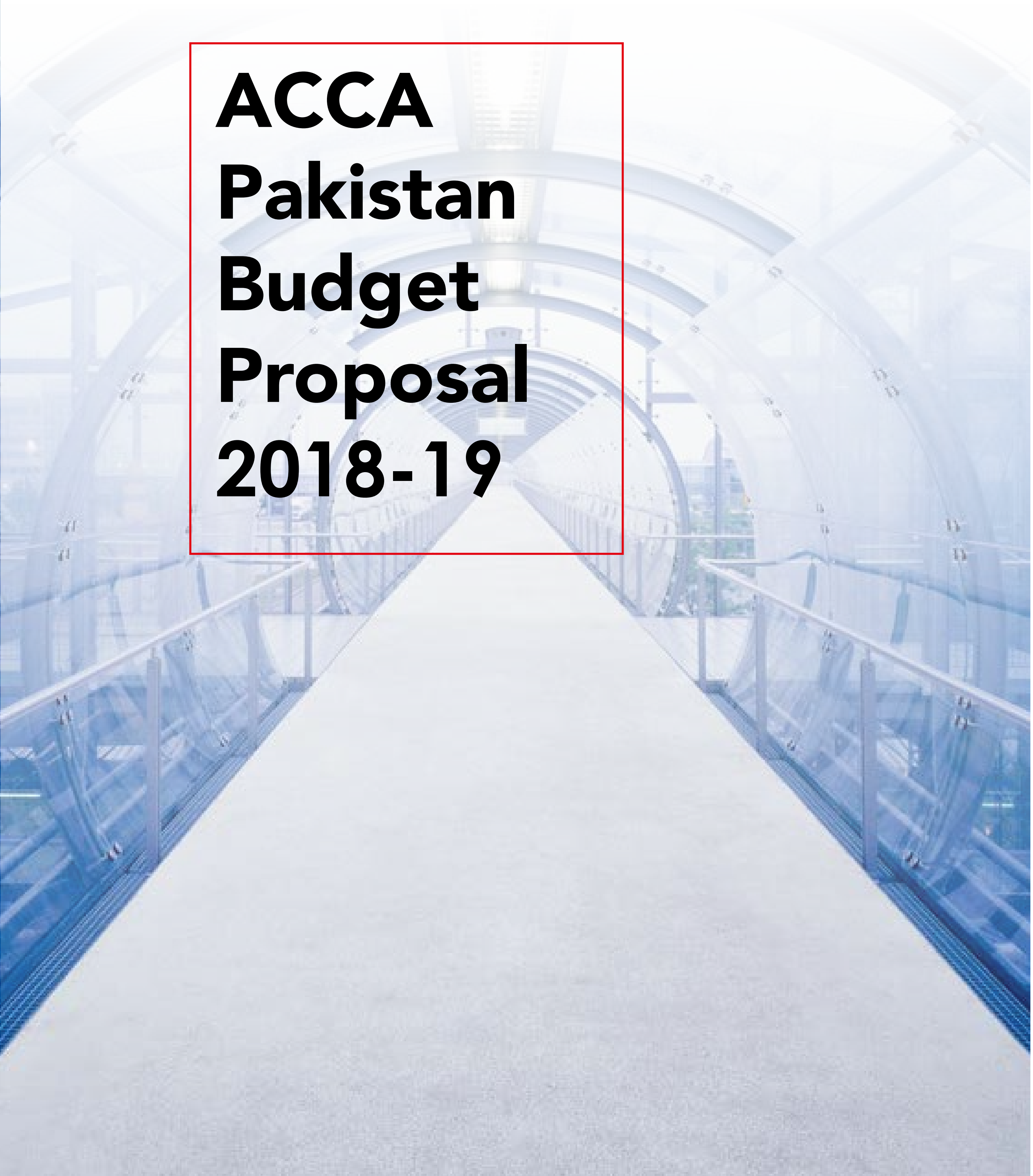
Think Ahead ACCA

ACCA Pakistan Budget Proposal 2018-19



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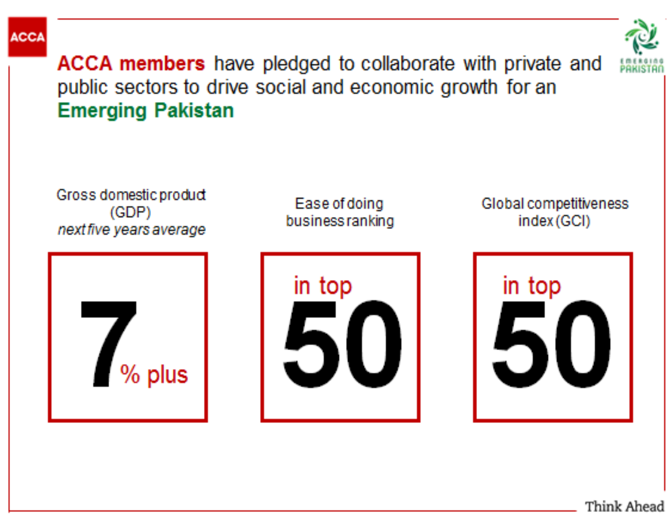
1. Foreword by Head of ACCA Pakistan

ACCA is the world's most **forward-thinking** global professional accountancy body. Through our collaborations with governments, employers, the international donor community, academia and other bodies, we work together to boost trade, grow the invest`ent climate, and make sure accountants all over the world are working to the same high international standards.

The annual Budget, or Fiscal Statement, is a feature of the political and administrative calendar in almost every economy around the globe. Annual budgets are an opportunity for ACCA to fulfil our public interest role by providing commentary for policy makers and budget 'users'

ACCA believes:

- Tax systems play an essential role in the creation and development of society. The annual budget should be an opportunity to improve the operation of the tax system in line with the goals of simplicity, certainty and stability.
- Change to tax systems should be managed carefully and appropriately. Tax administrations should grasp the opportunities which digitalisation of process can offer to them, but must recognise the varying capacity of taxpayers when developing taxpayer facing elements of the compliance process.
- Policy makers should be supported in the goal of reducing tax evasion and tax avoidance.



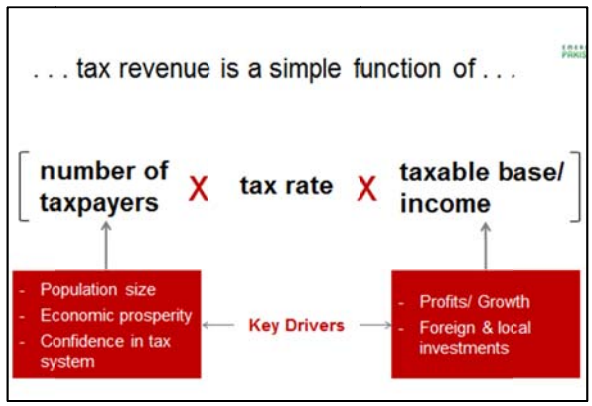
ACCA

2. Preface by Chairman ACCA Pakistan Taxation Subcommittee

With a global presence in over 180 countries and having achieved over 200,000 members globally, ACCA is well placed to share **global insights** for the benefit of the economy in Pakistan.

