TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

TAX PAK

NEWSLETTER BY TOLA ASSOCIATES

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

Email: connect@tolaassociates.com

Website: www.tolaassociates.com

Ph# 35303294-6

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CONTRIBUTORS

Mr. Ashfaq Tola - FCA
Editor in Chief

Mr. Muhammad Furqan - ACA - Managing Editor

Mr. Muhammad Amayed Tola - Contributor

Ms. Baria Khushnuma Hashmi - Contributor

Mr. Haseeb Naushad
Designer

EDITORIAL NOTE

Asalam-o-alaikum everyone and Eid Mubarak! Hope this monthly issue of TAXPAK finds you in good spirits and immaculate health! I welocme you to another edition of TAXPAK,
our monthy publication, the purpose of which is to provide the monthy update on the ongoing legal and administrative development that take place within the world of tax in Pakistan. Alhumdulillah, so far, we have been successful in our mission to educate about, developments on a monthly basis.

Moving on to the contents of this letter, I would like to apprise the readers 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 Provincial Revenue Authorities / Boards. Moreover, notifications from the corporate regulatory body i.e. SECP are also discussed briefly. Furthermore, keeping in mind the aforementioned stated purpose of this document, we usually discuss a (relatively) recent judgment passed by the courts of law. In this monthly edition, we have opted to discuss a judgment passed by the Lahore High Court discussing the fact that FBR cannot seek records time barred u/s 174 but it can conduct proceedings and pass speaking order u/s161.

Lastly, this newsletter is concluded with our Topic of the month that is titled "TAXATION OF PERMANENT ESTABLISHMENT OF A NON-RESIDENT".

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. EXPLANATIONS OF IMPORTANT AMENDMENTS INTRODUCED IN THE INCOME TAX ORDINANCE 2001 THROUGH THE INCOME TAX (AMENDMENT) ORDINANCE 2022

The FBR has issued an explanatory Circular bearing No. C.No. 4(5)IT-Budget/2022-78512-R, dated 7th April 2022, through which it has explained 3 amendments made through the captioned Amendment Ordinance. Our comments on same were issued earlier which may be accessed through link https://tolaassociates.com/wp-content/uploads/2022/03/Comments-on-Income-Tax-Amendment-Ordinance-2022.pdf The explanations are as under:

A. Explanation of Section 59C of the Income Tax Ordinance 2001

The captioned Section has been inserted in the Income Tax Ordinance 2001 ("ITO") through the captioned Income Tax (Amendment) Ordinance 2022 ("Amendment Ordinance"). The main aim of this Section seems to be the revival of 'Sick Industrial Unit'. The modus operandi thereof includes the 'acquiring company' (which acquires a 'sick industrial unit' also termed as the 'acquired company') to be able to set-off losses for the latest tax year and brought forward assessed business losses, excluding capital loss, of the acquired company, against its own income up to Tax Year 2026. The said Circular goes on to further explain that this benefit shall not be available to any scheme of amalgamation or merger. Furthermore, the circular further states that the set-off of losses will be available upto Tax Year 2026 to the acquiring company in proportion to the share capital acquired by it. However, beyond Tax Year 2026, i.e Tax Year 2027 and onwards, the acquiring company shall not be able to adjust the losses of the acquired company against its (acquiring company's) own income. The acquired company (sick industrial unit) shall, however, be able to set-off its losses against its own income in accordance with Section 57 of the ITO.

Nevertheless, should the sick industrial unit not be revived by Tax Year 2027, the income set-off due to the aforementioned adjustment of losses, shall have to be offered by the acquiring company for tax for Tax Year 2027, thereby reversing the benefit that was obtained. The revival of the sick industrial unit has to be certified by the Engineering Development Board and the acquired company must file the certificate along with its Return of Income for Tax Year 2026.

