# PSX FEDERAL BUDGET PROPOSALS

# FY2020-21

PAKISTAN
STOCK EXCHANGE
LIMITED

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# INTRODUCTION

Pakistan's capital market saw robust growth over the years in terms of its market capitalization, which was around PKR 8 trillion on January 30, 2020 but as a result of global downturn of events due to Corona Virus pandemic that spiraled down the market capitalization to around PKR 5.7 trillion on April 01, 2020. This has led to uncertainty and pessimism surrounding Pakistan's national economic indicators. The first half of fiscal 2020 showed some clear signs of a path towards economic recovery, however, considering the existing situation, the journey towards sustainable long term growth is expected to take time, the turnaround efforts are well under way.

Globally, the Coronavirus has severely increased in reach, causing major disruptions to economic activity and it has been reported that the IMF has also significantly downgraded its global growth outlook for 2020 from 3.3 percent growth previously to below zero.

Keeping in mind the chronic macro-economic stability challenges, low savings and investment rates, underdeveloped rural economy, digitalization of financial transactions and the emerging connectivity with China and other neighboring economies, Pakistan has immense potential given implementation of strong structural reforms in the capital market.

The government's fiscal policies and reforms will continue to shape the path to encourage manufacturing, exports, and discourage unnecessary imports. Much work still needs to be done to enhance the ease of doing business, digitize the economy through innovation, and strengthen and diversify the export base.

We believe that in the coming years, Pakistan's capital market has immense potential for growth, and with the introduction of advanced products and our investment in world-class trading infrastructure, PSX remains committed to building the capacity and trust required for capital formation and financial inclusion.

As much as favorable tax treatment, investors need a stable and predictable tax environment. Government of Pakistan must consider adopting long term measures to promote savings and investment and development of the capital market.

In order to achieve its objectives, PSX wishes to present proposals for the Federal Government's Budget 2020. These proposals essentially focus on some impediments and disincentives that have crept into the development of the capital market, as well as the documented corporate sectors.

All the proposals outlined below are primarily designed to remove the disincentives, the incidence of double and at times multiple taxation that are penalizing capital formation, which is essential for our corporate sector to be able to compete effectively in the world. Most proposals are revenue neutral and in cases, likely to increase the government's revenue.

The core principle of our proposal is aimed at increasing the size and depth of the capital market by incentivizing listing of new capital without impacting government revenues. In view of the above, we are presenting the following proposals for the kind consideration of the Ministry of Finance and the Federal Board of Revenue.

# EXECUTIVE SUMMARY

| S. NO. | DESCRIPTION | PROPOSAL |
|---|---|---|
| 1. | INTRODUCTION OF REGISTERED SAVINGS AND INVESTMENT ACCOUNTS | *It is proposed that the Government of Pakistan introduce a mechanism and regulatory structure for the launch of registered savings and investment accounts (RSIAs) to help channel savings towards productive investments.*<br>*RSIAs will help bring capital from the large undocumented sector into the formal economy. Further, it is also crucial that firm guarantees be offered that contributions be subject to full amnesty – aside from AML and Terrorist Financing issues due diligence.* |
| 2. | FUNDING THE FEDERAL GOVERNMENT EMPLOYEES PENSION SCHEME | *The government should start funding its pension liabilities to avert a future pension crisis and encourage capital formation in Pakistan. An adequately funded pension scheme would offer old age benefits to retired employees at public sector enterprises and government workers, without putting burden on the annual budget. Further, it is recommended that a certain percentage of the funded pension scheme be invested in the capital markets.* |
| 3.1 | ELIMINATE / REDUCE CGT FOR NEXT 24 MONTHS OR AT A MINIMUM ALIGN RATES OF CAPITAL GAINS TAX ON DISPOSAL OF SECURITIES WITH OTHER REGIONAL EXCHANGES AND OECD COUNTRIES OF THE WORLD | *Eliminate / reduce CGT for next 24 months or at a minimum align rates of capital gains tax on disposal of securities with other regional exchanges and OECD countries of the world (Annexure B).* |
| 3.2 | ALIGN THE RATES OF CAPITAL GAINS TAX ON DISPOSAL OF EQUITY SECURITES WITH RATES OF CGT ON DEBT SECURITIES FOR NON-RESIDENT COMPANIES | *Align the rates of capital gains tax on disposal of equity securities of non-residents with that of debt securities for non-resident companies having no permanent establishment in Pakistan.* |
| 3.3 | DEFINITION OF "SECURITY" SEC. 37A(3) I.T. ORDINANCE, 2001 | *In order to nullify the Judgement of the Sindh High Court dated 04-03-2016 namely Khalid Mansoor Vs FBR and 3 others and in the interest of the capital markets, PSX proposes that shares of a company disposed of, in the tax year for which the company has the status of a Public Company, shall be deemed to be securities with effect from the date of acquisition, irrespective of the status of the Company at the time of acquisition of the said shares.* |