The unique advantage of a high-quality global resource base as well as our well-researched knowledge bank, ACCA offers a unique and unrivalled view for budgetary considerations. My personal experience of the ACCA's Global Tax Forum representing Pakistan, working with local Chambers in Pakistan on Taxation and Economic Affairs, advising policy makers on the same matters, while also heading the Taxation Committee of ACCA Pakistan, allows me to further delve into this unique forward-thinking perspective.
That is why we begin with the **twelve global principles of fair taxation,** which can be used as the basis of taxation policy in Pakistan.

We have also continued our tradition of "**thinking ahead**" by bringing into our proposals, the latest **game-changing technologies**, their impacts on economy and taxation policy considerations. Similarly the possibilities of **CPEC** as well the impact of the technological advancements on CPEC are also covered, providing a unique insight.



We have identified that the taxation system in Pakistan is in **need of a serious overhaul**. At present, the confidence of the taxpayers and general public in the tax authorities is much less than desired. The result is a mushrooming black economy, under-declaration and tax evasion leading to losses of billions for the exchequer. Several issues contribute to this mistrust and suggestions addressing this important problem are outlined in this budget proposal document.

We have also included **inputs from our local members** working in various segments of the local economy in this budget proposal. We hope that these will provide an insightful assistance in budget preparation and policy formulation and would be pleased to continue to assist in all possible manners. Last but not the least, I'd like to thank my committee members for their efforts and appreciate the support by ACCA Pakistan officials.

Omer Zaheer Meer
Chairman ACCA Pakistan Taxation Subcommittee

ACCA Pakistan Taxation Subcommittee Members

1	Omer Zaheer Meer	Chairman
2	Abdul Wahab	Member
3	Bilal Zafar	Member
4	Junaid Abbas	Member
5	Mirza Fasihuddin Baig	Member
6	Munir Malik	Member
7	Yawar Muhammad	Member

Analysis

As tax rises up the political agenda, ACCA believes that a clear exposition of what makes an efficient and just tax system in the 21st century remains essential, and has revisited the 12 Tenets to take account of the wider tax landscape and the new pressures facing governments.

When examining tax principles, it is worth starting with a review of the famous four canons of taxation put down by Adam Smith who is generally considered (certainly in the English speaking world) to be the father of modern political economy. In *The Wealth of Nations* (1776) he argued that 'the evident justice and utility of these maxims have recommended them more or less to the attention of all nations.'

I. The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state. (EQUITY)

II. The tax which each individual is bound to pay ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person. (CERTAINTY)

III. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it. (CONVENIENCE)

IV. Every tax ought to be contrived as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state. (EFFICIENCY).

Translated to the modern era, the first maxim is in some ways, the most contentious as it appears to argue for progressive taxation, where tax is levied according to the ability to pay. On fairness grounds it is hard to argue against this and most modern tax systems follow this principle, but whereas the huge inequalities of wealth in Smith's day made such a position necessary, it is arguable that it is now a political question rather than a statement of fact.

The other maxims are less contentious. Maxim II forms our point 4 below. A society's tax system must be known and understood by all its adult members; otherwise, they cannot play their part to the full. Maxim III is hard to argue against though is not always adhered to in practice. Maxim IV forms our point 7 – though it could be said this is the area where Smith's theory is furthest from modern reality, given the costs of the state's taxation apparatus and the subsequent cost of advisers to represent taxpayers.

Given the complexity of modern economies and society, it is a challenge to apply the tenets of even the greatest thinkers to contemporary tax systems. Smith could hardly have imagined the advances in communications and technology which have led to the concept of tax competition, the level of state expenditure as a proportion of GDP in many countries or the almost universal reliance of governments on withholding of payroll and consumption taxes to collect the bulk of their revenues. Unlike Smith, ACCA does not offer the following points as universal truths, but believes that if followed by governments these twelve policies would represent the basis of effective tax systems around the world.

The 12 tenets of tax

1. A presumption to tax neutrality

Tax distortions can artificially encourage certain kinds of economic behaviours over others. Tax policies should be non-discriminatory unless part of a declared discriminatory policy, such as one which is aimed to discourage undesirable behaviours. There is a wider political question about the extent to which it is appropriate for taxation to be used as an instrument of social policy (eg penalising smoking by heavy duties, or environmental taxes to mitigate climate change). ACCA's view is that this use of tax by elected governments is legitimate but such taxes should then meet the other principles such as being transparent, simple and effective. Governments should be wary of the effect on the complexity of the tax system of too much tinkering to 'reward' certain groups of taxpayers.

There has been criticism that the global financial crisis has been exacerbated (though not caused) by policies in many tax regimes allow companies to deduct interest payments against tax but not returns on equity. As a result both leveraged buy-outs by private equity organisations and the holding of debt rather than equity by institutions has increased, which fuelled the credit boom which preceded the economic downturn. The IMF has argued[2] that governments should consider changing their rules which have effectively encouraged companies to seek finance via debt rather than equity and allowed individuals to take out larger mortgages. The IMF has voiced its fear that 'corporate level tax biases favouring debt finance including in the financial sector are pervasive, often large and hard to justify given the potential impact on financial stability.'

While the deeper issues of whether neutrality is best served by taxation of income or consumption may never be amenable to definitive resolution, ACCA argues that governments must seek to remove the distortions in their own national tax systems (which also includes, for example, tax incentives being given for businesses to structure themselves in a certain way) and work together to try to iron out the differences in tax bases which give rise to tax arbitrage. For example in the EU, there are still many barriers which frustrate the workings of the Single Market.

The sharing of best practice and knowledge between countries, of the sort envisaged by the G20 in the new era of financial regulation, could certainly be useful in the international tax world. It is important however, that this does not stretch into cartel-like behaviour which would damage the global economy.

2. Openness and transparency

Tax payers should understand what they are paying, why they are paying it, and what the benefits of paying will be. Paying tax may never be fun, but engagement with a demonstrably fair tax policy will be more palatable.

There should be openness on the application of tax policy. So-called 'stealth taxes', such as the quiet reduction of tax exemptions, and the phenomenon of 'fiscal drag', whereby personal tax thresholds are not increased in line with rising prices and incomes, thus bringing more individuals into higher-rate tax bands, cannot be justified. Tax rises should be made openly and subject to debate.

ACCA believes that most countries' tax systems suffer from political positioning in the creation of tax policy rather than taking account of what would be best for the economy. This inevitably leads to poorly thought-out legislation, instability and complications in the system. And due to the complex and specialist nature of taxation we tend not to see sufficient scrutiny of the draft legislation during the democratic processes in many regimes.

Too often, consultation processes on tax policy either do not exist or are flawed exercises where Government policy has already been decided and are carried out largely for appearances' sake. On major issues of tax policy, there should be clear consultation where the differing options are specified at the start, and properly considered with an audit trail including unambiguous minutes and written responses.

In a policy paper of March 2009, ACCA promoted the use of independent tax policy committees. The proposal was that there should be a body of experts, separate from government– which would be tasked and empowered to formulate and propose tax policy. In addition, it would also have the express remit to seek to simplify tax systems which globally are far too complex.

