



**AUDIT REPORT  
ON  
THE ACCOUNTS OF  
FEDERAL BOARD OF REVENUE  
(INLAND REVENUE & CUSTOMS)  
AUDIT YEAR 2024-25**

**AUDITOR-GENERAL OF PAKISTAN**  
SERVING THE NATION BY PROMOTING ACCOUNTABILITY,  
TRANSPARENCY AND GOOD GOVERNANCE IN THE MANAGEMENT  
OF PUBLIC RESOURCES  
FOR THE CITIZENS OF PAKISTAN



## Preface

Articles 169 and 170 of the Constitution of the Islamic Republic of Pakistan, 1973 read with Sections 8 and 12 of the Auditor-General's (Functions, Powers and Terms and Conditions of Service), Ordinance 2001 require the Auditor-General of Pakistan to conduct the audit of expenditures and receipts of the Government of Pakistan.

This report is based on the audit of receipts of Inland Revenue & Customs and expenditures of the Federal Board of Revenue for the Financial Year 2023-24. The report also includes some observations related to the previous years. Directorates-General Audit Inland Revenue & Customs, Lahore and Karachi conducted the audit during the audit year 2024-25 on test check basis with a view to report significant findings to the stakeholders. The main body of the Audit Report includes systemic issues and material audit findings. Relatively less significant issues are listed in Annexure-1 which shall be pursued with the Principal Accounting Officer separately at the DAC level. In cases where the PAO does not initiate appropriate action, these audit observations will be brought to the notice of Public Accounts Committee through next year's audit report.

Three special types of audit have also been included in this report. Firstly, an *impact audit* evaluates effectiveness of FBR's policy initiatives on industrial investments. Secondly, *sectoral audit* analyzes the implications of tax amnesty schemes on real-estate sector. Thirdly, through *thematic audit* an attempt has been made to analyze and gain insight into impediments affecting revenue generation from the steel sector.

Audit findings indicate the need for adherence to the regularity framework besides instituting and strengthening internal controls to avoid recurrence of similar violations and irregularities.

Audit observations included in this report have been finalized in the light of departmental replies and discussions in DAC meetings held in July, October, November, December 2024 and January 2025.

There are certain audit observations which were also reported in Audit Reports for the last five financial years. Recurrence of such irregularities is a matter of concern and needs to be addressed.

This Audit Report is submitted to the President of Pakistan in pursuance of Article 171 of the Constitution of the Islamic Republic of Pakistan, 1973 for causing it to be laid before both Houses of the Majlis-e-Shoora [Parliament].

Islamabad  
Dated:

(Muhammad Ajmal Gondal)  
**Auditor-General of Pakistan**



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## **ABBREVIATIONS & ACRONYMS**

AGP	Auditor-General of Pakistan
AGPR	Accountant General Pakistan Revenues
ABAD	Association of Builders and Developers
AC	Assistant Commissioner/Collector
AEOI	Automatic Exchange of Information
AFU	Air Freight Unit
AI	Artificial Intelligence
AIIA	Allama Iqbal International Airport
AMIS	Audit Management Information System
ANOVA	Analysis of Variance
ATIR	Appellate Tribunal Inland Revenue
BMR	Balancing, Modernization and Replacement
BTB	Broadening of Tax Base
BWH	Bonded Warehouse
CCIR	Chief Commissioner Inland Revenue
CGO	Customs General Order
CoC	Collectorate of Customs
CNIC	Computerized National Identity Card
CPR	Computerized Payment Receipt
CTO	Corporate Tax Office
CVT	Capital Value Tax
DAO	District Accounts Office
DBA	Data Base Administrator
DAC	Departmental Accounts Committee
DAGP	Department of Auditor-General of Pakistan
DC	Deputy Commissioner/Collector
DDO	Drawing and Disbursing Officer
DFSL	Duty-Free Shops (Pvt.) Limited
DP	Draft Para
DR&S	Directorate of Research and Statistics

DTRE	Duty and Tax Remission for Exports
EDS	Exports Development Surcharge
EFS	Export Facilitation Scheme
EOU	Export Oriented Units
ERS	Expeditious Refund System
FASTER	Fully Automated Sales Tax Electronic Refund
FATA	Federally Administered Tribal Areas
FATE	Facilitation and Taxpayer Education
FBR	Federal Board of Revenue
FED	Federal Excise Duty
FIR	First Information Report
FMT	Fair Market Value
FTA	Free Trade Agreement
FY	Financial Year
GB	Gilgit Baltistan
GCCI	Gujranwala Chamber of Commerce & Industries
GD	Goods Declaration
GDP	Gross Domestic Product
GFR	General Financial Rules
GSP	Generalized System of Preferences
HQ	Head Quarter
HS Codes	Harmonized System Codes
ICT	Islamabad Capital Territory
IDT	Indirect Taxes
I&I	Intelligence and Investigation
IGM	Import General Manifest
IMF	International Monetary Fund
IOCO	Input Output Coefficient Organization
IREN	Inland Revenue Enforcement Network
IRIS	Inland Revenue Information System
IT	Information Technology
IR	Inland Revenue
JIAP	Jinnah International Airport

KPI	Key Performance Indicator
KPK	Khyber Pakhtunkhwa
Ltd	Limited
LTO	Large Taxpayers Office
MFDAC	Memorandum for Departmental Accounts Committee
MMBTU	Metric Million British Thermal Unit
MPR	Monthly Performance Report
MT	Metric Ton
MTO	Medium Taxpayers Office
NBP	National Bank of Pakistan
NESPAK	National Engineering Services Pakistan
NOC	No Objection Certificate
NTC	National Tariff Commission
NTN	National Tax Number
NLC	National Logistics Corporation
NPO	Non-Profit Organization
PBS	Pakistan Bureau of Statistics
PCA	Post-Clearance Audit
PFM	Public Finance Management
PMBQ	Port Muhammad Bin Qasim
PoS	Point of Sales
PRA	Post-Refund Audit
PAC	Public Accounts Committee
PAO	Principal Accounting Officer
PATA	Provincially Administered Tribal Areas
PCT	Pakistan Customs Tariff
POL	Petroleum Oil & Lubricants
PPRA	Public Procurement Regulatory Authority
PRAL	Pakistan Revenue Automation Limited
Pvt	Private
RCPS	Refund Claims Preparatory System
RMS	Risk Management System
RTO	Regional Tax Office

SAPT	South Asia Pacific Terminal
SBP	State Bank of Pakistan
SOPs	Standard Operating Procedures
SRO	Statutory Regulatory Order
STARR	Sales Tax Automated Refund Repository
STGO	Sales Tax General Order
SWAPS	Synchronized Withholding Administration and Payment System
SWH	State Warehouse
TDAP	Trade Development Authority of Pakistan
UIN	Unique Identification Number
USD	United States Dollar
VAT	Value Addition Tax
WeBOC	Web-based One Customs
WEO	World Economic Outlook
WDI	World Development Indicators
WPPF	Workers' Profit Participation Fund
WWF	Workers' Welfare Fund

## **EXECUTIVE SUMMARY**

The Directorates-General of Audit Inland Revenue and Customs are mandated to conduct regularity audit (financial attest audit and compliance with authority audit), as well as performance, impact, thematic and special audits and audit of Foreign Aided Projects of the Federal Board of Revenue (FBR). A risk-based audit of federal receipts collected and the expenditure incurred by FBR, was carried out. The FBR receipts include Income Tax, Sales Tax, Customs Duties, Federal Excise Duty (FED), Sales Tax on Services under Islamabad Capital Territory (ICT), Workers' Welfare Fund (WWF) and Workers' Profit Participation Fund (WPPF).

The objectives of the financial-attest audit/compliance with authority audit were to examine the accuracy of assessments and levy, collection and deposit of revenue into the government treasury in accordance with prevailing laws. Furthermore, the effectiveness of internal controls and checks relating to FBR's functions was also examined. On the expenditure side, the objective was to ascertain the consistency of expenditure with the nature and purposes of the appropriations and applicable legislation/rules/regulations.

Directorates-General of Audit Inland Revenue and Customs, Lahore and Karachi also conducted the following impact, sectoral and thematic audits which have been included as Chapters 9, 10 and 11 in this report.

Impact Audit of "Income Tax Credit Allowed Through Increase of Share Capital" analyzes whether tax credits indeed led to the objectives of increase in industrial investments. The audit findings indicate that a relatively limited number of taxpayers have opted to benefit from this scheme, and a few taxpayers have claimed tax credits without fulfilling the stipulated conditions, potentially leading to undue benefits and revenue leakages. The reasons for limited number of beneficiaries opting for the scheme could be high cost of production, infrastructure issues and lack of awareness.

Sectoral Audit of "Taxation in Real Estate Sector" was conducted with a view to assess the implications of amnesty schemes and taxation relief measures introduced by the Government to improve tax compliance and bring more individuals into the national tax net. These schemes were designed to encourage investments in the construction sector by providing significant tax incentives and

easing certain regulatory requirements. However, audit results showed that despite availing the benefits of scheme, taxpayers did not adhere to the conditions imposed and there was no visible increase in contribution of real estate sector to the economy, as envisaged under objectives of the scheme. The study divulged that causes of limited success of scheme included informal nature of real estate sector and a culture of evasion of tax by builders and developers in general.

Thematic Audit on “Sales Tax Mechanism in the Steel Sector” was conducted to gain insight into the operational impediments that were hampering or affecting optimal revenue generation from the steel sector. Following the decline in the import and production of steel in 2017, due to slow demand in the construction and automobile sectors, the Government of Pakistan introduced the facility of one-time charging of sales tax on the minimum price of steel to support the industry. The findings of this audit revealed that the incentive of minimum price fixing had been misused by manufacturers, who claimed inadmissible input tax in contravention of the prescribed rules. Additionally, blacklisted entities were allowed unjustified adjustment of input tax on purchases made. Furthermore, the FBR failed to bring local suppliers into the tax net, resulting in a loss of potential revenue.

#### **a. Scope of Audit**

Directorates-General of Audit conducted the audit of FBR’s receipts and expenditures. Total expenditure and receipts of the FBR formations were Rs 44.43 Billion and Rs 9,299.10 Billion respectively for the FY 2023-24. Audit coverage of expenditure for the current audit year was Rs 32.22 Billion (72 formations) and of receipts was Rs 5,013.47 Billion (123 formations). In terms of the percentage of the auditable amount, the audit coverage for receipts and expenditure was around 09% and 21% respectively.

The audit report also includes audit observations from the previous FY 2022-23, pertaining to the audit of expenditure of Rs 4.89 Billion (11 formations) and revenue of Rs 7,960.35 Billion (82 formations). A sectoral audit, an impact audit and a thematic audit are also part of this report.

#### **b. Recoveries at the Instance of Audit**

As a result of the audit, a recovery of Rs 925,841.59 million was pointed out. The recovery effected from January to December 2024 was Rs 19,265.05

million. There was a 25% increase in the amount of recovery pointed out compare to the previous FY.

**c. Audit Impact**

In addition to safeguarding the public exchequer, the Directorates-General of Audit reviewed and suggested improvements in the business processes of FBR to address larger questions of efficiency, fairness and effectiveness. This is reflective of the fact that the orientation of Audit has evolved over the years and moved away from traditional compliance and regularity audit.

- i) After pointation of various loopholes in a Sectoral Audit Report on Tax Evasion/Avoidance in Sugar and Cement Sectors in Audit Year 2022-23 and also on the recommendation of audit, FBR extended the implementation of Track and Trace System in cement industry in November, 2023. FBR has now shifted the accountal of production and sale of cement industry to the Track and Trace System, thereby ensuring the accurate reporting of production, sales and revenue, and improving tax compliance and enhancing government revenue.
- ii) After repeated pointation through various audit observations on sales tax and income tax refund in previous audit reports, FBR has introduced in all its field tax offices, a separate refund zone, to be headed by a Commissioner IR (Refund) who is exclusively entrusted with the function of processing, sanctioning and approving sales tax and income tax refunds. After introduction of these specific zones for refund, the issues of non-compliance, irregularities and other procedural lapses are more likely to be minimized thereby improving the tax compliance culture in future.
- iii) Audit repeatedly pointed out in Audit Reports 2019-20 and onwards that importers were taking concessions of lower rate of customs duty by wrongly availing benefit of Fifth Schedule to Customs Act, 1969, although imported goods were liable to be cleared at statutory rate of 16% and above, whereas concession was available only to the goods having statutory rates of duty of 3% and 11% as per Condition (iv) of the Schedule. In line with

the recommendations of Audit, necessary amendments in the Fifth Schedule have been incorporated through Finance Act, 2022.

- iv) The Audit has time and again identified cases wherein duties and taxes were non/short realized by the tax authorities, based on which, FBR has effected recovery of the short-paid duties and taxes worth billions of rupees.

#### **d. Audit Methodology**

Risk-based analytical approach was adopted during the planning phase to identify priority areas in terms of identified risks in receipts and expenditure. In addition to the above, field audit teams also drew samples from the data available with the field formations. Concurrent audit methodology was employed for collection of data for impact, sectoral and thematic audits through field audit teams primarily deployed for regularity audit. During the impact audit, opinion/suggestions from relevant Chambers of Commerce & Industries were also sought. Further, Audit employed statistical methods of data analysis including time series, trend analysis and regression analysis to arrive at conclusions and substantiate the audit findings.

#### **e. Comments on Internal Audit and Internal Controls**

This office requisitioned internal audit reports alongwith other information to evaluate performance of the internal audit function of FBR. However, no record had been shared with audit till finalization of this report. In the absence of information in respect of internal audit, the audit was unable to directly comment on the performance of internal audit function of FBR. However, the recurrence of audit observations on similar issues over the years indicates systemic weaknesses in internal audit mechanism of FBR.

#### **f. Key Audit Findings of the Report**

Overall audit findings highlight the following key issues:

- Systemic weakness in audit of tax assessments leading to leakage and less collection of tax from existing taxpayers
- A weak litigation mechanism due to which potential tax revenue of huge amounts continues to remain blocked in court cases

- Continued lapses in efforts at effective broadening of tax base, and gaps in implementation of initiatives like track-and-trace system, have limited the envisaged benefits. Furthermore, enhanced number of taxpayers has not necessarily translated into an expansion in the revenue base
- Weakly designed and implemented initiatives, like the tax amnesty and tax incentive schemes, did not yield the desired results and suffered abuse due to irregularities

### **Impact, Sectoral and Thematic Audit**

This audit report contains impact, sectoral and thematic audit regarding tax credits under 65E, reliefs provided to real estate sector and sales tax collection from steel sector respectively. Impact audit on effects of tax credit under Section 65E revealed that even though the tax credit led to increase in sales of some individual entities, there was minimal economy-wide effect, and overall adoption of the scheme by the industry was quite limited. Furthermore, instances of wrong claims of tax credits either on account of late registration or beyond stipulated period were witnessed by Audit. Sectoral audit of taxation on real estate sector disclosed that despite availing the benefits of relief in taxation, beneficiaries did not adhere to the conditions of the scheme and there were several cases of loss of potential revenue due to non-compliance of Section 100D by builders and transfer of property on fake NTN/CNICs. Thematic audit of sales tax collection from steel sector also pointed out huge losses to national exchequer on account of non-realization of sales tax from blacklisted persons and inadmissible adjustment of input tax. Following are some key irregularities identified during respective audits which further highlight the need for putting in place robust controls and effective monitoring and evaluation mechanism while designing and implementing tax incentive schemes.

- i) Claim of tax credit after due date of registration for incentive scheme amounting to Rs 3,882.61 million.<sup>1</sup>
- ii) Claim of tax credit beyond stipulated period of five years of Rs 2,461.47 million.<sup>2</sup>
- iii) Potential loss of revenue due to non-compliance of conditions of Rule 4 & Section 100D, pertaining to real estate sector, by builders and developers of Rs 8,385.75 million.<sup>3</sup>

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<sup>1</sup>Impact Audit 4.4.1 & <sup>2</sup>Para 4.4.2, Sectoral Audit <sup>3</sup>Para 5.1.3

- iv) Irregular/inadmissible tax credit allowed under Section 236K to purchaser/transferees of property on fake NTN/CNICs amounting to Rs 557.77 million.<sup>4</sup>
- v) Non-recovery of sales tax from blacklisted persons in the steel sector amounting to Rs 512.01 million.<sup>5</sup>
- vi) Inadmissible adjustment of input tax on goods and services in steel sector amounting to Rs 249.78 million<sup>6</sup>.

### **Regularity Audit**

Compliance audit of FBR revealed several instances of huge losses to national exchequer owing to weaknesses in internal control mechanisms of the department, deficiencies in audit procedures and sampling of the department at the key formations levels as well as weak follow up of audit observations brought in to the notice of the department in the previous years which resulted in repetition of similar systemic issues. As a testimony to above mentioned issues there were significant audit findings in the area of direct/indirect taxes amounting to Rs 643,822.86 million. For the area of customs/expenditure, main findings aggregated to Rs 19,385.88 million. These audit findings are based on a selected list of field formations which are further audited on sample basis indicating thereby that the actual scale of irregularities could be much higher.

### **Income Tax**

- i) 22 field offices of FBR did not realize or short-realized minimum tax amounting to Rs 22,874.66 million in 1652 cases<sup>7</sup>
- ii) 20 field offices of FBR did not realize super tax amounting to Rs 167,887.87 million in 1,026 cases.<sup>8</sup>
- iii) 18 field offices of FBR short-realized income tax due to claims of inadmissible expenses amounting to Rs 149,571.28 million in 1,084 cases.<sup>9</sup>
- iv) 19 field offices of FBR did not recover withholding tax of Rs 45,386.45 million in 1344 cases.<sup>10</sup>
- v) 16 field offices of FBR did not recover tax demands amounting to Rs 62,318.02 million in 1571 cases.<sup>11</sup>

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Sectoral Audit <sup>4</sup>Para 5.3.2, Thematic Audit <sup>5</sup>Para 7.2 & <sup>6</sup>Para 7.3, Regularity Audit <sup>7</sup>Para 4.1, <sup>8</sup>Para 4.2, <sup>9</sup>Para 4.3, <sup>10</sup>Para 4.4, <sup>11</sup>Para 4.5

- vi) 19 field offices of FBR sanctioned inadmissible adjustment/claim of refund amounting to Rs 6,795.41 million in 817 cases.<sup>12</sup>
- vii) 6 field offices of FBR short-realized tax due to non-apportionment of expenses amounting to Rs 2,253.86 million in 15 cases.<sup>13</sup>
- viii) Non-simplification of tax return forms & procedures and delayed refunds.<sup>14</sup>

### ***Sales Tax/FED***

- i) 19 field offices of FBR did not monitor inadmissible adjustment of input tax credit on invoices of suspended/blacklisted taxpayers/fake invoices amounting to Rs 123,585.02 million in 375 cases.<sup>15</sup>
- ii) 10 field offices of FBR short-realized sales tax due to non-apportionment of input tax amounting to Rs 8,539.37 million in 196 cases.<sup>16</sup>
- iii) 15 field offices of FBR did not realize sales tax amounting to Rs 35,974.73 million due to concealment of sales by taxpayers in 992 cases.<sup>17</sup>
- iv) 17 field offices of FBR did not prevent loss of revenue due to inadmissible exemptions of sales tax amounting to Rs 7,481.09 million in 508 cases.<sup>18</sup>
- v) 14 field offices of FBR short-realized sales tax due to inadmissible adjustment of input tax credit of Rs 5,521.66 million in 618 cases.<sup>19</sup>
- vi) 19 field offices of FBR did not impose penalties and default surcharge amounting to Rs 3,535.12 million in 9582 cases.<sup>20</sup>
- vii) 3 field offices of FBR did not register potential taxpayers liable for registration involving Rs 1,310.10 million in 121 cases.<sup>21</sup>
- viii) 4 field offices of FBR short realized federal excise duty on sales of natural gas/cement/air ticket of Rs 788.22 million in 5 cases.<sup>22</sup>

### ***Customs Duty***

- i) 27 field offices of FBR in 4396 cases did not dispose-of confiscated goods /vehicles amounting to Rs 12,600.09 million.<sup>23</sup>

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<sup>12</sup>Para 4.6, <sup>13</sup>Para 4.7, <sup>14</sup>Para 12.2, <sup>15</sup>Para 5.1, <sup>16</sup>Para 5.2, <sup>17</sup>Para 5.3, <sup>18</sup>Para 5.4, <sup>19</sup>Para 5.5, <sup>20</sup>Para 5.6, <sup>21</sup>Para 5.7, <sup>22</sup>Para 6.1 & 6.2, <sup>23</sup>Para 7.1

- ii) 5 field offices of FBR incurred loss of revenue due to non/short-realization of revenue on un-exported finished goods of Rs 3,288.51 million in 104 cases.<sup>24</sup>
- iii) 16 field offices of FBR granted inadmissible exemptions and concessions in duties and taxes amounting to Rs 1,556.52 million in 1,628 cases.<sup>25</sup>
- iv) 14 field offices of FBR short-realized of duties and taxes due to misclassification of imported goods of Rs 1,162.63 million in 5357 cases.<sup>26</sup>
- v) 4 field office of FBR did not realize of revenue due to non-clearance of warehoused goods of Rs 253.64 million in 57 cases.<sup>27</sup>

### ***Expenditure***

- i) FBR (HQ) and its 22 field offices made inadmissible payment on account of cash reward amounting to Rs 484.44 million in 40 cases.<sup>28</sup>
- ii) FBR (HQ) and its 17 field offices incurred expenditure by non-observance of Public Procurement Rules of Rs 40.05 million in 53 cases.<sup>29</sup>

### **g. Audit Recommendations**

- i) There should be a structured risk management and monitoring and evaluation mechanism in FBR to ensure that the desired objectives of initiatives like tax incentives and exemptions, are achieved so that corrective action could be taken timely.
- ii) In case of tax credits under 65E, clear enforcement protocols should be established for claims submitted after the stipulated deadlines, and claims made after due registration dates or beyond the five-year period should be disqualified, barring exceptional justification.
- iii) In case of tax relief measures in real estate sector, the department should get details of land area developed and constructed area built in Sq. Ft. by the builders and developers, finalize the assessment orders and recover the due amount of tax as per law.

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<sup>24</sup>Para 7.3, <sup>25</sup>Para 7.5, <sup>26</sup>Para 7.7, <sup>27</sup>Para 7.15, <sup>28</sup>Para 8.1 & <sup>29</sup>Para 8.6

- iv) The department should put in place validation checks while generating Computerized Payment Receipts (CPRs) in the E-Portal of Inland Revenue Information System (IRIS), to ensure that no CPR is generated without filling of mandatory fields, to plug the loopholes in the electronic tax collection system.
- v) Prompt recovery of the specified amount of tax should be made from the blacklisted persons besides, initiation of legal proceedings against the suppliers and buyers.
- vi) The department should recover the short-paid amount of tax due to inadmissible input tax adjustment along with penalties thereof.
- vii) The department should expedite recovery of admitted amount, pursue subjudice cases at appropriate fora and finalize legal proceedings besides strengthening of desk audit for assessment of minimum tax and super tax. Moreover, dedicated teams by hiring the competent lawyers may be deputed to pursue the cases at appellate fora for decision of the cases within stipulated period through strict monitoring and pursuance at senior level.
- viii) The department needs to strengthen monitoring controls by a dedicated supervisory team independent from the assessment function and should also ensure the post refund audits.
- ix) The department must ensure strengthening of the validation checks in return filing system for apportionment of expenses between final and normal tax regimes. Moreover, risk-based desk audit needs to be implemented in true letter and spirit besides periodic review and updating of the RMS.
- x) In collaboration with field tax offices and chambers of commerce and industries, FATE Wing should make efforts for simplifying the tax return forms to increase the voluntary tax compliance by the taxpayer.
- xi) IT-system based controls need to be introduced to disallow/defer input tax adjustments claimed on invoices issued by blacklisted/suspected registered persons.
- xii) The department should put in place systematic checks in the sales tax return filing system to link and cross-verify the claimed input for apportionment between taxable and exempt supplies.

- xiii) The department must ensure comprehensive integration of sales tax and income tax return filing systems besides 100% desk audit of exemptions claimed by taxpayers.
- xiv) The department needs to expedite the disposal of confiscated goods/ vehicles and over-stayed warehouse goods and pursue/expedite the cases for early recovery besides exploring introduction of artificial intelligence/system-based controls in WeBOC system to avoid claim of inadmissible exemptions/ concessions in duty & taxes.
- xv) The department should ensure classification of goods as per general rules for interpretation, description of goods provided in the First Schedule and guidelines contained in explanatory notes.
- xvi) The department must ensure compliance to DTRE rules regarding non-performing DTRE users.
- xvii) The department should strictly follow the system of payment of cash rewards and monitor the enforcement of defined criterion of meritorious services.
- xviii) The department should follow the laid down rules, regulations and procedures as enunciated in the PPRA Act, 2004.

## CHAPTER-1 PUBLIC SECTOR FINANCIAL MANAGEMENT ISSUES

This chapter highlights significant issues related to financial management, accounting, and reporting by the Federal Board of Revenue.

The accounting of receipt vouchers is performed primarily by FBR itself through departmental treasuries. FBR provided the collection record of its receipts (source documents–figures reported by FBR to Finance Division). The Audit analysed Civil Accounts received from AGPR Islamabad and figures of tax receipts from the main office of the State Bank of Pakistan, Karachi and the Head office of the National Bank of Pakistan, Karachi. The observations of Directorates-General Audit Inland Revenue and Customs, Lahore and Karachi are clubbed into the following paras;

### 1.1 Variation in figures of tax receipts (Net) between FBR and SBP - Rs 18,152 million

According to Para 3.4.2.12 of the Manual of Accounting Principles, each entity is required to reconcile its books of accounts with the bank record at the close of each month. This reconciliation is to be performed in accordance with policies and procedures set out in para 5.5.9 and 6.5.2 of the Accounting Policies and Procedures Manual.

Scrutiny of figures of tax receipts of SBP and the figures reported by FBR showed that there was a variation of Rs 18,152 million for the FY 2023-24 in respect of net tax receipts as summarized below:-

*(Rs in million)*

S#	Head of Accounts	Collection figures of FBR**	Collection figures of SBP (NET)*	Variation
1	Income Tax	4,461,337	4,477,815	(16,478)
2	Customs	1,082,783	1,082,940	(157)
3	Sales Tax	3,086,832	3,080,111	6,721
4	FED	569,854	578,092	(8,238)
	<b>Total Taxes</b>	<b>9,200,806</b>	<b>9,218,958</b>	<b>(18,152)</b>

\*Source: As per record of SBP provided to Audit for FY 2023-24

\*\*Source: Figures reported by DR&S to Finance Division up to June (Final) 2024.

This may impair true and fair presentation of financial statements because the receipts figure of FBR was on lower side as compared to the actual cash collected and reported by the State Bank of Pakistan.

The management replied that Audit has not taken into account the factors of “Book Adjustments and Exports Development Surcharge (EDS)” as those are required to be added in the collection of SBP. Had these figures been already included in the SBP’s collection, there would not have been such a huge variation as mentioned by the Audit. State Bank of Pakistan (SBP) provided final figures of net tax collection after taking into account all adjustment/recalled refund.

The Audit is of the view that after taking care of all the adjusting/transfer entries, there should not have been any variations left between the FBR/AGPR/SBP figures.

The DAC, in its meeting held in November 2024, discussed the matter in detail and directed the DR&S to get the stated position verified from Audit within 15 days. No further progress was reported till the finalization of this report.

The Audit recommends monthly reconciliation of receipts between FBR and SBP to accurately report on Federal Government accounts.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 1.1 (of each Audit Report) having a financial impact of Rs 36,426 million. The recurrence of the same irregularity is a matter of serious concern.

## **1.2 Variation in figures of refund of tax receipts between FBR and SBP - Rs 18,357 million**

According to Para 3.4.2.12 of the Manual of Accounting Principles, each entity is required to reconcile its books of accounts with the bank record at the close of each month. This reconciliation is to be performed in accordance with the policies and procedures set out in para 5.5.9 and 6.5.2 of the Accounting Policies and Procedures Manual.

Scrutiny of refund record of the FBR (figures up to June Final 2024), revealed variations in figures of refunds on account of Income Tax, Customs and Sales Tax amounting to Rs 18,357 million. The SBP’s total was lower than FBR’s as tabulated below: -

*(Rs in million)*

<b>Refund</b>	<b>Figures of refund/rebate of FBR*</b>	<b>Figures of refund/rebate of SBP **</b>	<b>Variation</b>
<b>Income Tax</b>	53,125	34,266	18,859
<b>Customs</b>	30,541	30,794	(253)
<b>Sales Tax</b>	398,192	398,441	(249)
<b>Total</b>	<b>481,858</b>	<b>463,501</b>	<b>18,357</b>

\* Source: Figures provided by FBR

\*\* Source: Figures provided by SBP

This may impair the true and fair presentation of financial statements because the refund figures from external source i.e. SBP were on lower side.

The management replied that FBR's figures of refunds are based on PRAL's dashboard which might include some adjustments under both "gross" and "refunds" figures, particularly under the head of Income Tax, and having no overall impact on the "net" figures. The management contested that it was unable to offer comments on these variations at this point of time as micro level reconciliation between FBR's treasuries and AGPR's sub-offices was held up and no reconciliation certificates were available with their office to know the actual refunds position.

Audit is of the view that after passing all the adjusting/transfer entries, there is still variation between the FBR/AGPR/SBP figures.

The DAC, in its meeting held in November 2024, discussed the matter in detail and directed the DR&S to provide breakup of refund adjustments and cash refunds to explain the difference in figures and get the same verified by audit within 15 days. No further progress was reported till the finalization of this report.

The Audit recommends monthly reconciliation of refund/rebate figures between FBR and SBP to enable more accurate reporting in the Federal Government accounts.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 1.2 (of each Audit Report) having a financial impact of Rs 86,006 million. The recurrence of the same discrepancy is a matter of concern and shows systemic nature of the issue which need to be resolved.

### **1.3 Variation in figures of tax receipts (Net) between FBR and AGPR - Rs 259 million**

According to Para 3.4.2.12 of the Manual of Accounting Principles, each entity is required to reconcile its books of accounts with the bank record at the close of each month. This reconciliation is to be performed in accordance with the policies and procedures set out in para 5.5.9 and 6.5.2 of the Accounting Policies and Procedures Manual.

Scrutiny of the data provided by AGPR and data statements provided by FBR upto the month of June (Final) 2024, showed that there was a variation of Rs 259 million in respect of net tax receipts summarized is as follows:

(Rs in million)

Head of account	Collection Figures of FBR**	Collection Figures of AGPR *	Variation
Income Tax	4,461,337	4,452,777	8,560
Customs	1,082,783	1,086,392	(3,609)
Sales Tax	3,086,832	3,091,529	(4,697)
FED	577,500	578,013	(513)
<b>Total Taxes</b>	<b>9,208,452</b>	<b>9,208,711</b>	<b>(259)</b>

\* Source: Scrutiny of data for the year 2023-24 prepared by AGPR, Islamabad

\*\* Source: Statement prepared by FBR up to June (Final) 2024.

This difference in tax collection figures may impair the true and fair presentation of financial statements of the Federal Government.

The department replied that the Audit has compared the “net” figures of the SBP and office of the AGPR. Both the departments are responsible to explain their position in the matter. It would therefore, be more appropriate if the subject audit observation is taken up by the Audit with the SBP and AGPR for an appropriate/ accurate reply.

The DAC, in its meeting held in November 2024, discussed the matter in detail and AGPR explained the reasons for apparent differences in the data included in the audit observation. After thorough deliberations, DAC directed the AGPR to provide the required figures within 30 days to Audit.

The Audit recommends establishment of IT linkage between FBR treasuries and AGPR to enable in-month or real-time reporting of receipts to AGPR, and at least monthly reconciliation of receipts between FBR and AGPR, to accurately report on Federal Government accounts.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20 and 2023-24 vide para numbers 1.3 and 1.4 having a financial impact of Rs 76 million. The recurrence of the same irregularity is a matter of serious concern.

#### **1.4 Variation in figures of refund of tax receipts between FBR and AGPR – Rs 20,254 million**

According to Para 3.4.2.12 of the Manual of Accounting Principles, each entity is required to reconcile its books of accounts with the bank record at the close of each month. This reconciliation is to be performed in accordance with the policies and procedures set out in para 5.5.9 and 6.5.2 of the Accounting Policies and Procedures Manual.

Scrutiny of refund record (figures up to June Final 2024), revealed variations in figures of refunds on account of Income Tax, Customs and Sales Tax amounting to Rs 20,254 million. The FBR's total figures for refunds was higher than AGPR's as tabulated below: -

*(Rs in million)*

<b>Refund</b>	<b>Figures of refund/rebate of FBR*</b>	<b>Figures of refund/rebate of AGPR **</b>	<b>Variation</b>
Income Tax	53,125	32,996	20,129
Customs	30,541	30,264	277
Sales Tax	398,192	398,344	(152)
<b>Total</b>	<b>481,858</b>	<b>461,604</b>	<b>20,254</b>

\* Source: Provisional Figures reported by DRS, Islamabad for the FY 2023-24

\*\* Source: Figures as per FCA June (Final) 2024 prepared by AGPR, Islamabad

This difference in refund figures may impair the true and fair presentation of financial statements.

The management replied that FBR's figures of refunds are based on PRAL's dashboard which might include some adjustments under both "gross" and "refunds" figures, particularly under the head of Income Tax, having no overall impact on the "net" figures. The management, however, stated that it was unable to offer comments on these variations as detailed reconciliation between FBR's treasuries and AGPR's sub-offices was held up and no reconciliation certificates were available with their office to ascertain the actual refunds position.

Audit is of the view that FBR treasuries and DR&S (FBR) should obtain transaction-wise data from SBP/NBP and carry out meaningful reconciliation of two sets of accounts with AGPR/SBP/NBP at micro and macro level for sorting out the requisite differences.

The DAC, in its meeting held in November 2024, discussed the matter in detail and directed the DR&S to provide breakup of refund adjustment and cash refund to explain the differential and get the same verified from Audit within 15 days. No further progress was reported till the finalization of this report.

The Audit recommends monthly reconciliation of receipts between FBR and AGPR/SBP/NBP to accurately report on Federal Government accounts.

**Note:** The issue was also reported earlier in the Audit Report for the Audit Year 2022-2023 vide para number 1.3 having a financial impact of Rs 1,607 million.

## **CHAPTER-2 FEDERAL BOARD OF REVENUE**

### **2.1 Introduction**

#### **A. Background**

The Federal Board of Revenue Act 2007 governs the Federal Board of Revenue (FBR). The Board comprises of at least seven members, headed by a Chairman appointed by the Federal Government. The powers of FBR to collect taxes are currently embodied in the Income Tax Ordinance 2001, Sales Tax Act 1990, Federal Excise Duty Act 2005, Customs Act 1969 and Islamabad Capital Territory (Tax on Services) Ordinance 2001. These statutory laws are amended through the Finance Act/Ordinance to implement budget proposals of the Federal Government. FBR operates as an attached department of the Revenue Division as per Rules of Business 1973.

The FBR is responsible for collecting income tax, sales tax, federal excise duty, customs duty and tax on services rendered under the territorial jurisdiction of Islamabad Capital Territory (ICT). Moreover, FBR is also responsible for collecting the Workers' Welfare Fund under the Workers' Welfare Fund Ordinance 1971 and the Workers' Profit Participation Fund, established under the Workers' Participation Fund Ordinance 1968.

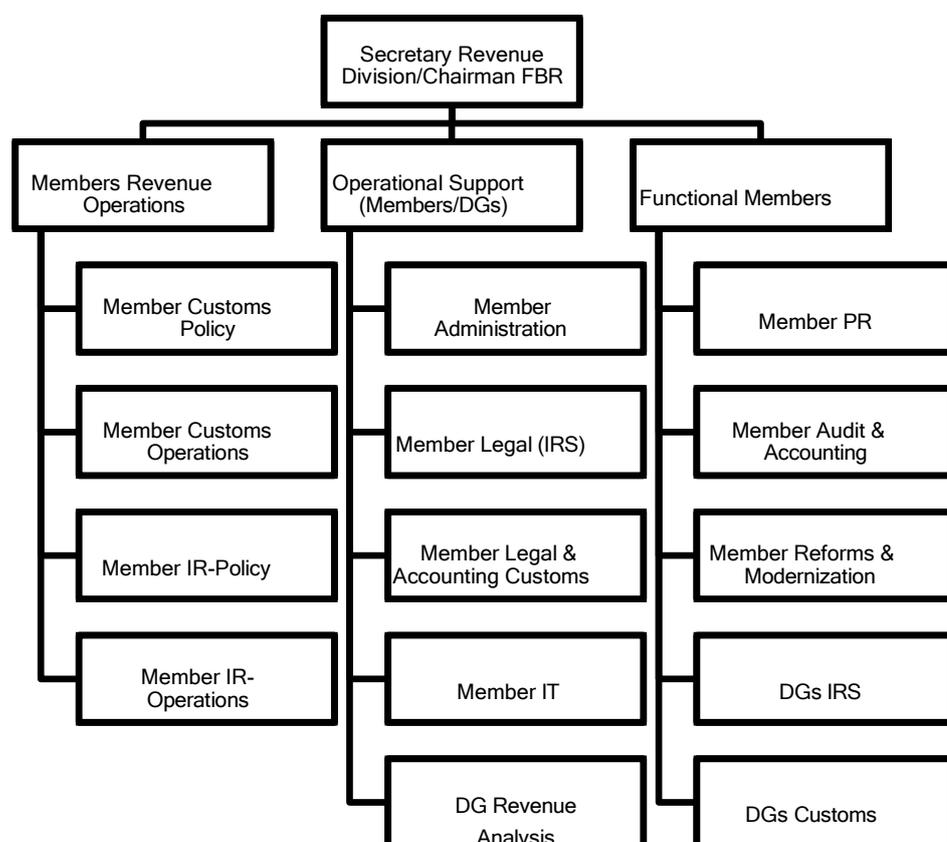
Significant powers and functions of FBR are as follow:

- i. Implementing the provisions of all fiscal laws for the time being in force and taking any action, making policy, issuing rules or guidelines for the purpose;
- ii. Honouring international obligations under a treaty, resolution or any global commitment;
- iii. Promoting a culture of voluntary tax compliance, making the Board a service-oriented organisation, and transforming the Board into a modern and efficient organisation;
- iv. Enabling electronic communication optimally effective in respect of all taxation matters such as e-filing, e-payments, e-notice, e-notification, digital imaging, protocols or agreements as may be prescribed from time to time;
- v. Setting up mechanisms and processes that facilitate the removal of grievances and complaints from the taxpayers;

- vi. Directing or advising investigations and inquiries into suspected duty tax evasion, tax and commercial fraud, money laundering, and financial crimes and coordinating with the relevant law enforcement agencies;
- vii. Taking appropriate measures, including devising internal controls to combat corruption within the organisations and providing checks to ensure the integrity of employees. There should be periodic verification of performance/integrity of the staff through an applicable procedure for promotions and incentives;
- viii. Granting additional allowances or any other incentives and rewards to the employees and members of the Board; and
- ix. Preparing an annual report of its activities and present it to the Prime Minister, the National Assembly and the Senate.

Currently, the Board has 14 members and 20 Directors-Generals (01 Director-General Revenue Analysis 10 for Customs and 9 for Inland Revenue), as detailed in Figure 1 below.

**Figure 1: Organogram of Federal Board of Revenue**



## B. Comments on Budget (Variance Analysis)

The original budget grant of FBR for the FY 2023-24 was Rs 40,557 million, later on, an amount of Rs 10,631 million was re-appropriated. The budget was again re-appropriated out of which an amount of Rs 125 million was unspent till the close of the FY.

The Audit observed that employee-related expenses were increased by Rs 3,721 million (an increase of 18.79% from Rs 19,800 million to Rs 23,521 million), whereas operating expenses were enhanced by Rs 3,845 million (a 36.82% increase from Rs 10,442 million to 14,287 million) out of which an amount of Rs 37 million remained unspent.

This excessive enhancement and unspent balance, depicts weak controls in the planning, allocation, and execution of the budget. Audit recommends that the budget planning should be rationalized to ensure effective utilization of public funds.

## C. Sectoral Analysis of the Federal Board of Revenue (FBR)

FBR has been assigned certain revenue targets through the Finance Act 2023. The purpose of this sectoral analysis is to review FBR's overall collection of taxes during the FY 2023-24 against the targets and to highlight certain areas of concern.

### (i) FBR's Performance for FY 2023-24

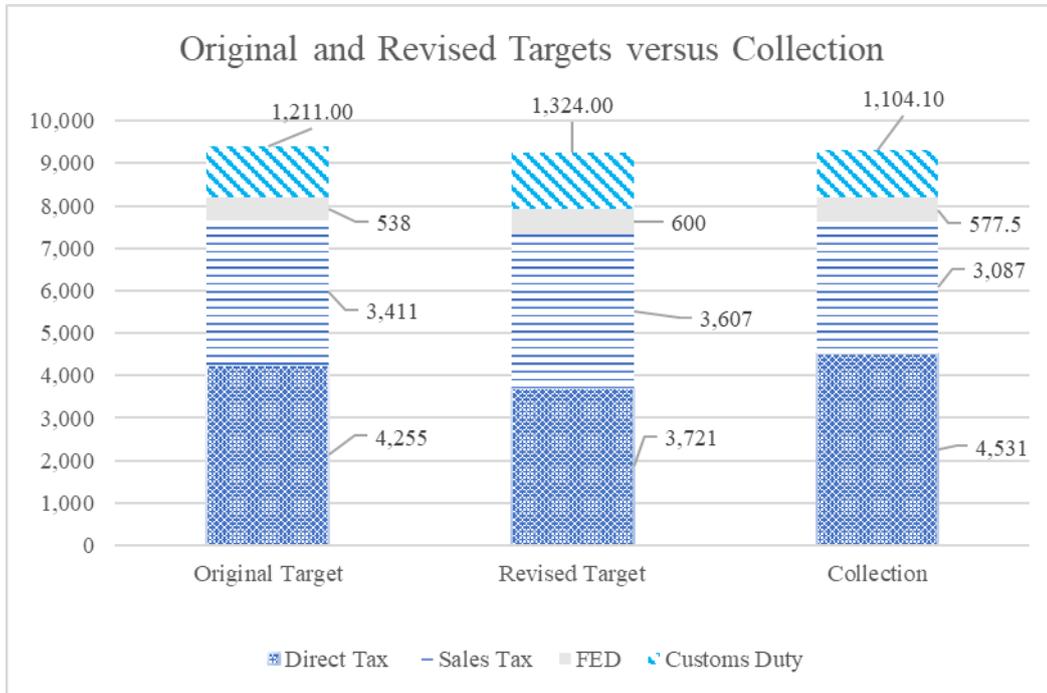
The original target of FBR collection under all heads was Rs 9,415.00 Billion, revised downwards to Rs 9,252.00 Billion for the FY 2023-24. However, FBR succeeded in collecting revenue of Rs 9,299.10 Billion as summarized below:

*(Rs in Billion)*

Head of account	Target		Collection	Achievement (Revised Target)	
	Original	Revised		Absolute	Percentage
<i>Direct Tax</i>	<b>4,255.00</b>	<b>3,721.00</b>	<b>4,530.70</b>	<b>809.70</b>	<b>121.80</b>
<i>Indirect Taxes</i>					
Sales Tax	3,411.00	3,607.00	3,086.80	-520.20	85.60
FED	538.00	600.00	577.5	-22.50	96.30
Customs Duty	1,211.00	1,324.00	1,104.10	-219.90	83.40
<b>Total (IDT)</b>	<b>5,160.00</b>	<b>5,531.00</b>	<b>4,768.40</b>	<b>-762.60</b>	<b>86.21</b>
<b>All Taxes</b>	<b>9,415.00</b>	<b>9,252.00</b>	<b>9,299.10</b>	<b>47.10</b>	<b>100.50</b>

Source: FBR Year Book 2023-24

(Rs in Billion)



The data shows that FBR met its revised revenue targets. The collection of direct taxes amounting to Rs 4,530.70 Billion was more than the original target of Rs 4,255.00 Billion as well as the revised target of Rs 3,721.00 Billion. However, the collection of sales tax, federal excise duty and customs duty could not meet the original or the revised target. Resultantly, FBR marginally missed its revised target of indirect taxes.

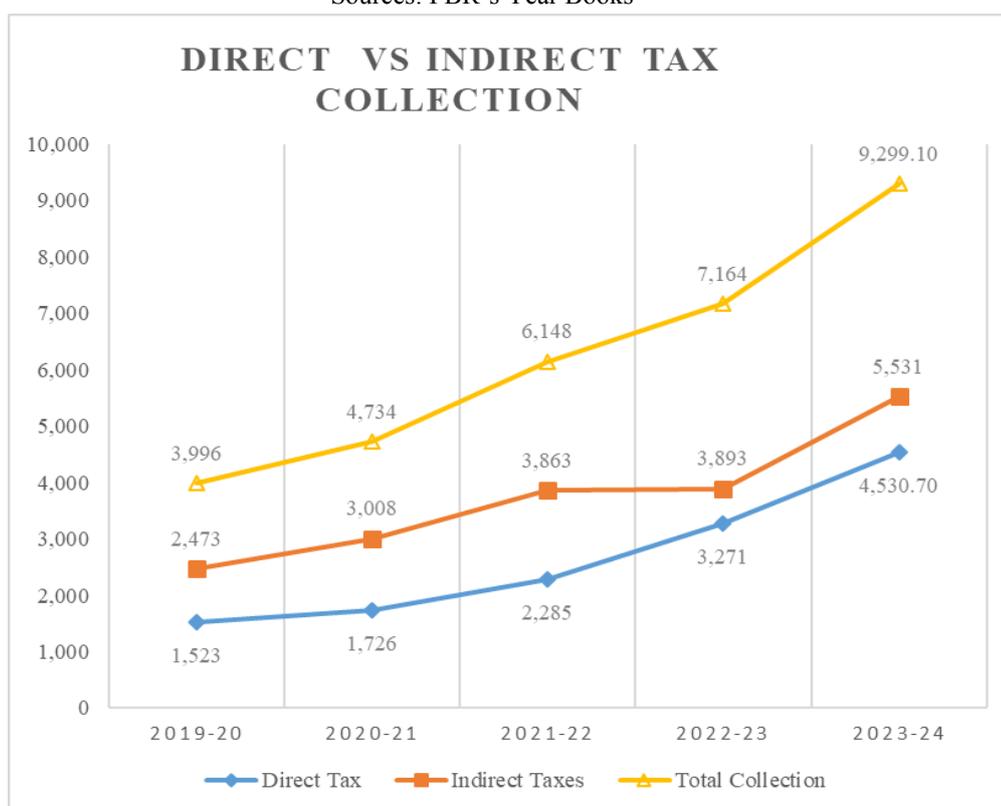
**(ii) Direct and Indirect Taxes**

Historically, indirect taxes have contributed more towards the total collection. However, in the FY 2023-24 direct taxes contributed 48.72% of the total collection as compared to 45.60% in the previous FY. This increase can be attributed to the collection of advance tax, high interest rates on bank deposits, rise in salaries, increased dollar rate and withholding of tax, which constituted 60.47% of the total collection in the FY 2023-24. A comparison for the last five years in respect of direct and indirect tax collection is tabulated as follows:

(Rs in Billion)

	2019-20	2020-21	2021-22	2022-23	2023-24
<b>Direct Tax</b>	1,523	1,726	2,285	3,271	4,530.70
<b>Indirect Taxes</b>	2,473	3,008	3,863	3,893	5,531.00
<b>Total Collection</b>	<b>3,996</b>	<b>4,734</b>	<b>6,148</b>	<b>7,164</b>	<b>9,299.10</b>

Sources: FBR's Year Books



The increase in direct tax collection was 38% which surpassed the increase of 13.55% in total tax collection.

