

RELEVANT TO ACCA QUALIFICATION PAPER F6 (PKN)

Amendments to the Finance Act 2011

This is the Finance Act 2011 version of this article. It is relevant for candidates sitting the Paper F6 (PKN) exam in 2012.

According to the Constitution of the Islamic Republic of Pakistan, no tax can be levied except by – or under – the authority of an Act of Parliament. The parliament amends the tax laws usually on an annual basis in the form of a Finance Act, to keep them relevant in the prevailing socio-economic circumstances of the country. For correct taxation, it is therefore essential that those who deal with tax keep themselves abreast of the latest changes.

According to guidelines issued by ACCA, relevant regulations issued and legislation passed on or before 30 September 2011 will be assessed for the first time in the June 2012 sitting of Paper F6 (PKN). The Finance Act 2011 is operative from 1 July 2011 and therefore examinable in the June and December 2012 papers of Paper F6 (PKN). Paper F6 (PKN) candidates are therefore advised to go through these amendments carefully. It may be noted that references to different provisions of Income Tax Ordinance 2001 and the Sales Tax Act 1990 are for additional knowledge of the candidates and not required in the paper.

The examinable amendments are explained below:

CHANGE IN THE BASIC THRESHOLD OF INDIVIDUAL TAXPAYERS

With effect from the 2012 tax year, an individual taxpayer [salaried and non-salaried] shall not pay any tax if taxable income of the taxpayer for the year does not exceed Rs350,000. [Para (1) and (1A) of Part I of the First Schedule]. Nevertheless, it should be remembered that in the case of an individual whose income under the head 'Income from business' exceeds Rs300,000, but does not exceed Rs350,000, the individual shall still be required to file an income tax return for that year [though no tax is payable]. [s114(2)]

CHANGES IN THE TAX CREDITS ALLOWABLE UNDER THE INCOME TAX ORDINANCE 2011

A. Changes in the provisions relating to the *existing* tax credits

Tax credit for investment in shares [s62]

Following the amendments made in the Finance Act, 2011, a person [**both resident and non-resident**], not being a company, was entitled to a tax credit for a tax year if the person acquired the shares either from:

- (a) a public listed company on its offer of new shares to the public, or
- (b) the Privatisation Commission of Pakistan.

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The tax credit was admissible at an average rate of tax computed before allowing any tax credit. The amount invested in the acquisition of shares eligible for tax credit was the lesser of the following:

- (i) Total cost of acquiring the shares
- (ii) **10%** of the person's taxable income for the year, or
- (iii) 300,000 rupees.

Following the amendments made in the Finance Act 2011, a **non-resident person is not** eligible for this credit. Further, there is change in the formula for the computation of tax credit. Now, the amount invested in the acquisition of shares eligible for tax credit will be the lesser of the following:

- (i) Total cost of acquiring the shares
- (ii) **15%** of the person's taxable income for the year, or
- (iii) 500,000 rupees.

If a person had been allowed a tax credit for investment in shares as discussed above, and later on disposed of these shares within 12 months of the acquisition of these shares, the tax liability of the year of disposal was to be increased by the amount of tax credit allowed earlier. Now this limit of **12 months** has been increased to **36 months**.

Contribution to an Approved Pension Fund [s63]

One of the limits on the total amount eligible for tax credit on contribution to the Approved Pension Fund was that it could have been allowed on a maximum contribution of Rs500,000 during a tax year. This upper limit has been withdrawn. All other conditions of eligibility and calculation of tax credit remain the same.

Tax credit for enlistment [s65C]

By virtue of amendment, if a taxpayer company opts for its enlistment in any registered stock exchange in Pakistan, a tax credit equal to **15%** of the tax payable shall be allowed for the tax year in which it is enlisted. Prior to amendment in the Finance Act, 2011, admissible rate of tax credit was **5%** of the tax payable for the relevant tax year.

B. Provisions relating to new tax credits introduced in the Finance Act 2011

Tax credit for insurance premium

If a person is resident and has not invested in shares eligible for tax credit [u/s 62] but is deriving income under the head 'salary' or 'Income from Business' and has paid life insurance premium on a policy to a life insurance company registered by the Securities and Exchange Commission of Pakistan [SECP] under the Insurance Ordinance 2000, such person shall be eligible for tax credit according to the following formula:

$$(A/B) \times C$$

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where

- A** is the amount of tax assessed for the tax year prior to any tax credit
B is the person's taxable income for the tax year, and
C is the lesser of:
 (i) the total contribution or premium paid by the person
 (ii) 15% of the person's taxable income, or
 (iii) Rs500,000.