Government, under this model, would set the overall economic framework of the tax environment. It would need to define the public policy objectives (eg environmental, social welfare) in terms of public finance demands and fiscal targets that taxation measures were designed to achieve.

It would be of benefit to society, individuals and businesses if there was a clear link from tax take to its application – ie taxpayers could see where the money is being spent. Issues such as 'green taxes' have fallen victim to cynicism as the public has not been convinced that the revenue raised has been spent on activities to help the environment but is simply an additional revenue-raiser cloaked with an environmentally-friendly banner. While we are not convinced that such 'hypothecation' of particular taxes to specific areas of spending is practicable, we do believe that there should be greater clarity in the public finances showing expenditure projections and how these are to be financed.

2 Debt bias and other distortions: Crisis-related Issues in Tax Policy. IMF staff paper June 2009.

3. Simplification

ACCA believes that tax legislation and operations should be as simple and straightforward to understand and to comply with as possible. Complexity in the tax system is in itself a distortion of the economy, diverting productive energies into non-productive administration. Research shows that globally companies spend almost two months per year complying with tax regulations – 15 days for corporate income taxes, 21 days for labour taxes and contributions and 21 days for consumption taxes.[3]

It is essential too that the volume of legislation is kept to a minimum. Much of the increase in tax law and administration in recent years[4] is due to the number of new anti-avoidance measures introduced by tax authorities. Small businesses in particular have no time to engage in esoteric tax planning and are simply trying to cope with the volume of laws. Changes in tax law – particularly those which reverse previous tax breaks or incentives and which businesses have planned on the basis of – should be kept to an absolute minimum.

4. Certainty

Certainty is another key requirement – and an area where tax systems in many jurisdictions can be criticised in terms of certainty of outcomes or operations. Many tax systems call upon the tax payer to self assess their liability to tax, yet the wording of the legislation may make it impossible for tax payers to accurately establish their liability under the law. The UK and US authorities do not explicitly ban certain types of tax planning, which are within the law, but nonetheless take a negative view of them. (In the US these are sometimes referred to as 'abusive transactions'). Companies using these legitimate tax planning techniques may find themselves having to report to the authorities or becoming the subject of onerous tax enquiries. Often these artificial 'blocks' are used by the tax authorities as a way of 'fine-tuning' the legislation where it is unclear where the boundaries of acceptable tax planning are drawn.

This is unacceptable for companies trying to plan their business activities and who need certainty. It should always be possible for different taxpayers who look at legislation to come to the same interpretation of the law. And it should not be possible for authorities to challenge long-established practice, which businesses are accustomed to, on an obscure point of law.[5] Taxpayers must have certainty over Revenue authorities' interpretations. Authorities should establish a proper and efficient clearing mechanism for complex anti-avoidance provisions.

5. Accountability and regular review

Tax systems should have a review principle whereby tax legislation is periodically overhauled and consolidated to bring it up to date and make it easier to follow. Outdated laws should be removed. Incentives operating to promote long term aims, such as investment in green infrastructure, should have be designed to incorporate regular reviews to ensure that the aim of the legislation is being met.

There needs to be a positive prompt for justifying the existence of legislation. All anti-avoidance legislation should have sunset clauses attached to it. This will ensure that it is regularly reviewed and the need for it to remain in place is actively considered. Governments and tax authorities should devise clear metrics to gauge whether the tax system is being appropriately and sufficiently reviewed.

3 Paying Taxes, World Bank, 2008. Time recorded is in hours per year.

4 Francis Chittenden, *Perspectives on Fair Tax*, ACCA, 2008.

5 The Arctic systems case involved IT consultant Geoff Jones and his wife Diana who won a long-running legal battle with the UK tax authorities in 2007. See http://www.thisismoney.co.uk/small-business/article.html?in_article_id=422721&in_page_id=10

6. Tax policy is a percentage of GDP

ACCA accepts that the current unprecedented economic turmoil may require special measures from governments. Notwithstanding current conditions, we believe that levels of taxation should be clearly stated as a percentage of Gross Domestic Product, as far as is practicable. History has shown that too rapid a rise in the taxation burden to a level unsupportable by the economy can do immense harm and governments should monitor the rate of change in tax levels to avoid fiscal shocks in already weakened systems from proving fatal.

In countries such as the UK and US, the trend prior to the current economic conditions has been for tax revenues to rise in recent years.[6] In other countries, increasing the tax receipts to GDP ratio by tightening the tax compliance system has been a higher priority for authorities such as the International Monetary Fund.[7 8]

ACCA does not seek to enter the political debate on the appropriate level of tax and public spending. But substantial tax increases represent a significant burden on businesses and individuals and should be subject to an impact assessment before being introduced. These impact assessments should be used to challenge the need for new regulations and to establish an accurate and updated estimate of costs. Once new measures are put into place there should be a means of measuring and evaluating their impact in terms of their proclaimed public policy objectives. Government should rationalise and set a target of tax levels as a percentage of GDP as part of its economic management and then be held to account via objective measurement and variance analysis.

7. Efficiency

Tax systems should be efficient for governments in terms of their ability to secure the revenue due and to prevent tax leakage and the development of a black economy. But it should also be efficient for taxpayers in terms of their ability to comply with its requirements. It should not be forgotten that small businesses represent the bulk of economic activity in most countries and regulation can have a disproportionate effect on small firms, as the smaller the business the heavier the compliance cost. Research has shown that the smallest companies incur five times the administrative burden per employee than larger firms[9] and so every effort must be made to increase efficiency of the system. Some test questions for administrations to consider might include: Can related companies be treated as single entities for VAT and other tax purposes and so be able to make only a single tax filing? Do multi-enquiries of the same taxpayer by different parts of the tax authority take place? Are the size of tax returns and the numbers of new or revised forms which need to be completed reasonable and can the taxpayer have flexibility between completing a paper return or an electronic return?

Governments should embrace new technology where practicable to streamline the administration of the tax system. Tax is part and parcel of economic activity, and as economic activity changes so should taxation. Computerisation of banking systems, the virtualisation of trade and commerce and the move to technologies such as e-invoicing has profound implications for the measurements and remission of taxes on income and consumption in particular.

8. Tax shifting and hypothecation have a role to play

We have said above that elected governments have the right to use taxation in certain circumstances in pursuance of agreed social policies. ACCA believes one of the most important examples is to change behaviour which can damage the environment. Accountants should play an active part in efforts to reduce global carbon dioxide emissions, and the concept of 'tax shifting' by increasing carbon taxes on the usage of fossil fuels but reducing them for payroll, income or corporate taxes should be promoted.

Governments must look to use tax policy as an instrument of positive change by incentivising investment in new cleaner technologies across a wide range of industries. When combined with other tax reductions, green taxes should be seen as a positive step rather than a threat to taxpayers. Governments across the world are beginning to take significant steps to creating a low-carbon economy[10] and accountants should help to identify the emerging fiscal incentives which will be a crucial part of that.