**(iii) Tax on Demand - Performance indicator of FBR (Direct Tax)**

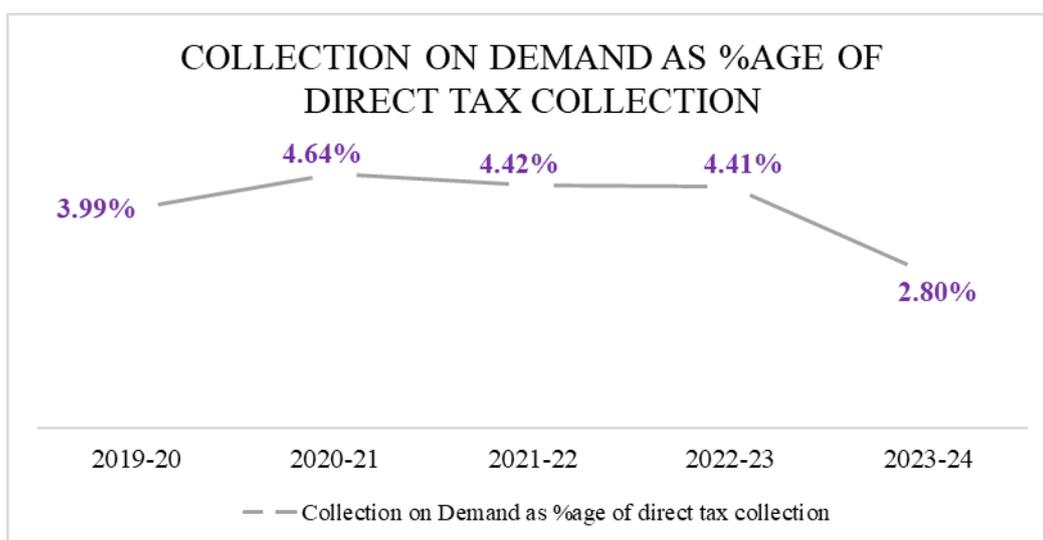
Tax collection in respect of direct taxes consists of advance payment of income tax, which includes tax deducted and collected under Income Tax Ordinance 2001. Under the self-assessment system introduced in tax year 2003, every return filed by a taxpayer is deemed an assessment order. The department is also responsible for preventing tax avoidance and evasion by amending these

deemed assessments and creating tax demand. The indicator of collection on demand depicts the department's actual performance which justifies its budgetary allocation and expenditure. An analysis of collection on demand is as follows:

*(Rs in Billion)*

	2019-20	2020-21	2021-22	2022-23	2023-24
Total Direct Tax	1,523.10	1,726.00	2,284.90	3,271.00	4,530.70
Collection on demand	60.81	80.14	101.09	144.30	126.86
Collection on Demand as %age of direct tax collection	3.99%	4.64%	4.42%	4.41%	2.80%

Sources: FBR's Year Books



The Audit observed that total direct taxes including withholding taxes collected by FBR amounted to Rs 4,530.70 Billion for the FY 2023-24. However, collection on demand was Rs 126.86 Billion for FY 2023-24, which constituted only 2.80% of the direct tax collection. Furthermore, the contribution of collection through tax demand in total direct tax collection had declined in FY 2023-24 as compared to the previous years.

**(iv) Withholding Taxes (Income Tax)**

Tax collection under the withholding tax regime relies on the person making the payment by treating him as a withholding agent. Tax collection under this head is easier due to at-source deduction, therefore, withholding taxes form a major part of the total tax collection.

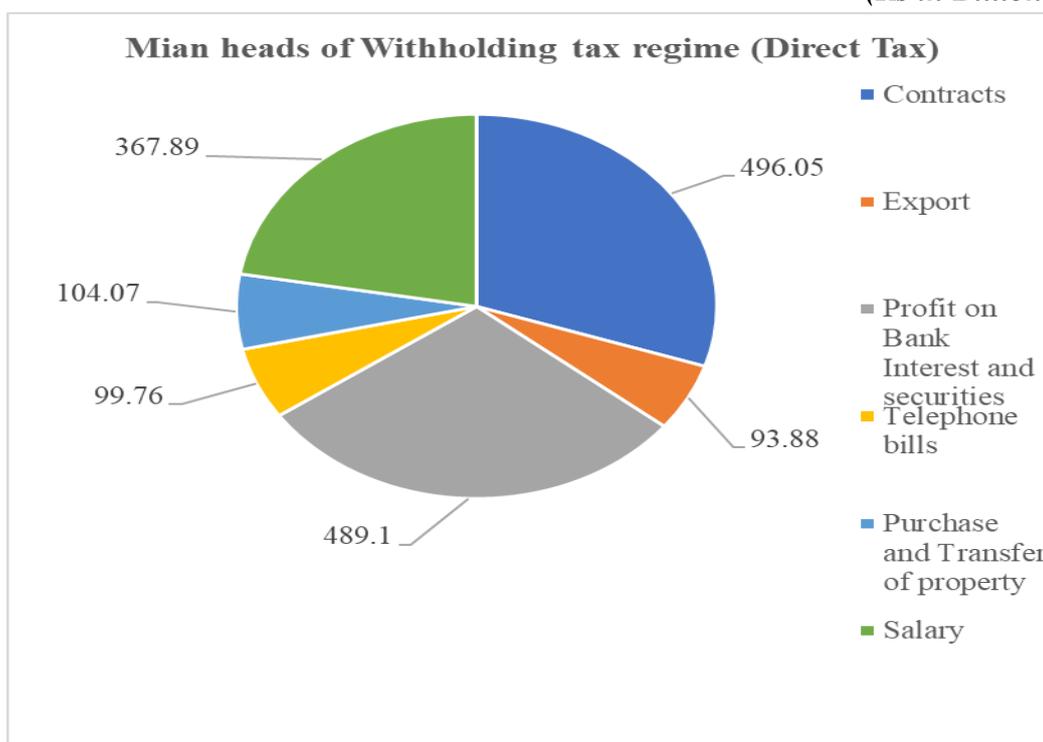
Tax collection on account of withholding taxes was Rs 2,740.10 Billion against the total direct tax collection of Rs 4,530.70 Billion for the FY 2023-24. In terms of proportion withholding taxes constituted 60.47% of the total direct taxes.

Among the ten major components of withholding tax, withholding taxes on contractual receipts, exports, bank interest and various other items fall under minimum tax or final tax regime. The Audit observed that collections under these heads were indirect in nature, but the same were being collected/reported as direct taxes by FBR. Moreover, the collections under the heads of telephone bills and purchases of properties were adjustable, however, these adjustments were not claimed by non-filers. FBR collected Rs 1,650.75 Billion withholding tax in these heads for the FY 2023-24, which was Rs 429.69 Billion more than the preceding FY. The increase in withholding tax was mainly attributable to increase in salary rates. The detail is tabulated under:

*(Rs in Billion)*

<b>Heads</b>	<b>FY 2023-24</b>	<b>FY 2022-23</b>	<b>Increase</b>
Contracts	496.05	390.83	105.22
Export	93.88	73.82	20.06
Profit on Bank Interest and securities	489.10	320.02	169.08
Telephone bills	99.76	87.28	12.48
Purchase and Transfer of property	104.07	84.77	19.30
Salary	367.89	264.34	103.55
<b>Total</b>	<b>1,650.75</b>	<b>1,221.06</b>	<b>429.69</b>

(Rs in Billion)



## 2.2 Classified Summary of Audit Observations

Audit observations amounting to Rs 925,841.59 million have been raised in this report as a result of the current audit of the Federal Board of Revenue. Summary of the audit observations classified by their nature is as under:

### Overview of Audit Observations

(Rs in million)

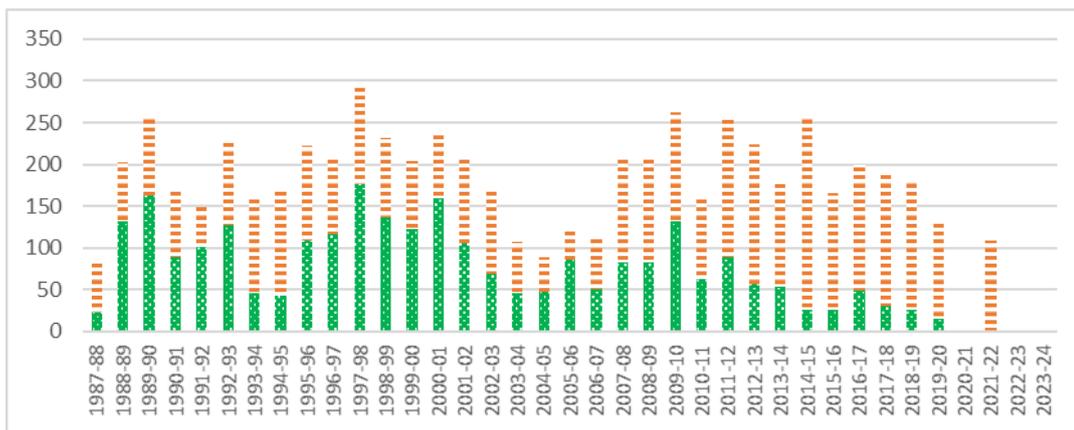
S. No.	Classification	Amount
1	Non-production of record	-
2	Receipts/expenditure-related Irregularities	-
	i. Direct Taxes (Income Tax)	638,529.22
	ii. Indirect Taxes (Sales Tax and FED)	213,182.29
	iii. Customs Duty	37,405.46
	iv. Expenditure	1,180.61
3	Impact Audit	10,235.74
4	Sectoral Audit	23,791.02
5	Thematic Audits	1,517.25
6	Other significant issues	0
<b>Total</b>		<b>925,841.59</b>

### 2.3 Comments on the status of compliance with the PAC directives

The Public Accounts Committee is the primary accountability structure in the governance framework of Pakistan. Audit reports are laid before the esteemed forum for discussion every year for directions. A summary of the total paras discussed in PAC and their compliance is presented in the table and graph below:

<b>Year</b>	<b>Total Paras</b>	<b>Compliance received</b>	<b>No Compliance</b>	<b>%age Compliance</b>
1987-88	83	22	61	27%
1988-89	203	132	71	65%
1989-90	259	163	96	63%
1990-91	171	89	82	52%
1991-92	148	101	47	68%
1992-93	229	127	102	55%
1993-94	160	45	115	28%
1994-95	168	43	125	26%
1995-96	222	108	114	49%
1996-97	207	117	90	57%
1997-98	292	177	115	61%
1998-99	232	137	95	59%
1999-00	204	123	81	60%
2000-01	239	159	80	67%
2001-02	206	106	100	51%
2002-03	169	69	100	41%
2003-04	107	46	61	43%
2004-05	88	47	41	53%
2005-06	121	85	36	70%
2006-07	114	51	63	45%
2007-08	210	83	127	40%
2008-09	210	82	128	39%
2009-10	263	132	131	50%
2010-11	163	62	101	38%
2011-12	253	88	165	35%
2012-13	224	57	167	25%
2013-14	176	54	122	31%
2014-15	259	25	234	10%

2015-16	166	26	140	16%
2016-17	199	48	151	24%
2017-18	187	31	156	17%
2018-19	183	26	157	14%
2019-20	131	15	116	11%
2020-21	42	Not discussed in PAC yet		
2021-22	108	0	108	0%
2022-23	93	Not discussed in PAC yet		
2023-24	120	Not discussed in PAC yet		



The aggregate mean from the table above shows that only 43% compliance with the PAC directives was made by FBR. Compliance with PAC directives as a percentage of total directives was 30% for direct taxes, 53% for indirect taxes and 44% for customs duties. Moreover, compliance with PAC directives was only 4.7% in the last five years (2015-16 to 2019-20). This reflects a lack of seriousness on the part of the FBR towards PAC directives. Resultantly, audit observations involving substantial revenue have been piling up year after year. This is alarming as chances of recovery of revenue diminish over time.

Compliance with PAC directives is a key performance indicator of FBR, but reporting on this Key Performance Indicator (KPI-10) is limited to timely communication of PAC directives by the Board to field formations and lacks active follow-up. The Audit recommends implementation of this KPI in letter and spirit through active follow-up of PAC directives and linking it with performance-based incentives.

### **CHAPTER-3 NON-PRODUCTION OF AUDITABLE RECORD**

According to Articles 169 and 170 of the Constitution of the Islamic Republic of Pakistan, 1973 “The Audit of the accounts of Federal and the Provincial Governments and the accounts of any authority or body established by or under the control of Federal or a Provincial Government is required to be conducted by the Auditor-General, who would determine the extent and nature of such audit”.

Section 12 of the Auditor-General’s Ordinance, 2001 empowers the Auditor-General of Pakistan to conduct audit of Receipts. Under Section 14 of the Ordinance, he has the authority to inspect any office of accounts including treasuries. Further, the officer in-charge of any office or the Department is obligated to afford all facilities and provide record for audit inspection. Any person or authority hindering the auditorial function of the Auditor-General regarding inspection of accounts is subject to disciplinary action under relevant Efficiency and Discipline Rules.

Performance audit of Dispute Resolution Mechanism in FBR was approved as a part of Annual Audit Plan 2022-23 of this office. For this purpose, field audit teams were directed to gather data from FBR Headquarter (HQ) and its field formations. Due to significance of matter and non-provision of data/record during the Audit Year 2022-23, the same subject was again included in Audit Plan 2023-24. In this connection, this office and field audit teams during currency of field audit made continuous efforts to collect data on the subject matter. Meetings with Member Legal (IR) and Chief Legal FBR were also convened but centralized data / record was not provided by FBR authorities. Some partial data was received from field formations in piece meal, which was not sufficient for meaningful analysis and reporting on the subject matter. This office made consistent correspondence with FBR (HQ) and several meetings were also convened with FBR authorities including Member Legal. After non-provision of data by FBR authorities, this office brought the issue in the notice of Deputy Auditor General (RRA/SSA), who took up the matter with Chairman FBR in writing. Non-provision of record/data to auditors is a matter of serious concern which tantamount to hindrance in auditorial functions of the Auditor-General of Pakistan.

The matter was reported to the Chairman FBR in June & August 2024, with a copy to the Members Legal IRS and Customs, Members Accounting IRS

and Customs. However, despite correspondence, concerned legal wings did not produce comprehensive data required in soft form which was imperative for carrying out a meaningful study.

During the DAC meeting with Customs Wing held in December 2024, the department replied that partial record of formations stationed at Lahore was available and record of remaining formations will be produced to Audit on priority basis. The DAC directed the department to produce the requisite record without further delay within 30 days. No further progress was reported by the department till finalization of this report.

During the DAC meeting with IR Wing held in January 2025, the department informed that partial data has been prepared and shared with the Board and the same will be forwarded to Audit. The department further informed that the requisite data in respect of four field formations is still awaited. DAC directed the Legal Wing to produce the complete record to Audit in soft as well as hard form within 15 days besides justifying the non-provision of data with cogent reasons. No further progress was reported by the department till finalization of this report.

The Audit recommends that production of auditable record must invariably be ensured and disciplinary proceedings may be initiated against the responsible officers/officials.

[DP No. 8957-NPR, Annexure-2]

## CHAPTER-4 INCOME TAX

### 4.1 Non/short-realization of minimum tax – Rs 22,874.66 million

Section 113 of the Income Tax Ordinance, 2001 provides for the realization of minimum tax based on the turnover of a taxpayer. The tax is to be paid if, otherwise, no tax is payable on taxable income due to any reason, or tax payable under the normal tax regime is less than the minimum tax liability in respect of specified categories of taxpayers.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in twenty-two (22) field offices of FBR, one thousand six hundred and fifty-three (1,652) taxpayers evaded the minimum tax because either no tax was payable under the normal tax regime or their normal tax liability was less than their minimum tax liability. However, the department did not initiate legal proceedings to recover the tax which resulted in non/short-realization of tax amounting to Rs 23,202.79 million.

These irregularities were pointed out to the department from February to November 2024. The management replied that Rs 328.13 million had been charged and recovered and Rs 1,085.62 million had been charged but recovery was awaited, proceedings for Rs 19,966.32 million were initiated under the law but not finalized and an amount of Rs 1,822.72 million was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the charged amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue subjudice cases at appropriate fora and finalize legal proceedings besides strengthening of desk audit.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide paras number 4.4.7, 4.1(vii), 4.6, 5.7 and 4.6 having financial impact of Rs 47,906.00 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-3]

#### **4.2 Short-realization of super tax – Rs 167,887.87 million**

Section 4C of the Income Tax Ordinance, 2001 provides that super tax shall be imposed for tax year 2022 and onwards at the prescribed rates specified on the income of high earning persons except banking company. Super tax is applicable on the persons whose income is above Rs 150 million.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in twenty (20) field offices of FBR, one thousand and twenty six (1,026) taxpayers did not pay super tax which resulted in short realization of super tax. The department did not initiate any legal proceedings to levy the super tax due to weak monitoring. This resulted in short realization of super tax amounting to Rs 167,935.88 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 48.01 million had been charged and recovered and Rs 1,942.77 million had been charged but recovery was awaited, proceedings for Rs 159,610.41 million were initiated under the law but not finalized and an amount of Rs 6,334.69 million was subjudice.

The DAC, in its meetings held in July, October, November, December 2024 and January, 2025 directed the department to recover the admitted amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue subjudice cases at appropriate fora and submit comprehensive replies besides strengthening desk audit for enforcement of super tax.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.3, 4.1(v), 4.4, 5.9 and 4.26 having financial impact of Rs 42,528.00 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-4]

#### **4.3 Short-realization of income tax due to inadmissible expenses – Rs 149,571.28 million**

Section 21 of the Income Tax Ordinance, 2001 provides that certain expenses such as lease financial charges, provisional expenses and expenses

which were not subjected to withholding tax shall not be allowed in computing taxable income under the head “Income from Business”.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in eighteen (18) field offices of FBR, one thousand and eighty-four (1,084) taxpayers claimed inadmissible expenses such as lease finance charges, provisional expenses and expenses where withholding tax was not deducted while computing their taxable income. The department did not take corrective action to disallow such expenses which resulted in short realization of tax amounting to Rs 149,866.75 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 295.47 million had been charged and recovered, and proceedings for Rs 149,571.28 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024, January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends finalizing legal proceedings and submit comprehensive replies besides strengthening internal controls through risk based desk audit.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.13, 4.11, 5.2 and 4.2 having a financial impact of Rs 208,375 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-5]

#### **4.4 Non/short realization of withholding tax – Rs 45,386.45 million**

Section 153, read with Section 161 of the Income Tax Ordinance, 2001 provides that where a withholding agent fails to deduct tax or does not deposit the deducted tax, he is personally liable to pay the amount of tax through legal proceedings initiated by the Commissioner.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in nineteen (19) field offices of FBR, one thousand, three hundred and forty-four (1,344) withholding agents did not deduct tax while making payments to suppliers, service providers and contractors. It was a statutory obligation of the

department to recover the tax from the withholding agents. However, no action was initiated by the department which resulted in non-recovery of tax amounting to Rs 45,388.86 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 2.41 million had been charged and recovered, proceedings for Rs 45,386.45 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends finalizing legal proceedings besides ensuring compliance of withholding regime through Commissioner, IR (Withholding). Moreover, Synchronized Withholding Administration and Payment System (SWAPS) be implemented on priority basis and periodically updated in the light of audit observations.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.7.2, 4.2, 4.20, 5.5 and 4.5 having financial impact of Rs 97,629 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-6]

#### **4.5 Non-recovery of tax demands – Rs 62,318.02 million**

Section 138 of the Income Tax Ordinance, 2001 provides the procedure for the recovery of the due tax from taxpayers through attachment and sale of any movable or immovable property, arrest and detention of the taxpayer.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in sixteen (16) field offices of FBR, one thousand five hundred and seventy-one (1,571) cases, tax was charged against the taxpayers, but recoveries thereof were not made despite a lapse of considerable time. This resulted in non-recovery of tax amounting to Rs 62,320.92 million due to negligence of the tax authorities.

These irregularities were pointed out from February to November 2024. The management replied that Rs 2.90 million had been charged and recovered, Rs 2,011.39 million had been charged but recovery was awaited, proceedings for

Rs 59,819.13 million were initiated under the law but not finalized and an amount of Rs 487.50 million was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the admitted amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery, finalizing legal proceedings and pursuing subjudice cases besides strengthening monitoring controls by a dedicated supervisory team independent from the assessment function.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.6, 4.17, 5.1 and 4.1 respectively having a financial impact of Rs 206,288.38 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-7]

#### **4.6 Inadmissible adjustment/claim of refund – Rs 6,795.41 million**

Section 170 of the Income Tax Ordinance, 2001 read with Circular No. 05 of 2003 of FBR, provides that a taxpayer who has paid tax in excess of tax liability is eligible for a refund subject to fulfilment of the prescribed conditions.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in nineteen (19) field offices of FBR, eight hundred and seventeen (817) taxpayers claimed excess refunds against tax liability for the tax years. The tax refund adjustments included credits of tax payments without verification of tax payment challans, adjustments of prior year's refunds in the absence of refund orders, or non-accountal of outstanding liabilities. The department did not take corrective action to recover the government dues. This resulted in inadmissible issuance and adjustments of refunds amounting to Rs 6,795.41 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 4.02 million had been charged but recovery was awaited, proceedings for Rs 6,791.39 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to expedite recovery of admitted

amounts, finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts and finalize legal proceedings besides strengthening post refund audits.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.5.1, 4.4.1, 4.29, 5.11 and 4.10 having a financial impact of Rs 17,091 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-8]

#### **4.7 Short-realization of tax due to non-apportionment of expenses - Rs 2,253.86 million**

Section 67 of the Income Tax Ordinance, 2001 read with Circular No. 12 of 1991 provides for apportionment of expenses between income chargeable to tax under normal and final tax regimes in proportion to sales in the respective regime.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in six (06) field offices of FBR, fifteen (15) taxpayers earned income under normal and final tax regimes. However, the apportionment of expenses in proportion to sales was done incorrectly and higher expenses were allowed under the normal income tax regime which resulted in less assessments of taxable income. The department did not amend assessment orders which resulted in short-realization of tax amounting to Rs 2,253.86 million.

These irregularities were pointed out from February to November, 2024. The management replied that proceedings for Rs 2,253.86 million were initiated but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting legal proceedings and strengthening validation checks in return filing system for apportionment of expenses between final and normal tax regimes. Moreover, risk-based desk audit needs to be strengthened besides periodic review and updating of the RMS.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers

4.4.16, 4.1(xi), 4.10, 5.20 and 4.16 having financial impact of Rs 2,150 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-9]

#### **4.8 Non-recovery of income tax on sales to retailers, wholesalers and distributors – Rs 6,520.64 million**

Sections 236 G & H of the Income Tax Ordinance, 2001 provides for the collection of advance tax by manufacturers, commercial importers, distributors, dealers and wholesalers at prescribed rates while making sales to specified persons. Further, Section 161 of the law *ibid* provides that in case of non-compliance the person responsible for collection will pay the tax.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in sixteen (16) field offices of FBR, one thousand seven hundred and seventy-nine (1,779) taxpayers did not collect advance tax from retailers, wholesalers and distributors at the time of sale. The department did not initiate legal proceedings which resulted in the non-recovery of tax amounting to Rs 6,521.16 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 0.52 million had been charged and recovered, Rs 3.42 million had been charged but recovery was awaited, proceedings for Rs 6,510.62 million were initiated under the law but not finalized and an amount of Rs 6.60 million was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to expedite the recovery of admitted amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue the subjudice cases at appropriate fora and finalize legal proceedings. Enforcement of tax on retailers, distributors and wholesalers should be ensured through risk based desk audit.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.11, 4.23, 5.14 and 4.12 having a financial impact of Rs 14,353.73 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-10]

#### **4.9 Non-realization of default surcharge on late payment of tax – Rs 9,658.42 million**

According to Section 205 of the Income Tax Ordinance 2001, where a person fails to pay any tax on or before the due date of payment, the person shall be liable to pay default surcharge at the prescribed rate on the unpaid amount of tax.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in eighteen (18) field offices of FBR, five thousand, nine hundred and seventy seven (5,977) taxpayers did not pay due tax within the prescribed time under the law. However, tax authorities did not levy and recover default surcharge from the taxpayers. This resulted in non-realization of default surcharge amounting to Rs 9,685.30 million.

These irregularities were pointed out from February to November 2024. The management replied that Rs 26.88 million had been charged and recovered, Rs 6.44 million had been charged but recovery was awaited, proceedings for Rs 9,648.86 million were initiated under the law but not finalized and an amount of Rs 3.12 million was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the admitted amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue the subjudice cases and finalize legal proceedings besides fixing of responsibility against the concerned for not enforcing default surcharge. Moreover, consistent enforcement of default surcharge needs to be ensured to prevent misuse of self-assessment regime.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.10, 4.15, 5.12 and 4.11 having a financial impact of Rs 17,181.99 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-11]

#### **4.10 Non-realization of income tax due to concealment of income – Rs 54,194.09 million**

Section 111 of the Income Tax Ordinance, 2001 provides a detailed procedure for taxation of concealed income. According to the provision where a

person is the owner of any money or valuable article or has made any investment or credited any amount in his books of accounts, the amount is chargeable to tax if not adequately explained by the taxpayer.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in twenty one (21) field offices of FBR, one thousand, one hundred and eighty one (1,181) taxpayers had either shown excess sales or purchases of different items in sales tax returns compared to that shown in income tax returns/financial statements and did not explain accretion in assets pertaining to the tax years 2022 & 2023. This implies that the taxpayers concealed their sales, purchases or assets to evade the due tax. The irregularity resulted in non-realization of income tax of Rs 54,194.33 million.

These irregularities were pointed out from February to November, 2024. The management replied that Rs 0.24 million had been charged and recovered, Rs 24.87 million had been charged but recovery was awaited, proceedings for Rs 54,169.22 million were initiated under the law but not yet finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the charged amount, finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts and finalize legal proceedings besides strengthening the integration of Federal and Provincial databases of land records, provincial revenue authorities, excise and taxation etc. Furthermore, cases of mis-statements uncovered due to discrepancies found in Federal and Provincial interfaces may be reported separately in the annual performance report.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22 and 2023-24 vide para numbers 4.4.1, 4.1(iii), 4.18 and 4.18 having a financial impact of Rs 88,916.40 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-12]

#### **4.11 Irregular claim of tax credit – Rs 2,481.67 million**

According to Section 100C of the Income Tax Ordinance, 2001 income of non-profit organizations, trusts or welfare institutions are allowed a tax credit equal to one hundred per cent of the tax payable on fulfilling certain conditions,

which include that the administrative and management expenditure should not exceed fifteen percent of the total receipts.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in six (06) field offices of FBR, thirty eight (38) taxpayers were not entitled for the tax credits because the taxpayers claimed administrative and management expenditure in excess of the prescribed limit of fifteen percent (15%) of revenue. Therefore, their income was required to be assessed under the law without allowing the tax credit. This resulted in non-levy of tax amounting to Rs 2,561.67 million.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 80.00 million had been recovered and verified, Rs 367.98 million had been charged but recovery was awaited, proceedings for Rs 2,053.85 million were initiated under the law but not finalized and an amount of Rs 59.84 million was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the admitted amounts, finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the recovery, pursuing subjudice cases, finalizing legal proceedings and strengthening of risk-based monitoring of tax credits besides periodically reviewing and updating Risk Management System (RMS) in the light of repeated audit observations.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.9, 4.1, 4.2, 5.4 and 4.22 having a financial impact of Rs 7,493 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-13]

#### **4.12 Non-recovery of tax on brokerage and commission – Rs 2,521.44 million**

Section 233 read with Section 161 of the Income Tax Ordinance, 2001 provides for tax to be deducted at prescribed rates while making payment to brokerage or commission. Section 161 provides that in case of non-compliance, the person responsible for the tax deduction will pay the tax.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in eleven (11) field offices of FBR, one hundred twenty-five (125) withholding agents did not deduct the due amount of tax while making payments of brokerage and commission. However, the department did not take corrective action to recover the due amount of tax. This resulted in non-recovery of tax amounting to Rs 2,521.44 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 2,521.44 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to finalize the legal proceedings besides strengthening monitoring controls over withholding agents through risk based desk audit and effective utilization of IT based systems.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.7.9, 4.25, 5.21 and 4.17 having a financial impact of Rs 569.27 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-14]

#### **4.13 Non-deduction of tax on income from property – Rs 1,016.31 million**

Section 155, read with Section 161 of the Income Tax Ordinance, 2001 provides that every prescribed person, while making a payment to any person in respect of rent of immovable property is required to deduct tax at the specified rates. In case of non-deduction, the Commissioner enforces the payment of tax by invoking provisions of Section 161 *ibid*.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in seventeen (17) field offices of FBR, four hundred and seventy-two (472) withholding agents did not deduct the tax while making payments of rent to property owners. This resulted in non-recovery of withholding tax amounting to Rs 1,017.33 million.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 1.02 million had been recovered

and verified, Rs 0.06 million had been charged but recovery was awaited, proceedings for Rs 1,016.25 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the charged amount, finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to recover the admitted amounts, finalize the legal proceedings besides monitoring of withholding agents for accurate deduction and timely deposit of tax in government's exchequer. Compliance of withholding regime needs to be ensured through Commissioner, IR (Withholding).

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.7.10, 4.24, 5.15 and 4.13 having a financial impact of Rs 2,556.93 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-15]

#### **4.14 Short-realization of income tax due to inadmissible claims of initial allowance/ tax depreciation – Rs 9,244.16 million**

Sections 22 and 23 of the Income Tax Ordinance, 2001 provide that a taxpayer is allowed normal and initial depreciation allowance at specified rate in a tax year on the written down value or purchase value of plant and machinery used for the first time in the business.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in six (06) field offices of FBR, ninety-six (96) taxpayers claimed normal and initial depreciation allowance on assets other than plant and machinery which was not admissible as per law. The department did not take corrective action of disallowing the depreciation allowance and failed to recover the due tax from the taxpayers. This resulted in short-realization of income tax amounting to Rs 9,277.80 million.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 33.64 million had been recovered and verified, proceedings for Rs 9,244.16 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to finalize the legal proceedings besides strengthening risk-based desk audit.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2022-23 and 2023-24 vide para numbers 4.4.17, 4.1(x), 5.18 and 4.15 having a financial impact of Rs 3,175.87 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-16]

#### **4.15 Short-realization of tax due to excess claim of tax credit on donations – Rs 251.23 million**

According to Section 61 of the Income Tax Ordinance 2001, a person shall be entitled to a tax credit in respect of any sum paid, or any property given by the person in the tax year as a donation, voluntary contribution or subscription. Further, as per Section 61(2) of the Ordinance *ibid*, the donation is restricted upto 30% of taxable income in respect of individuals or association of persons and 20% for corporate sector.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in four (04) field office of FBR, seventy-one (71) taxpayers while filing their income tax returns claimed tax credits on donations in excess of the prescribed limit. The assessing officers were required to disallow the excess claims of donations and charge the due tax, but the department did not charge the due amount of tax. This resulted in short realization of tax amounting to Rs 251.23 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 251.23 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening internal controls in return filing system for ensuring allowance of tax credit on donations within prescribed limit.

**Note:** The issue was also reported earlier in the Audit Report for the Audit Year 2023-24 vide para number 4.24 having a financial impact of Rs 479.00 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-17]

#### **4.16 Non-taxation of income earned from head of other sources – Rs 23,281.20 million**

According to Section 39 of the Income Tax Ordinance 2001, income of any kind earned by a person in a tax year shall be chargeable to tax in that year under the head “Income from Other Sources”, if the income is not included in any other head of income under the law.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in seventeen (17) field offices of FBR, one thousand seven hundred and sixty-four (1,764) taxpayers derived taxable income under the head “Income from Other Sources” but did not pay tax on that income. The assessing authorities did not initiate legal action to recover the tax. This resulted in non-realization of tax amounting to Rs 23,281.20 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 23,281.20 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening the desk audit function. Moreover, the performance of the assessing officers should be gauged in term of new tax demand created and recoveries thereof.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.15, 4.14, 5.10 and 4.9 having a financial impact of Rs 30,658.87 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-18]

#### **4.17 Non-levy of Alternative Corporate Tax – Rs 805.79 million**

Section 113C of the Income Tax Ordinance, 2001 provides that Alternative Corporate Tax at a rate of seventeen per cent of accounting income will be paid by a company if the tax payable under normal tax or minimum tax is less than the Alternative Corporate Tax.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in four (04) field offices of FBR, seven (07) companies did not pay Alternative Corporate Tax despite the fact that the tax was higher than the normal tax and minimum tax. This resulted in non levy of alternative corporate tax amounting Rs 805.79 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 805.79 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides fixing of responsibility against the concerned.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Year 2019-20, vide para numbers 4.4.8 having a financial impact of Rs 4,984.06 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-19]

#### **4.18 Non-levy of penalty for late/non filing of returns – Rs 26,585.63 million**

According to Section 114 of the Income Tax Ordinance 2001, every person who has obtained National Tax Number is required to furnish a return of income for a tax year and the person whose taxable income for the year exceeds the maximum amount that is not chargeable to tax under this Ordinance for the year. Further, Section 182 ibid provides for levy of penalty at applicable rates, where a taxpayer, fails to furnish or late furnish the return of total income.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in twelve (12) field offices of FBR, fourteen thousand six hundred and ninety-

seven (14,697) taxpayers did not file Income Tax returns despite the fact that the taxpayers had been allotted National Tax Numbers meaning thereby they have to compulsorily file Income Tax return. No remedial action was initiated by the department to enforce the filing of the returns besides imposition of penalty calculated at Rs 26,585.63 million alongwith tax chargeable on the basis of the returns. Audit further observed that there was no effective internal control system in place in the department which could enforce the filing of the returns and imposition of the penalty.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 0.05 million had been recovered and verified, an amount of Rs 10.08 million charged but not recovered and proceedings for Rs 26,585.68 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the charged amount, finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to recover the admitted amounts, expedite the legal proceedings and improve internal controls for effective monitoring of non-filers.

**Note:** The issue was also reported earlier in the Audit Report for the Audit Year 2021-22 vide para number 4.16 having a financial impact of Rs 5,943.03 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-20]

#### **4.19 Inadmissible claims of tax credit on investment – Rs 1,606.32 million**

Section 65 of the Income Tax Ordinance, 2001 provides for tax credits to corporate industrial undertakings at prescribed rates for investment in existing plant and machinery through equity.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in six (06) field offices of FBR, fourteen (14) taxpayers claimed tax credits despite the fact that the taxpayers were not industrial undertakings. These inadmissible tax credits were required to be disallowed to recover the due tax from the taxpayers. However, the department did not initiate the proceedings which resulted in claim of inadmissible tax credit amounting to Rs 1,606.32 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 1,606.32 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings and implementing monitoring controls besides strengthening desk audits. Periodic review of Risk Management System (RMS) should be undertaken in the light of repeated audit observations.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Year 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.9, 4.1(ii), 4.2, 5.4 and 4.4 having financial impact of Rs 39,715 million. Recurrence of same irregularity is a matter of serious concern.

[Annexure-21]

#### **4.20 Excess adjustments of withholding tax deductions – Rs 13,627.01 million**

Section 168 of the Income Tax Ordinance, 2001 provides that where an amount of tax has been collected or deducted from a payment made to a person by a withholding agent, the person shall be allowed the effect of tax deduction in computing his tax liability under normal tax regime.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in ten (10) field offices of FBR, one hundred and forty-one (141) taxpayers, claimed tax deductions or tax collection in excess of admissible amount of tax collected or deducted. However, the department neither verified these tax deductions nor recovered due tax from the taxpayers. This resulted in short-realization of tax amounting to Rs 13,700.34 million due to excess adjustments of withheld tax.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 73.33 million had been recovered and verified, an amount of Rs 19.28 million charged but not recovered and proceedings for Rs 13,607.73 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the admitted amounts, finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to recover the admitted amounts, finalize legal proceedings besides strengthening the monitoring of withholding tax regime along-with introduction of validation checks in IT system for verification of such tax credit.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.5, 4.1(iv), 4.3, 5.8 and 4.7 having financial impact of Rs 4,463.85 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-22]

#### **4.21 Non-realization of Workers Welfare Fund – Rs 10,677.91 million**

Under Section 4 of the Workers Welfare Fund Ordinance, 1971 every industrial establishment, whose total annual income exceeded a statutory threshold, is required to pay Workers Welfare Fund @ 2 percent of its total income.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in thirteen (13) field offices of FBR, five hundred and nine (509) taxpayers for the Tax Years 2021 to 2023 did not pay WWF. The department did not initiate legal proceedings for the recovery of the same. This resulted in non-realization of WWF amounting to Rs 10,677.91 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 10,677.91 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

Audit recommends expediting the finalization of legal proceedings and implementation of preventive controls to monitor self-assessment system.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, and 2022-23 vide para numbers 4.6.1, 4.3, 4.31 and 5.13 having a financial impact of Rs 7,041.96 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-23]

#### **4.22 Non-realization of tax on salary income – Rs 3,116.20 million**

According to Section 149 read with Section 161 of the Income Tax Ordinance, 2001 every employer paying salary to an employee is required to deduct tax from the amount of salary at the time of payment. The deduction is to be made at the average rate of tax computed at the rates specified in Division-I Part-I to the First Schedule.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in twelve (12) field offices of FBR, four hundred and ninety five (495) withholding agents had not correctly deducted tax at the time of making payments on account of salaries. The department did not monitor and prevent non-deduction of tax on salaries which resulted in the non-realization of tax amounting to Rs 3,116.20 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 3,116.20 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening monitoring controls over withholding agents for accurate deduction and timely deposit of tax in government's exchequer.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23, and 2023-24 vide para numbers 4.7.8, 4.21, 5.17 and 4.25 having a financial impact of Rs 1,698.54 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-24]

#### **4.23 Non-deduction of tax on dividend – Rs 2,154.60 million**

Section 150, read with Section 161 of the Income Tax Ordinance, 2001 provides that every person paying a dividend shall deduct tax from the gross amount of the dividend at specified rates. In case of non-compliance, the person responsible for the tax deduction is required to pay the tax.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in five (05) field offices of FBR, twenty-eight (28) taxpayers did not deduct tax while making payments of dividend. However, the department did not recover the tax under the law. This resulted in non-recovery of tax amounting to Rs 2,154.60 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 2,154.60 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings and enforcement of monitoring controls over withholding agents. Compliance of withholding regime needs to be ensured through Commissioner, IR (Withholding).

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.7.4, 4.22, 5.16 and 4.14 having a financial impact of Rs 8,983.75 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-25]

#### **4.24 Irregular amendment of assessment orders – Rs 2,552.50 million**

According to Section 122(5A) read with Section 177 of the Income Tax Ordinance, 2001, the Commissioner may amend an assessment order treated as issued under Section 120 or issued under Section 121, on the basis of definite information by making such alterations or additions as the Commissioner considers necessary. No order shall be amended by the Commissioner after the expiry of five years from the end of the financial year in which the

Commissioner has issued or treated to have issued the assessment order to the taxpayer.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in thirty four (34) cases of four (04) field offices of FBR, the tax authorities had made amendments in assessment orders under Section 122, but the tax authorities while passing assessment orders either allowed inadmissible expenses or applied incorrect rate of tax. It was also noticed that imputable income was also not calculated to arrive at income to charge super tax as per law. The said omissions rendered the assessment orders erroneous and prejudicial to the interest of revenue. This resulted in loss of revenue amounting to Rs 2,553.56 million.

These irregularities were pointed out from February to November 2024. The management replied that an amount of Rs 1.06 million had been charged and recovered, an amount of Rs 25.43 million had been charged but not recovered, proceedings for Rs 2,232.53 million were initiated but yet not finalized and Rs 294.54 was subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the charged amount finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue the subjudice cases and finalize the legal proceedings besides fixing of responsibility against the concerned.

**Note:** The issue was also reported earlier in the Audit Report for the Audit Year 2023-24 vide para number 4.23 having a financial impact of Rs 5,408.00 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-26]

#### **4.25 Short-realization of income tax due to application of incorrect tax rates – Rs 2,396.37 million**

First Schedule of the Income Tax Ordinance, 2001 specifies rates for assessment of income for the tax year in order to determine tax liability of taxpayers.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in Large Tax Office, Lahore, three (3) taxpayers had charged less income tax by

applying incorrect tax rates resulting in short-realization of tax amounting to Rs 2,396.37 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 2.24 million were initiated under the law but not finalized and an amount of Rs 2,394.13 million was subjudice.

The DAC, in its meetings held in July, October, November and December, 2024 directed the department to finalize legal proceedings, pursue the subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings and pursuing the subjudice cases besides strengthening the desk audit function.

[DP No.22978, 22792-IT]

#### **4.26 Loss of revenue due to incorrect assessment of tax under respective heads of income – Rs 165.42 million**

According to Section 4 read with Section 11 of the Income Tax Ordinance, 2001 total income was to be computed for charging of tax under the respective heads of income which includes salary, property, business, capital gain and other sources.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in two (02) field offices of FBR, nine (09) taxpayers had not correctly computed tax liability under respective heads of income. The department did not initiate any legal action under the relevant provisions of law for correct levy of tax. This resulted in short assessment of tax amounting to Rs 165.42 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 165.42 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening the desk audit function.

**Note:** The issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22 and 2023-24 vide para numbers 4.4.4, 4.1(i), 4.1 and 4.20 having financial impact of Rs 120,954 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-27]

**4.27 Non-withholding of tax on payment of royalty – Rs 52.83 million**

According to Section 152(1) and Section 153B(1) of Income Tax Ordinance 2001, every person paying an amount of royalty or fees for technical services to a non-resident and resident person shall deduct tax from the gross amount paid at the specified rates.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in one (01) field office of FBR, six (06) withholding agents made payment of royalty but did not deduct due amount of tax during tax year 2022 and 2023 as required under the law. This resulted in non-withholding of tax on payment of royalty amounting to Rs 52.83 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 52.83 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening the desk audit function.

[Annexure-28]

**4.28 Loss of revenue due to non-realization of tax on deemed income - Rs 18.44 million**

According to Section 7E(1) of the Income Tax Ordinance, 2001 as amended through Finance Act 2022, for the Tax Year 2022 and onwards, a tax shall be imposed at the rates specified in Division VIIC of Part-I of the First Schedule on the deemed income i.e. fair market value of capital assets exceeding rupees 25 million with certain exclusions and conditions as specified in the law.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in two (02) field offices of FBR, eight (08) taxpayers were obliged to pay tax on deemed income as the Fair Market Value (FMV) of their capital assets exceeded the statutory threshold as prescribed under the law. But neither the taxpayers made voluntary compliance of law to pay obligatory tax nor the assessing officers of the department initiated proceedings to enforce recovery of tax on deemed income for the Tax Year 2023. This reflects weak internal controls and enforcement of law by the department. The lapse resulted in loss of revenue amounting to Rs 18.44 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 13.23 million were initiated under the law but yet not finalized by the department whereas cases involving an amount of Rs 5.21 million were subjudice.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings, pursue subjudice cases and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings, pursuing the subjudice cases vigorously besides strengthening the desk audit function.

[DP No.22789, 22809 & 23081-IT]

#### **4.29 Non recovery of tax on profit on debt – Rs 316.36 million**

According to Section 151(1) read with Section 80 of the Income Tax Ordinance 2001, where a banking company, a financial institution, Federal Government, a Provincial Government or a Local Government including a person, pays any yield on an account, deposit, certificate, bond, debenture, security or instrument of any kind, the payer of the profit on debt or mark up while making payment shall deduct tax at the rate specified in Division IA of Part III of the First Schedule from the gross amount of the yield, profit or mark up.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in three (03) field offices of FBR, eight (08) taxpayers made payment on account of mark-up charges to its associated undertakings and interest on director's loan. The payers of mark-up or profit on debt did not deduct tax while making payments to the recipients as required under the law. Non deduction of income

tax on mark-up/profit on debt resulted in loss of revenue amounting to Rs 316.36 million for the tax years 2022 and 2023.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 316.36 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings besides strengthening monitoring controls over withholding agents for accurate deduction and timely deposit of tax in government's exchequer.

[DP No.23753, 23365, 23573 & 23396-IT]

#### **4.30 Short-realization of income tax on capital gains – Rs 18.75 million**

According to Section 37(1) read with Section 111 of the Income Tax Ordinance 2001, a gain arising from the disposal of a capital asset by a person in a tax year, other than a gain that is exempt from tax under this Ordinance, shall be chargeable to tax in that year under the head "Capital Gains".

It was observed during the audit of the FYs 2022-23 and 2023-24, that in three (03) field offices of FBR, six (06) taxpayers derived capital gains from the sale of immovable property during the tax year 2022 and 2023 but failed to pay the tax at prescribed rates. The department did not take any action to retrieve the loss of revenue. This resulted in short realization of tax amounting to Rs 18.75 million.

These irregularities were pointed out from February to November 2024. The management replied that proceedings for Rs 18.75 million were initiated under the law but not finalized.

The DAC, in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to finalize legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings and strengthening desk audit besides establishing integration with SBP/NBP/ Provincial land records authorities.

**Note:** The issue was also reported earlier in the Audit Report for the Audit Year 2023-24 vide para number 4.19 having financial impact of Rs 26.00 million. The recurrence of the same irregularity is a matter of serious concern.

[DP No. 23711, 23460 & 23319-IT]

#### **4.31 Incorrect adjustment of brought forward losses – Rs 5,045.17 million**

Section 57 of the Income Tax Ordinance, 2001 provides that if a taxpayer sustains a loss under the head income from the business for a tax year, the loss would be carried forward to the following six tax years and would be adjusted only against profit and gains of such business in the following tax years.

It was observed during the audit of the FYs 2022-23 and 2023-24, that in three (03) field offices of FBR income of fifteen (15) taxpayers was incorrectly assessed at losses. These losses were either assessed incorrectly or carried forward and set off against business income beyond the prescribed limit of six years. This resulted in short realization of Rs 5,045.17 million.

These irregularities were pointed out from February to November 2024. The department replied that proceedings have been initiated but yet not finalized by the department.

The DAC, in its meetings held in October and December, 2024 directed the department to finalize the legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expediting the legal proceedings and introducing systematic checks in return filing systems to flag cases of abnormal brought forward losses besides strengthening risk-based desk audits.

**Note:** The similar issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.4.2, 4.1 (viii), 4.7, 5.23 and 4.21 having a financial impact of Rs 67,442 million. The recurrence of the same irregularity is a matter of serious concern.

