Report of the

NATIONAL FINANCE COMMISSION

2009

Government of Pakistan
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List of Acronyms

ACGR	:	Annual Compound Growth Rate
AJ&K	:	Azad Jammu and Kashmir
BBTU	:	Billion British Thermal Unit
BE	:	Budget Estimates
CCI	:	Council of Common Interests
DFIs	:	Development Financial Institutions
FATA	:	Federally Administered Tribal Areas
FBR	:	Federal Board of Revenues
GDP	:	Gross Domestic Product
GDP(mp)	:	Gross Domestic Product (market price)
GDS	:	Gas Development Surcharge
GST	:	General Sales Tax
HDI	:	Human Development Index
IMF	:	International Monetary Fund
IPD	:	Inverse Population Density
MEF	:	Macroeconomic Framework
MMBTU	:	Million British Thermal Unit
NFC	:	National Finance Commission
NHP	:	Net Hydel Profit
NWFP	:	North West Frontier Province
OGRA	:	Oil and Gas Regulatory Authority
OZT	:	Octroi and Zilla Tax
P&NR	:	Petroleum and Natural Resources
PRSP	:	Poverty Reduction Strategy Paper
PO	:	President's Order
SBP	:	State Bank of Pakistan
ToR	:	Terms of Reference
VAT	:	Value Added Tax
WAPDA	:	Water and Power Development Authority

Preface

A federal democratic form of government today enjoys an ever increasing acceptance throughout the world. Federalism is a flexible instrument for state organizations that keep adapting to new needs and different historical, political and economic factors. This much lauded flexibility is ideally suited to a country like Pakistan. Pakistan has a federal democratic form of Government having four provinces viz. Balochistan, NWFP, Punjab and Sindh as federating units along with special areas which include Gilgit-Baltistan, Federally Administered Tribal Areas (FATA) and Azad Jammu and Kashmir (AJ&K).

The functions and responsibilities as well as taxation powers of the federal and provincial governments are defined in the Constitution of the Islamic Republic of Pakistan. A major part of the resources (more than 93%) is generated at the federal level, whereas the provinces generate less than 7% of the total resources. On the other hand, the Federal Government accounts for 70% of the aggregate national expenditure while the provinces spend only 30% of it. Provinces have to thus rely on the federation to meet their expenditures.

The inter-governmental fiscal relationship in Pakistan remains complex and contentious. The fact that the province of Punjab is the biggest in terms of population, while the province of Balochistan is the smallest in terms of population but is the largest as far as its area is concerned, hence it makes the relationship complex. Likewise, the province of Sindh is the hub of business activity because of sea ports. NWFP is a province with high incidence of poverty and has become a hub of terrorist activities. It is thus most financially and economically distressed. Due to the factors mentioned above financial needs of all the provinces have substantially increased.

The nature and extent of inter-governmental revenue sharing arrangements have to be evolved in a flexible manner so that changing expenditure obligations of the two levels of government and their ability to finance these obligations can be adequately addressed. Recognizing the need for a periodic review of inter-governmental fiscal relations, the Constitution has provided for the establishment of the National Finance Commission (NFC) at intervals not exceeding five years. This would ensure that the distribution of revenues out of the Divisible Pool Taxes between the federation and the provinces and amongst the provinces can be reviewed.

The present state of public finance necessitates a fundamental re-examination of the issues related to revenue sharing arrangements. This re-examination is particularly important considering the constraint on resources, the need to contain budget deficit, and the need to meet the requirements of Government of Pakistan for debt servicing, defence and the growing need of the provinces to fund social sector programs such as health and education. Further, it is also equally necessary that the tax to GDP ratio should be adequately improved to increase up to 15% of GDP in the coming years. The report of the 7th NFC has endeavored to adequately address all these issues.

Introduction

1.1: Composition and appointment of National Finance Commission (NFC)

NFC being the premier resource distribution body has evolved on the core principles of fiscal decentralization, development etc. The main charter of NFC is to recommend on the following:

(i) The distribution of specified taxes, duties between federation and provinces.

(ii) The making of grants-in-aid by the federation to provinces.

(iii) The borrowing powers exercised by the federal and provincial governments.

(iv) Any other financial matter referred to the Commission by the President of Pakistan.

The composition of appointment of National Finance Commission (NFC) by the President is provided under the Article 160 of the Constitution of Islamic Republic of Pakistan 1973.The details of article 160 are given at Annex I.

The first NFC was constituted on 9th February, 1974 with the Terms of References (ToR) as provided in the Constitution. The NFC, through its unanimous report and recommendations, had given a definite shape to fiscal federalism in Pakistan in a democratic setup.

The second NFC was constituted on 11th February, 1979. The excise duty on tobacco and tobacco manufactures was included in the ToR of the Commission with a view to broadening the base of the Divisible Pool Taxes. The Commission was also directed to submit its recommendations regarding distribution of local funds between

Provinces and local bodies. However the second NFC was unable to finalize its recommendations.

The third NFC was constituted on 25th July, 1985. The Commission held nine meetings over a period of three years. The Commission's recommendations could not be finalized although it had done some useful work and had nearly reached a consensus. The elected political government was removed in May 1988, and thus the work of the commission could not be finalized.

The fourth NFC was constituted on 23rd July, 1990. After the induction of newly elected government in November, 1990, the Commission was reconstituted after a change in the composition of non-statutory members. On the recommendation of Governments of Sindh, NWFP and Balochistan the following items were added in the ToR of the Commission:

- i) Excise Duty on Tobacco and Tobacco Manufactures;
- ii) Royalty on Crude Oil; and
- iii) Surcharge on Natural Gas (GDS).

In addition, the Council of Common Interests (CCI) on 12th January, 1991 also assigned the task to the NFC to suggest as to whether the net Hydel profit due to the concerned provinces should be paid by the Federal Government or by the generating agency. The Commission, after detailed deliberations, submitted its recommendations on 9th April, 1991. The recommendations of the Commission were implemented with effect from 1st July, 1991 through Presidential Orders No.1 and 3 of 1991 (Annexes II & III). In the 1991 NFC Award, Divisible Pool Taxes was enlarged by adding two taxes i.e. excise duty on tobacco and tobacco manufactures and excise duty on sugar. However, the vertical distribution formula between federation and provinces remained the same i.e. 20:80. The net proceeds of GDS and royalty on crude oil were also declared as straight transfers. As such provinces received larger share as compared to the earlier Award of 1974. In addition, Federal Government also guaranteed the payment of net Hydel profits to provinces by the concerned undertaking i.e. Water and Power Development Authority (WAPDA).

The fifth NFC was constituted on 23rd July, 1995. It was reconstituted by the interim government on 10th December, 1996. The Commission submitted its recommendations, which were implemented through Distribution of Revenues and Grants-in-Aid Order, 1997 (President's Order No.1 of 1997) with effect from 1st July, 1997 (Annex-IV).

The sixth NFC was constituted on 22nd July, 2000. After the induction of the political government in 2003, the Commission was reconstituted on 13th November, 2003. Despite holding more than 13 meetings, the Commission could not reach consensus to submit the recommendations. However, the distribution ratios of the provinces were revised through President's Order No.6 of 2002 when the census report was finalized.

The seventh NFC was set up on 21st July, 2005. An informal meeting was held in 2005 but could not reach a consensus on the mechanism for resource distribution. In order to provide a larger share to the provinces, the Distribution of Revenues and Grants-in-Aid Order, 1997 was amended by the President vide President's Order No.1 of 2006. The revised sharing arrangements were implemented with effect from 1st July, 2006. The Commission did not convene any meeting till formation of the present government. The present government reconstituted the seventh NFC on 24th July, 2009.

1.2: Salient features of NFC Awards

Three awards have been announced by the NFC so far under the 1973 Constitution of Islamic Republic of Pakistan. The salient features of these Awards are highlighted in the following paragraphs.

1.2.1: 1974 Award

The salient features of 1974 Award were:

(i) The Divisible Pool Taxes were consisted of the following taxes:

a) Export Duty on Cotton

b) Taxes on Sales

c) Taxes on Income

(ii) The provincial share in the Divisible Pool Taxes was fixed at 80%.

(iii) The share of the Provinces was given on the basis of population, namely

Punjab	60.25 %
Sindh	22.50 %
NWFP	13.39 %
Balochistan	3.86 %
Total	**100.00 %**

The share of each province was subsequently revised on receipt of 1981 Census Report in 1982.

(iv) Balochistan and the NWFP were given a fixed amount of subvention by the Federal Government which were as under:-

a) Balochistan Rs. 50 million

b) NWFP Rs.100 million

1.2.2: 1990 Award

The salient features of 1990 Award were:

(i) The Divisible Pool Taxes was enlarged by including the following additional taxes:

a) Excise Duty on Tobacco & Tobacco Manufacturers.

b) Excise Duty on Sugar

(ii) The provincial share in the Divisible Pool Taxes remained at 80%.

(iii) The Provincial Share in the Divisible Pool Taxes was distributed based on the respective share in population of each province.

(iv) The net proceeds of Development Surcharge on Natural Gas and Royalty on Crude Oil was made as straight transfers for provinces.

(v) Grants-in-Aid to Provinces was as under:

a)	Punjab	:	1000 million for 3 years
b)	Sindh	:	700 million for 5 years
c)	NWFP	:	200 million for 3 years
d)	Balochistan	:	100 million for 3 years

(vi) The net profit from hydro electric stations was to be paid by WAPDA. Federal Government would guarantee payment of the same.

1.2.3: 1996 Award

The salient features of 1996 Award were:

(i) The entire FBR taxes excluding the following were made part of the Divisible Pool Taxes:

a) Excise Duty on Natural Gas.

b) Income Tax paid out of the Federal Consolidated Fund.

(ii) The Provincial Share in the Divisible Pool Taxes was fixed at 37.5%.

(iii) The Provincial Share in the Divisible Pool Taxes was to be distributed based on the respective share in population of each province (1981 Census). It was recommended that the ratio of provinces be reworked on receipt of final population census which was overdue at that time.

(iv) The net proceeds of Development Surcharge on Natural Gas and Royalty on Crude Oil was continued as straight transfers.

(v) Grants-in-Aid to the provinces of NWFP and Balochistan was fixed as follows:

a) NWFP: 3,310 million for 5 years

b) Balochistan: 4,080 million for 5 years

[To be increased annually at 11% subject to subsequent adjustment in line of inflation rate.]

