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Strengthening Self-Assessment in Pakistan to Achieve Higher Level of Voluntary compliance

by
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Abstract

In Pakistan, income tax is an important source of revenue for the government to balance the budget. Income tax is collected via voluntary payments, collection on demand and withholding taxes. However, share of voluntary payments in gross income tax collection though improved in the early years of introduction of universal self-assessment scheme, has been declining in the recent periods. In this article, the author discusses the various aspects of self-assessment system with a focus on voluntary compliance and concludes that voluntary compliance has not yet taken roots in the socio-economic and political set-up of Pakistan. Measures to strengthen self-assessment system to achieve enhanced level of voluntary compliance have also been discussed.

1. Introduction

Many countries have introduced self assessment for income taxation to encourage voluntary compliance to engender more efficient and cost effective tax administration. Pakistan adopted universal self assessment for all taxpayers in 2002/03 to ensure voluntary compliance for income tax collection.¹ Under the old tax law, there was no voluntary compliance, and in principle, official assessment was employed to determine the taxable income. Practically, all taxpayers with the exception of companies, could avail self assessment scheme announced separately each year by the Central Board of Revenue (CBR), now Federal Board of Revenue (FBR).

However, based on a decade's experience, it appears that voluntary compliance has not taken root in the socio-economic and political set-up of Pakistan. The share of voluntary payments in gross income tax collection after showing phenomenal improvement from about 32.8% in 2002/03 to about 47.7% in 2006/07, has been declining (Table-1). More importantly, the share of this important source in gross income tax has reached minimum (28.5%) in the recent past.

Table-1: Share of Voluntary Payments in Gross Income Tax Collection

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¹ See section 121 of the Income Tax Ordinance, 2001.

Years	Gross Income Tax (Million PKR)	Voluntary Payments (Million PKR)	Share of Voluntary Payments in Gross Income Tax (%)
	(A)	(B)	(A/B)
2002/03	164,407	53,895	32.8
2003/04	178,207	66,543	37.3
2004/05	202,801	73,803	36.4
2005/06	243,736	87,358	35.8
2006/07	347,385	165,736	47.7
2007/08	393,782	145,616	37.0
2008/09	461,239	141,680	30.7
2009/10	559,698	165,801	29.6
2010/11	629,102	196,066	31.2
2011/12	831,908	237,362	28.5

Source: Central Board of Revenue / Federal Board of Revenue Year Books

The main problems of the income tax system in Pakistan are: (i) the lower income tax-to-GDP ratio, (ii) the lower tax base, (iii) failure to curb evasion, and (iii) failure to bring new forms of incomes in the tax net.¹ Others include (iv) too many tax exemptions and concessionary tax rates, (v) generous array of tax credits, and (vi) striking imbalance between adjustable and final (presumptive) withholding taxes.² Insufficient administration and staff is another weakness of the income tax system in Pakistan.

Thus setting up of a simple and broad based income tax system is crucial to the development of a better tax administration³, which has long been a concern of many countries. The best tax administration is not simply that which collects the most revenues; facilitating tax compliance is not simply a matter of adequately penalising non-compliance; tax administration depends as much on private as on public actions (and reactions); and there is a complex interaction between various environmental factors, the specifics of substantive and procedural tax law, and the outcome of a given administrative effort.⁴

¹ V. Ahmed and C. O'Donoghue. Redistributive Effect of Personal Income Taxation in Pakistan. Working Paper No. 0143, March 2009, p. 6, available at http://aran.library.nuigalway.ie/xmlui/bitstream/handle/10379/363/paper_0143.pdf?sequence=1 (accessed on 26 January, 2013).

² W. Thirsk. Tax Policy in Pakistan: An Assessment of Major Taxes and Options for Reforms. Working Paper 08-08, December, 2008, available at <http://aysps.gsu.edu/isp/files/ispwp0808.pdf> (accessed on January 26, 2013).

³ T. K. Sarker. Improving Tax Compliance in Developing Countries via Self-Assessment System s- What could Bangladesh Learn from Japan? Asia-Pacific Tax Bulletin Vol. 9, No. 6 June 2003.

⁴ R. M. Bird. Administrative Dimensions of Tax Reform. Asia-Pacific Tax Bulletin, P.135, March 2004, available at <http://unpan1.un.org/intradoc/groups/public/documents/unpan/unpan015761.pdf> (accessed on 26 January, 2013).

Understanding of the macro-economic indicators of the economy of Pakistan is considered to be crucial for assessing the scope of income tax policy.

Pakistan's gross domestic product (GDP) averaged 3% over the period of 2007/08 to 2011/12.¹ In terms of the sectoral contribution to GDP agriculture accounts for 21%, services for 54%, manufacturing for 19% and others (largely oil, gas, mining and quarrying) for 6%. Agricultural income is not taxable under the federal tax laws of Pakistan.

With a current population of 177 million² these growth rates have been translated into per capita income of \$1372 or PKR 121,173.³ However, the minimum wage is PKR 7,000 per month or PKR 84,000 per annum.

With a work force of approximately 59 million, agriculture accounts for about 45%, manufacturing 16%, construction 7%, wholesale and retail trade 17%, transport/storage and communication 5%, community/ social and personal services 11% of this labour force, respectively.

For the financial year 2011/12, GDP was PKR 20,653 billion. The overall fiscal deficit was 6.6% of GDP as the total revenue stood at 12.4% of GDP while the total expenditure was 19.1% of GDP,⁴ almost all of this expenditure is attributable to federal government.

The share of tax revenue in the overall national revenue was 9.9% of GDP. The contribution of federal taxes was 9.4% of GDP and of provincial taxes only 0.5%.⁵

The federal tax revenues are raised from direct and indirect taxes. The share of direct taxes in the overall national tax revenues was 3.5% of GDP and of indirect taxes 6.4% of GDP. Income tax is the major source of direct revenue, whereas federal excise duty, sales tax and customs duty are main sources of indirect tax revenues in Pakistan.

The contribution of direct taxes in the total federal tax receipts was 39% the year 2011/12. Indirect taxes comprise the remaining tax share of 61% and, within that sales tax contributes 43%, federal excise 6.5% and customs duty 11.5%, respectively.

