



# The Audit Policy, 2019

Taxpayers Audit Wing

Federal Board of Revenue, Islamabad

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## Glossary

FBR	Federal Board of Revenue
FED	Federal Excise Duty
FTR	Final Tax Regime
I&I	Intelligence and Investigation
IR	Inland Revenue
RAMS	Risk based Audit Management System
TPA	Taxpayers Audit
TY	Tax Year
USAS	Universal Self-Assessment Scheme

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## Executive Summary

**T**axpayers Audit Wing is persistently assisting the Federal Board of Revenue to achieve the objective of promoting voluntary tax compliance and making the Board a service oriented organization through implementing policies envisaged under Federal Board of Revenue Act, 2007. In order to facilitate the voluntary tax compliance, the Taxpayers Audit Wing has brought a landmark change by adopting principle of modern compliance risk management strategy through implementation of Audit Policy 2019. The strategy will effectively identify defaulting taxpayers through a system of audit and penalties. The already initiated reform agenda of the Federal Board of Revenue (FBR) to enhance its revenue collection and service standards will be completed under Vision 2025. In this regard, existing Audit Policy is a roadmap to promote compliance of tax laws, promoting tax culture and discourage the practice of giving false declarations with impunity by selecting taxpayers for audit. On the basis of lessons learnt from the past Audit policies, the aforementioned policy document takes into consideration all guidelines, constraints and restrictions, legal or otherwise that ensures efficient, effective, transparent and judicious system of audit. The **'Audit Policy 2019 for Tax Year 2018'** will adopt a regulation on risk-based selection of audit cases. The aim of bringing such regulation is to ensure the quick disposal of audit related issues and bring transparency in clearance of tax audits. Furthermore, this policy document takes into consideration the exclusions and exemptions to facilitate the potential taxpayers by giving them respite from unnecessary pains of audit.

## 1. Introduction

The tax system in Pakistan is operating mainly on self-assessment/ compliance basis. Taxpayers' audit holds a significant position under Universal Self-Assessment Scheme (USAS) as it aims at creating deterrence against non-compliance, false declaration and tax evasion. TPA Wing, FBR has been entrusted with the task of designing /preparing audit policy on yearly basis. In addition to that, the wing also monitors audit activities carried out in the field formations throughout the year. In the past, cases were selected for audit on either random or parametric basis with a possibility of selection of non-potential taxpayers. Thus, in order to overcome this issue, this time cases have been selected on scientific approach for which a software has been designed and put in place named as Risk Based Audit Management System (RAMS). Selection on scientific matrix allowing allocation and distribution of weightage to different parameters in Risk Grid will segregate the potential and high-risk cases for audit through parametric computer balloting. This will enable FBR to focus on cases with maximum revenue impact along with facilitating compliant taxpayers and building the confidence of taxpayers in the Audit system.

## 2. Aims and Objectives

Right audit approach will not only help FBR in retrieving the loss of revenue but will also help in improving the credibility of the institution. Broadly, the aims and objectives of equitable tax policy are summarized as under:-

- To ensure efficient and standardized professional audit.
- To develop fair and effective tax administration by selecting cases for audit in a transparent manner through risk based approach.
- To identify non compliant taxpayers through risk scoring techniques.
- To enforce compliance of the tax laws and accounting principles as enshrined in Tax Laws and Rules by creating effective deterrence against tax evasion.
- To ensure that selection of cases for audit does not cause any prejudice to a taxpayer in any manner. If after an audit the declaration is found in order, the audit shall be closed. This will allay the fear of the taxpayer whose case is being audited.
- To promote taxpayer facilitation and education in respect of audit cases that require clarification in addressing the taxpayers' representation.

### 3. Scope

Audit Policy 2019 shall apply to persons or classes of persons falling under all or any of the three domestic Federal Tax Statutes i.e. Income Tax Ordinance 2001, Sales Tax Act 1990, and Federal Excise Act 2005 and shall provide the necessary framework for selection of cases for audit by the Board.