(vi) The Commission also recommended matching grants to provinces subject to a maximum limit as specified below in case the Provincial Governments achieved a minimum growth of 14.2% in Provincial revenues:

(a) Punjab	500 million
(b) Sindh	500 million
(c) NWFP	100 million
(d) Balochistan:	100 million

(vii) Collection charges were recommended at 5% on the Divisible Pool Taxes and 2% in case of straight transfers.

1.2.4: Interim Arrangements made in 2006

The sixth NFC could not finalize the award due to divergent views on the basic issues. The seventh NFC was constituted in the year 2005 and held one informal meeting on 15th September, 2005 and was also unable to reach any conclusion. The then Chief Ministers and Finance Ministers of the provinces reposed confidence on the then President of Pakistan for revision of the Distribution of Revenues and Grants-in-Aid Order, 1997 enhancing the provincial share in the Divisible Pool Taxes. Accordingly, the Distribution of Revenues and Grants-in-aid (Amendment) Order, 2006 (Annex-V) was issued. The Revised Order was effective with effect from 01.07.2006. The salient features were:

(i) The Provincial share in the Divisible Pool Taxes was enhanced from 37.5% to 41.5% in 2006-07 to be increased further to 46.25% in 2010-11. The year wise provincial share in the Divisible Pool Taxes were as follows:

2006-07	41.50%
2007-08	42.50%
2008-09	43.75%
2009-10	45.00%
2010-11	46.25%

(ii) All the four provinces were made eligible for Grants-in-Aid. The Grants-in-Aid were fixed at Rs.27.75 billion for the year 2006-07. The Grants-in-Aid were to be increased annually in line with the growth in the Divisible Pool Taxes.

(iii) With the arrangements made in (i) and (ii) above, the overall provincial share in the net Divisible Pool Taxes would be 45% in 2006-07 and 50% in 2010-11.

(iv) The provincial share in the Divisible Pool Taxes net minus amount equivalent to 1/6th of General Sales Taxes (GST) would be distributed based on ratio of population of each province.

(v) Amount equivalent to 1/6th of GST would be distributed giving weight of 50% to population and 50% to the ratio of collection of audited octroi and zilla tax for the year 1998-99.

(vi) Grants-in-Aid would be distributed amongst the provinces of Punjab, Sindh, NWFP and Balochistan in the ratio of 11:21:35:33.

Review of 1996 NFC Award

2.1: The NFC Award

In the NFC report of 1996, the concept of national resource picture was introduced. The national resource picture was derived through the projection of tax and non-tax revenues of federal and provincial governments combined, and adding the borrowing to finance national budget deficit. The expenditure projections were then made to be consistent with the available national resources.

One another important aspect of the 1996 NFC Award was that it bifurcated the public expenditures into priority and non-priority expenditures. Defence, debt servicing, social sector and development expenditures were regarded as the priority expenditures while general administration, community services and law and order were termed to be the non-priority expenditures. This was done to solve the emerging financial and other challenges, issues and accordingly prioritize the path of development.

For projections of the receipts and expenditures the following Annual Compound Growth Rate (ACGR) was adopted:

i. 17.9% for federal tax receipts and 16.1% for non-tax receipts;

ii. Provincial tax and non-tax receipts at 13.5%.

iii. Total federal expenditures at 16% and provincial expenditures at 15.6%.

The report stated that the priority expenditures of the federal and provincial governments would be protected. Furthermore, the overall fiscal deficit would be reduced to 3% of GDP by the end of the award period i.e. 2001-02. Keeping these two factors in view and after projecting the receipts and expenditures of the federal and provincial governments, the Commission recommended inclusion of all taxes in the Divisible Pool Taxes and provincial share in the pool was fixed at 37.5%.

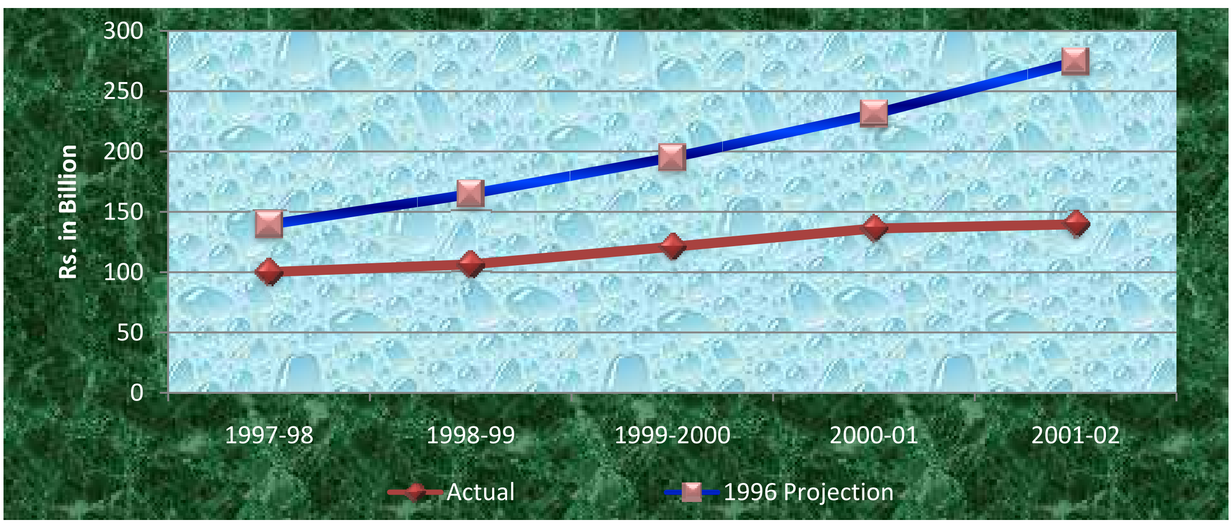
The projections showed that the provincial expenditures were between 30% to 31% of the total expenditures.

Comparisons of the projections with the actual shows the projections were unrealistic and ambitious. As a result the provincial share in the Divisible Pool Taxes was much less than projected. A comparison of the actual Divisible Pool Taxes transfers with the projections (province-wise) is at Annex-VI. The summarized position is tabulated below:

Table 2.1: Provincial Share in the Divisible Pool Taxes

	1997-98	1998-99	1999-2000	2000-01	2001-02
Actual	100.1	106.5	121.1	136.2	139.7
1996 Projection	139.6	164.9	195.1	231.2	274.3
Difference	-39.5	-58.4	-74.0	-95.0	-134.6

Figure 2.1: Provincial Share in the Divisible Pool Taxes



The table followed by the graphical presentation clearly indicates the wide gap between the actual collection and the projection of 1996 NFC Report. In the first year of the Award, provinces received less transfers to the tune of Rs.40 billion, which was increased to Rs.135 billion in the terminal year of the Award i.e. 2001-02. It is evident that the tax receipts have been projected ambitiously and achieving the target remained difficult.

2.2: Interim arrangements of 2006

The provincial governments were complaining that the federal transfers were not as projected and as such they were facing financial hardship. On the other hand, the Commission was unable to reach a consensus. During the financial year 2005-06, after adding Grants in Aid to NWFP and Balochistan and District Support Grant, the provinces were receiving approximately 43% of the Divisible Pool Taxes. Keeping the financial need of the provinces in view, the President enhanced provincial share in the Divisible Pool Taxes through Distribution of Revenues and Grants-in-Aid (Amendment) Order, 2006. Through this amendment, all the four provinces were made eligible for Grants-in-Aid. The Grants-in-Aid was fixed at Rs.27.75 billion to be increased annually in line with increase in the Divisible Pool taxes. As a result of the revised distribution arrangement, after adding Grants-in-Aid, the provinces received 45% of the Divisible Pool Taxes in the financial year 2006-07 as against 43% (approximately). This 45% would be gradually increased to 50% in the financial year 2010-11. As a result of this interim arrangement, the provinces comparatively received a higher share vis-à-vis the 1996 Award.

7th NFC

3.1: Constitution and composition;

The 7th NFC was constituted on 21st July, 2005 (Annex-VII). After the general elections and with the induction of new political governments both at the center and provinces, it had become important to get consent of the provinces regarding the non-statutory members. The NFC was reconstituted on 24th July, 2009 after confirmation from the provinces with the following composition (Annex-VIII):

(1)	Minister for Finance Government of Pakistan	Chairman
(2)	Minister for Finance Government of the Punjab	Member
(3)	Minister for Finance Government of Sindh	Member
(4)	Minister for Finance Government of NWFP	Member
(5)	Minister for Finance Government of Balochistan	Member
(6)	Mr.Abdul Ghafoor Mirza (Punjab)	Member
(7)	Mr.Kaiser Bengali (Sindh)	Member
(8)	Senator Haji Muhammad Adeel (NWFP)	Member
(9)	Dr. Gulfaraz Ahmed (Balochistan)	Member

ToR assigned to the Commission are at Annexes-VII and VIII.

3.2: Deliberations

3.2.1: First NFC Meeting

The first meeting of the reconstituted NFC was held at Islamabad on August 27-28, 2009. All the members of the Commission presented their viewpoint in detail before the Commission in this meeting. Federal Finance Secretary presented the overall fiscal resource position of the Federal Government whereas the provincial governments presented their respective positions.

The Chairman NFC was of the view that each member of the Commission should table the issues to be resolved after which an in-depth discussion would be held on every issue. The following issues were thus identified:

(i) Horizontal distribution formula : adoption of multiple indicators;

(ii) Rationalization of distribution criteria for Development Surcharge on Gas;

(iii) Net Profit from hydro electric stations [dispute of NWFP Government versus WAPDA];

(iv) GST on Services : interpretation of constitutional provisions;

(v) War on Terror;

(vi) Distribution of $1/6^{th}$ of GST.

(vii) Vertical distribution;

(viii) Benchmarking.

After identification of above issues, it was debated that whether the issue of vertical distribution of resources formula be evolved or formula for horizontal distribution of resources be decided first. The Sindh Province was of the view that the main responsibility of NFC was to devise a formula for horizontal distribution irrespective of the size of resources. Sindh maintained that any change from the single criterion formula is likely to reduce Punjab's share. Thus, in order to be fair to

Punjab, it would be necessary to raise the vertical transfers at least to the extent of Punjab's absolute loss. Thereafter, it would become easier to finalize vertical formula. Punjab province was, however, of the view that it would be appropriate to evolve formula for vertical distribution of resources in the first instance. To resolve the issue, the Commission constituted two sub committees with specific TORs to resolve the issues identified above.