¹ Percent annual GDP growth rate was 3.7, 1.7, 3.1, 3.0 and 3.7, respectively for the financial years 2007/08, 2008/09, 2009/10, 2010/11 and 2011/12, available at <http://www.tradingeconomics.com/pakistan/gdp-growth> (accessed on 5 January, 2013).

² B. Hassan and T. Sarker. Reformed General Sales Tax in Pakistan. *International VAT Monitor* November/December 2012. P.417

³ See Economic Survey of Pakistan 2011/12, available at http://www.finance.gov.pk/survey/chapter_12/01-GrowthAndStabilization.pdf (accessed on 5 January, 2013).

⁴ In absolute numbers, Pakistan's fiscal deficit was PKR 1,369 billion because total national revenue was PKR 2,567 billion and the total national expenditure was PKR 3,936 billion. See, Table 1, Summary of consolidated federal and provincial budgetary operations, 2011/12, note 5.

⁵ The tax revenue was PKR 2,053 billion. The contribution of federal taxes was PKR 1,946 billion and of provincial taxes PKR 107 billion. See, note 5.

2. An Overview of Income Tax System in Pakistan

Institution

Income tax in the undivided India (now consisting of Pakistan, Bangladesh and India) was introduced for the first time in 1860 via Income Tax Act, 1860. However, a new Income Tax Act was introduced in 1886, which was replaced by Income Tax Act, 1918. In 1922, a new Income Tax Act was adopted, which provided complete machinery and procedure for assessment. In Pakistan, this act was used, albeit with modifications, until 1979, when Income Tax Ordinance, 1979 was introduced. Later in 2002/03, this ordinance was repealed and new Income Tax Ordinance, 2001 with the one of the objectives of broadening the self-assessment system.

The CBR was created in 1924 through the Central Board of Revenue Act. The CBR was converted into FBR in 2006 through the Federal Board of Revenue Act. There are two executive wings of the FBR -the Inland Revenue Service (IRS) and Pakistan Customs Service (PCS). So income tax along with general sales tax (GST) and federal excise duty (FED) is administered by the IRS wing of the FBR.

This wing of the FBR conducts field operations under one roof of Regional Tax Offices (RTOs) and Large Taxpayer Offices (LTUs). The RTOs and LTUs are headed by the Chief Commissioner Inland Revenue. There are five functional divisions each headed by a commissioner Inland Revenue. These include: (i) Enforcement and Accounting, (ii) Audit, (iii) Facilitation & Taxpayer Education, (iv) Legal, and (v) Information Processing.

Besides these functional divisions, there are specialized offices: (i) the Directorate of Intelligence & Investigation, Inland Revenue tasked with broadening of tax base, financial investigation, economic and fiscal intelligence; (ii) the Directorate General of Internal Audit, Inland Revenue tasked with seeking evidence whether revenue is assessed and collected according to law and errors and omissions are avoided; (iii) the Directorate General of Training & Research, Inland Revenue tasked with conducting training of officers/officials of Inland Revenue Service and carrying out tax related research; and (iv) the Directorate General of Withholding Taxes for management and collection of withholding taxes.

A typical executive functional division has the following structure.

Commissioner Inland Revenue

Additional Commissioner Inland Revenue

Deputy/Assistant Commissioner /Inland Revenue Officer

Auditor /Inspector Inland Revenue

Processes

Under the old tax law, official assessment was made to determine the taxable income. Every year, the CBR announced self assessment scheme for all medium to large taxpayers with the exception of companies.¹ However, Income Tax Ordinance, 2001 introduced much needed changes in the tax administration procedure. Universal voluntary tax compliance for all taxpayers was introduced for the first time. The self-assessment procedure was simplified, and the submission of tax return under self-assessment scheme together with the due taxes is suffice and treated as assessment order. The new provisions also provide for a system of random or parametric selection of cases for audit of income tax affairs through computer ballot.² Besides, the Commissioner Inland Revenue has also been empowered for conducting audit of the income tax affairs of taxpayers.³

3. An Assessment of Self-Assessment System in Pakistan

Under self-assessment system, a taxpayer is required to assess his tax liability using a tax return form in which he declares his gross income, allowable deductions, and net income.⁴ This tax return must then be filed either electronically or manually with the tax authority together with prescribed annexure, statements, and documents.⁵ Thus the basic feature of a self-assessment scheme is that it is the taxpayer rather than the income tax authority that assess his tax liability. There is no checking of the return prior to assessment. However, under the provisions of section 120(3) of the Ordinance, the Commissioner is empowered to issue notice for any deficiency in a return, notified to the taxpayer in writing, which if not removed within given time can render a return invalid as if it was never filed.

A number of studies have highlighted the merits of self-assessment system compared to an official assessment system. According to Sarker (2003), self assessment system is more cost effective as it only selects exceptional cases for audit, it encourages an early and timely income tax collection, and it reduces corruption by reducing contacts with taxpayers. Therefore, the main objectives supporting the introduction of self-assessment system include reducing tax authorities' burden of assessing

¹ Based on the legal sanction given under Section 59 of the old tax law, every year prior to filing, FBR would issue a circular for Self-Assessment Scheme of the year during July to September period that laid terms and conditions to avail the scheme. Companies however, remained excluded from the purview of Self-Assessment Scheme.

² See Section 214C of the Income Tax Ordinance, 2001. Audit of income tax affairs or tax examination is an investigation performed at RTOs and LTUs to check whether the content of a tax return based on taxpayer records is appropriate or not.

³ See Section 177 of the Income Tax Ordinance, 2001.

⁴ Sarker, note 5, P. 8.

