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Budget Red-Eye 2024

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Preamble

The Finance Bill, 2024 has been presented in the National Assembly amid heavy expectations that the budget will be driven by the measures agreed with or suggested by the International Monetary Fund (IMF). Pakistan is facing some of the worst challenges in its history with respect to economy, growth and confidence of businesses / investors and it was expected that in addition to the measures suggested by the IMF, there would be some measures included by the Government that will focus on the broadening of tax base, revival of economy and restoration of the confidence of businesses / investors.

However, the Finance Bill, 2024 seems more focused on the old and much criticized approach of collecting more tax from the persons already in the tax net while hoping that the higher tax rates for non-filers will force non-tax paying persons to come in the tax net. This approach has resulted in continuous decline in the development and confidence of businesses as well as increase in cash based / undocumented economy to avoid the tax net.

While there are some good measures in the Finance Bill, 2024 that will enable the Government to collect more tax revenue, in most cases there seems to be a disconnect between the measures proposed by the Government and the measures suggested by the tax experts / chambers of commerce / economists. It is imperative for any proposed measures to be successful that the key stakeholders / advisors of the economy / businesses are on board with the measures proposed by the Government.

Lastly, there is still time for some deliberation before the Finance Bill, 2024 is approved by the National Assembly and the Senate. Therefore, we may see some changes made specially in the areas or sectors most impacted.

This document briefly outlines the changes proposed by the Finance Bill, 2024 in the areas of income tax, sales tax, customs duty and federal excise duty and their link with the economy. Our Commentary on Finance Bill, 2024 will address the changes in more detail along with our comments.

Economy

The coalition government has presented its first budget for the FY 24-25 with proverbial one eye or probably, in this case, both eyes on ongoing negotiations for the IMF program.

Majority of the budget proposals are not expected to rattle ongoing parlays with lender of the last resort. Authorities, for now, seem to be keen on maintaining current economic trajectory where higher GDP growth rate is traded off with contractionary fiscal and monetary policies.

GDP growth rate target of 3.6% for the next financial year while, higher than a lowly 2.4% rate expected to be achieved during the ongoing financial year, is still substantially lower than the rate at which country's economy is required to grow to bring large segments of populations out of the poverty trap. However, overall growth direction is positive and in view of early signs of economic recovery, we expect the targeted GDP growth rate to be achievable albeit any internal or external shocks.

While some of the taxation measures including increase in Petroleum Development Levy coupled with expected upward adjustments in energy prices will result in higher inflationary pressures, however, considering State Bank of Pakistan's (SBP) tight monetary policy and government's contractionary fiscal policy, we expect targeted inflation rate of 12% broadly achievable.

The Government has set an ambitious tax collection target for the Federal Board of Revenue (FBR) at Rs. 12,970 billion, a 38% increase from last year's goal which will help it to contain budget deficit at 6.9% of the GDP. While the Government is expected to achieve 30% growth in tax revenues during the outgoing financial year, high inflation rates played key role in making it possible. With inflation rate expected to settle at 12% and targeted GDP growth rate of 3.6%, a 38% increase in tax collection is a stretched target. Notwithstanding, we believe that with improved tax enforcement and new taxation measures, Pakistan may yet be able to come close to targeted primary and fiscal deficits.

Irrespective, of strong statements from the authorities, on broadening of tax base and bringing all economic segments equally into the tax net, taxation measures announced in the budget fall short on this count. No significant measures have been announced to tap into undocumented economy. Focus seems to be on generating higher tax revenues by increasing tax rates on existing taxpayers.

Some of the proposed new measures seem to be designed to encourage higher filing of income tax returns by making business transactions prohibitively expensive for non-filers, however, empirical evidence does not support significant increase in tax base due to these steps.

There have been few limited measures proposed in the budget to encourage growth in certain sectors including agriculture, however, there are no significant incentives to expand local manufacturing for import substitution and export growth.

We maintain that economic targets given in the budget are broadly achievable and proposed taxation measures are focused on enhancing tax revenues from existing tax base, preferring stability overgrowth.

This may provide sufficient fiscal space to the Government to successfully negotiate new long-term lending with the IMF, however, unless the promised key reforms and structural changes are successfully made, the opportunity for the economy to turn a corner and move to high growth trajectory will be lost.

