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Finance Act 2020, Lack of initiatives & innovations — I

The adoption of the Finance Bill 2020 on June 29, 2020 and exceeding the target by the Federal Board of Revenue (FBR) for fiscal year (FY) 2019-20 was an achievement of the coalition Government of Pakistan Tehreek-i-Insaf (PTI) considering stern resistance from the opposition and working under extraordinary unfavourable circumstances of continuous onslaught of Covid-19 endemic. Indeed, it is an achievement worth recognition that FBR exceeded collection target of Rs 3908 billion by Rs 92 billion, collecting Rs 4126 billion gross and Rs 4000 billion net—first ever in its history—when businesses were closed, imports largely suspended and duties were slashed to ease out business houses. FBR paid Rs.122 billion refunds of sales tax and income tax against last year's figure of Rs. 53 billion—Rs 69 billion more (increase of 57%).

In FY 2019-20, FBR paid Rs 95 billion sales tax refunds against Rs 21 billion last year, showing an increase of Rs 74 billion. This is paid from its own collection. Additionally, an amount of Rs 70 billion paid in respect of long-outstanding refunds through technical supplementary grant (TSG) by the government. These refunds were blocked/consumed by the government of Pakistan Muslim League (Nawaz)—PMLN. Thus, it is unfair to say that FBR's collection is overstated by paying through TSG. Factually, these reflect inflated figures by PMLN to years which these relate! With industry at a halt, payment to business community from TSG was for primarily for payment of salaries. The most admirable step was strictly adhering to collection of due tax only and taking no advances. It is reported: "The new Member Operations FBR, Mohammad Ashfaq, had also given instructions to his team not to force the taxpayers to pay taxes in advance. While breaking from the past practice, the FBR also paid tax refunds even on the last day of the fiscal year". The collection figures (see Table) reflect bona fide net tax collection, registering a growth of 4.3% over last year when growth was –(0.4). It is an extraordinary feat by FBR when the country was under strict lockdown for over a month during April/May 2020.

It is true that the coalition Government of PTI failed to give tax relief to the salaried class, especially with no raise in the pay and pension of government employees, substantial reduction in income tax and sales tax rates for businesses, removing and/or deferment of withholding and advance taxes so that they can survive and revive in difficult times. On the contrary, FBR proposed luxury tax on the rich owners of farmhouses and palatial bungalows in Islamabad Capital Territory (ICT) but it was withdrawn after rich legislators reportedly opposed it. FBR authorities deserve appreciation for proposing a progressive tax. It exposes the tall claims of PTI that it came to power to ensure socio-economic justice and establishment of an egalitarian society!

Table: FBR's collection for fiscal year 2018-19 & 2019-20

Collection (Rs. in million)

Tax Head	FY 2019-20			FY 2018-19			Growth	
	Gross	Refund	Net	Gross	Refund	Net	Absolute	%age
Income tax	1,525,502	27,635	1,497,867	1,456,600	32,290	1,424,310	73,557	5.2
Sales tax	1,688,620	95,135	1,593,485	1,482,699	21,083	1,461,616	131,869	9.0

FED 257,590 25 257,565 240,972 45 240,927 16,638 6.9

Customs 634,868 12,026 622,842 695,225 15,585 679,640 (56,798) (8.4)

Total 4,106,580 134,819 3,971,760 3,875,496 69,003 3,806,493 165,267 4.3

Book Adjustment* 19,000 - 19,000 20,000 - 20,000 (1,000) (5.0)

Grand Total 4,125,580 134,819 3,990,760 3,895,496 69,003 3,826,493 164,267 4.3

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*Provisional

Source: PRAL as on July 1, 2020 at 4pm

Compliance cost has also been increased in the Finance Act 2020 by reverting to quarterly statements instead of half-yearly. Shockingly, the power of real-time data access or otherwise is given to FBR under Income Tax Ordinance, 2001, Sales Tax Act, 1990 and Federal Excise Act, 2005 in the absence of Personal Data Protection Law in the country and no safeguards against hacking and leakages as well as abuse for self-aggrandizement though this issue was raised in the Finance Bill and data privacy, The News, June 21, 2020.

The PTI Government could have done a number of positive things for resource mobilisation—tax and non-tax—as well as reducing cost of doing business in Budget for fiscal year 2020-21 but it decided to substantially increase prices of petroleum products on June 26, 2020 with disastrous consequences (Unconstitutional levy, The News, June 30, 2020 and The POL bomb, Business Recorder, April 5, 2019). It showed no will to reduce exemptions/concessions/waivers/immunities causing tax expenditure of Rs 1.5 trillion in the just ended fiscal year 2019-2020 as per own admission in Annex-II appended to Economic Survey 2019-20 [see a detailed discussion in Analysing 'tax expenditure', Business Recorder, June 26, 2020]. In fact, more exemptions and benefits are given to the influential, whereas proudly claiming "no new tax" levied showing total apathy towards the weaker sections of society and small and medium enterprises (SMEs) facing the unbearable economic toll of Covid-19 outbreak/lockdown by reducing the incidence of exorbitant sales tax, withholding taxes and high cost of utilities and other oppressive levies like 12.5% advance income tax from all mobile [166 million as on May 31, 2020 as per Pakistan Telecommunication Authority] and internet users (82 million).