⁵ See Section 114 of the Income Tax Ordinance, 2001.

tax returns by improving voluntary compliance and thus increasing tax collection efficiency.¹

However, self-assessment is difficult to implement effectively. For instance, approximately 70% of taxpayers who are required to file tax return under self-assessment in 1948 in Japan were subjected to correction or determination by the tax authorities for non-filing or under-filing of returns, which resulted in additional revenue nearly half of the total revenue from self-assessment income tax. As a result, there were large number of appeals by taxpayers and a huge amount of tax delinquency.²

Therefore, for effective implementation of self-assessment system, certain critical factors needed are: (i) effective audits crucial to prevent non-filing or under-filing tax returns, (ii) strong criminal tax investigation system to detect fraud or non-compliance, (iii) an appropriate level of exemption threshold to keep small traders out of tax net and to prevent them from the hassle of record keeping, and (iv) enhancing the level of knowledge and understating of the taxpayers about income tax procedures.

In Pakistan, the main objectives to be achieved from self-assessment system include: (i) creating mutual confidence between taxpayers and tax collectors; (ii) relieving taxpayers from procedural tangles of the official tax assessment system and at the same time to ensure better tax collection; (iii) enforcing increased voluntary compliance through tax education about the merits of the self-assessment system; (iv) reducing litigation; and (v) utilizing the efforts of the tax administration in more constructive manner through educating new taxpayers, detecting concealment and improving overall efficiency.

Income Tax Return Filers

The voluntary compliance improved significantly during the early years of self-assessment scheme. The scheme was termed successful in confidence building between the taxpayers and tax collectors, and in reducing the direct interface between the two. At the same time, the scheme proved to be effective in broadening the income tax base. Tax returns increased from 1.03 million in 2004/05 to 1.81 million in 2006/07, indicating 75.7% growth in the number of return filers. Similarly, the payments from this source also increased substantially from PKR 66.5 billion to PKR 165.7 billion during the same period, indicated a growth of 149.2%. However, since 2007/08 the performance of voluntary compliance is showing a declining trend. Number of income tax returns has decreased steadily from historic highest figure of 1.81 million in 2006/07 to currently 1.29 million in 2011/12, indicating a decline of 28.7% during this period (Table-2).

¹ M. R. Palil. Tax Knowledge and Tax Compliance Determinants in Self Assessment System in Malaysia. The University of Birmingham, 2010, P. 5.

² N. Usui. Penetration of the Self-Assessment System for Income Tax Half-A- Century's Experience in Postwar Japan. June 2002, P.7.

Table-2: Trends in Income Tax Returns

Year	Income Tax Returns (In millions)	Increase/Decrease (%)
2003/04	1.03	-
2004/05	1.23	19.4
2005/06	1.49	21.1
2006/07	1.81	21.5
2007/08	1.57	-13.3
2008/09	1.72	9.6
2009/10	1.60	-7.0
2010/11	1.51	-5.6
2011/12	1.29	-14.6

Source: Own Collection from FBR Year Books, Quarterly Reviews, and newspapers' articles

The declining trend in filing of income tax returns via the self-assessment scheme is indicative of the fact that voluntary compliance has yet to establish roots in Pakistan. Moreover, tax return filing is much lower as compared to National Tax Number (NTN) base in the country. For instance, the percentage of tax filers to NTN holders was 63.2% in 2001/02. Similarly, the ratio of taxpayers to NTN holders was 63.4% in case of companies registered with SECP.¹

The voluntary compliance by the corporate sector also remained very poor over the years. For instance, out of 50,952 corporate entities registered with Security and Exchange Commission of Pakistan (SECP) up to 30 June, 2008, only 17,430 entities filed tax returns during tax year 2008. It means level of compliance is only 34% and the level of deficiency in compliance is 66%.² Moreover, out of the total returns filed by companies only 24% have declared income and 76% filed returns without any contribution to the federal revenue in 2008/09. The trend of declaring nil or loss by the companies was even poorer in the past as declaring income has registered a growth of 9.4% in 2008/09.³

Revenue Performance of Voluntary Payments

A comparison of relative share of sources of income tax collection viz. voluntary payments, collection on demand and withholding taxes is presented in Table-3, which is helpful in ascertaining the success or failure of the self assessment system in Pakistan. Major portion of income tax comes from taxes deducted at source (withholding taxes). The other sources are voluntary payments with returns and advances and from demands issued by tax authorities. The amount of tax collected under

¹ See CBR Quarterly Review, Vol.2, No. 4, April-June, 2003.

² See FBR Quarterly Review April-June, 2008. P.7.

³ See FBR Quarterly Review. Vol. 8, No.4, April-June, 2009.

self-assessment scheme increased and reached 47.8% of gross income tax in 2006/07, however, after that ratio has been declining every year.

Table-3: Relative Share of Voluntary Compliance, Collection on Demand and Withholding Taxes in Gross Income Tax Collection (%)

Year	Voluntary Payments	Collection on Demand	Withholding Taxes
2002/03	32.8	15.5	51.7
2003/04	37.3	11.2	51.5
2004/05	36.4	8.6	55.0
2005/06	35.8	6.9	57.3
2006/07	47.8	3.2	49.0
2007/08	37.0	10.9	47.9
2008/09	30.7	16.7	52.6
2009/10	29.6	17.6	52.8
2010/11	31.2	11.5	57.3
2011/12	28.5	15.6	55.9

Source: Own Calculations from FBR Year Books, FBR Quarterly Reviews.

Income Tax-to-GDP Ratio

Another way to see how much self-assessment system has penetrated in Pakistan is to look at tax-to-GDP and income tax-to-GDP ratios since 2002/03. Tax-to-GDP ratio has been declining from 9.4% in 2002/03 to 9.1% in 2011/12. Pakistan's tax-to-GDP ratio is one of the lowest in the world. Likewise, income tax-to-GDP ratio has also been declining since 2007/08, which shows that self-assessment system has not been working well particularly in the recent periods. These ratios also indicate the fact that there is a huge revenue potential in Pakistan, which can be tapped by promoting voluntary compliance through strengthening of the self-assessment system. Ahmed and Rider (2008) estimated the income tax GDP gap for 2004/05 at PKR 262.8 billion or around 152% of the actual income tax revenue of PKR 172.5 billion. The income tax gap estimated on salaried individuals, non-salaried individuals and corporations was PKR 13 billion, PKR 7.3 billion and PKR 242.5 billion, respectively or around 97%, 15% and 217% of the actual income tax collection of PKR 26.3 billion, PKR 55.1 billion and PKR 353.9 billion, respectively.¹

Table-4: Tax-to-GDP and Income Tax-to-GDP Ratio

Year	Tax-to-GDP Ratio	Net Income Tax-to-GDP Ratio
2002/03	9.4	3.0
2003/04	9.2	2.8
2004/05	9.1	2.7

¹ R. A. Ahmed and M. Rider. Pakistan's Tax Gap: Estimates by Tax Calculation and Methodology. Working Paper 08-11, December 2008, P.50.