Income Tax

- Proposal for inclusion of a member of the FBR, to whom powers of the FBR have been delegated under section 8 of the Federal Board of Revenue Act, 2007, in the definition of “Board”.
- Proposal for deduction of advance tax from the consideration paid or payable against acquisition of shares of a company, to be made at the time of payment or at the time of registration of shares by the Securities and Exchange Commission of Pakistan (SECP) or by the SBP, whichever is earlier.
- Proposal to allow carry forward of business losses for a period of ten (10) years in case of Pakistan International Airlines Corporation Limited.
- Proposal to clarify that tax credit under section 65F would be allowed on the income derived from the operations of coal mining projects only in Sindh, supplying coal to power generation projects.
- Proposal for tax exemption to the members of such Association of Persons (AOP) whose turnover is Rs. 300 million or more, subject to filing of duly audited financial statements along with return of income of AOP.
- Proposal for levy of higher rates for persons not appearing in the Active Taxpayers List (ATL) to be applicable on persons not filing return by the specified due date or the period extended by the FBR or the Commissioner.
- Proposal to disallow 25% of sales promotion, advertisement and publicity expense if a deduction has been claimed on account of royalty paid or payable to an associate.
- Proposal for restriction on foreign travel, for a citizen of Pakistan excluding persons having NICOP, minors, students and other classes of persons as notified by the FBR for non-filing of return if liable to file return of income.
- Proposal for disclosure of foreign assets in the wealth statement.
- Proposal to extend the Commissioner’s powers for best judgment assessment in case where a person fails to file return of income in response to notice issued to the person discontinuing a business.
- Proposal to define the value of assessment of tax as the net increase in tax liability and value of refund as net reduction in refund of a person as a result of order sought to be assailed for the purpose of filing of appeal before the Commissioner Appeals and Appellate Tribunal.
- Proposal for extension of the cutoff date from 16 June 2024 to 16 September 2024, for transfer of appeals pending before Commissioner (Appeals) to Appellate Tribunal involving amount exceeding Rs. 20 million.
- Proposal to empower the Commissioner to reject the lower estimate of advance tax and estimate in absence of last assessed income where certain specified documents and details are not furnished along with such estimate. Further, 120% instead of 110% of turnover of latest tax year proposed in case where the turnover for the relevant quarter is not known.
- Proposal to empower the FBR to determine the minimum value of goods for the purpose of collection of advance tax on imports. Definition of value of goods proposed to include minimum value as notified by the FBR for this purpose.
- Proposal to convert the facility of exemption certificate to reduced rate certificate on supply of goods for both the residents and the permanent establishments of non-residents.
- Proposal to convert the facility of exemption certificate to reduced rate certificate for certain withholding tax provisions.
- Proposal to tax receipts from exports of goods under minimum tax regime which are currently taxed under final tax regime.

Income Tax

- Proposal to penalize and prosecute a person who has discontinued the business and has failed to file the return in response to notice issued by the Commissioner Inland Revenue as under:
 - a) Penalty higher of:
 - 0.1% of the tax payable per day; or
 - Rs. 1,000 per day (not exceeding Rs. 10,000 for individuals and Rs. 50,000 for all other cases).
 - b) Prosecution for offence punishable with fine up to Rs. 25,000 or imprisonment up to two (2) years.
- Proposal to penalize with sealing of the shops of the Shopkeepers on account of failure to register under the Tajir Dost Scheme or similar schemes in the event of non-registration as under:
 - Sealing for seven (7) days for first default; and
 - Sealing for twenty (20) days for second default.
- Proposal for imposition of penalty on implementing agencies who fail to block sims or disconnect utilities or allow exit from Pakistan of non-filers as under:
 - Rs. 100 million for first default; and
 - Rs. 200 million for each subsequent default.
- Proposal for imposition of penalty of 50% of the amount of tax involved for failure to deduct tax at the time of making payment for acquisition of shares or at the time of registration of shares by the SECP or the SBP, whichever is earlier.
- Proposal for imposition of penalty on companies and AOPs for leaving the relevant particulars of return blank or filing incomplete particulars, at higher of:
 - Rs. 500,000; or
 - 10% of tax chargeable.
- Proposal to prosecute companies and AOPs who commit default by leaving the relevant particulars of return blank or who file incomplete particulars as following:
 - a fine; or
 - imprisonment for one year; or
 - both of the above.
- Proposal to prosecute for failure to get registered for Tajir Dost scheme with punishment of imprisonment which may extend to six (6) months, or with fine, or both.
- Proposal to increase default surcharge on account of late payment of tax from 12% to KIBOR + 3%.
- Proposal to authorize National Database Registration Authority (NADRA) to receive taxpayers' data to process and analyze the same for the purpose of broadening of tax base.
- Manufacturers and commercial importers of certain specified sectors are currently obliged to collect advance tax from distributors, dealers and wholesalers at the time of sale. Proposal to now oblige all business sectors for collection of said advance tax.
- Manufacturers, distributors, dealers, wholesaler and commercial importers of certain specified sectors are currently obliged to collect advance tax from the retailers at the time of sale. Proposal to now oblige all the business sectors for collection of said advance tax from the retailers.
- Cases decided by the Appellate Authorities prior to the Tax Laws (Amendments) Act, (Act) proposed to follow the period of limitation provided under section 131 and 133 of the Income Tax Ordinance, 2001 (Ordinance) prior to commencement of the Act.
- Significant increase in tax rates proposed for salaried and other than salaried persons.