Green taxation is one area where it is particularly important that there is international co-ordination, partly because of the global nature of the environmental problem and also to prevent polluting companies moving operations to avoid the taxes. Arbitrage opportunities here would defy the purpose of protecting the environment.

It should, however, be recognised that a significant shift in the tax base which places a great deal of reliance on green taxes at currently recognisable rates will probably prove unsustainable in the long term. This is because where such taxes are imposed on emissions and general pollution, a successful system will erode its own tax base. This is not merely theorising but a realistic medium-term prospect where the UK government, for instance, intends to reduce CO_2 emissions by 80% by 2050. Therefore, the way forward may be through a well balanced and broad tax base as well as relying more on regulation to drive down pollution.

6 *Revenue Statistics*, OECD, October 2006.

7 Statement by IMF deputy managing director Takatoshi Kato at the conclusion of a visit to Mozambique, 26 July 2005.

8 Statement by the International Monetary Fund, Delivered by Mohsin S. Khan, director, Middle East and Central Asia department, at the Pakistan Development Forum, Islamabad, 25–26 April, 2005.

9 *Businesses' Views on Red Tape*, OECD, 2001.

10 *Is the Green Economy Coming?* ACCA, February 2009.

9. Tax is a matter of national sovereignty

The globalisation of business means that each country should ensure its tax rates are competitive and its regime user-friendly. Tax is a key factor in ensuring the overall attractiveness of a location to mobile capital (businesses and individuals). Sophisticated taxpayers and investors recognise the importance of considering the underlying tax base of a country and not just the rates of tax. For instance the headline corporate tax rate could be cut but if other aspects of business tax such as capital allowances are consequently abolished then the net effect can be an increase in tax.

It is the quality of the underlying tax system – rather than a simple focus on comparative tax rates – which is of interest to companies. An ACCA study[11] of the tax systems in Hong Kong, Singapore, the US, UK, Australia and Canada in 2008 revealed that accountants believed the first two fared clearly better than the others on key issues such as tax fairness, complexity, transparency and above all, sheer volume of tax laws. Retrospective changes to tax laws and stealth taxes were also criticised and the situation was exacerbated by lack of communication and an aggressive attitude on the part of the tax authorities to taxpayers. If this perception takes hold for long enough with no effective action to ameliorate it, a country's tax system could seriously damage prospects for inward investment and competitiveness.

The problem with competition, however, can lie in very low tax rates, where offshore tax havens or flat tax systems can lead to 'beggar my neighbour' approaches, in which inward investment can be lured from one country to another and which may undermine agreed international financial regulation initiatives. They can also have regressive rather than progressive tax outcomes and so entrench wealth inequality.

It is a difficult issue to balance the rights of sovereign nations to set their own tax rates and policies with the danger of low tax regimes causing retaliatory action and trade wars. ACCA supports the principle of nations being free to determine their tax affairs within the context of a global competitive environment. And it is important that powerful, but high-tax countries (for example in 'old Europe') do not use their influence to pressurise neighbouring countries and emerging economies to give up lower-tax regimes in the name of 'harmonisation', which can be a means to cover up economic inefficiencies. The same can be said of G20 pressure on tax havens – while transparency and efforts to prevent tax evasion must be supported, actions motivated by protectionism and dislike of the downward pressure that low-tax jurisdictions engender, cannot be.

10. Tax is subject to the rule of law

'Anyone may arrange his affairs so that his taxes shall be as low as possible; he is not bound to choose that pattern which best pays the treasury. There is not even a patriotic duty to increase one's taxes. Over and over again the Courts have said that there is nothing sinister in so arranging affairs as to keep taxes as low as possible. Everyone does it, rich and poor alike and all do right, for nobody owes any public duty to pay more than the law demands: Taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant.'
Honourable Learned Hand, US Appeals Court Judge, Helvering v. Gregory, 69 F.2d 809 (1934).

'Taxes are the price we pay for a civilized society.'
Oliver Wendell Holmes Jr.

Taxpayers are under a moral obligation to pay the level of tax set by the law. There is a clear division between tax **avoidance** (or planning, or mitigation), which is legal, and tax **evasion** which is not. The former is the legal exploitation of the tax regime to one's advantage, to attempt to reduce the amount of tax that is payable by means that are within the law whilst making a full disclosure of the material information to the tax authorities. In contrast, tax evasion works outside the rules by trying to frustrate legal obligations by hiding income through nondisclosure, or improperly taking deductions that one is not qualified for.

But governments increasingly try to blur the distinction between the two by using phrases such as 'unacceptable tax avoidance' which is not helpful to taxpayers or their advisers. Tax law must be clear and certain and it should be remembered that businesses will look to minimise tax impact as a part of their normal commercial activity. Tax is a business cost like any other and company directors typically have a fiduciary duty to run the business in the most cost effective manner.

As the case above reminds us, it is not unethical to minimise ones taxes. But while most businesses try only to comply with the law, there have been many cases of convoluted tax planning schemes which are designed not for any proper business purpose but to exploit loopholes in the law and avoid its spirit. ACCA does not support this artificial activity, which could be considered the equivalent of the creation of some of the extremely complex financial products, designed to get round banking regulation and which have had such a disastrous effect on banks.[12] Such actions, which may generate short-term financial advantage at the cost of long-term value, cannot be supported.

11 Francis Chittenden and Hilary Foster, *Perspectives on Fair Tax*, ACCA, 2008.

12 Lord Turner, chairman of the UK City watchdog, the Financial Services Authority, said in his landmark report on regulation, referred to this as 'adventures in risky proprietary trading activities of little social value'.

11. Respect for human rights

Taxpayers have rights as well as responsibilities. They are obliged to pay their tax due, in full and on time, as this is the only way governments can generate the funding to provide the public services everyone depends on, and in this sense tax is part of the social contract of any civilised society.

But the huge inequality in resources and power between governments and individual taxpayers places a responsibility on states not to impose their will in the field of taxation in an arbitrary or vexatious way. For instance the incorporation in to UK law since the 2nd October 2000 of the European Human Rights Act has empowered tax payers to challenge pernicious tax law in cases where it could be argued there is fundamental uncertainty or unjustified additional cost of operating in one particular business vehicle rather than another.

A similar approach throughout tax jurisdictions should become the norm.

12. Avoidance of double taxation

An essential principle of tax law must be that income should be subject to tax only once. This applies both to direct tax where an individual or business should suffer tax once and consumption taxes such as VAT where input tax recovery should be available at each stage of the transaction chain and only the end user, in the form of a private individual, ultimately pays the tax.

In the case of direct taxes there needs to be an efficient and effective mechanism available in all countries to give relief to a company which has already paid tax in another jurisdiction before subjecting that same income, in whole or in part, to taxation. In practice, too many countries do not consider it an important enough priority to seek to offer this full relief for tax suffered in another jurisdiction and this aspect of the global fiscal regime is an additional cost burden on multinational businesses.

The 'arm's length' principle whereby tax authorities treat transactions between connected parties by reference to the amount of profit that would have arisen if the same transactions had been executed by unconnected parties is a sensible and long-established convention which should be the basis of international tax affairs.