3.2.2: Sub Committees & their deliberations

Sub Committee-I was headed by the Federal Finance Minister and consisted of all the members of the Commission. The issues before the Sub Committee-I were devising a formula for horizontal distribution of Divisible Pool Taxes amongst the provinces, War on Terror, Net Hydel Profit, Gas Development Surcharge (GDS) and General Sales Tax (GST) on Services. The Committee after detailed deliberations decided that War on Terror and net Hydel profit should be discussed outside NFC. The viewpoint of Sindh and Balochistan was presented on the issue of GDS before the Committee. It was decided that Ministry of Petroleum & Natural Resources and Oil and Gas Regulatory Authority (OGRA) would be requested to give presentations expressing their point of view. On the issue of GST on Services, it was decided that Government of Sindh would arrange a legal expert who would give his/her point of view. In addition, Federal Board of Revenue (FBR) would also present its point of view before the Commission.

The main task of the Sub Committee-II was to determine vertical distribution of resources between Federal Government and its federating units and benchmarks for the FBR receipts, non-tax receipts, provincial receipts and current and development expenditures of the Federal and Provincial governments. Federal Government presented its estimation before the Committee. It was proposed that the Budget Estimates (BE) of current financial year with minor adjustments be adopted as a benchmark by the Commission. Furthermore, the historical growth trend was proposed to be applied for the next five years. The provincial Finance Secretaries were of the view that due to tight budgetary position they had underestimated the expenditures and as such these could not be used as benchmarks. It was decided that in the next meeting provinces would submit their macroeconomic framework. Federal Government would also revise its framework and submit it to the Committee. Accordingly the provinces submitted their estimates before the Committee in the next meeting where it was decided that these estimates would be placed before the Commission for discussion and decision.

3.2.3: NFC Meetings (2nd & 3rd)

The second meeting of the NFC was held on 18th September, 2009 at Islamabad in the Conference Room of Finance Division. The Government of Sindh gave a detailed presentation on the issue of rationalization of GDS distribution mechanism. It was clearly stated by Government of Sindh that the province of Sindh was neither in favour of confrontation nor in favour of encroaching the territories of other provinces but the vested interests of the province was that the rights and interests of every provinces should be safeguarded. The least developed provinces should be able to exploit their resources fully for development of their areas as development in other parts of the country would result in less migration of the people. Therefore Sindh Province would support the revision of GDS formula to benefit Balochistan but not at the cost of Sindh province. The presentation was followed by a response from Dr. Gulfaraz Ahmad, Member (Balochistan) and a detailed presentation by Chairman, Oil and Gas Regulatory Authority (OGRA).). It was agreed that the provinces producing gas must be given due incentives so that they may be encouraged to boost production and the dichotomy, if existed, must be removed. A committee consisting of the four non-statutory members, Secretary Petroleum and Chairman, OGRA was constituted. Chairman OGRA was nominated as its Coordinator and the Committee opted for Secretary Petroleum as its Chairman. The Committee was tasked to submit its report in the next of meeting of NFC scheduled at Quetta.

The third meeting of the Commission was held at Quetta on October 12-13, 2009. In this meeting, Sindh Province gave a presentation on GST regime and reiterated that Sindh has lost a total of Rs.196 billion since 2001 on account of various anomalies and desired for their removal. FBR gave a presentation on the legal position on the GST on Services imposed in central excise mode. The independent legal expert arranged by Government of Sindh also gave a detailed presentation on its legality. The expert was of the view that with the abolition of Central Excise Act, 1944 and enactment of Federal Excise Act, 2005 the constitutional protection provided under Article 279 ceased to exist. The taxation powers had clearly been spelt out in the Federal Legislative List and the GST on Services did not exist in the Constitution. Chairman NFC accepted the contention of the legal expert and accordingly the Commission accepted that GST on Services was the constitutional domain of the provinces and Federal Government would make necessary amendments in the Federal Excise Act in order to enable provinces to levy the tax.

Secretary Petroleum on behalf of the Committee presented a mechanism for distribution of development surcharge on natural gas. The Commission, after a detailed discussion, approved this mechanism. In the mechanism it was proposed that for the purpose of calculating GDS, royalty on natural gas and GDS would be notionally clubbed into one and the rate per MMBTU would be worked out. Thereafter, royalty would be distributed based on the existing mechanism keeping in view the constitutional obligations whereas GDS would be distributed by making adjustments based on this effective rate. The impact of this revised mechanism is evident from the following tables with data for the year 2008-09:

Table 3.1: Working of the average effective rate

Province	GDS	Royalty	Total	Volume	Effective Rate
	Rs Million	Rs Million	Rs Million	BBTU	Rs / MMBTU
Balochistan	4,282	4,716	8,998	233,179	38.59
NWFP	469	876	1,345	32,533	41.34
Punjab	1,121	1,207	2,328	61,939	37.59
Sindh	15,361	27,696	43,057	873,840	49.27
Pakistan	21,233	34,495	55,728	1,201,490	46.38

Table 3.2: Share of each province showing gain/losses

Rs. In million

Province	Current Mechanism			Proposed Mechanism			Gain/ (Loss)
	GDS	Royalty	Total	GDS	Royalty	Total	
Balochistan	4,282	4,716	8,998	6,099	4,716	10,815	1,817
NWFP	469	876	1,345	633	876	1,509	164
Punjab	1,121	1,207	2,328	1,666	1,207	2,873	545
Sindh	15,361	27,696	43,057	12,835	27,696	40,531	(2,526)
Pakistan	21,233	34,495	55,728	21,233	34,495	55,728	0

As evident from the table, the new mechanism would result in financial loss to the tune of Rs.2.5 billion to the Sindh Province. The Sub Committee, in order to compensate the Sindh Province proposed increase in the rate of excise duty from the existing rate of Rs.5.09 per MMBTU to Rs.8.0 per MMBTU. However, in the meeting it was decided that the rate of excise duty would be raised to Rs.10.0 per MMBTU. This increase in the rate of excise duty would not only mitigate the loss of the Sindh province but will increase the benefit in financial terms to all the four provinces. The impact of this increase is worked out as follows:

Table 3.3: Impact of increase in the rate of Excise Duty

Province	Volume	Current Excise Duty @ Rs 5.09/MMBTU	Excise Duty @ Rs.10/MMBTU	Increase
	MMBTU	Rs. billion	Rs. billion	Rs. billion
Balochistan	233,179	1.2	2.3	1.1
NWFP	32,533	0.2	0.3	0.1
Punjab	61,939	0.3	0.6	0.3
Sindh	873,840	4.4	8.8	4.4
Pakistan	1,201,490	6.1	12.0	5.9
Increase in Gas Price		2.00%		

The GDS for the province of Balochistan based on the above new mechanism would be worked out for the period from July 1, 2002 to June 30, 2009 as the five years period of 1996 Award ended on 30th June, 2002. The amount subject to a maximum of Rs.10 billion would be paid by the Federal Government to Balochistan province over a period of five years.

The Sub Committee-III was also constituted to deliberate upon the horizontal distribution including applicability of multiple indicators in the 3rd meeting.

3.2.4: Sub Committee-III

Sub Committee-III was constituted to deliberate upon applicability of the multiple indicators on horizontal distribution of resources. The Committee consisted of the four non-statutory members. The members having divergent views on the horizontal distribution could not reach a consensus and it was decided to submit the viewpoint of each member before the Commission for discussion/decision.

3.2.5: NFC Meetings (4th, 5th & 6th)

The fourth meeting of the Commission was held at Peshawar on October 29, 2009. The meeting started with a presentation by Governor, State Bank of Pakistan on the monetary policy and loans extended by commercial banks and Development Financial Institutions (DFIs). The Special Secretary Finance, Finance Division, Government of Pakistan presented the revised macroeconomic framework and the position of the Federal Government under various options of vertical distribution, which were as follows:

- Existing with provincial share in the Divisible Pool Taxes net at 50%;
- Option-1 with provincial share at 52.5%; and
- Option-2 with provincial share at 55%.

Under the options proposed the overall fiscal deficit would neither be consistent with the one agreed with International Monetary Fund (IMF) nor desirable for a stable economy. The Sub Committee-III informed the Commission that the members had divergent views on various indicators i.e. population, poverty/ backwardness, inverse population density/area and revenue generation/collection. The Commission started deliberations on possible indicators. Punjab showed its willingness to adopt multiple indicators. All the four provinces agreed on adopting population as a major indicator. Poverty/backwardness was the second indicator supported by all the four provinces. However there were differences over using either area or Inverse Population Density (IPD) as an indicator and revenue collection versus generation.

The fifth meeting was held at Karachi on November 18-19, 2009. On the first day of the meeting various options on vertical distribution were discussed at length. The Chairman observed that the tax base needed to be expanded. He desired that the entire projections should be reworked by increasing the tax to GDP ratio to 15% by the terminal year of the Award i.e. 2014-15. This working was carried out and presented to the Commission on the same day. Pending decision on vertical distribution, Sindh province suggested to discuss the horizontal distribution formula on the next day as per its agenda first which was supported by the Balochistan and NWFP. The suggestion was accepted by the Commission.

The second day was spent discussing various indicators of horizontal distribution. Detailed discussions were held to adopt Inverse Population Density or Area as one of the indicators. Sindh and Balochistan provinces were in favour of IPD whereas Punjab and NWFP supported Area as indicator. Maintaining the spirit of accommodation, both the provinces also agreed to adopt IPD as one of the indicators. Consensus was emerged on using population, IPD and poverty/ backwardness as three possible indicators. However, difference still existed on the use of either revenue collection or revenue generation. It was also decided that an upfront amount (1% of Divisible Pool Taxes was decided later on) for War on Terror will be given to NWFP province.

The sixth meeting of the Commission was held at Lahore on December 9-12, 2009. During the first day, detailed discussions were held on using indicators and possible weights to be assigned to the indicators. Special Secretary Finance, Finance Division gave a detail presentation in this regard. The remaining two days were spent deliberating on the vertical and horizontal distribution mechanism informally. The Chief Ministers of the four provinces were also associated with the deliberations. At the end of the deliberation, following record note was signed by all the members of the Commission and endorsed by the Chief Ministers:

"The Federal Government recognized the need of the provinces for a larger share in the Divisible Pool Taxes since provinces are assigned the task of provision of basic services like health, education, water supply and sanitation.

I. **Divisible Pool Taxes**: The size of the Divisible Pool Taxes is proposed to be increased in the interest of national solidarity and provincial harmony. Federal Government shall make major efforts to boost tax revenue. In addition, the Divisible Pool Taxes will be increased by reducing the collection charges from 5% to 1%.