B. Section 65H

Section 65H has been inserted in the ITO through the Amendment Ordinance. This section pertains to investment through foreign exchange remittances in a Company incorporated on or after 1st March 2022 ("incorporation date") to establish an industrial undertaking. The modus operandi thereof is that Foreign Remittance must be remitted through normal banking channel into a dedicated rupee account opened by a company incorporated on the incorporation date. The minimum amount that must be remitted is PKR 50 million, and the procedure to remit the same shall be laid down by the State Bank of Pakistan. However, a non-resident Pakistani can only avail a benefit under this Section if he is having a non-resident status for 5 years.

Moreover, the circular further goes onto state that a resident Pakistani can only remit foreign exchange out of his declared assets in terms of Section 116 or Section 116A.

The benefit this Section provides is that a 100% tax credit will be available equal to the amount invested as equity from foreign exchange remitted in terms of the above. This tax credit can be fully adjusted in the year the industrial undertaking commences its commercial production, which in any case must be by 30th June 2024, i.e end of Tax Year 2024. In case the tax credit cannot be fully adjusted in the commencing year, the same can be carried forward for upto a maximum of 5 years.

However, this scheme will not be applicable to a company or an industrial undertaking established by splitting up or reconstitution of a company or an industrial undertaking already in existence or by transfer of machinery or plant from an industrial

undertaking established at any time before 1st March, 2022.

C. Section 100F

Immunity from probe under Section 111 of the ITO has been granted on equity investment made (a minimum of PKR 50 million) by **eligible persons** in a new company formed for establishing an industrial undertaking or to an existing company being an industrial undertaking (for investment in expansion and modernization) after paying an **amount of tax equal to five percent on such investment** and upon fulfilling other conditions as mentioned in this section. The amount of undeclared funds for investment has to be **credited into a dedicated bank account of such company before due date of filing of statement i.e. 30th September, 2022** and can only be used either for purchase or import of plant and machinery including IT hardware through a letter of credit or software and IT services, or for construction of building and structure in case of new industrial undertaking and for construction of only manufacturing premises in case of existing unit.

It may be noted that the tax paid under this section is not refundable or adjustable against any other tax liability of the company and the declarant will be entitled to incorporate the amount of declared funds in his wealth statement, financial statements or books of accounts.

The industrial undertaking will have to commence its commercial production by 30th June 2024, and the same will be certified by the Engineering Development Board through a certificate which is required to be furnished by the company with its return of income for Tax Year 2024.

Where there has been misrepresentation or suppression of facts, the statement filed under subsection (1) will be treated as void ab-initio and all the provisions of the ITO will apply accordingly. The circular further states that this Scheme is not an amnesty scheme, rather a conditional tax concession.

2. CONSTITUTION OF COMMITTEE FOR RESOLUTION OF ISSUES OF PHARMACEUTICAL COMPANIES

The FBR, has through an Order bearing No. C.No.1 (20) ST-L&P/2022/87440-R, dated 20th April 2022, has constituted an "Issues Resolution Committee" headed by the Chief Commissioner LTO- Karachi. The said Order contains the list of the Members of the Committee. Moreover, the TORs are as follows:

(A) Review the nature of grievance/issue, possible solution and take immediate action for its resolution;

(B) Follow up with concerned field formations till issue is resolved;

(C) Maintain complete record of complaints/issues, mechanism adopted for resolution and post resolution action required, if any; and

(D) Share data with Board on monthly basis indicating issues received, issues resolved and issues pending for resolution and reasons for pendency.

3. AMENDMENT IN THE ITR

The FBR has, through, SRO 549(I)/2022, dated 23rd April 2022, issued a draft amendment to Rule 74(2) of the ITR. The draft amendment is published and the FBR has invited any potential objections to be raised within 15 days of the publishing of the said draft amendment. The draft amendment intends to substitute sub rule (2) of Rule 74 as under:

Current Provisions	Proposed Provisions
"(2) Where a person has notified the Commissioner in writing of an electronic address for service of documents under the Ordinance or rules, a document required to be served on the person by the Commissioner of Chief Commissioner shall be considered sufficiently served if sent to that address."	"(2) Where a person has provided an electronic address, the document required to be served on the person shall be considered sufficiently served if sent to that address."