We have a complex tax system of over 70 unique taxes and at least 37 government agencies administering these taxes, yet not collecting enough and pushing the country into deeper debt trap. The PTI Government has made no effort to reform the fragmented and highly complex tax system, remove policy distortions and reduce fiscal deficit by various measures as suggested in various articles: Essential reforms, Business Recorder, March 29, 2019, Challenges for budget-makers, Business Recorder, March 22, 2019,?Optimising tax collection, Business Recorder, March 15, 2019, Fixing the ailing tax system, Business Recorder, March 1, 2019, Country needs massive reforms, Business Recorder, January 25, 2019, Time up for fiscal integration, Business Recorder, December 21 & 23, 2018, Tax policy for investment, Business Recorder, December 14, 2018, Productive tax reforms, Business Recorder, October 27, 2018, Overcoming fragmented tax system, Business Recorder, October 19, 2018, PTI & revival of economy, Business Recorder, October 12, 2018, Bridging the tax gap, Business Recorder, October 5 & 7, 2018, Case for All-Pakistan Unified Tax Service: PTI & innovative tax reforms, Business Recorder, August 31, 2018, Overcoming debt burden, Business Recorder, August 27, 2018, PTI and tax reforms, Business Recorder, August 17, 2018 and Wither tax reforms, Business Recorder, August 2, 2019,

In its two years in power, the PTI Government incurred 'tax expenditure' (forgoing of revenues) of Rs 1149.95 billion in FY 2019-20 and Rs 972.4 billion in FY 208-19 (total of Rs 2122.35 billion (shown in Annex II of relevant Economic Surveys), but ignoring impact of asset-whitening schemes of 2018 and 2019 and many other items which FBR in 'Statement of Estimated Tax Expenditure of Federal Government' says could not be quantified for lack of data! The total tax expenditure, according to independent estimates, was not less than Rs. 3 trillion. Even if half of the concessions were withdrawn through Finance Act 2020, fiscal space of Rs 600 billion could have been created for meaningful tax reductions for revival of economy and helping out the SMEs to survive and helping the needy without job.

In a report [Finance Bill 2020: NA approves major tax relief], the following points have been raised showing benefits allegedly extended to particular vested interests:

* Tax concessions extended for certain individuals and influential groups of society, weakening the tax base broadening drive and creating more distortions in the tax system.

* New tax concessions that were not part of the Finance Bill 2020 but later included to reduce income tax rates for engineering services, shipping business, exempting from tax the income of real estate investment trusts, few educational institutions, lowering tax rates for electric vehicles and Hajj operators.

* Amendment to section 73 of the Sales Tax Act, 1990 was dropped placing a bar on persons from selling goods to unregistered people above the value of Rs100 million in a year. Currently, this applies to the manufacturers/producers—"this would weaken the drive to document the informal economy".

* Capital gains tax rates have been lowered for companies not listed on the stock exchange through a provision inserted into section 37A of the Income Tax Ordinance, 2001 that deals with tax rates for securities traded on the stock market.

* Proposal to impose 25% regulatory duty on energy drinks has been withdrawn. The duties on imported cigarettes of tobacco, cigars, cheroots and cigarillos of tobacco have been imposed at a rate of 65% as against the budget proposal of 100%.

It may be noted that the passage of amendments in the Petroleum Products Petroleum Levy Ordinance, 1961 and the Public Finance Management Act, 2019 was in gross violation of the Constitution of the Constitution as held by the Supreme Court in the Workers Welfare Funds m/o Human Resources Development, Islamabad through Secretary and others v East Pakistan Chrome Tannery (Pvt.) Ltd through its GM (Finance), Lahore etc. and others [(2016) 114 TAX 385 (S.C. Pak.)], Mir Muhammad Idris v FOP PLD 2011 SC 213 and Sindh High Court Bar v FOP PLD 2009 SC 789. These should have gone to both the Houses [Senate and National Assembly].

The following proposals were sent to the Ministry of Finance and FBR as a result of consultation on May 18, 2020 with Adviser to the Prime Minister on Finance and Revenue, aimed at providing ease of doing business, reducing business cost and helping revival of badly-hit economy as well as revenue generation of Rs. 5 trillion in fiscal year 2020-21 (since most of these are not implemented the same may be introduced through Finance Supplementary (Amendment) Bill as was done twice in 2018 after assuming power by the PTI Government):

1. “Presently, barring a few, income tax is levied on net income with minimum tax to the extent of amounts collected through over 60 withholding provisions. It is patently unconstitutional as held by Supreme Court in the Elahi Cotton Mills & others v Federation of Pakistan & others [PLD 1997 Supreme Court 582]. The apex court held that the National Assembly through Money Bill can impose taxes on income under Entry 47, Part I, Fourth Schedule to the Constitution or impose the same under Entry 52 on the basis of capacity to earn, but “it cannot adopt both the methods in respect of one particular tax”. The Finance Act 2019 blatantly violated this constitutional command. This may be corrected by opting either to net income taxation or presumptive but not both as suggested.