Tax credit for newly established industrial undertakings [s65D]

Tax credit equal to 100% of the tax payable by a newly incorporated company for establishing industrial undertaking is admissible for a period of five years beginning from the date of setting up of such industrial undertaking or the date of commencement of commercial production, whichever is later. For such tax credit, the company has to fulfil all of the following conditions:

- (a) the company is incorporated and industrial undertaking is set up between 1 July 2011 and 30 June 2016
- (b) industrial undertaking is managed by a company formed for operating the said industrial undertaking and is registered under the Companies Ordinance 1984 and has its registered office in Pakistan
- (c) the said industrial undertaking is established with 100% equity owned by the said company
- (d) the industrial undertaking is not established by the splitting up or reconstruction or reconstitution of an undertaking already in existence
- (e) the industrial undertaking is not established by transfer of machinery or plant from an industrial undertaking established in Pakistan at any time before 1 July 2011.

Note: if later on it is found that tax credit was allowed wrongly, tax payable for the relevant year shall be recomputed and payable by the taxpayer company.

Tax credit for industrial undertakings established before 1 July 2011 [s65E]

The Finance Act 2011 provides a tax credit on investment by a company with 100% equity investment in balancing, modernisation, replacement, or for expansion of the plant and machinery already installed in an industrial undertaking set up in Pakistan before 1 July 2011:

- (i) Tax credit shall be admissible only if the plant and machinery is purchased and installed at any time between 1 July 2011 and 30 June 2016.
- (ii) The amount of credit shall be allowed against the tax payable by the taxpayer in respect of a tax year in which the plant or machinery is purchased and installed and for the subsequent four years.
- (iii) In case no tax is payable by the taxpayer in the year of installation of the plant and machinery or such tax is less than the amount of tax credit, the amount of such credit or the amount of unadjusted tax credit, as the case may be, shall be carried forward and deducted from the tax payable by the

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taxpayer in respect of the following tax year, and so on, but no such amount shall be carried forward for more than four tax years.

- (iv) Tax credit shall be allowed on the basis of proportion, which such equity investment bears to the total investment in the company.

Total amount of tax credit allowed in different years as explained above shall not exceed in aggregate the limit of tax credit.

Note: if later on it is found that tax credit was allowed wrongly, tax payable for the relevant year shall be recomputed and payable by the taxpayer company.

UNEXPLAINED INCOME OR ASSETS

Suppression of any production, sales, any amount chargeable to tax and any item of receipt liable to tax in whole or in part will now be treated as 'concealed income' if the taxpayer is unable to explain sources of these items satisfactorily. Consequently, now penalty provisions will attract to such items also. [s111]

MINIMUM TAX ON THE INCOME OF CERTAIN PERSONS [u/s 113]

Where minimum tax paid on the basis of turnover [u/s 113] exceeds the actual tax payable on the basis of taxable income by applying rates given in the First Schedule to the Ordinance, the excess amount of tax paid is carried forward for adjustment against the tax liability of three tax years immediately succeeding the tax year for which the amount was paid. To facilitate the taxpayers this period of adjustment has been extended from three to five years by the Finance Act 2011.

RETURN OF INCOME [u/s 114]

By virtue of amendments in the Finance Act 2011:

- (a) a person who is the holder of commercial or industrial connection of electricity, the amount of annual bill of which exceeds rupees one million, shall also be required to file return of income for the relevant tax year
- (b) evidence of payment of due tax, as per return of income, and wealth statement [u/s 116] will have to be filed with return of income.

WEALTH STATEMENT [u/s 116]

- (a) Existing income threshold for the requirement of filing of wealth statement has been increased from Rs500,000 to Rs1,000,000 in the Finance Act 2011.
- (b) It has been clarified that an individual member of an Association of Persons (AOP) shall also file wealth statement if share of income of such individual from the AOP is Rs1,000,000 or more. For determination of share, income of the AOP is to be taken before tax.

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- (c) The Finance Act, 2011 further requires that where provisional assessment order [u/s122C] has been passed in the case of an AOP and it intends to file a return of income to prevent the order from becoming final order, each member of the AOP shall file his/her wealth statement, wealth reconciliation statement with the return of AOP.