Sales tax regimes are meant to be on the end user only but all too often Governments place restrictions or long delays on full input tax recovery and this again is creating unfair costs on businesses. If full recovery is not facilitated then it is unjust to charge the full VAT rate on the end user and only adds to creating a less efficient business environment.

4. Broadening of Tax Base

This is a serious concern as without broadening the tax base, the existing small taxpayer base for direct taxation can only bear the constantly increasing burden of taxation to a limited extent with serious ramifications for business competitiveness.

Reduction in tax rates to single digits while focusing on broadening the tax base making the cost of tax avoidance along-with the penalties non-attractive. This, coupled with structural reforms can assist in expanding the tax base.

Similarly, salaried class should be given relief to increase the net national savings and provide impetus to economy. These measures will be more effective collectively.

Increased impetus on Direct Taxation:
To reduce the reliance on indirect taxes which normally lead to inflation, uncompetitive businesses on a global stage and a reduction in real GDP growth? As compared to developed economies, the South Asian region has a serious challenge due to the lack of documented economy and resulting tax evasion owing to black money. As per various studies, the tax potential of Pakistan is at Least twice the current level if the focus is shifted to lower tax rate, broadening of tax base and reduced focus on indirect taxes as a proportion of total revenue.

Volume over Margin – Low number of filers:

Pakistan has one of the highest rates of the indirect as well as direct taxes in the region. The high cost of taxation contributes to a culture of tax evasion where a few have to bear a heavy taxation burden.

Out of a population of over 210 million, only 1.3 million filed their income tax returns in the last tax year. Out of these over 0.5 million were NIL returns as per the Honourable Prime Minister.

Utilization of NADRA database:

NADRA database should be integrated with FBR's databases to identify the individuals living beyond their declared means and to bring them under the tax net.

Utilization of WHT data:

The withholding taxes data can be analysed to focus on non-filers paying higher rates of withholding taxes and to bring them under the formal tax net considering the amount of taxes already deducted from them.

Utilization of database of other tax authorities:

FBR should have integrated access to the databases of other national/ provincial tax authorities or at least be able to get information to utilize for identifying high net worth and otherwise taxable individuals and entities to bring them under the tax net.

Formalized Asset Valuations:

There is a general tendency to undervalue assets leading to tax avoidance. To curb this, FBR can form desks to declare formalized asset valuations in line with the fair market values or a policy on similar lines can be introduced by the Government to discourage under-valued asset declarations.

CNIC should be made the NTN and the requirement of all with taxable income to file Income Tax Returns must be enforced. However an important concern to consider would be that using the same identifier for tax as other civic rights/responsibilities, there may be a risk of the identity being used to generate a false tax refund which is then paid to the impersonator. The system needs to have safeguards in place to prevent this.

While it was declared that CNIC would be the NTN, there have still been many issues pending. With an extensive database such as the NADRA's CNIC records which is also a necessity for businesses and most of the working class, it should be utilized intelligently along with the use of other measures and databases to expand the tax base.

5. Structural Reforms

- A **single tax return** for all taxation affairs of a taxpayer which all authorities can utilize to obtain the relevant data.

- **Harmonization of Federal-Provincial taxation laws** in the country e.g. jurisdiction issues, differences in tax rates, differences in tax treatments etc.
- **Resolving issues within IRIS** to make it more user friendly. The current IRIS portal has several issues including crashing during peak times, non-compatibility with various common browsers and potential for improving ease of use. The current returns especially the income tax returns are often pointed out as too complex to be filled by even accountants not specializing in taxation. The aim should be to simplify the processes as well as make the portal user friendly for the common people so that maximum compliance can be achieved.
- **Integration** of Federal and Provincial Revenue Authorities' systems.

- **Reducing the discretionary powers** vested in FBR officials and shifting towards an objective criterion based approach.

Comparative Budgetary Position

Expenditure

	2016-17 (R)		2017-18 (B)	
	PKR'tr	%	PKR'tr	%
MarkUp Payments	1.36	28%	1.36	27%
Pension	0.25	5%	0.25	5%
Defence Affairs & Services	0.84	17%	0.92	18%
Grants & Transfers	0.38	8%	0.43	8%
Subsidies	0.17	3%	0.14	3%
Running of Civil Government	0.40	8%	0.38	7%
Foreign Loan Repayment	0.51	10%	0.29	6%
Current Expenditure	**3.90**	**81%**	**3.76**	**74%**
Federal PSDP	0.72	15%	1.00	20%
Dev Expenditure outside PSDP	0.13	3%	0.15	3%
Dev Loans and Grant to Provinces	0.09	2%	0.19	4%
Development Expenditure	**0.94**	**19%**	**1.34**	**26%**
Total Expenditure	**4.84**	**100%**	**5.10**	**100%**

- Developing the existing **policy of differential tax treatments and incentives for filers** while penalizing non-filers.

- **Introducing impact on economic sectors** (GDP development) along with collections target as performance evaluation criteria for FBR functionaries.

- Ensuring **time limits** adherence as specified in the laws and rules particularly pertaining to refund matters.

- **Facilitating the tax payers** meaning making life easier for them with more efficient/effective administration as well as user friendly processes and provisions in order to ensure maximum compliance and an increased trust in the tax apparatus leading to a broader tax base.

Governance & confidence building

Policy Formulation | Tax Administration | Appeals / Dispute Resolutions

- Resolving the **<u>outstanding refunds issue</u>** positively.
- Introducing confidence by establishing a **<u>swift response complaint resolution cell</u>** to deal with corruption and harassment of tax payers.
- Ensuring **<u>no post remains vacant for more than two weeks</u>** to avoid delays in resolving tax-payers issues arising out of transfers, postings and additional charges, etc.
- Appointing **<u>independent officials as Commissioner Appeals</u>** ideally from the judicial service.
- **<u>Transferring both the Appellate Tribunal Inland Revenue and the Commissioner Appeals under the control of the respective High Courts.</u>**
- **<u>Tax Amnesties</u>** without proper penal clauses had been a failure. With the strengthening of OECD, they should be done away with and focus should instead be shifted on using the organization's platform to retrieve necessary information and ensure proper enforcement of applicable laws and regulations.
- Hiring and training of adequately qualified staff with ongoing **<u>capacity building</u>** should be focused on to ensure efficient and productive results from the tax apparatus.
- Effective enforcement should be ensured by working on maximum **<u>automation of the taxation system</u>**.

