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Withdrawal of zero-rating regime

BUSINESS RECORDER Withdrawal of zero-rating (under Statutory Regulatory Order 1125) to the five key export-oriented sectors (textile, leather, carpets, surgical and sports goods) in the Finance Act 2019 was necessary as the Pakistani negotiating team had committed its withdrawal as part of the prior conditions to the International Monetary Fund (IMF) under the 39-month 6 billion dollars bailout package. Ironically, however, the man who revealed this to the Standing Committee on Commerce and Textiles was none other than the Advisor to the Prime Minister on Commerce, Abdul Razzak Dawood, who had reportedly urged the government, albeit unsuccessfully, not to withdraw this facility at the present time given a woeful decline or stagnation in exports.

Withdrawal of zero-rating regime implies compelling the manufacturing sector to pay and then claim refund of sales tax paid by them on their procurement for exports. Furthermore, in the case of textiles specially the manufacturing sector is charged sales tax on the retail price of its product as the Federal Board of Revenue (FBR) has failed to register the retailers and wholesalers and therefore there are gaping holes in the sales tax net. Withholding taxes account for over 70 percent of all direct tax collections in this country and for this the FBR relies heavily on withholding agents for collection. Different rates of tax withholding on acquisition of different goods and services have resulted in a maze. With passage of time, the cost of compliance of this regime has become significant and is beyond reach of Small and Medium Enterprises (SMEs). It is also one the major impediments in the way of movement from informal to formal sector of the economy.

The IMF website uploaded a press release dated 12 May 2018, the day the staff-level agreement was reached, stating that "the budget will aim for a primary deficit of 0.6 percent of GDP supported by tax policy revenue mobilisation measures to eliminate exemptions, curtail special treatments, and improve tax administration." However, some special treatments have been accorded to some favoured sectors such as real estate.

Be that as it may, the budgeted export package is estimated at around 40 billion rupees - 35 billion rupees under the duty drawback of taxes order 2016-17 (as a component of development outside PSDP), and another 5 billion rupees as a component of grants to others which in turn is a component of current expenditure (with the bulk earmarked for Ehsaas programme). It is unclear whether the IMF would insist on withdrawing these allocations given that the IMF's press release specifies a market-based exchange rate as a prior condition and stipulates "facilitating trade" as a priority which, without any special treatments/exemptions may well imply exclusive reliance on the exchange rate to enhance exports.

The latest export data released by the Pakistan Bureau of Statistics (PBS) indicates that exports declined by 1.72 percent in May 2019 compared to May 2018; however exports rose from 2.094 billion dollars in April 2019 to 2.95 billion dollars in May 2019 – a rise of 0.38 percent. Disturbingly, however, total exports from July-May 2019 were 21.26 billion dollars against 21.33 billion dollars in the corresponding period of the year before reflecting a decline of 0.30 percent.

To conclude, any further decline in exports would seriously compromise the country's ability to meet our foreign exchange requirements from borrowing, including the bailout package from the IMF. We are sure that the government is aware of this and hope that they have a 'Plan B' for taking appropriate as well as timely mitigating measures.

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