

MYTH OR REALITY

Presented By:

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(Benjamin Franklin)

**In this world nothing can be
said to be certain, except
death and taxes.**

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Basic Terms

- ✧ Direct Tax vs. Indirect Tax
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- ✧ Input Tax vs. Output Tax
- ✧ Fake, Flying and VAT Invoice
- ✧ Exempt, Zero Rated and Taxable Goods/Services

Direct Tax vs. Indirect Tax

- ☞ A tax that cannot be shifted by the taxpayer to someone else.(income tax)
- ☞ The person who sales collect tax from the buyer and hence the buyer ultimately pays the tax. (VAT)
- ☞ Collection of tax in Pakistan 33% : 77%

Ad valorem, Value added and Specific Tax

- ⌘ Ad valorem: a tax with respect to value.
- ⌘ Value added: a tax with respect to value addition.
- ⌘ Specific: A tax with respect to quantity.(
Re.1 per Liter)

Input Tax vs. Output Tax

- ⌘ Input Tax: Sales tax paid/payable with purchases.
- ⌘ Output Tax: Sales tax received/receivable with sales.

Fake, Flying and VAT Invoice

- ❧ Fake: Non-genuine invoice or a self created invoice.
- ❧ Flying: Receipt of invoice without receipt of goods/services.
- ❧ Vat Invoice: Which is genuine and bear the GST numbers of both the supplier and the buyer

Exempt, Zero Rated and Taxable Goods/ Services

- ☞ Exempt: Wherein an input tax is a part of cost
- ☞ Zero rated: Wherein an output tax is being charged at the rate of Zero percent and taxpayer is entitled to claim refund of input tax
- ☞ Taxable: Wherein an output tax is being charged at the prescribed rate (say 15%) and taxpayer is entitled to adjust input tax against output tax

Exempt, Zero Rated and Taxable Goods/ Services

Exempt: Input is part of Cost

Zero Rated: Input is refundable

Taxable: Input is payable/adjustable

Accounting entries in case exempt and taxable goods

Payment of Electricity Bill in case of exempt goods

Electricity Expense	115,000	
Tax deduction at source	10,000	
Bank		125,000

Payment of Electricity Bill in case of taxable goods

Electricity Expense	100,000	
Input Tax	15,000	
Tax deduction at source	10,000	
Bank		125,000

Our 20 years History

- ❧ Revenue has fallen from 18% to 9% of GDP
- ❧ This ratio is one of the lowest in the world
- ❧ Non development expenditures has increased 350% during this period
- ❧ 2% rich owns 80% of country's wealth
- ❧ A corruption of 500 Billion Rupees/Annum is only in FBR (Shoukat Tareen)

Major Source of Revenue

↳ Import

↳ Export

↳ Oil, Gas, Communication

↳ 1600 Companies are paying 85% of Total Tax.

Main reasons of low tax collection

- ✧ Exempt sectors such as agriculture, Property, Stocks, services etc.
- ✧ Lack of system
- ✧ Corruption/Tax evasion
- ✧ Energy crises
- ✧ Loss in government owned entities
- ✧ Afghan Transit

Pakistan Steel Mills

- ☞ Earned profit from 2000-01 to 2007-08.
- ☞ Gross loss Rs. 19.5 billion during 2008-09.
- ☞ 200% increase in administrative expenses in 2008-09 compare to previous year.
- ☞ Pre tax loss Rs 22.1 billion in year 2008-09 compare to a profit of 3.6 billion in previous year.
- ☞ A bail out package of Rs. 10 billion was given to PSM.
- ☞ Same situation is in PIA, WAPDA, Railway etc.

Afghan Transit

Example:		Rs.
Purchase Price		<u>100</u>
Invoice Price		25
Assessed Value		50
Customs Duty(10%)	5	
Sales Tax(16%)	8	
Income Tax(4%)	2	
Further Tax(2%)	<u>1</u>	<u>16 (Govt. Revenue)</u>
Total Cost		116

Afghani offer the same product at **110**

What Is VAT ?

VAT is similar to a Sales Tax. It is a tax on the market value added to a product or material at each stage of its manufacture or distribution, ultimately passed on to the consumer. (Maurice Laure)



History of VAT

- ✧ Value Added Tax (VAT) is a consumption tax of up to 25% that is levied on both **goods and services** in most countries around the world. This system is present in Europe, Japan, and Australia and a number of others countries. They also allow a refund of VAT to non-resident and Resident persons.
- ✧ VAT has its origin in European Countries (EC). It was pioneered in France, which introduced a value added type of consumption tax on goods in 1954 that was levied at the production stage.
- ✧ In the world, more than 160 countries have successfully implemented VAT system of taxation. Out of 31 member countries of Organization for Economic Cooperation and Development (OECD), Most of the countries have accepted VAT as their main consumption tax.