2005/06	9.4	2.8
2006/07	9.8	3.6
2007/08	9.8	3.6
2008/09	9.1	3.3
2009/10	8.9	3.3
2010/11	8.6	3.1
2011/12	9.1	3.4

Source: Own calculations from FBR Year Books

From above analysis, it is clear that the voluntary compliance has not lived up to the expectations of the Pakistani tax administration, so more reliance has been placed on withholding taxes for collection of income tax revenue (Table-3). Overwhelming withholding provisions are presumptive in nature and tend to introduce regression.

4. Factors Responsible for Poor and Declining level of Voluntary Compliance in Pakistan

Tax compliance means a taxpayer complies with the tax rules enforced by his country.¹ It is widely accepted that the goal of an efficient tax administration is to improve tax compliance using all possible methods. The question why Pakistan has not succeeded in raising the level of voluntary compliance during the last half decade is addressed here.

Ineffective Audits

It has been recognized that since 2006/07, the important source of revenue on account of voluntary payments is on the declining trend mainly due to non-effective audits by the department. The primary objective of audit to act as deterrent against possible tax evasions rather than a source of revenue receipts has been reduced.² The cases selected for complete audit remained on lower side. For instance, Slightly less than 3% or 24,693 cases of all the returns received were selected for complete audit during 2003-04.³ Table-5 depicts poor and dismal audit performance for 2007/08.

Table-5: Audit Performance -2007/08

	Audit cases for disposal	Cases amended	%age of cases amended	Demand created (Million PKR)
Corporate entities	6,600	688	10.4	10,008
Non-Corporate entities	15,593	1,640	10.5	1,813

Source:http://www.dgtrdt.gov.pk/Research/37th_synndicate_%20rports/5.pdf.

¹ Sarker, note 5, P.18.

² See FBR Quarterly Review, Vol. 11, No.4, April June 2011-12, P.6, available at <http://download1.fbr.gov.pk/Docs/20129119955205602012961092945449AprilJune2012.pdf>.

³ See CBR Quarterly Review. Vol. 3, No. 4, April-June, 2004.

The above data reveals that not only the cases selected for audit are on lower side but also the disposal of these cases is quite discouraging and dismal.

Weak Enforcement

The share of collection on demand in gross income tax collection is also very low (Table-3), which shows weaknesses in the enforcement mechanism. Because this component of income tax includes the amount detected through audit, penalties imposed for failing to comply with the provisions of tax laws, and taxes recovered for failure to deposit tax within the prescribed limit of time. This source of revenue expected to be increased in the wake of poor and declining voluntary compliance but the performance is depressing. Another aspect of weak enforcement is that tax returns filers are less for a wide margin as compared to NTN holders. Moreover, there are many companies which do not file return even though they are active on the record of SECP.

Inadequate Tax Policy

Administrative penalties [additional tax (now called default surcharge), additional charges, etc.] are supportive elements for smooth functioning of the self-assessment system. On one hand, administrative penalties are not effectively enforced while on the other, such penalties are waived off by the government through statutory regulatory orders, which may be considered as an element of weak tax policy.¹ It is because if taxpayer knows that he has not to pay additional tax or penalties for tax default, there is potential for him to avoid due and timely payment of taxes.

Weak Intelligence and Investigation System

The system of intelligence and investigation plays an important role for supporting the self-assessment system. Its selective and effective use is crucial to create deterrence toward tax evasion. In Pakistan, the system of intelligence and investigation is not fully equipped with resources (staff and equipments) to create enough deterrence against tax evasion. As a result, tax evasion is rampant in Pakistan. For instance, the Chairman FBR claimed that there are three million citizens who had enormous wealth but had not been paying their taxes.²

Inadequate Taxpayers Service

The taxpayers promptly comply with the tax rules if it is easier and less costly for them to pay taxes. In this regard, public relation activities are quite helpful. In Pakistan, the taxpayers have to spend considerable time for tax compliance. In a recent study "Paying Taxes 2013" conducted by

¹ For instance, government exempted whole amount of default surcharge and penalty on account of non-deduction/deposition of advance tax by the withholding agents. See Statutory Regulatory Order (SRO) 547(I)/2012, available at <http://download1.fbr.gov.pk/SROs/20125231753142215547.pdf>. Also see, SRO 1053(I)/2010, available at <http://download1.fbr.gov.pk/sros/IncomeTaxSROS/2010/2010sro1053.pdf>

² See FBR chief issues warning to tax evaders. 26 January, 2013, available at <http://dawn.com/2013/01/26/fbr-chief-says-countrys-tax-system-needs-reforms/>.

the World Bank, Pakistan ranked 162 out of 185 world economies with regard to tax dealing. Pakistan spends 560 hours on dealing tax matters against the world average of 267 hours.

5. What is Necessary and What Should Pakistan do to Strengthen Self-assessment System to Achieve Voluntary Compliance

Extending good tax services to taxpayers is essential to increase voluntary compliance. Taxpayers' services may have a broad range but at least those which are globally practiced such as tax guidance, tax education, tax consultations, etc. are needed to be provided to the taxpayers vigorously besides strengthening audits, enforcement, intelligence and investigation system. Though these services do exist in the taxation system of Pakistan to some extent, but there is a wide scope for improvement.