Income Tax

- Rate of tax on dividend received from mutual funds proposed to be enhanced from 15% to 25% in case 50% or more of income of mutual fund is derived from profit on debt with corresponding change in withholding tax provision.
- Uniform rate of 15% proposed on capital gain on disposal of securities as well as on immovable properties which are acquired on or after 1 July 2024 for the persons whose names are appearing on the ATL. Whereas for persons who are not on the ATL at the acquisition and disposal dates, capital gain proposed to be taxed as normal income subject to minimum tax rate of 15%.
- Proposal for increase in withholding tax rates on capital gain by mutual funds and REIT Schemes from 10% to 15%.
- Proposal for withholding tax rates for Toll manufacturer at 9% for company and 11% in other cases.
- Proposal for advance tax @ 1% of export proceeds in addition to withholding tax @ 1%.
- Advance tax collection rates in case of vehicle purchased proposed to be collected as a percentage of value of vehicles instead of fixed amounts.
- Tax collection on sale or purchase of immovable properties proposed to be collected at varying rates based on consideration received or fair market value instead of fixed rate. Similarly, rates for persons not appearing on the ATL proposed to be enhanced manifold.
- Separate rate of tax collection on sale or purchase of immovable property proposed for persons who though are on the ATL but did not file their returns of income within the due date or who are considered as 'late filers'.
- Withholding tax rates in case of certain persons not appearing on the ATL proposed to be increased substantially, e.g., in cases of mobile telephone from 15% to 75%.
- Exemption on subsidy granted by Federal Government proposed to be withdrawn.
- Withholding tax rate for distributors of cigarettes proposed to be enhanced from 1% to 2.5%.
- Benefit of reduction in tax liability of a fulltime teacher or researcher proposed to be withdrawn.
- Exemption from income tax as well as withholding of tax proposed to be extended up to 30 June 2025 for residents of former FATA & PATA.
- Proposal for amendments in Seventh Schedule for Banking Companies:
 - Bad debts classified as 'doubtful', provision for advances, off-balance sheet items or any other financial assets classified as performing, under-performing or non-performing under any applicable accounting standard are proposed not to be allowed; whereas only bad debts classified as 'loss' pertaining to non-performing assets under the Prudential Regulations proposed to be allowed.
 - Provisions or expected credit loss for advances and off-balance sheet items or any other financial assets existing before or after 1 January 2023 under IFRS 9 proposed not to be allowed as expense or deduction.
 - Rule regarding inadmissibility of notional gain or loss under International Accounting Standards 39 and 40 proposed to be replaced by 'any applicable accounting standard or policy or any guidelines or instructions of SBP'.

Sales Tax

- Proposal to enhance the scope of 'tax fraud' by introducing specific instances which may constitute tax fraud, which was previously defined broadly.
- Proposal for levy of sales tax on advance payment to be reinstated in time of supply of goods.
- Pursuant to proposed omission of section 11, several new sections proposed to be inserted, which include provisions for limitation on issuing assessment orders, best judgment assessments and recovery of unpaid tax, failure to withhold sales tax, and limitations for assessments.
- Proposal for section 25 to be substituted to introduce a comprehensive framework for auditing sales tax affairs.
- Proposal for section 25AB to be inserted to empower an inland revenue officer to initiate an investigative audit for suspected tax fraud, with the Commissioner's prior approval, which may result in assessment of tax, blacklisting, imposition of penalties, disallowance of input tax or prosecution.
- Proposal for the rate of default surcharge to be changed from 12% to KIBOR + 3%.
- Proposal to introduce electronic invoicing system which will be implemented by a "licensed integrator". Section 23(3) proposed to be amended to obligate registered persons making taxable supplies to issue electronic invoices according to the FBR's specifications.
- Proposal for DAP fertilizer to be made part of Third Schedule to the STA, 1990. Previously it was exempt from levy of sales tax under the Sixth Schedule to the STA, 1990.
- Proposal for abolishment of zero rating for local supplies of commodities, raw materials, components, parts and plant and machinery to registered exporters under Export Facilitation Scheme.
- Proposal for abolishing zero rating on certain products, including infant preparations, milk, and certain stationery items. Stationery items proposed to be taxed at 10%, while unpacked milk proposed to be exempted from sales tax.
- Proposal to exempt levy of sales tax on POL products (petrol, HSD, kerosine & light speed diesel) which was previously a zero-rated supply.
- Proposal to impose sales tax on supplies, imports of plant, machinery, and electricity in tribal areas at reduced rates: 6% and 12% for FY 2025 and FY 2026 respectively.
- Proposal to abolish sales tax exemption on certain items (such as stationery, tractors etc.) which have been either made subject to standard rate or reduced rate.
- Proposal for standard sales tax rate of 18% on medicaments in contrast to current rate of sales tax at 1%.
- Proposal for standard rate of sales tax on retailers of textile and leather which are integrated with the FBR's computerized system for real time reporting of sales.
- Proposal to introduce sales tax withholding at 80% for certain sectors (such as coal, cement, crush stone silica etc.).
- Proposal to charge sales tax at 18% ad-valorem on certain categories of cellular phones.
- Proposal for extension of the cutoff date from 16 June 2024 to 16 September 2024, for transfer of appeals pending before Commissioner (Appeals) to Appellate Tribunal involving amount exceeding Rs. 10 million