The above proposed amendment will treat any electronic address, whether or not provided for the specific purpose of communication, as the valid address for service of any document.

4. AMENDMENTS IN SRO 499(I)/2013 DATED 12TH JUNE 2013

The FBR has issued SRO 497(I)/2022 dated 6th April 2022, through which it has made corrective amendments to the SRO 499(I)/2013 and has omitted unnecessary reference to the term 'sales tax' and 'Sales Tax Act, 1990'.

5. ADJUSTMENT OF SALES RETURN THROUGH CREDIT NOTE AGAINST UN-REGISTERED SALES

The FBR, has through a Letter bearing No. C.No. 5(17) ST-L&P/CN/2021/81632-R, dated 11th April 2022, has stated that adjustment through Credit Notes against sales returns from unregistered buyers may be allowed through automated system to the taxpayers registered as Manufacturer-cum-Retailers and Retailers upto maximum limit of 10% of the total unregistered sales declared during the month. The facility is being enabled subject to the condition that no negative sales values shall be allowed through automated system.

6. SRO 489(I)/2022

The FBR has through SRO 489(I)/2022, has revised minimum value of supply of locally produced steel goods as under:

Steel Goods	Previous Values	Revised Values
	Rs. Per metric ton	
Steel bars and other long profiles	153,000	164,037
Steel Billets	131,000	133,813
Steel Ingots/bala	126,000	126,000
Ship plates	126,000	129,584
Other re-rollable iron and steel scrap	119,000	125,688

It is also clarified that in case actual values are higher than the specified values, sales tax shall be charged at actual values.

7. AMENDMENTS IN SRO 345(I)/2022 DATED 2ND MARCH 2022.

Through SRO 548(I)/2022 dated 23rd April 2022, the FBR has made amended the captioned SRO to correct the typo errors in the captioned notifications.

8. SRO 500(1)/2022

The FBR has vide the captioned SRO made amendments to the form STR-7 (Sales Tax and Federal excise Return) in the Sales Tax Rules 2006 ("STR").

9. SRO 541(I)/2022

The FBR has through the captioned SRO, amended the rule 150ZF in Chapter XIV-B, rule with respect to electronic monitoring, tracking and tracing, and licensing have also been made applicable on 'steel sector'.

10. IMPLEMENTATION OF TRACK & TRACE SYSTEM UNDER SRO 250/2019 (26.02.2019) FERTILIZER BAGS:

The FBR vide CNo.2(5)T&Ts/Fertilizer/2021-111126-R and Sales Tax General Order No. 15 of 2021 dated 26th April 2021, has directed that no Fertilizer bags can be removed from the production site, factory, premises or manufacturing plant/import station without bearing tax stamps/Unique Identification Markings (UIMs) with effect from 1st July 2022. UIMs can be obtained from FBR's Licensee M/s AJCL/MITAS/ Authentix Consortium.

2. CORPORATE NOTIFICATIONS / CIRCULARS

1. AMENDEMENTS IN PUBLIC OFFERINGS REGULATED SECURITES ACTIVITIES REGULATIONS 2017:

The SECP has issued an amendment to the Public Offerings Regulated Securities Activities Regulations 2017, vide SRO 537(I)/2022, dated 19th April 2022. For further reading please follow link: https://www.secp.gov.pk/laws/notifications/.

2. AMENDMENTS TO THE COMPANIES INCORPORATION REGULATIONS 2017:

The SECP has issued an amendment in the Companies Incorporation Regulations 2017 vide SRO 530(I)/2022,

dated 18th April 2022 and has amended sub-regulation (3) of the Regulation 15.

3. ROLE OF OFFICERS OF LISTED COMPANY REGARDGING GENERAL MEETINGS

The SECP in its 17-page guidelines for the Role of Officers of Listed Companies regarding General Meetings has incorporated the brief responsibilities pertinent to the Company's Secretary, Chairman, Chief Executive Officer, and Share Registrar. It has also provided checklists for the above-mentioned officers to ensure relevant laws had been complied with in the proceedings of the General Meetings.

