BUDGET FLASH 2016

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Income Tax

- **Super tax for rehabilitation of displaced persons -** *Section 4B*

  The Finance Bill proposes to extend the Super Tax Levy for a further period of one year to tax year 2016.

  The Scheme of taxation for levy of super tax for tax year 2016 by and large remains the same except that it is now proposed that for computation of income, depreciation and business losses shall not be taken into account when calculating income.

- **Income from property derived by non-corporate taxpayers -** *Section 15 and 15A*

  Presently income from property for all taxpayers is chargeable to tax on net income basis after claiming eligible deductions provided in Section 15A.

  The Bill now seeks to tax non-corporate taxpayers i.e. individuals and association of persons on account of income from property on a gross basis.

  Conversely the income from property of a company remains chargeable to tax on a net income basis after claiming eligible deductions as provided in Section 15A.

- Disallowance of expenditure in case of non-deduction of tax from their payments - *Section 21(l)*

  Presently only specified expenses can be disallowed if tax has not been withheld from the payment.

  The bill proposes to disallow all expenditure where withholding tax is not deducted at the time of making payment(s). This restriction will apply to all expenses whether part of trading account or profit and loss account.

  The proposed amendment however, restricts the disallowance to a maximum of 20% on purchase of raw materials and finished goods.

- Limit on claim of sales promotion, advertisement and publicity expenses by pharmaceutical manufacturers - *Section 21(o)*

  The Finance Bill proposes to restrict the claim of expenditure by a pharmaceutical manufacturer in respect of sales promotion, advertisement and publicity upto a maximum of 5% of turnover.

- Restriction on depreciation during tax holiday period - *Section 22(5)*

  The Bill proposes to insert an explanation to clarify that where any building, furniture, plant or machinery is used for the purposes of business, the income of which is exempt, the admissible depreciation (normal and initial depreciation) shall be deemed to have been allowed in respect of the said tax year and after expiration of the exemption period, the WDV of such asset will be worked out after taking into effect the depreciation deemed to have been allowed.

- Group relief - *Section 59B & Clause 103A of Part I of the Second Schedule*

  Under the present law, subject to fulfilment of certain conditions, group companies are allowed to surrender losses of a tax year within the group to accelerate the realization of available business losses. At present, whatever loss is available to a company can be entirely surrendered to another group company subject to fulfilment of required conditions.

  The Bill now proposes to place a restriction on the quantum of loss that can be surrendered to another group company by inserting a formula to restrict the losses to the extent of the percentage of share capital that is held by the holding company in such loss surrendering company.

  Further, the Bill proposes to withdraw the exemption from inter-corporate dividend to such companies that fall within the scheme of section 59B availing group relief.

- Tax credit for investment in health insurance - *Section 62A*

  It is proposed to insert Section 62A whereby a resident person other than a company shall be entitled to a tax credit in respect of health insurance premium or contribution paid to any insurance company registered with the Securities and Exchange Commission of Pakistan under the Insurance Ordinance, 2000. The amount of tax credit shall be restricted to the lesser of :

  - Total premium
  - 5% of person's taxable income
  - Rs.100,000

- Tax credit on contribution of the investment to an approved pension fund - *Section 63*

  The proposed amendment now restricts the 2% additional contribution upto the year ending 30 June 2019 irrespective of the number of years the credit has been allowed to the individual and restricts the total contribution allowed to such person upto 30% of total taxable income of the preceding year. This limit is presently 50% of the previous year's taxable income.

- Deductible allowance for profit on debt - *Section 64A*

  The Bill proposes to enhance the allowable limit against profit on debt paid by an individual for the purposes of construction of new house or acquisition of a house from Rs.1 million to Rs.2 million.

- Deductible allowance for education expenses - *Section 64AB*

  The Bill proposes to introduce a deductible allowance for education expenses comprising of tuition fee paid by an individual whose taxable income is less than Rs.1 million in that tax year. The allowance is however restricted to the lesser of –

  a) 5% of the tuition fee paid by the individual;
  b) 25% of the person's taxable income;
  c) an amount computed by multiplying Rs.60,000 with number of children of the individual.

