

## **Punjab Sales Tax on Services – An Overview**

Value added taxes or taxation (VAT) is one of the four marvelous innovations of the twentieth century, the other three being atomic energy, anti-biotics and computers or information technology. Historically, VAT replaced turnover taxes and also emerged as a precursor of income taxation. Typically, VAT is charged on both goods and services. VAT is charged on every supply or sale or rendition stage of goods and services in the commercial chain of production, distribution and consumption. There are several forms of VAT in the world but the one based on tax invoice-related credit mechanism is considered to be the ideal type because of its in-built automatic system of converting multi-stage tax assessments into a simple stage levy.

2. At the time of independence, sales tax on goods was a provincial subject but its collection was entrusted to the Federal government. The subject was subsequently federalized in 1951. The primary responsibility to collect and enforce sales tax on goods remained with Income Tax department till 1981, when it was shifted to the Customs and Central (later on Federal) Excise department. Levy of sales tax on imports always remained the responsibility of Pakistan Customs. In 2009, in consequence of national tax reforms, administrative powers for collection and enforcement of all domestic taxes administered by the Federal Board of Revenue (FBR) were clubbed and a new department of “Inland Revenue” was created for their composite administration.

3. Federal government has never remained empowered to levy the sales tax on services. However, from 1971 onwards, different services were subjected to traditional Central / Federal Excise duties. But the international development partners continued to persuade Pakistan to introduce VAT-type sales tax on services. Provinces were therefore, asked in 2000 to introduce their service tax legislations and entrust FBR to collect and administer provincial sales tax on services. Excise duties were however, kept intact on services included in the list of Federal subjects (e.g. communication). Nevertheless, the 18<sup>th</sup> Constitutional Amendment has changed the

whole landscape of national fiscalism in Pakistan. Now the Federation is not empowered to levy (consumption) taxes on services.

4. The ideal VAT system in a country is no doubt the one which is operative at national level in a manner that, for the purpose of sales taxation, distinction between commodity (goods) and non-commodity (services) is artificially eliminated and the system is made uniformly and seamlessly applicable on both goods and services. But now true materialization of this ideal appears to be a difficult venture in Pakistan where provinces are determined to manage the collection of sales tax on services on their own level. In this regard, Sindh has pioneered and Punjab is taking a second lead.

5. Through an independent legislation, Punjab has established a semi-autonomous organization, Punjab Revenue Authority (PRA) to collect and enforce sales tax on services. It has also enacted the Punjab Sales Tax on Services Act, 2012 in supersession of the Punjab Sales Tax Ordinance, 2000 (as amended from time to time). To begin with, Punjab has kept the tax coverage only to the fourteen categories of services covered under the repealed ordinance, viz,

- Hotels.
- Clubs.
- Caterers.
- Advertisements on T.V & Radio (including Cable TV).
- Customs Agents.
- Ship Chandlers.
- Stevedores.
- Telecommunication.
- Insurance and Re-insurance.
- Banking companies.
- Non-banking financial institutions.
- Stock brokers.
- Shipping agents.
- Courier services.

Under the taxable categories, the exemptions earlier available under the Federal Excise Act, 2005 on account of international commitments and societal welfare etc have been kept unaltered. Scope of sales tax on services shall be progressively expanded in future after examining the multi-disciplinary viabilities of new tax obligations. As of today, the scope of Punjab's sales tax on services is less wider than

its counterpart in Sindh. Sales tax rate (s) have also been kept unchanged. Thus, for the time being no new service tax has been introduced in Punjab.

6. The Punjab Sales Tax on Services Act, 2012 contains thirteen chapters and eighty seven sections. It covers all dimensions of a complete tax system like definitions, scope (charge) of tax, payment and collection of tax, registration (including de-registration), record keeping, audit including special audit, filing of declarations (returns including statements and applications etc), tax administration, offences and penalties, adjudications including appeals, revisions and references, recovery of arrears (government dues), representation and e-intermediation and general administration of the system etc. There are two schedules in the statute. The first schedule gives a descriptive list of services and their classifications. It is a base list and not exhaustive. Punjab has delinked the classification of services from Pakistan Customs Tariff. The second schedule covers taxable services. Its exclusions are basically exemptions. Since the definition of the term “service or services” given in the statute (sub-section (38) of section 2) is very exhaustive, rather all-inclusive, there are four categories of services in the context of Punjab Sales Tax on Services Act, 2012 as follows: -

- (i) Services which are services in business parlance and practice but not covered in the first schedule.
- (ii) Services which are covered in the first schedule of the 2012 Act.
- (iii) Services which are taxable under the second schedule of the Act.
- (iv) Services which are included in the exclusions of the second schedule and are hence exempt.

