

Press Release *For immediate Release* **July 11, 2016**

Government introduces 2% tax rebate for Shari'ah compliant listed manufacturing companies

ISLAMABAD, July 11: The federal government, to incentivize the listed manufacturing companies to become Shari'ah compliant has introduced a tax reduction of 2 percent for Shari'ah compliant listed companies through Finance Act 2016.

The tax rebate, introduced on the suggestion of the Securities and Exchange Commission of Pakistan (SECP) is part of reforms being introduced for the elimination of Riba and for the promotion and development of the Islamic capital market. To implement this tax rebate, a new clause 18(b) has been inserted in the Second Schedule Part II of the Income Tax Ordinance, 2001 through the Finance Act, 2016.

The screening criteria to eligible for the tax rebate will be approved by the State Bank of Pakistan (SBP), the SECP and the Federal Board of Revenue (FBR). However, the listed companies deriving their income only from the manufacturing activities and have declared their taxable income for three consecutive years and have had paid dividends for the last five consecutive years could qualify and apply for the tax rebate.

The tax incentive will attract new listings of companies on the Pakistan Stock Exchange (PSX) and add depth to the market. Moreover, it will create vibrant primary and secondary markets; capitalize the limited capital base; mobilize resources through channeling of faith-based investor savings; counter market anomalies and malpractices due to larger free-floats; create employment; and generate revenue for the national exchequer in terms of additional direct and indirect taxes.

An analysis of the data compiled for listed manufacturing companies reveals that 8 companies can immediately qualify the criteria for Shariah compliance and avail 2% tax savings (as their interest-bearing debt or gearing is 0%) provided they convert their interest income from investments to income from Shariah compliant capital market equity and debt securities.

Another six companies, with gearing ratios of up to 10%, can also easily become eligible for the tax rebate subject to the condition that interest income and financing, be relocated to Shariah compliant modes of financing and investments. Similarly, other companies which are leveraged by conventional borrowings may also avail the discount in corporate tax by structuring on Islamic modes. Though tax rebate to companies will have a cost for the national exchequer, the liquidity created means that additional funds are available for distribution as dividends on which withholding tax can be realized.

On the direction of the Finance Minister, to pass on the benefits of tax rebate to the public shareholders of the eligible companies, the SECP is considering additional conditions in consultation with the SBP and FBR for the companies to i) maintain a minimum of 25% free-float; ii) conduct business that is Halal; iii) all income and financing activities should be riba-free.