Federal Excise Duty

- Proposal of Federal Excise Duty (FED) on Acetate tow at the rate of Rs. 44,000 per kg.
- Proposal of FED on allotment or transfer of commercial and first allotment or transfer of residential property at 5%.
- Proposal for FED on supply of sugar to manufacturers at Rs. 15 per kg.
- Proposal for FED rate on E-liquid for electric cigarette at higher of Rs. 10,000 per kg or 65% of retail price.
- Proposal for FED on Nicotine pouches at the rate of Rs. 1,200 per kg.
- Proposal for increase in threshold of on-pack printed retail price of locally produced cigarettes for determining rate of FED from Rs. 9,000 to Rs. 12,500.
- Proposal for increase in FED on cement from Rs. 2 per kg to Rs. 3 per kg.
- Proposal for increase in FED on filter rod for cigarettes from Rs. 1,500 per kg to Rs. 80,000 per kg.
- Installation / removal of plant and machinery having value exceeding Rs. 50 million without prior permission of Commissioner proposed to be an act of offence attracting penalty.
- Proposal for extension of the cutoff date from 16 June 2024 to 16 September 2024, for transfer of appeals pending before Commissioner (Appeals) to Appellate Tribunal involving amount exceeding Rs. 5 million.
- Proposal for continuation of limitation period of 60 days in case of filing of appeal before Appellate Tribunal and 90 days for filing of reference before High Courts against orders passed before commencement of the Tax Laws (Amendment) Act, 2024.
- Proposal for exemption from FED on imports by diplomats, diplomatic missions, privileged persons and privileged organization.
- Proposal to grant powers to seal business premises of retailers selling illicit cigarettes.

Customs

- Proposal for exemption of Customs duties on Bovine lipid extract surfactant.
- Proposal for withdrawal of concession of customs duties on import of fresh and dry fruits.
- Proposal for reduction in concession of customs duties on import of Electric vehicles having value above USD 50,000.
- Proposal for incentivizing manufacturing of Solar Panels and Allied Equipment.
- Proposal for extension in scope of exemptions on import of machinery and equipment for farming and processing of Fish / Shrimp and Seafood.
- Proposal for increase of Customs duty on Import of Containers for Aerosol Products.
- Proposal for rationalization of Customs duty on import of parts of submersible pumps.
- Proposal for rationalization of Customs duties on import of Wheat, Sugar, HSD, LNG.
- Proposal for streamlining the imports of Aviation related Good.
- Proposal for establishment of Directorate General of National Targeting Centre (NTC), as a national single window of enforcement for all Law Enforcement Agencies (LEAs) and Directorate General of Trade Based Money Laundering for cognizance of offences related to trade-based money laundering.
- Proposal to empower Officers of National Command Authority (NCA) and Pakistan Nuclear Regulatory Authority (PNRA) for implementing and enforcing Customs Act.
- Proposal to add Intelligence Bureau (IB) in the list of Government agencies mandated to assist Customs in investigations.
- Proposal for assigning power for extension of detention period to Additional Collector or Additional Director for smooth functioning.
- Proposal for modification of some penal provisions.
- Changes proposed with the objective of making the system more efficient by accelerating the disposal of pending cases in the Customs Appellate Tribunal.
- Changes proposed with a view to ensure that the cases are swiftly decided in the High Courts and also to meet the principles of natural justice and fair trial.
- Proposal for strengthening the provision of Alternate Dispute Resolution mechanism.

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