Comparative Budgetary Position

Resources

	2016-17 (R)		2017-18 (B)	
	PKR'tr	%	PKR'tr	%
Gross Revenue Receipts	4.74	95%	5.31	103%
Less Provincial Share in Taxes	(2.12)	-43%	(2.38)	-46%
Net Revenue Receipt	2.62	53%	2.93	57%
Capital Receipts	0.32	7%	0.64	12%
Estimated Provincial Surplus	0.29	6%	0.35	7%
Internal Resources	3.23	65%	3.91	76%
External Resources	1.00	21%	0.84	16%
Privatization Proceeds	0.02	0%	0.05	1%
Total Internal & External Resources	4.10	85%	4.71	92%
Borrowing	0.74	15%	0.39	8%
Total Resources	4.84	100%	5.10	100%

6. Direct Tax

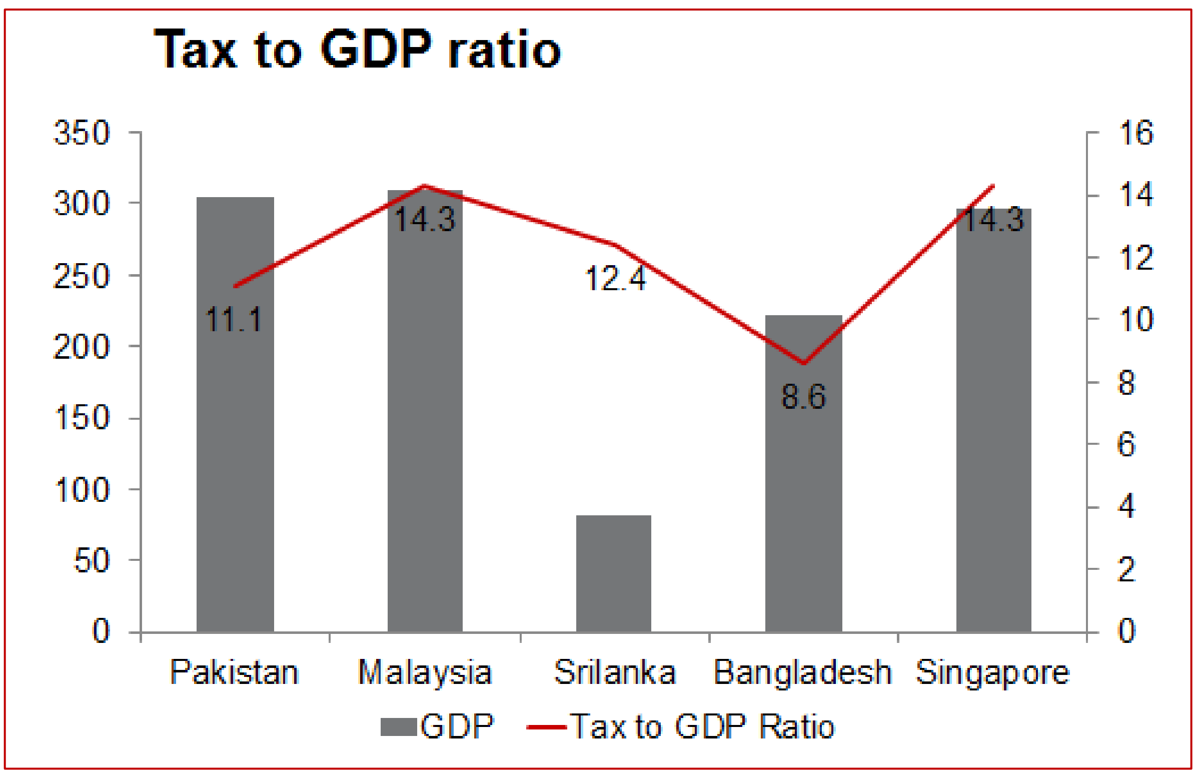
CORPORATE TAX RATE SHOULD BE REDUCED:

Pakistan's tax-to-GDP ratio is one of the lowest in the region. While, we appreciate the reduction in Corporate Tax Rate, it's still very high at 30%. Comparatives from some of the regional countries are as below:

Hence, in order to attract FDI and facilitate the local business eco-system the corporate tax rate should be reduced from the current level to the range of 20%-25%.

Tax Rates for Individuals should be reduced:

The current slabs with the upper slab being 30% are very high and place undue burden



on the growing middle and upper-middle class of the country.

The rates should be reduced and the ranges should be widened with the tax exempt limit also recommended to be increased from the current level of PKR. 400,000/- which is PKR 33,333/- approximately and outdated compared to the current inflation level.

Coupled with the other measures proposed, this can result in economic impetus for the country and an improvement in the compliance.

Inter Corporate Dividends should be tax exempt:

This was previously withdrawn and results in higher tax incidence without a "real" outflow of resources from the group. To attract the investments and encourage corporate sector the previously withdrawn exemption should be reinstated U/S 59B.

Section 111 (4) regarding Foreign Exchange Remitted from Outside Pakistan:

It should be amended to:

any amount of foreign exchange remitted from outside Pakistan through normal banking channels that is encashed into rupees by a scheduled bank and a certificate from such bank is produced to that effect and a declaration along-with evidence of the source of funds.

This will continue to promote the inflow of foreign exchange remittances towards the country while stopping the misuse of the provision to whiten/launder black monies and de-incentivizing genuine tax paying businesses.

This way, the "non-enquiry" clause which has been extensively abused, will be abolished while still providing the tax relief for foreign exchange remittance.

Section 113 regarding Minimum Tax:

The minimum tax on turnover is charged irrespective of the net profit or loss. This often gives rise to a situation where businesses end up paying double taxes on their revenues and profits as well as loss making businesses facing additional cash-flow pressures by paying this tax. They're distortive, and in particular bad for start-ups because of the serious cash flow implications.

The current rate of 1.25% applicable generally except for a few sectors should be brought down to 0.4%.

The now deleted exception in case of a gross loss needs to be reinstated in line with the principles of natural justice and equity.

This will facilitate the business eco-system contributing to a growth in GPD which can lead to increased revenue collections for the treasury.

Section 138 & 140 regarding Recovery of Tax through Attachment of Bank Accounts and/or Property or Arrest:

Currently, the allowance for the commissioner to attach the property of the taxpayer before expiry of notice period on "satisfaction" of the commissioner regarding possible removal, cancellation or disposal of attachable property is misused in many cases to harass the businesses. This change can bring an end to this, increase taxpayers' trust in the tax apparatus and improve the ease of doing business in the country.

Any such attachment of any movable/ immovable property before expiry of the notice period may only be authorized by the Commissioner in the presence of objective evidence, which should be shared with the taxpayer.

Section 152 regarding Payments to non-residents:

Section 153(4) empowers the Commissioner Inland Revenue for issuing Exemption Certificates in cases where the underlying payment is not chargeable to tax due to various reasons.

This provision should also be inserted in Section 152 to facilitate the business with non-residents companies/businesses where the underlying payments are not chargeable to taxes as the current backlog of refunds creates undue stresses on businesses.

Section 153 regarding Minimum Tax for Providing or Rendering Services:

In the presence of Section 113 already dealing with minimum tax on turnover, the minimum tax should not be applicable on companies providing services. These should be subject to the normal tax regime (by reinstating the deleted clause 79, Part IV of Second Schedule). As a minimum, this minimum tax should be made adjustable against future tax liabilities.

Service sector has been one of the largest growing employer and contributing to national economy as well as the treasury and most of the segments of this sector does not enjoy very lucrative margins. The current provisions have resulted in many service sector businesses shutting down due to cash-flow challenges and more taxation than their profits.