4. FREQUENTLY ASKED QUESTIONS (FAQS) ON ANTI MONEY LAUNDERING AND COUNTERING OF TERRORISM & PROLIFERATION FINANCING (AML/CT/PF)- 5TH EDITION

The SECP in its 5th Edition of the FAQs on Anti-money Laundering and Countering of Terrorism and Proliferation Financing (AML/CT/PF) explained in brief the purpose of SECP's regulated persons (RPs) and SECP expectations for the Anti-money Laundering (AML) and sanctions compliance. For further reading: https://www.secp.gov.pk/laws/guidelines/ .

5. DRAFT AMENDMENTS IN THE MODARABA REGULATIONS, 2021:

The SECP on 15th April 2022, vide its SRO 539(I)/2022 issued the draft amendment in the Modaraba Regulations 2021, which can be accessed by visiting https://www.secp.gov.pk/laws/regulations/ for further reading.

6. AMENDMENTS IN THE COMPANIES (ASSET BACKED SECURITIZATION) RULES, 1999:

The SECP issued amendment in the Companies (Asset Backed Securitization) Rules, 1999 on 14th April 2022, vide its SRO 520(I)/2022 which can be accessed by https://www.secp.gov.pk/laws/rules/.

3. FBR CANNOT SEEK RECORDS TIME BARREDU/S 174 YET IT CAN CONDUCT PROCEEDINGS AND PASS SPEAKING ORDER U/S 161 - LHC

1. FACTS OF THE CASE

Against the judgement dated 13th October 2021 of Lahore High Court, Lahore, passed **in Writ Petition No. 21602 of 2021,** Pepsi Cola International (Private) Limited ("Petitioner") filed a petition before the Honorable Lahore High Court ("LHC") reported as **2022 PTD 51** against the Federation of Pakistan ("Respondent").

The controversy involved in the case was the interpretation of Section 161 and Section 174 of the Income Tax Ordinance 2001 ("ITO") with respect to the maintenance of accounts and documents for a period of six years and request for documentary evidence by the Commissioner.

The question put before the LHC was as under:

Quote
In the present case the taxpayer impugned notices required taxpayer to provide record in respect of transactions pertaining to period which fell outside the time-period required for maintenance of such record under S.174 of the Income Tax Ordinance, 2001
Unquote

2. ARGUMENTS BY THE RESPONDENT

2.1 THAT THE PETITION IS NOT MAINTAINABLE AS PROCEEDINGS U/S 174(3) DO NOT BAR PROCEEDINGS U/S 161

Learned counsel for the Respondents argued that the provisions of Section 174(3) of the ITO do not bar proceeding initiated under Section 161 of the Ordinance. They further argued that failure to pay tax can be investigated by the department at any given time and that the limitation period to maintain the record is for the purpose of assessment and any other proceedings under Section 161 of the ITO can be continued. They placed reliance on the case **2016 PTD 2074** and D. G. Khan Cement Co. Ltd through Chief Financial Officer and others v. Federal Board of Revenue through Chairman and 5 other **(2020 PTD 2111).**

3. ARGUMENTS BY THE PETITIONER

3.1 THAT THE PETITIONER IS NOT REQUIRED TO PRODUCE ACCOUNTS OR DOCUMENTS AFTER SIX YEARS

Learned counsel of the Petitioner argued that in terms of Section 174(3) of the ITO, the taxpayer is required

to maintain accounts and document for period of six years after the end of the tax year and such had lapsed, therefore, the Petitioner is not required to maintain any accounts or documents which were being asked by the Respondents. Reliance was made on Maple Leaf Cement Factory Ltd v. The Federal Board of Revenue and others **(2016 PTD 20174)** and Habib Bank Ltd. V. The Federation of Pakistan through Secretary, Revenue Division and 5 others **(2013 PTS 1659).**