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| 3.4 | SEC. 37A READ WITH SEC. 58 & 59 | *It is proposed to allow carry forward of losses, for 6 years rather than for 3 years as stated in Proviso of sub section 5 of section 37A of the Income Tax Ordinance, 2001.* |
| 4. | TAX TREATMENT ON CREATION OF UNITS OF EXCHANGE TRADED FUNDS | *It is proposed that in order to facilitate the market for Exchange Traded Funds, transfer of Portfolio (basket of securities) from Authorized Participants (AP) to ETF's Account should not be treated as disposal and therefore holding period of ETF constituents be carried forward to the ETF, upon conversion of Portfolio Deposit to ETF units, for the purpose of CGT calculation.* |
| 5. | REDUCTION OF WITHHOLDING TAX ON INCOME FROM MARGIN FINANCING TRANSACTIONS | *It is proposed to reduce the rate of withholding tax on the gross income earned on MF transactions from 10% to 2.5%.* |
| 6. | RATIONALISATION OF WITHHOLDING TAX ON DIVIDENDS | *Government should introduce a mechanism to remove the double taxation of company's profits - once in the hands of the company and once in the hands of shareholders as dividends - such that the effective tax rate on dividends is on par with profit on debt.*<br>*Rationalize the current tax rate on dividends to make it equal to the tax rate on profit from debt.*<br>*Provided that there should be no withholding tax on dividends up to Rs. 100,000 per annum.* |
| 7. | BRING REIT DIVIDEND TAX IN LINE WITH OTHER MUTUAL FUNDS | *Applicable rate of tax on dividend by a REIT scheme should be levied as it is applicable for mutual funds.* |
| 8. | TAX CREDIT FOR COMPANIES LISTED ON STOCK EXCHANGE | *The tax rate should be permanently lowered for listed companies, by giving tax credit of 20% of tax payable for those companies that meet the prescribed requirements including a minimum free float of 25% throughout.* |
| 9. | ENHANCED TAX CREDIT FOR LISTED SMALL AND MEDIUM ENTERPRISES (SME) | *In order to encourage small and medium enterprises to get listed on the SME Board, it is proposed that the rate of tax for such listed SME companies be permanently lowered by giving tax credit of 50% of tax payable.* |
| 10. | TREATMENT OF UNREALIZED GAIN ON SALE OF IMMOVABLE PROPERTY TO A REIT SCHEME | *The tax exemption on sale of immovable property to both types of REIT schemes (Development and Rental), which was available prior to Finance Act,* |

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| | | *2015 should be restored and made available up to June 2025.* |
| 11. | DISPARITY IN FBR & SECP RULES RELATING TO SHARIAH COMPLIANCE | *The Shariah compliance criteria under the income tax laws be modified to make it practically possible to meet it. This will help the promotion and development of Islamic capital markets by encouraging new listings of companies on PSX through mobilizing resources towards faith-based investor savings.* |
| 12. | PROVINCIAL SALES TAX ON SERVICES – JURISDICTION ISSUES TO BE SETTLED IN COUNCIL OF COMMON INTEREST | *The wordings of the laws enacted by the Sindh Revenue Board, Punjab Revenue Authority and Khyber Pakhtunkhwa Revenue Authority are overlapping. The matter being of equal relevance to all the provinces and affecting the entire Services Sector, may be placed on the agenda of the Council of Common Interests so that a sharing formula for each province can be devised.* |
| 13. | REQUEST FOR CONSISTENT AND LONG TERM TAX POLICIES | *Government of Pakistan must move away from short term measures and frequent changes to tax treatment and adopt long term measures to promote savings and investment and development of the capital market.* |