- Tax credit for employment generation by manufacturer - *Section 64B*

  The Bill proposes to extend the tax credit available to a company which sets up a new manufacturing unit between 01 July 2015 to 30 June 2019 (from 30 June 2018). It is further proposed that the rate of tax credit at 1% for every 50 employees registered with EOBI and Employees Social Security Institution of the Provincial Government be enhanced to 2%. All other conditions to avail the tax credit remain the same.

- Tax credit for investment - *Section 65B*

  The Bill proposes to extend the date of purchase and installation of plant and machinery for the purpose of extension, expansion, balancing, modernization and replacement of plant and machinery already installed by an industrial undertaking to avail credit of 10% of the amount so invested upto to 30 June 2019.

- Tax credit for enlistment - *Section 65C*

  The Bill proposes to extend the tax credit equal to 20% of the tax payable, to a corporate taxpayer, who opts for enlistment on a Stock Exchange in Pakistan in the year of listing and the year following.

- Availability of tax credit - *Sections 65D and 65E*

  Availability of tax credit under Sections 65D and 65E to new and already established industrial undertaking has been extended upto 30 June 2019. Further, condition of 100 percent equity investment has been relaxed to 70 percent thereby allowing long term debt financing upto 30 percent.

- Apportionment of deductions - *Section 67*

  Section 67 read with Rule 13 of the Rules deals with apportionment of common expenses incurred by a taxpayer in deriving more than one source of income.

  In the past, there has been a difference of opinion between taxpayers and tax officials as to whether allowances would also be apportioned. The appellate authorities also had a divergent view on the issue and conflicting judgments on this subject exist.

  The Bill now lays to rest this controversy in favour of the Revenue by substituting the word "expenditure" with the expression "expenditures, deductions and allowances". This would effectively mean that now all common deductions, whether in the nature of an actual expenditure or an allowance, would be apportioned amongst the various streams of income.

- Agreements for the avoidance of double taxation and prevention of fiscal evasion - *Section 107*

  The information received or supplied or communication or correspondence made under a tax treaty and other like arrangement shall be confidential and that the tax authorities will not disclose such information except as required under Section 216(3) i.e. except where the information is required by a court or by a Government or regulatory authority.

  The Bill now proposes to omit such exclusion under section 216(3) to the requirement of confidentiality.

- Transfer pricing documentation - *Section 108*

  Presently, contrary to the law in other countries, there is no requirement to mandatorily maintain any transfer pricing documentation in Pakistan.

  In line with the growing global emphasis on the concept of Base Erosion and Profit Shifting (BEPS) and transparency in transactions between related parties, the Bill now proposes to introduce a requirement to maintain transfer pricing documentation in respect of all transactions undertaken with associates.

  Although the Bill does not provide a practical mechanism in relation to the requirements or the prescribed format for preparing the information, it is anticipated that these would be incorporated in the Rules along lines similar to the guidelines issued by the OECD on transfer pricing documentation.

- Minimum tax - *Section 113*

  The Bill proposes to reduce the threshold of turnover for individuals and association of persons from Rs.50 Million to Rs.10 Million effective from tax year 2017 for levy of minimum tax.

  The Bill also seeks to omit the provision of exclusion of corporate taxpayer due to gross loss before depreciation and other inadmissible expenses from the ambit of applicability of minimum tax with effect from tax year 2017.

  For the purposes of comparison of tax payable by a taxpayer under normal basis with minimum tax, Super tax paid under section 4B shall be excluded from the tax paid under normal basis.

- Advance tax - *Section 147*

  The Bill seeks to provide an explanation regarding determination of quarterly advance tax liability. The tax assessed to the taxpayer shall include minimum tax and Alternative Corporate Tax.

- Tax collection on cash withdrawal from a bank - *Section 231A*

  The Bill seeks to insert an explanation to clarify that the aggregate of Rs.50,000 shall be withdrawal from all the bank accounts of the account holder in a single day.

- Advance tax on private motor vehicle - *Section 231B*

  The Bill seeks to introduce an advance tax from non-filers @ 3% of the value of the motor vehicle where the vehicle is being leased by a leasing company, schedule bank, investment bank, Development Financial Institution or a Modaraba.