Thus, the services which are neither taxable nor exempt are non-taxable services. For the purposes of benefits and privileges under VAT, exempt and non-taxable services are treated interchangeably on equal footing. The statute does not provide for automatic zero rating of any services. PRA may however, grant refund on the export of services (see section 12).

7. The system of sales tax as provided under the Punjab Sales Tax on Services Act, 2012 has several silent features. The fundamental principle of the system is that every person who is carrying out an economic activity and thus engaged

in providing taxable service or services is liable to charge, collect and pay sales tax on such services. For this purpose, he needs registration (which is free of any fee or charge) whereupon he can issue tax invoices. Application for registration is required to be filed in a prescribed form and in the manner specified by PRA in the relevant rules. He is required to pay sales tax due on his services on monthly basis (unless the period has been extended by PRA in case of any category of registered persons or services) through a return in a prescribed form and manner. He will keep record (as per his convenience) and will be liable to sporadic audits by the PRA's functionaries. However, no undeclared tax liability will be determined through audit or otherwise by the PRA department without the process of adjudication based upon the internationally recognized principles of natural justice and fairplay. Besides revision, three appeal opportunities are available. However, the third appeal opportunity in the form of reference to the High Court against the orders of Appellate Tribunal is confined only to questions of law. Judgments of the High Courts shall of course be appealable before the Supreme Court as per law of the land. Moreover, alternative dispute resolution (ADR) system has also been provided under which tax disputes can be settled through public- private sectors partnership.

8. In order to implement the provisions of the Punjab Sales Tax on Services Act, 2012, PRA has drafted different rules covering the following regimes.

- Definitions.
- Registration and De-registration.
- Filing of Returns.
- Adjustment of Tax.
- Specific Provisions.
- Computerized System.
- Authorized Representatives.
- Audit.
- Adjudication and Appeals.
- Alternative Dispute Resolution.
- Recovery.

In order to facilitate the service sector businesses right from the outset, PRA has honoured and accepted the registrations of FBR relating to the services chargeable to sales tax in the province of Punjab. The businesses who already have a FBR's registrations need not to apply to PRA for new registrations. Their registrations will be

automatically adopted by the PRA computer system with the help of Pakistan Revenue Automation Ltd. A prefix “P” will be added to their registration numbers under intimation to them. The other important features of the sales tax on services system as adopted in Punjab are as follows: -

- (i) A common jargon of VAT already popular amongst the taxpayers’ community has been used in the Act as well as in the rules.
  - (ii) There is no exemption threshold for any of the taxable services except hotels about which PRA will soon announce its decision.
  - (iii) There will be no input tax adjustment admissible in respect of tax liability dischargeable on account of the application of the principles of origin and reverse charge as envisaged in section 4 of the Act.
  - (iv) Apportionment formula shall apply where a person is providing both taxable and exempt (including non-taxable) services.
  - (v) Credit of tax paid on goods and services paid either under Federal or under Provincial sales tax law shall be admissible to the extent and subject to the conditions and restrictions specified in the rules on the subject of adjustment of tax.
  - (vi) In respect of tax assessment, the principal concept of “open market price” has been adopted for valuation of taxable services.
  - (vii) The whole system is based upon the globally applauded principles of “voluntary compliance” such as self-assessment, self-recordkeeping, self-declaration and self-policing etc.
  - (viii) The system provides for the application of a “structured approach” towards taxation and tax-implementation. That is why clear and detailed rules have been prepared to curtail the discretion of the PRA’s tax officials and protect the bonafide rights and entitlements of the taxpayers.
  - (ix) Besides electronic filing of applications, statements, declarations and returns, manual filing facility has also been provided.
  - (x) Several provisions have been introduced whereunder bonafide mistakes and genuine self-corrections of the taxpayers are automatically condonable under the system.
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