NO APPEAL AGAINST PROVISIONAL ASSESSMENT ORDER [u/s 127]

The Finance Act 2011 stipulates that no appeal can be filed before the Commissioner (Appeals) against a provisional assessment order [u/s 122C]. However, when the provisional assessment order becomes final, it shall be appealable.

DISPOSAL OF APPEAL BY THE APPELLATE TRIBUNAL [u/s 132]

If an appeal proceedings was not attended by the appellant, the Appellate Tribunal had the powers to dismiss the appeal. After amendment in the Finance Act 2011, the Appellate Tribunal – in the case of default – shall decide the appeal on merit on the basis of available record instead of dismissing it without going into merits of the case.

CHANGE IN DATE OF DEPOSITING ADVANCE TAX ON ACCOUNT OF GAIN ON DISPOSAL OF SECURITIES

Gain on securities is taxable as a separate block and advance tax on such gain is payable [u/s 147] on a quarterly basis by taxpayers other than individuals. For the first three quarters, payment of advance tax for each quarter can now be made within 21 days of the close of each quarter instead of the existing limit of seven days. However, payment for the last quarter ending 30 June is to be made by 15 June each year. [s147]

PROFIT ON DEBT [s151]

By virtue of amendment in the Finance Act 2011, tax deducted on profit on debt [u/s 151] of all categories shall be final tax on such income.

Note: there are certain exceptions from the above treatment like in the case of banking companies, etc, but they are not examinable in Paper F6 (PKN).

WITHDRAWAL OF BALANCE UNDER PENSION FUND [u/s 156]

By the Finance Act 2011, the existing tax free limit of 25% withdrawal from the accumulated balance under a pension fund has been enhanced to 50%. The exemption to such withdrawal is only available if made at the time of retirement age or after that age.

WITHHOLDING TAX STATEMENTS [u/s 165]

Amendments in the Finance Act, 2011 have been made to the following effect:

- (i) Instead of quarterly statements, now statements shall be filed on a monthly basis.

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- (ii) Monthly statement shall be furnished, or e-filed, by the 15th day of the month following the month to which the withholding tax pertains.
- (iii) Additional information regarding Computerised National Identity Card Number and National Number of the taxpayer whose tax is withheld shall have to be recorded in the monthly statements.

AMENDMENT IN THE PROVISIONS RELATING TO PENALTY [u/s 182]

Two amendments made in the Finance Act, 2011 are:

- (i) In the case of non-filing or late filing of a return, statement in lieu return, or a withholding tax statement, a penalty is leviable with reference to 'tax payable'.

Previously, there was ambiguity about the term 'tax payable' as to whether it referred to the gross amount of tax computed on the basis of assessment or the net amount of tax payable after giving credit of amount already paid as advance tax, etc.

The expression 'tax payable' has now been explained in the Act, to mean tax chargeable on the basis of assessment made or treated to have been made. [u/Ss120, 121, 122 or 122C]

- (ii) When an appellate order is passed by the Commissioner (Appeals), the department issues an order giving effect to such order and a demand notice giving a date for payment of the tax is issued. An incentive of 50% reduction in the penalty payable, if any, has been provided to a taxpayer where tax due is paid within the due date given in the demand notice and the taxpayer does not file an appeal against the order of the Commissioner (Appeals).

FBR has also explained amendments in the Finance Act, 2011 through its Circular No. 07 of 2011 dated 1 July 2011, which can be accessed at www.fbr.gov.pk

Amendments in the Sales Tax Act 1990

Important amendments in the Sales Tax Act 1990 by the Finance Act 2011, examinable in Paper F6 (PKN) from June 2012 onward, are as follows:

1. Reduction of the rate of sales tax

Rate of sales tax has been reduced from 17% to 16% by the Finance Act 2011. [s3]

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2. Input to be restricted to 90% of output tax-exception

Restriction on the adjustment of input in excess of 90% of the output tax shall now not apply in case of fixed assets or capital assets. [Proviso to s8B]

- 3.** Many exemptions available in the Sixth Schedule have been omitted by the Finance Act 2011. For example, import and local supply of defence stores, supply of bricks, cement/concrete blocks is no more exempt.
- 4.** The zero-rating regime has been rationalised to limit its application only to selected sectors.

Note: since the syllabus requires listing of principal zero rating and exempt supplies, the candidates are advised to consult Fifth and Sixth Schedules to the Sales Tax Act 1990 to update their knowledge.

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