THE FIRST SCHEDULE

- Capital gain on disposal of securities - *Section 37A*

  Presently, where the holding period of securities is more than 4 years, the sale of such securities is subject to capital gains tax at 0 percent.

  The Bill now proposes to withdraw such benefit and instead provides for the taxation of any security where the holding period is 24 months or more and the security was acquired on or after 01 July 2012.

  However, where the securities were acquired prior to 01 July 2012, a 0 percent rate would be applicable if they have been held for 24 months or more.

THE SECOND SCHEDULE

PART - I

- Exemption for setting up businesses in Gawadar Free Zone Area - *Clause (126AA)*

  A new Clause (126AA) is being proposed to be inserted by virtue of which profits and gains derived by taxpayers from businesses set up in Gawadar Free Zone Area will be exempt from tax for a period of twenty three years commencing from 01 July 2016.

- Exemption to income arising from export of computer software or IT services or IT enabled services - *Clause (133)*

  The Bill proposes to extend the period of the exemption available under Clause 133 to income arising from exports of computer software or IT services or IT enabled services upto 30 June 2019 provided that eighty percent of the export proceeds is brought into Pakistan in foreign exchange through normal banking channel.

PART - II

- Export of services rendered and construction contracts executed outside Pakistan - *Clause (3)*

  The Bill proposes to enhance the rate of tax on income from services rendered and construction contracts outside Pakistan as opposed to current tax rate of 1% of the gross receipts. The Bill specifies 50% of the rate as prescribed for various services and contracts in Division-III of Part-III of First Schedule to the Ordinance. The proposed rates of tax are summarized as under -

	Rate of tax			
	Corporate		Non-Corporate	
	Filer	Non filer	Filer	Non filer
For transport services	1	1	1	1
For services other than transport services	4	6	5	7.5
For construction contract	3.5	5	3.75	5

PART - IV

- Large Trading Houses - *Clause (57)*

  Large Trading Houses are inter-alia exempt from payment of minimum tax under Section 113 of the Ordinance. The Bill seeks to withdraw the above exemption and proposes that Large Tading Houses are required to pay minimum tax at the reduced rate of 0.5% for tax years 2017 to 2019 and 1% for tax year 2020 and onwards.

- Concession of exemption from payment of tax under Section 148 - *Clause (72B)*

  Industrial undertakings are entitled to obtain exemption certificate under Section 148 of the Ordinance on the fulfillment of conditions as specified therein.

  The Bill proposes to impose certain other conditions which are as under-

  - The industrial undertaking would be subject to tax audit in respect of consumption, production and sales of the latest tax year for which the return has been filed.

  - If the taxpayer fails to present accounts or documents to the Commissioner, he is empowered to cancel the certificate and recover the tax which was not paid due to the exemption.

THE FOURTH SCHEDULE

- Enhancement in rate of capital gains and dividends derived by insurance companies - *Rule (6B)*

The Bill proposes to tax capital gains in the hands of insurance companies at the corporate tax rates specified in Division II, Part I of the First Schedule to the Ordinance, effective from the tax year 2017. Earlier such gains were taxable at the slab rates based on the holding period of such securities (subject to a maximum rate of 15%).

The Bill also seeks to amend Rule (6B) of the Fourth Schedule whereby dividend income is proposed to be taxed at the corporate tax rates as specified in Division II, Part I of the First Schedule to the Ordinance.

THE EIGHTH SCHEDULE

- Capital gain on disposal of open ended mutual fund units - *Rule (100B)*

The Bill proposes that capital gain on disposal of units of open ended mutual funds to which section 100B applies, shall also be computed and determined under the Eighth Schedule and tax thereon shall be collected and deposited by NCCPL.

Sales Tax

- Cottage Industries

Under the ST Act, supplies made by Cottage Industries is exempt from levy of sales tax. The prescribed threshold of the annual turnover from taxable supplies of Rs.5 million is proposed to be enhanced to Rs.10 million.

- Due date - *Section 2 (9)*

The Bill seeks to insert various filing dates for different Annexures to the returns. This proposed amendment is in line with the FBR decision to launch a new automated system for e-filing of sales tax and federal excise returns to facilitate taxpayers. The new system is expected to be put in place from 01 July 2016.