[DP No. 3200, 3219, 3236 & 3366-IT/K]

#### **4.32 Non-realization of Capital Value Tax – Rs 3,133.21 million**

Section 8 of the Finance Act 2022 provides that Capital Value Tax shall be levied, charged, collected and paid on the value of assets at the rates specified in the First Schedule. The tax shall be charged on the assets like motor vehicles and electric vehicles which are held in Pakistan. Foreign assets of a resident individual where the value of such assets in aggregate exceeds rupees one hundred million (Rs 100 million) shall also be charged CVT at the rate of one percent (1%) of the value of asset.

It was observed during the audit of the FYs 2022-23 that in seven (07) field offices of FBR, seven hundred and sixty-nine (769) taxpayers neither paid Capital Value Tax (CVT) nor did the taxation officers initiate any legal proceedings to recover the due tax. This resulted in non-realization of Capital Value Tax amounting to Rs 3,149.12 million.

These irregularities were pointed out from February to November 2024. The department replied that Rs 15.91 million had been recovered, Rs 1.36 million was subjudice and proceedings for Rs 3,131.85 million were initiated but not finalized.

The DAC, in its meetings held in October and December, 2024 directed the department to recover the admitted amounts, finalize the legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends to expedite recovery of admitted amounts, pursue the subjudice cases at appropriate fora and finalize legal proceedings besides ensuring the compliance of CVT.

**Note:** The similar issue was also reported earlier in the Audit Reports for the Audit Year 2023-24 vide para number 4.27 having a financial impact of Rs 527 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-29]

## **CHAPTER-5 SALES TAX**

### **5.1 Inadmissible adjustment of input tax credit on fake/flying invoices of suspended/blacklisted taxpayers – Rs 123,585.02 million**

According to Section 21 of the Sales Tax Act 1990, during the period of suspension of registration, the invoices issued by such person shall not be entertained for the purposes of sales tax refund or input tax credit, and once such person is blacklisted, the refund or input tax credit claimed against the invoices issued by him, whether prior or after such blacklisting, shall be rejected through a self-speaking appealable order and after affording an opportunity of being heard to such person.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in nineteen (19) field offices of FBR, three hundred and seventy-five (375) registered persons adjusted input tax credit against fake/flying invoices issued by suspended/blacklisted registered persons. The tax authorities did not monitor or initiate legal proceedings to recover the due tax. This resulted in inadmissible adjustment of input tax amounting to Rs 123,585.02 million.

These irregularities were reported to the department from February to November 2024. The management replied that in two cases of RTO Multan, inquiry regarding tax fraud had already been initiated for Rs 2,852.82 million. In remaining cases, it was replied that cases amounting to Rs 2,479.45 million were under recovery, legal proceedings for Rs 31,346.42 million had been initiated, Rs 82,107.19 million were under adjudication, Rs 3.61 million were subjudice in court of law, however, in cases amounting to Rs 4,795.53 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to share inquiry proceedings for tax evasion to Audit, expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice case, and submit comprehensive replies in non-responsive cases. No further progress was reported till the finalization of this report.

The Audit recommends expediting the inquiry, recovery, legal proceedings and pursuance of subjudice case. Furthermore, IT-system based controls should be introduced to disallow/defer input adjustments claimed on invoices issued by blacklisted/suspected registered persons.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.1.7, 5.2, 6.2.3.10 and (5.2, 5.3) respectively having a financial impact of Rs 37,803.17 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-30]

## **5.2 Short-realization of sales tax due to non-apportionment of input tax – Rs 8,539.37 million**

According to Section 8(2) of the Sales Tax Act 1990, a registered person can reclaim only such proportion of input tax which is attributable to taxable supplies. Adjustment of input tax on raw materials relating to exempt supplies is not admissible. Further, Section 8 (1) (m) read with Section 73(4) of the Act provides that a registered person shall not be entitled to deduct input tax which is attributable to taxable supplies to unregistered persons in excess of the prescribed limit given in the law.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in ten (10) field offices of FBR, one hundred and ninety-six (196) registered persons either adjusted input tax on exempt supplies or made sales to unregistered persons in excess of the prescribed threshold. The registered persons were required to apportion the input tax between taxable and exempt supplies and against sales made to unregistered persons to arrive at their tax liability. However, entire amounts of input tax were adjusted without subject apportionment. The tax authorities did not initiate proceedings to recover the due tax. This resulted in short-realization of sales tax due to non-apportionments of input tax amounting to Rs 8,539.37 million.

These irregularities were reported to the department from February to November 2024. The management replied that cases amounting to Rs 74.20 million were under recovery, legal proceedings for Rs 3,229.54 million had been initiated, Rs 1,495.82 million were under adjudication, Rs 157.30 million were subjudice and in cases amounting to Rs 3,582.51 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice cases and submit comprehensive replies in non-responsive cases. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery/legal proceedings and strengthening of the risk-based desk audits besides introducing systematic checks in the sales tax return filing system to link and cross-verify the claimed input for apportionment between taxable and exempt supplies.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23, 2023-24 vide para numbers 4.1.8, 5.2(i), 5.1, 6.6, & 5.4 respectively having a financial impact of Rs 18,322.68 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-31]

### **5.3 Non-realization of sales tax due to concealment of sales – Rs 35,974.73 million**

According to Section 3(1) read with Section 26 of the Sales Tax Act, 1990 there shall be charged, levied and paid sales tax at the prescribed rates on the value of taxable supplies made by a registered person. Further, every registered person shall furnish a true, complete and correct return in the prescribed form.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in fifteen (15) field offices of FBR, nine hundred ninety-two (992) registered persons declared less sales in sales tax returns for the FYs 2021-22 & 2022-23 as compared with their income tax returns. Further, the registered persons either declared less production (compared to electricity bills) or concealed the sales of closing stocks. The department did not initiate legal proceedings to recover the due tax. This resulted in non-realization of sales tax amounting to Rs 35,974.73 million.

These irregularities were reported to the department from February to November 2024. The management replied that cases amounting to Rs 1,278.30 million were under recovery, legal proceedings for Rs 32,572.92 million had been initiated, Rs 1,818.17 million were under adjudication and in cases amounting to Rs 305.34 million no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings and submit comprehensive replies. No further progress was reported till the finalization of this report.

The Audit recommends for expeditious recovery/legal proceedings of government revenue and ensure comprehensive integration of sales tax and income tax return filing systems besides strengthening risk-based desk audit.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2022-23 and 2023-24 vide para numbers (4.1.2 & 4.1.13), (5.12 & 6.2.3.11) and 5.1 respectively having a financial impact of Rs 46,124.65 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-32]

#### **5.4 In-admissible exemption of sales tax – Rs 7,481.09 million**

According to Section 3(1)(a) of the Sales Tax Act, 1990 sales tax is chargeable at prescribed rates of the value of taxable supplies. Further, as per Section-13 of the Act *ibid*, goods specified in Sixth Schedule shall be exempt from sales tax.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in seventeen (17) field offices of FBR, five hundred and eight (508) registered persons made supplies of taxable goods (i.e. scrap, fixed assets, rice husk and oil by cotton ginner etc.), however, sales tax was not levied or paid against such supplies. The registered persons claimed inadmissible exemption on supply of taxable goods which resulted in non-realization of sales tax amounting to Rs 7,481.09 million.

These irregularities were reported to the department from February to November 2024. The management replied that cases amounting to Rs 567.68 million were under recovery, legal proceedings of Rs 4,290.57 million had been initiated, Rs 1,506.59 million were under adjudication and in cases amounting to Rs 1,116.25 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends prompt action in cases not finalized and fixing of responsibility for inordinate delay/lapse against the person(s) at fault besides ensuring 100% desk audit of claimed exemptions.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers (4.1.5, 4.1.15, 4.1.16 & 4.1.21), 5.1(i), 5.5, (6.7 & 6.11) and 5.7 respectively having a financial impact of Rs 13,232.34 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-33]

#### **5.5 Short-realization of sales tax due to inadmissible adjustment of input tax credit – Rs 5,521.66 million**

According to Section 8(1) of the Sales Tax Act 1990, input tax adjustment is not admissible on goods or services where sales tax has not been deposited in the government treasury by the respective supplier and where goods have not been used in taxable supplies.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in fourteen (14) field offices of FBR, six hundred and eighteen (618) registered persons either adjusted input tax against purchase invoices of goods which were not used in taxable supplies or sales tax was not deposited by the respective suppliers. The department failed to monitor and initiate legal proceedings to recover the due tax in these cases. These inadmissible input tax adjustments resulted in short-realization of sales tax amounting to Rs 5,521.66 million.

These irregularities were reported to the department from February to November, 2024. The department replied that cases amounting to Rs 12.93 million were under recovery, Rs 1,280.56 million were under adjudication, legal proceedings of Rs 2,729.45 million had been initiated, Rs 1.45 million were subjudice and in cases amounting to Rs 1,497.27 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October and December 2024, directed the department to expedite the recovery, legal/ adjudication proceedings, pursue the subjudice case and submit comprehensive replies in non-responsive cases. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery and finalization of legal proceedings besides fixing of responsibility against the person(s) at fault. Further, systematic checks in the sales tax return filing system be introduced to link and cross-verify claimed credit.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.1.4, 5.2(ii), 5.3, 6.2 and 5.8 respectively having a financial impact of Rs 29,350.87 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-34]

#### **5.6 Non-imposition of penalties and default surcharges – Rs 3,535.12 million**

According to Section 33, read with Section 34 of the Sales Tax Act 1990, if a person fails to furnish a return within the due date, such person shall pay a penalty of ten thousand rupees (Rs 10,000). Further, if any person who knowingly or fraudulently makes a false statement, such person shall pay a penalty of twenty-five thousand rupees (Rs 25,000) or one hundred per cent (100%) of the amount of tax involved, whichever is higher. Moreover, a registered person who does not pay the due tax or any part thereof in time is liable to pay default surcharge in addition to the due tax.

It was observed during the audit of the FYs 2022-23 and 2023-24 that nineteen (19) field offices of FBR, in cases of nine thousand five hundred and eighty-two (9582) taxpayers, did not impose penalty and default surcharge. The registered persons either did not submit sales tax returns or submitted the returns late or deposited the sales tax after due dates. The department did not initiate legal proceedings against these registered persons. This resulted in non-imposition of penalties and default surcharge amounting to Rs 3,535.12 million.

These irregularities were reported to the department from February to November 2023. The management replied that cases amounting to Rs 47.00 million were under recovery, legal proceedings for Rs 3,035.92 million had been initiated, Rs 215.37 million were under adjudication, and in cases amounting to Rs 236.83 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery/adjudication/legal proceedings and to provide updated replies besides enforcement of leviable penalties and default surcharge.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide paras number 4.1.18, 5.14, 6.10 and 5.10 respectively having a financial impact of Rs 2,970.83 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-35]

#### **5.7 Non-registration of potential taxpayers liable for registration – Rs 1,310.10 million**

According to Section 2(5AB), 2(25) & 14 of the Sales Tax Act 1990, every person engaged in making taxable supplies in Pakistan, including zero-rated supplies, any manufacturer having turnover of taxable supplies of more than eight million rupees (Rs 8,000,000) or having an industrial gas or electricity connection, if not already registered, is required to be registered under this Act. Further, Section 3, read with Section 26 of the Act, provides that any person making taxable supplies shall pay sales tax at the prescribed rate and furnish true and correct information while filing his sales tax return. Furthermore, the penalty shall be imposed under Section 33(7) of the Act *ibid* for non-registration.

It was observed during the audit of the FYs 2022-23 and 2023-24 that three (03) field offices of FBR did not register one hundred and twenty-one (121) persons even though they were manufacturers, retailers, distributors, wholesalers, dealers, and having large volume of business as evident from income tax record and met the prescribed conditions for compulsory sales tax registration. Non-registration of taxpayers resulted in potential tax effect amounting to Rs 1,310.10 million.

These irregularities were reported to the department from February to November 2024. The department replied that Rs 745.13 million were under adjudication and legal proceedings for Rs 564.97 million had been initiated.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to complete the legal/adjudication proceedings. No further progress was reported till the finalization of this report.

The Audit recommends finalization of legal/adjudication proceedings besides introduction of systematic checks in the return filing systems to flag such cases. In addition to above, monitoring mechanisms for high value transactions may be evolved and reviewed periodically.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.1.23, 5.5, 6.2.3.3, 6.2.3.12 and 5.19 respectively having a financial impact of Rs 6,394.17 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-36]

### **5.8 Non-realization of minimum sales tax liability – Rs 1,238.16 million**

According to Rule 157 of Sales Tax Rules 2006, if a registered person fails to file a return by the due date, his minimum liability would be determined in the prescribed manner. Moreover, Rule 158 (1) of the law *ibid* provides that the minimum tax liability of the registered person for a tax period shall not be less than the highest amount of tax paid by the registered person in any of the tax periods during the previous twelve months.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in four (04) field offices of FBR, forty-eight (48) registered persons did not file sales tax returns for certain tax periods. The tax authorities were required to recover minimum tax liability, however, no efforts were made to recover the government revenue. This resulted in non-realization of minimum tax liabilities of Rs 1,238.16 million.

These irregularities were reported to the department in February to November 2024. The department replied that cases of Rs 776.10 million were under recovery, legal proceedings for Rs 5.03 million had been initiated, Rs 67.56 million were under adjudication, Rs 371.59 million were subjudice and in cases of Rs 17.88 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice cases and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends to pursue the recovery/legal/adjudication proceedings, incentivize early submission of sales tax returns and consistent enforcement of minimum tax and penalties where returns are not submitted timely.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 5.1(ii), 5.11, 6.15 and 5.18 respectively having a financial impact of Rs 405.05 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-37]

### **5.9 Excess adjustments of input tax – Rs 809.62 million**

According to Section 8B of the Sales Tax Act 1990, a registered person shall not be allowed to adjust input tax in excess of ninety per cent (90%) of the output tax for the tax period for which the return was filed.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in four (04) field offices of FBR, twenty-five (25) registered persons adjusted the whole amount of input tax against output tax instead of the permissible limit of ninety percent (90%) of output tax. The department did not initiate legal action to recover the revenue. This resulted in excess adjustment of input tax amounting to Rs 809.62 million.

These irregularities were reported to the department from February to November 2024. The department replied that cases amounting to Rs 203.61 million were under adjudication and legal proceedings for Rs 606.01 million had been initiated.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to complete the legal/adjudication proceedings. No further progress was reported till the finalization of this report.

The Audit recommends to finalize legal/adjudication proceedings besides instituting risk based desk audit and implementing validation checks in the return filing system to automatically disallow adjustments beyond the prescribed limit.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide paras number 4.1.14, 5.6, 6.12 and 5.14 respectively having a financial impact of Rs 1,852.01 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-38]

### **5.10 Short-realization of sales tax on ginned cotton – Rs 1,495.50 million**

According to Section 26 (1) of the Sales Tax Act 1990, every registered person shall furnish not later than the due date a true and correct return in the prescribed form. Further, as per provision (d) of SRO 1087(1)/2019 dated 19.09.2019, the recipient of ginned cotton shall deposit the sales tax due thereon under a payment challan indicating the name and registration number of supplier, along with the return for tax period in which invoice is issued for the relevant supply.

It was observed during the audit of the FY 2023-24 that ten (10) cotton ginners under the jurisdiction of Regional Tax Office, Sahiwal, made taxable supplies and claimed sales tax withheld by the withholding agents but no proof of deposit of sales tax was provided to Audit, as challans were not available on record. The tax payments were required to be deposited by the spinners against the NTN of the ginners but amounts deposited by the spinners were not matched with amounts claimed against the NTN of the ginners. The tax authorities did not initiate legal proceedings against the taxpayers to recover the revenue. This resulted in non/short realization of sales tax and default surcharge of Rs 1,495.50 million.

The irregularity was reported to the department during September to November 2024, with the direction to recover the government dues under intimation to Audit. The department replied that cases were under process and assured that notices under relevant provisions will be issued within 15 days.

The DAC, in its meeting held in December 2024, directed the department to expedite the legal proceedings as per law under intimation to Audit/FBR. No further progress was reported till the finalization of this report.

The Audit recommends expeditious legal proceedings besides introduction of systematic checks in the IT system of FBR to reconcile payments made by spinners against those declared by the ginners.

[DP No.23447 & 23465-ST]

### **5.11 Non-recovery of adjudged dues – Rs 11,653.47 million**

According to Section 48 of the Sales Tax Act 1990 read with Sales Tax Rules 2006, sales tax due from any person shall be recovered by sales tax officers in accordance with the prescribed procedure.

It was observed during the audit of the FYs 2022-23 and 2023-24 that seven (07) field offices of FBR, in four hundred and nineteen (419) cases, did not take prescribed measures for recovery of adjudged dues, like freezing of bank accounts, attachment and sale of moveable/immoveable property even after the lapse of considerable time period. This resulted in non-recovery of Rs 11,653.47 million.

These irregularities were reported to the department in February to November 2024. The department replied that cases of Rs 111.82 million were under recovery, legal proceedings for Rs 10,965.05 million had been initiated, Rs 2.26 million were under adjudication, Rs 530.03 million were subjudice and in cases of Rs 44.31 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice cases and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery and legal proceedings, regular follow up by higher authorities in cases of adjudged dues and devising performance indicators for average timelines during assessment proceedings.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22 and 2022-23 vide paras number 4.1.3, 5.13, 6.1 and 5.5 respectively having a financial impact of Rs 73,145.06 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-39]

#### **5.12 Non-realization of 4/5<sup>th</sup> amount of sales tax from the suppliers – Rs 307.36 million**

According to Section 3(1)(a) and 3(7) read with S. No. 1 of 11<sup>th</sup> Schedule of the Sales Tax Act 1990, there shall be charged, levied and paid a tax known as sales tax at the rate of eighteen percent of the value of taxable supplies made by a registered person. The tax shall be withheld at the rate as specified in the Eleventh Schedule, by any person or class of persons being purchaser of goods or services as withholding agent for the purpose of depositing the same.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in seven (07) field offices of FBR, the DDOs of the respective formations, being

withholding agents, deducted 1/5<sup>th</sup> amount of sales tax in one hundred and twenty-nine (129) cases. However, the suppliers in subject cases failed to pay the remaining 4/5<sup>th</sup> amount of sales tax. The management did not take any action to ensure deposit of the remaining amount of sales tax by the suppliers. The omission resulted in non-realization of 4/5<sup>th</sup> sales tax amounting to Rs 307.36 million.

These irregularities were reported to the department in February to November 2024. The department replied that cases of Rs 56.35 million were under recovery, legal proceedings for Rs 1.47 million had been initiated, Rs 235.37 million were under adjudication and in cases of Rs 14.17 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice cases and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery/legal/adjudication proceedings besides enforcement of monitoring controls over withholding regime.

[Annexure-40]

### **5.13 Non-realization of further tax – Rs 267.06 million**

According to Section 3(1A) of the Sales Tax Act 1990, in case of a supply of taxable goods to unregistered persons, further tax at prescribed rates of three per cent (3%) for FY 2022-23 and four per cent (4%) for FY 2023-24 shall be charged on the value in addition to the rate specified in Section 3 and 4 of the Act.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in six (06) field offices of FBR, eighteen (18) registered persons made taxable supplies to unregistered persons, however, the applicable further tax was not realized under the law. The tax authorities did not initiate legal proceedings to recover the due tax. This resulted in the non-realization of further tax amounting to Rs 267.06 million.

These irregularities were reported to the department from February to November 2024. The management replied that cases amounting to Rs 109.03

million were under recovery, legal proceedings for Rs 56.86 million had been initiated, Rs 73.42 million were under adjudication, Rs 24.57 million were subjudice and in cases amounting to Rs 3.18 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, complete the legal/adjudication proceedings, pursue the subjudice cases and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery and to finalize adjudication/legal proceedings besides strengthening IT based controls to apply further tax in cases where sales are made to unregistered persons.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 & 2023-24 vide para numbers 4.1.11, 5.3, 5.7, 6.8 & 5.16 respectively having a financial impact of Rs 3,677.99 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-41]

#### **5.14 Inadmissible adjustments of input tax credits against sales tax deducted by withholding agents – Rs 208.54 million**

According to Section 8A of the Sales Tax Act 1990, where a registered person receiving a taxable supply of the goods suspects that the goods were supplied without payment of due tax, such person as well as the person making the taxable supply shall be jointly and severally liable for payment of such unpaid amount of tax.

It was observed during the audit of the FYs 2022-23 and FY 2023-24 that in four (04) field offices of FBR, twenty-four (24) registered persons reduced their sales tax liability by the amount of withholding tax credit deducted by their buyers. The buyers either filed nil sales tax returns or they were un-registered persons. This resulted in inadmissible adjustments of input tax credits amounting to Rs 208.54 million.

These irregularities were reported to the department from February to November 2024. The department replied that cases of Rs 198.48 million were under adjudication, and legal proceedings for Rs 7.91 million had been initiated

and in cases amounting to Rs 2.15 million, no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery and adjudication/legal proceedings and submit comprehensive reply where no response was furnished. No further progress was reported till the finalization of this report.

The Audit recommends expediting adjudication/legal proceedings besides enforcement of monitoring controls provided in the law. Compliance of withholding regime needs to be ensured through Commissioner, IR (Withholding).

**Note:** This issue was also reported earlier in the Audit Report for the Audit Year 2023-24 vide para number 5.6 having a financial impact of Rs 3,754.14 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-42]

#### **5.15 Short-payment of sales tax due to mis-declaration in tax return/record - Rs 2,355.57 million**

According to Section 11A of the Sales Tax Act 1990, where a registered person pays the amount of tax less than the tax due as indicated in his return, the less paid amount of tax along with default surcharge shall be recovered from such person by stopping/removal of any goods from his business premises and through attachment of his business bank accounts, without giving him a show cause notice.

It was observed during the audit of the FY 2022-23 that in three (03) field office of FBR, nineteen (19) registered persons paid less sales tax than the liability depicted in their annual financial statements. The tax authorities did not take action to recover the amount from the taxpayers despite the fact that both set of data i.e. sales tax returns and financial statements were available with the department. The lapse resulted in short payment of sales tax amounting to Rs 2,355.57 million.

These irregularities were reported to the department during February to November 2024. The management replied that cases amounting to Rs 2,328.26 million were under scrutiny and in cases for Rs 27.31 million, no response was furnished by the department

The DAC, in its meetings held in July, November, October and December 2024, directed the department to submit comprehensive reply and expedite the legal proceedings. No further progress was reported till the finalization of this report.

The Audit recommends finalization of legal proceedings besides implementation of risk-based desk audit and monitoring of financial statements.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2021-22, 2022-23 and 2023-24 vide paras number 5.10, 6.14 and 5.15 respectively having a financial impact of Rs 988.26 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-43]

#### **5.16 Non-realization of fixed sales tax from bricks kilns – Rs 144.02 million**

According to Section 3(1B) & 14 of the Sales Tax Act, 1990 read with Tenth Schedule and Rule 6 of the Sales Tax Rules 2006, the tax on bricks, falling in PCT heading [6901.0000], shall be paid on fixed basis at the rate of Rs 10,000 per month upon the Brick Kilns. Every person engaged in making taxable supplies in Pakistan, in the course or furtherance of any taxable activity carried on by him, if not already registered, is required to be registered under this Act. Further according to Sub Section 25 of Section 2 of the Act *ibid*, registered person means a person who is registered or is liable to be registered under this Act.

It was observed during the audit of the FY 2023-24 that in five (05) field offices of FBR, five hundred and forty-eight (548) taxpayers operating as bricks kilns were liable to pay fixed sales tax at the prescribed rates but the same was not deposited. However, the tax authorities failed to recover the fixed sales tax or to get the bricks kilns registered in sales tax regime. Thus, public exchequer sustained loss due to non-monitoring of sales tax collection under fixed tax regime. The inefficiency resulted in non-realization of fixed sales tax of Rs 144.02 million.

These irregularities were reported to the department from February to November 2024. The department replied that cases of Rs 1.03 million were under recovery, Rs 4.96 million were under adjudication and legal proceedings for Rs 138.03 million had been initiated.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the recovery, adjudication/legal proceedings and submit comprehensive reply. No further progress was reported till the finalization of this report.

The Audit recommends registration of the unregistered bricks kilns and finalization of legal proceedings for recovery of government dues.

[Annexure-44]

**5.17 Inadmissible adjustment of input tax credit due to non-integration of retail outlets – Rs 490.58 million**

According to Section 3(9A) read with Section 8B(6) of the Sales Tax Act, 1990, Tier-I retailers from such date, and in such mode and manner, as prescribed by the Board, shall integrate their retail outlets with Board's computerized system for real-time reporting of sales. In case a Tier-1 retailer does not integrate his retail outlet in the manner as prescribed during a tax period or part thereof, the adjustable input tax for whole of that tax period shall be reduced by 60%.

It was observed during the audit of the FY 2023-24 that in six (06) field offices of FBR, thirty-nine (39) registered persons failed to integrate their business with POS as evident from sales tax returns. However, neither the department disallow the 60% input tax nor the taxpayers reduced their input tax from output tax. The lapse resulted in inadmissible adjustment of input tax credit amounting to Rs 490.58 million.

These irregularities were reported to the department from August to November 2024. The department replied that cases amounting to Rs 123.55 million were under adjudication and Rs 367.03 million were under process/examination.

The DAC, in its meetings held in October, December 2024 and January 2025, directed the department to expedite the adjudication/legal proceedings.

The Audit recommends expediting adjudication/legal proceedings. Further, systematic checks in the sales tax return filing system be introduced to disallow the claimed input tax credit by Tier-I retailers.

[Annexure-45]

### **5.18 Short-payment of sales tax due to claim of credit notes issued by unregistered persons – Rs 88.99 million**

According to Rule 18(5)(iii) of Sales Tax Rules, 2006, if any buyer of the registered person has not accepted a Credit Note, the supplier shall be allowed provisional reduction in his output tax against the said Credit Note but if the buyer fails to accept such Credit Note in the sales tax and federal excise return by the 10<sup>th</sup> day of the next month, the registered person's said reduction in output tax shall be adjusted or recovered.

It was observed during the audit of the FY 2022-23 that a manufacturer of steel products in Large Taxpayers Office Lahore, claimed sales of goods returns (credit notes) from unregistered persons and reduced its output tax liability. As per law credit/debit notes can only be issued by registered persons. The authenticity of the debit/credit notes could not be verified through FBR's IT system as to whether these were issued by unregistered persons or not. Hence, the reduction of output tax was against the rules, resulting in short payment of sales tax amounting to Rs 88.99 million.

The irregularity was reported to the department from February to May 2024. No progress was reported by the LTO, Lahore.

The DAC in its meeting held in July 2024, directed the LTO Lahore to complete the legal proceedings but no further progress was reported. The DAC in its another meeting held in November 2024, showed its concern over non-compliance of its previous directives and directed the CCIR, LTO, Lahore to personally intervene into the matter and submit a compliance report.

The Audit recommends to justify the delay in finalization of legal proceedings besides improvisations in FBR's IT System to disallow claim of such credit notes.

[DP No. 22962-ST]

### **5.19 Non-withholding of sales tax – Rs 80.51 million**

According to Section 3(7) read with S.No.4 & 5 of the Eleventh Schedule of the Sales Tax Act 1990, a tax is to be withheld at prescribed rates by any person or class of persons being (purchaser of goods or services) as withholding agent for depositing the same. Corporate sector is responsible for withholding sales tax @5% on purchases from persons other than active taxpayers.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in four (04) field offices of FBR, seventy-one (71) registered persons did not withhold sales tax on payment of goods purchased from unregistered persons. However, the tax authorities did not initiate legal proceedings to recover the due tax. This resulted in non-withholding of sales tax amounting to Rs 80.51 million.

These irregularities were reported to the department from February to November 2024. The management replied that legal proceedings for Rs 32.42 million had been initiated and in cases amounting to Rs 48.09 million no response was furnished by the department.

The DAC, in its meetings held in December 2024 and January 2025, directed the department to complete the legal/adjudication proceedings and submit comprehensive replies in non-responsive cases. No further progress was reported till the finalization of this report.

The Audit recommends expediting recovery and to finalize adjudication and initiating legal proceedings where action is awaited besides fixing of responsibility against the person(s) at fault. Moreover, effective monitoring of withholding taxes through automated system be ensured.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide paras number 4.7.1, 5.17, 6.3 and 5.13 respectively having a financial impact of Rs 13,379.87 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-46]

#### **5.20 Irregular sanction of sales tax refund through Fully Automated Sales Tax e-Refund System (FASTER) – Rs 4,335.43 million**

According to Rule 39B, 39D and 39F of the Sales Tax Rules 2006, for all the refund claims, for the tax period July 2019 and onwards, as filed by the exporters of five export-oriented sectors shall be processed through FASTER. The data provided in the monthly sales tax return shall be treated as data in support of refund claim and no separate electronic data shall be required. The amount specified in column 29 of the sales tax return shall be considered as amount claimed once the return has been submitted along with all prescribed annexures thereof. The data in the refund claim shall be scrutinized and verified by the system and the payable refund amount shall be determined on the basis of input consumed in exports or supplies.

It was observed during the audit of the FY 2023-24 that in RTO Faisalabad, the registered persons in two hundred and forty-nine (249) cases got sales tax refund of Rs 4,335.43 million through FASTER system. It was noted that the registered persons filed their monthly sales tax returns by declaring zero closing balances of certain stocks. The refund processing system “FASTER” could not check the quantity wise & value wise comparison of purchases & exports, manufacturing status of taxpayers, production capacity, relevancy of input material with finished products, consumption of utilities by taxpayers, payments through banking channels, and calculation of wastage etc. Also no review/update of FASTER has been done since its inception to overcome its deficiencies. Therefore, being high risk area, the department was required to conduct post refund audit of the claims sanctioned through FASTER, but the same was not conducted which showed weak monitoring of sales tax refund through FASTER resulting in irregular sanction of sales tax refund of Rs 4,335.43 million.

These irregularities were reported to the department from August to November 2024. The department replied that all the cases have been selected for post refund audit.

The DAC, in its meeting held in January 2025, directed the field formation to expedite the post refund audit proceedings. No further progress was reported till finalization of this report.

The Audit recommends to finalize legal proceedings besides ensuring post refund audits under Sales Tax Rules besides an overall review to point out and overcome any system deficiencies.

[DP No.23601, 23613, 23622 & 23694-ST]

#### **5.21 Inadmissible payment of sales tax refund – Rs 928.44 million**

According to Section 10 read with Section-8 of the Sales Tax Act 1990, input tax adjustment is not admissible on goods permanently attached to immovable property such as building material, vehicles and their parts, office equipment and entertainment, goods for personal use. Further, as per Section 73 of the Act *ibid*, transactions exceeding the value of fifty thousand rupees shall be made through banking channels. Moreover, Rule-33 of the Sales Tax Refund Rules 2006, provides that refund shall be paid to the extent of the input tax paid on purchases/imports that are actually consumed in the zero-rated/exported good.

It was observed during the audit of the FYs 2022-23 and 2023-24 that four (04) field offices of FBR, in one hundred and ninety-four (194) cases, sanctioned and paid sales tax refunds on goods not used in taxable supplies or in excess of the input tax consumed in zero-rated/exported goods. Further, refunds were sanctioned without verifying the proof of payments through banking channels or without ascertaining the sales tax liability. This resulted in inadmissible payment of sales tax refunds of Rs 928.44 million.

These irregularities were reported to the department from February to November 2024. The management replied that legal proceedings for Rs 794.78 million had been initiated and in cases amounting to Rs 133.66 million no response was furnished by the department.

The DAC, in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the legal proceedings and submit comprehensive replies in non-responsive cases. No further progress was reported till the finalization of this report.

The Audit recommends expeditious finalization of legal proceedings and initiation of action in non-responsive cases besides initiating disciplinary proceedings against the person(s) at fault.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 & 2023-24 vide paras number (4.2.1, 4.2.2), 5.6, (5.19, 5.20), 6.4 & 5.12 respectively having a financial impact of Rs 7,632.22 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-47]

## **5.22 Non-conduct of post refund audit**

According to Rule 36(1) of the Sales Tax Refund Rules 2006, after disposing of the refund claims, the officer-in-charge shall forward the relevant file to the Post Refund Audit Division for post-refund audit, which shall include verification of input tax payment by respective suppliers along with compliance of Section 73 of the Sales Tax Act 1990.

It was observed during the audit of the FYs 2022-23 and 2023-24 that nine (09) field offices of FBR, in one thousand one hundred forty-three (1143) cases, paid sales tax refund amounting to Rs 35,502.19 million. However, post refund audit (PRA) was not conducted to verify input tax consumption in zero-rated/exported goods and payment of input tax by claimant through banking

channel. The authenticity of refund could not be established without conducting post refund audit. This resulted in non-conducting of post refund audit.

These irregularities were reported to the department from February to November 2024. The department replied that legal proceedings for post refund audit were initiated in all the cases.

The DAC in its meetings held in July, November, October, December 2024 and January 2025, directed the department to expedite the post refund audit of cases. No further progress was reported till the finalization of this report.

The Audit recommends finalization of post-refund audit in the cases pointed out by the Audit, improving the post-refund audit system, and sharing the post refund audit reports with the external Audit for effective feedback.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 5.17, 5.21, 6.17 and 5.20 respectively having a financial impact of Rs 27,121.35 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-48]

### **5.23 Doubtful sanction of sales tax refund – Rs 347.65 million**

According to Section 10 (1) of the Sales Tax Act, 1990, if the input tax paid by a registered person on taxable purchases made during a tax period exceeds the output tax on account of zero-rated local supplies or export made during that tax period, the excess amount of input tax shall be refunded to the registered person.

It was observed during the audit of the FY 2023-24, that LTO Lahore sanctioned sales tax refund amounting to Rs 347.65 million in case of a registered person. Record/file for the same refund was requisitioned, in response LTO Lahore replied that as the refund amount has not yet been credited into the bank account of the registered person so the record cannot be provided. The issue of illegal refund was highlighted on newspaper as well as on electronic media that the refund was sanctioned without fulfilment of legal obligations/credit verification of claimed amount whether the same was admissible to registered person under the law or not. An inquiry committee was also constituted by the Federal Board of Revenue to sort out the same matter. Audit requested the department for provision of sales tax refund sanctioned record/file and report of the inquiry committee constituted by the FBR but the same was not provided to Audit. Without scrutiny of record, authenticity of the sanctioned amount could not be verified, which rendered the sanctioned amount of refund doubtful.

The irregularity was reported to the department in October and November, 2024 with the request that all the relevant record may be provided to Audit, fix responsibility against the persons at fault and status of enquiry report be intimated to Audit but no further reply was received from the department till finalization of the para.

The DAC, in its meeting held in November 2024, directed the LTO, Lahore to complete the legal proceedings, provide relevant record to Audit for scrutiny and submit a comprehensive report. No further progress was reported till the finalization of this report.

The Audit recommends to provide all the relevant record to Audit, fix responsibility against the persons at fault and share inquiry report to Audit.

[DP No.23265-ST]

#### **5.24 Non-realization of sales tax on supply of free electricity – Rs 1,418.95 million**

According to Section 3(1) read with Section 11 of the Sales Tax Act, 1990, there shall be charged, levied and paid a tax known as sales tax at the rate of eighteen per cent of the value of taxable supplies made by a registered person in the course or furtherance of any taxable activity carried on by him.

It was observed during the audit of the FYs 2022-23 and 2023-24 that four (04) electricity distribution companies in four (04) field offices of FBR, had supplied free electricity to their employees without charging sales tax as required under the law. The department did not assess and recover the government revenue. This resulted in non-realization of sales tax amounting to Rs 1,418.95 million.

These irregularities were reported to the department from March to November 2024. The management replied that cases amounting to Rs 674.44 million were under adjudication and Rs 744.51 million were under process/examination.

The DAC, in its meeting held in October, December 2024 and January 2025, directed the department to expedite the legal/adjudication proceedings. No further progress was reported till the finalization of this report.

Audit recommends expeditious finalization of legal/adjudication proceedings besides strengthening the desk audit of the sales tax returns.

[Annexure-49]

**Para from “Special Audit of Selected Inland Revenue Warehouses for the Audit Year 2022-23”**

**5.25 Non-recovery of adjudged government revenue – Rs 53.64 million**

According to Section 48 of the Sales Tax Act 1990 read with Sales Tax Rules 2006, sales tax due from any person shall be recovered by sales tax officers in accordance with the prescribed procedure.

Audit observed during the Special Audit of Selected Inland Revenue Warehouses for the Audit Year 2022-23 that Orders-in-Original have been passed involving tax demand of Rs 53.64 million. However, no recovery was made despite lapse of a considerable period. Detail is given as follow: -

(Rs in million)

Station	Period	No. of cartons	Duty/taxes involved	Manufacturer / Brand
Bahawalnagar	17/12/2019	80	19.14	Gold Street, Classic & Hero
Chishtian	1/12/2021	201	22.02	Gold Street, Classic, Hero & Kisan
Haronabad	17/11/2021	80	11.47	-
Hasilpur	30/11/2021	45	1.01	M/s Khyber Tobacco Co.
<b>Total</b>		<b>406</b>	<b>53.64</b>	

As evident from the table above the oldest seizure activity pertained to 2019 whereas the assessment order was passed in 2022 after a lapse of almost 03 years. No further legal action was initiated by the authorities.

During DAC meeting held in January 2024, RTO Bahawalpur informed that entire amount was under recovery. The DAC directed the RTO to expedite the recovery proceedings and submit progress to Audit and FBR by 31.01.2024. The department did not intimate recovery position till the finalization of the report.

The Audit recommends proactive action to materialize and recover government revenue besides fixing responsibility.

[Para 4.2.2 of Special audit of Selected Inland Revenue Warehouses for the Audit Year 2022-23]

## **CHAPTER-6 FEDERAL EXCISE DUTY**

### **6.1 Non/short-realization of federal excise duty – Rs 390.45 million**

According to Section 3 of the Federal Excise Act, 2005, there shall be levied and collected federal excise duty on excisable goods at prescribed rates. Further, as per Section 14 of the Federal Excise Act, 2005, where any amount of duty levied and penalty imposed or any other amount payable is due from any person, the officer of Inland Revenue may deduct the amount from any money owing to person.

It was observed during the audit of the FYs 2022-23 and 2023-24 that three (03) field offices of FBR in four (04) cases, either did not levy and collect federal excise duty on dutiable goods (cement, air tickets) or did not recover the liability of FED declared by the registered persons in Annual Audited Accounts. This resulted in non/short-realization of federal excise duty amounting to Rs 390.45 million.

These irregularities were reported to the department from February to November 2024. The department replied that legal proceedings in cases of Rs 152.88 million had been initiated, however, in cases of Rs 237.57 million, no response was furnished by the department.

The DAC in its meeting held in July, November, December 2024 and January 2025, showed its concern over non-responsive cases and directed the CCIR, LTO, Lahore to personally intervene in the matter. In remaining cases, the DAC directed to expedite the legal proceedings in under process cases. No further progress was reported till the finalization of this report.

The Audit recommends to expedite the legal proceedings to recover the government revenue besides strengthening risk based desk audits.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para number 4.3.1, (6.3 & 6.4), 7.1 and 6.1 respectively having a financial impact of Rs 5,849.06 million. The recurrence of the same irregularity is a matter of serious concern.

[DP No.22888, 22898, 23496-FED & 7273-FE/K]

## **6.2 Short-realization of FED on sales of natural gas – Rs 397.77 million**

According to Section 3 of the Federal Excise Duty Act 2005, duties specified in the First Schedule are to be levied subject to the provisions of this Act and rules made there under on specified goods produced or manufactured in Pakistan, goods imported into Pakistan and such goods as the Federal Government may, by notification in the official Gazette, specify.

It was observed during the audit of the FY 2022-23 that a registered person under the jurisdiction of Large Taxpayers' Office, Karachi was required to pay FED on natural gas @ Rs 10 per MMBTU, whereas, the registered persons paid less FED than required as per provision of law. The department did not initiate legal proceedings to rectify the same. This resulted in short-realization of federal excise duty amounting to Rs 397.77 million

The irregularity was reported to the department in March 2024. The department replied that the matter was under process/examination.

The DAC, in its meeting held in December 2024, directed the department to expedite the legal proceedings and submit comprehensive reply. No further progress was reported till the finalization of this report.

Audit recommends early finalization of legal proceedings besides strengthening of assessment mechanism of federal excise duty.

[DP No.7305-FE/K]

## **6.3 Short-realization of FED on sales of motor vehicles – Rs 223.49 million**

According to Sr. No.55B (as amended by Finance Supplementary Act, 2022) of Table-1 First Schedule read with Section 3 of Federal Excise Duty Act, 2005, federal excise duty shall be charged on locally manufactured or assembled motor cars, SUVs and other motor vehicles, excluding auto rickshaws at the specified rates.

It was observed during the audit of the FY 2022-23 that a registered person under the jurisdiction of Large Taxpayers' Office, Karachi was required to pay FED on sale of motor cars amounting to Rs 526.04 million, whereas the taxpayer actually paid Rs 302.79 million. The department did not initiate any legal proceedings to rectify the same. This resulted in short-realization of FED amounting to Rs 223.49 million.

The irregularity was reported to the department in March 2024. The department replied that the matter was under process/examination.

The DAC, in its meeting held in December 2024, directed the department to expedite the legal proceedings and submit comprehensive reply. No further progress was reported till the finalization of this report.

Audit recommends early finalization of legal proceedings besides strengthening of assessment mechanism of federal excise duty.

[DP No.7300-FE/K]

## **CHAPTER-7      CUSTOMS DUTY**

### **7.1      Blockage of revenue due to non-disposal of confiscated goods/vehicles - Rs 12,600.09 million**

According to Sections 82, 89, 169, 182 and 201 of the Customs Act, 1969 read with Rule 58(1) of the Customs Rules, 2001 and Customs General Order 12 of 2002 dated 15.06.2002, confiscated goods are required to be disposed of after observing codal formalities within the shortest possible time.

It was observed during audit of the FYs 2015-18, 2022-23 and 2023-24 that twenty-seven (27) field offices of FBR including DG (FC) Peshawar and DG Rangers Lahore, in four thousand three hundred and ninety-six (4396) cases, did not dispose of confiscated goods, including vehicles, edibles and valuables, as per law. These goods/vehicles were lying either in open spaces or unhealthy atmospheric conditions in the warehouses since long which not only resulted in declining in value but also fitness of edible goods for human consumption. This resulted in a blockage of revenue of Rs 12,600.09 million.

These instances were pointed out during February 2018 and February to November 2024. The management replied that cases amounting to Rs 395.41 million were under recovery, Rs 11,519.12 million were under scrutiny/ under auction, Rs 1.60 million were pending in adjudication, and Rs 683.98 million were pending in court of law.

The DAC, in its meetings held in December 2020, August, December 2024 and January 2025, directed the department to expedite recovery, early disposal of confiscated goods and pursue the cases pending in the adjudication/ courts. No further progress was reported till the finalization of this report.

Audit recommends expediting recovery, storage facilities of confiscated goods may be improved to ensure their fitness and fetching of compatible bids, besides fixing of responsibility on the person(s) at fault.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.1, 7.3, 7.16, 8.2 and 7.1 respectively having financial impact of Rs 35,824.56 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-50]

## **7.2 Blockage of revenue due to non-encashment of financial instruments – Rs 9,354.05 million**

According to Section 81 of the Customs Act, 1969 imported goods may be assessed provisionally. Further, imported goods are cleared without payment of duty and taxes on submission of bank guarantees, indemnity bonds or post-dated cheques. These instruments were required to be encashed to recover government dues upon non-fulfilment of prescribed conditions.

It was observed during audit of the FYs 2022-23 and 2023-24 that twelve (12) field offices of FBR, in two thousand eight hundred and eighty-one (2881) cases, did not encash financial instruments where the importers/exporters failed in fulfilling the requisite conditions of law within the stipulated time period. Moreover, the expired financial instruments were not re-validated by the customs authorities due to weak monitoring and financial controls. This resulted in blockage of revenue amounting to Rs 9,354.05 million.

These irregularities were pointed out from February to November 2024. The management replied that cases amounting to Rs 338 million were under recovery, Rs 5,766.11 million were under scrutiny, Rs 0.56 million were pending in adjudication, and Rs 3,249.38 million were pending in court of law.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases under adjudication or pending in the courts, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends strict compliance to Rules and encashment of financial instruments without fail where importers/exporters did not comply with requisite conditions, besides fixing of responsibility against the person (s) at fault in cases where financial instruments had expired.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.9, 7.1(iv), 7.5, 17, 8.3 and 7.29 respectively having a financial impact of Rs 15,414.59 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-51]

### **7.3 Non/short-realization of revenue on un-exported finished goods - Rs 3,288.51 million**

The Customs Rules, 2001 provided the facility of duty-free imported goods under different schemes i.e. duty and tax remission for exports, manufacturing bonds, exports processing zone and export oriented units for subsequent export of finished goods. Further, under SRO 492(I)/2009 dated 13.06.2009, whole of custom duty and sales tax was exempt on temporary import of goods for subsequent exportation subject to prescribed conditions.

It was observed during audit of the FYs 2013-17, 2022-23 and 2023-24 that five (05) field offices of FBR, in one hundred and four (104) cases, did not initiate action against the importer-cum-manufacturers who either failed to clear/utilize the goods under various export schemes within the stipulated period or illegally removed the input goods from the premises. This was an indication of weak internal controls and weak monitoring by the customs authorities. This resulted in non-realization of government revenue of Rs 3,288.51 million.

These instances were pointed out during February to April 2018 and March to October 2024. The management replied that cases amounting to Rs 169 million were under recovery, Rs 292.88 million were under scrutiny, Rs 13.55 million were under adjudication and Rs 2,791.54 million were pending in court of law. The management contested an amount of Rs 21.54 million on the plea that the user was authorized vide DTRE PCSE-2303-15092022 for a period of one year till 15.09.2023 and the collectorate accordingly informed the user switched to EFS, as the DTRE discontinued from 30.06.2023. Audit is of the view that the relevant record should be produced to substantiate departmental stance in contested case.

The DAC, in its meetings held in December 2020, August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases pending in the courts, and to get their stated position verified by the Audit. No further progress was reported till the finalization of this report.

Audit recommends strict adherence to rules for realization of government revenue in such instances, besides fixing of responsibility against the concerned officers/officials.

[Annexure-52]

#### **7.4 Non-recovery of adjudged government revenue – Rs 2,268.52 million**

According to Section 2 of the Customs Act, 1969 read with Chapter-XI of the Customs Rules, 2001, when under this Act or under any other law for the time being in force, which provides for any tax, duty or other levy being collected in the same manner as customs-duties are collected, a penalty is adjudged against, or notice or demand is served upon, the appropriate officer shall recover the government dues as per procedure given in rule and law. Further, Annexure-4 of CGO 12/2002 dated 15.06.2002 states that failure to submit a properly completed reconciliation statement on time shall result in an automatic fine equivalent to 2 percent of all duties and taxes remitted in application form.

It was observed during audit of the FYs 2015-18, 2022-23 and 2023-24 that fourteen (14) field offices of FBR, in five hundred and sixteen (516) cases, did not initiate further legal proceedings for recovery of adjudged revenue, penalty and fine while releasing goods on payment of duty and taxes and encashment of bank guarantees of DTRE users. The adjudged revenue amounting to Rs 2,268.52 million remained un-recovered due to inaction of the department.

