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PUNJAB REVENUE AUTHORITY
FINANCE DEPARTMENT
GOVERNMENT OF THE PUNJAB
5-B, DANEPUR ROAD, GOR-I,
LAHORE
Dated:22nd August, 2013



Circular No.06 OF 2013 **(Punjab Sales Tax)**

Subject:- **LEVY OF PUNJAB SALES TAX ON TOLL MANUFACTURING -----**
CLARIFICATION REGARDING.

Punjab sales tax has been levied on the "services provided in respect of manufacturing or processing on toll or job basis (against processing on conversion changes)" with effect from 01-07-2013. Some business quarters/circles have contended that toll manufacturing (industrial vending) cannot be treated as services because of the definition of the "manufacture" and "manufacturer" given in section 2(16) & (17) of the Sales Tax Act, 1990. Punjab Revenue Authority has examined the matter and is pleased to observe as follows:

- (i) The description and listing of services given in the First Schedule of the Punjab Sales Tax on Services Act, 2012 is minimum. Punjab government can levy sales tax even on services not mentioned in the said schedule that any transaction which is not a supply of goods is service is the major underlying principle of the definition/treatment of such transaction as service.
- (ii) Under item 49 of Part-I of the Fourth Schedule of the Constitution of the Islamic Republic of Pakistan, 1973, the Federation can levy taxes only on the sales and purchases of goods (whether goods are) imported, exported, produced, manufactured or consumed, which means that the Federation cannot levy sales tax simply on the manufacturing or production of goods *per se*. Only their sale and purchase can be taxed. Imports are in fact purchases at the hand of importers and are taxed on the basis of destination principle.
- (iii) Under section 2(38) of the Punjab Sales Tax on Services Act, 2012, an explanation has been added that "a service shall remain and continue to be treated as service regardless whether or not rendering thereof involves any use, supply or consumption of any goods either as an essential or as an incidental aspect of such rendering". This explanation was/is imperative because there are several categories of services where goods are involved for the purpose of rendering of services. Treatment of goods for processing purposes falls under the use of goods for vending purposes.
- (iv) It is clear from the language of section 3 (1) of the Sales Tax Act, 1990 that Federal sales tax is payable only on the taxable supplies (besides goods imported into Pakistan). Under section 2(41), taxable supply means a supply of taxable goods by an importer, manufacturer, wholesaler, distributor or retailer. Again under section 2 (33), the

pivotal principle for any transaction to become a supply is that it must be a sale or the transfer of the right to dispose of goods as owner, which means "ownership title" must be transferred from seller to buyer, otherwise the transaction is not a supply for the purpose of Federal sales tax.

- (v) Under toll manufacturing, ownership title of goods is not transferred to the vendor under any circumstances, which means a transaction for the purpose of toll manufacturing can never be treated as supply. Put more succinctly, the ownership of both input goods (raw materials, semi-finished products or components etc) and output goods (processed or finished products) remains with the principal throughout the performance or the execution of the toll manufacturing contract, whether written or otherwise.
- (vi) The very use of the words "conversion charges" in sales tax jargon several years back indicates that the goods are not priced for sale purposes between the principal and the vendor. No commercial transaction not involving price of goods (whether actual or open market price) for the purpose of transfer of ownership title can be treated as supply (or sale).
- (vii) Under the goods-related sales tax regime, the concept of manufacture or manufacturer has been used not for the purpose of taxation as such. Historically, this concept was used to facilitate categorization of registered persons for registration, declaration data management and tax concessions' management purposes. Even a time has been experienced in Pakistan when several industrial vendors once started predicating that their industrial processing activities do not fall in the category of manufacturing and they be treated as engaged in service business so as to keep them away from sales tax liabilities accruable in respect of processed goods. This eventually culminated in the amendment of the definition of the words "manufacture" and "manufacturer". Such amending measures were adopted only because of the fact that during those days the Provinces were not exercising their constitutional rights to levy and collect sales tax on services at their own level. Now the position has changed and Federal sales tax regime is no more in position to manipulate the thin lines of distinction between "commodity" and "service" in its favor. Under no stretch of imagination sales tax is a "production tax" so far as the constitutional scheme of fiscal powers or assignments in Pakistan is concerned.
- (viii) Several websites define and explain the features of toll manufacturing (also cited as toll processing and sometimes even as contract manufacturing). According to the available definitions, toll manufacturing is defined as performing a specific service or services on customers' goods or products against payment of agreed charges. The vendor, in fact, on the basis of manufacturing or processing infrastructure available with him sells to the principals, the facility of availing the production-related benefits from such infrastructure against a specific amount of charges (sometimes internationally known as vending fee or processing fee). Vending contracts may carry different conditions including delivery of finished products directly to the buyers of the principals. Sale invoices are however, required to be

and are always issued by the principals. The vendors generally issue invoices to their principals only to the extent of service charges.

3. Thus all such industrial businesses/concerns who are providing services in respect of manufacturing or processing on toll or job basis against processing or conversion charges are required to pay Punjab sales tax in respect of such charges. Any interpretation contrary to this legal position will not be accepted for the purpose of Punjab sales tax. The vendors are entitled to avail tax adjustment in respect of inputs (both goods and services-related) used for the purpose of such services subject to the provisions of the Punjab Sales Tax on Services (Adjustment of Tax), Rules, 2012. Similarly, their principals are reciprocally entitled to avail input tax adjustment against their Federal sales tax liabilities, if any.


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- (vi). All Presidents of Chambers of Commerce and Industry in Punjab.
- (vii). All Presidents of Tax Bar Associations in Punjab.