Rate of VAT in different countries

Denmark	25%	Finland	22%	Germany	19%
France	19.60%	Ireland	21%	Italy	20%
Netherlands	19%	Portugal	20%	Spain	16%
Sweden	25%	United Kingdom	17.50%	Poland	22%
Argentina	21%	Canada	5%	Croatia	22%
Iceland	24.50%	India	12.50%	Mexico	15%
Russia	18%	China	17%	Uruguay	22%
Switzerland	17.60%	Norway	25%	South Africa	14%
Indonesia	10%	Kenya	18%	Korea	10%
Nigeria	5%	Nepal	10%	Sri Lanka	12.50%
Bangladesh	15%	Egypt	15%		

Source: Economy Watch



VAT VS. GST

Similarities:

- ✧ Both are indirect taxes.
- ✧ Both are value added taxes.

Differences (in case of Pakistan)

- ✧ Services
- ✧ Zero rating
- ✧ Exempt List
- ✧ Discretionary Powers



46(5) The Board may, by notice, cancel the registration of a person if the Board is satisfied that—

... (a) the person does not have a fixed place at which the person's economic activity is carried on;

... (b) the person has not kept proper records of its business;

... (c) the person has not filed regular and reliable returns; or

(d) the person has not complied with its obligations under other taxation laws, including the customs laws, and there are reasonable grounds to believe that the person will not keep proper records or file regular and reliable returns.



Difference between VAT & GST (in case of Pakistan)

✧ The following points create difference between newly introduced VAT and existing GST, in case of Pakistan:



Tax Rate

- ☞ VAT: Only one tax rate which is 15%. (9)
- ☞ GST: Multiple tax rate such as 16%, 18%, 21% and 25%



Exempt Goods

- ✧ VAT: In 14 entries, Exempt goods are clearly defined. (first Schedule)
- ✧ GST: 82 (71+11) goods ambiguously defined as per Table-I & II of sixth schedule of Sales Tax Act 1990 and with almost 30 SRO's.
- ✧ Food items, medical, educational services & material is exempt in EU countries. In UK and Australia, these are zero rated.
- ✧ Indian exemption list is very comprehensive even covering textile and electricity.



Domestic Zero Rating (23 and 2nd Schedule)

✧ VAT: Export and only few other such as

Warranty claims, maintenance, sale of economic activity, Basic medicine etc.

✧ GST: A number of sectors are zero rated such as:

✧ Textile	✧ Sewing Machines
✧ Leather	✧ Surgical goods
✧ Cooked and un-cooked meat based products	✧ Dairy Industry
✧ Carpet	✧ Stationery Industry
✧ Sports Items	✧ Bicycles



Zero rated Goods in UK

- ℳ food
- ℳ books, newspapers and magazines
- ℳ young children's clothing and footwear
- ℳ special exempt items - for example equipment for disabled people



Zero-rated goods in South Africa

Brown bread.

Dried beans.

Dairy powder blend.

Vegetables.

Vegetable oil.

Cultured milk.

Eggs.

Maize meal.

Milk powder.

Rice.

Fruit.

Milk.

Brown wheaten meal.



Zero rated goods in Canada

☞ Drugs and Biologicals

☞ Medical and Assistive Devices

☞ Basic Groceries

☞ Agriculture and Fishing



Retail Price

- ✧ VAT: No concept
- ✧ GST: Manufacturer will pay tax according to retail price on 17 items.



Sale of retail price item in GST

		Sale Price	Retail Price	GST	Total Price
✧	Manufacturer	90	100	16	106
✧	Distributor	92	100	16	108
✧	Wholesaler	95	100	16	111
✧	Retailer	100	100	16	116



SRO'S (13)

- ✧ VAT: No exemption or zero rating can be made by any government department or authority , except as expressly provided in this Act.
- ✧ GST: Board has power to issue SRO under number of sections even regarding zero rating, exempt goods and lower rating.



Transfer of an economic activity (5)

- ✧ VAT: Zero rated
- ✧ GST: No concept



Late Filing or Revised Return (56)

In VAT:

- ☞ Late filing with the approval of the board.
- ☞ Revision within three years and after the approval of Board.

In GST:

- ☞ No approval from commissioner in case of late filling
- ☞ Within 120 days in case of revision and after the approval of Commissioner



Input tax adjustment in case of manufacturer

✍ VAT: 100%

✍ GST: 90% of output tax



Second hand goods (21)

- ✍ VAT: SHG are subject to tax, Input tax adjustment is allowed by tax fraction
- ✍ GST: No tax on sale and purchase of second hand goods



Example (Sale and Purchase of SHG)

- ✧ Purchase from unregistered person of Rs. 100.
- ✧ Tax fraction = $\text{VAT Rate}/100 + \text{VAT Rate}$ (15/115)
- ✧ Input tax in purchase = $15/115 * 100 = 13.04$
- ✧ Sale to registered person Rs. 115. (Value Ex. VAT Rs. 100 plus VAT Rs. 15.)
- ✧ VAT Payable = Output Tax – Input tax
 $= 15 - 13.04 = 1.96$



Input Tax adjustment in case of purchase of Fixed Asset

☞ VAT: 100%

☞ GST: Equal proportion in twelve months



VAT and Bad Debts (30)

- ☞ Supplier is entitled to adjust output tax paid which relate to bad debts in the period in which he/she actually write off these bad debts.