These irregularities were pointed out from February to April 2018 and February to November 2024. The management replied that cases amounting to Rs 1,056.15 million were under recovery, Rs 1,044.08 million were under scrutiny/ not responded, Rs 8.16 million were pending in adjudication and Rs 160.02 million were pending in court of law.

The DAC, in its meetings held in December 2020, August, December 2024 and January 2025, directed the department to expedite recovery of admitted amount, pursue the cases under adjudication, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends expeditious recovery of adjudged government revenue besides pursuance of cases pending decision at various forums.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2018-19, 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.7, 4.8.6, 7.15, 8.1 and 7.14 respectively having a financial impact of Rs 5,956.94 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-53]

## **7.5 Loss of revenue due to inadmissible exemptions/concessions in duties and taxes – Rs 1,556.52 million**

Under Section 19 of the Customs Act, 1969, Section 13 of the Sales Tax Act, 1990 and Section 53 of the Income Tax Ordinance 2001, goods imported into Pakistan have been granted exemptions/concessions in duties and taxes subject to the fulfilment of prescribed conditions.

It was observed during audit of the FYs 2022-23 and 2023-24 that sixteen (16) field offices of FBR, in one thousand six hundred and twenty-eight (1628) cases, granted exemptions and concessions in duties and taxes on goods (like PCB boards, scientific equipment, edible oil, pharmaceutical items etc.) which did not qualify for such exemptions/concessions. This resulted in loss of revenue amounting to Rs 1,556.52 million due to inadmissible exemptions.

The lapses were pointed out from February to November 2024. The management replied that cases amounting to Rs 253.84 million were under recovery, Rs 250.13 million were under scrutiny, Rs 4.91 million were pending in adjudication, and Rs 1,041.25 million were pending in court of law. The management contested an amount of Rs 6.39 million on the plea that benefit of concerned Schedule/SROs was granted as per law. However, the Audit disagrees with the contention as the imported goods were not entitled for exemptions as these goods were not included in the concerned schedules of the exemptions.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases under adjudication or pending in the courts, and submit comprehensive replies in cases under scrutiny and to get their stated position verified by Audit. No further progress was reported till the finalization of this report.

Audit recommends inclusion of artificial intelligence in WeBOC system to avoid claim of inadmissible exemptions/concession in duty & taxes, besides fixing of responsibility against the person(s) at fault.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.3, 11.12, 7.1(ii), 7.3, 8.4 and 7.2 respectively having a financial impact of Rs 15,000.28 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-54]

## **7.6 Non/short-realization of government revenue on wastage – Rs 1,424.92 million**

According to Section 95(2) of the Customs Act, 1969 in case of goods exported, waste generated from their manufacturing shall either be destroyed or duty shall be paid on such waste if it had been imported in Pakistan in that form. Further, according to Rule 307A (e) of the Customs Rules, 2001 read with clarification issued by the FBR issued vide C. No. 5(10)EP/2017/20/856-R dated 06.12.2021, local sale of B-grade products, factory rejects or wastage shall be allowed on payment of leviable duties and taxes.

It was observed during audit of FYs 2013-17 and 2023-24 that five (05) field offices of FBR, in thirty-three (33) cases, either did not initiate action for disposal of wastage produced during manufacturing process by the users/licensees of exports schemes namely DTRE, Manufacturing Bond, Exports Facilitation Scheme or allowed disposal of wastage without realization of leviable duty & taxes. This was an indication of weak internal controls and weak monitoring by the customs authorities. This resulted in blockage of revenue due to non-disposal of wastage amounting to Rs 1,424.92 million.

These lapses were pointed out during February to April 2018 and August to September 2024. The management replied that cases amounting to Rs 7.60 million were under recovery, and Rs 1,417.32 million were under scrutiny.

The DAC, in its meetings held in December 2020, August, December 2024 and January 2025, directed the department to expedite recovery, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends that disposal of wastage be ensured strictly in line with provisions of the Customs Act and clarification issued by the FBR to avoid such instances in future.

[Annexure-55]

## **7.7 Short-realization of duties and taxes due to misclassification of imported goods – Rs 1,162.63 million**

Goods imported into Pakistan are classified according to PCT headings given in the First Schedule to the Customs Act, 1969 for the realization of customs duties and allied taxes at rates provided therein.

It was observed during the audit of the FYs 2022-23 and 2023-24 that fourteen (14) field offices of FBR, in five thousand three hundred and fifty-seven (5357) cases, cleared imported goods (like mobile phones pouches, thermostats, power cable, printing ink, packing material, flavour, auto parts, packing machinery parts, glassware and rubber items etc.) by misclassifying these items under incorrect PCT headings, attracting lower rates of duties and taxes instead of correct PCT headings with higher rates. This resulted in short-realization of duties and taxes amounting to Rs 1162.63 million.

These instances were pointed out from February to November 2024. The management replied that cases amounting to Rs 450.54 million were under recovery, Rs 310.45 million were under scrutiny, Rs 14.30 million were pending in adjudication, and Rs 0.51 million were pending in court of law. The management contested an amount of Rs 386.83 million on the plea that the goods were correctly classified. Audit is of the view that the goods were required to be classified as per descriptions provided in the First Schedule and guidelines contained in the explanatory notes.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases under adjudication or pending in courts, submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends that imported goods should be classified as per general rules for interpretation, description of goods provided in the First Schedule and guidelines contained in explanatory notes, besides fixing responsibility against persons at fault.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2018-19, 2019-20, 2021-22, 2022-23 and 2023-24 in para numbers 4.8.8, 4.8.5, 7.4, 8.9 and 7.7 respectively having a financial impact of Rs 3,068.10 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-56]

#### **7.8 Non-finalization of cases under adjudication – Rs 973.87 million**

According to Section 179(3) of the Customs Act 1969, the cases shall be decided within ninety (90) days of the issuance of show cause notice or within such period extended by the Collector for which reasons shall be recorded in writing, but such extended period shall in no case exceed sixty days.

It was observed during the audit of the FYs 2022-23 and 2023-24 that four (04) field offices of FBR, in forty-three (43) cases did not finalize adjudication proceedings within stipulated or extended period. This resulted in non-finalization of cases involving revenue amounting to Rs 973.87 million.

The irregularity was reported to the department from February to November 2024. The management replied that cases amounting to Rs 114.18 million were finalized/adjudicated and confiscated goods were under auction and cases involving Rs 859.69 million were under adjudication.

The DAC, in its meetings held in January 2025, directed the department to refer the finalized cases to the respective Collectorate for further necessary action as per law and pursue cases with Adjudication Collectorate for early decision.

The Audit recommends implementation of DAC directives.

[Annexure-57]

#### **7.9 Ineffective pursuance of court cases resulted in blockage of government revenue – Rs 972.39 million**

According to Section 196(7) of the Customs Act, 1969 read with Article 199 (4A) of the Constitution of the Islamic Republic of Pakistan 1973, where recovery of duty has been stayed by the High Court by an order, such order shall cease to have effect on the expiration of a period of six months. Further, according to Section 194B of the Customs Act, 1969, appeal shall be decided by the Appellate Tribunal within sixty days of filing the appeal or within such extended period as the Tribunal may, for reasons to be recorded in writing, fix, further in cases, wherein the provisions of clause (s) of Section 2 have been invoked, appeals shall be decided within a period of thirty days.

It was observed during the audit of the FYs 2022-23 and 2023-24 that in four (04) field offices of FBR, ninety-three (93) cases were subjudice before Honourable Supreme Court, High Court and Customs Appellate Tribunal, Karachi, which were instituted during the years from 2012 to 2023. The Collectorates neither pursued the cases proactively for early finalization nor initiated any legal action for recovery of revenue against the importers who were granted stay orders by the High Courts but the same had expired after lapse of six months. The inefficiency of the Collectorate resulted in blockage of government revenue of Rs 972.39 million.

These lapses were pointed out from February to November 2024. The management replied that cases amounting to Rs 243.99 million were subjudice in various legal forums and in cases involving Rs 728.40 million reply of the management is still awaited.

The DAC, in its meeting held in January 2025, directed the department to pursue the legal cases proactively and submit comprehensive reply in cases not responded by the department.

The Audit recommends detailed progress report be provided to Audit in respect of each case, in chronological order, in order to ascertain the efforts made by the Collectorate in pursuance of the court cases.

[Annexure-58]

#### **7.10 Non/short-realization of sales tax and value addition tax – Rs 834.02 million**

According to Section 3 of the Sales Tax Act, 1990 there shall be charged, levied, and paid a tax known as sales tax at prescribed rates on goods imported into Pakistan, irrespective of their final destination inside territories of Pakistan. Further, according to the Twelfth Schedule of the Sales Tax Act, 1990 value addition tax shall be levied and collected at the rate of three percent (3%) on all imported goods subject to exclusions provided therein.

It was observed during audit of the FYs 2022-23 and 2023-24 that twenty (20) field offices of FBR, in one thousand seven hundred and fourteen (1714) cases, either did not realize the sales tax and value addition tax or realized the same at lower than applicable rates on imported goods (like glue, vaccine, power cable, pen and highlighter etc.). Non-adherence to relevant laws and weak monitoring controls caused non/short-realization of sales tax and value addition tax amounting to Rs 834.02 million.

These irregularities were pointed out from February to November 2024. The management replied that cases amounting to Rs 665.94 million were under recovery, Rs 29.59 million were under scrutiny/ not responded, Rs 0.06 million were pending in adjudication, and Rs 0.73 million were pending in court of law. The management contested an amount of Rs 137.71 million on the plea that sales tax was either collected correctly or exempted as per law. Audit is of the view that the value addition tax was not recovered from the commercial importers and exemption / concession under the Sales Tax Act, 1990 was granted incorrectly.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases pending in adjudication/ courts, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends enhanced supervision at higher level to ensure genuineness of exemption or concession in applicable rate of sales tax and value addition and expeditious recovery in admitted cases.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.2,15,22, 7.1(i), 7.2, 8.8 and 7.8 respectively having a financial impact of Rs 7,639.48 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-59]

#### **7.11 Short-realization of duties and taxes due to under-valuation of imported goods – Rs 865.78 million**

Section 25 read with Sections 30 and 31(a) of the Customs Act, 1969 provides a detailed procedure for determining the value of imported/warehoused goods. Further, Section 25-A of the Act ibid empowers the Directorate General of Customs Valuation Karachi to fix the value of imported goods or any class of goods.

It was observed during audit of the FYs 2015-18, 2022-23 and 2023-24 that twenty-three (23) field offices of FBR, in one thousand six hundred and eighty-nine (1689) cases, either assessed the imported goods (like porcelain articles, LED drivers, cleaning brushes, chain parts, LED television, toys, LED lights, steel pipe, padlock and mobile back covers etc.) at lower values as required under the concerned Sections of the Act or did not comply with the valuation rulings issued by the Directorate General of Valuation, Karachi. This resulted in short-realization of duties and taxes amounting to Rs 865.78 million.

These instances were pointed out from February 2018 and February to November 2024. The management replied that cases amounting to Rs 209.69 million were under recovery, Rs 404.66 million were under scrutiny/ not responded, Rs 24.44 million were pending in adjudication, and Rs 7.49 million were pending in court of law. The management contested an amount of Rs 219.50 million on the plea that the goods were correctly assessed, and government revenue was realized accordingly. Audit is of the view that the

goods were required to be assessed according to Section 25 of the Act, valuation rulings in vogue and evidential data available in WeBOC System.

The DAC, in its meetings held in December 2020, August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases under adjudication, submit comprehensive replies in cases under scrutiny and sought clarification from DG Valuation, Karachi on the issue of mobile back covers. No further progress was reported till the finalization of this report.

Audit recommends that WeBOC controls should be strengthened by ensuring timely uploading and application of valuation ruling, as and when issued, besides fixing of responsibility against person(s) at fault.

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2020-21, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.8, 7.1(iii), 7.1, 8.13 and 7.6 respectively having a financial impact of Rs 5,291.48 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-60]

#### **7.12 Non/short-collection of income tax – Rs 534.52 million**

Section 148 of the Income Tax Ordinance, 2001 provides rates of income tax applicable at import stage as specified in Part-II of the First Schedule in respect of goods classified in Parts I to III of the Twelfth Schedule to the Ordinance.

It was observed during audit of the FYs 2022-23 and 2023-24 that eighteen (18) field offices of FBR, in two thousand eight hundred and eighty-one (2881) cases, either did not collect income tax at the time of clearance of imported goods or collected it at lower than specified rates. This resulted in non/short-collection of income tax amounting to Rs 534.52 million.

These instances were pointed out from February to November 2024. The management replied that cases amounting to Rs 383.75 million were under recovery, Rs 23.68 million were under scrutiny, Rs 0.06 million were pending in adjudication, and Rs 1.64 were pending in court of law. The management contested an amount of Rs 125.37 million on the plea that withholding income tax on import stage was correctly assessed and recovered. However, the Audit disagreed with the contention as withholding income tax was recoverable from

the importers in line with the rates provided in the Twelfth Schedule to the Income Tax Ordinance.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, pursue the cases under adjudication or pending in courts and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends that controls in WeBOC System may be improved for correct application of approved rate of income tax as per Twelfth Schedule, besides fixing of responsibility against the concerned person(s).

**Note:** This issue was also reported earlier in the Audit Reports for the Audit Years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.8.28, 4.8.31, 7.8, 8.11 and 7.10 respectively having a financial impact of Rs 1,169.21 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-61]

### **7.13 Irregularities in auction of vehicles/goods – Rs 427.35 million**

According to Rule 58 (2) of the Customs Rules, 2001, the Collector shall cause the reserved price of the auction-able goods to be determined in accordance with the provisions of Section 25 read with Clause C of Sub-section 2 of the Customs Act 1969. Furthermore, Rule 73 of the Customs Rules, 2001 states that the highest bid given at an auction may be accepted.

It was observed during the audit for the FYs 2022-23 and 2023-24, that six (06) field offices of FBR, in fifty (50) cases, committed the following irregularities during auction process amounting to Rs 427.35 million;

- (i) Incorrect/lesser determination of reserve price (as the applicable duty and taxes were not included and undue depreciation was allowed in the value);
- (ii) Unjustified acceptance of lower bid;
- (iii) Irregular release of one seized vehicle;
- (iv) Non-reconciliation of auction proceeds, incomplete/non-maintenance of auction record and non-verification of vouchers with bank.

These irregularities were pointed out during February to November 2024. The management replied that cases where reserve price was short assessed were referred to the Appraisal Collectorate for obtaining their view point, auction

record was being maintained properly and auction proceeds were being reconciled with the concerned bank.

The DAC, in its meetings held in January 2025, directed the department to obtain view point from Appraisement Collectorate regarding less determination of reserve price, expedite reconciliation process and get the stated position verified from Audit.

The Audit recommends implementation of DAC directives.

[Annexure-62]

#### **7.14 Evasion of government revenue due to non-fixation of time for consumption or installation of goods/machinery – Rs 290.85 million**

According to S. No. 151 of Table-1 to the 6<sup>th</sup> Schedule of the Sales Tax Act, 1990, Sales Tax is exempt on imports of plant, machinery, equipment for installation in tribal areas and of industrial inputs by the industries located in the tribal areas on presentation of a post-dated cheque for the amount of sales tax and the same shall be returned to the importer after presentation of a consumption or installation certificate as issued by the Commissioner Inland Revenue having jurisdiction.

It was observed during the audit of the FYs 2022-23 and 2023-24 that three (03) field offices of FBR, in twenty-six (26) cases, granted exemption of Sales Tax to the importers of the Tribal Area. The importers failed to provide requisite consumption/installation certificate of the imported goods/machinery. The Collectorate lodged FIRs against the importers as the post-dated cheques were dishonoured. Audit further observed that there is lack of internal control as time limit for the consumption or installation of the imported goods/machinery was also not fixed by the FBR. Audit is of the view that this exemption facility should be time bound. The inaction of the Department resulted in loss of government revenue of Rs 290.85 million.

These irregularities were pointed out from February to November 2024. The management replied that cases involving an amount of Rs 263.56 million are subjudice before the Special Judge (Customs, Taxation and Anti-Smuggling), Karachi and Rs 27.29 is under recovery.

The DAC, in its meeting held in January 2025, directed the department to pursue the legal cases proactively, expedite recovery and refer the matter to the FBR for necessary amendment in the statutory provisions of law.

The Audit recommends expediting recovery of admitted amounts besides pursuance of court cases and necessary amendments in relevant provisions of law.

[Annexure-63]

#### **7.15 Non-realization of revenue due to non-clearance of warehoused goods – Rs 253.64 million**

According to Section 98 of the Customs Act, 1969 warehoused goods, other than perishable goods notified by the Board, may remain in the warehouse for a period of six months following the date of their admission into the warehouse.

It was observed during audit of the FY 2022-23 that four (04) field office of FBR, in fifty-seven (57) cases, did not initiate action for clearance of warehoused goods despite lapse of warehousing period of six months. The extension in warehousing period was neither applied for by the bonders nor granted by the customs authorities. This resulted in blockage of government revenue of Rs 253.64 million.

These instances were pointed out during March 2024. The management replied that cases amounting to Rs 34.01 million were under recovery and Rs 219.63 million were under scrutiny / not responded.

The DAC, in its meetings held in August 2024 and January 2025, directed the department to expedite recovery, ensue disposal of goods in pointed out cases, and provide comprehensive replies in cases not responded. No further progress was reported till the finalization of this report.

Audit recommends to expedite recovery besides timely initiation of legal action in cases of non-removal of warehoused goods for recovery of deferred amount of duty & taxes.

[Annexure-64]

#### **7.16 Non-realization of duty & taxes from non-performing DTRE user - Rs 225.36 million**

According to Rule 307A of Sub-Chapter VII of the Customs Rules, 2001 amended through SRO 510(I)/2010 dated 11.06.2010, if a DTRE user fails to consume the duty and tax free input goods in exports in full except wastage, if not covered under valid extension, he shall be liable to pay duties and taxes

including additional duties or additional tax and penalties leviable on such goods under the relevant Acts or the Ordinance.

It was observed during audit of FY 2023-24 that one (01) field office of FBR, in one (01) case, released bank guarantee of DTRE user after realization of leviable duty and taxes on un-consumed quantities only. This was wrong as the DTRE user not only failed in procurement of approved quantities of input goods but also failed in utilization and export of actual quantities imported/procured. This resulted in undue remission of duty and taxes to a non-performing DTRE user amounting to Rs 225.36 million.

The irregularity was pointed out during August 2024. The management contested the para on the grounds that the unconsumed quantities of input goods have been cleared on payment of duty & taxes. Audit disagreed with the contention of the formation based on misunderstanding of changes in DTRE Rules made through SRO 510(I)/2010.

The DAC, in its meeting held in December 2024, directed the Collectorate to re-visit its stance in the light relevant provisions and get the same verified from the Audit. No further progress was reported till the finalization of this report.

Audit recommends strict compliance to DTRE rules regarding non-performing DTRE users to avoid such instances in future.

[DP No. 9061-Cus]

#### **7.17 Release of smuggled vehicles in violation of orders of the Apex Court – Rs 246.98 million**

According to the condition (b) of the SRO 499(I)/2009 dated 13.06.2009 no option shall be given to pay fine in lieu of confiscation in respect of lawfully registered conveyance including packages and containers found carrying smuggled goods in false cavities or being used exclusively or wholly for transportation of offending goods under clause (s) of Section 2 of the Customs Act, 1969. Further, a full bench of Supreme Court of Pakistan had given verdict on 23.02.2017 that no option of payment of redemption fine could be given against smuggled goods covered under Section 2(s) of the Customs Act.

It was observed during audit of FYs 2015-18 and 2023-24 that ten (10) field offices of FBR, in one hundred and ninety (190) cases, released the offending vehicles in the light of orders passed by adjudicating authorities on

payment of redemption fine in violation of aforesaid judgment passed by the Honourable Supreme Court of Pakistan instead of filing of appeal at next forum. This happened due to weak monitoring and weak internal control. This resulted in release of government property to smugglers valuing Rs 246.98 million.

These irregularities were pointed out during February 2018 and September 2024. The management replied that cases amounting to Rs 246.98 million were under scrutiny.

The DAC, in its meetings held in December 2020 and December 2024, directed the department to submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

The Audit recommends dissemination and placing of such important decisions on the official website of FBR for strict compliance to avoid such instances in future.

[DP Nos. 9097, 9105-Cus& 4.2.2 PAR (Pr. Function)]

#### **7.18 Loss of revenue due to non-recovery of surcharge – Rs 48.13 million**

Ministry of Commerce vide SRO 598(I)/2022 dated 19.05.2022 banned the import of certain goods. Later on, import of such goods was allowed on payment of surcharge fixed by the Ministry. Further, Section 83 (2) read with Section 202A the Customs Act, 1969 where the owner/defaulters fails to pay assessed duty & taxes/arrears within the prescribed time, he shall, in addition to the duty & taxes/arrears, be liable to pay surcharge at the rate of KIBOR plus three per cent per annum of the total amount of duty & taxes/arrears.

It was observed during audit of the FYs 2022-23 and 2023-24 that six (06) field offices of FBR, in two hundred and sixty-one (261) cases, did not recover the surcharge where either banned items were imported or assessed duty & taxes/arrears were not deposited by the importers/defaulters within stipulated period of time. This resulted in non-recovery of surcharge amounting to Rs 48.13 million.

These lapses were pointed out from February to November 2024. The management replied that cases amounting to Rs 36.66 million were under recovery. The management contested an amount of Rs 11.47 million on the plea that the goods either imported by the industrial undertaking or did not cover under the SRO. However, Audit disagreed with the contention as the goods were covered under the SRO and surcharge was recoverable from the importers.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to expedite recovery, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends expeditious recovery, strengthening the system to eliminate such instances in future besides fixing of responsibility on person(s) at fault.

[Annexure-65]

#### **7.19 Non-realization of anti-dumping duty – Rs 23.71 million**

According to the Notification of National Tariff Commission (NTC) issued under Section 50 of the Anti-Dumping Duty Act, 2015, NTC imposed definitive anti-dumping duty on import of certain items at the rates specified therein.

It was observed during the audit of the FYs 2022-23 and 2023-24 that three (03) field offices of FBR, in twelve (12) cases cleared imported goods without realization of anti-dumping duty, whereas the goods (like hydrogen peroxide, polyester staple fibres, CR coils etc.) were liable to anti-dumping duty under the NTC Notification. It indicated weak internal controls in assessment and monitoring. The omission resulted in non-realization of revenue amounting to Rs 23.71 million.

These lapses were pointed out from February to November 2024. The management replied that the amount is under recovery.

The DAC, in its meeting held in January 2025, directed the department to expedite recovery.

The Audit recommends expediting recovery of admitted amounts.

[Annexure-66]

#### **7.20 Blockage of revenue due to non-clearance of unclaimed IGMs - Rs 12.44 million**

Section 82 of the Customs Act, 1969 provides the detailed procedure where imported goods are not cleared for home-consumption or warehoused or transhipped or are not loaded on the conveyance for export or removed from the port area within fifteen days of their arrival at a customs station or within such extended period not exceeding five days.

It was observed during audit of the FYs 2022-23 and 2023-24 that four (04) field offices of FBR, in fifty-five (55) cases, either issued notices after lapse of considerable time i.e. up to twelve years or no notices were issued to the owners of unclaimed IGMs, at all. Such unnecessary delay deteriorated the goods in quality and value which either fetched no bid or lower bids at the time of disposal through auction. This was an indication of weak internal controls and weak monitoring by the customs authorities. This resulted in potential loss to national exchequer of Rs 12.44 million.

These irregularities were pointed out during March to November 2024. The management replied that cases amounting to Rs 7.44 million were under scrutiny and Rs 5.00 million were pending in court of law.

The DAC, in its meetings held in August, December 2024 and January 2025, directed the department to pursue the cases pending in the courts, and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends strict adherence to relevant provisions of law to ensure timely disposal of such un-claimed goods without delay besides fixing of responsibility against the concerned officers/officials.

[DP Nos. 8941, 8987, 9169 & 9311-Cus]

#### **7.21 Un-authorized import of unapproved input goods – Rs 19.92 million**

According to Rules 352, 880 and 882 of the Customs Rules, 2001, the input goods for production of finished goods according to the specification approved in the Analysis Certificate shall be procured by the licensee of a manufacturing bond and Export Facilitation Scheme (EFS) user without payment of customs duty, federal excise duty, sales tax and withholding tax.

It was observed during audit of the FY 2022-23 that three (03) field office of FBR, in five (05) cases, did not initiate legal action against licensees of manufacturing bond/EFS users who had imported goods classifiable under PCT headings which were not approved in the analysis certificate. The licensee/users imported the un-authorized input goods in violation of the Customs Rules. This resulted in loss of revenue of Rs 19.92 million.

The irregularity was pointed out during February to April 2018 and March, 2024. The management replied that an amount of Rs 7.30 million was under recovery and Rs 12.62 million was under scrutiny.

The DAC, in its meetings held in December 2020, August 2024 and January 2025, directed the department to expedite recovery of the admitted amount and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends to expedite recovery of admitted amount besides improving the system to eliminate such lapses in future.

[DP No. 8810, 8811-Cus& 4.7 of PAR (DTRE)]

## **7.22 Non-realization of capital value tax – Rs 5.61 million**

Section 8 of the Finance Act, 2022 provides that capital value tax shall be charged on the motor vehicle held in Pakistan where (i) the engine capacity exceeds 1300 cc; or (ii) in case of electric vehicles, the battery power capacity exceeds 50kwh.

It was observed during the audit of FY 2023-24 that three (03) field offices of FBR, in sixty-one (61) cases, cleared vehicles like Audi, Aqua, Honda FIT, Toyota Hiace, etc. without charging Capital Value Tax (CVT). It was a clear indication of weak monitoring of assessment process by the customs authorities. This resulted in loss of revenue amounting to Rs 5.61 million.

These instances were pointed out from July to November 2024. The management replied that the amount is under recovery.

The DAC, in its meeting held in January 2025, directed the department to expedite recovery of the pointed out amount.

The Audit recommends expediting recovery of admitted amount.

[Annexure-67]

## **7.23 Illegal release of imported goods in violation of Import Policy Order – Rs 3.83 million**

Ministry of Commerce vide SRO 598(I)/2022 dated 19.05.2022 banned the import of certain goods. Later on, import of these goods was allowed which landed after 30<sup>th</sup> June 2022 and on or before 31<sup>st</sup> July 2022, subject to payment of surcharge fixed by the Ministry.

It was observed during audit of the FY 2022-23 that one (01) field office of FBR, in eighteen (18) cases, cleared different imported goods i.e. vacuum cleaners, mobile phones, parts for VCD/DVD and sewing machine etc. upon payment of leviable duty and taxes, whereas, the same were required to be

confiscated being imported in violation of Import Policy Order in vogue. This resulted in illegal release of banned items valuing Rs 3.83 million.

The irregularity was pointed out during May 2024. The management replied that the goods were imported by the industrial/ manufacturing concerns for the purpose of sampling and in a non-commercial quantity through courier services. However, Audit disagreed with the contention as the goods were not industrial inputs thus the goods i.e. vacuum cleaners, mobile phones, wall sockets etc were released illegally in violation of IPO.

The DAC, in its meetings held in August 2024 and January 2025, directed the Collectorate to submit a comprehensive reply and get the stated position verified from Audit. No further progress was reported till the finalization of this report.

Audit recommends necessary changes in the customs clearance system for strict compliance of the IPO, besides fixing of responsibility of the person(s) at fault.

[DP No. 8933-Cus]

#### **7.24 Inadmissible payment of rebate – Rs 4.29 million**

According to Section 35 of the Customs Act, 1969 read with SROs 209, 210 & 211(I)/2009 dated 05.03.2009, when any goods, capable of being easily identified, which have been imported into Pakistan and upon which customs-duties have been paid on importation, are exported to any place outside Pakistan or as provisions or stores for use onboard a conveyance proceeding to a foreign territory, such duties shall be repaid as draw back and rebate. Rebate is payable on FOB value of exported goods mentioned therein at the rates mentioned in the SROs *ibid*.

It was observed during audit of the FY 2023-24 that one (01) field office of FBR, in forty-five (45) cases, either paid rebate at rates more than the rates provided in the aforesaid SROs on exported goods like sports wears made of 100% polyester, leather jackets, and leather bags etc. or paid rebate on goods i.e. barber scissors, leather hats not provided in the SROs *ibid*. This was an indication of weak internal controls and weak monitoring by the customs authorities. This resulted in excess payment of rebate of Rs 4.29 million.

These irregularities were pointed out during September 2024. The management replied that cases amounting to Rs 4.29 million were under recovery.

The DAC, in its meeting held in January 2025, directed the department to expedite recovery of the amount pointed out. No further progress was reported till the finalization of this report.

The Audit recommends expeditious recovery of admitted amounts, besides improvement in the system devised for payments of rebate to eliminate such irregularities in future.

[DP Nos. 9024, 9025, 9026 & 9027-Cus]

#### **7.25 Non-realization of federal excise duty – Rs 4.02 million**

Federal excise duty is leviable under Section 3 of the Federal Excise Act 2005, on imported goods at rates specified in the First Schedule of the Act.

It was observed during the audit of the FYs 2022-23 and 2023-24 that two (02) field offices of FBR, in sixteen (16) cases, did not realize federal excise duty on imported goods like fertilizers and vehicles. This resulted in non-realization of federal excise duty amounting to Rs 4.02 million.

These instances were pointed out from February to November 2024. The management replied that the amount is under recovery.

The DAC, in its meeting held in January 2025, directed the department to expedite recovery.

The Audit recommends expediting recovery of admitted amount.

[DP Nos. 3668 & 4062-CD/K]

#### **7.26 Non-realization of duty & taxes on retained goods – Rs 2.51 million**

According to condition (v) of PCT Heading 9919, goods imported for demonstration, display, test or trial purposes temporarily for a period not exceeding 6 months into Pakistan with a view to subsequent exportation, subject to furnishing of bank guarantee or other security/ guarantee as determined by Federal Board of Revenue equivalent to customs duty chargeable at the rates specified in Chapter 1 to 97 of the 1<sup>st</sup> Schedule to the Act for such goods and other taxes leviable thereon.

It was observed during audit of the FY 2023-24 that one (01) field office of FBR, in one (01) case, released bank guarantee without comparing the goods imported and the goods stated to be exported subsequently. This resulted in irregular release of bank guarantee without realization of duty & taxes on goods retained and not exported by the importer concerned. The government was thus deprived of due share of revenue of Rs 2.51 million.

The lapse was pointed out during August 2024. The management replied that the entire amount of Rs 2.51 million was under recovery.

The DAC, in its meeting held in December 2024, directed the department to expedite recovery of the amount pointed out. No further progress was reported till the finalization of this report.

Audit recommends improvements in WeBOC system for comparison of temporary imports at the time of re-export to avoid such instances in future.

[DP No. 9038-Cus]

#### **7.27 Abnormal reduction in reserve price causing loss to national exchequer**

According to Rule 58(2) of Chapter-V of the Customs Rules, 2001, reserved price of the goods to be auctioned to be determined in accordance with the provisions of section 25 of the Act, and payable duties or taxes under clause (c) of sub-section (2) of that section on the date of fixation of the reserve price shall be added to this value provided that depreciation in the value of goods, will be allowed after one month from the date of importation, at the rate of one percent per month during the first year, and at the rate of 2% per month during the 2<sup>nd</sup> year onwards, up to a maximum of fifty percent, in case of imported goods.

It was observed during audit of the FY 2023-24 that one (01) field office of FBR, in two (02) cases, auctioned two vehicles after reducing the reserve price abnormally as compared to assessed values, shown in seizure reports issued just five months ahead of auction. This abnormal reduction in the reserve price led to lower bids and corresponding loss to national exchequer.

The irregularity was pointed out during September 2024. The management did not submit its stance.

The DAC, in its meeting held in December 2024, expressed displeasure at non-response from the Collectorate and directed to submit a comprehensive

reply within 15 days. No further progress was reported till the finalization of this report.

Audit recommends for supervision of auction process at higher level, besides explanation for abnormal reduction in reserve price in the instant cases.

[DP No. 9098-Cus]

### **7.28 Non-conduct of post-exportation audits**

According to Rule 307E (1) of Sub-Chapter-7 of the Customs Rules, 2001 post-exportation audit is to be carried out and completed satisfactorily within a period of three months. Further, according to Rule 361 of the Customs Rules, 2001 an appropriate officer of customs, authorized by the concerned Assistant Collector of Customs, shall conduct stock taking and detailed audit of a warehouse as and when so directed but at least once in a year.

It was observed during audit of the FY 2022-23 that five (05) field office of FBR, in one hundred and thirty-four (134) cases, did not conduct post-exportation audits of DTRE users and licensees of manufacturing bonds. This resulted in irregular remission of duty and taxes amounting to Rs 3,385.09 to the users/licensees of export regime.

The irregularity was pointed out from February to May, 2024. The management replied that cases amounting to Rs 5.7 million were under recovery, Rs 3,003.32 million were under scrutiny, and Rs 376.07 million were pending in adjudication.

The DAC, in its meeting held in December 2024, directed the department to expedite recovery, pursue the cases under adjudication and submit comprehensive replies in cases under scrutiny. No further progress was reported till the finalization of this report.

Audit recommends to expedite recovery besides involvement at senior management in order to streamline the process of post exportation audits.

[Annexure-68]

### **7.29 Improper monitoring of revenue collected through International Mail Office/Postal Appraisement Department**

According to Para 90 of CGO 12 of 2002 dated 15<sup>th</sup> June 2002, the Director of Accounts after consolidation of accounts on quarterly basis will issue a sanction within two months of close of the quarter to the Senior Post Master,

Karachi General Post Office for payment of the amounts realized by Post Office to the Collector of Customs (Preventive). Within 15 days of the receipt of sanction, the Senior Post Master, Karachi GPO will issue two cheques in favour of Collector of Customs (Preventive), Karachi, one for payment of Customs Duty and the other for the payment of Sales Tax realized on inward postal articles. On receipt of cheques, the Collector shall make payment of commission charges to GPO at the rate of 12% of the amount of duty and tax collected by the postal authorities out of the amount provided for this purpose in the Sea Customs grant within 15 days of the receipt of cheques. Further according to Section 155A of the Act, the Board is responsible to bring the provisions relating to the Customs Computerized System in force throughout Pakistan progressively.

It was observed during the audit of the FY 2022-23, that the International Mail Office/Postal Appraisal Department committed the following irregularities, but the Collectorate of Customs, JIAP, Karachi did not enforce the above provision of law.

1. Postal Authority itself deducted commission charges at the rate of 14.52% from the gross amount of duty & taxes instead of payment by the Collectorate at permissible rate of 12%.
2. Postal Authority collected income tax also on inward postal parcels but there is no proof available with the Collectorate that the same has been deposited in the Collector's account
3. Postal Authority collected revenue of millions of rupees on inward postal parcels manually without recording in the WeBOC system. Further, there was no record available with the Customs for actual revenue collection by the GPO. The Customs is heavily relying on the revenue figures reported by the Postal Authority. Due to this deficiency, the revenue collected by the GPO and deposited with the Customs cannot be authenticated. The Collectorate did not automate/develop module in the WeBOC System for digitalization of the business process.

These irregularities were pointed out in February 2024. The management replied that the matter has been taken up with the Postal Authorities for early resolution of the matter.

The DAC, in its meeting held in January 2025, directed the department to take up the matter with the Postal Authority as well as with the Board for removal of variation in the rate of commission charged by the Postal Authorities and provided in the CGO, to stop deduction of commission charges at source and

make efforts to roll out the WeBOC module at IMO for system based collection of revenue through Pakistan Post.

The Audit recommends implementation of DAC directives, besides automation of the system so that the government revenue may be secured.

[DP Nos. 3317, 3318, 3319 & 3320-CD/K]

### **7.30 Irregularities observed during audit of the Directorate of Customs Transit Trade, Karachi**

According to the Customs Rules, 2001, at the time of cross-border of the transit goods, the office en-route shall take a print-out of the GD, which will be handed over to Afghan Customs for endorsement in token of receipt of transit goods, the Afghan Customs will also provide a copy of T-1 bearing cross reference of GD filed in Pakistan and a certificate to the effect that the transit goods have crossed the border. Further, under Electronic Data Interchange (EDI) between Afghanistan and Pakistan Customs, the confirmation regarding cross border movement and arrival of the goods at the Afghan Customs shall be received electronically. Further, the Deputy/Assistant Director of Securities of the Office of Departure shall be responsible for taking appropriate steps on a fortnightly basis for timely reconciliation, encashment, revalidation or physical release of financial guarantee. In case of non-receipt of cross border certificate along with T-1 or non-fulfilment of any conditions against which the security was furnished by the Afghan importer or exporter, the security shall be en-cashed for recovery of government revenue.

It was observed during audit of the FY 2023-24 that despite the above legal framework, the Directorate of Customs, Transit Trade, Karachi did not function proactively and committed the following irregularities:

1. Thirty-two (32) containers/trucks of transit commercial cargo forwarded to Afghanistan from Karachi port had not crossed the Afghanistan-Pakistan Border despite the lapse of 3 to 15 months time;
2. Two hundred and sixty-nine (269) containers/trucks of transit commercial cargo forwarded to Afghanistan from Karachi port and crossed the Afghanistan-Pakistan Border, however, their receipt in Afghanistan by the Afghan Customs Authorities was not acknowledged; and

3. Two hundred and five (205) insurance guarantees involving an amount of Rs 3,957.49 million in respect of transit commercial cargo forwarded to Afghanistan from Karachi port were pending despite the fact that their validity period had expired. The Directorate neither obtained fresh insurance guarantees nor revalidated the expired guarantees.

These instances were pointed out in August 2024. The management replied that in 25 cases cross border certificates were issued, in 12 cases acknowledgements from Afghan Customs were received and in 122 cases insurance guarantees had been released and remaining cases were under process.

The DAC, in its meeting held in January 2025, directed the department to expedite disposal of the remaining cases at the earliest.

The Audit recommends implementation of DAC directive.

[DP Nos. 4014, 4015 & 4016-CD/K]

## **CHAPTER-8 EXPENDITURE**

### **8.1 Inadmissible payment on account of cash reward – Rs 484.44 million**

According to Rule 2(v) read with Rule 8(1) of the Customs Reward Rules 2012 and Rule 2(vii)-(viii), 6 & 7 of the Inland Revenue Reward Rules 2021, the calculation of reward in cases involving evasion of duty and taxes and confiscation of goods shall be sanctioned after the realization of the duty and other taxes involved. Furthermore, cash reward to the employees would be allowed on the basis of meritorious/extra-ordinary services performed. “Meritorious services” include exceptional performance like exceeding budgetary targets through extra-ordinary planning and efforts, displaying exceptional results in the recovery of arrears, enlarging the base of taxpayers, exceptional performance in defending cases before the ATIR, and displaying extraordinary devotion to duty and acumen towards making some original contribution.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its twenty-two (22) field offices, in forty (40) cases paid cash reward to officers/officials in violation of reward rules. Cash reward was paid without determination of merit in accordance with aforesaid rules. This rendered payment of cash reward of Rs 484.44 million as inadmissible.

These irregularities were pointed out during February to November 2024. The department informed that reward was granted to employees based on meritorious services rendered by the officers/officials duly approved by the Board.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to provide detailed justification in line with criteria / circular issued by the Board for processing and sanctioning of reward. No further progress was reported till finalization of this report.

The Audit recommends strict compliance of criteria laid down for disbursement of cash reward for meritorious services besides expediting recovery from the concerned officers/officials.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.9.1, 8.4, 9.2 and 8.1 respectively having a financial impact of Rs 1,845.06 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-69]

## **8.2 Excess/inadmissible expenditure – Rs 334.61 million**

According to Rule 10 of General Financial Rules, every public officer authorized to incur expenditure from the public funds shall observe the high standards of financial propriety and is expected to exercise the same vigilance in respect of expenditure from public money, as a person of ordinary prudence will exercise in respect of expenditure of his own money. Similarly, Rule-11 of General Financial Rules Vol-I provides that the head of the department and subordinate disbursing officers are responsible for enforcing financial order and strict economy at every step.

It was observed during audit of the FYs 2022-23 and 2023-24 that thirty-six (36) field offices of FBR, in two hundred and nineteen (219) cases made certain violations in purchase and repair/maintenance of various items. The violations including excess payment to lawyers, payment of electricity bills to different company instead of K-Electric, made heavy payments in the month of June etc. This depicted poor internal controls on the part of the department. This resulted in excess and inadmissible expenditure amounting to Rs 334.61 million due to lack of vigilance and internal control lapses.

These irregularities were pointed out during February to November, 2024. The management replied that the expenditure was incurred after fulfilling all codal formalities.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to provide relevant documentary evidence besides fixing responsibility on the person (s) at fault for sanctioning expenditure without necessary documents. No further progress was reported till the finalization of this report.

The Audit recommends recovery of excess and inadmissible expenditure besides fixing of responsibility against the persons at fault.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20 and 2023-24 vide para numbers 4.9.10 and 8.5 respectively having a financial impact of Rs 90.05 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-70]

## **8.3 Non-withholding of sales tax on services – Rs 36.01 million**

According to Rule-5 of notification No.PRA/Orders 06/2012 dated 20<sup>th</sup> February 2015 issued by Punjab Revenue Authority, a withholding agent, other

than a recipient of advertisement services, shall withhold the whole amount of sales tax shown in the tax invoice issued by a registered person as service provider and make payment of the balance amount of the invoice to the registered person. Section 8(1)(a) of the Sales Tax on Services Acts (Punjab/Sindh), the drawing and disbursing officer, preparing bill for the accounting office, shall indicate the amount of sales tax withheld under the rules and the accounting office shall adopt the payment procedure.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its twenty-seven (27) field offices, made payments in forty-six (46) cases on acquiring taxable services without collection of sales tax. This resulted in non-withholding of sales tax amounting to Rs 36.01 million.

These irregularities were pointed out during February to November 2024. The management replied that the amount pointed out was under-recovery and subjudice.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to expedite recovery and pursue the subjudice cases. No further progress was reported till finalization of this report.

The Audit recommends to expedite recovery of amount pointed out and pursue the subjudice cases for early hearing.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.9.13, 8.10, 9.9 and 8.18 respectively having a financial impact of Rs 45.73 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-71]

#### **8.4 Irregular expenditure on POL and unauthorized use of official vehicles – Rs 95.53 million**

According to Cabinet Division's notification No.6/7/2011-CPC, Islamabad, dated 12.12.2011, departments needing operational vehicles were required to get authorization for such vehicles from the vehicle committee constituted for the purpose. Furthermore, Rules 9, 15 & 18 of Staff Car Rules 1980, provide that proper records in the shape of log books, movement registers, and requisition slips shall be maintained in respect of all government vehicles to effectively control the expenditures of POL and repair/maintenance.

It was observed during audit of the FYs 2022-23 and 2023-24 that thirty-four (34) field offices of FBR, in one hundred and three (103) cases, incurred expenditure on POL, repair/maintenance of vehicles without maintaining log-books, movement registers and requisition slips. Further, the vehicles were used without authorization of the concerned quarter. Thus, expenditure on account of POL aggregating to Rs 95.53 million was irregular and unauthorised.

These irregularities were pointed out during February to November 2024. The management replied authorization of vehicles were obtained from the committee of the Cabinet Division and the requisite record duly signed by the concerned quarter was available.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 showed serious concern over poor progress and submission of improper working papers. The DAC further directed the department to look into the matter besides fixing responsibility on person (s) at fault. No further progress was reported till the finalization of this report

The Audit recommends to enforce Staff Car Rules, 1980 in letter and spirit besides implementation of DAC directives.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.9.3, 8.15, 9.3 and 8.4 respectively having a financial impact of Rs 524.55 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-72]

#### **8.5 Inadmissible expenditure on account of pay and allowances Rs 64.05 million**

According to the Revised Leave Rules, 1980 and Rule 7-A of Supplementary Rules, any employee proceeding on leave is not entitled to draw conveyance allowance. In case of extraordinary leave, no pay and allowance are admissible to government servants. Further, FBR's Circular No.01 of 2015 dated 6<sup>th</sup> March, 2015, provides that the Performance Allowance shall not be admissible in case of leave beyond 48 days.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its forty-five (45) field offices, in one thousand three hundred and forty-eight (1348) cases paid inadmissible pay and allowances during leave

period. This depicts ineffectiveness of HR and DDO functions. This resulted in inadmissible payment of pay and allowances amounting to Rs 64.05 million.

These irregularities were pointed out during February to November, 2024. The management replied that the recovery of amount pointed out was underway.

The DAC in its meetings held in July, October, November and December, 2024 directed the department to recover the amount pointed out and submit comprehensive reply. No further progress was reported till the finalization of this report.

The Audit recommends expeditious recovery from the officers/officials involved. Moreover, sanctioning and authorizing functions need to be segregated and pre-audit role should be performed at DDO level.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.9.5, 8.1, 9.5 and 8.3 respectively having a financial impact of Rs 499.21 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-73]

#### **8.6 Irregular expenditure due to non-observance of Public Procurement Rules – Rs 40.05 million**

According to Rule 8 read with Rule 9 and 16-A of Public Procurement Rules 2004, all procuring agencies shall devise a mechanism, for planning of proposed procurements with the object of realistically determining the requirements of the procuring agency. Further, procuring agency shall announce in an appropriate manner all proposed procurements for each financial year and shall proceed accordingly without any splitting or regrouping of the procurements so planned. Furthermore, as per Rule 12(1), procurements over five hundred thousand Pakistani Rupees and up to the limit of three million Pakistani Rupees shall be advertised on the Authority's website.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its seventeen (17) field offices, in fifty-three (53) cases incurred expenditure on purchase of office stationery, payment of service rendered, uniform and liveries, cost of other stores and repair & maintenance in violation of provision of the rules. These violations pertain to lack of planning, splitting, repeated purchases without any specific justification, demand requisition, satisfactory work completion certificate, acknowledgement receipts etc. Poor

internal controls lead to mis-procurement which resulted in irregular expenditure on procurement amounting to Rs 40.05 million.

These irregularities were pointed out during February to November 2024. The management contested the para on the grounds that the expenditure was made after fulfilling all codal formalities. Furthermore, the procurement of different items was made from time to time based on requirements. Audit holds that the record provided by the department to Audit did not support their stance.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the head of the department to look into the matter and take action against the responsible officers/officials besides taking corrective action. Furthermore, the department was directed to either provide relevant documentary evidence or get the matter regularized. No further progress was reported till the finalization of this report.

The Audit recommends fixing responsibility against the persons at fault and regularization of subject mis-procurement besides preparing and uploading annual procurement plans on PPRA website.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22, 2022-23 and 2023-24 vide para numbers 4.9.7, 8.7, 9.1 and 8.2 respectively having financial impact amounting to Rs 833.86 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-74]

#### **8.7 Non-recovery of loans/advances and interest – Rs 24.16 million**

According to Rules 243 to 258 of GFR Vol-I, recovery of loans and advances is to be made in specified instalments and the first instalment is to commence after the advance is drawn and the recovery of interest will commence from the month following the month in which the principal amount has been repaid.