II. **Sales Tax on Services:** NFC recognized that sales tax on services is a provincial subject under the Constitution of Pakistan, and may be collected by respective provinces, if so desire.

III. **War on Terror:** The Federal Government and all the four provinces recognize the role of NWFP as a frontline state against war on terror. The Federal Government reiterates its commitment to bear all expenditures incurred on the War on Terror. However, as a gesture of support by all provinces and the Federation, 1% of the total Divisible Pool Taxes has been earmarked for NWFP as an additional resource for War on Terror during the Award period. This would be equivalent to 1.83% of the provincial pool.

IV. **Vertical Distribution:** The provincial share of the Divisible Pool Taxes will increase from the present 47.5% to 56% in the first year of NFC and 57.5% in the remaining years of the Award.

V. **Horizontal Distribution:** The discussions among provinces on horizontal distributions of the Divisible Pool Taxes were held in a spirit of utmost cordiality and accommodation. All four Provincial Chief Ministers actively participated in the discussions.

- Long standing demand of Sindh, NWFP and Balochistan to distribute the Divisible Pool Taxes according to multiple indicators has been accepted.
- The NFC expressed its special thanks to the government of Punjab for showing grace in acceptance of this demand.

VI. **The new formula has the following features**:-

i) The Federation and the provinces of Punjab, Sindh and NWFP accepted the special needs of Balochistan and agreed to provide Balochistan Rupees 83 billion (9.09 %) of the provincial pool in the first year of the Award. Any shortfall in this amount would be made up by the Federal Government from its own resources. This arrangement for Balochistan would also remain protected through the remaining four years of the Award.

ii) The province of Sindh would receive an additional transfer of Rs.6 billion from the Federal Government which is equivalent of 0.66% of the provincial pool.

iii) The multiple indicators and their respective weights as agreed upon are:-

a.	Population	82.0%
b.	Poverty/backwardness	10.3%
c.	Revenue collection/generation	5.0%
d.	Inverse Population Density (IPD)	2.7%

iv) After giving effect to the special needs of Balochistan and application of the aforesaid multiple indicators, the final percentage share of the provinces will be as under:

Punjab	51.74%
Sindh	24.55%
NWFP	14.62%
Balochistan	9.09%

The Federation and the provinces reciprocated to the spirit of accommodation shown by each in reaching an amicable agreement on vertical and horizontal distribution of resources for the purpose of the 7th NFC Award."

Macroeconomic Framework and the Fiscal Resource Position

4.1: Macroeconomic Framework

The macroeconomic framework (MEF) was based on the following assumptions:

Table 4.1: Projections for nominal GDP

	Benchmark 2009-10	Projections				
		2010-11	2011-12	2012-13	2013-14	2014-15
Real GDP Growth (%)	3.0	4.0	4.5	5.0	5.5	6.0
Inflation (Period Average %)	10.0	7.0	6.0	6.0	6.0	6.0
Nominal GDP (Rs billion)	14,837	16,510	18,288	20,355	22,763	25,563
Nominal GDP Growth (%)	13.3	11.3	10.8	11.3	11.8	12.3

The tax to GDP ratio currently stands at 9.3%. Federal Government is committed to undertake efforts to improve tax to GDP ratio including the implementation of Value Added Tax (VAT). As such it is expected that the tax to GDP ratio of FBR taxes would be around 12.3% by 2014-15. However, Chairman NFC observed that in order to meet the growing needs of the provinces, the tax to GDP ratio must reach 15%. He informed the NFC that the tax to GDP ratio of our neighboring countries was around 20% of GDP. Accordingly, there was consensus amongst the members of the Commission that the tax to GDP ratio by the terminal year i.e. 2014-15 should be increased to 15%. Provinces would also take efforts to improve the provincial own tax to GDP ratio respectively. Accordingly, the following assumptions were approved by the Commission:

Table 4.2: Projections of Tax Receipts

	Benchmark	**Projections**				
	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
FBR Taxes	9.30	10.30	11.20	12.00	12.70	13.25
Surcharges	0.90	0.80	0.80	0.70	0.60	0.60
Provincial taxes	0.50	0.65	0.80	0.90	1.00	1.15
Total	10.70	11.75	12.80	13.60	14.30	15.00
FBR tax efforts		*1.00*	*0.90*	*0.80*	*0.70*	*0.55*
Provinces' tax efforts		*0.15*	*0.15*	*0.10*	*0.10*	*0.15*

All the projections were based on the above assumptions.

4.2: Benchmarking

4.2.1: Federal Receipts

Federal Receipts consisted of the following:

(i) **FBR Receipts:** The benchmarking and projections for the FBR receipts are based on the above assumptions;

(ii) **Surcharges:** This includes development surcharge on natural gas and petroleum development levy. The benchmarking and projections are based on the assumptions given above.

(iii) **Non-tax Receipts:** The non-tax receipts include State Bank of Pakistan (SBP) profits, dividends, interest receipts and receipts from civil administration among others. As a result of privatization policy of the government and prevalent situation, it is expected that the profits from SBP and dividends would shrink. As such the non-tax receipts have been taken as Rs.474.8 billion by making downward adjustment against the budgeted figure of Rs.627 billion. This has been projected by applying Annual Compound Growth Rate (ACGR) of 7.8%.

4.2.2: Federal Expenditures

The benchmark for the current expenditures of the Federal Government has been fixed at Rs.1,736.27 billion after making necessary adjustments, considering these expenditures as a result of security situation of the country. In addition, Federal Government has also agreed to pick up the following expenditures:

(i) Rs.110 billion accrued against WAPDA as a result of the Arbitral Tribunal payable to WAPDA. Rs.10 billion has been paid during the current financial year 2009-10. The balance Rs.100 billion will be paid to NWFP Government in four years at the rate of Rs.25 billion per annum.

(ii) Rs.10 billion to Balochistan province on account of Gas Development Surcharge arrears to be accrued on applying the new mechanism of distribution for the period from 2002-03 to 2009-10.

(iii) Rs.120 billion payable as Gas Development Surcharge arrears prior to 1991 announced in the Balochistan Package “Aaghaz-e-Huqooq-e-Balochistan” to be payable in 12 years.

(iv) Amount equivalent to 0.66% of the provincial share in the Divisible Pool Taxes to be paid to the province of Sindh to compensate the losses of Octroi and Zilla Tax (OZT) collection.

The current expenditure of the Federal Government has been projected to decrease as a percentage of GDP.

The development expenditure of the Federal Government has been adjusted downward in relation to the budget estimates of the current financial year. The figure has been adopted as Rs.358.0 billion. This has been further projected at the ACGR of 17.1%.

4.2.3: Provincial Receipts

The Provincial tax receipts have been benchmarked and further projected based on the assumptions already explained. However, the non-tax receipts have been projected at 11.5%.

4.2.4: Provincial Expenditures

The budget estimates for the current expenditures for the financial year 2009-10 have been adopted as benchmarks and the same has been projected at the rate of 14%. The budget estimates for the development expenditures have also been adopted as benchmarks. However, further projections have been made keeping in view the surpluses available to each province under the revised distribution formula and other resources available to provinces.

In summary, the benchmarks and the ACGR for the receipts and expenditures of the federal and provincial governments are tabulated as follows:

Table 4.3: Benchmarks and ACGR for Projection

	Benchmark 2009-10	ACGR applied
FBR Receipts	1,380.00	19.67%
Surcharges	133.53	1.84%
Non Tax Receipts	483.70	7.38%
Current Expenditure	1,736.27	6.95%
Development Expenditure	358.00	17.01%
Provinces' own tax receipts	**74.20**	**31.70%**
Punjab	*44.52*	*31.70%*
Sindh	*23.00*	*31.70%*
NWFP	*4.45*	*31.70%*
Balochistan	*2.23*	*31.70%*
Provinces' own Current Expenditure	**661.35**	**14.00%**
Punjab	*314.87*	*14.00%*
Sindh	*213.40*	*14.00%*
NWFP	*80.00*	*14.00%*
Balochistan	*53.08*	*14.00%*
Provinces' Development Expenditure	**319.70**	**32.93%**
Punjab	*175.00*	*31.35%*
Sindh	*75.00*	*31.22%*
NWFP	*51.16*	*33.82%*
Balochistan	*18.54*	*47.98%*

Based on the above assumptions and the proposed revenue sharing criteria, the fiscal positions of the Federal Government and the provincial governments are at Annex-IX [Table 1-6].

Revenue Sharing Criteria

5.1: Vertical Revenue sharing

The approach adopted in the 1996 NFC Award for the vertical sharing of the Divisible Pool Taxes was to first determine the national resource picture by clubbing the total resources available at federal and provincial levels together with the borrowings to fill the gap of acceptable/ targeted national budget deficit. Then the expenditures, both current and development of both federal and provincial governments, were assessed and determined through benchmarking. While assessing the expenditures requirements, priority expenditures such as defence, debt servicing and social sector expenditures were protected. Keeping in view the requirements of the federal and provincial governments, the share from the Divisible Pool Taxes for both the federal and provincial governments was determined.