2. For the next two-three years due to recovery phase of businesses hit by Covid-19 endemic, the actual quantification of income of non-corporate businesses and professions should be given up and taxation may be moved to gross basis at fixed rate (after determining the fair rate for each class of business/profession). There should be no audit/raids. The taxpayers in their books should be allowed to take credit of imputable income.

3. For ease of doing business and waiving off lengthy disclosures in exceptional circumstances, if presumptive tax is imposed on turnover/receipts under Entry 52 as was done in 1991-92, the collection will be around Rs. 800 billion from all businesses and professions other than companies and employees that will keep on paying taxes under the existing tax rates and system [working and enforcement steps are attached].

4. The total collection, if we add corporate sector’s contribution after levying excess profit tax to counter monopolies and cartels, under the head income tax for fiscal year 2020-21 alone can be Rs. 2000 billion against the net collection of Rs. 1445 billion in 2018-19 [we are not taking 2019-20 collection into account due to massive shortfall in the wake of Covid-19 outbreak and lockdown]. The additional revenue of around Rs. 555 billion under one head alone will be a great achievement without hampering economic revival and, in fact, giving businesses and professions a stimulant to grow in the next three years. FBR will get much more tax than what it is presently collecting after giving share of 57.5% to provinces under the National Finance Commission (NFC) Award.

5. The federal government should amend the definition of “agricultural income” to bring into its ambit receipts from sale of orchards, lease of lands, nurseries and in this way, the rich absentee landowners and those engaged in businesses of nurseries will come under the Income Tax Ordinance, 2001. Additional revenue of Rs. 200 billion can be obtained from this source, if taxation is based under Entry 52 as discussed above.

6. Multinational Companies (MNCs) through an “abusive” transfer pricing mechanism allegedly deprive Pakistan of taxes of over Rs. 200 billion every year and this can easily be recouped with advance transfer pricing agreements, presently no provision exists to this effect.

7. If we take even negative effect of Covid-19 pandemic, the retail sales in fiscal year 2020-21 will not be less than $105 billion, otherwise would have cross $ 140 as per a study of Punjab Board of Investment and Trade. By applying sales tax of 4% and income tax of 2% on gross turnover, the total collection will be around Rs. 1.2 trillion from this sector alone [details will be in second instalment].

8. The total collection by imposing unified sales tax on goods and services (as done by India in 2017) can reach Rs. 3500 billion as against collection of around Rs. 1659 by the Federal Government through sales tax on goods [Rs. 1459 billion in 2018-19] and provinces by sales tax on services [cumulatively Rs. 190 billion]. The additional revenue collection of Rs. 1400 billion will not only give fiscal space to the federal government to narrow down fiscal deficit but will also enhance distribution amount to the provinces. Distribution will be strictly as per the Constitution. The collection under new law will be by FBR as provincial assemblies need to pass only resolutions under Article 144 of the Constitution empowering the National Assembly to enact integrated sales tax on goods and services. There is no need to enter into controversial amendment in the Constitution disturbing 18th Amendment. The

slogan of ‘One nation, One Tax’, adopted by India in 2017, and Harmonised Sales Tax (HST) by Canadian federal and provincial governments is the way forward as taxpayers operating on trans-provincial level are facing many difficulties.

9. In case the provinces do not agree for above, then for trans-provincial entities, FBR can include in Finance Bill 2020, sales tax on services, following the command of Supreme Court in the case of Messers Sui Southern Gas Ltd & Others v Federation of Pakistan & Other 2018 SCMR 802. It extensively elucidates that the post-Eighteenth Amendment position vis-à-vis legislative competence of federation and federating units as under:

“We are in agreement with the observation made by the learned High Court that though in a Federal system, provincial autonomy means capacity of a province to govern itself without interference from the Federal Government or the Federal legislature, but as the Provincial legislature does not possess extra-territorial legislative authority i.e. it cannot legislate regarding the establishments operating beyond the territorial boundaries of that province”.

The above pronouncement of the Supreme Court is not restricted to any particular law and cover tax laws as well. It is binding under Article 189 of the Constitution and provinces if do not agree for integrated sales tax of goods and service will suffer.

10. In Customs, massive evasion takes place due to under-invoicing, misclassification and mis-declarations. The collection in 2018-19 by FBR was 686 billion. If revenue leakages are plugged as suggested in Dismantle containers’ mafia, Business Recorder, September 14, 2018, it can be Rs. 1200 billion. An extra generation of Rs. 500 billion under this head alone is possible.

11. The loss in FED due to illicit local manufacturing and smuggled cigarette sector alone is of Rs 60-80 billion a year. It can be recouped by trace and track (T&T) system that should also be extended to all industries across the board, e.g. textile, sugar, cement, beverages etc.

In the next week, the remaining proposals as how to provide incentives, relief and stimuli to the businesses to survive and revive as well as accelerating growth and investment for new jobs, presented but not implemented, will be documented. The new initiatives and innovations alone can lead to better revenue collections whereas present system is just doing the opposite!

(To be continued)

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