It was observed during the audit for the FYs 2022-23 and 2023-24 that nineteen (19) field offices of FBR, in one hundred and six (106) cases paid different kinds of loans and advances to their employees, however, recovery of principal/interest amount was not initiated. The omission resulted in non-recovery of loans/advances and interest amounting to Rs 24.16 million.

These irregularities were pointed out from February to November 2024. The management informed that recovery from the concerned employees was underway through AGPR and concerned District Accounts Offices.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to expedite the recovery from concerned employees. Further, no progress was reported till finalization of this report.

The Audit recommends expeditious recovery of advances along with interest.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2021-22, 2022-23 and 2023-24 vide para numbers 8.2, 9.10 and 8.11 respectively having a financial impact of Rs 63.54 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-75]

#### **8.8 Non-deduction of tax on payment for goods and services – Rs 28.33 million**

According to Sections 149 & 153 of the Income Tax Ordinance 2001, every person responsible for paying salary to an employee shall, at the time of payment, deduct tax from the amount paid at the employee's average rate of tax computed at the rates specified on the estimated income of the employee chargeable under the head "Salary" for the tax year. Every prescribed person making a payment in full or part including a payment by way of advance to a resident person for the sale of goods, rendering or providing of services and on the execution of a contract is liable to deduct tax from the recipients.

It was observed during the audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its eleven (11) field offices, in three hundred and fifteen (315) cases made payments for goods & services, salaries and cash reward but income tax was not withheld/deducted at the time of making payments. This resulted in non-deduction of income tax amounting to Rs 28.33 million.

These irregularities were pointed out during February to November 2024. The management replied that necessary changes had been sent to AGPR/DAO for recovery from concerned vendors. Further LTO Lahore reported that work related to installation of electrical/networking falls under manufacturing

category. However, the Audit is of the view that the vendor was a manufacturer of furniture instead of electrical networking.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to expedite recovery of amount pointed out by Audit from the concerned and get the departmental contention verified in contested cases. No further progress was reported till the finalization of this report.

The Audit recommends expeditious recovery at the earliest besides fixing of responsibility against the concerned.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22 and 2023-24 vide para numbers 4.9.18, 8.11 and 8.7 respectively having financial impact of Rs 63.87 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-76]

### **8.9 Irregular expenditure due to mis-classification of head of account – Rs 14.81 million**

According to Para 5(d) of the System of Financial Controls and Budgeting 2006, Principal Accounting Officer (PAO) is responsible for ensuring that the expenditure is not incurred in excess of the budget allocation. He shall ensure that payments are correctly classified under the appropriate heads of accounts and that departmental accounts are regularly reconciled every month with the figures communicated by the Controller General of Accounts (CGA)/Accountant General of Pakistan Revenues (AGPR).

It was observed during audit of the FYs 2022-23 and 2023-24 that three (03) field offices of FBR, in three (03) cases incurred expenditure in violation of stated rule. Furthermore, due to misclassification certain heads were disbursed more than the actual grant. This resulted in irregular expenditure of Rs 14.81 million.

The irregularity was pointed out during February to November, 2024. The management replied that the expenditure was incurred under the correct head of accounts. The departmental contention is not tenable as expenditure was mis-classified therefore the matter may be regularized.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025, directed the department to provide detailed justification

of misclassification and sought clarification from FBR. No further progress was reported till the finalization of this report.

The Audit recommends regularization of irregular expenditure from competent authority and compliance of DAC directives.

**Note:** The issue was reported earlier also in the Audit Report for Audit Year 2019-20 and 2023-24, vide para numbers 4.9.21 and 8.12 respectively having financial impact of Rs 15.23 million. Recurrence of same irregularity is a matter of serious of concern.

[DP-22926, 1470-Cus/K & 1200-IR/K]

### **8.10 Excess expenditure in violation of Finance Division directions - Rs 13.97 million**

According to Austerity Measures for Financial Year 2022-23 issued by Government of Pakistan Finance Division (Expenditure Wing) vide letter No.F.7(1)Exp. IV/2016-340 Islamabad, the 7th July, 2022, wherein as per para-1(i) “there shall be complete ban on purchase of all type of vehicles”. Furthermore, as per para-2 “Principal Accounting Officers shall ensure that: (i) consumption of utilities be reduced by 10%; (ii) existing entitlement for POL for government functionaries be reduced by 30%”.

It was observed during audit of the FYs 2022-23 and 2023-24 that two (02) field offices of FBR, in two (02) cases, did not reduce the consumption of utilities and POL as prescribed in the above referred austerity measures issued by the Finance Division. This resulted in irregular expenditure of Rs 13.97 million.

These irregularities were pointed out during July to November 2024. The management replied that in one case the matter is pending with FBR for clarification and in other case no reply was submitted by RTO Sukkur.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025, directed the RTO Sukkur to submit comprehensive reply and sought clarification from FBR. No further progress was reported till the finalization of this report.

The Audit recommends compliance of DAC’s directives at the earliest.

[DP-23479 & 1267-IR/K]

### **8.11 Inadmissible Payment of TA/DA claims – Rs 10.07 million**

According to FBR's Admn/HR Wing C. No.21(5)/HRM.IR-VI/2022 dated 21<sup>st</sup> November, 2023, Hon'ble Wafaqi Mohtasib (Ombudsman)'s Secretariat in consultation with Finance Division (Regulations Wing) decided the matter that Daily Allowance (D.A) cannot be sanctioned to the officers/staff of Inland Revenue Field Formations during the period of their posting under Section-40-B of the Sales Tax Act, 1990. Moreover, Para 11.8 of Manual of Travelling Allowance Rules provides that, the advance TA should be adjusted through T.A. bill immediately on return to headquarters or on 30<sup>th</sup> June whichever is earlier. Further ordinary daily allowance is admissible for non-specified stations.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its fifteen (15) field offices, made excess payments under the head TA/DA in one hundred and forty-one (141) cases to officers/officials. The department incurred expenditure on account of excess mileage charges, hotel accommodation charges, travelling allowance and daily allowance on posting/transfer of the officers/officials. This resulted in inadmissible payment of TA / DA amounting to Rs 10.07 million.

These irregularities were pointed out during February to November 2024. The management contested the para, in some cases, on the grounds that the department paid the correct amount of TA/DA. The departmental contention is not tenable as expenditure was over and above the entitlement.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the amount pointed out and submit comprehensive reply in cases under scrutiny. No further progress was reported till the finalization of this report.

The Audit recommends compliance of DAC directives at the earliest.

**Note:** The issue was also reported earlier in the Audit Report for Audit year 2019-20 vide para number 4.9.17 having a financial impact of Rs 0.58 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-77]

### **8.12 Excess payment of hired residential accommodations – Rs 9.16 million**

According to Ministry of Housing and Works letter No.F.2(3)/2003-Policy dated 31.07.2004, scale-wise rental ceiling and covered area has been specified for assessment of rent. Further, as per paras 8(10) of Accommodation Allocation Rules 2002, a hired or requisitioned house is to be allotted at the station of posting at specified stations.

It was observed during audit of the FYs 2022-23 and 2023-24 that eleven (11) field offices of FBR, in forty-four (44) cases incurred expenditure on account of rent of residential accommodations which did not comprise prescribed covered area. Further, payments were also made on account of rent of accommodation at specified station whereas posting was at non-specified station. This resulted in excess payment of hired residential accommodation amounting to Rs 9.16 million due to weak monitoring by the department on financial matters.

These irregularities were pointed out during February to November 2024. The management informed that the recovery of over-payment was under process.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to enforce recovery and get the contention verified from Audit. No further progress was reported till finalization of this report.

The Audit recommends expeditious recovery of excess payment of rent from the concerned quarter besides strict compliance of relevant rules and observance of all necessary codal formalities in hiring cases.

**Note:** The issue was also reported earlier in the Audit Reports for Audit Years 2019-20, 2021-22 2022-23 and 2023-24 vide para numbers 4.9.9, 8.3, 9.8 and 8.9 respectively having a financial impact of Rs 87.60 million. The recurrence of the same irregularity is a matter serious of concern.

[Annexure-78]

### **8.13 Non/short-deduction of house rent allowance/charges – Rs 8.60 million**

According to Rule 26 of the Accommodation Allocation Rules, 2002, unless entitled to rent free accommodation, the allottee of an accommodation is to be charged normal rent at the rate of 5% of the emoluments as defined in Rule

2(d) of the Rules ibid. Further according to Finance Division O.M. No. F-3(8)Gaz-IMP/73, dated 10<sup>th</sup> January, 1974, house rent allowance will be admissible subject to the condition that government accommodation has not been made available to the employee concerned.

It was observed during audit of the FYs 2022-23 and 2023-24 that FBR (HQ) and its sixteen (16) field offices, in one hundred and seventy-seven (177) cases neither deducted 5% house rent charges nor discontinued the house rent allowance of the officers/officials who were allotted Government accommodation or availed hired accommodation. The omission resulted in non-deduction of house rent allowance/charges amounting Rs 8.60 million due to internal controls lapses.

These irregularities were pointed out during February to November 2024. The management replied that the action regarding recovery had been initiated from the employees.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to recover the excess payment and get the stance verified from Audit. No further progress was reported till finalization of this report.

The Audit recommends expediting the recovery from the concerned officers/officials.

**Note:** The issue was also reported earlier in the Audit Reports for Audit Years 2019-20 and 2023-24 vide para numbers 4.9.15 and 8.17 respectively having a financial impact of Rs 7.04 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-79]

#### **8.14 Irregular payment on printing and publications – Rs 7.65 million**

According to S. No. (9)13 of the System of Financial Control & Budgeting 2006, the printing to certain items was required to be carried out from Government Printing press, However, printing at a press other than the Printing Corporation of Pakistan, should be undertaken only if the Principal Accounting Officer is satisfied that it is in public interest to do so and record a certificate to that effect. Moreover, NOC from Printing Corporation of Pakistan is also required to get the printing done from a private printer.

It was observed during audit of the FYs 2023-24 that twelve (12) field offices of FBR, in twelve (12) cases made payment on account of A03902-Printing and Publication without observing the government instructions. This resulted irregular payment on account of printing and publication amounting to Rs 7.65 million.

These irregularities were pointed out during February to October 2024. The management replied that printing of files and miscellaneous items was made from authorized vendor and was sanctioned by the controlling authority. The Audit holds that it is a clear violation of government instructions, therefore, department reply is not tenable.

The DAC in its meetings held in November, December, 2024 and January, 2025 directed the department to justify the stance with documentary evidence and get it verified from Audit. No further progress was reported till finalization of this report.

The Audit recommends implementation of DAC directives at the earliest besides regularization of the expenditure from competent authority.

**Note:** The issue was also reported earlier in the Audit Reports for Audit Years 2019-20, 2021-22 and 2023-24 vide para numbers 4.9.20, 8.13 and 8.15 respectively having a financial impact of Rs 7.98 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-80]

### **8.15 Irregular reimbursement of medical charges – Rs 5.61 million**

Finance Division (Regulation Wing), Islamabad vide O.M No. F.6 (1)R-10/2010-171-2011 dated 24.03.2011 has allowed reimbursement of amount spent on account of purchase of medicines for medical treatment at OPD by civil employees of the Federal Government or member of his/her family, suffering from chronic diseases as detail given in the O.M ibid. Re-imburement of medical charges for treatment taken from private hospital/clinic without an emergency or without referring by an authorized medical attendant is not allowed under the rules.

It was observed during audit of the FYs 2022-23 and 2023-24 that fourteen (14) field offices of FBR, in thirty-seven (37) cases made reimbursement of medical charges without fulfilling the codal formalities and basic requirements for re-imburement of medical claims. The claims were

sanctioned without proper prescriptions for the treatment from private hospital/clinic or without an emergency or without referral by the authorized medical attendant for medical treatment of non-chronic disease. This resulted in irregular payment of medical re-imburement charges amounting to Rs 5.61 million due to internal control lapses.

These irregularities were pointed out during February to November 2024. The management replied that the re-imburement of medical charges was sanctioned by the competent authority after compliance of codal requirements. The contention of the department is not tenable. Audit emphasizes to fulfil all the codal formalities or make recovery from officers/officials concerned.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department either to provide relevant documentary evidence or recover the amount pointed out by Audit. No further progress was reported till the finalization of this report.

Audit recommends recovery of inadmissible expenses on medical charges besides strengthening of internal controls to avoid recurrence of such lapses in future.

**Note:** The issue was also reported earlier in the Audit Reports for Audit years 2019-20, 2021-22 and 2023-24 vide para numbers 4.9.12, 8.5 and 8.14 respectively having a financial impact of Rs 18.88 million. The recurrence of the same irregularity is a matter of serious concern.

[Annexure-81]

**8.16 Excess payment of house rent allowance @ 45% instead of 30% - Rs 3.56 million**

According to Para 7 of the Basic Pay Scales 1987, all employees not provided with government accommodation are entitled to house rent allowance @ 45 % of the minimum of the basic pay scales at the specified stations whereas at all other stations, this allowance will be allowed @ 30 % of the minimum of basic pay scale.

It was observed during the audit of the FYs 2022-23 and 2023-24 that six (06) field offices of FBR, in one hundred and fifty-four (154) cases, made excess payment of house rent allowance @ 45% instead of 30% as admissible at non specified stations. This resulted in excess payment of house rent allowance of Rs 3.56 million.

These irregularities were pointed out during February to November 2024. The management replied that the action regarding recovery had been initiated from the employees.

The DAC in its meetings held in July, October, November, December, 2024 and January, 2025 directed the department to make recovery from officers/officials concerned and get it verified from Audit. No further progress was reported till the finalization of this report.

The Audit recommends expeditious recovery from the officers/officials concerned.

[Annexure-82]

## **CHAPTER-9      IMPACT AUDIT OF INCOME TAX CREDIT ALLOWED THROUGH INCREASE OF SHARE CAPITAL**



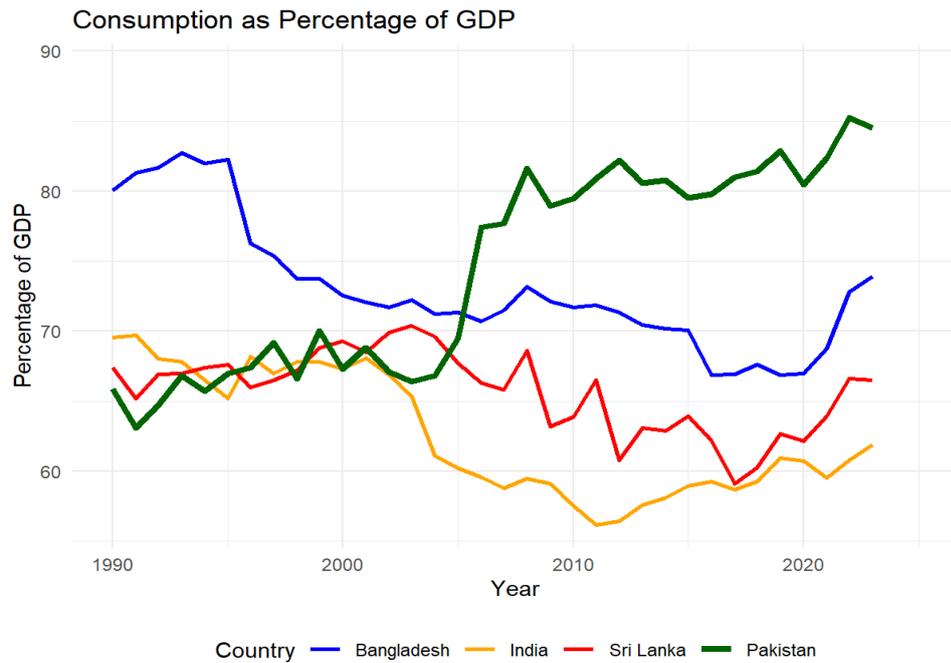
### **1.      INTRODUCTION**

#### **1.1      Background**

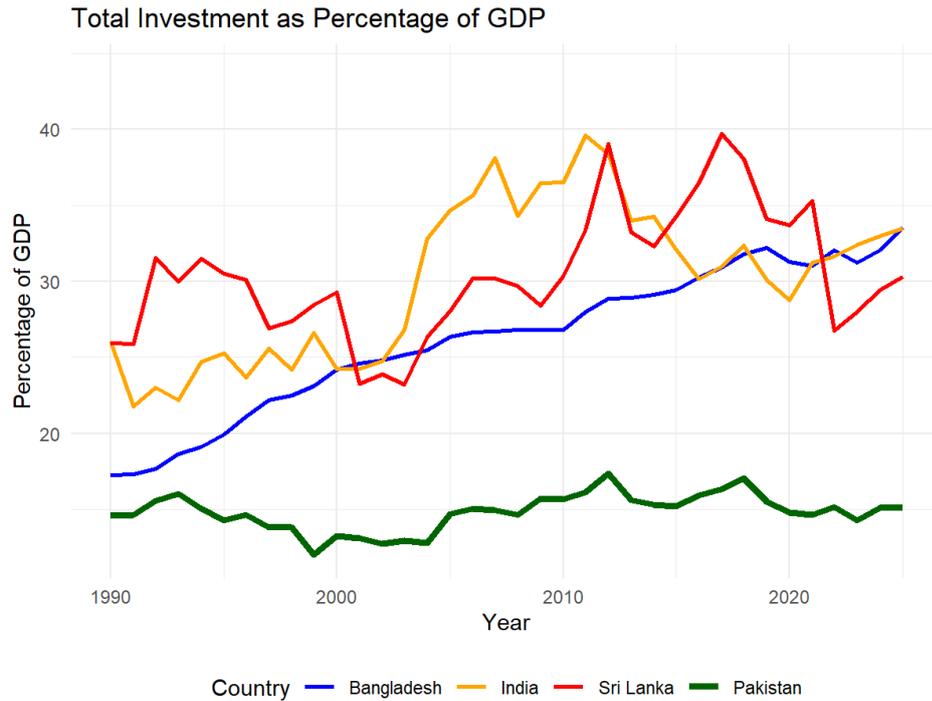
An impact audit is aimed at evaluation of the effectiveness of initiatives taken through different projects or programs by the government. Specifically, impact audit focuses on determining the outcomes directly attributable to an initiative defined as a new program or recent change to an existing program. It answers cause and effect questions about outcome results attributable to an initiative by separating other contributing factors or variables. The initiative that is the focus of this impact audit is Section 65E of the Income Tax Ordinance 2001, which was introduced through Finance Act, 2011 to promote industrial investments through the provision of tax credits. The aim of this audit is to evaluate the effectiveness of this initiative in achieving its intended goals by assessing the impact imputable to the tax credit policy on industrial investments and broader economic and business performance related indicators. This audit will also delve into the challenges and compliance issues pertaining to the implementation and utilization of this tax credit policy.

## 1.2 Role of Income Tax Credit allowed through Section 65E

Pakistan historically has a consumption oriented economy with low levels of investments compared to peer countries. This is evident in the graphs below, which show that Pakistan's consumption has been considerably higher, while total investment has been significantly lower than those of its peer countries. A consumption driven economy with profoundly low levels of investments leads to lack of accumulation of physical capital which tends to result in low labour productivity which in turn leads to weak income per capita growth rates. Hence, investments and capital formation play a profound role in economic growth and development.



**Figure 1. Source: Economist Intelligence Unit database**



**Figure 2. Source: IMF’s World Economic Outlook database**

To remedy this situation, several investment promoting policies have been devised by the state. One such policy initiative is Section 65E of the Income Tax Ordinance 2001, which was introduced through the Finance Act 2011. The section states that where a taxpayer being a company, setup in Pakistan before the first day of July, 2011, invests any amount, with “at least seventy per cent” new equity raised through issuance of new shares, in the purchase and installation of plant and machinery for an industrial undertaking, including corporate dairy farming, for:

(i) the purposes of expansion of the plant and machinery already installed therein, or

(ii) undertaking a new project, a tax credit shall be allowed against the tax payable for a period of five years beginning from the date of setting up or commencement of commercial production from the new plant or expansion project, whichever is later.

The *raison d'être* of this policy is to encourage industrial investment in Pakistan and promote economic growth by offering tax incentives to industrial undertakings that involve investments in expansion of existing plant and

machinery, and new projects. Such investments are expected to boost businesses productivity, create new jobs, and spur economic growth.

## **2. Overview**

Before the insertion of Section 65E through Finance Act 2011, there were four tax credit provisions under Section 65 of the Income Tax Ordinance 2001 namely, Section 65A (tax credit for sales to registered persons, introduced in 2005), Section 65B (tax credit for investment in plant and machinery, introduced in 2010), Section 65C (tax credit for companies enlisted in stock exchange, introduced in 2011) and Section 65D (tax credit for newly established industrial undertakings, introduced in 2011). Section 65A was eventually omitted by the Finance Act, 2017, Section 65C and Section 65D were omitted by the Finance Act, 2021. Hence, currently 65E along with 65B are the only two existing provisions under Section 65 which offer tax credits to promote industrial growth.

Section 65E was introduced in 2011 and later amended in 2016, to provide tax credits to existing industrial undertakings that sought to enhance their production capacities through balancing, modernization, and replacement (BMR) of machinery and equipment. Originally, it required taxpayers to raise 100% new equity through issuance of new shares for investing in plant and machinery and new projects. The amendment reduced the equity requirement to 70% of the value of investment making it more convenient for firms to avail the tax credit policy. It aimed to encourage the expansion and technological upgradation of existing businesses. The key features of Section 65E have been described in detail below:

### **i) Eligibility**

It applies to companies set up in Pakistan before the first day of July, 2011. The undertaking must make 70% equity investment from its own resources and shall not include loans obtained from shareholders or directors.

### **ii) Tax Credit**

A tax credit is allowed against the tax payable for a tax year as per a formula given in the section. The credit is available for a period of 5 years after the investment is made. As mentioned before the investment should either be for the purposes of expansion of the plant and machinery already installed therein, or for undertaking a new project. Furthermore, the investment should be in new plant and machinery and cannot include used or second-hand equipment.

### **iii) Time Frame**

The tax credit can be claimed for investments made if the plant and machinery is installed at any time between the first day of July, 2011 and the 30<sup>th</sup> day of June, 2021.

## **3. Scope and Methodology**

### **3.1 Scope**

This impact audit attempts to analyze the impact of Section 65E on business investments, business performance indicators, and relevant national economic indicators. For this purpose, Audit obtained income tax returns and audited accounts from the twelve field formations of the FBR *viz* LTOs Lahore, Islamabad, Multan & Karachi, RTOs Peshawar, Abbottabad, Faisalabad, Multan, CTOs Lahore, Islamabad, Karachi and MTO Karachi. The scope of period under audit was limited to six years i.e 2018 to 2023, keeping in view statutory restrictions upon FBR regarding powers to reopen the cases beyond a time period of six years. Therefore, the Audit did not evaluate data or claims for tax credits related to investments in plant and machinery prior to tax year 2018 including its evaluation of investments' trends at the firm level in the period before the implementation of the policy for comparison purposes. Nevertheless, data from Tax Years 2018 to 2023 were used to assess the co-relation between business performance and tax credit claims at the company level and national economic indicators whose data are publicly available in databases such as that of the World Bank and Pakistan Bureau of Statistics were used to evaluate the period before and after the implementation of Section 65E in order to gauge the impact of the tax credit policy upon the broader economy.

### **3.2 Audit Methodology**

The methodology primarily adopted is to analyze quantitative data obtained from FBR and its field formations, State Bank of Pakistan, Pakistan Bureau of Statistics, as well as international databases such as WEO of the IMF, WDI of the World Bank, and the Economist Intelligence Unit. Economic reports and other relevant documents from these sources have also been reviewed to develop a more comprehensive understanding of the issue. In order to obtain a deeper qualitative understanding of the outcomes of the tax credit policy, the Audit also prepared a questionnaire for the various Chambers of Commerce and Industries in Punjab, ICT, and KPK.

A number of audit techniques and analytical methods were utilized while undertaking this Impact Audit, which includes regression and trend analyses. These methods aimed to evaluate the impact of Section 65E upon the performance of industry and the national economy. Issues related to compliance and misuse of the tax credit policy were also assessed in this audit. The overall aim of the methodology along with some of the audit tools and data sources have been discussed below.

**a) Review of Tax Credit Policy Objectives**

Analysis of the extent to which the intended objectives of Section 65E have been achieved including intended economic impact on industrial investments and broader economic development.

**b) Compliance and Regulatory Oversight**

Review of compliance measures and the effectiveness of regulatory oversight in preventing misuse or over-claiming of credits under Section 65E.

**3.3 Data collection from primary and secondary sources**

The details of data collected from the studies' primary and secondary sources are as follows:

**a) Federal Board of Revenue (FBR)**

The FBR is the primary source for tax-related data in Pakistan. For analysis under Section 65E, it is important to gather detailed information regarding tax incentives, deductions, and exemptions that fall under this provision. Audit obtained tax related data from twelve field formations of the FBR namely LTO Lahore, Multan, Islamabad and Karachi, RTO Peshawar, Abbottabad, Faisalabad, Multan and CTO Lahore, Islamabad and Karachi and MTO Karachi.

The data collected includes:

- Tax filings and returns: Records of companies that availed tax credits under 65E.
- Tax credit amounts: The value of credits provided, categorized by industries and sectors.

- Investment figures: Data on investments made by companies in expansion or balancing, modernization, and replacement (BMR) projects that qualify for Section 65E.
- Sector-wise performance data: Focus on specific sectors that received incentives for growth or modernization.

**b) State Bank of Pakistan (SBP)**

The SBP provides vital macroeconomic and financial data that complements the fiscal insights from FBR. The data from SBP was gathered to help contextualize the effects of tax credits in terms of economic performance, investment trends, and sectoral growth. Data points of interest include:

- Macroeconomic data: National GDP growth rates, sectoral contributions to GDP, inflation trends, and investment inflows during 2018-2023.
- Credit and investment trends: SBP's data on credit availability to the private sector, particularly for industrial expansion and modernization, as well as trends in domestic and foreign direct investments.
- Financial stability reports: Insights into the financial health of industries benefiting from Section 65E, including sectoral growth reports, and overall economic resilience.

**c) Pakistan Bureau of Statistics (PBS)**

PBS provides comprehensive data on national and sectoral economic performance. The data from PBS helped in understanding the broader economic impact of Section 65E, such as its effect on industrial production, employment, and investment in various sectors. The data points include:

- Investment trends: National and sector-wise investment trends over the past five years, with a focus on the manufacturing and industrial sectors.
- Industrial output and growth rates: Data on production indices, large-scale manufacturing (LSM), and sector-specific growth that is directly linked to industries benefitting from the tax credits.

**d) Chambers of Commerce and Industry**

Audit had circulated a comprehensive questionnaire to various chambers of commerce and industry across the country. The aim was to gather valuable

insights, feedback, and comments from the actual beneficiaries of the tax credit policy regarding the practical implications, and any benefits/shortcomings associated with this provision. However, despite follow-ups, Audit was unable to obtain any substantive response from these chambers with the exception of Gujranwala Chamber of Commerce & Industries (GCCCI).

#### **4. Findings**

##### **4.1 Positive correlation of tax credit claims with business performance indicators**

The findings of this study reveal a positive correlation between tax credit claims and key business indicators, including investments, sales, and net profits. This suggests that businesses claiming higher tax credits under Section 65E tend to achieve greater levels of investments, larger turnovers, and higher profits. In other words, larger tax credit claims are associated with better business performance. However, audit could only analyse and process data for trend analysis upto five years as FBR did not provide any data beyond five years owing to operational and legal limitations regarding opening any case of a taxpayer outside the said time limit.

##### **4.1.1 Increased capital investment on plant and machinery**

Since tax credit under Section 65E can only be claimed after an increase in investment through 70% equity, the analysis of the financial statements of companies which availed the tax credit policy depicts a marked increase in capital investments. This is particularly evident in sectors like construction, manufacturing, beverages and steel. The quantum of investments for thirteen companies with the largest investments in ICT, Punjab, Sindh and KPK has been shown below:

(Rs in millions)

<b>S. No.</b>	<b>Taxpayer name</b>	<b>Amount of capital invested from 2018 to 2023</b>
1	M/s. Unity Foods Limited	27,322
2	Izhar Construction (Pvt.) limited	10,250
3	Pak Elektron Limited	9,010
4	Mughal Iron and Steel Industries Limited	3,356
5	Izhar Engineering (private) Limited	2,200

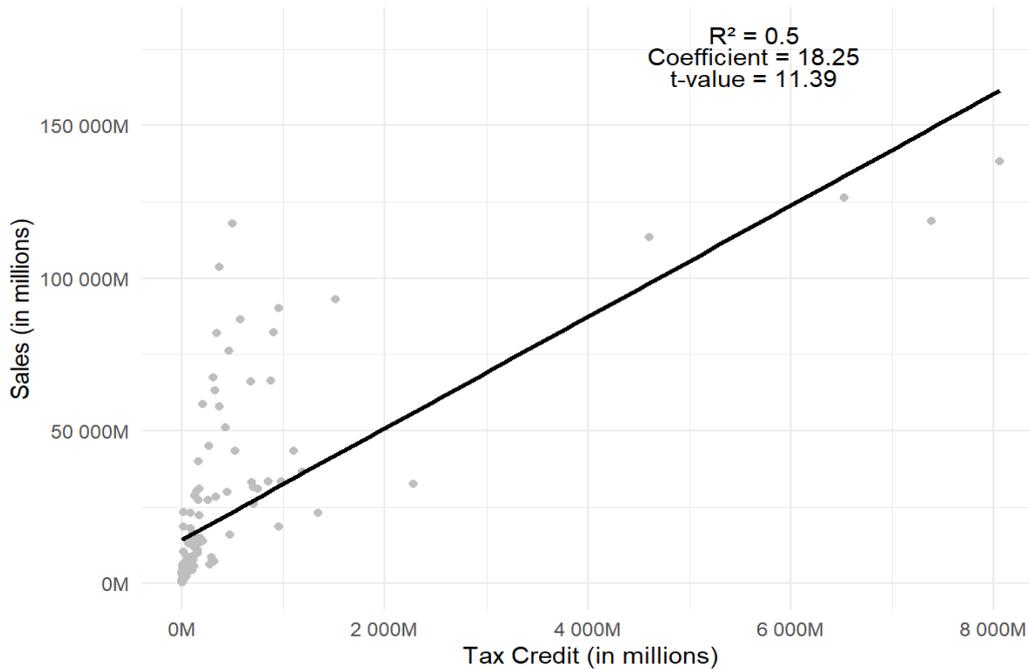
6	Pepsi-Cola International (Private) Limited	2,153
7	Agro Processors & Atmospheric Gases Ltd	1,700
8	A. T. S. Synthetic (Private) Limited	1,455
9	Roshan Packages Limited	1,419
10	Brighto Paint (Private) Limited	1,276
11	Dairyland (Pvt) Limited	1,236
12	Synthetic Products Enterprises Limited	943
13	Sika Pakistan (Private) Limited	825

Companies taking advantages of this provision are enhancing/upgrading their production capacities, potentially leading to improved productivity, efficiency, and job creation. Below, an analysis has been done to assess whether increased investments and corresponding tax credit claims are correlated with improved company performance.

#### **4.1.2 Positive correlation of sales with tax credit claims**

Sales for companies availing the tax credit have generally shown positive growth in the five years' period from 2018 to 2023. In order to assess the relationship between sales and the tax credit claimed under Section 65E, a bi-variate regression with sales as the dependent variable and the amount of tax credits claimed under Section 65E as the independent variable has been run using panel data of taxpayers who availed the tax credit policy from LTOs Lahore & Karachi and who represent nearly 97% of the total tax credit claims in ICT, Punjab, Sindh and KPK for the period ranging from 2018 to 2023.

Regression of Sales against Tax Credit Claimed Under Section 65E  
LTO Lahore & LTO Karachi (2018 – 2023)

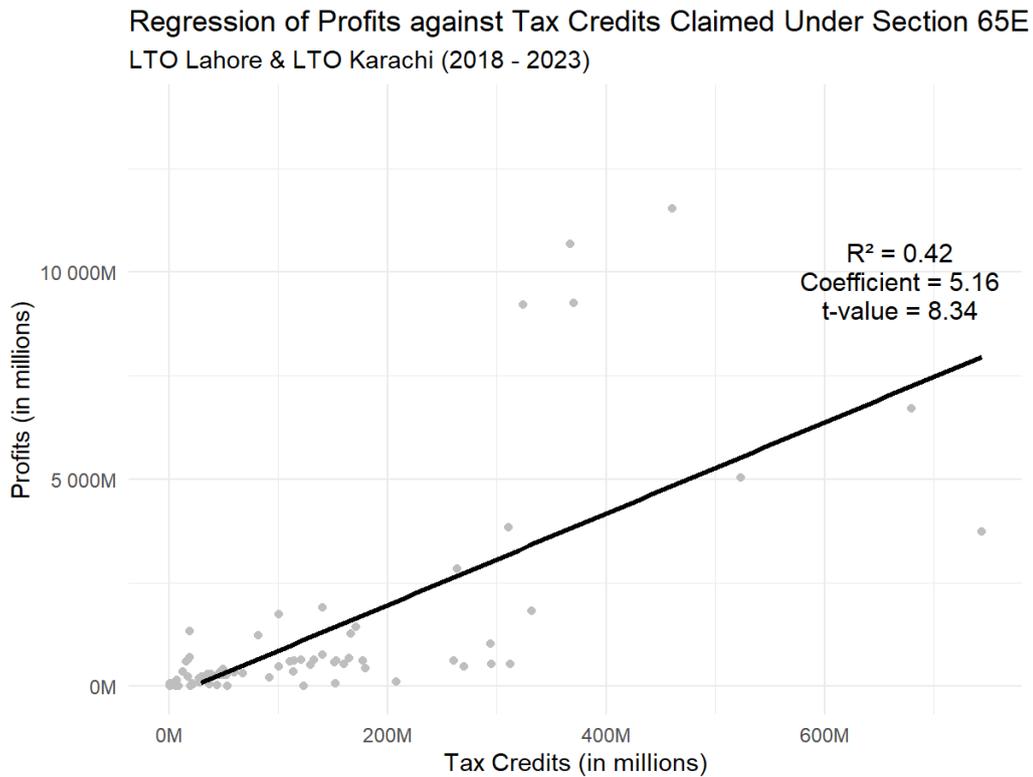


As the regression results show there exists a practically and statistically significant relationship between company sales/turnover and the tax credits claimed under 65E. The outcome of the regression shows that, *ceteris paribus*, one unit increase in tax credits claimed is correlated with a 18.25 units corresponding increase in sales. Since the t-value at 11.39 is well above 2.58, the coefficient is statistically significant at a 1% significance level.

The increase in sales can potentially be due to improved production capacity and product quality resulting from additional investment. That being said, the regression analysis above depicts correlation and not necessarily causation and other omitted variables could potentially be affecting company sales. More complex models to tease out causal links required more data which was either not shared by FBR or was not available. Nevertheless, a statistically significant and positive relation between sales and tax credits under Section 65E does exist, with companies making more tax credit claims experiencing larger sales as well on average.

### 4.1.3 Positive correlation of profit margins with tax credit claims

Companies benefiting from tax credits under section 65E have reported improved profit margins in their financial statements. To analyze the relationship between profits and the tax credit policy a similar regression to the one above has been run by using firm level data from LTO Lahore and LTO Karachi with profits as the dependent variable and the amount of tax credit claims under section 65E as the independent variable.



The regression results show that, similar to sales, there exists a practically and statistically significant relationship between company profits and the amount tax credits that they claimed under section 65E. This indicates that on an average, companies which have greater tax credit claims also tend to have larger profits. The outcome of the regression shows that a unit increase in tax credits claimed is correlated with a 5.16 increase in profits. Since the t-value is greater than 2.58 the coefficient is statistically significant at the 1% level.

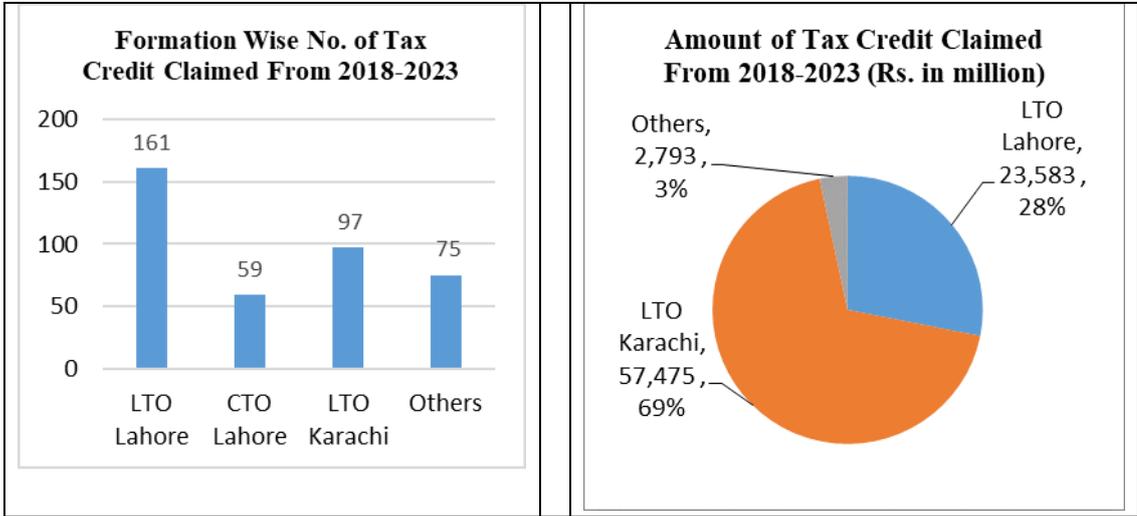
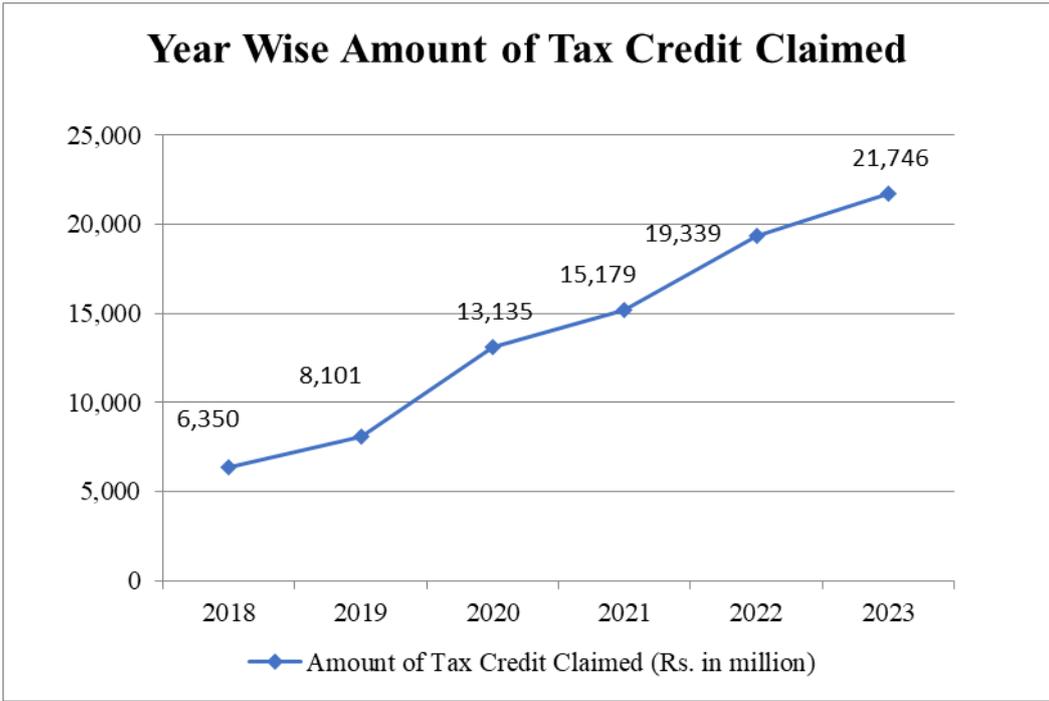
#### 4.2 Extremely low utilization of the tax credit policy by industries

Audit obtained data regarding claims of tax credits under Section 65E by taxpayers which were being assessed in the following field formation of FBR.

*(Rs in million)*

Sr. No.	Formation	Year of tax credit claims	No. of claims	No. of taxpayers involved	Amount of tax credit u/s 65E claimed
1	LTO Karachi	2018-2023	97	33	57,475.44
2	LTO Lahore	2018-2023	161	41	23,582.61
3	RTO Peshawar	2018-2022	06	02	1,222.40
4	RTO Abbottabad	2018-2023	15	04	782.40
5	CTO Lahore	2018-2023	59	28	464.07
6	LTO Multan	2018-2023	19	07	170.42
7	MTO Karachi	2018-2023	09	04	58.56
8	RTO Faisalabad	2018-2019	02	02	41.15
9	CTO Karachi	2018-2023	13	09	28.93
10	LTO Islamabad	2018-2022	04	02	18.17
11	CTO Islamabad	2019-2022	05	05	6.04
12	RTO Multan	2020-2021	02	02	0.46
<b>Total</b>			<b>392</b>	<b>139</b>	<b>83,850.64</b>

As shown in the above analysis, only 139 taxpayers availed this policy during the period ranging from 2018-2023. This shows that out of the hundreds of thousands of taxpaying businesses spread across the country, only an exceedingly minute portion availed this policy. This raises the issue of why majority of taxpayers have not taken steps to potentially benefit from this policy.

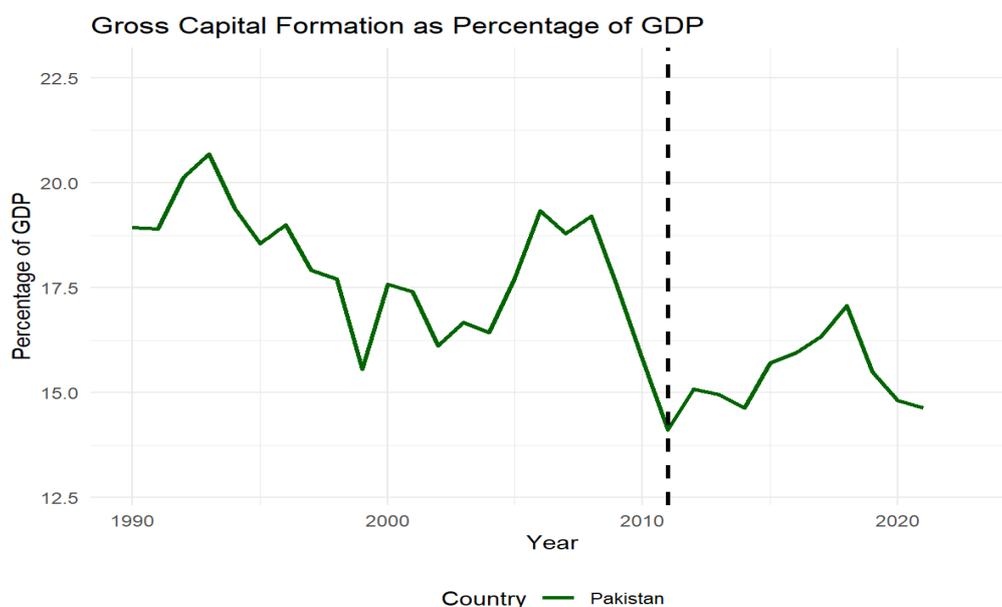


As evident from the charts above, the total instances of tax credits claims are just 392, with 161 of those claims being made by taxpayers from LTO Lahore. The quantum of total tax credits claimed is also quite moderate which indicates the limited impact of the policy, with 69% of all claims in rupee terms being made by taxpayers from LTO Karachi. It was observed that there was no mechanism adopted by FBR for periodic reviews and

assessment of incentives availed, under Section 65E, by the concerned taxpayers and relevant stakeholders for analysing the efficacy of the scheme.

### 4.3 No major impact upon national economic indicators

As mentioned previously the utilization of the tax credit policy by the business community is extremely low. This low utilization is in keeping with the changes in relevant national economic indicators, such as gross capital formation, investment as a percentage of GDP, and industrial growth, all of which have exhibited extremely low levels of growth in recent years. Hence, the tax credit policy does not seem to have had any major impact in terms of bringing any major improvements in the national economy.



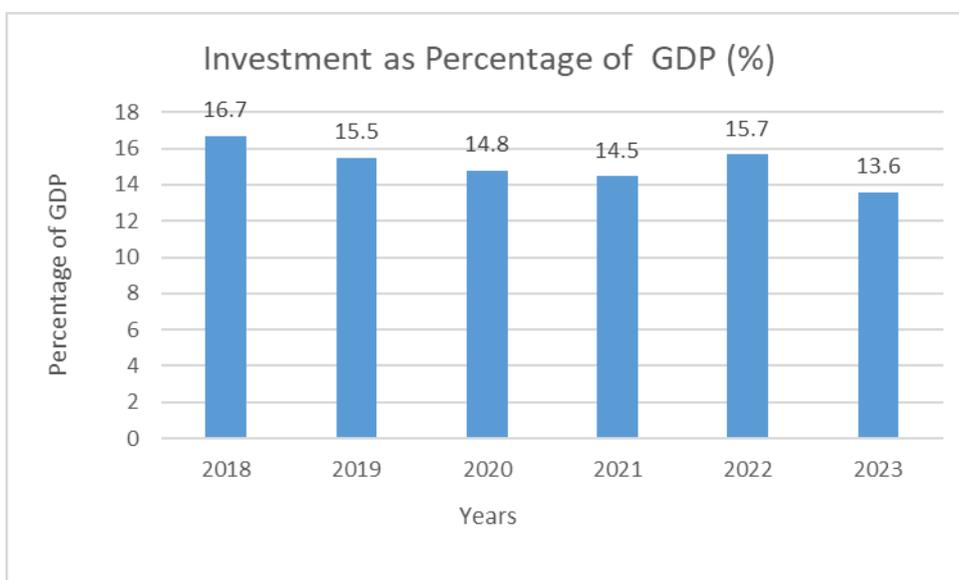
**Figure 3. Source: World Development Indicators data**

The graph above, using data from the World Bank’s World Development Indicators database, shows the Gross Capital Formation as a percentage of GDP in Pakistan since 1990. Gross Capital Formation consists of the addition in inventories and fixed assets in the country, which includes, inter alia, addition in plants, machinery, equipment, and building construction. The dotted line in the graph represents the time at which the tax credit policy came into force i.e. 2011.

Since section 65E incentivizes investments leading to increase in capital formation we should ideally see a rapid rise in this indicator after the implementation of the tax credit policy.

The graph above clearly depicts that although Gross Capital Formation as a percentage of GDP increased after 2011, it eventually started declining around 2018. The graph does increase with a lag and then falls in Covid years. Moreover, the increase was not large enough to bring it to levels seen before the implementation of the policy. Hence, growth in this indicator has been moderate and its recent decline has resulted in low levels of additional capital formation.

Looking at investment levels as a percentage of GDP in the last six years also reveals a similar situation. As the bar chart below shows investment levels have seen a downward trend since 2018 representing the limited impact the tax credit policy has had on spurring investments in recent years.



The table below shows that overall GDP and industrial growth have also not seen any major growth barring a few years and have even experienced negative growth. Hence, it can be stated that the tax credit policy has not coincided with rapid changes in national economic indicators.

