



Stimulus Package for Construction Sector

Proposed Measures & ValYou Insights

Index



3

Preamble

4

A) Cost of Doing Business – Reduction in Duties & Taxes

9

B) Ease of Doing Business – Business Friendly Laws & Procedures

11

C) Financing Needs – Reduction in Financing Rates

12

Additional Considerations



Preamble

By the time these lines are put into publication, as per John Hopkins University, over 1.3 million population of the world has been diagnosed with COVID-19 and this disease has taken more than 76,000 lives all over the world. This disease which is now officially declared as pandemic has driven 1/3rd of world population into lockdown. It is feared that this disease will result one of the worst economic recession world has ever seen in its recent history following by major job losses, unprecedented industry shutdowns, huge budgetary deficits, hyper-inflation and the worst out of all i.e. food shortages, God Forbids.

Governments all over the world are battling hard to reduce the spread of this disease and also announcing financial relief packages for

their people and businesses. Prime Minister of Pakistan has recently announced that his government has allocated USD 8 billion as Coronavirus relief package. Various administrative and policy measures are being taken to ease out the situation for the businesses and people including softening the regulatory compliances, reducing tax and interest rates, allowing extension in compliance deadlines and removing procedural delays of the system. Likewise, Prime Minister also announced a major relief package for construction sector on April 3, 2020. Here below, we are presenting key initiatives announced by the government including our insights:



A) Cost of Doing Business

Reduction in Duties & Taxes

| Measure | ValYou Insights |
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| <p>1. Regularization of Undisclosed Wealth</p> <p>Investment in Real Estate sector is proposed to be exempted from section 111 of ITO, 2001 thereby source of investment will not be asked if investment made till June 30, 2022.</p> <p>This scheme is only applicable for investment made in:</p> <ul style="list-style-type: none">• First purchase of constructed property; or• Purchase of land for construction (not or investment / holding purposes) or construction on already purchased land <p>Further, the subjected property can be used for commercial and non-commercial purposes.</p> | <p><i>Previously, similar amnesty was granted to corporate sectors for their investment made on or after January 1, 2014 to 2019 period under clause 86 of Part IV of 2nd Schedule of ITO, 2001. Now, effectively, this facility is going to be extended for another 3 years with the expanded beneficiary list as it is now proposed to include all sectors whether corporate or not.</i></p> <p><i>Although, it is still unclear that will any tax liability be associated with the regularization of this investment but considering recent amnesty schemes launched by this and earlier governments, government may come up with some strings attached thereto including levitation of a tax otherwise declarant under previous amnesty schemes may raise a voice of foul play since they declared their assets by payment of their tax liability.</i></p> <p><i>While approving this policy, government has to take into the implications of the anti-money laundering and countering terrorism financing guidelines/provisions. Further, it is expected that public officer bearers and politicians would also be excluded from the list of qualifying persons for this scheme.</i></p> |



A) Cost of Doing Business

Reduction in Duties & Taxes

| Measure | ValYou Insights |
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| <p>2. Construction Sector is Declared Industry Benefits of Industrial Undertakings are now proposed to be available for Construction sector also.</p> | <p><i>Construction sector will now be able to claim various tax credits/exemptions provided under section 23A, 65B, 65D, 65E unless exceptions provided therein.</i></p> |
| <p>3. Reduction in Business Income Tax</p> <ul style="list-style-type: none">• Fixed tax regime is proposed in place of NTR• It is proposed that Tax rate will be levied on the basis of land / area measurement and thus Builders and Land-Developers may declare ten times of the actual tax paid hereunder as their imputed income in their wealth statements.• Reduction in tax liability by 90% for Builders of low cost housing projects and/or projects developed by Naya Pakistan Housing and Development Authority is proposed | <p><i>So with this proposed change, section 7C and 7D of ITO, 2001 are come to life again which were previously applicable only for tax year 2017.</i></p> <p><i>But for enforcement purpose, a question may arise that at what stage this tax will be collected i.e. at project completion stage or in installments after certain periods during the construction period of the project. This issue needs to be fixed for avoiding any future anomalies.</i></p> <p><i>A reference to the definition of Low cost housing project is given in clause 9 of Part III of ITO, 2001 i.e. projects worth not more than Rs. 2.5 million. But we believe that this definition is neither fair nor comprehensive as a price tag is fixed without determining the minimum area and keeping this tag uniform for all types of constructed properties in all areas of Pakistan.</i></p> |



