High Court on the following grounds:

1. GROUNDS OF TAXPAYERS

1.1 THE SCOPE OF SECTION 221 IS LIMITED

The scope of Section 221, 'rectification of mistakes', is limited and is only applicable when the mistake in the Order is apparent on the face of record, such as a clerical or calculation error, as these are the mistakes which do not

require any material efforts. In cases where legal issues and interpretations are involved, Section 221 of the ITO 2001 cannot be invoked.

1.2 THE FBR CIRCULAR DATED 25.05.2021 IS ULTRAVIRES THE ITO

The Circular issued by the FBR is ultravires to the ITO, as the Supreme Court of Pakistan in the Workers Welfare case decided that the payment to WWF is not a tax, however it was for the purposes of Article 73 of the Constitution of Islamic Republic of Pakistan, 1973 and consequently held that Ordinance 1971 cannot be amended through Money Bill. However, the counsels for the petitioners emphasized that this does not mean that WWF cannot be deemed to be a tax for the limited purpose of collection and paying WWF. It only means that amendment cannot be carried out through a Money Bill.

2. SHC OBSERVATIONS AND CONCLUSION

2.1 NOTICES ISSUES UNDER SECTION 221

The SHC observed that in this case there is no such mistake disclosed on the face of record. Where an officer investigates into the matter, reassesses the evidence or takes into consideration additional evidence and on that basis interprets the provision of law and forms an opinion different from the order, it will not be regarded as rectification of the order. In this matter officer was required to answer following questions, inter-alia, such as; (A) whether the Circular dated 25.05.2021 has retrospective effect?; (B) Could the original assessment order be amended under section 221(1) of Ordinance 2001?; (C) Can the WWF adjustment be reversed without making a refund allegedly due to the taxpayer as it is only against a refund claim which came for consideration for the adjustment of WWF? The answer to these questions require interpretation of law. This exercise cannot be carried out under section 221 of the ITO 2001.

Therefore, the SHC held that notices issued under Section 221 of the ITOclaiming WWF prior to the effect of impugned Circular dated 25.05.2021 are illegal and unlawful for the purposes of Section 221 of the ITO 2001. Moreover, deemed assessment, other than clerical or calculation error on face of record, could be subjected to amendment under section 122 of Ordinance 2001 within the available time limitation.

2.2 VALIDITY OF FBR CIRCULAR DATED 25.05.2021

The process of refund is governed by Section 170 of Ordinance 2001 which provides a complete mechanism. As per Section 170(3) if the Commissioner is satisfied that the **tax** has been overpaid, he shall

a. apply the excess in reduction of any other tax due from the tax payer under the Ordinance
b. apply the balance of the excess in reduction of any outstanding liability of the tax payer to pay other taxes and
c. for the remainder to the tax payer.

The refund of any excess tax paid could not become due on mere filing of return disclosing such amount of refund or in the alternate on just initiating proceedings under Section 170 of Ordinance 2001. The SHC held that the procedure of adjustment was only facilitated by the FBR when Circular 4 was issued on 17.02.2000.

AS per the Circular 4, since collection of WWF is also the responsibility of the FBR, therefore, refund of income tax be adjusted against demand of WWF. After the Supreme Court Order in the aforesaid case, the WWF is not considered as tax, therefore, it cannot be under the ambit of Section 170 which deals only with tax. The SHC held, that Section 170 leaves no room for adjustment of WWF, therefore Circular dated 25.05.2021 is valid but to be applied prospectively and adjustments made earlier under Circular 4 dated 17.02.2000 cannot be questioned under Section 221.

4. TOPIC OF THE MONTH

FAIR VALUE FRAMEWORK IN GAAP AND THE INCOME TAX ORDINANCE, 2001

➢ PREAMBLE

In the end, we conclude our newsletter with our very own topic of the month, in which we will discuss issues related to the valuation of assets. The ongoing discussion on lack of documentation in economy, vast circulation of untaxed money and assets beyond may imply that transactions, exchanges and book entries of assets and goods are not at

a fair value. This might partly be due to tax planning purposes, but another crucial reason behind this is the amount of complexity and efforts needed to arrive at fair value which we will see both in Generally Accepted Accounting Principles (GAAP) as applicable in Pakistan, and in the Income Tax Ordinance 2001 ("ITO"). Before going through applicable frameworks, we will highlight the real concept of value in economic terms.