Year	GDP Growth Rate (%)	Industrial Growth (%)
2018	6.1	4.6
2019	3.1	0.2
2020	- 0.9	-5.7
2021	5.7	8.2
2022	6.0	6.8
2023	0.3	-2.9

Source: State Bank of Pakistan Annual Reports

#### 4.4 Tax credit claimed after stipulated timeline

The taxpayers cannot claim a tax credit under Section 65E of the Income Tax Ordinance 2001, if the stipulated timeline for registration up to June 30, 2011, was not adhered to. Furthermore, the plant and machinery must have been installed between first day of July, 2011 and the 30<sup>th</sup> day of June, 2021 to qualify for tax credit. The tax credit under this section can only be availed for a period of five years, commencing from the date of setting up or the start of commercial production from the new plant or expansion project, whichever occurs later. However, it was observed that tax credit was claimed after stipulated timeline and also allowed in many instances by the FBR which is in contravention to the basic stipulation stated in the tax credit policy under Section 65E. In the following paras, taxpayers have not adhered to these conditions.

##### 4.4.1 Claim of tax credit after due date of registration - Rs 3,882.61 million

According to Section 65E of the Income Tax Ordinance 2001, tax credit is restricted to such taxpayers who got registered before first day of July 2011.

In few cases, Audit analyzed that the following taxpayers who got registered after 1<sup>st</sup> day of July 2011 and claimed irregular tax credit under Section 65E for an amount of Rs 3,881.61 million.

(Rs in million)

Name of Taxpayer	Name of Formation	Registered on	Tax year of credit claim	Amount of Tax credit claimed	DP/ Observation No
M/s National Power Parks Management Company Private Limited	LTO Lahore	July,2015	2019 2020 2021 2022	1,387.72 2,184.97 35.38 62.68	23585

M/s TCL Electronics Pakistan Pvt Ltd	LTO Lahore	May, 2013	2023	100.35	23259
M/s Relaxo Pvt Ltd	LTO Lahore	Sep, 2012	2018	26.84	23248
M/s Akbari Chemicals Industries Pvt Ltd	LTO Lahore	April,2014	2018	1.07	23248
M/s GE Healthcare Pakistan Pvt Ltd	CTO Lahore	May, 2019	2020	0.26	23656
M/s Izhar Pavers Pvt ltd	CTO Lahore	Nov, 2020	2021 2022 2023	0.65 8.66 25.00	23656
M/s Livewell Capsules Pvt Ltd	CTO Lahore	Dec,2017	2022 2023	0.01 0.34	23656
M/s Million Classic Cables Pvt Ltd	CTO Lahore	Mar,2017	2019	0.67	23656
M/s Cresset Strategic Partners Pvt Ltd	CTO Lahore	Feb,2019	2022	0.45	23664
M/s Byonyks Pvt Ltd	CTO Lahore	Dec,2017	2022	3.52	23664
M/s Moh's Tech Pvt Ltd	CTO Lahore	Oct,2020	2022	0.09	23664
M/s Polyplas Pvt Ltd	CTO Lahore	June,2014	2022	2.48	23656
M/s Pakistan Coating Chemicals Pvt Ltd	CTO Lahore	Sep,2015	2019	0.70	23657
M/s Bahawalpur Steel Mills Pvt Ltd	LTO Multan	Feb, 2014	2022 2023	7.97 10.54	23393
M/s Fahad Shahid Flour & General Mills Pvt Ltd	LTO Multan	Nov, 2013	2019	2.41	23393
M/s Waqas Fahad Flour & General Mills Pvt Ltd	LTO Multan	Nov, 2013	2020	5.90	23393
M/S.Bandhi Sugar Mills (Pvt) Ltd	LTO, Karachi	Jan,2012	2018	1.51	9
M/S. Seahawks Asia Global (Pvt) Ltd	CTO, Karachi	June, 2017	2018	0.10	10
M/s. Sunridge Foods (Private) Limited	MTO, Karachi	April,2015	2021	5.41	11
M/s. BNB Enterprises (Private) Ltd	CTO, Karachi	Feb,2018	2018	0.05	12
M/s. Glowell Industries (Private) Ltd	CTO, Karachi	June,2021	2023	0.09	13
M/s.I Tecknologi (Private) Ltd	CTO, Karachi	July,2017	2018	0.89	14
M/s. Tecno Auto Glass Ltd	CTO, Karachi	Mar,2017	2021	4.90	15
<b>Total</b>				<b>3,881.61</b>	

The government has potentially lost revenue due to these ineligible claims. The incorrect claims result in a reduction in tax liabilities of the taxpayers who are not entitled to the credit, impacting overall tax collections.

The lapse was pointed out from July to November, 2024. The field formations replied that an amount of Rs 0.26 million had been charged and recovery was awaited in one case, however, legal proceedings were initiated in remaining cases. The department was requested to finalize the cases as per law.

The DAC, in its meetings held in November, December 2024 and January, 2025 directed the department to recover the admitted amount, expedite legal proceedings and report compliance to Audit/FBR. However, DAC in respect of CTO Karachi, MTO & LTO Karachi could not be convened. No further progress was reported till the finalization of this report.

#### **4.4.2 Claim of tax credit beyond stipulated period of five years - Rs 2,461.47 million**

According to Section 65E of the Income Tax Ordinance 2001, tax credit is admissible to taxpayers against the tax payable for a period of five years beginning from the date of setting up or commencement of commercial production from the new plant or expansion project, whichever is later.

In the following cases, it was revealed that taxpayers invested in the plant and machinery and claimed tax credit beyond five years without raising any new equity shares.

*(Rs in million)*

<b>Name of Taxpayer</b>	<b>Name of Formation</b>	<b>Year in which wrong tax credit claimed (beyond five years)</b>	<b>Amount</b>	<b>DP/ Observation No</b>
M/s Next Pharmaceutical Products Pvt Ltd	CTO Lahore	2023	3.20	23658
M/s Pepsi Cola International Pvt Ltd	LTO Lahore	2023	370.24	23239
M/s. Procter & Gamble Pakistan (Pvt) Ltd	LTO, Karachi	2023	426.00	01
M/s. Bulk Management Pvt Ltd	LTO, Karachi	2023	125.79	02
M/s. Unity Foods Ltd	LTO, Karachi	2023	950.00	03
M/s. Dalda Foods Ltd	LTO, Karachi	2023	586.23	04
<b>Total</b>			<b>2,461.47</b>	

The government has potentially lost revenue due to these ineligible claims. The incorrect claims resulted in reduction in tax liabilities for the taxpayers who were not entitled to the tax credits, impacting overall tax collections.

The lapse was pointed out from July to November, 2024. The field formations replied that the cases were still under consideration of the tax authorities. The department was requested to finalize the cases as per law.

The DAC, in its meetings held in November 2024 and January 2025, directed the department to expedite legal proceedings and report compliance to Audit/FBR. However, DAC in respect of LTO Karachi could not be convened. No further progress was reported till the finalization of this report.

#### **4.4.3 Increase in share capital after prescribed time period – Rs 1,402.65 million**

According to Section 65E of the Income Tax Ordinance 2001, tax credit can be claimed for investments made in the plant and machinery and installed at any time between the first day of July, 2011 and the 30<sup>th</sup> day of June, 2021 through the new equity raised by the issuance of new shares (at least seventy percent).

Audit analyzed that following taxpayers have increased their share capital by issuing new shares to invest in plant and machinery during tax year 2022 and 2023 and claimed tax credit under Section 65E which is inadmissible as the plant and machinery was required to be installed at any time between the first day of July, 2011 and the 30th day of June, 2021.

*(Rs in millions)*

<b>Name of Taxpayer</b>	<b>Name of Formation</b>	<b>Tax year in which equity raised</b>	<b>Amount of Tax credit claimed u/s 65E</b>	<b>DP / Observation No.</b>
M/S Mughal Iron and Steel Industries Ltd	LTO Lahore	2022	679.76	23259
M/S Izhar Engineering Pvt Ltd	LTO Lahore	2023	110.92	23259
M/s Izhar Construction Pvt Ltd	LTO Lahore	2023	295.21	23241
M/s. Habib Oil Mills Pvt Ltd	LTO, Karachi	2022	93.64	05
M/S. Power Cement Ltd	LTO, Karachi	2022	223.12	06
<b>Total</b>			<b>1,402.65</b>	

The wrongful claim of the tax credit reduces the tax liability of taxpayers, resulting in a direct loss of tax revenue for the Government.

The lapse was pointed out from July to November, 2024. The field formations replied that the cases were still under consideration of the tax authorities. The Department was requested to finalize the cases as per law.

The DAC, in its meeting held in November and December, 2024, directed the department to expedite legal proceedings and report compliance to Audit/FBR within 30 days. However, DAC in respect of LTO Karachi could not be convened. No further progress was reported till the finalization of this report.

#### **4.5 Claim of tax credit without fulfilling requirements**

According to Section 65E of the Income Tax Ordinance 2001, taxpayers cannot claim a tax credit if no actual investment has been made in the purchase of plant and machinery, even if they have raised equity shares, or if they attempt to claim the tax credit without raising new equity shares as required. Further, in a number of cases department neither verified the installation of machinery nor ensured the submission of audited accounts by the taxpayers as highlighted by the audit in the following paras.

##### **4.5.1 Failure to verify installation of machinery – Rs 727.32 million**

According to Section 65E of the Income Tax Ordinance 2001, the taxpayers can claim tax credit only where the actual investment has been made on the purchase of plant and machinery and the department is required to verify the installation of plant and machinery before grant of tax credit.

The Audit highlighted the lack of monitoring regarding the installation and operationalization of machinery for which the tax credit had been claimed. The department neither conducted physical inspections nor required documentary evidence in the following cases to confirm whether the machinery had been installed and is contributing to production as required under the law.

(Rs in millions)

Name of Taxpayer	Name of Formation	Tax Year	Tax Credit claimed	DP No
M/s Ahmad Brothers Materials Pvt Ltd	CTO Lahore	2021	0.06	23660
		2023	29.51	
M/s Pharmasol Pvt Ltd	CTO Lahore	2019	1.35	23657
		2020	7.57	
		2021	12.62	
		2022	8.38	
		2023	82.20	
M/s Azhar Corporation Pvt Ltd	LTO Multan	2018	36.78	23393
M/S Aisha Steel Mills Ltd	LTO Karachi	2023	236.64	PDP-3391-IT-K
M/S Amreli Steels Ltd	LTO Karachi	2023	312.21	PDP-3391-IT-K
<b>Total</b>			<b>727.32</b>	

This weak monitoring opens up the possibility for taxpayers to claim tax credits without actually installing or utilizing the machinery. The taxpayers may claim the credit for machinery that is either non-existent or irrelevant to their manufacturing operations. The failure to monitor installations can also lead to inefficiencies, as the incentive does not drive the intended economic benefits of increased industrial output.

The lapse was pointed out from July to November, 2024. The field formations replied that the cases were still under consideration of the tax authorities. The Department was requested to finalize the cases as per law.

The DAC, in its meetings held in December 2024 and January 2025, directed the department to expedite legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

#### **4.5.2 Claim of tax credit without raising new equity shares – Rs 475.22 million**

According to Section 65E of the Income Tax Ordinance, 2001, in order to claim tax credit, it is necessary for the taxpayers to raise their equity through issuance of new shares (at least seventy percent).

Audit analyzed that following taxpayers have claimed tax credit under Section 65E without raising their share capital through issuance of new shares

which resulted in irregular claim of tax credits amounting to Rs 475 million as detail given below:

(Rs in millions)

Name of Taxpayer	Name of Formation	Equity raised from tax year 2017 to 2022	Tax Year in which tax credit claimed	Amount of Tax credit claimed	DP/ Observation No.
M/s Pak Elektron Ltd	LTO Lahore	Nil	2022	129.12	23259
M/s Kualitatem Pvt Ltd	CTO Lahore	Nil	2022	1.90	23657
M/s Pulcra Chemicals Pakistan Pvt Ltd	CTO Lahore	Nil	2018 & 2019	26.64	23657
M/s Vision Engineering Pvt Ltd	CTO Lahore	Nil	2022	2.01	23657
M/s Sinco Steel re-rolling Mills Pvt Ltd	LTO Multan	Nil	2018 2019 2020	11.89 7.87 5.48	23393
M/s Fazal Paper Mills Pvt Ltd	LTO Multan	Nil	2019	8.46	23393
M/s. Amreli Steels Ltd	LTO Karachi	Nil	2019 to 2022	281.87	07
<b>Total</b>				<b>475.22</b>	

The above table shows that taxpayers claimed tax credit incorrectly as new equity was not raised per law. It undermines the integrity of tax regulations and creates an environment where taxpayers might feel encouraged to manipulate tax provisions for financial gain.

The lapse was pointed out from July to November, 2024. The field formations replied that the cases of Rs 8.46 million were subjudice, whereas, remaining cases were still under consideration of the tax authorities. The Department was requested to finalize the cases as per law.

The DAC, in its meetings held in November and December 2024 and January 2025, directed the department to expedite legal proceedings and report compliance to Audit/FBR. However, DAC in respect of LTO Karachi could not be convened. No further progress was reported till the finalization of this report.

#### **4.5.3 Claim of tax credit without investment in plant and machinery - Rs 379.75 million**

As per Section 65E of the Income Tax Ordinance 2001, in order to claim tax credit, it is mandatory for the taxpayers to invest in plant and machinery and raise their share capital through issuance of new shares.

Audit analyzed that following taxpayers raised their equity through issuance of new shares but no investment is made in the plant and machinery as envisaged in the depreciation chart of their tax returns for the relevant tax years and irregularly claimed tax credit amounting to Rs 379.75 million as per detail given below:

*(Rs in million)*

Name of Taxpayer	Name of Formation	Tax Year in which Equity raised to invest in plant and machinery	Tax Year in which no addition in plant and machinery was made	Amount of Tax credit claimed u/s 65E	DP/ AO No.
M/s Mughal Iron And Steel Industries Ltd	LTO Lahore	2021	2021	263.42	23259
M/s Izhar Engineering (Private) Ltd	LTO Lahore	2021	2021	100.75	23259
M/s Agro Processors & Atmospheric Gases Ltd	LTO Karachi	2021	2021	15.58	08
<b>Total</b>				<b>379.75</b>	

Section 65E was introduced to encourage capital investment in plant and machinery to promote industrial growth. Wrongful claims undermine the purpose of the incentive, reducing the policy's effectiveness in stimulating economic activity.

The lapse was pointed out from July to November, 2024. The field formations replied that the cases were still under consideration of the tax authorities. The Department was requested to finalize the cases as per law.

The DAC, in its meetings held in November 2024, directed the department to expedite legal proceedings and report compliance to Audit/FBR within 30 days. However, DAC in respect of LTO Karachi could not be convened. No further progress was reported till the finalization of this report.

#### **4.5.4 Claim of tax credit without submission of audited accounts – Rs 23.18 million**

As per provisions of Section 65E of the Income Tax Ordinance 2001, in order to claim tax credit the submission of audited accounts is mandatory for the claimants.

The audit reveals that the tax department has not established an effective mechanism for monitoring and verification of tax credit claims of taxpayers. There is no systematic process to assess whether the taxpayers who claim the tax credit for investment in plant and machinery have submitted audited accounts along with tax returns and also fulfilled all stipulated conditions as per law.

*(Rs in millions)*

Name of Taxpayer	Name of Formation	Tax Year	Tax Credit claimed	DP No	Departmental Reply
M/s Unique Tanning Industries Pvt Ltd	CTO Lahore	2018	1.29	23662	Under Process
		2019	0.04		
		2021	0.12		
M/s Fazal Paper Mills Pvt Ltd	LTO Multan	2020	13.13	23393	T/Y 2020
		2021	6.60		Subjudice T/Y
		2022	0.65		2021 to 2023
		2023	1.35		Under process
<b>Total</b>			<b>23.18</b>		

Without proper verification, there is risk that taxpayers may overstate their investments or claim the tax credit without actually meeting the eligibility criteria. This undermines the effectiveness of the tax incentive, leading to potential revenue loss to national exchequer due to fraudulent or exaggerated claims.

The lapse was pointed out from July to November 2024. The LTO Multan replied that tax year 2020 was subjudice and tax years 2021 to 2023 were under process for finalization of legal proceedings. CTO Lahore replied the case was still under consideration. The department was requested to finalize the cases as per law.

The DAC, in its meetings held in December 2024 and January 2025, directed the department to expedite legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

#### **4.6 Incorrect tax credit claims and decreased sales**

The intention of the government while introducing tax credit policy under section 65E was to stimulate the growth by boosting industrial production and

consequent increase in sales. However, during the course of audit, it was noted that there were cases in which the tax credit was claimed despite a decrease in sales and even sometimes before the start of commercial production. In the following paras, either the taxpayers had wrongly claimed tax credit of section 65 E on the trial production basis or claimed tax credit by the negligence of the department.

#### **4.6.1 Unjustified/wrong tax credit claimed – Rs 882.20 million**

According to the provisions of Section 65E of the Income Tax Ordinance 2001, viz a viz other conditions tax credit is admissible to newly established undertaking on installation of plant and machinery.

It was observed during the audit of M/s Lipton Pakistan Limited having NTN (A072912) that the taxpayer had claimed tax credit amounting to Rs 882.20 million under Section 65E of the Income Tax Ordinance 2001. Further scrutiny of the tax record revealed that taxpayer was not a new establishment, as it had already an existing business previously owned by M/s Unilever Pakistan Limited (i.e. Unilever Tea Pakistan “Brand name Lipton Tea”) and sold out during the tax year 2023. Audit is of the view that tax credit under Section 65E is admissible only against the investment of new purchase and installation of plant and machinery during the period from 1<sup>st</sup> July, 2011 to 30<sup>th</sup> June, 2021. Hence, M/s Lipton Pakistan is an existing business not a new establishment. Therefore, tax credit u/s 65E was not admissible to the taxpayer as per existing provisions of law. The department did not initiate any legal proceeding to rectify the same, instead of accepting the taxpayer version. This resulted in loss of revenue amounting to Rs 882.20 million for the tax year 2023.

The lapse was pointed out from July to November, 2024. The field formation replied that the case was still under consideration of the tax authority. The Department was requested to finalize the cases as per law.

The DAC, in its meeting held in December 2024, directed the department to expedite the legal proceedings as per law under intimation to Audit/FBR within 30 days. No further progress was reported till the finalization of this report.

[DP No.3140-IT-K]

#### **4.6.2 Claim of tax credit before commencement of commercial production - Rs 1.34 million**

According to Section 65E of the Income Tax Ordinance 2001, tax credit is admissible to the taxpayer against the tax payable for a period of five years beginning from the date of setting up of industrial undertaking or commencement of commercial production from the new plant or expansion project, whichever is later.

It was observed during the audit of CTO Lahore, that a taxpayer had not started the commercial production for the tax year 2019, who had claimed tax credit of Rs 1.34 million as the entire sales were made from trial production which is clearly evident from the audited accounts. Without proper verification, there is risk that taxpayers may overstate their investments or claim the tax credit without actually meeting the eligibility criteria. This undermines the effectiveness of the tax incentive, leading to potential revenue loss to national exchequer due to fraudulent or exaggerated claims. Department replied that Order u/s 122 (5A) of the Income Tax Ordinance, 2001 was passed on 27.2.2021 and subsequently annulled by CIR(A) with the remarks to give another opportunity of being heard to the taxpayer. Audit is of the view that issue of 65E was not discussed in the assessment order passed u/s 122(5A).

The lapse was pointed out from July to November, 2024. The field formations replied that the cases were still under consideration of the tax authorities. The Department was requested to finalize the cases as per law.

The DAC, in its meeting held in January 2025, directed the department to report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

[DP No. 23661-IT]

#### **4.6.3 Decreased sales after availing tax credit**

A regression analysis of the tax credit scheme under section 65E clearly depicted that one unit increase in tax credits claimed under subject scheme is correlated with 18.25 units corresponding increase in sales.

Contrary to the above general trend, Audit observed that M/s Bahoo Engineering Pvt Ltd assessed in CTO Lahore availed the tax credit of Rs 1.49 million from tax year 2018 to 2019 but shown negative growth in sales following the investment in new machinery. In the tax year 2018 taxpayer declared sales of Rs 87.42 million, Rs 31.87 million in tax year 2019 and zero sales in the tax year

2020. Further, taxpayer was declared blacklisted in sales tax w.e.f 18.07.2023 on FBR portal.

There is a risk that businesses may be claiming the 65E tax credit without ensuring that investments are well-targeted for business growth, leading to a misallocation of public resources meant for economic stimulation. The department replied that the legal proceedings had been initiated.

The lapse was pointed out from in November, 2024. The field formation replied that the case was still under consideration of the tax authorities. The department was requested to finalize the cases as per law.

The DAC, in its meeting held in January, 2025 directed the department to finalize the legal proceedings and report progress to Audit/FBR. No further progress was reported till the finalization of this report.

[DP No. 23659-IT]

#### **4.6.4 Wrong claim of tax credit and non-pursuance of case before CIR (A)**

According to Section 122(5A) read with Section 65E of the Income Tax Ordinance, 2001 the Commissioner may amend or further amend an assessment order, if he considers that the assessment order is erroneous in so far it is prejudicial to the interest of revenue.

During the audit of CTO, Lahore, it was observed that M/s Sharif Oxygen (Pvt) Ltd. claimed tax credit of Rs 116.68 million during the tax years 2018, 2019, 2021 and 2022. The taxation officer passed orders u/s 122(5A) in the instant case for the tax years 2018 and 2022, but the CIR(A) annulled the demand in 2018 on the ground that no departmental representative was present during proceedings. In tax year 2022, the CIR(A) directed to re-visit the case as the assessing officer did not provide concrete evidence to reject the tax credit. Audit is of the view that due to departmental negligence and non-pursuance of the case before CIR(A), demand was annulled by the appellate authority. Non-pursuance of the case lead to reduction in tax revenue and encouraged the taxpayers to claim incorrect tax credit claims.

The lapse was pointed out in November, 2024. The department replied that an amount of Rs 75.38 million was subjudice for the tax year 2018 and 2022, whereas an amount of Rs 41.30 million was under process for the tax years 2019 and 2021.

The DAC, in its meeting held in January 2025, directed the department to pursue the subjudice case, finalize the legal proceedings and report compliance to Audit/FBR. No further progress was reported till the finalization of this report.

[DP No. 23663-IT]

## **5. Conclusion**

The audit of tax credits claimed by taxpayers under Section 65E of the Income Tax Ordinance, 2001, has revealed that the uptake of the tax credit policy was extremely low. Even though the scheme had positive correlations with business indicators, its broader impact upon the economy was extremely limited. Out of hundreds of thousands of businesses in Punjab, KPK, Sindh and ICT only 139 taxpayers have actually utilized the tax credit policy during the period from 2018 to 2023. The study has also shown that those companies which availed this policy increased their capital investments and that the amount of tax credits claimed has had a practically and statistically significant and positive relation with business performance indicators like annual turnover and net profits. However, since only a handful of businesses have actually benefited from this policy the positive effects have not been large enough to improve national economic indicators such as gross capital formation, total investments, and industrial growth, which have seen a downward trend over the past six years.

Several discrepancies and non-compliances with the statutory requirements have also been found. The audit findings indicate that a significant number of taxpayers have claimed tax credits without fulfilling the stipulated conditions, potentially leading to undue fiscal benefits and revenue leakage. The audit findings demonstrate instances of non-adherence, such as delayed increases in share capital, tax credit claims made without requisite investment in new plant and machinery, and claims made before commencing commercial production or without necessary documentation such as audited accounts. Collectively, these issues highlight the need for a more rigorous monitoring framework to ensure compliance and proper utilization of tax credits to meet the Ordinance's intended purpose.

## **6. Recommendations**

1. A detailed evaluation of the scheme encompassing a holistic approach, should be carried out to ascertain the reasons for low utilization of exemptions under Section 65E of the Income Tax Ordinance 2001.
2. Strong monitoring and evaluation mechanism should be established to ensure effective implementation of all such schemes, and to prevent against misuse or abuse of such tax-exemptions besides evaluating overall success or otherwise in achieving desired objectives.
3. Implement robust verification mechanisms to ensure all conditions like mandatory checks on share capital increases, investment in machinery and adherence to prescribed timelines etc. are fulfilled before approving claims.
4. A system should be developed to monitor sales performance following the availing of tax credits, so as to avoid and probe trends of decreased sales after claiming credits.
5. Clear enforcement protocols should be established for claims submitted after the stipulated deadlines. It should be ensured that claims made after due registration dates or beyond the five-year period are disqualified unless there are exceptional justifications.
6. FBR should share industrial data of last twenty years with Audit for trend analysis and data processing to ascertain the efficacy of the scheme.
7. Submission of audited accounts should be made a mandatory requirement for tax credit claims under Section 65E. Tax credits should not be approved in cases where the audited financial statements are not submitted, as they are crucial for validating the financial and investment details of the taxpayer.
8. Periodic compliance audits should be conducted by FBR authorities to verify the physical installation and operational status of machinery purchased under the tax credit scheme. This will help confirm that investments are being utilized as intended and prevent misuse of policy.
9. Awareness programs and trainings should be developed for taxpayers and tax practitioners regarding the precise requirements under Section 65E to improve compliance and reduce the volume of non-compliant claims, as well as to enhance and expand adoption of the scheme by the industry.

## **CHAPTER-10    SECTORAL AUDIT OF TAXATION IN REAL ESTATE SECTOR**

### **1.     Introduction**

#### **1.1    Background**

Tax and fiscal policies are key determinants for a country's economic policies, among which amnesty schemes emerge as opportunities for the taxpayers and non-taxpayers to pay a certain amount in exchange for relief on tax liability relating to previous tax years, without any criminal or civil prosecution. It is a short-term strategy used primarily by developing countries for increasing tax brackets and national revenue by incentivizing people to declare their income and assets.

The Directorate General Audit, Inland Revenue and Customs, Lahore, conducted sectoral audit of taxation in real estate sector from July to November, 2023 and March to May, 2024 with a view to assess the implications of amnesty schemes and taxation relief measures introduced by the Government to improve tax compliance and bring more individuals into the national tax net. These schemes were basically designed to encourage investments in the construction sector by providing significant tax incentives and easing certain regulatory requirement.

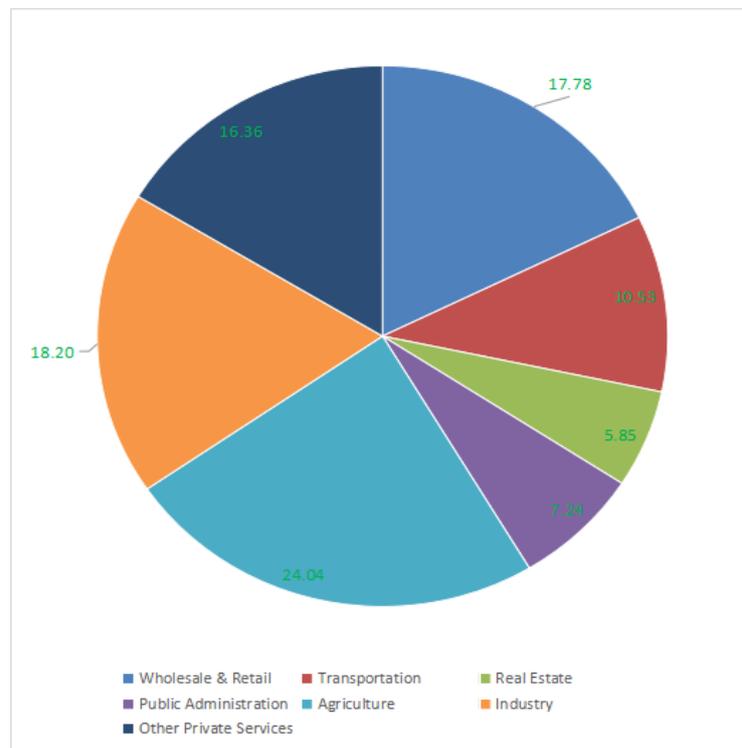
#### **1.2.    Significance of real estate sector in Pakistan's economy:**

Over the years, Pakistan has witnessed notable growth and transformation in its real estate market, with expansions in size and diversity evident in residential, commercial, and other sectors. This growth has been fuelled by factors such as population growth, urbanization, and rising investments. According to the World Bank, the real estate sector is the second-largest employer in the country after agriculture. As per Economic Survey of Pakistan, the contribution of real estate sector in Pakistan GDP as of FY 2023-24 is as follows:

<b>Table showing sector-wise contribution in GDP during FY 2023-24</b>		
<b>Sr. No.</b>	<b>Sector</b>	<b>Share in GDP %</b>
1	Wholesale & Retail	17.78
2	Transportation	10.53
3	Real Estate	5.85
4	Public Administration	7.24
5	Agriculture	24.04
6	Industry	18.20
7	Other Private Services	16.36

Source: Economic Survey of Pakistan

**Graph showing contribution of real estate sector to GDP during FY 2023-24**



Source: Economic Survey of Pakistan

The above tabular and pie chart presentation shows that the real estate sector contributed 5.85% to Gross Domestic Product (GDP) during the FY 2023-24.

The overall growth of economy is affected by the sector wise growth, the growth of real estate sector in Pakistan during last six years is tabulated as follow:

<b>Table showing growth of real estate sector in Pakistan</b>		
<b>Sr. No.</b>	<b>Financial Year</b>	<b>Growth in Percentage</b>
1	2018-19	3.62
2	2019-20	3.7
3	2020-21	3.64
4	2021-22	3.7
5	2022-23	3.78
6	2023-24	3.78

Source: Economic Survey of Pakistan



Source: Economic Survey of Pakistan

The above tabular and graphical presentation shows that real estate sector in Pakistan witnessed an average growth of 3.7% during the last six years. This trend is against the general perception that the tax exemptions announced for the real estate sector during 2020-21 resulted in a significant boost for the overall growth of real estate sector.

Pakistan has a significant informal economy, especially in the case of real estate sector, where many transactions are conducted in cash and are not properly documented. This informal economy provides opportunities for individuals to conceal assets and evade taxes. The tax amnesty schemes

introduced by the Governments provide the impetus to non-compliant taxpayers to avoid filing of regular returns, as they ever remain hopeful that the assets created through unexplained sources/black money may be whitened through availing the tax amnesty schemes introduced time and again by the Government.

Among the representative organizations of builders and developers in Pakistan, the most significant name is Association of Builders and Developers (ABAD). This organization was formed in the year 1972 comprising of 1,004 active members in Pakistan. The principal aims and objectives of (ABAD) include: unifying builders and developers for their collective good, promoting housing industry in the country, providing assistance to the Government in formulating its housing policies and plans and exploring the prospects of large-scale projects in the public sector.

## **2. Overview**

The successive governments in Pakistan have on the whole failed to focus on having structural policies that promote governance, structural reforms and methodologies that can help in discouragement of tax evasion. Tax amnesty schemes are not an appropriate mechanism to get people into tax bracket. There should be sustainable mechanisms through which people could be forced to declare concealed assets and pay due taxes. There must be asset-seizure schemes to discourage concealment of income and assets. Moreover, there is a need for the government to strengthen FBR as an institution to ensure effective tax-collection.

Tax amnesty schemes send the wrong message that evading taxes or engaging in illegal activities can be condoned through periodic schemes, undermining the integrity of the tax system. Without addressing underlying systemic issues, amnesty schemes will never yield the desired result of promoting long-term compliance, as has been seen in the past. These schemes on the contrary encourage genuine taxpayers to evade tax liability in expectation of some future tax amnesty scheme.

### **2.1 The Governing Laws and Rules**

The Government of Pakistan (GoP) has introduced various policy reforms to stimulate investment in real estate sector. In this regard, Section 100D was inserted in Income Tax Ordinance, 2001 through Finance Act 2020, which refers to an amnesty scheme introduced for builders and developers. Section

100D mandates the documentation of immovable properties, including land, buildings, and other real estate assets. As per the legal provisions, for tax year 2020 and onwards, the tax payable by a builder or a developer, as defined in sub-Section (9), who opts to avail such scheme, shall pay fixed tax in accordance with the rules of Eleventh Schedule @ per Sq. Ft. on the basis of completion of projects.

As per Rule 4 of Eleventh Schedule ibid every builder or developer shall be required to obtain and provide to the Board in the prescribed manner a certificate from map approving authority or NESPAK, as the case may be, to the following effect, namely:

- (a) 'total land area' developed in square yards;
- (b) 'covered area' in square feet;
- (c) 'saleable area' in square feet; and
- (d) type (commercial, residential or industrial) of saleable area or the total land area, as the case may be.

Further, as per sub Section 8 ibid notwithstanding anything contained in this Section or the Eleventh Schedule, where a return or declaration has been made through misrepresentation or suppression of facts, such return or declaration shall be void and all the provisions of this Ordinance shall apply accordingly.

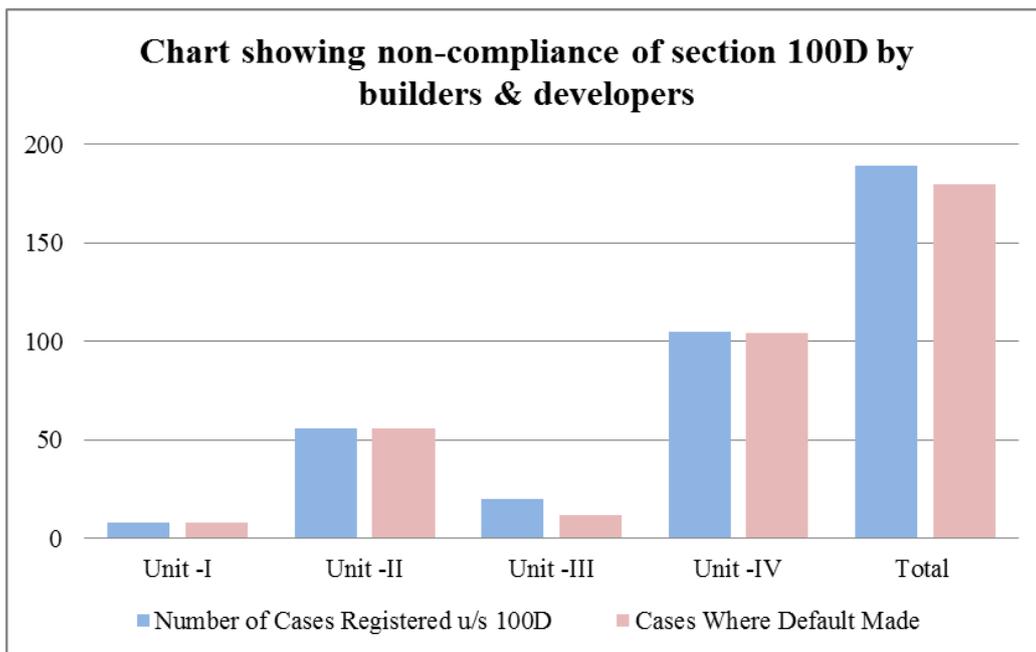
Section 236C and 236K of the Income Tax Ordinance 2001, provide for collection of advance tax from the sellers and purchaser or transferee of property respectively at the rate specified in Division X of Part IV of the First Schedule.

According to Section 37(1) of the Income Tax Ordinance 2001, Capital Gain Tax (CGT) is levied on the gains from the sale of capital assets i.e. land and buildings.

## **2.2 Weak compliance of legal provisions by builders and developers**

As of 30<sup>th</sup> June 2023, the unit wise compliance of Section 100D and relevant rules by the builders and developers assessed under the jurisdiction of RTO Islamabad is shown as under:

Sr. No.	Unit Name	Number of Cases Registered u/s 100D	Number of Cases which Complied with Rule 4	Cases Where Default Made	Percentage of Default
1	Unit –I	8	0	8	100
2	Unit –II	56	0	56	100
3	Unit -III	20	8	12	60
4	Unit –IV	105	1	104	99
	<b>Total</b>	<b>189</b>	<b>9</b>	<b>180</b>	<b>95</b>

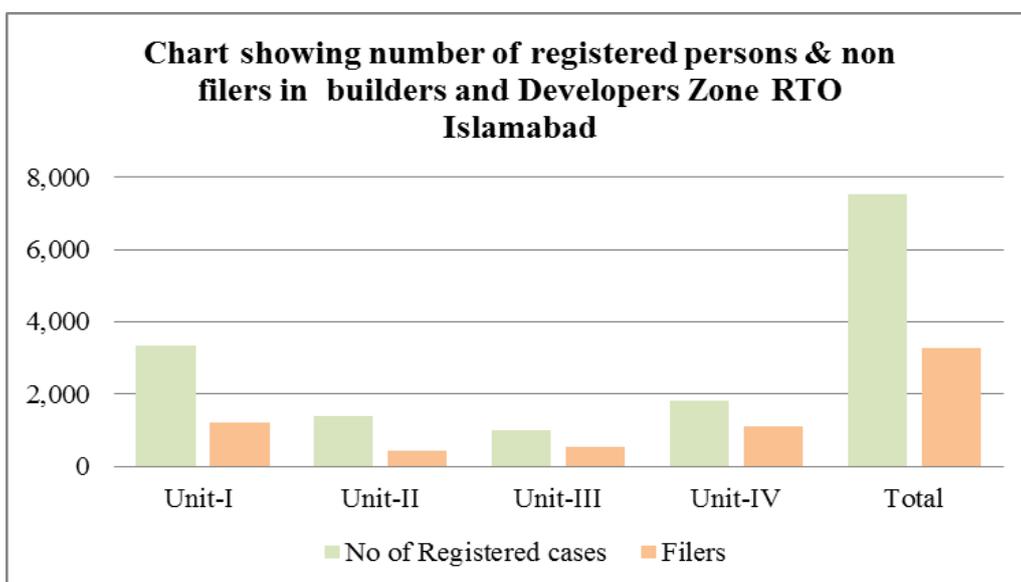


Source: Data provided by the Commissioner Special Zone for builders and developers RTO Islamabad

The above tabular and graphical presentation shows that 95 percent of the builders and developers who availed the tax amnesty scheme failed to comply with the conditionalities of the scheme. It is pertinent to mention here that as per Federal Board of Revenue (FBR) Islamabad data, 993 builders and developers got themselves registered under Section 100D, availed the tax amnesty and are being assessed by the various field formations of the FBR.

Audit scrutinized the data of filers and non-filers assessed under the jurisdiction of the Commissioner; Special Zone for Builders & Developers. As of 30<sup>th</sup> June, 2023, unit wise detail of filers and non-filers is elaborated below:

Sr. No.	Name of Unit	No of Registered cases	Filers	Non-Filers	% of Non-Filers
1	I	3,352	1,210	2,142	64%
2	II	1,382	444	938	68%
3	III	984	524	460	47%
4	IV	1,823	1,102	721	40%
	<b>Total</b>	<b>7,541</b>	<b>3,280</b>	<b>4,261</b>	<b>57%</b>



Source: Data provided by the Commissioner Special Zone for builders and developers of RTO Islamabad

The above tabular and graphical presentation shows that 57 percent of the taxpayers assessed in Regional Tax Office Islamabad, were non-filers, which shows weak enforcement of returns and recovery of taxes by the tax authorities.

Audit also observed that all the cases of builders and developers from the provinces of Punjab and KPK were clustered into the Regional Tax Office, Islamabad as of June, 2023, clustering of the cases in RTO Islamabad was not a

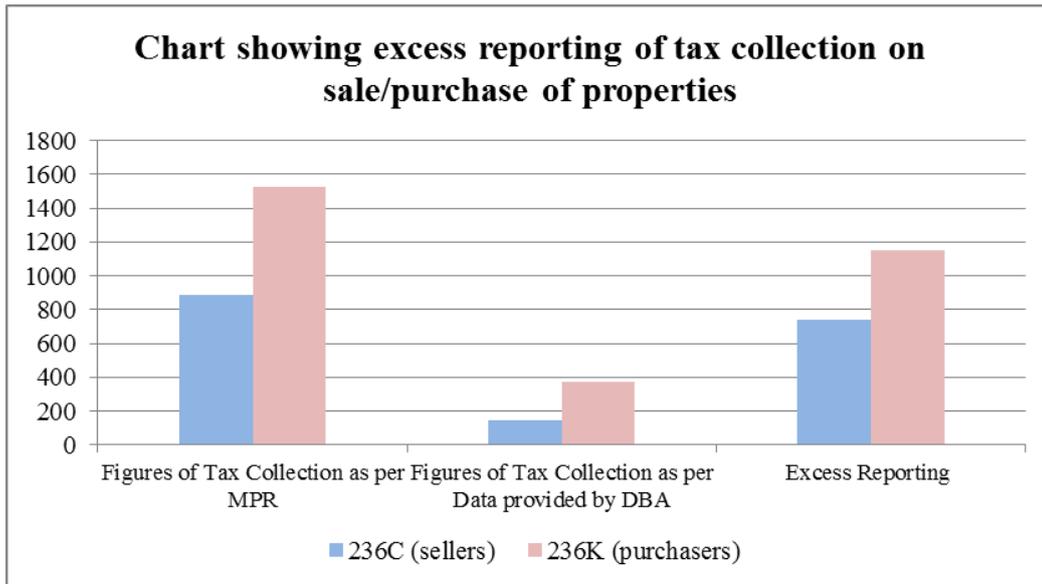
judicious decision which not only impaired the monitoring, assessment and recovery of taxes but also caused hardships to taxpayers. Keeping in view the hardships, the tax authorities out of total 11,243 cases re-assigned the jurisdiction of 3,702 cases to the concerned RTOs/LTOs. The said matter had time and again been highlighted/discussed in the Departmental Accounts Committee (DAC) meetings, because frequent transfer of jurisdiction causes delay in assessment and recovery of due taxes.

### **2.3 Excess reporting of tax collection on account of purchase and sale of properties**

During comparative analysis of tax collection regarding sale and purchase of properties between Monthly Performance Report, (MPR) prepared by the Commissioner Inland Revenue, Special Zone for Builders & Developers Regional Tax Office Islamabad and data provided by Pakistan Revenue Automation (Pvt.) Limited (PRAL), it was revealed that there was a huge discrepancy between tax collection figures reported by the two sources. The detail of excessive reporting of tax collection of Rs 1,892.49 million on sale and purchase of property is as follows:

*(Rs in million)*

<b>Table showing excess reporting of tax collection under Section 236C &amp; 236K</b>						
<b>Sr. No.</b>	<b>Tax Year</b>	<b>Section</b>	<b>Figures of Tax Collection as per MPR</b>	<b>Figures of Tax Collection as per Data provided by PRAL</b>	<b>Excess Reporting</b>	<b>Percentage of Excess Reporting %</b>
1	2023	236C (sellers)	889.21	146.41	742.80	83.53
2	2023	236K (purchasers)	1525.74	376.05	1,149.69	75.35
<b>Total</b>			<b>2,414.95</b>	<b>522.46</b>	<b>1,892.49</b>	



The above tabular and graphical presentation shows that Regional Tax Office, Islamabad had reported approximately 78 % excess collection as compared to tax collection reported by Pakistan Revenue Automation (Pvt.) Limited (PRAL) as on 30<sup>th</sup> June 2023 which needs reconciliation.

### 3. Audit Scope and Methodology

Sectoral audit was carried out at Regional Tax Offices Islamabad, Lahore and Corporate Tax Office Lahore from July to November, 2023 and March to May, 2024 and analysis thereon for last three Financial Years from 2020-21 to 2022-23. Audit selected field formations at Lahore and Islamabad because all cases of taxes pertaining to real estate sector of Punjab and KPK were transferred to these two Regional Tax Offices. Further, three financial years were chosen as the amnesty schemes regarding real estate sector were mostly initiated in 2020-2021.

The Directorate General Audit, Inland Revenue and Customs, Lahore, planned the sectoral audit of real estate sector in the Annual Audit Plan 2023-24. Following audit techniques were used for arrival at conclusions and findings:

- Inspection and examination of evidence through review of relevant documents
- Analysis of soft data collected from RTOs

- Concurrent audit methodology was used whereby the field audit teams of compliance audit also collected data for sectoral audit
- Inquiry-based auditing technique was also used, inclusive of letters and queries to other stakeholders for collection of additional information

Tax record of the builders and developers was collected from the RTOs at Lahore, Islamabad and Corporate Tax Office, Lahore. Whereas, data regarding tax collection under Sections 236C, 236K, 7E and 100D was collected from Pakistan Revenue Automation (Pvt) Limited (PRAL) working at Regional Tax Offices Islamabad and Lahore.

#### **4. Audit Objectives**

The sectoral audit of taxation in real estate sector was conducted with a view to assess the implications of amnesty schemes and taxation relief measures introduced by the Government to improve tax compliance and bring more individuals into the national tax net. This overall objective entails evaluation of advance tax collection on sale/purchase of property as well as scrutiny of application of provisions of tax amnesty scheme for builders/developers. Specific objectives of the sectoral audit were to check whether:

- (i) Correct amount of tax under Section 236C and 236K had been collected from purchaser and seller of property, and the department employed effective internal controls to monitor collection of tax by the registration authorities and housing societies.
- (ii) The provisions of Section 100D of the Income Tax Ordinance, 2001 were complied with by the builders and developers, who opted to pay tax under tax amnesty scheme / concessionary regime introduced through Finance Act, 2020.
- (iii) Non-filers were registered with the tax department to enable further monitoring and to examine that the proceedings under normal tax regime had been initiated and finalized in cases of non-compliance.
- (iv) The department was been able to recover due amount of tax from the persons who could not adequately explain the sources of investment/trail of funds under Section 111 for the purchase of the property.
- (v) Computerized Payment Receipts (CPRs) indicated Name, CNIC/NTN of persons on whose behalf tax had been deducted or collected to ensure

non-occurrence of *Benami* (proxy) transactions and incorrect claim of tax credit by the taxpayers.

## **5. Audit Findings**

### **5.1 Non-compliance of conditions in Amnesty Scheme**

In April 2020, the government announced a construction package to revive the construction industry and boost economic activity. The package included incentives such as tax exemptions, reduced taxes on construction materials and amnesty for the construction sector

Tax amnesty schemes emerge as opportunities for the taxpayers and non-taxpayers to pay a certain amount, in exchange for relief on tax liability relating to previous tax years. It is one of the short-term strategies which are used mostly by the developing countries for broadening tax net and increasing revenue by encouraging people to declare their concealed incomes and assets. In this way, tax amnesties facilitate non-compliant taxpayers to pay tax without any criminal or civil prosecution. Audit observed that despite availing incentives, taxpayers failed to comply with the conditions as contained in tax amnesty scheme which resulted in loss of revenue as detailed in the succeeding paras.

#### **5.1.1 Short payment of tax due to non-compliance of provisions of Section 100D of the Income Tax Ordinance, 2001 - Rs 1,963.00 million**

According to Section 100D (1) read with rules of Eleventh Schedule to the Income Tax Ordinance 2001, for tax year 2020 and onwards, a builder or a developer, who opts to avail tax amnesty scheme, shall pay fixed tax @ per Sq. Ft. on the basis of completion of projects duly certified by approving authority or NESPAK as the case may be.