Progressive or Periodic Supply (16)

☞ Supply that is progressive or periodic
and

☞ that provides for progressive or periodic
payments

shall be treated a separate supply.



Default Surcharge (88)

In VAT

Mistake 1%/M

Fraud 2%/M

In GST

Mistake KIBOR + 3%

Fraud 2%/M



VAT on Goods

☞ All Goods are Taxable, except following:

☞ Wheat	☞ Wheat flour
☞ Unprocessed peas	☞ Water without brand name
☞ Salt without brand name	☞ Books, Newspaper, Periodicals
☞ Diaper for adults	☞ Artificial parts of body
☞ Contraceptives	☞ Precious metal other than a first supply



VAT on Services

In VAT services were divided in to two categories

- ✧ Federal Services
- ✧ Provincial Services



Federal Services (2 xiii)

☞ Carriage of goods or passengers by railway, sea, or air



Provincial Services

All services are subject to provincial Sales Tax except the following

- ✧ Funeral, burial or similar services
- ✧ Services by religious institutions
- ✧ Services by an approved non-profit charitable organization
- ✧ Certain Financial services.
- ✧ Certain education services provided by an institution duly registered by the Minister of education
- ✧ Certain supplies of immoveable property.



Services in Provincial GST

Only the following four services are subject to tax

- 1. Hotels, Marriage Halls, Lawns, Clubs and Caterers
- 2. Advertisement on TV and Radio
- 3. Customs Agents, Ship Chandlers and Stevedores
- 4. Courier



VAT and Supply Chain

∞ VAT: A claim to complete supply chain from manufacturer or importer to retailer.

∞ GST: Distortion after manufacturer or importer



VAT and Documentation (Chapter Vii)

☞ Tax invoices

☞ Sales receipts

☞ Debit and Credit notes

☞ Period of retention for record.

1. Six years from the end of the tax period.
2. Until the final decision is made in case of any audit, recovery, prosecution and proceeding.



Tax Invoice (49)

Tax invoice will include the followings:

- ☞ Serial No.
- ☞ Date
- ☞ Name, Address and NTN of Supplier.
- ☞ Name address, NTN or CNIC of Buyer.
- ☞ Description and Quantity.
- ☞ Value Ex. Tax, Tax Rate, Tax and Value Inc. Tax.



Sales Receipt (50)

If sales are up to 25,000 and the buyer is unregistered person then supplier will issue Sales receipt which will include the followings:

- ✓ Date
- ✓ Name and Registration numbers of Supplier
- ✓ Description of goods or services
- ✓ Total amount
- ✓ An indication that tax is included in amount



Anomalies in Sales Receipt (50)

- ❧ Sales receipt can be issued to that un registered person which is not required to be registered. (a shift of responsibility)
- ❧ Serial number is missing
- ❧ Name and address of buyer is missing
- ❧ Quantity is missing
- ❧ Manufacturer can also issue Sales Receipt.
- ❧ No per day sales receipts limit for same buyer.



Registration (41)

Turnover for Registration:

VAT: 7.5 Million/Annum

- ✍ Decision regarding registration or refusal will be issued within 15 days and an appeal can be made against decision (41)
- ✍ Section 79, dealing with appeals does not provide the right of appeal.

GST: For Manufacturer not being a cottage industry and retailer whose turnover exceeds 5 Million/Annum

ALL wholesaler, trader, distributor , importer and dealer without any limitation of turnover



4. Requirement of registration.—The following persons engaged in making of taxable supplies in Pakistan (including zero-rated supplies) in the course or furtherance of any taxable activity carried on by them, if not already registered, are required to be registered in the manner specified in this chapter, namely:—

- ... (a) a manufacturer not being a cottage industry
- ... (b) a retailer whose value of supplies, in any period during the last twelve months exceeds five million rupees;
- ... (c) an importer;
- ... (d) a wholesaler (including dealer) and distributor;
- ... (e) a person required, under any other Federal law or Provincial law, to be registered for the purpose of any duty or tax collected or paid as if it were a levy of sales tax to be collected under the Act; 20[and]
- (f) a commercial exporter, who intends to obtain sales tax refund against his zero-rated supplies.