4. LHC FINDINGS

4.1 THAT IF ANY ONE OF THE LIMITATION IS FOUND TO EXIST, THEN THE IMPUGNED ACTION CANNOT BE TAKEN AT ALL BEYOND THE PERIOD IDENTIFIED

The Honorable Sindh High Court in **2013 PTD 1659** held that there were three instances of limitation: (a) Where there is an express time bar imposed by statute; (b) Where such bar can or is to be inferred from and on a proper reading and interpretation of the relevant provisions; or (c) where the action has been taken beyond a reasonable period of time. In this case it was identified that the second possibility was applicable; i.e. on proper reading of various provisions including in particular sections 161 and 174, such bar had/ought to be inferred and that the third possibility was considered a secondary submission without prejudice to the main case.

4.2 THAT THE COMMISSIONER IS NOT BARRED FROM TAKING ACTION U/S 161

The Honorable LHC upon proper interpretation and application of Section 161, concluded that there is no period of limitation, a point in time must be reached and if such action is taken thereafter, the Commissioner shall have to justify as to why action was taken belatedly as onus would lie on the Commissioner. If he fails to provide justification, then the proceedings would be liable to be set aside.

It was further clarified that the Commissioner shall have to discharge their burden before declaring any liability and cannot simply conclude that for want of documentary evidence and accounts, the taxpayer is liable. And that delayed action means that the burden is on the Commissioner to justify the demand raised and the imposition of any liability.

Therefore, to the extent of the repeated demands for production of documents in the impugned notices, the same are without any legal basis and against the mandate of the law.

4.3 THAT THE RELEVANCE OF SECTION 174 APPLY FOR THE DETERMINATION OF BAR OF LIMITATION

The LHC also decided that section 174 becomes relevant if the Commissioner takes action under section 161 for a failure to deduct tax and the amount from which the deduction had to made was relatable to the deducting authority's income then any such action taken beyond the period up to which the deducting authority had to maintain its books of accounts under Section 174 would require proper justification. Onus would be on the Commissioner to explain why action was taken belatedly. If there is a proper justification, then the onus would stand discharged, and the action would be sustainable in law. However, if there is no proper justification then the onus would not be discharged, and action would be liable to be set aside.

4.4 THAT PRODUCTION OF RECORD IS NOT REQUIRED BEYOND SIX YEARS IN TERMS OF SECTION 174(3) OF THE ITO

The LHC considered in the matter in 2020 PTD 2111 wherein the Court held that:

Quote
In view of the above, both these petitions are allowed. However, it is made clear that the proceedings of audit of income tax under section 177 of the Ordinance may continue but the petitioners shall not be required by the department to produce the record.

Unquote
Furthermore, a judgement passed by the Honorable Sindh High Court 2013 PTD 1659 went a step further to hold that there is some obligation on the department when it initiates actions beyond the six-year period and calls for documents and record which the taxpayer is not required to maintain under the law. The Court

held that purpose of setting a time limit and maintaining accounts and documents is to ensure that proceedings were held within time and in case of delay the obligation rests on the Commissioner to justify the cause of delay and reasons for seeking documents beyond the six-year period.

4.5 THAT THE PROCEEDINGS U/S 161 ARE INDEPENDENT AND SHALL PROCEED

Proceedings under Section 161 of the Ordinance were independent proceedings which may continue, and the department shall make use of the information provided and pass speaking orders on the basis of which it shall determine whether there is failure to pay the tax collected / deducted without placing any burden on the taxpayer and its inability to produce relevant documents.

5. CONCLUSION

The LHC concluded that the Petition was accepted, and that the onus lies on the Commissioner to provide justification for imposition of any liability on the taxpayers beyond six years and cannot demand documentary evidence and accounts thereafter unless proceedings were already initiated and are pending before the authority or court. As per a widely circulated newspaper, FBR approached Honourable Supreme Court against the decision of LHC. The apex court has also upheld the decision of LHC which means the matter has attained finality.