A) Cost of Doing Business

Reduction in Duties & Taxes

| Measure | ValYou Insights |
|---|--|
| <p>4. Reduction in Capital Gain Tax</p> <ul style="list-style-type: none">• For computation of capital gains, immoveable properties be revalued• Rate of tax to be reduced in proportionate to the increase in the valuation.• Constructed property: Holding period is being proposed to reduce from 4 years to 3 years for availing reduction/exemption from CGT.• Real Estate / Open Plot: No reduction in holding period for claiming full exemption from CGT but a reducing CGT rate scale is proposed from year 4 and onwards.• First house purchase, sale and construction is exempted from all taxes. | <p><i>Proposed measures would reduce CGT liability and thus will clear the passage for some extent which was choked with the revenue measures of recent past as claimed by this sector.</i></p> <p><i>Incentive for the first house purchase is a significant relief but the concept of first house purchase could be mis-utilized therefore, needs to be properly accounted for while approving this package.</i></p> |

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| <p>5. Waiver from Withholding Tax</p> <p>Builders & Land-Developers are now only required to withhold tax from:</p> | <p><i>This will encourage B2B business model in cement and steel industry i.e. direct purchase of material from manufacturers and perhaps, this is also intended to corporatize steel sector.</i></p> |
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A) Cost of Doing Business

Reduction in Duties & Taxes

| Measure | ValYou Insights |
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| <ul style="list-style-type: none">All Corporate vendorsNon-corporate suppliers of cement, steel and certain services like shuttering & electrical | <p><i>On the other hand, this will further strengthen non-corporate culture in industries like Paint, Tiles, Sanitary and Electrical equipment and consequently, may further add to their miseries of competing with undocumented and non-formal sector.</i></p> |
| <p>6. Reduction in General Sales Tax</p> <p>Reduction in sales tax and excise duty is proposed on construction material including cement.</p> | <p><i>This will reduce cost of construction and will bring down prices of constructed properties. This is an encouraging move to revive this sector.</i></p> |
| <p>7. Provincial Sales Tax on Construction Services</p> <ul style="list-style-type: none">Fixed sales tax rates of Rs. 50 per square foot for Builders and Rs. 100 per square yards for Land-Developers are proposed.As a fixed sales tax rate on area of constructed property or land is proposed therefore, it is proposed that all other construction services be covered under Zero Tax Regime | <p><i>This change is proposed in line with the change proposed in taxing revenues of Builders and Land-Developers. This will bring an ease to the sector and enforcement authorities and it is also expected that this will reduce tax burden too and may also reduce cost of construction.</i></p> |



A) Cost of Doing Business

Reduction in Duties & Taxes

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|--|---|
| <ul style="list-style-type: none">• Low cost housing by federal and provincial authorities are exempted from tax. | |
| <p>8. Provincial Excise & Taxation</p> <p>Standard rate of 2% on valuation is proposed in place of multiple taxes and duties imposed by provincial and municipal authorities.</p> | <p><i>Primarily, this will make the life easy of construction sector and may also bring some savings for this sector.</i></p> |