The proposed amendment should help expand the sector leading to improved revenue collections in the long term.

Section 170 regarding Refunds:

Sub section (4) states The Commissioner shall, within 2[sixty] days of receipt of a refund application under sub-section (1), serve on the person applying for the refund an order in writing of the decision 3[after providing the taxpayer an opportunity of being heard].

However the issue of not following the time limit set in the law has been resulting in delayed refunds and a deterioration of trust in the taxation apparatus while resulting in serious cash-flow challenges for genuine claimants resulting in loss to economy and exchequer through lost opportunities for the economy.

It should be amended to add:

after the lapse of the above-mentioned time period, the refund application shall be deemed to be successful.

Section 177 regarding Audit:

It should be amended to clarify that:

the powers can be exercised in cases of existing audits or on the basis of precise information which should be disclosed in the notice issued and not as a tool for audit selection.

This is to remove the practical problem of some commissioners using the powers under this section as an audit selection tool in addition to the annual audit cases selection already done under a different system by the FBR.

Section 214 A regarding Condonation of Time Limit:

It should be amended to add that:

the condonation should not be exercised to be detrimental to the taxpayers.

This is in line with the principles of fair and equitable taxation.

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7. Indirect Tax

SALES TAX RATE SHOULD BE REDUCED:

The existing rate of Sales Tax at 17% is one of the highest in the region with an average of around 12% in Asia (15% in India and Bangladesh, 10% in Indonesia and just 6% in Malaysia).

Sales Tax should be used to broaden the tax base and not as a replacement of direct taxation.

In order to avoid the net negative costs for the economy, the rate should be brought down to single digit in a phased manner starting with a proposed reduction to 14%.

approximately **90%** of revenue is generated through indirect taxes and withholding tax regimes

Also, standardizing the applicable rates while also reducing them could facilitate the businesses while also increasing the tax revenues simultaneously.

HARMONIZATION OF INTER-PROVINCIAL AND FEDERAL-PROVINCIAL TAXATION - AVOIDING DOUBLE TAXATION:

The conflict between various provincial revenue authorities and the federation is resulting in double taxation of services owing to the classification and jurisdiction disputes.

Similarly, the lack of inter-provincial harmonization also results in double taxation of services owing to the classification and jurisdiction disputes.

These issues should be resolved to create a business-friendly environment and facilitate the tax-payers.

Point of origination or deliverance of services can be agreed upon by all revenue authorities as the basis of classification and the resulting jurisdiction to resolve the major inconvenience to the taxpayers.

ADJUSTABLE INPUT TAX U/S 8-B:

With the introduction of the STRIVE system resulting online matching of invoices, the chances of sales tax fraud and/or error have been minimized.

Therefore the current restriction of limiting the input tax adjustment to 90% (ninety percent) of the output tax is outdated and needs to be abolished.

This will be in line with the principles of fairness, equity and justice for all and help restore the confidence of businesses.

REVISION OF SALES TAX RETURN:

This should be made easy and automated as with the STRIVE system in place, chance of tax fraud are minimized to the maximum possible extent as claimed by FBR.

APPEALS U/S 45-B:

In line with the principles of fairness, equity and justice for all, the appeals should be heard by a person not under the administrative jurisdiction/influence of FBR.

TIMELY UPDATED CUSTOMS VALUES:

Standard and regularly updated customs values should be used by Customs to avoid mis-declarations.

FED ON SERVICES:

Post 18th amendment, the powers to levy and administer Sales Tax on services has been transferred to the provinces.

Hence, FED on any such remaining services should be withdrawn.

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PAST REFUNDS ISSUE:

To solve the liquidity crisis arising out of the blocked refunds of over Rs.400 billion as per business community, these should be made into discounted instruments backed by Government's guarantee to be used as collateral or traded at discounts with the banks.

This will resolve the ongoing refunds crisis without creating extraordinary pressure on revenue collection by the FBR.

SAVINGS TO GDP RATIO:

Once again the ratio of savings to GDP has declined and it is even less than half of that in India.

Government should encourage savings by offering better returns on its' saving schemes as well as ensuring a conducive business eco-system.

CURRENT ACCOUNT DEFICIT:

Tangible measures must be taken to decrease the Import burden.

Heavy duties should be levied on non-essential imports like expensive electronics, Cars & Luxury items. In addition incentives should be announced for local industry to encourage use of domestic products as well as increasing the exports especially with a focus on neighbouring markets

AGRICULTURAL SECTOR:

Agricultural sector needs to be re-evaluated. Being an Agricultural country its GDP share must be according to its volume. Currently its share in GDP is 24% while it has the potential to reach up to 55%.

Large agricultural landowners should be taxed at minimal rates i.e. 7%. The revenue generated through this should be used to subsidize seeds, fertilizers, water, electricity, fuel, etc. for the small farmers.

Smuggling of agriculture produce of Pakistan should be controlled with strong law enforcement. Cheap and low quality imports of agri products should be regulated as it puts the local growers at a disadvantage.

HUMAN RESOURCE DEVELOPMENT:

For Pakistan, a country of 220 million people, human capital is a huge resource in new era, but unfortunately due to inadequately developed and implemented and poor policies we are unable to convert this power in to workable force, un-employment has increased to almost 6 % and over 4 million people are unemployed.

Keeping in view the above indicators govt. needs to encourage Services sectors, new industries and agriculture. Banking sector should be used to incentivize and promote a culture of entrepreneurship.

Incentives must be announced for Services sectors particularly Telecom, home based industries, Young entrepreneurship programs with special focus on Women.

9. Latest Game-Changing Technologies

In addition to the above mentioned challenges and proposals, these are times of exciting innovations and technological advancements which need to be addressed to facilitate the business eco-system in Pakistan while simultaneously ensuring the due share of the treasury is also recovered without compromising the economic potential stemming from these latest technologies. It is time that we need to address some vital questions such as:

- What are these technologies?
- How can they contribute to Pakistan's economy and what is their current impact, if any?
- How are they been taxed elsewhere and how to tax them locally?
- What laws need to be enacted and/or amended?

Some of the latest technological advancements requiring proper policies and inclusion within the scope of taxation are as below:

- "**Artificial Intelligence (AI)** is the broader concept of machines being able to carry out tasks in a way that we would consider "smart".
- "**Machine Learning** is a current application of AI based around the idea that we should really just be able to give machines access to data and let them learn for themselves."
- **Big Data** refers to extremely large data sets that may be analysed computationally to reveal patterns, trends, and associations, especially relating to human behaviour and interactions.
- A lot of investment is being made in managing and maintaining big data. It has the potential to change the economic landscape of the country.

- Just like AI and Machine Learning, the possibilities are endless.

- **BlockChain** is a continuously growing list of records, called blocks, which are linked and secured using cryptography. Each block typically contains a cryptographic hash of the previous block, a timestamp and transaction data. By design, a **blockchain** is inherently resistant to modification of the data.

- In other words it is a digital, decentralized ledger that keeps a record of all transactions that take place across a peer-to-peer network.

- It offers transparency, security and efficiency. Blockchain is already been used around the world for several purposes and is been seen as the **"Internet" of this century**. The applications particularly in the public sector are amazingly productive.