The total resources available were the tax and non-tax receipts of the Federal Government, tax and non-tax receipts of the provincial governments and the borrowing to finance the budget deficit consistent with a stable economy. The projected resources are accordingly tabulated as follows:

Table 5.1: National Resource Picture

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Federal	1,997.23	2,337.58	2,724.91	3,138.49	3,651.81	4,223.98	16.2%
Tax receipts	1,513.53	1,842.58	2,194.56	2,588.90	3,037.21	3,533.40	18.5%
out of which FBR	*1,380.00*	*1,710.50*	*2,048.26*	*2,442.60*	*2,890.90*	*3,387.10*	*19.7%*
Non-tax receipts	483.70	495.00	530.35	549.59	614.60	690.58	7.4%
Provinces	163.20	206.42	256.00	305.30	364.23	447.47	22.4%
Tax receipts	74.20	107.32	146.30	183.20	227.63	293.97	31.7%
Non-tax receipts	89.00	99.10	109.70	122.10	136.60	153.50	11.5%
Borrowings	727.01	693.42	603.50	631.01	660.13	715.76	-0.3%
Total	2,887.45	3,237.42	3,584.42	4,074.79	4,676.16	5,387.22	13.3%
GDP (mp)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

A comparison of the composition of National Resource Picture in terms of Federal, provinces and borrowings as well as in terms of tax, non-tax and borrowings are given as follows:

Figure 5.1: Comparison of Receipts under Federal, Provincial and Borrowings

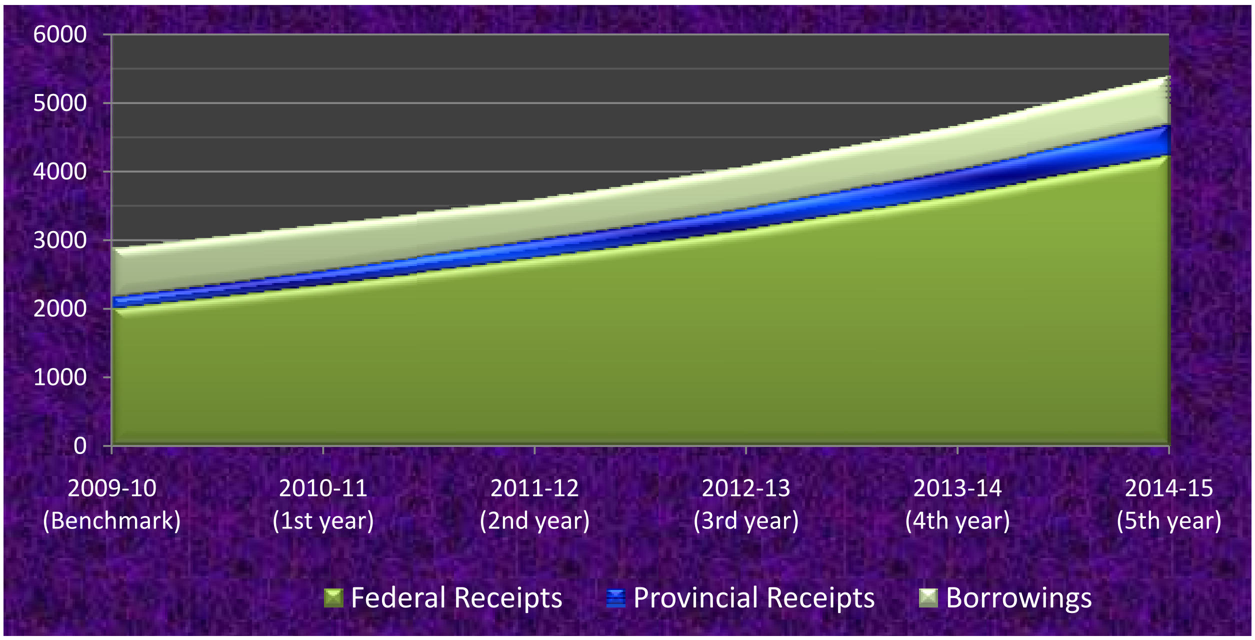
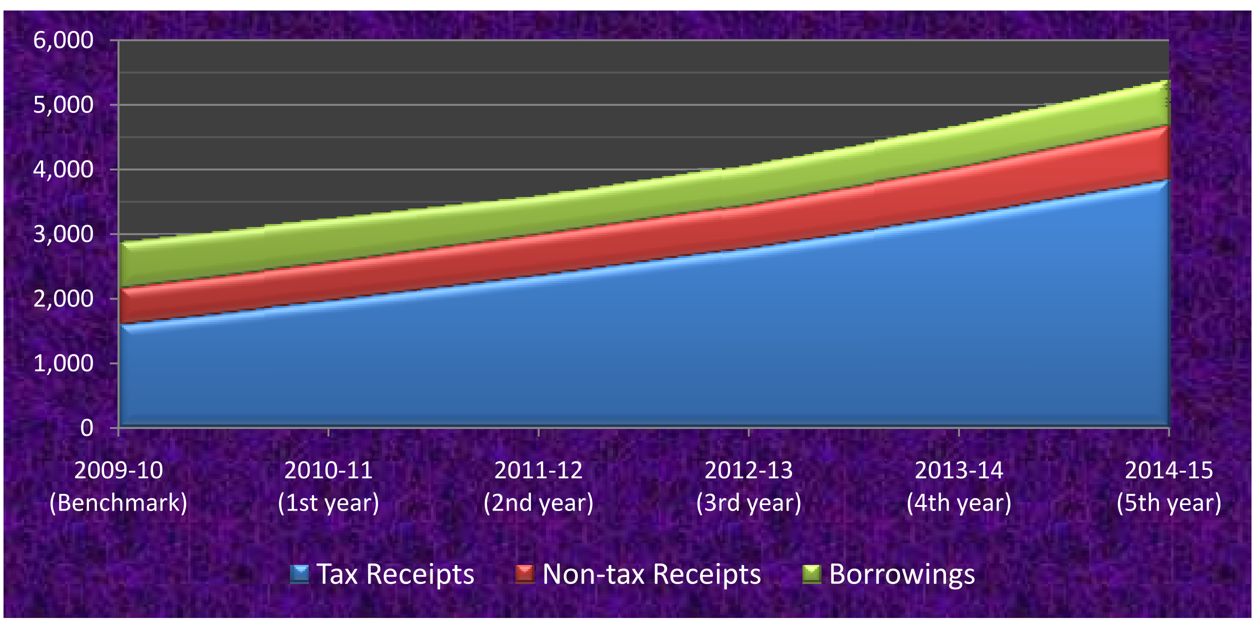


Figure 5.2: Comparison of Receipts under Tax, Non-tax and Borrowings



The approach adopted by the seventh NFC is rooted on the premise that most of the development work needs to be initiated at the provincial level to ensure results at grass root level. Furthermore, the responsibility of providing social sectors services also rest with the provincial governments. As such the needs of the provinces must be addressed first.

The Commission was also of the unanimous opinion that the vertical programs of the Federal Government were not providing the desired results and should be thus reduced. Instead greater resources should be placed at the disposal of the provincial governments. The Commission was also of the view that there is a duplication of functions i.e. the same functions were being performed by departments of the federal and provincial governments resulting in wastage of government resources. Thus, instead of determining the expenditures requirement of the federal and provincial governments simultaneously, in the first instance the requirements of the provincial governments would be assessed and worked out, and the share of the provinces in the Divisible Pool Taxes net would then be determined. After setting aside the provincial shares, the federal expenditures would be adjusted to maintain the borrowing level at an acceptable level.

Initially Finance Minister/Chairman NFC offered 55% from the Divisible Pool Taxes net and in addition offered to reduce the cost of collection to 1% (being the actual incurred cost). However, on the instance of the provinces, the Chairman agreed that in the first year of NFC i.e. 2010-11, the provincial share in the Divisible Pool Taxes would be 56% and for the remaining years the share would be 57.5%. However, 1% of the undivided Divisible Pool Taxes net would be set aside and given to the province of NWFP for meeting the expenses on War on Terror as a goodwill gesture from both federal and provincial governments. Based on this sharing arrangement, the fiscal position of the federal and provincial governments (combined) has been worked out. [Annex-IX (Table-1)]. In order to maintain the borrowings at an acceptable level, the Federal Government has to make adjustments in the consolidated expenditures. The projected requirement of adjustments is tabulated as follows:

Table 5.2: Adjustments in the Federal PSDP (As % of GDP)

	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)
Acceptable OFD	4.2%	3.3%	3.1%	2.9%	2.8%
Projected OFD based on the proposed sharing arrangements	5.5%	4.9%	4.6%	4.3%	4.1%
Adjustments required	1.3%	1.6%	1.5%	1.4%	1.3%

In addition to the substantial increase in the provincial share out of the Divisible Pool Taxes, the Finance Minister/Chairman NFC also agreed that the Federal Government would pick up following liabilities:

1. The outstanding dues of Rs.110.0 billion accrued against WAPDA as a result of Award of the Arbitral Tribunal, Rs.10.0 billion has been paid during the current financial year 2009-10. The balance amount of Rs.100.0 billion shall be paid to NWFP province in four year's period at the rate of Rs.25.0 billion per annum.

2. One of the TOR of the NFC was rationalization of the distribution formula of the development surcharge on Natural Gas. During the third meeting held at Quetta, a consensus was developed for a new distribution formula. However, Government of Balochistan was of the view that the five years period of sixth NFC expired on 30th June, 2002 and the proposed formula should be implemented with effect from 01.07.2002. The Chairman agreed that GDS due to Balochistan based on this proposed formula would

be worked out and the amount subject to a maximum of Rs.10.0 billion would be paid by the Federal Government in five years.

3. Government of Sindh had a claim of less payment on account of 1/6th of GST which was basically meant for the local governments. The NFC also agreed to make a yearly grant equivalent to 0.66% of the provincial share in the divisible pool to Government of Sindh.

5.2: Horizontal Revenue Sharing

The second main issue before the NFC for decision is horizontal distribution of Divisible Pool Taxes. As per interim arrangements 2006, distribution of resources amongst the provinces is as follows:

- Provincial share minus amount equivalent to 1/6th of sales tax are distributed based on the ratio of population of each province.
- Amount equivalent to 1/6th of sales tax are distributed based on 50% on the ratio of population and 50% on the ratio of Octroi and Zilla Tax audited collection for the financial year 1998-99.
- Grants-in-Aid are distributed amongst the provinces of Punjab, Sindh, NWFP and Balochistan at the ratios of 11%, 21%, 35%, 33% respectively.

The shares of each province in the benchmark year i.e. 2009-10 are as follows:

Table 5.3: Sharing Arrangements based on PO No.1 of 2006

	Punjab	Sindh	NWFP	Balochistan	Total
Div. pool minus 1/6th of sales tax	281.438	116.333	67.808	25.072	490.651
	57.36%	*23.71%*	*13.82%*	*5.11%*	*100.00%*
1/6th of Sales Tax	39.585	27.591	7.862	4.133	79.170
	50.00%	*34.85%*	*9.93%*	*5.22%*	*100.00%*
Grants-in-Aid	4.972	9.492	15.819	14.915	45.198
	11.0%	*21.0%*	*35.0%*	*33.0%*	*100.0%*
Total:	**325.994**	**153.416**	**91.489**	**44.120**	**615.019**
	53.01%	*24.94%*	*14.88%*	*7.17%*	*100.0%*

Provinces agreed to use multiple indicators for horizontal resource distribution after detailed deliberations. However, it was principally agreed that no province would receive lesser benefit in absolute terms based on the new sharing arrangements. Consensus was developed for using the following indicators for resource distribution:

- Population;
- Inverse Population Density (IPD);
- Poverty/backwardness; and
- Revenue Collection/Generation.

Brief positions of each of the indicators are given in the following paragraphs.

