

June 1, 2018

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General

The Parliament of Pakistan, the National Assembly and Senate, has passed 31st Amendment to the Constitution of Islamic Republic of Pakistan. Through this amendment, Articles 1, 246 and 247 of the Constitution relating to 'Tribal Areas' have been amended.

This note briefly describes the effect of that amendment on the tax status of entities and persons residing in these areas and the continuation of certain concessions to existing entities as decided by the Economic Coordination Committee of the Cabinet on May 31, 2018.

Republic and its territories

Under Article 1 of the Constitution 'Republic' of Pakistan is a Federation of Provinces of Baluchistan, Khyber Pakhtunkhwa (KPK), Punjab and Sindh. Under the same Article the territory of Pakistan also includes 'Federally Administered Tribal Areas' and territories as or may be included such as PATA.

Article 246 of the Constitution specifies the areas which are territories to be treated as Tribal Areas for the purposes of the Constitution. These areas have been specified in **Appendix A** to this note.

Applicability of Tax Laws

All the Federal tax laws such as Income Tax Ordinance, 2001, Sales Tax Act, 1990, Federal Excise Act, 2005 and Customs Act, 1969 are applicable to 'Whole' of Pakistan that in principle includes all territories of Pakistan including tribal areas as described in earlier paragraphs. Same is the case with the Provincial tax laws *inter alia* sales tax on services.

Basis of Non-Applicability in the past

Though the Acts passed by the Parliament on any matter including taxes are applicable throughout Pakistan as defined in aforesaid paragraph however by way of special provisions contained in Article 247(3) of the Constitution no act of Parliament or the Provincial Assembly as the case may be was applicable on the areas referred to as 'Tribal Areas' as identified in Article 246 of the Constitution. Accordingly, by way of the provisions contained in Article 247(3) read with preamble of the respective tax legislation, such laws were not applicable on persons and entities located / residing in the 'Tribal Areas'. Resultantly such entities and persons were not subject to provisions of income, sales, customs or excise laws and provincial taxes. This included provisions relating to withholding on payments made by persons / entities and branches residing and located in that areas.

Change by 31st Amendment to the Constitution

Parliament in its last session, on May 28, 2018 passed 31st Amendment to the Constitution. As a result of this amendment, Article 247 of the Constitution has been omitted from the Constitution and certain amendments have been made in Article 246. This means that such areas will now be treated as part of Federation of Pakistan if such areas form part of any province as referred above. By way of another amendment, the Provincial Assembly of KPK, by two third majority, has included the areas previously being Federally Administered Tribal Areas as part of Province of KPK.

PATA territories shall form part of the Province of KPK or Baluchistan as the case may be.

On the removal of Article 247(3) the non-applicability of taxation laws on these territories has finished. Now such territories are subject to all Acts of the Parliament as part of a province of Pakistan.

Effect of the Amendment

Resultantly, taxation laws as referred above have become applicable on territories previously referred to as 'Tribal Areas'. The laws will be applicable prospectively. There will be no retrospective application.

Nevertheless, exemption from tax for entities on the income established in these areas will finish in the period after 31st Amendment. This will also include application of withholding provisions.

Decisions of Economic Coordination Committee of the Cabinet

It has been reported in the press that ECC of the Cabinet of Pakistan in its meeting held on May 31, 2018 decided to continue certain concession and immunities to persons and entities in FATA and PATA. The highlights of the same as reported in the press are as under:

- 1) Exemption of income tax on profits and gains of existing businesses conducted by individuals for a period of five years. These businesses however need to be registered with FBR by 30th September 2018.
- 2) Exemption from sales tax to the retailers to facilitate the general consumers.
- 3) Domestic consumers of electricity would be exempted from sales tax on domestic consumption of electricity.

- 4) Federal Excise Act 2005 shall replace the erstwhile Central Excise Act 1944.
- 5) Non customs paid vehicles would be allowed to be used in erstwhile FATA/PATA for a period of five years ending on 30th June 2023. However, these vehicles will not be allowed to cross over to other areas of the country. On the expiry of the five years' relaxation period, the vehicles would be regularized on payment of leviable duty and taxes.
- 6) Exemption from all withholding taxes, except on salary.
- 7) Any person seeking to set up new industrial undertaking is granted exemption from Income Tax subject to prior approval of the ECC.

Details of exemption provided by the ECC are expected to be notified in near future.

This therefore implies that entities being industrial undertakings in FATA and PATA will continue to avail exemption as provided in the existing taxation laws. New entities will require specific exemption. New businesses by individuals will be taxable. Practical aspects of such changes would require consideration.

There will be no exemption for salary income for persons residing and exercising services in the areas of FATA and PATA and the employers are required to withhold tax with immediate effect. The income for the period prior to 31st Amendment will however remain exempt from tax.

The Provincial Government of KPK and Baluchistan would have to provide concessions and immunities as provided by the Federation through ECC if they intend to continue the present status relating to provincial taxes for a certain period/ entities.

Karachi: June 1, 2018

APPENDIX A**TRIBAL AREAS**

246. **Tribal Areas.** - In the Constitution, -

- (a) "Tribal Areas" means the areas in Pakistan which, immediately before the commencing day, were Tribal Areas, and includes -
- (i) the Tribal Areas of Balochistan and the Khyber Pakhtunkhwa Province;
 - (ii) the former States of Amb, Chitral, Dir and Swat;
 - (iii) * * * * *
 - (iv) * * * * *
- (b) "Provincially Administered Tribal Areas" means -
- (i) The districts of Chitral, Dir and Swat (which includes Kalam) the Tribal Area in Kohistan district, Malakand Protected Area, the Tribal Area adjoining Mansehra district and the former State of Amb; and
 - (ii) Zhob district, Loralai district (excluding Duki Tehsil), Dalbandin Tehsil of Chagai district and Marri and Bugti tribal territories of Sibi district; and
- (c) "Federally Administered Tribal Areas" includes -
- (i) Tribal Areas adjoining Peshawar district;
 - (ii) Tribal Areas adjoining Kohat district;
 - (iii) Tribal Areas adjoining Bannu district;
 - (iiia) Tribal Areas adjoining, Lakki Marwat district;
 - (iv) Tribal Areas adjoining Dera Ismail Khan district;
 - (iva) Tribal Areas adjoining Tank district.]
 - (v) Bajaur Agency;
 - (va) Orakzai Agency;]
 - (vi) Mohmand Agency;
 - (vii) Khyber Agency;
 - (viii) Kurram Agency;
 - (ix) North Waziristan Agency; and
 - (x) South Waziristan Agency.