Public Relations¹

The public relation activities are helpful in diffusing and increasing tax knowledge,² enhancing tax compliance,³ listening to opinions and requests of public,⁴ to improving mutual understanding and trust between taxpayers and tax administration, and providing information to mass media.⁵ Public relations activities may be handled at the levels of FBR, the RTOs, LTUs and Taxpayers Facilitation Offices.⁶ The mass media including regular television and newspapers, public relations media such as pamphlets to be made available at the tax offices as well as municipal offices is to be used extensively for providing current tax information, answering questions, and reminding the public of tax deadlines.

¹ In Japan, the National Tax Agency (NTA), the Regional Taxation Bureaus (RTBs) and Tax Offices (TOs) handle cooperatively public relations activities . See National Tax Agency Report 2012 , P.11 for various public relations activities such as provision of information regarding tax law and procedures, tax education, tax consultation, etc.

² In Japan, public relations activities undertaken for diffusing and increasing tax knowledge include utilizing internet (websites, mail magazine, YouTube, etc.), public relations materials (Brochure, Poster, etc.), and holding briefings for taxpayers.

³ In Japan, public relations activities undertaken for enhancing tax compliance include arranging "Think-Your-Tax-Week" (November 11-17) which include many public relations activities such as campaign on the street, Ad in the public areas, open class at the National Tax College (NTC), etc. and through tax education by issuing supplementary textbooks, conducting classes on taxation, sponsoring essay writing contest on tax topics, conducting seminars on public finance and economy , video programs on kids page at NTA website, etc.

⁴ In Japan, public opinion is obtained through website, questionnaires, roundtable talks with private organizations, etc.

⁵ In Japan, information are provided to mass media through annual press release , for instance, number of examinations/investigations, tax amount collected by examinations, number of filing returns, number of litigation cases, etc.

⁶ In Japan, the National Tax Agency (NTA), the Regional Taxation Bureaus (RTBs) and Tax Offices (TOs) handle cooperatively public relations activities . See National Tax Agency Report 2012 , P.11 for various public relations activities such as provision of information regarding tax law and procedures, tax education, tax consultation, etc.

Tax Consultation¹

The objective of tax counseling is to assist taxpayers in matters related to tax and encourage the voluntary submission of accurate tax returns and payment of taxes. Generally, tax counseling offices provide advice on the interpretation and application of tax laws, procedures for filing returns and applications, etc. However, it can further be extended by establishing telephone consultation centers, and automatic answer network system for electrical requests, etc.²

Guidance and the Role of Private Tax Associations

In order to increase voluntary tax compliance in filing tax returns and paying due taxes, the tax administration needs to provide taxpayers with guidance on how to improve bookkeeping standards and tax returns. Guidance is particularly important for firms launching new business. Explanatory sessions for guidance of taxpayers may be held when laws are amended. The role of private organizations dealing with tax matters of the taxpayers is also crucial in enhancing voluntary compliance.³ However, there is no clear regulation for associations dealing in tax matters of the taxpayers. All these tax associations are required to be registered under the act enacted for the purpose.⁴ Any person who is not member of any of these associations strictly not be allowed to provide tax services. Also the scope of tax services may be described in the act beyond which the members are strictly not allowed to go.⁵ Then there must be a limit for tax consultation fee to be charged from clients by the members of these associations.⁶ This will promote clarity, transparency, impartiality and confidence among the taxpayers. To qualify for membership of such associations, there must be hard criteria to be followed including examination on subjects related to taxes, accounting and finance, etc. At the same time, the retired tax authorities who had served for sufficient period of time may be exempted from the examination ordeal.

¹ In Japan, tax counseling through a formal tax counsel office was first introduced in 1970.

² In Japan, telephone consultation service started in 1965 followed by Tax ANSWER system in 1987, which has the capability to answer using telephone messages, and has now expanded to include the internet.

³ For instance, in Japan, the tax administration is assisted by various private cooperative organizations, such as Blue Return Taxpayers' Associations, Corporations Associations, Indirect Tax Association, Savings-for-Tax Associations, and Tax Payment Associations.

⁴ For instance, in Japan, Zeirishi Act was enforced in 1951 and all tax associations are required to be registered under this act in order to qualify for providing tax services.

⁵ For instance, a Zeirishi member can provide services regarding bookkeeping, preparation of tax returns and tax documents, representation of taxpayers and tax consultation, etc.

⁶ Under Zeirishi Act, there was a limit up to which the members can charge fee. Recently, this provision has been removed from the act.

Effective Audits

The self-assessment system must be backed by strong and disciplined tax audit system in order to secure proper voluntary compliance and payment from taxpayers. Only revenue potential cases may be selected for audit based on risk profile of the taxpayers. The audit must not be conducted for the revenue purpose but for creation of deterrence. Strict discipline is to be followed throughout the audit procedure to ensure independence, impartiality, quality, accuracy and to prevent possible abuses.

6. Conclusion

It takes time for the income taxation to be supported by the original style of self-assessment based on taxpayers' voluntary compliance.¹ Supplementary measures such as wise use of withholding taxes and appropriate administrative actions gradually prove helpful in penetration of self-assessment system in the income tax system. At the same time, efforts of the tax authorities and related private organizations are also helpful in elevating the bookkeeping standards of the taxpayers and in enhancing their compliance level. Continued and improved taxpayer services supported by tax consultation will ultimately prove beneficial in diffusing and penetrating the self-assessment system backed by voluntary compliance.

¹ For instance, the self-assessment system based on taxpayers' voluntary compliance was penetrated after half a century since its introduction. See Usui, note.18, P.19.

Switzerland

SPD open to Reviving Germany Switzerland Tax Deal

Marking a huge about-turn and substantial concession during ongoing Grand Coalition discussions, Germany's Social Democrats (SPD) have indicated that the party might be prepared to renegotiate the bilateral tax agreement concluded with Switzerland, aimed at resolving the longstanding issue of German residents with undeclared bank accounts held in the Confederation. The SPD and the Green Party blocked the initial tax deal in the German Bundesrat, or upper house of parliament, at the beginning of the year.

In an interview with *Der Spiegel*, North Rhine-Westphalia's Finance Minister and SPD negotiator Norbert Walter-Borjans explained that although the party remains committed to the idea of an automatic exchange of banking information, bilateral accords could "make sense" along the way to achieving this objective.