5.2.1: Population:

The province-wise ratios of population as per 1998 Census are as follows:

Table 5.4: Province-wise Population (1998 Census)

	Punjab	Sindh	NWFP	Balochistan	Total
Population	73,621,290	30,439,893	17,743,645	6,565,885	128,370,713
	57.36%	23.71%	13.82%	5.11%	100.00%

5.2.2: Inverse Population Density

Based on the 1998 Population Census, province-wise ratios of IPD are worked out as follows:

Table 5.5: Province-wise Inverse Population Density

	Punjab	Sindh	NWFP	Balochistan	Total
Area (in sq. km)	205,345	140,914	74,521	347,190	767,970
As % of total	*26.74%*	*18.35%*	*9.70%*	*45.21%*	*100.00%*
Population	73,621,290	30,439,893	17,743,645	6,565,885	128,370,713
Population density	358.52487	216.01752	238.10262	18.91150	831.56
Inverse population density	0.0028	0.0046	0.0042	0.0529	0.0645
As % of total	*4.32%*	*7.18%*	*6.51%*	*81.99%*	*100.00%*

5.2.3: Human Development Index (HDI) or Poverty

No reliable data on HDI or poverty is available. Poverty Reduction Strategy Paper-I (PRSP-I) titled "Accelerating Economic Growth and Reducing Poverty: the Road Ahead" report published by the PRSP Secretariat of Finance Division in the year 2003 has illustrated poverty levels of both rural and urban regions separately of each province based on Household and Income Expenditure Survey, 1998-99 as follows:

Table 5.6: Incidence of Poverty in Provinces 1998-99

Provinces	Urban	Rural
Punjab	26.50%	32.40%
Sindh	19.00%	29.20%
NWFP	31.20%	44.30%
Balochistan	28.40%	24.60%

As the PRSP report does not provide aggregate data, therefore the same has been aggregated based on urban and rural population proportion of 1998 census. It may be added that the above poverty level has been derived based on the data of 1998. The aggregated position is as follows:

Table 5.7: Working of Province-wise Poverty

	Incidence of Urban poverty [PRSP-1]	Population urban proportion [1998 census]	Incidence of Rural poverty [PRSP-1]	Population Rural proportion [1998 census]	Aggregate Poverty	Poverty translating into percentage
Punjab	26.50%	31.27%	32.40%	68.73%	30.56%	25.0%
Sindh	19.00%	48.75%	29.20%	51.25%	24.23%	19.8%
NWFP	31.20%	16.87%	44.30%	83.13%	42.09%	34.4%
Balochistan	28.40%	23.90%	24.60%	76.10%	25.51%	20.8%

The Pakistan National Human Development Report 2003 published by UNDP lists HDI of each province. Based on this report, the province-wise position is as follows:

Table 5.8: Province-wise Human Development Index (UNDP Report)

Area	HDI	%	Backwardness level	%
Pakistan	0.541		0.46	
Punjab	0.557	26.4%	0.44	23.4%
Sindh	0.540	25.6%	0.46	24.3%
NWFP	0.510	24.2%	0.49	25.9%
Balochistan	0.499	23.7%	0.50	26.5%
	2.106	100.0%	1.894	100.0%

In the year 2008, Statistics Division was assigned the task to work out province-wise HDI. They compiled a report which was circulated to all members of the NFC. According to this report, the province-wise HDI has been reported as follows:

Table 5.9: Province-wise Human Development Index (FBS Report)

Area	Education Index	Health Index	Facility Index	Economy Index	HDI	%	Poverty level	%
Pakistan	0.768	0.601	0.690	0.183	0.561		0.44	
Punjab	0.839	0.653	0.716	0.199	0.602	28.5%	0.398	21.1%
Sindh	0.695	0.548	0.662	0.125	0.507	24.0%	0.493	26.2%
NWFP	0.693	0.581	0.715	0.264	0.563	26.6%	0.437	23.2%
Balochistan	0.591	0.405	0.602	0.173	0.443	20.9%	0.557	29.5%
					2.115	100.0%	1.885	100.0%

To sum up, a comparison of all the above three reports is as follows:

Table 5.10: Province-wise Backwardness/ Poverty (Summary)

	Punjab	Sindh	NWFP	Balochistan	Total
Statistics Div	21.11%	26.15%	23.18%	29.55%	100.00%
UNDP Report 2003	23.4%	24.3%	25.9%	26.5%	100.00%
PRSP-1 Report	25.0%	19.8%	34.4%	20.8%	100.00%

The Commission agreed to use average of the three reports, which is tabulated below:

Table 5.11: Province-wise Backwardness/ Poverty (Average)

Punjab	Sindh	NWFP	Balochistan	Total
23.17%	23.42%	27.83%	25.62%	100.00%

5.2.4: Revenue Generation and Revenue Collection

Accurate data on revenue generation was hard to ascertain. Sindh advocated the use of revenue collection as an indicator whereas the other three provinces demanded the use of revenue generation as an indicator. The Commission, after in-depth deliberations, decided to use both by giving 50% weight to each indicator. Federal Board of Revenue (FBR) showed inability to provide data on revenue generation as they have no mechanism to collect data on generation basis. It was decided that the withholding tax paid on electricity consumption may be used as proxy for revenue generation. For the purpose the data of FBR Year Book 2007-08 was used as a basis. The province wise ratio is worked out as follows:

Table 5.12: Province-wise Tax Collection/Generation

Rs. billion

	Punjab	Sindh	NWFP	Balochistan	Total
Total Tax Collection excluding Islamabad in 2007-08	214,564	558,948	21,452	8,360	803,324
	27%	70%	3%	1%	100%
Withholding Tax on Electricity excluding Islamabad in 2007-08	3,320	1,455	370	111	5,257
	63.0%	28%	7%	2%	100%
Giving weight 50% each of the above	44%	50%	5%	1%	100%

The Federation and the provinces of Punjab, Sindh and NWFP accepted the special needs of Balochistan and agreed to provide Balochistan Rs.83 billion (9.09%) of the provincial pool in the first year of the Award. Any shortfall in this amount would be supplemented by the Federal Government from its own resources. This arrangement for Balochistan would also remain protected throughout the remaining four years of the Award based on annual budgetary projections.

The multiple indicators and their respective weights as agreed upon are:-

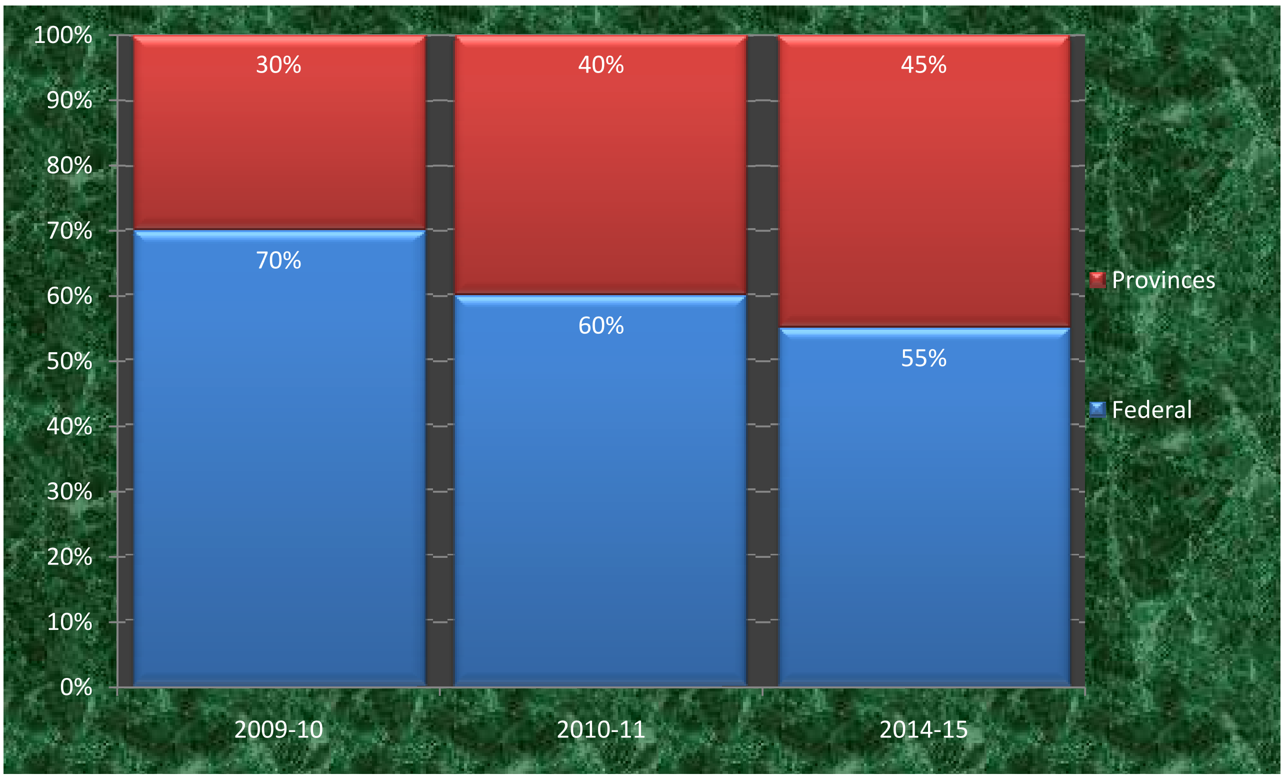
a) Population 82.0%
b) Poverty/backwardness 10.3%
c) Revenue collection/generation 5.0%
d) Inverse Population Density (IPD) 2.7%

After giving effect to the special needs of Balochistan and application of the aforesaid multiple indicators, the final percentage share of the provinces will be as under:-

- Punjab 51.74%
- Sindh 24.55%
- NWFP 14.62%
- Balochistan 9.09%

The projected resource available positions of each province are at Annex IX (Tables 1-6). As a result of the new sharing arrangements, there would be a paradigm shift in the spending pattern of the Federal Government and provinces. This paradigm shift is evident from the following graph, which compares the spending patterns of the federal and provincial governments for the financial year 2009-10 (under the existing arrangements) with the projections of financial years 2010-11 (1st year) and 2014-15 (5th year) (under the new arrangements):

Graph 5.1: Spending Pattern of the Federal and Provincial Governments



Recommendations of the Commission

The NFC has made the following recommendations for approval of the President of the Islamic Republic of Pakistan:-

1. The Divisible Pool Taxes will consist of the following taxes:-

   (i) Taxes on income, including corporation tax, but not including taxes on income consisting of remuneration paid out of the Federal Consolidated Fund;

   (ii) Taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed;

   (iii) Export duties on cotton, and such other export duties as may be specified by the President;

   (iv) Wealth Tax;

   (v) Capital Value Tax;

   (vi) Customs duties;

   (vii) Federal excise duties, excluding excise duty on gas charged at well-head; and

   (viii) Any other tax which may be levied by the Federal Government.