1. REAL CONCEPT OF 'VALUE'

1.1 COST PRODCUTION MODEL

The purpose of discussion of concept of 'value' is to explain the exchange value of goods, services, assets and liabilities. The old way of thinking to determine the value or price of goods or assets, is use of cost theory or labor theory of value, whereby, the value or price is equal to its total cost of production or as per labour theory goods price is equal to the quantity of labour required to produce it. An example is the system used in Pakistan to determine the prices of petroleum products. The said price is arrived at through adding components of cost such as Ex-Refinery price, In-land Freight Equalization Margin (IFEM), Distributor Margin, Dealer Commission, Petroleum Levy, Sales Tax etc. If this concept is accepted as true, then considering that the MS Petrol prices fixed by the Government of Pakistan ("GoP") in June 2021 were PKR 110.69 per liter, whereas, the prices of HOBC (which is not regulated by GoP, and is considered a more refined form than MS Petrol), having more cost of production, was PKR 142 during mid of June 2021, the difference of PKR 30 would be considered as an additional cost of HOBC over MS Petrol. If this concept is accepted as true, then this difference must remain same whenever the price of MS Petrol changes. However, for reasons discussed in the forthcoming paragraph, this is not true.

1.2 SUBJECTIVE MODEL

Now it is widely accepted that the value is subjective, and it is in the mind of consumer. The value of goods or service is what the buyer thinks in his mind i.e. value is not derived from the cost of production. Something of value to one person may not be valuable to his neighbor. The producer, or the Government, cannot force the consumer to value something highly by saying that it costs a lot to produce, as the consumer does not care what something costs to produce. The consumer only cares about how much the product or asset will benefit him. Now continuing with the above example, the current prices of MS Petrol is approximately PKR 146 per liter, and according to the cost of production as a driver of value, the HOBC price should have been Rs 176/liter. But this is not the case as current prices are in range of PKR 149 to PKR 155/liter. In other words, the current subjective value the consumer places on HOBC is PKR 149 and Oil Marketing Companies have no option to offer this price otherwise the consumer will switch to the next available alternative. Therefore, even with such a basic commodity such as petrol the concept of subjectivity of value holds true, which implies that value is subjective with each individual and cannot be compared even between 2 individuals.

2. FAIR VALUATION MODELS IN GAAP USING THREE LEVEL HIERANCHY OF INPUTS

IFRS 13 (Fair Value Measurement) provides detailed guidance on how the fair value of assets and liabilities should be determined. The IFRS 13 aims to define fair value and set out a single IFRS a framework for measuring fair value. Moreover, the IFRS 13 defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an ordinarily transaction between market participants at the measurement date."

Fair value is a market-based measurement, not an entity-specific measurement. It focuses on assets and liabilities and on exit (selling) price. It also takes into account market conditions at the measurement date.

The IFRS 13 states that valuation techniques must be those which are appropriate and for which sufficient data are available. Entities should maximize the use of relevant **observable inputs** and minimize the use of **unobservable inputs.** (Source: IFRS 13:61 and IFRS 13:67)
In other words, the standard requires that the following aspects are considered in measuring the fair value:

a. The asset or liability being measured;

b. The principal market (i.e. that where most of the activity takes place). In case where there is no principal market, the most advantageous market (i.e. the market in which the best price could be

achieved) in which an orderly transaction would take place for the asset or liability;

c. The highest and the best use of the asset or liability;

d. Assumptions that market participants would use when pricing the asset or liability.

The standard establishes a 3-level hierarchy for the inputs that valuation techniques used to measure fair value:

- **Level 1:** Quoted prices in active markets for identical assets or liabilities
- **Level 2:** Inputs other than quoted prices that are observable directly or indirectly for the assets or liabilities.
- **Level 3:** Unobservable inputs for the assets or liability.

Example of the Valuation of Immovable Property

Company A has acquired land in a business acquisition transaction. The Land is currently developed for industrial use as site for a factory. The current use of land is presumed to be its highest and best use, unless market or other factors suggest a different use. The sites nearby have recently been developed for residential use as sites for high-rise apartment buildings. Based on that development, Company A determines that land currently used as a site for factory could be developed as a site for residential use as a high rise apartment building, because market participants would take into account the potential to develop the site for residential use when pricing the land. The highest and the best use of land would be determined by comparing both

a. The value of land as currently developed for industrial use; and

b. The value of land as vacant site for residential use, taking into account the costs of demolishing the factory and other costs etc.