B) Ease of Doing Business

Business Friendly Laws & Procedures

| Measure | ValYou Insights |
|---|---|
| 1. Construction Industry Development Board It is proposed to establish a board for development of construction industry. | <i>Mainly these boards are constituted to promote their subject matters, to provide support to government in policy making and to extend their assistance to public sector. Normally, these boards are constituted of ex-officio members of government machinery (in this case perhaps representation from Ministry of Housing & Works would play the key role) and representatives from private sector. Currently, we have other similar boards operating in Pakistan like Board of Investment, National Information Technology Board and National Tourism Coordination Board etc.</i> <i>Representative bodies from construction sector or industries directly/indirectly associated with this sector should send their nominations to authorities for protecting their interests.</i> |
| 2. High-rise construction policy A formal policy on high-rise Construction will be approved. | <i>With this announcement, Government has reiterated its focus to promote high-rise buildings. Government has been focusing on this policy since they came into power for combating environmental and urbanization issues and promoting low cost housing.</i> |
| 3. Legal Issues / Delays in Civil Proceedings <ul style="list-style-type: none">Establishment of special benches of courts | <i>This contentious issue is considered one of the major impediment in the growth of this</i> |



B) Ease of Doing Business

Business Friendly Laws & Procedures

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|---|---|
| <ul style="list-style-type: none">Changes in civil proceedings laws | <p><i>sector as there are many civil proceedings which remained unresolved since ages.</i></p> <p><i>This will be a tough task as federal government has to take all provinces and judiciary on board.</i></p> |
| 4. Misc. Measures <ul style="list-style-type: none">E-stamping system in all provincesNew/updated master plan / zonesIntroduction of new zoning in-lawsReduction of approval time to 45 daysOnline automated system for granting approvals | <p><i>Punjab has already been using e-stamping system and it receives a positive feedback from the general public too as this brought more transparency and security. In line with the experience of Punjab, other provinces are also encouraged to digitize their processes.</i></p> |



C) Financing Needs

Reduction in Financing Rates

| Measure | ValYou Insights |
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| <p>Lower/Concessional Interest Rates</p> <ul style="list-style-type: none">• Green field projects are proposed to be charged an interest rate of 7%.• 100,000 low cost housing projects are proposed to be charged as low as 6%. | <p><i>These measures will improve liquidity in the construction sector and will also reduce cost of doing business too. SBP should now bring adequate changes in its prudential regulations and should also increase threshold of financing limits for construction sector.</i></p> |



Additional ValYou Suggestions

Although this package contains various initiatives those will have a positive impact on the construction industry and business sectors associated with it but the following measures should also be considered for extending the warmth of support further from the policy makers:

- Geographical area specific 100% tax exemption should also be granted for rural area economic uplift as this package may be deemed by some as a package for urban pockets.
- Limit for deductible allowance on profit on debt u/s 60C of ITO, 2001 i.e. needs to be linked with the policy rate. In 2016, this limit was determined at Rs. 2 million when policy rate was 5.75% but it is not increased ever since though policy rate has been increased more than double.
- In 7th Schedule of ITO, 2001 (Banking Company Taxation), currently tax reduction is given on bank's portfolio relating to low cost housing project. This should also be enhanced and the whole construction sector should be included therein.
- While encouraging banks to finance more low cost housing projects, government should also extend its refinancing facility to banks for financing first house purchase/construction taking into account middle class community needs as well. It can limit the maximum exposure per account or even can fix a reasonable maximum value of these middle class housing projects.
- Under Clause 126O of Part I of 2nd Schedule, profits and gains of companies operating as Green Field Industrial Undertaking are exempt uptill June 30, 2024. Though not mentioned specifically, we expect this exemption would also be available to Green Field Construction Projects.
- Maximum value used to determine low cost construction projects should be uniform for taxation as well as refinancing purposes as stated before that in Income Tax Law this limit is Rs. 2.5 million and in SBP guidelines it is Rs. 3 million.

The End



Disclaimer

Information contained in this document is only for the guidance purposes and all the insights / commentary provided therein are the viewpoint of the ValYou which are developed considering a general perspective therefore, application of these guidelines in a particular scenario / case may produce incorrect results.

We tried our best to provide accurate information but there could be some errors or omissions therefore, we advise you to refer the original document / statute first before proceeding further.

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