2. The net proceeds of the Divisible Pool Taxes shall be derived after deducting 1% as collection charges.

3. The Federal Government reiterates its commitment to bear all expenditures incurred on the War on Terror in any part of Pakistan. The Federal Government and all the four provinces recognize the role of NWFP as a

frontline province against War on Terror. As a gesture of support by the Federal Government and all the provinces, 1% of the net proceeds of Divisible Pool Taxes will be earmarked for NWFP as an additional resource for War on Terror during the Award period. (This could be equivalent to approximately 1.8% of the provincial share in the Divisible Pool Taxes for the year 2010-11.)

4. After deducting the amounts as prescribed in Paras-2&3, of the balance amount of the proceeds of Divisible Pool Taxes, 56% shall be assigned to provinces during the financial year 2010-11 and 57.5% from the financial year 2011-12 onwards. The share of the Federal Government in the net Divisible Pool Taxes shall be 44% during the financial year 2010-11 and 42.5% from the financial year 2011-12 onwards.

5. It was agreed with consensus, for the first time, to include multiple indicators in the criterion for horizontal distribution amongst the provinces. The multiple indicators and their respective weights as agreed upon are:

i.	Population:	82.0%
ii.	Poverty/backwardness:	10.3%
iii.	Revenue collection/generation:	5.0%
iv.	Inverse population density:	2.7%

6. After giving effect to the special needs of Balochistan and application of the aforesaid multiple indicators, the final percentage share of the provinces for distribution of provincial share in the Divisible Pool Taxes will be as under:-

Punjab	51.74%
Sindh	24.55%
NWFP	14.62%
Balochistan	9.09%

7. The Federation and the provinces of Punjab, Sindh and NWFP have accepted the special needs of Balochistan and have agreed to provide Balochistan Rs.83 billion (9.09% of the provincial share in the Divisible Pool Taxes) in the first year of the Award. Any shortfall in this amount shall be made up by the Federal Government from its own resources. This arrangement for Balochistan would also remain protected throughout the remaining four years of the Award based on annual budgetary projections.

8. The province of Sindh would receive an additional transfer of an amount equivalent to 0.66% of the provincial pool from the Federal Government.

9. The net proceeds of Development Surcharge on Natural Gas shall be distributed amongst the provinces. For the purpose of distribution of development surcharge on Natural Gas, the royalty on Natural Gas and development surcharge would be notionally clubbed into one and the average rate per MMBTU would be worked out. Thereafter, Royalty on Natural Gas would be distributed in accordance with Article 161(1) of the Constitution whereas the development surcharge on Natural Gas would be distributed by making adjustments based on this average rate. The rate of excise duty on natural gas will be raised to Rs.10.0 per MMBTU in order to give effect to this formula.

10. The development surcharge on natural gas for Balochistan with effect from 01.07.2002 would be worked out and this amount, subject to maximum of Rs.10.0 billion, would be paid by the Federal Government in five years in five equal installments.

11. The net amount of royalty on Crude Oil shall be paid to the provinces according to production in each province as per current practice.

12. NFC recognizes that sales tax on services is a provincial subject under the Constitution of Pakistan, and may be collected by respective provinces, if they so desire.

13. The Federal and Provincial Governments should streamline their tax collection systems to reduce leakages and increase their revenues through efforts to improve taxation in order to achieve a 15% tax to GDP ratio by the terminal year i.e. 2014-15. Provinces would initiate steps to effectively tax the agriculture and real estate sectors.

14. Federal and provincial governments would develop and enforce mechanism for maintaining fiscal discipline at the federal and provincial levels.

15. The Federal Government may assist the provinces through specific grants in times of unforeseen calamities.

16. The meetings of the NFC would be convened regularly on a quarterly basis to monitor implementation of the Award in letter and spirit.

30/12/2009
Mir Asim Kurd
Finance Minister, Balochistan

Dr. Gulfaraz Ahmed
Member NFC, Balochistan
30/12/09

Muhammad Humayun Khan
Finance Minister, NWFP

Senator Haji Muhammad Adeel
Member NFC, NWFP

Tanvir Ashraf Kaira
Finance Minister, Punjab

A. Ghafoor Mirza
Member NFC, Punjab
30/12/2009

Syed Qaim Ali Shah
Finance Minister, Sindh

Dr. Kaiser Bengali
Member NFC, Sindh

30/12/2009
Shaukat Fayaz Ahmad Tarin
Federal Finance Minister/Chairman NFC

Annexes

Annex-I

Extract: Article 160 and 161

Article 160 of the Constitution of Islamic Republic of Pakistan

(1) Within six months of the commencing day and thereafter at intervals not exceeding five years, the President shall constitute a NFC consisting of the Minister of Finance of the Federal Government, the Ministers of Finance of the Provincial Governments and such other persons as may be appointed by the President after consultation with the Governors of the Provinces.

(2) It shall be the duty of the NFC to make recommendations to the President as to:-

a) The distribution between the Federation and the Provinces of the net proceeds of the taxes mentioned in Clause (3);

b) The making of grants-in-aid by the Federal Government to the Provincial Governments;

c) The exercise by the Federal Government and the Provincial Governments of the borrowing powers conferred by the Constitution; and

d) Any other matter relating to finance referred to the Commission by the President.

(3) The taxes referred to in paragraph (a) of Clause (2) are the following taxes raised under the authority of [(Majlis-i-Shoora) (Parliament)], namely:-

i) Taxes on income, including corporation tax, but not including taxes on income consisting of remuneration paid out of the Federal Consolidated Fund;

ii) Taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed;

iii) Export duties on cotton, and such other export duties as may be specified by the President;

iv) Such duties of excise as may be specified by the President; and

v) Such other taxes as may be specified by the President.

(4) As soon as may be after receiving the recommendations of the NFC, the President shall, by Order, specify, in accordance with the recommendations of the Commission under paragraph (a) of Clause (2), the share of the net proceeds of the taxes mentioned in Clause (3) which is to be allocated to each Province, and that share shall be paid to the Government of the Province concerned, and, notwithstanding the provision of Article 78 shall not form part of the Federal Consolidated Fund.

(5) The recommendations of the NFC, together with an explanatory memorandum as to the action taken thereon, shall be laid before both Houses and the Provincial Assemblies.

(6) At any time before an Order under Clause (4) is made, the President may, by order, make such amendments or modification in the law relating to the distribution of revenues between the Federal Government and the Provincial Governments as he may deem necessary or expedient.

(7) The President may, by order, make grants-in-aid of the revenues of the Provinces in need of assistance and such grants shall be charged upon the Federal Consolidated Fund.

Article 161 of the 1973 Constitution of Islamic Republic of Pakistan

(1) Notwithstanding the provisions of Article 78 the net proceeds of the Federal duty of excise on natural gas levied at, well-head and collected by the Federal Government, and of the royalty collected by the Federal Government, shall not form part of the Federal Consolidated Fund and shall be paid to the Province in which the well-head of natural gas is situated.

(2) The net profits earned by the Federal Government, or any undertaking established or administered by the Federal Government from the bulk generation of power at a hydro-electric station shall be paid to the Province in which the hydro-electric station is situated.

Explanation.- For the purposes of this clause "net profits" shall be computed by deducting from the revenues accruing from the bulk supply of power from the bus-bars of a hydro-electric station at a rate to be determined by the Council of Common Interests, the operating expenses of the station, which shall include any sums payable as taxes, duties, interest or return on investment, and depreciations and element of obsolescence, and over-heads, and provision for reserves.

Annex-II

Government of Pakistan
Ministry of Law, Justice, & Parliamentary Affairs
(Law and Justice Division)

No.F.2(2)-/91-Pub **Islamabad, the 22nd April, 1991**

The following Order made by the President on 20th April, 1991 is hereby published for general information:-

PRESIDENT ORDER NO. 1 OF 1991

WHEREAS, in pursuance of clause (1) of Article 160 of the Constitution, the President, by the Finance Division's Notification No. SRO 764(I)/90, dated the 23rd July, 1990, appointed a National Finance Commission to make recommendations, among other matters, as to the distribution between the Federation and the Provinces of the net proceeds of certain taxes;

AND WHEREAS the said Commission has submitted its recommendations with regard to the said distribution;

NOW, THEREFORE, in pursuance of clauses (4) and (7) of Article 160 of the Constitution, the President is pleased to make the following Order:-

1. **Short title and commencement.-** (1) This Order may be called the Distribution of Revenues and Grants-in-Aid Order, 1991.

(2) It shall come into force on the first day of July, 1991.

2. **Definition.-** In this Order, unless there is anything repugnant in the subject or context;

(a) **"net proceeds"** means, in relation to any tax, duty or levy, the proceeds thereof reduced by the cost of collection, as ascertained and certified by the Auditor-General of Pakistan; and
(b) **"taxes on income"** includes corporation tax but does not include taxes on income consisting of remuneration paid out of the Federal Consolidated Fund.

3. **Distribution of Revenues.-** (1) The Provincial Governments shall be assigned in each financial year a share equal to eighty percent of the net proceeds of the following taxes and duties levied and collected by the Federal Government in that year, namely:-

a. Taxes on income;
b. Taxes on sales and purchases;
c. Export duties on cotton;
d. Excise duties on tobacco and tobacco manufactures;
e. Excise duty on sugar.

4. **Allocation of shares to the Provincial Governments.-** The sum assigned to the Provincial Governments under Article 3 shall be distributed amongst the provinces on the basis of their respective population in the percentage specified against each:-

The Punjab	57.88%
Sind	23.28%
The North-West Frontier Province	13.54%
Balochistan	5.30%
Total:	100.00%

5. **Payment of net proceeds of royalty on crude oil.-** Each of the provinces shall be paid in each financial year as a share in the net proceeds of the total royalties on crude oil an amount which bears to the total net proceeds the same proportion as the production of crude oil in the Province in that year bears to the total production of crude oil.

6. **Payment of net proceeds of development surcharge on natural gas to the Provinces.-** Each of Provinces shall be paid in each financial year as a share in the net proceeds of surcharge on natural gas an amount which bears to the total net proceeds the same proportion as the well-head production of natural gas in the province in that year bears to the total well-head production of natural gas.