The highest and the best use of the land would be determined on the basis of higher of those values. (Source IFRS 13: IE7)

The Valuation techniques that use the above inputs are the following:

a. **Income approach:** Valuation techniques that convert future amounts (e.g. cashflows or income and expenses) to a single current/discounted amount. In other cases, the valuation of a strategic business unit can be done using a financial forecast (e.g. of cash flows or profit or loss) developed using the company's own data **(Level 3 Input).**

b. Market approach: A valuation technique that uses prices and other relevant information generated by market transactions involving identical assets, liabilities or group of assets. For example, the valuation of a strategic business unit can be done using Valuation multiple e.g multiple of earnings or revenue derived from observable market data **(Level 2 Input)** e.g. from prices in observed transactions involving comparable business. The valuation of the building using Price per square meter derived from observable market data **(Level 2 Input)** e.g prices in observed transaction involving same buildings in the same location.

c. Cost Approach/current replacement cost: A valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset.

3. MODEL OF FAIR VALUATION IN SECTION 68 OF INCOME TAX ORDINANCE, 2001

3.1 GENERAL RULES:

The fair market value of any property or rent, asset, service, benefit or perquisite at a particular time shall be the price which the property or rent, asset, service, benefit or perquisite would ordinarily fetch on sale or supply in the open market at that time.

The fair market value of any property or rent, asset, service, benefit or perquisite shall be determined without regard to any restriction on transfer or to the fact that it is not otherwise convertible to cash.

In other words, the prices are market based not entity specific and it considers market conditions at the date of valuation.

3.2 DETERMINATION OF FAIR MARKET VALUE OF ITEMS OTHER THAN IMMOVABLE PROPERTY

Where the price of items other than the price of immovable property is not ordinarily ascertainable i.e. no active market exists, such price may be determined by the Commissioner.

3.3 DETERMINATION OF FAIR MARKET VALUE OF IMMOVABLE PROPERTY

Prior to the Finance Act 2016 ("FA 2016"), the fair market value for the purpose of probing the source of investment in the acquisition of immovable property was determined by the Commissioner. However, under the Income Tax Rules, the fair market value was to be determined as value fixed for the purpose of collecting stamp duty by Provincial Authorities and it was binding upon the Commissioner Inland Revenue. Through the FA 2016, read with Circular 7/2016 dated 27.07.2016, the powers of the Commissioner had been withdrawn, and valuation now had to be made by a panel of approved valuers of the SBP. Similarly, the binding nature of the value determined by Provincial Revenue Authorities for the purpose of collecting stamp duty was also withdrawn.

Subsequently, through Income Tax (Amendment) Ordinance, 2016 it has been provided that instead of the valuation made by the approved valuers of the SBP, the FBR will notify fair market value tables itself for the purpose of the calculation of the Capital gains u/s 37(1A) of the ITO, Collection of withholding tax under Sections 236C and 236K of the ITO.

Where the fair market value of any immovable property of an area or areas has not been determined by the FBR, the fair market value of such immovable property shall be deemed to be the value fixed by the District Officer (Revenue) or provincial or any other authority authorized in this behalf for the purposes of stamp duty. In this regard, the FBR has issued various SROs from time to time for all major cities.

However, for the purpose of calculation of Capital Gain, the Fair Market Value shall not be less than consideration received for the disposal of the Immovable property.

CONCLUSION

As we can see that tax officials have been given power to determine fair value for assets other than immovable property, and a simplified guideline is also given in GAAP. However, in practice, the proper procedures are not usually followed and the assigning of arbitrary values is a common practice which should not be the case.

DISCLAIMER

TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

OFFICES IN PAKISTAN

Karachi Address:

Office no. 408, 4th Floor, CTC Building, Clifton Block-8, Karachi

Tel #: +92 21 3530 3293-6

Islambad Address:

144, 1st Floor, Street No.82

Sector E-11 / 2 FECHS

Islamabad 44000,

Tel #: +92 51-835 1551

Lahore Address:

202-E, 2nd Floor, Sadiq Plaza 69-The Mall Road, Lahore

Tel #: +92 42 3628 0403