- **Crypto-currency** is a digital asset designed to work as a medium of exchange that uses cryptography to secure its transactions, to control the creation of additional units, and to verify the transfer of assets. It is based on blockchain technology and often referred to as a showcase of the same.

The incentives of a super quick, cheap and highly secure medium of exchange has excited many.

Crypto-currency aims to cut the financial middle-man, delays and costs involved in the traditional banking with the fiat (Government backed paper based) currencies.

As with any ground-breaking technology, the opinions have been divided about the crypto-currency as being a currency (medium of exchange) or an asset (store of value) or both.
While some countries have encouraged it, others have not adopted the concept.

Maggie McGhee, director of Professional Insights at ACCA says:

'Bitcoin has at least three dimensions that are causes for concern. Firstly, its pseudonymous nature means that while one may identify the address a given payment goes to, it is not possible to confirm the identity of the underlying beneficiary.

'This is an obvious risk for money laundering, terrorist financing and the funding of other types of illegal activities. Secondly, its high volatility makes it inherently risky and unstable. Thirdly, it is funding a speculative bubble in other areas like Initial Coin Offerings (ICOs) with speculators chasing poorly formed business propositions.

The global accountancy profession has an important role to play in enabling stable economies and secure societies where consumers are not exploited. As new technologies become adopted, it is vital that professional accountants develop their digital understanding alongside their ethical responsibilities to flag areas of concern.

‘In that context, ACCA supports a close relationship between regulators and the accountancy profession to ensure that a robust regulatory approach is crafted, and refined as developments emerge, so that it is fit-for-purpose in a digital age.

With Pakistan’s ever increasing debt problem, lack of foreign investments, huge un-mined reserves of natural resources, the advent of CPEC and low value of national currency, a national crypto-currency may offer substantial benefits.

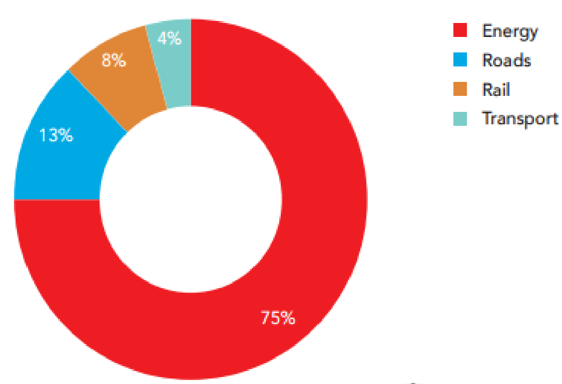
10. CPEC

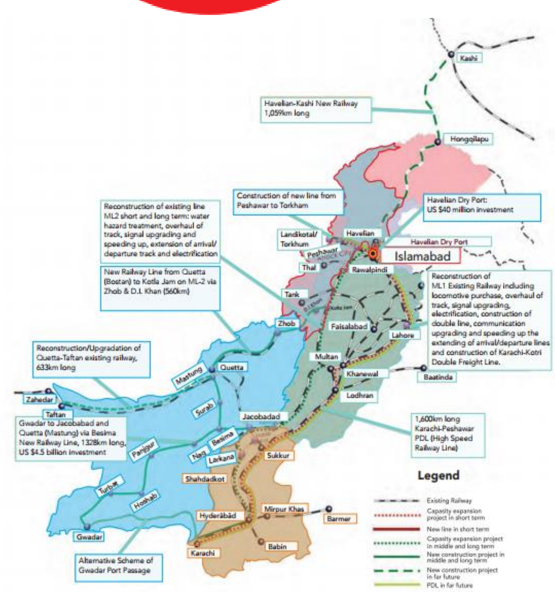
- CPEC is the flagship project of the Chinese Belt & Road Initiative.
- With over $69 billion investment in road infrastructure, energy, railways, communications, etc projects in Pakistan, it's worth more than the foreign investment in Pakistan for past several decades.
- The establishment of economic zones along the CPEC route can generate some very exciting economic opportunities.

Among the six corridors, the China– Pakistan Economic Corridor (CPEC) has achieved the fastest and most effective progress:

Highlights from the ACCA's research on CPEC:

1: CPEC investment breakdown, USD46bn





- **700K -800K +** new jobs shall be created
- Addition of **12,000 km – 15,000 km** of roads
- **Constructions & Infrastructure** industry will benefit
- **800,000** additional cars are required
- Banking loan shall grow **2%-3% per year**
- Projects worth over **USD 30b will be insured** locally and internationally
- **Goods transportation businesses** are expected to grow
- Sports goods, leather, handmade products and food (meat and fruit) **export to China**

- CPEC has been termed as the ground-breaking initiative for not just Pakistan but the entire region.

- CPEC projects should involve experts and practitioners in Pakistan to ensure most benefits to the national economy.

- The economic zones should require at least a material stake by local businesses, which can be funded by the finance industry. This can be made attractive by introducing benefits and/or lower tax rates (when they become applicable) for businesses operating in the zones.
- Information about CPEC including processes systems incentives requirements etc should be publically shared and informational workshops especially for businesses should be held on a regular basis in collaboration with the private sector.

- ACCA is prepared to collaborate with regulatory authorities and other partner organizations to assist by sharing its expertise and global knowledge base in this regard. It is worth pointing out here that ACCA has presence in 23 of the 65 countries connected by Belt and Road Initiative (BRI). This places ACCA in a unique position to capitalize on its stakeholder contacts to connect and facilitate businesses.

- In addition, future challenges also need to be addressed. The technologies discussed in the aforementioned section will also have an impact on CPEC.

  - It is possible that global businesses transiting through CPEC may be executing their contracts in block-chain based databases.

  - At least some of the payments may be made in crypto-currencies.

  - AI and Machine Learning maybe utilized by border agencies and will help increase the efficiencies.

  - Big-Data analytics will likely be used extensively by various corporations as well as Government Agencies to analyse various trends and capitalize on that by improving the systems, processes and procedures to enhance the ease of doing business.

- This renders the question that whether we just want CPEC to be a transit route with some economic zones with payments, contracts and ancillary services taking place elsewhere or are we ready to address these in order to capitalize on these exciting business opportunities.

- Similarly what taxation model should be used for these and at what rates, needs to be addressed.

ACCA Pakistan's has prepared detailed proposals on these considering the current global practices, developing trends and the local challenges for Pakistan.

For more details on CPEC, Crypto Currencies and Blockchain technologies ACCA has produced detailed reports which are available on our website at the below mentioned links:

The Economic Benefits of the Modern Silk Road
http://www.accaglobal.com/uk/en/technical-activities/technical-resources-search/2017/october/the-economic-benefits-of-the-modern-silk-road.html

Risks of cryptocurrencies like bitcoin must be better understood by accountancy profession
http://www.accaglobal.com/vn/en/news/2018/march/risk-cryptocurrencies.html

ICOs: real deal or token gesture?
http://www.accaglobal.com/gb/en/professional-insights/technology/ICOs-real-deal-or-token-gesture.html

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