Walter-Borjans nevertheless made clear that a new treaty between the two countries must be fairer and serve to close existing loopholes. Furthermore, the overarching aim of ensuring that the country's tax authorities gain access to relevant tax information must not be undermined, he emphasized. Here, the Minister underscored that the reason for the failure of the initial text in parliament was the inclusion of provisions guaranteeing anonymity and banning the future purchase of tax data discs.

Commenting, Swiss President Ueli Maurer said that while he supports the idea of new "confidential" round table negotiations, no progress will be made if both sides constantly make public their demands. Alluding to the fact that Switzerland has already made far-reaching concessions, Maurer hinted that it is now Germany's turn to bend. Concluding, Maurer reiterated that although Switzerland has not ruled out the idea of an automatic exchange of information in tax matters, it would be on condition that the mechanism has become the international standard, and is applied in rival jurisdictions, including Singapore. Switzerland must not be put under pressure, however, Maurer warned. – *Courtesy tax-news.com*

New Zealand

NZ Revenue Releases Details of Compliance Program

The New Zealand Inland Revenue Department (IRD) has released details of its Compliance Focus program, intended to help businesses “get it right” and meet their tax obligations.

In the past, the IRD has produced a single annual Compliance Focus document. This year, however, a series of reports will be published, dealing with a wide range of issues, and providing in-depth information for both the public and tax community.

To date, the IRD has issued documents relating to multinational firms, and small- to medium-sized enterprises (SMEs).

A basic compliance package has been introduced for most groups of companies with annual turnover in excess of NZD80m (USD66.1m). Around 500 major groups are now either under direct management or subject to the Significant Enterprises Initiative. These groups provide the IRD with copies of their financial statements, tax reconciliations and group structures, at return filing time. The aim is for multinationals to receive more tailored information requests and audit inquiries from the IRD.

The IRD recommends that multinationals ask themselves four key questions. These are:

- Are appropriate resources (including local capacity) being applied to tax matters?
- Are sufficient internal controls, checks, and balances in place and actually carried out?
- Is there good tax awareness in critical business areas beyond the central tax or finance team?
- Are you aware of legislation changes affecting your business?

The document also sets out ten compliance “red flags” that draw the IRD’s attention:

- Is the group’s effective tax rate substantially less than the statutory rate of 28 percent?
- Has the group participated in any material transactions involving “low or no tax” jurisdictions?
- Are there material differences in the treatment of major items for financial reporting and tax reporting purposes?

- Has the group taken part in any transactions where the anticipated net return is predominantly due to projected tax benefits?
- Are there any differences in tax treatment of a transaction of an entity between countries – for example, debt in one, but equity in another?
- Has the group been involved in any complicated arrangements, such as major restructures, use of special purpose vehicles, or innovative financial arrangements?
- Have any untaxed profits been derived or unusually high foreign tax/imputation credits been claimed by the group?
- Have any uncharacteristic tax losses arisen (or been utilized) within or across the group as a whole?
- Have any mergers, takeovers, or ownership changes occurred and affected community tests for losses and imputation credits?
- Are there any material differences in profitability, tax payable, or major line items in supporting financial statements for the group?

The documents relating to SMEs deal with issues including goods and services tax (GST), employers' monthly schedule, record keeping, resident and non-resident contractors, industry benchmarks, superannuation, and income tax.

Revenue Commissioner Naomi Ferguson said: "The vast majority of New Zealanders and businesses do the right thing and contribute to New Zealand's prosperity. We collect the revenue needed to deliver essential services like healthcare, education and safer communities for New Zealanders.

"By providing information and assistance to our small-medium enterprises, Inland Revenue is not only directly supporting those businesses to get it right but in turn helping those who they employ to meet their tax obligations as well."

New Zealand is working with the Organization for Economic Cooperation and Development on its Base Erosion Profit Shifting (BEPS) initiative, and with its major treaty partners on mechanisms for tackling international tax avoidance and evasion.
– *Courtesy tax-news.com*

Colombia**Colombia Simplifies Taxes for Fixed Rate Investors**

Colombia has simplified its system for calculating taxes paid by those investing in fixed-rate securities, with the intention of reducing distortions and overcharging, the country's Finance Ministry revealed on October 31, 2013.

Streamlining the system will reduce the tax levy and attract additional investment to the fixed-rate market, the country's biggest attractor of overseas investment into its capital markets.

"Simplifying the rules possibly may lead to brokerages and overseas investors that previously weren't in the public debt market to come to see it as easier to enter," Michel Janna, the head of the Finance Ministry's public credit office said to Reuters.

Foreign investment in Colombia's public debt market only accounts for 6 percent of the total, compared with 57 percent in Peru, nearly 40 percent in Mexico, and 15 percent in Brazil. – *Courtesy tax-news.com*

Rs162b FED collected in 3 years

A sum of Rs 162.002 billion has been collected as Federal Excise Duty (FED) from tobacco/cigarettes in last three years.

According to a document placed in the Parliament, as many as Rs 47.099 billion FED had been collected in 2010-11, Rs 53.233 billion in 2011-12 and Rs 61.670 billion in 2012-13.

Revenue collection from Federal Board of Revenue (FBR) has jumped from Rs 520 billion in 2003-04 to Rs 1,939 billion in 2012-13 with the increase of Rs 1.4 trillion in absolute terms. The average growth during the period was 16 per cent. However tax to GDP ratio did not increase for various reasons.

The total GDP of the country recorder / reported during the financial year 2012-13 is Rs 22,909 billion. – *Courtesy The Nation*

Ishaq Dar reviews progress of Finance Ministry

The Finance Minister Senator Ishaq Dar held meetings separately with the Chairman Federal Board of Revenue (FBR) Tariq Bajwa, Governor State Bank of Pakistan Yasin Anwar and senior officials of the Ministry of Finance to review the progress at the Finance Ministry on Sunday.

The Chairman FBR informed the Finance Minister that their was no let up in the efforts of the FBR for achieving the revenue target of Rs 2475 billion set out by the government.