VAT Payable (21)

∞ VAT Payable = (Output Tax + Increasing adjustments) – (Input Tax + Decreasing adjustments)



Carry Forward and Refund (37)

- ☞ VAT Carry forward = If (Input Tax + Decreasing adjustments) are greater than (Output Tax + Increasing adjustments)
- ☞ Carry forward can be made up to six month
- ☞ If C/F remains unadjusted up to six month, it will be claimed refund.



Refund of VAT without carry forward (38)

☞ If

- (i) 50% or more person's turnover is or will be zero rated export;
- (ii) 50% or more input relate to zero rated export.

then input tax will be refunded. (38)



Refund in case of Adv. Tax or Withholding Tax (24)

☞ If advance tax paid + tax withheld by others (Government department or LTU) is greater than out put tax + increasing adjustments then the amount shall be refunded without carry forward.



Time of Refund

- ☞ Within 45 days after application (37,38)
- ☞ In case of delay additional refund @ KIBOR (93)
- ☞ Where an officer of IRS suspects or believes that some documents are not genuine, true or correct , he may reject the claim. (82)



Increasing adjustment (24)

- ⌘ Post supply adjustment (29)
- ⌘ Bad debts adjustment (30)
- ⌘ Private use adjustment (31)
- ⌘ Cancellation of registration (32)
- ⌘ Change in rate (34)
- ⌘ Withholding tax (36)
- ⌘ Default surcharge, fine, penalty, fee etc.



Decreasing adjustment (24)

- ∞ Advance Tax (35)
- ∞ Withholding tax (36)
- ∞ Post supply adjustment (29)
- ∞ Bad debts adjustment (30)
- ∞ Registration (33)
- ∞ Carry forward (37)



Advance tax (35)

☞ VAT: 3.75% (25% of 15%)

☞ GST: 2%



	VAT(15%)	GST(16%)
Import Value	= 100	100
Input tax	= 15	16
Add. Tax	= 3.75	2
Total Input	= 18.75	18
Sale Price	= 125	112.5
Output Tax	= 18.75	18

If the sale price is lower than 125, the importer will claim refund.



Withholding Tax (36)

☞ VAT: 3.75% (25% of 15%)

☞ GST: 3.2%



VAT

Purchase Price = 100

Input tax = 15

Sale price = 133.33

Output tax = 20

Withholding tax = 5

If Price is lower than 133.33, the supplier will claim refund.



Method of Payment in VAT (26,30)

- ☞ If the taxable supply including sales tax exceeds fifty thousand rupees the payment shall be made by verifiable banking instrument from the bank account of the buyer to the bank account of the seller.
- ☞ If the buyer do not make payment within six month, the buyer will make an increasing adjustment.



Apportionment of Input Tax (27)

- Where purchases of goods & services or imports are partly for creditable purpose.
- A restriction on deducting the input tax partly applies.
- Criteria for apportionment is not defined.



Input Tax in VAT (2 xviii)

Input tax will include:

- ℘ VAT paid on purchase of goods
- ℘ VAT paid on import of goods
- ℘ VAT paid on purchase of services
- ℘ VAT paid on import of services



Output Tax in VAT (2 xxiv)

Output tax will include:

- ℘ VAT received on sales of goods
- ℘ VAT received on sales of services
- ℘ VAT paid on purchases of services



Claim of Input Tax (28)

- ☞ The period in which buyer will claim input tax, supplier will consider it output tax.
- ☞ Six succeeding tax periods after considering it output tax by the supplier.



Forensic Audit (69)

- ⌘ means fact behind the figures
- ⌘ Forensic Audit would give unlimited powers to the officers of Inland Revenue to go to any extent for carrying out investigation against a registered unit.
- ⌘ The forensic audit involves the scope beyond tax record required to be maintained.



VAT and Inflation

The prices of the following goods will increase

- ✍ Domestic zero rated goods in GST
- ✍ Goods and services which will be subject to tax in VAT
- ✍ Value addition in supply chain

The prices of the following goods will decrease

- ✍ Goods and services which are subject to tax @ 16%, 18%, 21%, 25% in GST



VAT and Production

- ∫ Increase in smuggling/Afghan Transit
- ∫ Increase in Undocumented production



VAT and Economy

- ∫ Documentation of economy
- ∫ Increase in Govt. revenue
- ∫ Broad base



VAT and IRS

- ⌘ Lack of system or infrastructure
- ⌘ No one knows the pros and cons
- ⌘ Lack of support of trade associations/chambers



Role of IMF and World Bank

- ✍ Stand-By Arrangements (SBA) of \$7.6 billion to be paid in 23 months
- ✍ Enhancement in July 2009 to \$ 11.3 billion

Conditions:

1. VAT from July-2010
2. Monitoring of revenue collection by IMF

Monitoring Team consist of :

1. 6 Directors of IMF
2. 2 Directors of WB



(Jewish Proverb)

**Taxes grow without
rain.**



Thank You

