

Zero-rating regime withdrawal commitment to IMF

The government has given the commitment of withdrawing zero-rating regime for the five exports-oriented sectors to the International Monetary Fund (IMF). This was revealed by Adviser to Prime Minister on Commerce and Textile Abdul Razak Dawood while briefing the National Assembly Standing Committee on Commerce and Textile, which met with Naveed Qamar in the chair here on Tuesday.

The committee strongly opposed the proposed imposition of sales tax on domestic sale of export sectors and recommended the government to go for a middle way to save the industry from total collapse as well as unemployment to get a win-win situation for all.

However, representatives of the five zero-rated sectors claimed that IMF Resident Representative in Pakistan in a recent meeting with them negated the government's stance while saying that no such commitment has been taken from the government.

The Commerce Division informed the committee that according to Federal Board of Revenue (FBR), zero-rating scheme has been grossly misused by the business community. The sales tax exempted raw material is being used in other sectors which are not part of zero-rating or export-oriented. Moreover, business community is not paying full tax on their local sale, which is unfair with the country.

The advisor admitted that the imposition of 17 percent sales tax would create problems for the industry, and said that it may result in fake invoices as was observed in the past. Replying to a question, Dawood said that 17 percent sales tax should not be implemented at once. "We always went for revenue but not for industrial growth," he added.

Dawood further said that Pakistan is heavily relying on customs duty for revenue generation and it accounts for 42 percent compared to 7-8 percent in other countries as it is an easy way of collection for the Federal Board of Revenue (FBR).

He further said that exports for the current fiscal year would remain almost the same as of the previous year; however, imports declined by around \$5.5 billion. He said that Finance Ministry informed them that the IMF had asked for elimination of zero-rating regime and they have given them the commitment to withdraw the zero-rated status.

Dawood further said that he has been against the withdrawal of zero-rating since the first day; however FBR has opposed the proposal. He further said that FBR wants to clear all the flaws in the system of 40 years in 40 days. "If you have to pay back the sales tax refund, why you collect it," Dawood asked.

According to the Commerce Division presentation, payment of sales tax refunds has always remained a problem for exporters. Since it creates liquidity problems for the exporters, the government in 2005 introduced zero-rating facility for the export-oriented industrial sectors namely, textile, carpets, sports goods, surgical and leather to be solve the issue.

The facility was based upon "no payment no refund" principle and provides exemption from sale tax to the abovementioned sectors on raw material used in the manufacturing of abovementioned sectors.

In the Finance Bill 2019, the government has withdrawn the facility to meet the revenue targets. According to FBR, the scheme has been grossly misused by the business community.

The business community is not paying full tax on their local sale, which is unfair with the country. As informed by FBR, local sales of these sectors is Rs 1,200 billion and the business community is paying only Rs 6-8 million of taxes on local sales.

The FBR has suggested to ensure that there would be no difficulty in payment of refunds and it would announce a complete plan for smooth payments on the pattern of China and Bangladesh to minimise the period of refund payment. The FBR is also working on payment of refunds just after export realisation.

As per business community, the facility of zero-rating had not only solved the problems of sales tax refunds but had also generated considerable revenue and stopped fake refunds claims. Discontinuation of the facility would create additional revenue, but at the same time it would create liquidity problem for the exporters as FBR has no speedy mechanism to release the sales tax refunds.

Further, as the government is unable to refund the amount of sales tax collected from the export sector, there should be no sales tax on exports and even the current two percent sales tax should be withdrawn and the "no payment no refund regime" be revived, as globally there is no tax on export sectors and export goods are manufactured for the foreigners.

The Commerce Division further informed the committee that according to All Pakistan Textile Mills Association (APTMA), total production value of the zero-rated sectors is \$18 billion out of which 70 percent or \$13 billion is exported. Domestic sales are of \$5 billion on which total tax for 2019-2020 at exchange rate of Rs 150 will be Rs 37 billion. They have proposed that FBR may manage its targets by collecting sales tax on the sale in domestic market. In the past, it could not make it possible to collect sales tax on domestic sales.

The committee was further informed that sales tax on imported raw material for the five zero-rated sectors amounts to \$750 million to \$850 million. It means that the discontinuation of this facility would create additional revenue amounting to \$850 million.

Moreover, Rs 180 billion more would be collected if the business community pays complete tax on their local sales. Collectively, this amount definitely will contribute to meeting the target of FBR.

On the other hand, it would create a liquidity problem if FBR could not manage speedy payment refund mechanism for exporters that would create problems for exporters as they would not be able to sell their products aggressively in the international markets. Moreover, high prices of electricity and gas would also make the Pakistani products uncompetitive in the international market, maintained the Commerce Division. The zero-rating facility is linked with liquidity problem for the business community.

The Commerce Division tabled several proposals including that facility of zero rating may be done away with as revenue is needed for the country, the FBR may develop a speedy mechanism for payments of refunds to control the liquidity problem of the business community, all the raw materials

used in the domestic industry may be exempted from all types of tariffs irrespective of specific sector as envisaged in the National Tariff Policy and FBR may chalk out an effective mechanism to avoid tax evasion and take strict action against the business community members who are not paying tax on local sales.

Chief Coordinator of five zero-rated sectors Javed Bilwani said that they wanted continuation of sales tax zero-rating regime under SRO No 1125. He added that the industry's refunds have been stuck with FBR for years, adding that he does not think there can be any improvement in the refund system. He further said that GST will destroy the industry including Sialkot-based small and medium industry.

He said that government's proposal to discontinue zero-rating scheme by abolishing SRO No 1125 will be a deadly blow on exporters' liquidity which will create hardships for exporters, eliminate SMEs and exports. To save the export sector, zero-rated scheme of "no payment no refund" of sales tax must be continued. He maintained that the wholesale and retail sectors are also not registered. "We are of the same opinion that the government should get tax from goods sold in the local market. We feel that it should be collected by registering wholesale and retail sectors. Disturbing the manufacturing sector for mere 20 percent would not be a wise decision," said Bilwani.

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