Bajwa also informed the Finance Minister about the notices issued to new income tax payers as part of the campaign to increase the number of assesses by identifying new asesees, says a press release.

The Finance Minister expressed the confidence that FBR would continue its efforts to collect taxes and facilitate the tax payers in filing their returns.

In a separate meeting with the Governor State Bank of Pakistan the Finance Minister reviewed the Foreign Exchange reserves and the Balance of Payment position.

He directed the Governor SBP to redouble efforts to increase inflows as per plan

The Finance Minister also chaired a High level meeting which was attended by senior officials of Ministry of Petroleum and Natural Resources, Privatization Commission, Ministry of Commerce

,Board of Investment. Income support plan and senior officials of Ministry of finance.

The Secretary Petroleum informed the Finance Minister that 260mmcf/d gas would be added to the system by December, 2013 which would be dedicated for the Power sector.

The officials of BOI gave various proposals to further improve the investment climate in the country and improve business environment.

The Finance Minister directed the Secretary Income Support Program to streamline the process of release of Funds so that maximum number of families can benefit from the program. –

Courtesy Business Recorder

Shifting of DTRE scheme to IOCO: certain MCCs raise serious objections

The Federal Board of Revenue has received serious objections of certain Model Customs Collectorates (MCCs) on draft notifications and rules for shifting the entire Duty and Tax Remission for Exports (DTRE) scheme from regulatory collectorates to Input Output Coefficient Organisation (IOCO).

Sources told on Sunday the FBR had sought comments of the MCCs on draft notifications and rules on functioning and powers of the IOCO. Through Finance Act, 2013, the FBR has amended Customs Act 1969, seeking powers for functioning of the Directorate General of Input Output Co-efficient Organisation. The FBR has set up an office of the Director IOCO (South) at Karachi, which would deal with exporters of Sindh and Balochistan. The second Director IOCO (North) established at Lahore would deal with exporters of Punjab, KP and Gilgit-Baltistan.

Exporters and some of the collectorates have raised objections in the draft rules on the IOCO functioning, sources said.

Commenting on the draft DTRE rules, experts stated that the FBR has decided to shift the DTRE scheme from Regulatory Collectorates to IOCO for granting of DTRE approval and security instruments without consultation and recommendations of major stakeholders like export associations and other trade bodies.

They said the IOCO was created to assist on various technical and industrial issues relating to input/output wastage, determination

of correct duty drawback in an institutionalised manner containing the sector specialists like engineers, cost accountants, and chemical examiners to do surveys in the fields on the basis of information provided by the applicant as well as by the regulatory collectorates.

The question arises why the IOCO Karachi has been given power of regulatory authorities and shifting its original domain of technical supporter of the custom wings. An organisation needs to give support as helping and technical hand to regulatory authorities on huge amount of remission, but it plans to get power from the regulatory authorities. The IOCO should have to improve itself in international standards and on industrial grounds to provide technical support within an appropriate timeframe, as many cases are pending on regular basis as well as in review especially in last 8-10 months to save the govt revenue and foreign exchange. The IOCO has to improve by new technical methods, particularly industrial knowledge and international standards to meet the new requirements by hiring technical engineers and examiners, experts explained.

Experts said the proposed SRO has been chalked out to shift the DTRE from all Collectorates to IOCO, without seeking comments of major stakeholders like export association, chambers or other trade bodies. There is a panic like situation among the exporters since February-13 who were not expecting that the customs authorities would take such an anti-export measure. Practically, exporters will face more problems and burdens in processing of their DTRE related approvals and security instruments submission and then at the time of release after reconciliation of DTRE.

After the drastic changes of shift of powers and functions, exporters would be bound for compliance of only two Directorates in Pakistan as regulatory bodies for application and processing of DTRE and the exporters belonging to city like Islamabad, Rawalpindi, Peshawar, Lahore, Multan, Faisalabad, Sialkot or any other city would approach Lahore for getting final approvals and processing of their cases. The exporters belonging to the said cities would have to physically go to Lahore which is almost impossible to spare time and money as compared to existing scheme where concerned Collectors of Customs are dealing with the issues of exporters.

Sources said the FBR has issued the proposed draft of SRO, some of the important proposed changes in DTRE Rules-Custom Rules-2001 are:

Firstly, the director IOCO may determine, wherever required input-output ratio and wastages, as may be deemed appropriate within a period of thirty days. Secondly, provided Director IOCO may grant provisional DTRE approval pending receipt of survey report up to 25 percent of the quantity applied or the production capacity of the applicant whichever is less, if he is satisfied with the bona fides of the DTRE application. Thirdly, on the basis of DTRE application Director IOCO, if he is satisfied with the bona fides of the DTRE application, shall grant DTRE approval and issue authorisation allowing import of the approved quantity of goods without payment of due duty and taxes and each such authorisation shall be fed into customs computerised systems over the web in the given format. The amounts suspended by the Director IOCO in respect of leviable custom duties, excise duty, sales tax and withholding tax shall be secured with Collector of Customs in whose jurisdiction import take place.

Fourthly, under draft rules, in case of commercial exporter holding a DTRE approval for same state-goods, the Director of IOCO after conforming that the goods acquired by commercial exporter against such approval have been exported in full, shall issue discharge certificate on the basis of which the clearance collectorate shall release the securities furnished at the time of imports.

Under the draft rules, all liabilities or dues if payable or outstanding under any of the provisions of this sub-chapter shall be finally ascertained by the directorate of IOCO and shall intimate to the collector of customs for the recovery under the relevant recovery rules.

Experts were of the view that there are implications, duplication of work and increase in cost and wastage of time will increase by the proposed changes in DTRE rules.

Tax experts pointed out that the proposed changes in new rules would create two major problems. Firstly, the exporter should submit the security instruments on every consignment to every port of clearance in whose jurisdiction the import takes place, this is totally impractical, wastage of time, increase complications for exporters as well as for custom officials and after audit of DTRE from one station, exporters will always be busy at different

stations of Imports (Collectorate of Customs) to get release of their securities, which may be in various numbers across the Pakistan.

It seems that DTRE approval for local procurement is abolished. The new rule is silent about the grant of DTRE for local procurement and for its securities instruments.