It was observed during the audit of tax record of M/s Future Development Holdings (Pvt.) Limited NTN-7246022 assessed under the jurisdiction of RTO Islamabad, that the taxpayer had registered a project namely “Capital Smart City” as on December 31, 2020. The company was liable to pay tax in accordance with above provisions of law. Scrutiny of tax returns/accounts for the tax period from 2021 to 2023 revealed that the taxpayer did not declare any percentage completion of project nor paid tax amounting to Rs 1.963 billion as per agreed eight (8) instalments of Rs 245 million per quarter w.e.f.

15.01.2022. As such, non-compliance of provisions of Section 100D resulted in loss of revenue of Rs 1,963.00 million.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to revisit the case, finalize legal proceedings as per law and report compliance within 45 days. Further progress was not reported till finalization of the report.

The Audit recommends that department shall invoke the provisions of Section 100D of the Income Tax Ordinance 2001, recover the admitted amount of tax or make the assessment of income under normal tax regime and also invoke the provisions of Section 111 and withholding taxes.

[AO No.01]

#### **5.1.2 Irregular registration and non-payment of tax under Section 100D of the Income Tax Ordinance, 2001 – Rs 1,302.72 million**

According to Section 100D (1) read with rules as per the Eleventh Schedule to the Income Tax Ordinance 2001, for tax year 2020 and onwards, a builder or a developer, who opts to avail tax amnesty scheme, shall pay fixed tax @ per Sq. Ft. on the basis of completion of projects duly certified by approving authority or NESPAK as the case may be.

It was observed during the audit of one hundred and five cases (105) taxpayers registered as builders and developers, assessed under the jurisdiction of RTO Islamabad, that out of total cases, seventy one (71) taxpayers had registered various projects of housing colonies, apartments and commercial malls/plazas during September, 2020 to September, 2021 without declaration of covered or developed area in Sq. Ft as required under the law. In the absence of covered/developed area of projects in Sq. Ft. registration of the taxpayers under Section 100D was irregular. As per provisions of the amnesty scheme, taxpayers were also absolved to deduct withholding taxes and explain sources of investment made in the projects. In case of failure, provisions of Section 111 are invoked and tax liability is determined under normal tax regime. As such, registration of builders & developers was irregular which resulted in loss of revenue amounting to Rs 1,302.72 million during the tax years 2022 and 2023.

The lapse was pointed out from March to May, 2024. The Department informed that assessment proceedings had been initiated but yet not finalized.

The DAC in its meetings held during July and December 2024 directed the field formation of FBR to finalize legal proceedings and report compliance within 45 days. Further, progress was not reported till finalization of the report.

Audit recommends that the Department shall get details of land area developed and constructed area built in Sq. Ft. from the builders and developers, make assessment of income, and recover the due amount of tax as per law.

[Annexure-83]

### **5.1.3 Potential loss of revenue due to non-compliance of conditions of Rule 4 & Section 100D by builders and developers - Rs 8,385.75 million**

According to Section 100D (1) read with rules as per the Eleventh Schedule to the Income Tax Ordinance 2001, for tax year 2020 and onwards, a builder or a developer, who opts to avail tax amnesty scheme, shall pay fixed tax @ per Sq. Ft. on the basis of completion of projects. As per Rule 4 ibid every builder or developer shall be required to provide a certificate regarding details and completion of projects from approving authority or NESPAK as the case may be.

It was observed that one hundred and eighty-one (181) builders and developers, assessed under the jurisdiction of RTO Islamabad, and CTO Lahore, had registered various projects of housing colonies, apartments and commercial malls/plazas during September, 2020 to September, 2023 without declaration of covered or developed area as required under the law. In the absence of covered/developed area of projects in Sq. Ft., registration of the taxpayers under Section 100D was irregular. The builders and developers were also absolved of the obligations to explain sources of investment made in the projects and deduction of withholding taxes, otherwise, provisions of Section 111 were invoked and tax liability was determined under normal tax regime. Hence, non-observance of conditions of amnesty scheme resulted in potential loss of revenue amounting to Rs 8,385.75 million during the tax years 2021 to 2023.

The lapse was pointed out from July to November, 2023 and March to May, 2024. The Department informed that assessment proceedings had been initiated but yet not finalized.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law within 30 days. Further, progress was not reported till finalization of the report.

Audit recommends that the Department shall get details of land area developed and constructed area built in Sq. Ft. by the builders and developers, finalize the assessment orders and recover the due amount of tax as per law.

[Annexure-84]

#### **5.1.4 Loss of revenue due to acceptance of void returns/declaration - Rs 228.60 million**

As per sub Section 8 of Section 100D of the Income Tax Ordinance 2001, notwithstanding anything contained in this section or the Eleventh Schedule, where a return or declaration has been made through misrepresentation or suppression of facts, such return or declaration shall be void and income of the taxpayers charged to tax under normal tax regime.

It was observed during the audit scrutiny of income tax returns / data in respect of twenty cases (20) registered as builders and developers, assessed under the jurisdiction of RTO Islamabad and Corporate Tax Office, Lahore, that taxpayers while filing income tax returns / declarations did not declare developed or constructed area in Sq. Ft which rendered the declaration as void. Hence, income of the taxpayers was required to be assessed under normal tax regime, but assessing authorities did not proceed as per law which resulted in loss of revenue amounting to Rs 228.60 million during the tax years 2022 and 2023.

The lapse was pointed out from July to November, 2023 and March to May, 2024. The Department informed that the cases were still under consideration of the department.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that department shall finalize the assessment proceedings, assess the income and recover due tax vis-a-vis recovery of withholding taxes as per law.

[Annexure-85]

## **5.2 Non-enforcement of tax on deemed income and super tax**

Inconsistent enforcement of laws and regulations pertaining to real estate transactions had contributed to the menace of asset concealment and consequent loss of revenue. In order to enhance and accumulate additional revenue, Government of Pakistan, introduced tax on deemed income i.e. Fair Market Value (FMV) of capital assets exceeding certain limits. Further, super tax was also levied on high earning persons. Such policies are intended to reduce inequalities and disparities of income and assets within the country. Audit observed that department did not make strenuous efforts to assess value of capital assets, and to charge and recover tax from taxpayers having assets exceeding the prescribed limit.

### **5.2.1 Potential loss of revenue due to non-realization of tax on deemed income - Rs 1,291.31 million**

According to Section 7E (1) of the Income Tax Ordinance, 2001 as amended through Finance Act 2022, for Tax Year 2022 and onwards, a tax shall be imposed at the rates specified in Division VIIC of Part-I of the First Schedule on the deemed income i.e. Fair Market Value (FMV) of capital assets exceeding 25 million with certain exclusions and conditions as specified in the law.

It was observed during audit of tax record / analysis of data provided by the Data Base Administrator (DBA) of Regional Tax Office, Islamabad that out of 1,955 cases of the taxpayers only four (4) taxpayers voluntarily paid tax on deemed income amounting to Rs 7.294 million for Tax Years 2022 and 2023. Out of selected cases, the remaining 904 taxpayers were obliged to pay tax on deemed income as the Fair Market Value (FMV) of their capital assets exceeds the statutory threshold as prescribed under the law. But neither the taxpayers made voluntarily compliance of law to pay obligatory tax nor the assessing officers of the Department initiated legal proceedings to assess value of capital assets and enforce recovery of tax on deemed income from the potential taxpayers. This shows weak internal controls and enforcement of law to recover the government revenue. This resulted in potential loss of revenue amounting to Rs 1,291.31 million cases during the tax years 2022 and 2023.

The lapse was pointed out from March to May, 2024. The Department reported that the matter is subjudice before the Supreme Court of Pakistan, therefore, recovery proceedings will be taken after finality.

The DAC in its meetings held during July and December 2024 directed the field formation to pursue the case with Honorable Supreme Court of Pakistan under intimation to FBR / Audit.

The Audit recommends that FBR may pursue the subjudice cases.

[Annexure-86]

### **5.2.2 Loss of revenue due to non-levy of super tax on high earning persons - Rs 288.51 million**

According to Section 4C of the Income Tax Ordinance 2001, a super tax shall be imposed on income of every person for tax year 2022 and onwards at the rates specified in Division IIB of Part I of the First Schedule.

It was observed during the audit of tax records of nine (09) taxpayers falling under the jurisdiction of RTO, Islamabad for the year 2023, that the taxpayer's income was liable to super tax as per law. But the taxpayers did not pay due amount of tax. The tax authorities also did not take the remedial action to recover the government dues. This resulted in non-levy of super tax amounting to Rs 288.51 million.

The lapse was pointed out from March to May, 2024. The Department reported that the matter is subjudice before the Supreme Court of Pakistan, therefore, recovery proceedings will be taken after finality.

The DAC in its meetings held during July and December 2024 directed the field formation to pursue the case with Honorable Supreme Court of Pakistan under intimation to FBR / Audit.

The Audit recommends that FBR may pursue the subjudice cases under intimation to Audit.

[Annexure-87]

### **5.2.3 Non-levy of super tax under Section 4B of the Income Tax Ordinance, 2001 – Rs 106.87 million**

According to Section 4B of the Income Tax Ordinance, 2001 a super tax shall be imposed for rehabilitation of temporarily displaced persons for tax years 2015 and onwards at the rates specified in Division IIA of Part I of the First Schedule, on income of every person specified in the said Division.

It was observed during the audit of tax record of two (02) taxpayers falling under the jurisdiction of RTO Islamabad, that the taxpayers' income had

been assessed for tax year 2018 & 2019 vide orders under Section 122(1) of the income tax ordinance 2001, which was liable to super tax as per law. But the assessing officer did not charge super tax while calculating their tax liability. The omission resulted in loss of revenue amounting to Rs 106.87 million.

The lapse was pointed out from March to May, 2024. The Department reported that in one case an amount of Rs 93.57 million was charged but taxpayers preferred appeal before Commissioner Inland Revenue Appeals, hence, case was subjudice, whereas, in the other case involving Rs 12.45 million assessment proceedings were initiated but yet not finalized by the Department.

The DAC in its meetings held during July and December 2024 directed the field formation to pursue the subjudice case and finalize the legal proceedings within 45 days where Departmental action was pending. Further, progress was not reported till finalization of the report.

The Audit recommends that FBR authorities shall finalize the pending assessment and pursue the subjudice case under intimation to Audit.

[Annexure-88]

### **5.3 Taxation on sale and purchase of property**

The Income Tax Ordinance, 2001 provides for collection of tax from purchasers/transferees and sellers/transfersors of property. In Pakistan, one common practice in the real estate sector is under reporting of property values during transactions. In addition to this, cash transactions are prevalent in the real estate sector, making it easier to conceal income and evade taxes. These practices allow individuals to conceal actual value of property resulting into short collection of taxes by land registering authorities and housing societies. Further, as per international best practices, unique identification number (UIN) is allotted to each taxpayer to avoid any legal or financial implications. Audit opined that in a number of cases, short collection of tax was made by the land registration authorities and housing societies. Moreover, Audit also observed that while generating mandatory fields of computerized payments receipts (CPRs) Names, CNICs or NTN of purchasers and sellers were not mentioned which leads to claim of incorrect tax credit by the said persons which also facilitates “*Benami*” transactions.

### **5.3.1 Short realization of tax on purchase of property under Section 236K of the Income Tax Ordinance, 2001 - Rs 766.07 million**

According to Section 236K of the Income Tax Ordinance 2001, any person responsible for registering, recording or attesting transfer of any immovable property shall at the time of registering, recording or attesting the transfer shall collect from the purchaser or transferee advance tax at the rate specified in Division XVIII of Part IV of the First Schedule.

It was observed during audit of tax record of M/s Future Development Holdings (Pvt.) Limited NTN-7246022 assessed under the jurisdiction of RTO Islamabad that the taxpayer had undertaken a project namely “Capital Smart City” along with other services as on December 31<sup>st</sup> 2020. The company had purchased land worth Rs 40,125.35 million during the tax period commencing from 2020 to 2023 as per note 7 to the audited accounts as on 30<sup>th</sup> June, 2023. Scrutiny of tax return/record along with audited accounts for the tax period from 2021 to 2023 revealed that the taxpayer had paid tax under Section 236K amounting to Rs 36.43 million whereas, tax payable as worked out on the basis of land purchased at cost is Rs 802.50 million (2 percent of Rs 40,125.35 million). Hence, an amount of Rs 766.07 million (Rs 802.51 million – Rs 36.43 million) was short realized by the department.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that Department shall devise a mechanism for monitoring of tax collections made by the land registration authorities and housing societies, enforce submission of withholding statements by the concerned withholding agents and recover due amount of tax from taxpayers as per law.

[AO No.02]

### **5.3.2 Irregular/inadmissible tax credit allowed under Section 236K to purchaser/transferees of property on fake NTN/CNICs – Rs 557.77 million**

Section 236K of the Income Tax Ordinance 2001, provides for collection of advance tax from the purchaser or transferee of property at the rate specified in Division X of Part IV of the First Schedule. As per Section 165 *ibid* a tax collecting agent shall, furnish to the Commissioner a quarterly statement in the prescribed form setting out the Name, CNIC Number, NTN and address of each person from whom tax has been collected under the law.

It was observed in 17,684 cases of purchasers / transferees of property for the Tax Year 2023 assessed under the jurisdiction of RTO, Islamabad that the tax collecting agents/registration authorities or housing authorities either deliberately did not fill or filled fake Name, NTN/CNICs along with other particulars of purchasers of property. This shows weak monitoring and realization of tax collected by registration authorities. It is pertinent to mention here that the said challans are the basis of claim of tax credit/refund by the purchasers of property. As such, incorrect tax credit amounting to Rs 557.77 million was allowed on the basis of invalid NTN/CNICs.

The lapse was pointed out from March to May, 2024. The department contested three (03) cases only out of 17,684 cases of invalid CPRs and did not furnish reply in remaining cases. Audit is of the view that in the absence mandatory fields claim / admissibility of the tax credit is invalid and chances of multiple claim of tax credit by the taxpayers cannot be ruled out along with *Benami* transactions of holding property.

The DAC in its meetings held during July and December 2024 directed the field formation to forward the case to FBR for strengthening internal control mechanism regarding generation of valid online CPRs and report compliance within 30 days. Further progress was not reported till finalization of the report.

The Audit recommends that Department shall devise and enforce systemic validation checks while generating Computerized Payment Receipts (CPRs) by the withholding/tax collecting agents in the E-Portal of Inland Revenue Information System (IRIS) to ensure filling of mandatory fields of (CPRs) to plug the loopholes in the electronic tax collection system under intimation to Audit.

[AO No.07]

### **5.3.3 Short payment of tax on sale of property under Section 236C of the Income Tax Ordinance, 2001 - Rs 545.38 million**

According to Section 236C (1) any person responsible for registering, recording or attesting transfer of any immovable property shall at the time of registering, recording or attesting the transfer shall collect from the seller or transferor advance tax at the rate specified in Division X of Part IV of the First Schedule.

It was observed during the audit of tax record of (04) four taxpayers falling under the jurisdiction of Commissioner RTO, Islamabad that the taxpayers had registered themselves as builders & developers. Scrutiny of tax returns and withholding statements for the tax period 2022 & 2023 revealed that the taxpayers had not collected and deposited due amount of tax under Section 236C of the Ordinance. As such, non-collection of tax resulted in loss of revenue amounting to Rs 545.38 million.

The lapse was pointed out from March to May, 2024. The Department replied that the provisions of Section 236C (4)(b) are not applicable in the cases. Audit is of the view that provisions of clause (4)(b) of Section 236C were omitted through Finance, Act 2016 hence, tax was chargeable as per law. The Department was requested to revisit the cases as per existing provisions of law.

The DAC in its meetings held during July and December 2024 directed the field formation to revisit the cases and finalize the legal proceedings as per law and report compliance within 30 days. Further, progress was not reported till finalization of the report.

The Audit recommends that Department shall devise a mechanism in collaboration with housing societies and land registration authorities to enforce recovery of due amount of tax from sellers of land as per law.

[Annexure-89]

### **5.3.4 Irregular/incorrect tax credit allowed under Section 236C to sellers/transferor of property on fake NTN/CNICs - Rs 234.22 million**

Section 236C of the Income Tax Ordinance 2001 provides for collection of advance tax from the sellers or transferor of property at the rate specified in Division X of Part IV of the First Schedule. As per Section 165 of the Income Tax Ordinance 2001, every person collecting tax shall, furnish to the

Commissioner a quarterly statement in the prescribed form setting out the Name, CNIC/NTN and address of each person from whom tax has been collected.

It was observed in 8,899 cases / paid challans in respect of sellers / transferors of property for the Tax Year 2023 and 2024 assessed under the jurisdiction of RTO, Islamabad that the collecting agents either deliberately did not fill or filled fake Name, NTN/CNICs along with other particulars of the tax payers. This shows weak monitoring and realization of tax collected by registration authorities / housing societies. It is pertinent to mention here that the said challans are the basis of claim of tax credit/refund by the sellers of property. As such, incorrect tax credit amounting to Rs 234.22 million was allowed on the basis of invalid NTN/CNICs.

The lapse was pointed out from March to May, 2024. The Department contested two (02) cases out of 8,899 cases of invalid CPRs and did not furnish reply in remaining cases. Audit is of the view that in the absence mandatory fields claim / admissibility of the tax credit is invalid and chances of multiple claim of tax credit by the taxpayers cannot be ruled out along with *Benami* transactions of holding property.

The DAC in its meetings held during July and December 2024 directed the field formation to forward the case to FBR for strengthening internal control mechanism regarding generation of valid online CPRs and report compliance within 30 days. Further progress was not reported till finalization of the report.

The Audit recommends that Department shall devise and enforce systemic validation checks while generating Computerized Payment Receipts (CPRs) by the withholding/tax collecting agents in the E-Portal of Inland Revenue Information System (IRIS) to ensure filling of mandatory fields of (CPRs) to plug the loopholes in the electronic tax collection system under intimation to Audit.

[AO. No.06]

### **5.3.5 Short-realization of advance tax from purchasers of property due to application of incorrect rate of tax - Rs 271.73 million**

Section 236K read with Section 161 of the Income Tax Ordinance, 2001 provides that any person responsible for registering, recording or attesting transfer of any immovable property shall at the time of registering; recording or

attesting the transfer shall collect from the purchaser or transferee advance tax at the rate of 2% of fair market value.

It was observed during audit in five thousand nine hundred and twenty-seven (5,927) cases, assessed under the jurisdiction of RTO, Lahore, that tax collecting agent M/s Defense Housing Authority Lahore deducted tax at the rate of 1% instead of 2%. The assessing authorities of RTO didn't take remedial action for the recovery of the balance amount from the concerned tax collecting agent along with default surcharge leviable as per law. As such, due to non-initiating of legal proceedings against the tax collecting agent, the Government suffered a revenue loss amounting to Rs 271.37 million during tax year 2023.

The lapse was pointed out from March to May, 2024. The Department replied that jurisdiction of the case pertains to Corporate Tax Office Lahore, DAC directed to get incorporation certificate from the concerned office under intimation to Audit.

The DAC in its meetings held during July and December 2024 directed the Department to obtain incorporation certificate from the concerned filed formation under intimation to Audit.

The Audit recommends that Department should have outreach programs to educate withholding agents of real estate sector to avoid such errors, recover the withholding taxes from the withholding agent/builder or developer as per law.

[AO No.01 RTO- Lahore]

### **5.3.6 Excess reporting of tax collection under Sections 236C & 236K - Rs 1,892.49 million**

Section 236C and 236K of the Income Tax Ordinance 2001 provides for collection of advance tax from the sellers and purchasers or transferee of property respectively at the rate specified in Division X of Part IV of the First Schedule. The collection of taxes such made is reported to FBR through Monthly Performance Report (MPR) for each month and a consolidated (MPR) is prepared at the end of each year.

Audit made comparative analysis of tax collection on account of sale and purchase of property between two sets of figures, as per Monthly Performance Report, (MPR) prepared by the Commissioner Inland Revenue, Special Zone for Builders & Developers Regional Tax Office, Islamabad and data provided by

Data Base Administrator (DBA) Pakistan Revenue Automation (Pvt.) Limited (PRAL). Audit observed that there was a huge difference between tax collection in both sets of figures as reported by the Regional Tax Office, Islamabad to the Federal Board of Revenue (FBR), Islamabad for consolidation in the Federal Consolidated Fund. The detail of excess reporting of tax collection of Rs 1,892.49 million on sale and purchase of property is as follows:

*(Rs in million)*

Sr. No.	Tax Year	Section	Figures of Tax Collection as per MPR	Figures of Tax Collection as per Data provided by DBA	Variation
1	2023	236C (sellers)	889.212	146.41	742.80
2	2023	236K (purchasers)	1,525.74	376.05	1,149.69
<b>Total Excess Reporting</b>					<b>1,892.49</b>

The above comparative analysis of tax collection on transaction for sale and purchase of property during the Tax Year 2023 revealed that tax collection reported by the Regional Tax Office, Islamabad on account of both the heads was on higher side as compared to actual tax collection reported to Audit by the Data Base Administrator (DBA) of Pakistan Revenue Automation (Pvt.) Limited (PRAL) Islamabad. The position may be justified and collection under both the heads be reconciled with Data Base Administrator (DBA) under intimation to Audit.

The lapse was pointed out from March to May, 2024. The department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to reconcile the figures of tax collection within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department shall reconcile substantial difference in tax collection figures on account of sale and purchase of property under intimation to Audit.

[Based on AO No.66]

#### **5.4 Irregularities in assessment and adjustment of refunds**

Income Tax Ordinance is based on Universal Self Assessment Scheme. The return filed by the taxpayer is taken as assessment order passed by the Commissioner Inland Revenue, while filing income tax returns, tax payers assess undue refunds and claim credit of such taxes which are not admissible to the taxpayers. Further, such assessed refunds are also carried forward for adjustment against tax liabilities of the subsequent tax years. Section 170 of the Income Tax Ordinance 2001, read with Circular No. 05 of 2003 of FBR, provides that a taxpayer, who has paid tax in excess of the amount to which the taxpayer is properly chargeable, is eligible for a refund subject to fulfilment of prescribed conditions. Audit observed a number of cases, where excessive refunds were assessed by the Department, as refunds of tax paid are not admissible to the taxpayers who opted to avail tax amnesty scheme. Audit also observed such cases where tax paid was to be treated as minimum tax liability but the Department did not proceed as per law.

##### **5.4.1 Excess assessment of refund – Rs 203.19 million**

According to Section 170 read with Section 100D (1) of the Income Tax Ordinance 2001 for tax year 2020 and onwards, the tax payable by a builder or a developer, as defined in sub-Section (9), who opts to pay tax under this Section, shall pay fixed tax. Further, as per sub Section 2(e) ibid there shall be no refund of any tax collected or deducted under this Ordinance.

It was observed during the audit of tax record of (04) four taxpayers assessed under the jurisdiction of RTO Islamabad, that the taxpayers had registered themselves as builders & developers under Section 100D of the Ordinance. The taxpayers had paid tax under Section 100D and claimed refund out of payments made under the said section in their income tax returns for tax year 2023, whereas, no refund is admissible as per law. As such, the excess refund of Rs 203.19 million was assessed by the Department.

The lapse was pointed out from March to May, 2024. The Department replied that the cases were still under consideration of the department. RTO was requested to finalize the cases as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 30 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department should assess correct amount of refund to avoid excessive adjustment of refunds by the taxpayers under intimation to Audit.

[Annexure-90]

**5.4.2 Excess assessment of refund due to non-treating of tax deductions on contracts as minimum tax - Rs 25.30 million**

According to Section 153(1)(c) of the Income Tax Ordinance, 2001, every prescribed person making a payment in full or part including a payment by way of advance to a resident person or permanent establishment in Pakistan of a non-resident person, on the execution of contract, shall at the time of making the payment, deduct tax from the gross amount payable at the rates specified as per First Schedule. Further as per Finance Act 2019, sub Section 3 ibid was amended and tax deducted on contracts was treated as minimum tax liability.

It was observed during the audit of tax record of (02) two taxpayers falling under the jurisdiction of RTO Islamabad that the taxpayers had derived income from architectural/construction activities during the tax year 2023. The taxpayers while filing income tax returns claimed tax credit under Section 153(1)(c) as adjustable despite the fact that the tax deducted on execution of contracts was higher than the normal tax liability. Hence, tax deducted on execution of contracts was required to be treated as minimum tax liability as per law. As such, incorrect claim of tax credit under Section 153 as adjustable resulted in excess assessment of refund amounting to Rs 25.30 million.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department should assess correct amount of refunds as per law under intimation to Audit.

[Annexure-91]

## **5.5 Concealment of assets and income from contracts**

Legal provisions as contained in the income tax law imposes duties on both sellers and purchasers of immovable properties to ensure compliance with documentation requirements and declaration of fair market value of assets. Sellers are obligated to provide accurate information about the property's value, while purchasers are responsible for verifying the declared value and ensuring proper documentation. If the buyers or sellers conceal the particulars of their assets then legal remedy is available with the assessing authorities to charge tax on concealed income and investments. Audit observed that purchasers and sellers did not file income tax returns, hence, concealed their income and assets. Further, as per law contractors were required to declared the Sq. Ft. area constructed and pay tax accordingly but department did not enforce the said provisions of law.

### **5.5.1 Short realization of Income Tax due to concealment of investment and assets- Rs 930.08 million**

Section 111 of the Income Tax Ordinance, 2001 provides a detailed procedure for taxation of concealed income. According to the provision where a person is the owner of any money or valuable article or has made any investment or credited any amount in his books of accounts, the amount is chargeable to tax if not adequately explained by the taxpayer.

It was observed during the audit of tax record of eighty-one (81) taxpayers falling under the jurisdiction of Commissioner IR, RTO, Islamabad and RTO, Lahore that the taxpayers had derived income from construction and completion of buildings in Islamabad Capital Territory (ICT) Islamabad and Lahore. Out of total cases, seventy-nine (79) taxpayers purchased properties but failed to file returns and explain their sources of investment as required under the law, two (02) taxpayers while filing income tax returns declared the short amount of sales and paid short amount of tax in their income tax returns. The assessing officers were required to enforce income tax returns, make assessment of the concealed of assets by the taxpayers in their income tax returns, but the needful was not done. This omission resulted in loss of revenue amounting Rs 930.08 million.

The lapse was pointed out from March to May, 2024. The Department did not furnish reply till finalization of the report.

The para was not discussed in the DAC meeting due to non-submission of reply by the Department.

The Department is requested enforce income tax returns from purchasers of property and recover the due amount of tax under intimation to Audit

[Annexure-92]

### **5.5.2 Non levy of tax under Section 7C of the Income Tax Ordinance**

According to Section 7C of the Income Tax Ordinance 2001, a tax shall be imposed on the profits and gains of a person deriving income from the business of construction and sale of residential, commercial or other buildings at the rates specified in Division VIII A of Part I of the First Schedule.

It was observed during audit of income tax records of two (2) taxpayers falling under the jurisdiction of RTO, Lahore, that the taxpayers derived income from construction / building services for the Tax Years 2022 and 2023. The said taxpayers calculated and paid tax under normal tax regime instead of rates of as per Section 7C as specified in Division VIII A of Part I of the First Schedule for the persons involved in the business of construction. The department also did not take notice of this irregularity.

The lapse was pointed out from March to May, 2024. The Regional Tax Office reported that cases pertain to Corporate Tax Office Lahore.

DAC directed the Department to get incorporation certificate from the concerned office under intimation to Audit.

The Audit recommends that the Department shall monitor assessment and recovery of tax from the contractors as per legal provisions under intimation to Audit.

[Annexure-93]

### **5.6 Miscellaneous Taxation issues**

As per legal provisions, income tax shall be imposed for each tax year, at the rate or rates specified, as the case may be, on every person who has taxable income for the year. Capital gains, arising on the disposal of a capital assets by a person in a tax year, are chargeable to tax in that year under the head "Capital Gains." As per law housing societies/principals are required to withhold income tax under various provisions of income tax law while making payments to suppliers, service providers and commission agents. Further, as per sales tax Act,

sales tax is charged on services rendered by builders and developers. Audit observed that in number of cases, sales tax was not charged by the Department on services rendered by the said taxpayers as detailed in the paras below:

#### **5.6.1 Non-charging of Sales Tax on Services - Rs 3,974.20 million**

According to Section 3 of Islamabad Capital Territory (Tax on Services) Ordinance 2001, there shall be charged, levied and paid a tax known as Sales Tax at rates specified in column (4) of Table-1 of the Schedule to Ordinance of the value of the taxable services rendered or provided in the Islamabad Capital Territory. The term services, also includes construction services and services provided by the property developers and promoters.

It was observed during the audit of income tax records of thirty (30) taxpayers falling under the jurisdiction of RTO, Islamabad for the tax periods 2022 & 2023, that the taxpayers were deriving income from construction / building services in Islamabad Capital Territory (ICT) Islamabad. Hence, the taxpayers were required to pay sales tax on value of construction services as chargeable under the law, but failed to charge and pay sales tax on contractual services as per law. The tax authorities also did not take notice of this omission by the taxpayers. This resulted in loss of revenue amounting to Rs 3,974.20 million.

The lapse was pointed out from March to May, 2024. The Department replied that the cases were still under consideration of the department. RTO was requested to finalize the cases as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that Department shall monitor filling of sales tax returns by the builders and developers and recovery of due tax under intimation to Audit.

[Annexure-94]

#### **5.6.2 Loss of revenue due to non-deduction of tax on commission paid to real estate agents - Rs 496.64 million**

According to sub Section (1) of Section 233, where any payment on account of brokerage or commission is made by the Federal Government, a

Provincial Government, a Local Government, a company or an association of persons constituted by or under any law hereinafter called the principal to a person hereinafter called the agent the principal shall deduct advance tax at the rate specified in Division II of Part IV of the First Schedule from such payment.

It was observed during the audit of tax record of (06) six taxpayers falling under the jurisdiction of Commissioner IR, RTO Islamabad, that the builders/developers had paid commission to their selling agents during the tax periods 2022 & 2023. Scrutiny of withholding statements revealed that the taxpayers failed to deduct the due amount of tax while making payment of commission to the real estate commission agents. The Department did not take corrective action to retrieve the loss of revenue. The omission resulted in non/short recovery of tax amounting to Rs 496.64 million.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends to finalize the legal proceedings besides strengthening monitoring controls over withholding agents through risk-based desk audit and effective utilization of IT based systems

[Annexure-95]

### **5.6.3 Loss of revenue due to non-realization of minimum tax under Section 113 – Rs 82.85 million**

Section 113 of the Income Tax Ordinance, 2001 provides for the realization of minimum tax based on the turnover of a taxpayer. The tax is to be paid if, otherwise, no tax is payable on taxable income due to any reason, or tax payable under the normal tax regime is less than the minimum tax liability in respect of specified categories of taxpayers.

It was observed during audit of income tax records of (05) five taxpayers falling under the jurisdiction of RTO, Islamabad for the tax years 2020 to 2023, that taxpayers had not computed their minimum tax liability correctly on declared turnover in the income tax returns as required under the law. The tax

authorities also did not take notice of this omission by the taxpayers which reflects the weak internal controls within the department. This resulted in loss of revenue of Rs 82.85 million.

The lapse was pointed out from March to May, 2024. The Department replied that in one case an amount of Rs 4.39 million had been charged but yet not recovered, while the remaining cases were still under consideration of the department. RTO was requested to recover the charged amount and finalize the legal proceedings in the remaining cases as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to recover the charged amount and finalize the legal proceedings as per law within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that Department shall recover the charged amount and finalize the assessment proceedings under intimation to Audit.

(Annexure-96)

#### **5.6.4 Short payment of tax on capital gains under Section 37 - Rs 16.50 million**

According to Section 37(1) read with Section 111 of the Income Tax Ordinance 2001, a gain arising from the disposal of a capital asset by a person in a tax year, other than a gain that is exempt from tax under this Ordinance, shall be chargeable to tax in that year under the head "Capital Gains".

It was observed during the audit of tax record of Mr. Rizwan Ghani (CNIC 6110119220489) assessed under the jurisdiction of RTO Islamabad, that the taxpayer had declared capital gains from sale of immovable property amounting to Rs 176.67 million in his income tax return for tax year 2022 and paid tax at Rs 9.99 million, whereas, as per slabs rates introduced through Finance Act, 2021 effective from tax year 2022, tax chargeable is calculated at Rs 26.50 million but neither the taxpayer paid the due amount of tax nor the assessing officer enforced recovery of tax from the taxpayer. The omission resulted in loss of revenue amounting to Rs 16.50 million.

The lapse was pointed out from March to May, 2024. The Department replied that show-cause notice had been issued on 05.07.2024 for compliance on 23.07.2024 but case was not yet finalized by the department. RTO was requested to finalize the legal proceedings as per law.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that Departmental authorities shall devise systemic checks and controls to monitor and recover capital gain tax as per law.

[Annexure-97]

#### **5.6.5 Non recovery of default surcharge under Section 205 of the Income Tax Ordinance, 2001 – Rs 6.67 million**

According to Section 205 of the Income Tax Ordinance 2001, where a person fails to pay any tax on or before the due date of payment, the person shall be liable to pay default surcharge at the prescribed rate on the unpaid amount of tax.

It was observed during the audit of income tax records of (05) five taxpayers falling under the jurisdiction of the RTO, Islamabad for the tax year 2023 that the taxpayers were required to pay ninety percent of the tax payable for the tax year 2023 in advance during the year. The tax paid by the taxpayers was less than the ninety percent of the tax payable on which default surcharge was required to be recovered from April, 2023. The tax authorities did not take notice of this omission by the taxpayers which reflects the weak internal controls in the department. The non-recovery of default surcharge resulted in loss of revenue amounting to Rs 6.67 million

The lapse was pointed out from March to May, 2024. The department replied that legal proceedings in a case involving Rs 0.20 million had been initiated but yet not finalized. A case involving Rs 2.35 million was transferred to RTO Rawalpindi, further, Department has sought clarification in three cases involving Rs 4.12 million with respect to chargeability of default surcharge. RTO was requested to finalize the case where legal proceedings initiated, revisit and finalize the case as per law and obtain incorporation certificate where case transferred to other office.

The DAC in its meetings held during July and December 2024 directed the field formation to revisit the case and finalize the legal proceedings as per law and report compliance within 30 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department shall monitor payment of admitted tax liabilities along with return as per law and recover default surcharge wherever, taxpayers made default in making timely payment of tax as per law.

[Annexure-98]

#### **5.6.6 Non-withholding of Income Tax on dividend - Rs 4.5 million**

According to Section 150, every person paying a dividend shall deduct tax from the gross amount of the dividend paid or collect tax from the amount of dividend in specie at the rate specified in Division I of Part III of the First Schedule.

It was observed during the audit of tax record of M/s Cityscape Builders & Developers (Pvt.) Limited NTN-0094008 assessed under the jurisdiction of Commissioner IR, Special Zone for Builders & Developers, RTO Islamabad, that the taxpayer paid dividend to its shareholders/directors amounting to Rs 30.00 million for tax year 2023 vide cash flow statement as on 30<sup>th</sup> June, 2023. The taxpayer being withholding agent was required to deduct tax while making payment of dividend to its Directors. The Department did not take action to retrieve the loss of revenue as required under the law. The omission resulted in loss of revenue amounting to Rs 4.5 million (30.00 million \*15%).

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department shall devise a mechanism for monitoring of the withholding agents in real estate sector, enforce submission of withholding statements by the concerned and recover the due amount of tax as per law.

[AO No.36]

#### **5.6.7 Short-realization of Income Tax under Section 39 of Income Tax Ordinance 2001 - Rs 3.62 million**

According to Section 39 (1) of the Income Tax Ordinance 2001, income of every kind received by a person in a tax year, if it is not included in any other

head, other than income exempt from tax under this Ordinance, shall be chargeable to tax in that year under the head “Income from Other Sources”. Further, as per Section 7B(1)b “profit on debt” exceeding rupees five million is taxable under Section 39 as income from other sources and “small company” under Section 2(59AB) means a company which has its paid up capital plus undistributed reserves not exceeding 50 million rupees.

It was observed during audit of tax record of M/s Federal Investigation Agency (FIA) Employees Cooperative Housing Society Ltd, NTN-7225741 assessed under the jurisdiction of RTO Islamabad for the year 2023, that taxpayer declared income from profit on debt amounting to Rs 226.52 million in its income tax return for the year. The income being exceeding rupees five million is taxable @ 29 instead of @ 20 percent as other income under Section 39 of the Income Tax Ordinance, 2001. It is pertinent to mention here that taxpayer does not fall under the definition of a “small company” under Section 2(59AB) of the Income Tax Ordinance 2001, as it has paid up capital plus undistributed reserve accumulated to Rs 593.37 million as on 30<sup>th</sup> June, 2023 which exceeds the thresh-hold of fifty million as per legal provisions laid down for small company. The department was required to assess other income of the taxpayer as per law but the needful was not done. The omission resulted in short realization of income tax amounting to Rs 3.62 million.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Departmental authorities should recover the due amount of tax as per law under intimation to Audit.

[Annexure-99]

#### **5.6.8 Non-levy/recovery of penalty from non-filers of income tax returns - Rs 213.05 million**

According to Section 182(1), where any person who fails to furnish a return of income as required under Section 114 within the due date, such person

shall pay a penalty equal to higher of 0.1% of the tax payable in respect of that tax year for each day of default; or rupees one thousand for each day of default and or minimum penalty shall be rupees ten thousand in case of individual having seventy-five percent or more income from salary; or rupees fifty thousand in all other cases.

It was observed during the audit of taxpayers' data assessed under the jurisdiction of Commissioner IR, RTO Islamabad, that there are 7,620 taxpayers who were obligated to file income tax returns under Section 114 of the Income Tax Ordinance, 2001. As per data provided to audit, 4,287 taxpayers failed to file income tax returns during the tax period 2023. As such, more than 50 percent taxpayers did not made compliance of statutory provisions of tax law and concerned units also did not take notice of non-compliance of statutory provisions. This shows weak enforcement of tax returns by concerned officers/tax authorities. The assessing officers were required to invoke the provisions of Section 182, enforce returns and levy penalty amounting to Rs 213.05 million for tax year 2023.

The lapse was pointed out from March to May, 2024. The Department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to enforce income tax returns finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends that the Department shall enforce filing of income tax returns from the taxpayers, viz a viz impose and recover penalty from the non-filers of returns.

[AO. No.65]

#### **5.6.9 Non finalization of proceedings of withholding tax initiated under Section 161 / Rule 44(4) of the Income Tax Ordinance, 2001**

According to Section 161 read with Section 153(1)(a)(b)(c) of the Income Tax Ordinance 2001, every prescribed person making a payment in full or part including a payment by way of advance to a resident person or permanent establishment in Pakistan of a non- resident person, for the sale of goods, for the rendering or providing of services, on the execution of contract, shall at the time

of making the payment, deduct tax from the gross amount payable at the rates specified in the First Schedule to the Income Tax Ordinance, 2001.

It was observed during audit of tax record of M/s Aujla and Associates Town Developers (Private) Limited NTN-2476867 assessed under the jurisdiction of Commissioner IR, RTO Islamabad, that the taxpayer had undertaken a project namely Royal Palm City Housing Scheme, Gujranwala along with other services as on December 31<sup>st</sup> 2020. The taxpayer being withholding agent was required to deduct and collect tax while making and receiving payments. In this regard, a notice under Rule 44(4) of the Income Tax Rules, 2002 dated 23<sup>rd</sup> February, was served upon the taxpayer regarding default of withholding taxes for the Tax Years 2021, 2022 and 2023. In response, the taxpayer replied that said notice had been issued without basic lawful jurisdiction. The same is to be decided at the very outset before proceeding on merits of the case.

The lapse was pointed out from March to May, 2024. The department replied that the case was still under consideration of the department. RTO was requested to finalize the case at the earliest.

The DAC in its meetings held during July and December 2024 directed the field formation to finalize the legal proceedings as per law and report compliance within 45 days. Further, progress was not reported till finalization of the report.

The Audit recommends to finalize the legal proceedings besides strengthening monitoring controls over withholding agents through risk based desk audit and effective utilization of IT based systems

[AO. No.32]

#### **5.6.10 Frequent transfer of jurisdiction of builders and developers / non-obtaining of incorporation certificates from concerned RTOs**

Rule 73 (1) (b) of the Income Tax Rules 2002 require taxpayers to furnish documents and returns to the officers having jurisdiction over the cases or to such other officers, as the Commissioner may specify. Electronic filing of income tax returns and withholding tax statements shall be mandatory within due dates. On the basis of such returns and statements, the taxation officers finalize the assessment proceedings and charge tax accordingly.

Audit observed that all cases of builders and developers from the provinces of Punjab and KPK were clustered into the Regional Tax Office, Islamabad, which accumulated the number of cases to 11,243 as of June, 2023. Such a huge cluster of cases in one office was not a judicious decision which not only impaired the monitoring, assessment and recovery of taxes but also caused hardships to taxpayers. The department, in view hardships confronted by the taxpayers, re-assigned the jurisdiction of 3,702 cases to the concerned RTOs/LTOs having jurisdiction over the cases. The frequent transfer of jurisdiction of taxpayers among field offices causes undue delay in assessment and recovery of due taxes by the assessing authorities. The case of M/s Aujla & Associates Town Developers (Private) Limited Gujranwala, NTN-2476867 may be quoted as an instance, the taxpayer being withholding agent was required to deduct and collect tax while making and receiving payments. In this regard, a notice under Rule 44(4) of the Income Tax Rules, 2002 dated 23<sup>rd</sup> February, was served by the assessing authority of Regional Tax Office Islamabad upon the taxpayer regarding default of withholding taxes for the Tax Years 2021, 2022 and 2023. In response, the taxpayer replied that notice had been issued without basic lawful jurisdiction. The same is to be decided at the very outset before proceeding on merits of the case.

The lapse was pointed out from March to May, 2024. The Department did not furnish reply till finalization of the report. It was requested that position may be justified, incorporation certificates obtained from concerned filed offices of FBR to whom 3,702 cases of builders and developers had been transferred.

The para was not discussed in the DAC meeting due to non-submission of working papers by the Department.

The Audit recommends that the Department should justify the transfer of jurisdiction; get incorporation certificates from the concerned offices to ensure submissions of returns, withholding tax statements by the taxpayers, FBR may assign the jurisdiction on the basis of territorial jurisdiction to facilitate the taxpayers.

[AO. No.67]

## **Conclusion**

In Pakistan, real estate sector has been mostly a part of undocumented economy, which poses enduring challenges for the country's GDP. The undocumented transactions entail economic activities that escape from taxation by government authorities. According to data of the Economic Survey of Pakistan, the real estate sector despite enjoying tax amnesty scheme announced by government through Finance Act 2020, witnessed a constant growth of average 3.7% during last six years and 5.8 % meagre contribution to the Gross Domestic Product (GDP) during the FY 2023-24. This trend is against the general perception that the tax exemptions announced by the government for the real state sector resulted in a significant boost for the overall growth of economy.

Audit opines that periodic amnesty schemes announced by the government in the past three decades promoted the culture of non compliance of tax Laws, as people whitened their concealed assets with minimal payments of tax, without any prosecution, detention or penalty, hence tax avoidance was fuelled by irrational tax policies. According to data disclosed by the Federal Board of Revenue (FBR) 993 builders and developers availed the benefit of amnesty scheme declared for builders and developers but 95% percent of the cases who availed the scheme failed to comply with the conditionalities as contained in the scheme which resulted in a potential loss of revenue. Audit also pointed out that certain tax collecting and withholding agents while generating online computerized payments receipts (CPRs) did not disclose the Name, CNIC/NTNs and address of the taxpayers which render challans as invalid but the Inland Revenue Information System (IRIS) processed such challans which results in incorrect claim of tax credits by the beneficiaries and also promotes "*benami*" transaction as well.

In view of foregoing facts, there is a dire need to make strenuous efforts for documentation and formalization of real estate sector. This drive would not only enhance its share to Gross Domestic Product (GDP) but also a significant contribution to the national exchequer in the form of provincial and federal taxes.

## 7. Recommendations

- FBR must devise and enforce systemic validation checks while generating Computerized Payment Receipts (CPRs) in the E-Portal of Inland Revenue Information System (IRIS), to ensure filling of mandatory fields of (CPRs) for collection/deduction, deposit and accounting of withholding taxes as required under the provisions of Section 236C and 236K of Income Tax Ordinance, 2001.
- It is proposed that current format of returns should be revised to facilitate the taxpayers for the proper declaration of desired information as intended by the legislature and in line with provision of Section 100D of Income Tax Ordinance, 2001.
- FBR should enhance existing systemic Inland Revenue Enforcement Network (IREN) to real estate sector, in collaboration with housing societies and land registration authorities to develop a system on the analogy of Point of Sale (PoS) already implemented in retail sector.
- FBR in collaboration with housing societies should devise a mechanism to monitor the withholding and payment of due tax by commission agents as required under Section 233 of Income Tax Ordinance, 2001.
- FBR should devise a monitoring system to track, trace and assess the capital gain earned by the dealers of real estate and recover capital gain tax under section 37 on transactions of property.
- FBR should strengthen and enforce laws/ regulations related to *Benami* (proxy) transactions to prevent individuals from concealing property ownership through nominees or proxies.
- FBR should invest in capacity building and training for tax officials, law enforcement agencies, and regulatory authorities to enhance their capabilities in detecting, investigating, and prosecuting cases of tax evasion in the real estate sector. Promote collaboration with international counterparts to benefit from the best practices.
- Strengthen enforcement mechanisms and impose strict penalties, including fines, imprisonment, and confiscation of assets, for individuals and entities found guilty of tax evasion in the real estate sector. Ensure swift and effective prosecution of offenders to deter others from engaging in similar illicit activities.

## **CHAPTER-11 THEMATIC AUDIT ON SALES TAX MECHANISM IN THE STEEL SECTOR**

### **1.1 Introduction**

The steel industry provides essential inputs for the country's industrial and economic growth besides infrastructure development. The importance of steel in other sectors such as construction, transportation, machinery, metal products, energy and electrical equipment, and domestic appliances cannot be overstated. Steel comprises two main components: (i) iron ore and (ii) recyclable steel. The steel industry is resource-intensive; the production of iron and steel requires large factories, iron ore, energy, and labor. The high cost and low returns make it challenging for new investors to enter the market. Currently, the steel industry in Pakistan is a significant production sector, with 600 small and large mills having a combined production capacity of 3.3 million tons in 2019, which accounts for 0.18% of global production.<sup>1</sup>

Due to increased prices of steel products in domestic and international markets, the Federal Board of Revenue (FBR) raised the minimum prices of steel products through SRO 985, dated August 4, 2021. Previously, the prices of steel products were fixed by the FBR vide SRO 992, dated September 4, 2019. The FBR is authorized to set minimum prices of steel products under the proviso to clause (46) of Section 2 of the Sales Tax Act, 1990. The new prices, effective from April 20, 2023, have been set as follows: Bars at Rs 225,000/-, Billets at Rs 195,000/-, Ingots/Bala and Ship-plates at Rs 180,000/-, and Scrap at Rs 160,000/- per metric ton.

The instant report based upon Thematic Audit focuses on the collection of Sales Tax from the steel sector, its implications, and its potential impact on Pakistan's economy. The FBR clarified that the upward revision was essential due to the recent surge in local and international steel prices and to prevent potential revenue losses. The FBR has also indicated that, in the future, minimum prices will be adjusted on a quarterly basis. This policy impacts Pakistan's local industries, formal sector, and tax revenue.