- Input tax - *Sub-clause (d) of Section 2(14)*

Section 2(14) of the ST Act provides various categories of input adjustment against the output tax liability which inter-alia includes the provincial sales tax levied on services rendered or provided to the person. The aforesaid adjustment is now proposed to be omitted. This proposed omission will increase the cost of doing business resulting in the increase in the price of goods.

- Time and manner of payment - *Section 6(2)*

Currently tax in respect of taxable supplies made during a tax period shall be paid by a registered person at the time of filing the return of that period under Chapter V. This timing for filing of return has been proposed to be omitted and the Bill now seeks to propose any date that may be prescribed by the FBR in this regard.

- Determination of tax liability - *Section 7 Sub-section 2*

The Bill seeks to insert a proviso to Section 7 of the Act which stipulates additional conditions for the input tax claim unless the supplier declares the supplies in his return in respect of which the input is claimed alongwith payment of tax due as indicated in the return.

- Input tax credit not allowed - *Clause I of Section 8(1)*

The Bill also seeks to provide an additional condition for claim of input tax whereby the reclaim or input tax deduction will not be allowed if the supplier has not paid the amount of tax due as indicated in his return.

- Assessment of tax and recovery of tax not levied or short-levied or erroneously refunded - *Section 11 (4A)*

Under the existing provisions of the ST Act, the OIR is not empowered to recover the principal amount of tax from the payer (buyer) which was not deducted or deposited into the Government Treasury. The Bill now seeks to insert a new Sub-section (4A), whereby the OIR is empowered to determine and collect the amount in default in case where the buyer failed to withhold tax.

- Sales of taxable activity or transfer of ownership - *Section 49(2)*

This section provides the mechanism for charging of sales tax in case of transfer of taxable business activities or part thereof from a registered person to an un-registered person or a registered person to another registered person.

Sub-section (2) of Section 49 provides that in case of transfer of ownership between registered persons the sales tax chargeable on taxable goods shall be accounted for and paid by the registered buyer.

The Bill now proposed to substitute the above Sub-section (2) by classifying such transaction as zero rated.

- Certain Sales Tax and Federal Excise measures announced in the salient features of the budget documents

  In order to facilitate the exporters and provide for a No-Tax, No-Refund Regime for five export oriented sectors, the items as specified in the SRO 1125(1)/2011 dated 31 December 2011 and the purchase of energy i.e. electricity, gas, furnace oil and coal, are to be subjected to zero rate of sales tax. The retail sales of locally manufactured finished goods of these sectors are to be subjected to sales tax @5%.

  Sales tax is currently levied @5% at the import stage, @3% as value addition tax and 2% as further tax on second hand and worn clothing, which results in cumulative impact of sales tax at 10%. In order to provide relief to the low income segment, using second hand worn clothing, exemption from further tax is being provided.

  Tier -1 retailers are obliged to pay sales tax at the standard rate after input tax adjustment. It is proposed to provide an option to these retailers to pay sales tax at a flat rate of 2% of their total turnover without any input adjustment.

  In order to bring Marble industry in the ambit of sales tax, it is proposed to charge sales tax @ Rs.1.25 per KWH of electricity consumed. The proposed tax shall be in addition to standard sales tax of 17% on supply of electricity as well as extra tax of 5%.

  The rate of collection of sales tax at a fixed rate basis for steel sector, ship breaking sectors and steel melters are proposed to be revised upwards.

- Exemption of sales tax on pesticides

  Currently pesticides are subject to sales tax @7% without adjustment of input tax. Keeping in view the importance of pesticides for the agriculture sector, pesticides and their ingredients are being granted exemption from sales tax.

- Exemption from sales tax to businesses to be established in Gawadar

  Exemption from sales tax to supplies made by the businesses to be established in the Gawadar Free Zone for a period of 23 years.

- Abolition of zero-rated status of stationery items

  Stationery items are exempt from sales tax under the Sixth Schedule to the Sales Tax Act, 1990 as well as zero-rated under the Fifth Schedule thereof. It is proposed to withdraw zero-rating on stationery items and their inputs.

- Abolition of zero-rated status of Milk

  Milk, fat-filled milk and preparations for infant use have been enjoying zero-rating facility on supplies for many years. It is proposed to withdraw zero-rating on milk and fat filled milk. Zero-rating on preparations for infant use is proposed to be retained.