4. TOPIC OF THE MONTH

TAXATION OF A PE OF A NON-RESIDENT

The most common way of establishing a presence in any country by any foreign person is through setting up of a Permanent Establishment ("PE"). This involves movement of funds between the Non-resident Person ("NR") and the PE, and between PE and third parties. Entities often exploit their off- shore presence to report expenses and losses in the Jurisdictions having higher tax rates and reporting profits in the Jurisdictions having lower tax rates. To curb such practices, countries often have tax laws which ensure proper declaration of profits wherever due.

Pakistan also has such laws and we will discuss the same in this article.

1. DEFINITION OF PE

Section 2(41) of Income Tax Ordinance, 2001 ("ITO") defines a PE as a fixed place of business through which the business of the person is wholly or partly carried. The definition also includes other places like a place of management, a mine quarry, forestry, etc. (Please read our earlier Topic of the month through link https://tolaassociates.com/wp-content/uploads/2021/06/TaxPak-May-2021.pdf wherein we have differentiated between a PE and a Liaison office.)

2. TAXATION

All the incomes of a PE other than incomes under the head 'business income' will be charged to tax in a normal manner.

Business income of a PE of an NR will be determined subject to following principles:

a) Distinct and Separate Person

The profits of a PE shall be computed in the basis that it is a separate and distinct person independent from the Non-resident person.

This means that incomes of both the entities will neither be clubbed nor loss of any of the entity will be adjusted against profits of the other. Moreover, any transfer of assets, goods, services, etc. should be at arm's length and will be taken into account while computing revenues of the transferor.

b) Executive and Administrative Expenses Allowed

Expenses incurred for the purpose of the business activities of PE will be allowed whether incurred in Pakistan or outside Pakistan. However, such expenses shall be allowed subject to the provisions of ITO.

This means that PE shall have to comply with provisions of ITO such as, tax withholding, payments through banking channel, etc. to be able to claim such deductions.

c) Royalties, Management services and Profits on debt

PE shall not be allowed deduction for payments by it to its Head Office or another PE of the NR with respect to following:

- Royalties, fees or other similar payments for the use of tangible or intangible assets by the PE;
- Compensation for any services including management services; or
- Profit on debt on moneys lent to the PE by Head Office, except where the lender is involved in banking business.

However, any payment with respect to reimbursement of any of above expense **actually paid** by the Head Office to a third party will be allowed as deduction.

Similarly, since no deduction of expense is allowed in above cases, revenues shall also not be taken into account where PE receives any payment from NR with respect to any of the above mentioned transactions.

However, where such payments are received by the PE from third parties, such amounts will be treated as income from business attributable to PE in Pakistan [section 6(4) of ITO].

d) Limit of Head Office Expenditure

The ratio of amount of deduction to turnover of PE, with respect to any Head Office expenditure, will not be more than the ratio of the total head office expenditure of NR to its worldwide turnover.

For example, worldwide turnover of the NR is USD 54 million and its total Head Office expenditure is USD 2.7 million. The NR has a PE in Pakistan whose Pakistan turnover is Rs. 60 million. In such a case, the Head Office expenditure allowed to the PE will be not more than Rs. 3 million (2.7 / 54 x 60).

Head Office expenditure is defined as any executive or general administration general expenditure incurred by the NR outside Pakistan for the purposes of business of the Pakistan PE and also includes following:

- any rent, local rates and taxes excluding any foreign income tax, current repairs, or insurance against risks of damage or destruction outside Pakistan;
- any salary paid to an employee employed by the head office outside Pakistan;
- any travelling expenditures of such employee; and
- any other expenditures which may be prescribed.

This means, first Head Office expense will be computed as per the definition and thereafter it will be compared with the limit specified above.

e) Profit and Debt and Insurance paid by NR

Any profit on debt or any insurance payment on such debt paid by NR will not be allowed as deductions to PE irrespective of the fact whether such debts are procured for the operations of PE or not.

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