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<sup>1</sup> Pakistan Credit Rating Agency (PACRA) research report September 2022.

## **1.2 Background**

Prior to the implementation of the steel price revision policy, the Special Procedure 2007 was in vogue for the payment of Sales Tax by steel melters, re-rollers, and ship breakers. As per Rule 58H (1) of these rules, every steel melter, steel re-roller, composite unit of melting, re-rolling, and mild-steel cold drawing (having a single electricity meter excluding units operated by sugar mills or other persons using self-generated electricity) shall pay Sales Tax at the rate of nine rupees per unit of electricity consumed for the production of steel billets, ingots, and mild-steel products, excluding stainless steel. This amount shall be considered their final discharge of Sales Tax liability. However, the rates of sales tax based on electricity consumption shall only apply to units consuming electric power supplied by public sector electricity distribution companies and M/s K-Electric Limited. The payment of tax by steel melters, re-rollers, composite units of melting and re-rolling, and mild-steel cold drawing shall be made through electricity bills, along with the electricity charges.

Furthermore, if the due amount of sales tax mentioned in the sub-rule is not included in the electricity bill issued to any steel melter, re-roller, or composite unit of melting and re-rolling, the respective entity shall deposit the due amount of tax for the relevant tax period at the rate of nine rupees per unit of electricity consumed, excluding the amount of Sales Tax already paid on the electricity bill, through a monthly return.

An adjustable Sales Tax at the rate of Rs 5,600 per metric ton shall be levied and collected on the import of re-meltable iron and steel scrap falling under Pakistan Customs Tariff (PCT) headings 7204.3000, 7204.4100, and 7204.4990. Meanwhile, a non-adjustable Sales Tax of Rs 5,600 per metric ton shall be levied and collected on the import of waste and scrap of compressors falling under PCT heading 7204.4940. Additionally, local supplies of such imported waste and scrap of compressors shall not be subject to sales tax. Local supplies of re-meltable iron and steel scrap shall be charged sales tax at the rate of Rs 5,600 per metric ton. Steel melters may adjust the sales tax paid on imported re-meltable iron and steel scrap against the sales tax payable through their electricity bills, as prescribed by the Board through a general order.

Henceforth, as per the prevalent new mechanism, the FBR set minimum prices of steel products under the proviso to clause (46) of Section 2 of the Sales Tax Act, 1990 for the collection and payment of Sales Tax from the steel sector.

### **1.3 Establishing the Audit Theme**

#### **1.3.1 Reasons of selection**

- The production and import of steel have increased due to rising domestic demand; however, tax collection did not enhance significantly vis-a-vis the robust activity in the sector.
- Steel sector manufacturers have been inaccurately determining the value of taxable supplies.
- The chargeability of the Sales Tax on exclusive taxable supplies has reportedly been misused in the aftermath of introducing the minimum price valuation concept.
- Taxpayers have been claiming inadmissible input tax and reducing the minimum Sales Tax liability, violating the Sales Tax General Order.
- Refunds have been determined and paid to the steel sector without exports being involved.
- There was a need to assess whether the refunds sanctioned & paid complied with the prescribed rules.
- To ascertain whether raw materials have been purchased from the registered suppliers.

#### **1.3.2 Purpose/Objectives**

The main objective of the thematic audit was to analyse the mechanism for the payment and collection of sales tax from the steel sector, its possible implications for tax revenue, economic growth, and local industries, and to assess management's compliance with the applicable laws, rules, and regulations for enhancing revenue generation.

#### **1.3.3 Scope**

The scope of the audit was to assess the taxation mechanism being administered with respect to the steel sector in the relevant formations of the Federal Board of Revenue operating in the Southern Region. The record pertaining to the Financial Years from 2021 to 2024, involving Large Taxpayers

Office, Corporate Tax Office, Medium Taxpayers Office was scrutinized to supplement the thematic audit activity. The following terms of reference were chalked out for the subject audit exercise:

- To check collection & deposit of Sales Tax by the registered persons of steel sector under the Sales Tax Act 1990.
- To check and analyse the data as per mechanism for electricity consumed for production of steel products.
- To analyse the data with respect to minimum liabilities and actual supplies made during the year as per conditions mentioned in the Thirteenth Schedule of the Sales Tax Act 1990.
- To examine the payment of Sales Tax in accordance with the value of supplies fixed as per S.R.O. 501(1)/2023 & S.R.O. 489(1)/2022, dated 05.04.2022.
- To check the admissibility of input tax credit allowed as per section 08 of the Sales Tax Act 1990.
- To check the admissibility of input tax claimed by the registered persons of steel sector as per STGO No. 12/2022 vide C.No.1(22)SS/ST-L&P/Ops/2022/80839-R, issued by the Federal Government, dated 07.04.2022 applicable from 01.04.2022.
- To examine the assessment of sales tax registered persons of steel melters, re-rollers & ship breakers.
- To check the revenue reported in sales tax returns and income tax returns and audited accounts by registered persons.
- To check and analyse the refund (Sales Tax & Income Tax) claimed and issued by the department.

**2. Legal framework governing the theme**

- The Sales Tax Act, 1990.
- Sales Tax General Order (STGO).
- SRO 992(1)/2019 dated 4<sup>th</sup> September, 2019.
- SRO 985(1)/2021 dated 4<sup>th</sup> August, 2021.
- SRO 501(1)/2023 dated 20<sup>th</sup> April, 2023.

### **3. Stakeholders and government organizations**

The key stakeholders of the thematic audit are as follows:

- The Federal Board of Revenue.
- Ministry of Industries & Production.
- Pakistan Steel Melters Association.
- Registered persons in the steel sector.
- Association of Builders and Developers.
- General public & consumers.

### **4. Role of important organizations**

The Federal Board of Revenue is responsible for tax collection in Pakistan. FBR has to review and recommend suitable (automated) processes and filing structures for income/sales tax returns and withholding statements compatible with respective laws. FBR's main task is to investigate cases of tax evasion/avoidance, which may be in the form of non/short-deduction of taxes and to take appropriate action under the law in the cases of defaulters. Federal Board of Revenue is responsible for identifying the withholding agents, facilitating the issuance of National Tax Number/Free Tax Number to unregistered withholding agents and developing an accounting policy for the appropriation of the deduction to the respective tax offices.

The Ministry of Industries & Production supports the steel sector by aligning policies with industrial and economic needs, promoting growth, and ensuring fair pricing mechanisms. It works with stakeholders to address regulatory challenges and ensure sustainable production. The Ministry's efforts help stabilize the steel industry and strengthen its contribution to national development.

The Pakistan Steel Melters Association (PSMA) represents steel manufacturers, advocating for their interests and addressing challenges related to taxation, compliance, and raw material availability. It acts as a bridge between industry players and government authorities. The association plays a vital role in policy discussions to ensure the industry's growth and competitiveness.

Registered persons in the steel sector, including melters and re-rollers, are responsible for adhering to tax regulations, accurate reporting, and timely payments. Their compliance is crucial for maintaining transparency in tax

collection and preventing misuse of tax mechanisms. These entities are key players in supporting revenue generation and strengthening the steel industry.

The Association of Builders and Developers (ABAD) represents the construction sector's reliance on steel products, advocating for fair taxation and supply chain stability. It collaborates with policymakers to ensure affordable pricing for steel and sustainable practices in the construction industry. ABAD's role is crucial in addressing the sector's challenges and ensuring housing and infrastructure development.

## **5. Organization's Financials**

The Federal Board of Revenue meets its expenditure through the Consolidated Fund of the Government of Pakistan.

## **6. Field Audit Activity**

### **6.1 Methodology**

The methodology consisted of an initial review of the available documents i.e. Income Tax Returns, Sales Tax Returns, Refund Orders, Audited Accounts etc. Following the preliminary review, the management was requested to produce the relevant record. The audit was conducted in accordance with the Income Tax Ordinance 2001, the Sales Tax Act 1990, the Sales Tax Rules 2006, and SROs issued by the FBR. The audit activity was conducted by observing the sampling of available data, whereof taxpayers from the steel sector were selected to assess the collection, accuracy of sales tax liabilities, and fairness of accounts. Sales tax and income tax returns were reviewed to express an independent opinion on the following:

- The collection and deposit of sales tax by registered persons in the steel sector under the Sales Tax Act 1990.
- Analysis of the data based on the mechanism for electricity consumed for the production of steel products.
- Minimum liabilities and actual supplies made during the year as per the conditions mentioned in the Thirteenth Schedule of the Sales Tax Act 1990.
- Payment of Sales Tax in accordance with the value of supplies fixed under S.R.O. 501(1)/2023 and S.R.O. 489(1)/2022, dated April 5, 2022.

- Admissibility of input tax credit allowed under Section 8 of the Sales Tax Act 1990.
- Verification and analysis of refunds (Sales Tax and Income Tax) issued by the FBR.

## **6.2 Audit Analysis**

### **6.2.1 Review of Internal Controls**

The implementation of statutory obligations by the department was found to be slightly inadequate in terms of curbing tax evasion and avoidance within the Sales Tax regime. The striking feature that compromised internal controls was the failure to conduct regular Post Refund Audit (PRA) for the tax years under observation. In the absence of a systematic post-audit mechanism, there is a heightened risk of fraudulent claims going undetected, thus leading to significant revenue leakage. Owing to this operational oversight, the correctness of the periodic refunds issued remains questionable. Sales Tax in the form of inadmissible input/output tax claimed by the blacklisted entities was not recovered. This failure reflects weak enforcement measures and insufficient efforts to monitor and recover taxes from high-risk entities which undermines the integrity of the tax system. Inadmissible adjustment of input tax on goods or services was made, resulting in a significant shortfall in the realization of Sales Tax. This highlights the lack of adequate checks and verification processes to ensure compliance with statutory requirements. The incorrect claiming of adjustments for credit notes led to errors in output tax computation, thus reflecting the absence of a robust internal control mechanism. The department failed to collect Sales tax from steel furnaces using locally procured scrap. This negligence occurred due to the absence of a clear policy framework to govern and regulate tax collection in this sector. The lack of a defined policy rendered the internal control mechanism inefficient and confined the department's ability to capture potential revenue from these operations. Subsequent to the disposal of fixed assets, the sales tax was not realized, thus contributing to the loss of potential revenue. Furthermore, penalties for the late filing of Sales Tax returns were not imposed that weakened the compliance enforcement and reduced the deterrence effect that penalties typically provide. These issues highlight systemic inefficiencies and procedural gaps that have undermined compliance and revenue collection efforts.

### **6.2.2 Critical Review**

Based on an analysis of the steel sector's taxation profile, it is emphatically inferred that the field formations of the Federal Board of Revenue need to bring about a paradigm shift to address tax evasion and avoidance within the system. The following key observations highlight the taxation complexities regarding the steel sector:

- The accuracy of self-assessed tax declarations, which are available in FBR's records, is not being adequately monitored. The instances of tax evasion identified in this report indicate a lack of scrutiny over such declarations, compromising the credibility of the tax assessment process.
- FBR is not effectively monitoring claims for excess tax credits or exemptions that are inadmissible under the tax laws. This oversight creates opportunities for misuse and revenue leakage.
- FBR is not reviewing income tax returns to identify individuals or entities who are liable for mandatory registration under the Sales Tax Act of 1990. This lack of scrutiny results in potential revenue losses and non-compliance with legal obligations.
- Data from third-party sources, such as utility bills, is not being adequately utilized to identify unregistered taxpayers or taxable income. Leveraging such data could significantly enhance the identification and registration of potential taxpayers.
- FBR is not effectively following up on notices issued to individuals and businesses required to register and pay taxes under the sales tax laws. This undermines enforcement efforts and allows non-compliance to persist.
- There is insufficient vigilance regarding the concealment of stocks, purchases, production, sales, and the undervaluation of taxable goods. Such practices distort the tax base and result in significant revenue shortfalls.

### **6.2.3 Significant Audit Observations**

The findings of this audit revealed that the incentive of minimum price fixation had been misused by manufacturers, who claimed inadmissible input tax in contravention of the prescribed rules. Additionally, blacklisted entities were

allowed unjustified adjustments of input tax on purchases made. Furthermore, the FBR failed to bring local suppliers of raw materials into the tax net, resulting in a loss of potential revenue. These shortcomings can be attributed to operational negligence, weak internal control mechanisms, and inefficient oversight by the relevant FBR authorities. The significant audit observations are given as follows:

**6.2.3.1 Non-conducting of Post Refund Audit for the refunds issued - Rs 708.29 million**

According to Rule 36(1) of the Sales Tax Refund Rules 2006, “After disposing of a refund, a post-refund audit must be conducted by the department for the verification of input tax payments by respective suppliers.”

During the audit of the Sales Tax record for the tax period 2022 to 2024 under the jurisdiction of the Chief Commissioner Inland Revenue, Large Taxpayers Office Karachi, it was observed that the formation processed and cleared eight cases (Annexure-1) of sales tax refund involving payments of Rs 708.29 million to the registered persons of the steel sector without conducting the Post Refund Audit.

Audit is of the view that due to the absence of a sound internal control mechanism, the PRA was not conducted, and as a result, the authenticity of the refunds could not be verified, thus rendering these refunds doubtful/irregular.

The matter was reported to the department in December 2024, but no reply was furnished until the finalization of the report.

Audit recommends providing the relevant Post Refund Audit reports for verification and if any recovery is found due, the same may be made accordingly.

(Audit Observation No. 04)

**6.2.3.2 Non-recovery of sales tax from blacklisted persons in the Steel Sector - Rs 512.01 million**

According to Section 21 of the Sales Tax Act 1990, “during the period of suspension of registration, the invoices issued by such person shall not be entertained for sales tax refund or input tax credit, and once such person is blacklisted, the refund or input tax credit claimed, whether prior or after such blacklisting, shall be rejected through a self-speaking appealable order and after affording an opportunity of being heard to such person.”

During the audit of the Sales Tax record for the tax period 2022 to 2024, under the jurisdiction of the Chief Commissioner Inland Revenue, Regional Tax Office-II Karachi, it was observed that two (02) taxpayers of the steel sector were declared blacklisted. However, these taxpayers claimed an inadmissible input tax of Rs 255.57 million and charged an output tax of Rs 256.44 million contrary to the rules.

Audit is of the view that due to operational negligence, the formation did not initiate proceedings to recover the input tax claimed and the output tax charged by these taxpayers, resulting in a loss of Rs 512.01 million to the government exchequer.

*(Rs in million)*

Name of Taxpayer	NTN #	Date of BL	Amount of Purchases	Input Tax Claimed	Output Tax Charged	Sales Tax Paid
Marjan Steel Industries	4587955	17-Jan-2022	947.369	161.053	161.372	Nil
Hashmi Steel Traders	4643915	23-Dec-2021	555.970	94.515	95.070	Nil
<b>Total</b>			<b>1503.339</b>	<b>255.568</b>	<b>256.442</b>	

The matter was reported to the department in December 2024, but no reply was furnished until the finalization of the report.

Audit recommends justifying the matter; otherwise, prompt recovery of the specified amount should be made from the blacklisted persons. Additionally, legal proceedings should be initiated against the suppliers and buyers involved, as per the rules besides monitoring the production capacity of the steel units.

(Audit Observation No. 03)

### **6.2.3.3 Inadmissible adjustment of input tax on goods & services – Rs 249.78 million**

According to Section 8 of the Sales Tax Act, read with SRO 490(I)/2004 dated June 12, 2004, “A registered person shall not be entitled to reclaim or deduct input tax paid on goods or services used, or to be used, for any purpose other than taxable supplies made or to be made by them.”

During the audit of the Sales Tax record for the tax period 2022-23, three (03) registered persons of the steel sector under the jurisdiction of the Commissioner, Inland Revenue, Zone-IV, Large Taxpayers’ Office, Karachi,

claimed input tax adjustments for goods and services. These adjustments were neither relevant to the business activities of the taxpayers nor admissible under Section 8 of the Sales Tax Act 1990, read with SRO 490(I)/2004.

Audit is of the view that due to supervisory negligence on the part of the management, the registered persons' claims were accepted, and credit was allowed, resulting in the inadmissible adjustment of input tax amounting to Rs 249.78 million. The details are given as under:

*(Rs in million)*

Sl. No.	AO #	Name of Taxpayer	NTN	Tax Period	Non-realization of Sales Tax
1	38	Faizan Steel	1226268	12/21 to 9/23	40.745
2	39	Agha Steel Industries Limited	7383402	12/21 to 9/23	66.345
3	40	Agha Steel Industries Limited	7383402	7/20 to 6/21	142.686
<b>Total</b>					<b>249.776</b>

During the DAC meeting held on 03.12.2024, the management informed that the matter is under consideration. The DAC directed to submit the compliance report by 31.12.2024, but no reply was furnished until the finalization of the report.

Audit recommends compliance with the DAC directives besides, recovering the short payment due to inadmissible input tax adjustment and the imposition of applicable penalties thereof.

(PDP No. 7283)

#### **6.2.3.4 Irregular adjustment of output tax due to incorrect claiming of adjustment of credit notes – Rs 30.01 million**

According to Section 9 of the Sales Tax Act 1990, “Where a registered person has issued a tax invoice for a supply made, and as a result of the cancellation of supply, return of goods, a change in the nature of the supply, or a change in the value of the supply, the amount shown in the tax invoice or the return requires modification, the registered person may, subject to such conditions and limitations as the Board may impose, issue a debit or credit note and make a corresponding adjustment against output tax in the return.”

During the audit of the Sales Tax record for the tax period 2022-23, three (03) registered persons of the steel sector under the jurisdiction of the

Commissioner, Inland Revenue, Zone-IV, Large Taxpayers' Office, Karachi, decreased their tax liability by claiming or adjusting credit notes in Annex-C of their Sales Tax returns without issuing a declaration debit note or obtaining acceptance of the credit notes by the second party during the tax period 2022-23. This resulted in incorrect adjustments of output tax and short payment of tax in the returns amounting to Rs 30.01 million.

Audit is of the view that due to this financial oversight on the part of the management, an inadmissible adjustment of input tax was made, and no punitive action was taken against the defaulters as per Section 33(5) of the Sales Tax Act 1990. The details are given as under:

*(Rs in million)*

Sl. No.	AO No.	Name of Taxpayer	NTN	Tax Period	Non-realization of Sales Tax
1	47	ASG Metals Limited	3788888	Feb, 2023	15.471
2	47	Agha Steel Industries Limited	7383402	Mar, 2023	7.991
3	47	International Steel Limited	3020921	Aug, 2022	6.551
<b>Total</b>					<b>30.013</b>

During the DAC meeting held on 03.12.2024, the management informed that the matter is under consideration. The DAC directed to submit the compliance report by 31.12.2024, but no reply was furnished until the finalization of the report.

Audit recommends compliance with the DAC directives besides, recovering the short payment of output tax along with the applicable default surcharge.

(PDP No. 7290)

#### **6.2.3.5 Short realization of sales tax due to inadmissible adjustment of input tax – Rs 7.95 million**

According to Section 8 of the Sales Tax Act, 1990, read with STGO No. C.No. 1(22)SS/ST-L&P/Ops/2022/80839-R, “a registered person shall not be entitled to reclaim or deduct input tax paid on: (a) goods or services used or to be used for any purpose other than taxable supplies made and any other goods or services which the Federal Government may, by notification in the official Gazette, specify.”

During the audit of the Sales Tax record of the steel sector under the jurisdiction of the Chief Commissioner, Medium Taxpayers Office, Karachi, for the tax period 2022-23, it was observed that two (02) taxpayers claimed input tax credit amounting to Rs 7.95 million. These claims were contrary to the above STGO and were not admissible.

Audit is of the view that due to the operational negligence on the part of the management, neither any legal proceedings against the taxpayers were initiated nor the recovery of the inadmissible tax was made, thus resulting in a short realization of sales tax.

*(Rs in million)*

S#	Taxpayer Name	NTN #	Tax period	Inadmissible adjustment of input tax
1	HORIZON STEEL (PVT.) LIMITED	0094262	July 2022 to June 2023	2.59
2	USMAN STEEL (PVT.) LIMITED	4416247	-do-	5.36
<b>Total</b>				<b>7.95</b>

The matter was reported to the department in December 2024, but no reply was furnished until the finalization of this report.

Audit recommends justifying the matter otherwise, the taxpayers' liability may be assessed as per the law *ibid* and recovery of specified government dues may be made along with the imposition of penalty and default surcharge, if any.

(Audit Observation No. 01)

#### **6.2.3.6 Non-realization of Sales Tax on sale of fixed assets – Rs 7.76 million**

According to Section 3(1)(a) of the Sales Tax Act 1990, "Sales tax shall be charged, levied, and paid at the rate of seventeen percent on the value of taxable supplies made by a registered person in the course or furtherance of any taxable activity carried out by them."

During the audit of the Commissioner, Inland Revenue, Zone-IV, Large Taxpayers' Office, Karachi, it was observed that four (04) registered persons of the steel sector declared the deletion of assets in their Income Tax returns for the tax year 2022-23, but did not pay the sales tax against the sale proceeds. The fixed assets referred to in these cases are goods or taxable goods and fall within the ambit of taxable supply, making them liable for the levy of sales tax.

Audit is of the view that due to this financial oversight on the part of the management, a loss of Rs 7.76 million was caused to the national exchequer in the form of the non-levying of the applicable sales tax. The details are given as under:

*(Rs in million)*

Sl. No.	AO #	Name of Taxpayer	NTN	Tax Period	Non-realization of Sales Tax
1	5	Razaque Steels Pvt Limited	704137	2022-23	6.259
2	10	International Steels Limited	3020921	2022-23	1.317
3	21	International Industries Ltd	0710735	2022-23	0.097
4	22	Faizan Steel	1226268	2022-23	0.088
<b>Total</b>					<b>7.761</b>

During the DAC meeting held on 03.12.2024, the management informed that the matter is under consideration. The DAC directed to submit the compliance report by 31.12.2024, but no reply was furnished until the finalization of the report.

Audit recommends compliance with the DAC directives besides, recovering the short payment of Sales Tax on the sale of fixed assets.

(PDP No. 7288-ST/K)

#### **6.2.3.7 Inadmissible adjustment of input tax to the steel manufacturer – Rs 0.68 million**

Section 8(1)(a) of the Sales Tax Act 1990 read with (STGO) No. 12 of 2022, restricts the adjustment of input tax on goods not related to the business activities or services used, or to be used, for any purpose other than taxable supplies made or to be made by the registered Steel Melters and Re-rollers.

During the audit of the Commissioner, Inland Revenue, Zone-III, Corporate Tax Office, Karachi, for the tax period 2022-23 it was observed that M/s Barkat Steel (NTN# 5254325) claimed input tax adjustment against the goods that were irrelevant to their business activity and no legal proceedings were initiated by the department.

Audit is of the view that due to this operational negligence on the part of the department, an inadmissible adjustment of input tax amounting to Rs 0.68 million was allowed.

During the DAC meeting held on 03.12.2024, the management informed that the matter is under consideration. The DAC directed to submit the compliance report by 31.12.2024, but no reply was furnished until the finalization of the report.

Audit recommends compliance with the DAC directives besides, recovering the short payment of tax due to inadmissible input tax adjustment along with the imposition of applicable penalties thereof.

(PDP No. 7312–ST/K)

**6.2.3.8 Inadmissible adjustment of input tax on lubricants oil - Rs 0.47 million**

According to Section 8 of the Sales Tax Act, 1990, read with STGO No. C.No. 1(22)SS/ST-L&P/Ops/2022/80839-R, “A registered person shall not be entitled to reclaim or deduct input tax paid on: (a) goods or services used or to be used for any purpose other than taxable supplies made and any other goods or services which the Federal Government may, by a notification in the official Gazette, specify.”

During the audit of the Commissioner, Inland Revenue, Zone-II, Medium Taxpayers Office, Karachi, for the tax period 2022-23 it was observed that M/s H. S. J. Metals Pvt. Limited (NTN# 5024087) claimed an irregular input tax adjustment amounting to Rs 0.467 million on the purchase of lubricating oils (PCT-2710g) that was reflected in the Sales Tax returns for the tax period of October 2022. This adjustment facility had been disallowed under the FBR’s STGO dated April 1, 2022.

Audit is of the view that due to this supervisory negligence on the part of the management, an inadmissible adjustment of input tax was allowed, thus causing a loss to the government revenue. The details are given as under:

*(Rs in million)*

S#	Tax Period	Description of Goods	Value	Sales Tax involved
1	Oct, 2022	PCT-2710g LUBRICATING OILS	2.736	0.467

During the DAC meeting held on 03.12.2024, the management informed that the matter is under consideration. The DAC directed to submit the

compliance report by 31.12.2024, but no reply was furnished until the finalization of the report.

Audit recommends compliance with the DAC directives besides, recovering the amount paid against the inadmissible input tax adjustment.

(PDP No. 7337–ST/K)

#### **6.2.3.9 Non-imposition of penalty due to late filing of sales tax returns – Rs 0.30 million**

According to Section 33(1) of the Sales Tax Act 1990, “Where a person fails to furnish a return within the due date, such a person shall pay a penalty of ten thousand rupees. However, if a person files a return within ten days of the due date, they shall pay a penalty of two hundred rupees for each day of default.”

During the audit of data available on the e-portal of sales tax profiles under the jurisdiction of the Chief Commissioner, RTO-II, Karachi, for the tax period from 2022 to 2024, it was observed that four (04) registered persons of the steel sector filed their returns after the due date. The registered persons neither paid the penalty for the late filing of returns nor was any demand raised by the formation concerned. This resulted in the non-realization of penalties amounting to Rs 0.30 million.

Audit is of the view that due to this monitoring oversight on the part of the department, the penalty as per the prescribed rules was not imposed on the defaulting registered persons.

The matter was reported to the department in December, 2024 but no reply was furnished until the finalization of the report.

Audit recommends justifying the matter otherwise, a penalty amounting to Rs 0.30 million and default surcharge, if any, may be recovered as per the rules.

(Audit Observation No. 02)

#### **6.2.3.10 Non-imposition of 18% Sales Tax against the steel furnaces using local scrap material**

According to Section 4(1) (c) of the Federal Board of Revenue Act, 2007, “The Board shall exercise powers to adopt modern effective tax administration methods, information technology systems and policies in order to consolidate

assessments; improve processes, organize the registration of taxpayers, widen the tax base, and make departmental remedies more efficient.”

During scrutiny of the steel sector’s taxation record, it was observed that the Federal Board of Revenue did not frame a consolidated Sales Tax collection policy for the steel producers using local scrap procured from unregistered suppliers, thus contributing to a potential revenue loss. The key industry players in the steel sector claim that tax-compliant companies using imported scrap pay a total tax of 18%. In contrast, those using locally procured scrap pay only a minimal fraction of the tax.

The matter was also highlighted in The Express Tribune dated October 23, 2024, whereby it was reported that the government is losing nearly Rs 8 billion in taxes every month due to the Federal Board of Revenue's reluctance to issue SRO for imposing 18% Sales Tax on steel furnaces using locally procured scrap.

Audit is of the view that the FBR's ineffectiveness in streamlining a taxation policy in this context is causing a huge loss to the government exchequer.

The matter was reported to the department in December, 2024 but no reply was furnished till the finalization of this report.

Audit recommends framing a comprehensive policy at the earliest to safeguard potential government revenue.

(Audit Observation No. 05)

## **7. Departmental Responses**

Apart from a few observations, most were discussed in the DAC meeting held on 03.12.2024 whereof, decisions against the respective paras were taken accordingly.

## **8. Recommendations**

Diligent assessment of taxpayers’ sales tax liability under Section 11 of the Sales Tax Act 1990 and recovery of government dues along with penalties and default surcharges, if applicable, as per law.

- Developing a mechanism to ensure effective monitoring of sales tax collection. This mechanism should include a certification process for production capacity utilization by the steel sector.

- Conducting post-refund audit on a regular basis to ensure the authenticity of the refunds issued periodically.
- Establishing a proper mechanism and issuing a Statutory Regulatory Order (SRO) to notify changes in the tax regime for steel producers using locally procured scrap from unregistered suppliers.
- Monitoring the commercial activities of the blacklisted entities to avoid pilferage of revenue.

## **9. Conclusion**

The steel industry serves as a cornerstone of economic growth, significantly contributing to construction projects, infrastructure development, and industrial expansion. Given its critical role, it is imperative to improve the efficiency of monitoring sales tax collection within this sector. The Federal Board of Revenue has been striving diligently to attract optimum revenue from the steel sector. However, owing to operational and monitoring deficiencies, the intended benefits in the form of enhanced revenue collection could not be achieved properly. To streamline this process, the issuance of Statutory Regulatory Orders (SROs) based on valuation policies should be made on a quarterly basis, ensuring timely updates and effective oversight. The introduction of the valuation regime to bolster Sales Tax collection and facilitate better monitoring of taxation within the steel sector was a productive step on the part of the tax administration, however the lack of accurate assessment compounded by the failure to impose penalties on defaulters and inefficient measures to bring the local scrap producers under the ambit of tax net undermined the efficacy and intended outcomes of the valuation regime. To achieve the regime's objectives and ensure its successful implementation, the Federal Board of Revenue must prioritize the enhancement of internal controls. Historically, these controls have been either insufficient or entirely absent, necessitating immediate attention to address existing gaps and strengthen regulatory oversight. By doing so, the valuation regime can effectively fulfill its purpose of increasing transparency and improving tax compliance in the steel sector. This report sheds light on various shortcomings, operational mismanagement and lapses in internal controls. The findings highlighted above emphasize the need for adopting and executing stringent actions to curtail revenue pilferages and tax evasion.

## CHAPTER-12 OTHER SIGNIFICANT ISSUES

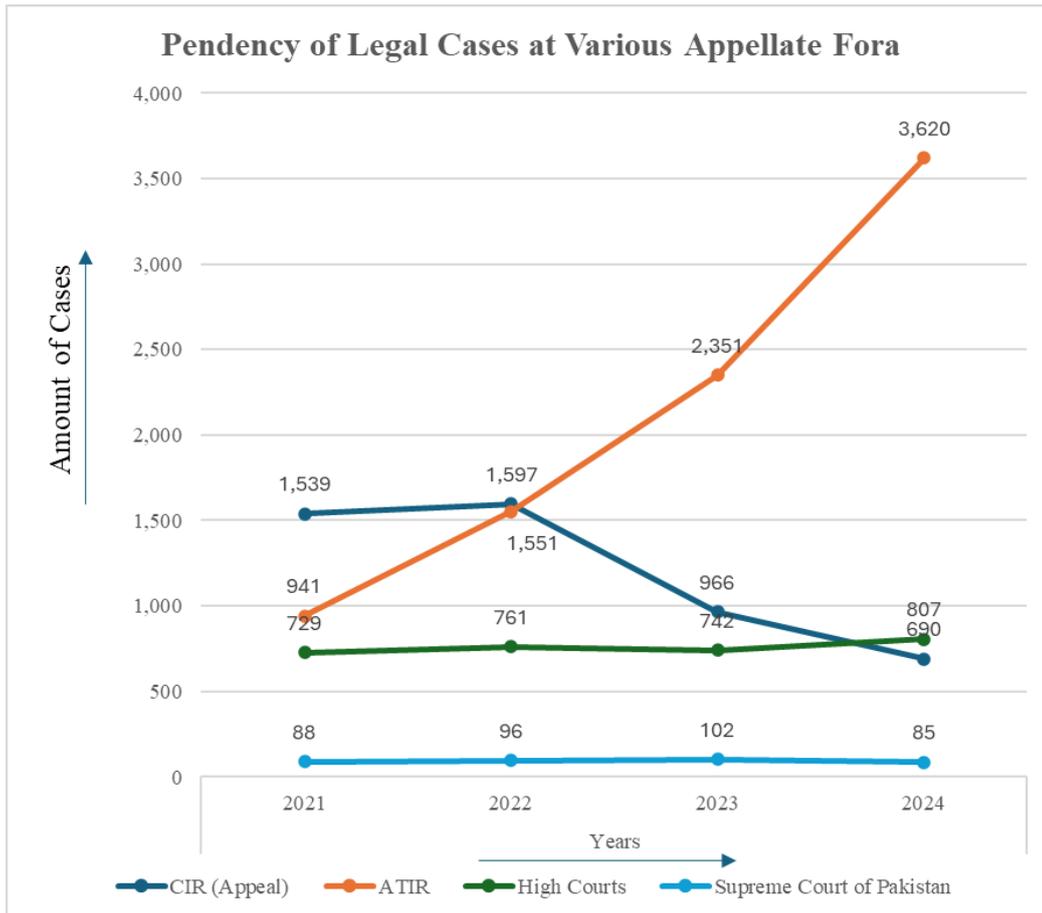
### 12.1 Huge pendency of legal cases at various Appellate fora resulting in blockade of potential tax revenue

The Income Tax Ordinance, 2001 provides the procedures for processing of appeals at various fora which include, appeal to the Commissioner Inland Revenue under Sections 127 to 129 (Taxpayer only); Appeal to Appellate Tribunal under Sections 131 & 132 (both taxpayers and the department); and Reference/Appeal to High Court and Supreme Court under Section 133. Further, Section 45B of the Sales Tax Act, 1990 provides the procedure for appeals as, any person, other than the Sales Tax Department, aggrieved by any decision or order passed by Inland Revenue Officer, may prefer an appeal to the Commissioner Inland Revenue (Appeals).

Execution of Performance Audit of “Dispute Resolution Mechanism of FBR” was planned during Audit Year 2022-23 but no record was produced throughout the year despite consistent correspondence and meetings with FBR authorities. In the following year, although there were repeated requests by this office for production of auditable data/record to this office, only summarized data/information about pending litigation cases was provided by Legal Wing IR (FBR) vide C.No 1(76)-SS(A&A)/2023 dated July 15, 2024 and C.No.1(76)-SS(A&A)/2023 dated October 30, 2024 as tabulated below;

*(Rs in Billion)*

Appellate For a	Year							
	2021		2022		2023		2024	
	No. of cases	Amount						
CIR (Appeal)	19,797	1,539	22,716	1,597	21,474	966	18,179	690
ATIR	58,440	941	62,986	1,551	71,509	2,351	70,637	3,620
High Courts	9,409	729	9,550	761	9,458	742	10,173	807
Supreme Court	2,813	88	3,271	96	3,027	102	3,485	85
<b>Total</b>	<b>90,459</b>	<b>3,297</b>	<b>98,523</b>	<b>4,005</b>	<b>105,468</b>	<b>4,161</b>	<b>102,474</b>	<b>5,202</b>

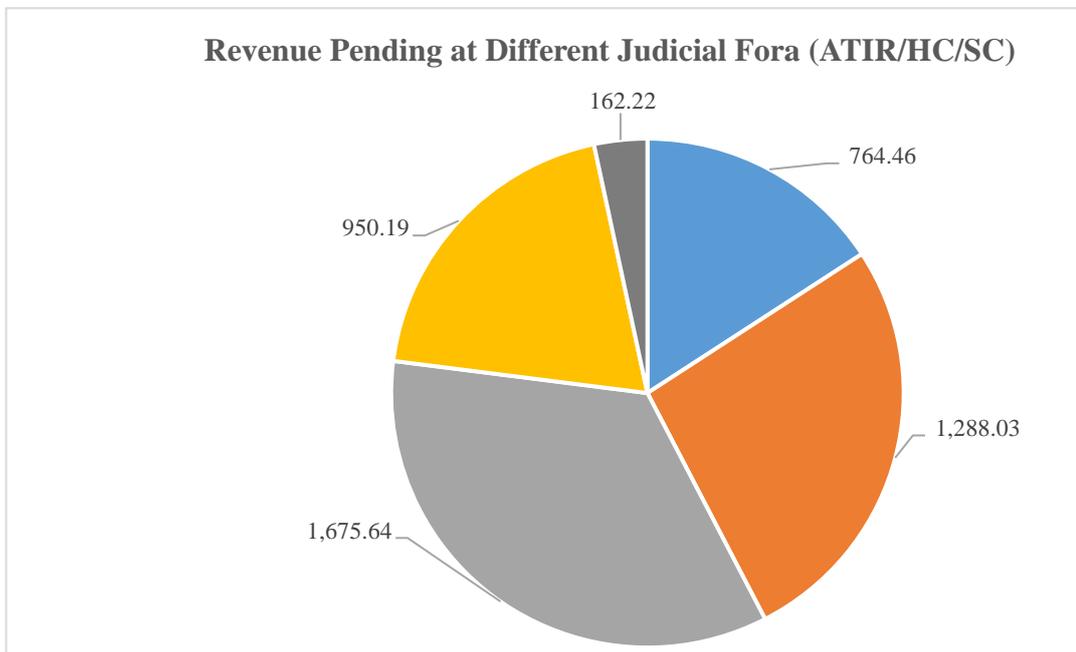


The above table and graph clearly depicts that the cases pending at Appellate Tribunals comprised the major chunk of all cases of FBR stuck due to litigation. On the basis of summarized data provided by FBR, following points/discrepancies were observed:-

- i. There were large number of pending cases involving billions of rupees of potential tax revenue which showed that initial assessments made by the tax authorities were mostly challenged in different Appellate forums including CIR (Appeal) and ATIR which further transpires that most of the taxpayers were not satisfied with the initial assessment made by the tax authorities.
- ii. Alternate Dispute Resolution Committees (ADRC) formed at field tax offices level were not functioning effectively to enable taxpayers to get their disputes settled in lesser time and without incurring litigation cost.

- iii. Analysis of the information provided also revealed that 31,143 cases involving revenue of Rs 906,362 million were annulled by CIR Appeals, meaning thereby 28% cases assessed by the adjudicating authorities were annulled by the CIR (Appeals) which needs to be justified. Whereas, 78% of the cases decided against the department in Supreme Court of Pakistan and 46% in High Courts which depicts poor pursuance of cases at highest appellate fora.
- iv. It is worth mentioning that despite such huge pendency of cases, cash rewards were also disbursed to the CIR (Appeals), its staff and departmental representatives responsible for pursuance of cases for early finalization at appropriate fora.
- v. Audit further observed that cases involving billions of rupees were stuck up at different appellate fora since long as indicated in the following graph:

*(Rs in billion)*



The matter was reported to the FBR in November, 2024 but no reply was received till finalization of this report

During the DAC meeting held in January 2025, the department informed that request had been submitted to respective forums for early fixation and

disposal of cases. The legal wing further opined that instructions on the matter of ADRC could be issued by IR Operations Wing. The DAC directed the legal wing to give a comprehensive reply and get the stance verified from Audit within seven days. No further progress was reported till finalization of the report.

The Audit recommends to:-

- Provide data related to aging of the pending cases at each fora along with number of cases/amount decided in favor/against the department;
- Devise a mechanism for proper assessment of the cases to reduce the number of cases decided against the department; and
- Monitor the proper functioning of ADRCs for early settlement of cases within the domain of prevailing laws and regulations

[DP No. 23688]

## **12.2 Non-simplification of tax return forms & procedures and delayed refunds**

According to Concept Paper on Facilitation and Taxpayer Education (FATE) provided by FBR vide letter No. 18/(S)/IT/2015/Pt.II/13391-R dated 31.01.2020, FATE Wing of FBR was created in April, 2002 to improve tax compliance through better facilitation, improvement in tax laws, and procedures creating an atmosphere conducive for doing business. As per Concept Paper, FBR being a public service organization was also required to develop its “*service delivery standards*” for timely processing of taxpayers refunds and redressal of other issues confronted by the business community.

It was observed during audit of FATE Wing for the FY 2020-21 that the income tax return form was complex. It comprised of several pages enlisting therein multiple sections of enacted provisions of income tax law and other applicable rules. There were numerous tax rates for various withholding tax deductions. Tax return form on FBR’s system (IRIS) was usually uploaded only a few days before the last date of filing returns. Consequently, when the taxpayers rushed to log on for filing of returns, they had to face problems like hanging of the system due to huge traffic of taxpayers using the IRIS system simultaneously. On the other hand, individual taxpayers were not properly trained/ educated for filing of online tax returns.

Audit further observed that as per data provided by Prime Minister’s Delivery Unit, (PMDU) of FATE Wing Islamabad, there were 17,933 complaints

lodged by the taxpayers regarding delayed payments of refunds during the FY 2019-20. As per test check of audit on sample basis, 1/3<sup>rd</sup> of all new complaints pertained to cases of delay of refund payments only.

The facts narrated above indicate that FATE wing failed in fostering an environment for transformation to simpler procedures and return forms and other SOPs for ease of the taxpayer in submission of their tax returns, withholding tax statements etc. Further, due refunds were delayed by the department as indicated by the Prime Minister's Delivery Unit.

The lapse was pointed out during March to April 2020. The FATE wing replied that simplifications of tax laws, rules and procedures is responsibility of Policy wing and payment of refund is monitored by Operations wing of FBR.

The DAC, in its meeting held on 26<sup>th</sup> January 2021, directed the FATE Wing to install a system to improve return forms for better understanding of taxpayers besides arranging outreach training programs. The DAC further directed the FATE Wing to coordinate with the concerned wings to ensure timely processing of refunds and plausible justification should be provided by the tax authorities in cases of delayed refunds.

The Audit recommends that FATE Wing should in collaboration with field tax offices make efforts for simplifying the return forms. FATE Wing must enhance the capacity of IRIS system in coordination with PRAL and redress the delay in payment of refunds through automation.

(Para Nos. 05 & 06 of AIR on FATE Wing)

### **12.3 Weak performance of Broadening of Tax Base Wing of FBR in terms of real increase in tax revenue**

FBR established Broadening of Tax Base wing (BTB) in 2013 to bring new taxpayers on the tax roll and to ensure the filing of returns by them. This wing is also responsible to coordinate and create a link or liaison with the organizations holding data of sizeable financial transactions, obtaining such data sets and utilizing the same to broaden the tax base. BTB wing collected data of high-value financial transactions of selected high-net-worth individuals from various third-party sources and transmitted it to the Regional Tax Offices to include these persons on the tax roll and obtain their returns.

FBR has claimed that during tax year 2024, taxpayers filed 5.215 million income tax returns as compared to 2.959 million tax returns for the tax year 2023

exhibiting 76% increase in tax filers whereas, the net increase in tax revenue during 2024 as compared to previous tax year 2023 has been found only 30%. However, Audit has observed that most of the taxpayers are filing tax returns just to avail the benefit of low tax rates for filers such as on buying and selling of movable and immovable properties etc. It was also observed that tax to GDP ratio in 2016-17 was 10.6% while tax to GDP ratio in 2023-24 was 8.7% which shows 2% decline in tax to GDP ratio.

It is pointed out that FBR has all kind of source data appearing on *Malomaat* Portal of IRIS which contains information about potential taxpayers who got industrial electricity connections, have history of foreign travelling, possess vehicles of more than 1500 cc etc. but the real potential of tax revenue from these taxpayers is not being realized as these taxpayers are filing nil returns with zero payment of actual tax liability.

Audit has already highlighted the following significant issues in its Special Audit Report on BTB for the year 2016-17, which is still awaiting compliance by the FBR.

1. Non-registration of 1807 persons having industrial electricity connections liable to be compulsory registered under the Sales Tax Law. (Para 1.1)
2. Non-registration/filing of returns by 702 industrial electricity connection holders and 992 gas industrial/commercial connection holders liable to be compulsory registered under Sales Tax Law as well as non-registration/filing of returns by 297 gas industrial connection holders who were liable to be registered under Income Tax Law. (Paras 1.2, 1.3 & 1.4)
3. Non-registration/filing of returns by 744 persons having motor vehicles of engine capacity beyond 1500CC. (Para 1.5)

The matter was brought to the notice of the department to provide update on all the issues reported by the audit in its Special Audit report on BTB for the year 2016-17. The department replied that BTB wing had made consistent efforts which included policy measures and enforcement mechanisms for broadening of tax base.

The DAC in its meeting held in January, 2025 directed the department to submit a comprehensive reply and get its stance verified from Audit and report progress to Audit within fifteen days. No further progress was reported till finalization of the report.

Audit recommends that:-

- FBR and its field formations should compulsorily register the potential taxpayers by using data of industrial electricity/gas consumers, registration of vehicles and obtaining history of foreign travellers available on *Malomaat* Portal besides provision of access to auditors to relevant data portals under mutually agreed data sharing protocols.
- FBR should improve internal control environment to enrol new taxpayers in coordination with other institutions i.e. NADRA, motor registration authorities, property registration authorities and other withholding agents and enforce legal proceedings to enhance revenue from potential taxpayers

[DP No. 23689]

#### **12.4 Inefficient performance and weak monitoring of the FBR Track and Trace System**

Rule 150ZF (Chapter XIV-B) of the Sales Tax Rules, 2006 specifies for electronic monitoring, tracking and tracing of production, import and supply-chain of the following goods, on real time basis, hereinafter referred to as the specified goods, namely tobacco products, beverages, sugar, fertilizer, cement; petroleum products and steel sector. Further, Rule 150ZQN provides that the Board shall establish Inland Revenue Enforcement Network (IREN) which shall be responsible for combating evasion and leakages of taxes and duties payable on specified goods, which shall coordinate with enforcement units and concerned field formations.

FBR introduced the Track and Trace system to increase tax compliance and reduce tax evasions by tracking the production, movement and sale of goods in four sectors *viz* tobacco, sugar, fertilizer and cement. During data analysis of track and trace system, Audit observed that:-

- i) Inland Revenue Enforcement Network (IREN) reported an amount of Rs 2,358 million as duty/taxes evaded but only recovered Rs 145 million during the period from July 2023 to June 2024. This depicts ineffective and weak monitoring on the part of IREN which was specifically created by the FBR under Rule 150ZQN of Sales Tax Rules 2006, for combating evasion and leakages of taxes and duties payable on specified goods.

- ii) IREN reported that they had conducted 671 raids all over Pakistan during the period July 2023 to June 2024. However, only 06 business premises were seized and 04 FIRs lodged on account of illicit trade activities by the registered persons. Further, no substantial improvement in revenue has been observed as a result of IREN activities. This shows weak performance on the part of IREN to control tax revenue leakages.
- iii) The Project Director of IREN is responsible to arrange and carry out audit of the track and trace system every year as specified in the Rule 150ZQP of the Sales Tax Rules, 2006. However, no evidence of any such examination or reports was shown to Audit, which shows weak and ineffective monitoring by the IREN.
- iv) IREN reported that they have formed 35 squads all over Pakistan for the period July 2023 to June 2024 to monitor the track and trace system installed in the manufacturing units, however, no evidence of its performance in combating evasion and leakages of government revenue was provided to Audit.

The matter was brought to the notice of the department in November, 2024. In response, FBR reported that majority of the amount relates to tobacco sector wherein no one claimed ownership of confiscated goods. Audit disagreed with the contention and asked for documented/comprehensive reply in all four sectors i.e. sugar, cement, fertilizer and tobacco.

The DAC, in its meeting held in January 2025, directed the Project Director (IREN) to give a detailed reply regarding the efficiency of system in different sectors for avoiding tax evasion and under reporting of overall production as well as control system to ensure fair and transparent reporting of sector wise production of all four segments of track and trace system within fifteen days. No further progress was reported till finalization of the report.

Audit Recommends that:

- Track and Trace System should be effectively implemented in cement and beverages sectors without any further delay.
- A mechanism should be evolved for periodic review and assessment regarding effective implementation of track and trace system across different sectors of industry.

[DP No.23761]