Exporters opined they are already facing difficulties to import the raw materials, accessories, packing materials on time in short orders which ultimately increase cost of purchase, increase the cost of sales in shape of delays in preparation of export consignment, shipment sent through Air or some shipments prepared under various undue duties and taxes despite the concessionaries facility available in laws, and some exporter are losing buyers due to these delays, which ultimately cause huge losses to exports and adversely affects the foreign exchange remittances to national exchequer.

At present exporters and other business community avail the concessionary facilities of DTRE, from their respective Regulatory Collectors which fall in their jurisdiction. In existing scenario the local Collectorates as Regulatory Collector granted provisionally approval after physical verification of factory premises and all other documents related to income tax, Sales tax, accounts and Production capacity, samples of the product, Technical data and particular industrial data and other information required from time to time by the regulatory Collector and sometime also get lab test of the product from private laborites, furthermore the Regulatory Collector may also have right to change or decrease or cancel the concessionary facility already approved. After given approval 25 percent of the applied quantity in DTRE, the Regulatory Collector refer the case to IOCO Karachi to determine the input output ratio and wastage of the consumer items for technical support and helping hand.

After these drastic changes of shift of powers and functions, exporters belonging to Islamabad, Rawalpindi, Peshawar, Lahore, Multan, Faisalabad, Sialkot or any other city would be bound to approach IOCO in Karachi for getting final approvals and processing of their cases. The exporters across Pakistan would have to physically go to Karachi which is almost impossible to spare time and money as compared to existing scheme where concerned Collectors of Customs are dealing with the issues of exporters.

Different export associations and trade bodies have approached the Chairman FBR, and Member Customs repeatedly about the implications of the irrational and negative decision to transfer the functions and key powers of Collectors of Customs to IOCO but not yet to give any appointment and positive response.

Exporters have requested the FBR to consult the exporters associations and trade bodies and meeting with IOCO and the FBR officials, so they could explain their point of view that it is practical not possible that exporters belonging to various cities from Multan to Peshawar will physically go to Directorate of Lahore to get approvals and submit security instruments in different locations and then reconcile the DTRE or audit justifications to every location from where they are imported. Exporters are confident that that new FBR Chairman Tariq Bajwa will give time to hear the viewpoint of exporters. – *Courtesy Business Recorder*

Achieving Rs 2,475 billion target: no let-up in FBR efforts, Dar told

Finance Minister Senator Ishaq Dar held meetings separately with the Chairman Federal Board of Revenue (FBR) Tariq Bajwa, Governor State Bank of Pakistan Yasin Anwar and senior officials of the Ministry of Finance to review the progress at the Finance Ministry on Sunday. The Chairman FBR informed the Finance Minister that there was no let-up in the efforts of the FBR for achieving the revenue target of Rs 2,475 billion set out by the government.

Bajwa also informed the finance minister about the notices issued to new income tax payers as part of the campaign to increase the number of assesses by identifying new asesees, says a press release. The minister expressed the confidence that the FBR would continue its efforts to collect taxes and facilitate the tax payers in filing their returns.

In a separate meeting with the Governor State Bank of Pakistan, Dar reviewed the foreign exchange reserves and the balance of payment position.

He directed the Governor SBP to redouble efforts to increase inflows as per plan. The minister also chaired a high level meeting which was attended by senior officials of Ministry of Petroleum and Natural Resources, Privatisation Commission, Ministry of

Commerce, Board of Investment, income support plan and senior officials of Ministry of Finance.

The Secretary Petroleum informed the Finance Minister that 260mmcf gas would be added to the system by December, 2013 which would be dedicated for the power sector.

The officials of the BoI gave various proposals to further improve the investment climate in the country and improve business environment. The Finance Minister directed the Secretary Income Support Program to streamline the process of release of Funds so that maximum number of families can benefit from the programme. – *Courtesy Business Recorder*

Hard copies of documents: customs staff's demands hurt importers

Importers are facing difficulties in clearing consignments at off-dock terminals and Air Freight Unit (AFU) as Customs officials ask for hard copies of import documents for clearance of consignments; it was learnt here on Saturday. According to sources, preventive officers posted at off-dock terminals and AFU have made hard copies of import documents mandatory for the clearance of consignments.

They said that Federal Board of Revenue (FBR) claimed to have installed hassle-free automated system at all Customs stations to facilitate the trade, however, this unwarranted requirement of producing hard had not only created hardships for traders but also opened doors for corruption.

“Despite past experience that clearance on hard copies may lead to fraud and illegal removal of consignments on fake documents, preventive staff is demanding the same from importers/clearing agents for gate out activity,” sources said.

“Similarly, staff at off-dock terminals has made production of hard copies of Goods Declarations (GDs), a necessary condition for payment of charges and release of consignments from terminals,” they maintained.

When contacted, official sources, on a condition of anonymity, said that the office of Director, Web Based One Customs (WeBOC) had taken strict action to avert said practices, saying that instructions were made to clear all consignments, whether cleared through One Customs or WeBOC after confirmation from computer system; no

reliance should be placed on the basis of hard copies of the documents.

They said that although WeBOC worked in paperless environment, the said practice was turning WeBOC into One Customs. Therefore the office of WeBOC is of the view that demanding such documents is against the spirit of automation and fraught with risk of illegal removal of consignments. To forestall such possibilities, the office has asked the concerned authority to stop this practice forthwith, the sources said.

Replying to a question, they said that preventive staff had been time and again informed, through extensive training sessions, that all relevant information required for gate staff/terminal operators was available on their screen hence there was no need to demand any customs documents from traders/clearing agents either by customs staff or terminal operator at gates.

Moreover, the sources said that authority concerned had been advised to adopt same procedure introduced by the Karachi Port Trust (KPT), saying that KPT had commenced the issuance of gate passes in two colours; one for One Customs and other for WeBOC to reduce the chances of illegal removal of consignments from the ports. It has also been proposed that a public notice should be issued to all stakeholders, clarifying the procedures observed at gate out stage, they said. – *Courtesy Business Recorder*