- Sales tax rate on import of mobile phones enhanced

  Mobile phones, are currently charged to sales tax under three categories i.e. Rs.300, Rs.500 and Rs.1,000, based on their features. The proposed new slabs are Rs.300, Rs.1,000 and Rs.1,500 respectively.

Federal Excise Duty

- Rate of duty on aerated waters enhanced - *First Schedule, Table I*

  The rate of duty on aerated waters, as mentioned in serial Nos. 4, 5 and 6 of Table I of the First Schedule to the FE Act, have been proposed to be enhanced from “10.5 of retail price” to “11.5 of retail price”.

- Rate of duty on cigarettes modified - *First Schedule, Table I*

  The rates of duty on cigarettes have been proposed to be enhanced in two phases i.e. from 01 July 2016 to 30 November 2016 and from 01 December 2016 onwards.

- Rate of duty on cement modified - *First Schedule, Table I*

  The rate of duty on Portland cement, aluminous cement, slag cement, super sulphate cement and similar hydraulic cements, whether or not coloured or in the form of clinkers is presently 5% of the retail price. It is now proposed to substitute it by Re.1 per kilogram.

- Withdrawal of duty on certain excisable services *First Schedule, Table II*

  Through an explanatory note inserted after Table II to the First Schedule of the FE Act, the Bill seeks to withdraw excise duty on such services which are subject to levy of sales tax under the provincial sales tax laws.

The said services are as under:

TABLE – II (Services)

S. Nos.	Description of goods	Heading / sub-heading Number
1	Advertisement on closed circuit T.V.	9802.3000
2	Advertisements on cable T.V. network.	9802.5000
2A	Advertisements in newspapers and periodicals (excluding Classified advertisements) and on hoarding boards, poles Signs and sign boards.	9802.4000 and 9802.9000
5	Shipping agents	9804.1000
8	Services provided or rendered by banking companies, cooperative financing g societies, modarbas , musharikas, leasing companies, foreign exchange dealers, non-banking financial institutions, assets management Companies and other persons dealing in any such services.	98.13
11	Franchise services	9812.9410
13	Services provided or rendered by stock brokers	9819.1000

The relevant Rules and Special Procedures of aforesaid services under the FE Act are also expected to be amended vide separate SROs at a later stage.

- Withdrawal of duty in VAT mode

The “White Crystalline Sugar” under tariff headings 1701.9910 and 1701.9920 is subject to federal excise duty in VAT mode @8%. The Bill seeks to replace this duty with sales tax which would be levied at 8%.

- Amendments in the Third Schedule

The Third Schedule to the FE Act lists down the goods and services that are exempt from duty of excise whether conditionally or otherwise.

The Bill proposes to omit the exemption available on supply of White cement. Further, the Government is focused to develop the Gawadar Port and therefore exemption is proposed on materials and equipment required for construction and operation of Gwadar port imported by and for China Overseas Ports Holding Company Limited (COPHCL) and its operating companies for a period of forty years as well as for Supplies made by the businesses to be established in the Gwadar Free Zone for a period of twenty three years.

Islamabad Capital Territory (Tax on Services) Ordinance, 2001

- Application of Sales Tax Act, 1990

Certain provisions of Sales Tax Act, 1990 are proposed to be inserted to apply mutatis mutandis under the Islamabad Capital Territory (Tax on Services) Ordinance, 2001.

- Exclusion of services

Regulatory and licensing services rendered or provided by an organization established by or under a Federal Statute proposed to be excluded from the ambit of service tax.

Customs

- First Schedule

Tariff slabs of First Schedule to be reduced from 5 to 4. New proposed slab rates, applicable to all goods other than vehicles, are 3%, 11%, 16% and 20%.

Slab rates of 2% and 5% to be replaced with 3%.

- Fifth Schedule

Fifth Schedule to the Customs Act relating to import of plant and machinery reduced the customs duty rate from 5% to 2% on dairy, livestock and poultry and from 5% to 3% on certain other machineries and equipment.

Customs duty is proposed at 0% on import of certain machinery and equipment of textile industry not manufactured locally.

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