For the purpose of selecting cases for audit through risk based approach by conducting computer ballots, this Policy shall be effective for Tax Year 2018 for Income Tax and corresponding Tax Period(s) for Sales Tax and FED. Besides Tax Year and Tax Period(s) mentioned above, the CIRs and Director I & I (IR) may also select cases of persons for audit for Tax Year(s) and corresponding Tax Period(s), provided the statutory limitations so permit.

### 4. Methodology

In order to determine the validity, veracity, correctness and compliance to relevant tax laws of the taxpayers' declarations, the FBR has a modern data warehouse, information technology systems and interface with different departments for collection of information. This facility enables FBR to cross match taxpayers' declaration with available data sources through a Risk Based Audit Management System. FBR will run taxpayers' data on Risk Management System and cases which attract one or more of the risks shall be dealt with. In this connection, FBR would conduct computer ballot by applying Risk Based Parameters for selection of 0.76 % of cases for audit out of the total filers after exclusions in Income Tax for the Tax Year 2018. For Sales Tax and Federal Excise Duty, the FBR would select 1.67 % and 5.65 % cases for audit respectively out of the total filers after exclusions for tax period corresponding to accounting period adopted for the purpose of returns of Income Tax, for TY 2018. However, FBR has limited the audit cases selected without the risk-based system to 10% of total audits subject to clearance by Member (Taxpayers Audit).

## 5. Exclusions

The following exclusions have been identified and approved by the Board under clause (b) of sub-rule (2) of Rule 231F of the Income Tax Rules, 2002 where selection for audit by the Board is not required.

### 5.1 Income Tax

- i. All cases already selected for audit by the Commissioner Inland Revenue and Director I & I (IR) under Section 177 and in consequence of action u/s 175 of the Income Tax Ordinance, 2001 for Tax Year 2018.
- ii. All cases where income chargeable to tax under the head salary and /or pension exceeds 50% of taxable income, except cases having business income. Directors of companies do not qualify for this exclusion.
- iii. All cases where entire income is covered under Final Tax Regime (FTR).
- iv. All cases where declaration has been made under the Voluntary Declaration of Domestic Assets Act, 2018.
- v. All cases where declaration has been made under the Asset Declaration Ordinance, 2019.

### 5.2 Sales Tax

- i. All cases already selected under Section 25 and 38 of Sales Tax Act, 1990 by the Commissioner Inland Revenue or Director I & I (IR) for tax periods corresponding to the accounting period adopted for the purpose of returns of income under the Income Tax Ordinance, 2001 for the Tax Year 2018 provided that where only a part of the said accounting period had been audited already, the relevant authority may select the remaining period for audit.
- ii. Federal, Provincial and Local Government Departments.
- iii. All cases where declaration has been made under the Voluntary Declaration of Domestic Assets Act, 2018.
- iv. All cases where declaration has been made under the Asset Declaration Ordinance, 2019.

### **5.3 Federal Excise Duty**

- i. All cases already selected under Section 46 and 45 of Federal Excise Act, 2005 by the Commissioner Inland Revenue and Director I & I (IR) respectively for tax periods corresponding to the accounting period adopted for the purpose of returns of income under the Income Tax Ordinance, 2001 for the Tax Year 2018 provided that where only a part of the said accounting period had been audited already, the relevant authority may select the remaining period for audit.
- ii. All cases where declaration has been made under the Voluntary Declaration of Domestic Assets Act, 2018.
- iii. All cases where declaration has been made under the Asset Declaration Ordinance, 2019.
- iv. Federal, Provincial and Local Government Departments.

## **6. Risk Parameters**

### **6.1 Income Tax**

The risk parameters would not be disclosed in accordance with section 214C (1A) of Income Tax Ordinance, 2001. However, the risk parameters applied to a taxpayer selected for audit can be communicated on demand as per order dated 27.06.2019 of Lahore High Court Lahore, in W.P # 10035/2017 titled M/s. Happy Manufacturing Company (Pvt) Ltd Vs FBR etc which has been confirmed by the Supreme Court of Pakistan in C.P Nos. 2649-L etc and others.

### **6.2 Sales Tax**

The risk parameters would not be disclosed in accordance with section 72B (1A) of Sales Tax Act, 1990.

### **6.3 Federal Excise Duty**

The risk parameters would not be disclosed in accordance with section 42B (1A) of Federal Excise Act, 2005.