7. **Grants-in-Aid to the Provinces.—**There shall be charged upon the Federal Consolidated Fund each year, as grants-in-aid of the revenues of the provinces, (for the period) specified against each, the amount so specified:-:-

Province	Period	Amount
The Punjab	For 3 years	Rs.1000 million
Sind	For 5 years	Rs. 700 million
The North-West Frontier Province	For 3 years	Rs. 200 million
Balochistan	For 3 years	Rs. 100 million

8. **Repeal.-** Articles 2,3,4 and 5 of the Distribution of Revenues and Grants-in-Aid Order, 1975 (P.O. No.2 of 1975), and the Distribution of Revenues Order, 1983 (P.O. No.8 of 1983), are hereby repealed.

Ghulam Ishaq Khan
President

Ihsan-ul-Haq Chaudhry
Secretary

Annex-III

Government of Pakistan
Ministry of Law, Justice, & Parliamentary Affairs
(Law and Justice Division)

No.F.2(2)/91 **Islamabad, the 2nd June, 1991**

The following Order made by the President is hereby published for general information:-

PRESIDENT ORDER NO. 3 OF 1991

WHEREAS, in pursuance of Clause (2) of Article 161 of the Constitution, the Council of Common Interests has decided on 12th January, 1991, the rate of operating expenses to be deducted from the revenues accruing from the hydro-electric stations for computing the 'net profits';

AND WHEREAS, the National Finance Commission on a reference from Council of Common Interests has recommended that the net profits shall be paid by the undertaking established or administered by the Federal Government;

AND WHEREAS, the other recommendations of the National Finance Commission, have been notified by the President under the President's Order No.1 of 1991, dated the 22nd April, 1991, under Clauses (4) and (7) of Article 160 of the Constitution;

NOW, THEREFORE, the President is pleased to make the following Order under Clause (2) of Article 161 of the Constitution:-

1. **Short title and commencement.-** (1) This Order may be called the Distribution of Electricity Profits from Hydro-Electric Stations to Provinces, Order, 1991.

(2) It shall come into force on the first day of July, 1991.

2. **Distribution of net profits from hydro-electric stations.-** The net profits from the bulk generation of power at a hydro-electric station located in the Provinces shall be paid by the concerned undertaking established or administered by the Federal Government (i.e. Water and Power Development Authority) to the Provinces.

3. The Federal Government shall guarantee payment of net profits to the Provinces concerned by the above undertaking on a regular basis.

Ghulam Ishaq Khan
President

Ihsan-ul-Haq Chaudhry
Secretary

Annex-IV

Government of Pakistan
Ministry of Law, Justice, Human Rights & Parliamentary Affairs

No.F.2(2)/97-Pub **Islamabad, the 12th February, 1997**

The following Order made by the President is hereby published for general information:-

PRESIDENT ORDER NO. 1 OF 1997

WHEREAS, in pursuance of Clause (1) of Article 160 of the Constitution, the President, by the Finance Division's Notification No. SRO 733(I)/95, dated 23rd July, 1995, as modified by the said Division's Notification No. SRO 1361(I)/96, dated the 10th December, 1996, appointed a National Finance Commission to make recommendations, among other matters, as to the distribution between the Federation and the Provinces of the net proceeds of certain taxes;

AND WHEREAS the said Commission has submitted its recommendations with regard to the said distribution;

NOW, THEREFORE, in pursuance of Clause (4) of Article 160 of the Constitution, the President is pleased to make the following Order:-

1. **Short title and commencement.-** (1) This Order may be called the Distribution of Revenues and Grants-in-Aid Order, 1997.

(2) It shall come into force on the first day of July, 1997.

2. **Definition.-** In this Order, unless there is anything repugnant in the subject or context;

(a) **"net proceeds"** means, in relation to any tax, duty or levy, the proceeds thereof reduced by the cost of collection, as ascertained and certified by the Auditor-General of Pakistan; and

(b) **"taxes on income"** includes corporation tax but does not include taxes on income consisting of remuneration paid out of the Federal Consolidated Fund.

3. **Distribution of Revenues.-** The Provincial Governments shall be assigned in each financial year a share equal to thirty-seven point five percent of the net proceeds of the following taxes and duties levied and collected by the Federal Government in that year, namely:-

a. taxes on income;
b. wealth tax;
c. capital value tax;
d. taxes on sales and purchases;
e. export duties on cotton;
f. customs-duties;
g. federal excise duties excluding the excise duty on gas charged at well-head; and
h. any other tax which may be levied by the Federal Government.

4. **Allocation of shares to the Provincial Governments.-** The sum assigned to the Provincial Governments under Article 3 shall be distributed amongst the provinces on the basis of their respective population in the percentage specified against each:-

The Punjab	57.88%
Sindh	23.28%
The North-West Frontier Province	13.54%
Balochistan	5.30%
Total:	100.00%

5. **Payment of net proceeds of royalty on crude oil.-** Each of the provinces shall be paid in each financial year as a share in the net proceeds of the total royalties on crude oil an amount which bears to the total net proceeds the same proportion as the production of crude oil in the Province in that year bears to the total production of crude oil.

6. **Payment of net proceeds of development surcharge on natural gas to the Provinces.-** Each of Provinces shall be paid in each financial year as a share in the net proceeds of surcharge on natural gas an amount which bears to the total net proceeds the same proportion as the well-head production of natural gas in the province in that year bears to the total well-head production of natural gas.

7. **Grants-in-Aid to the Provinces.—**There shall be charged upon the Federal Consolidated Fund each year, as grants-in-aid of the revenues of

the provinces, (for the period) specified against each, the amount so specified:-:-

Province	Period	Amount
The North-West Frontier Province	For 5 years	Rs. 3310 million
Balochistan	For 5 years	Rs. 4080 million

Note.- the grants-in-aid will be increased annually by 11% subject to subsequent adjustment in line with the actual rate of inflation for each year.

8. **Matching Grants to Provinces.-** Whereas the Provincial Governments achieve a minimum growth of 14.2% in Provincial receipts with fiscal efforts which include increases in tax rates, withdrawal of exemptions, imposition of new taxes and revision in rates of user charges, as ascertained and certified by the Auditor General of Pakistan, the Federal Government will pay to each province in the subsequent year, the matching grant subject to the maximum limits specified below:-

The Punjab	500 million
Sindh	500 million
The North-West Frontier Province	100 million
Balochistan	100 million

9. Repeal.- Articles 2,3,4,5,6, and 7 of the Distribution of Revenues and Grants-in-Aid Order, 1991 (P.O. No.1 of 1991), are hereby repealed.

Farooq Ahmad Khan Leghari
President

Justice (R) (Akhtar Hassan)
Secretary

Annex-V

Government of Pakistan
Ministry of Law, Justice, & Human Rights
(Law, Justice, & Human Rights Division)

No.F.2(2)/2006-Pub **Islamabad, the 19th January, 2006**

The following Order promulgated by the President is hereby published for general information.

ORDER NO. 1 OF 2006

AN

ORDER

Further to amend the Distribution of Revenues and Grants-in-Aid Order, 1997

WHEREAS, in pursuance of clause (1) of Article 160 of the Constitution, the President, by the Finance Division's Notification No. SRO 529 (1)/2000, dated 22nd July, 2000, as modified by SRO No.895(1)/2000, dated 18th December, 2000, Notification No.F.2(2)NFC/2000-508 dated 7th November, 2001, Notification No. F.2(2)NFC/2000-200 dated 6th April, 2002, SRO No.1043(I)/2003, dated 13th November, 2003, read with SRO No.739(I)/2005, dated 21st July, 2005 and SRO NO.950(I)/2005, dated 12th September, 2005, appointed a National Finance Commission to make recommendations, among other matters, as to the distribution between the Federation and the Provinces of the net proceeds of certain taxes;

AND WHEREAS the Commission could not submit its recommendations with regard to the said distribution and the matter being of urgent and national importance can not be further delayed;

AND WHEREAS it is expedient further to amend the Distribution of Revenues and Grants-in-Aid Order, 1997 (P.O.No.1 of 1997) for the purposes hereinafter appearing;

NOW, THEREFORE, in pursuance of clauses (6) read with clause (7) of Article 160 of the Constitution of Islamic Republic of Pakistan, the President is pleased to make the following Order:-

1. **Short title and commencement.-** (1) This Order may be called the Distribution of Revenues and Grants-in-Aid (Amendment) Order, 2006.

(2) It shall come into force on the first day of July, 2006.

2. **Substitution of Articles 3, 4 and 7, P.O. No.1 of 1997.** – In the Distribution of Revenues and Grants-in-Aid Order, 1997 (P.O. No. 1 of 1997) for Articles 3, 4 and 7 the following shall be substituted, namely:-

"3. **Distribution of Revenues.-** (1) The Provincial Governments shall be assigned in each financial year a share equal to the percentage of the net proceeds of the following taxes and duties levied and collected by the Federal Government in that year as specified in clause (2) :-

a. taxes on income;
b. wealth tax;
c. capital value tax;
d. taxes on sales and purchases;
e. sales tax on services (CE mode);
f. export duties on cotton;
g. customs-duties;
h. federal excise duties excluding the excise duty on gas charged at well-head; and
i. any other tax which may be levied by the Federal Government.

(2) The percentage share of the provinces from the net proceeds of taxes and duties in each year shall be as under:--

Financial year	Percentage share
2006-07	41.50%
2007-08	42.50%
2008-09	43.75%
2009-10	45.00%
2010-11and onward	46.25%

4. **Allocation of shares to the Provincial Governments.-** (1) Out of the sum assigned to the Provincial Governments under Article 3 an amount equal to the net proceeds of 1/6th of Sales Tax shall be distributed amongst the provinces at the following ratio and the Provincial Governments shall further transfer the whole of such amounts to the District Governments and Cantonment Boards without retaining any part thereof:-

The Punjab	50.00%
Sindh	34.85%
The North-West Frontier Province	9.93%
Balochistan	5.22%
Total:	100.00%

(2) The balance shall be distributed amongst the provinces on the basis of their respective population in the percentage specified against each:-

The Punjab	57.36%
Sindh	23.71%
The North-West Frontier Province	13.82%
Balochistan	5.11%
Total:	100.00%

7. **Grants-in-Aid to the Provinces.—**There shall be charged upon the Federal Consolidated Fund each year a sum of Rupees twenty seven billion seven hundred and fifty million, as grants-in-aid of the revenues of the provinces to be distributed amongst the provinces as per ratio specified against each province, namely:-

Province	Amount
The Punjab	11.00%
Sindh	21.00%
The North-West Frontier Province	35.00%
Balochistan	33.00%
Total:	100.00%

Note.-- The grants-in-aid will be increased annually in line with the growth of net proceeds of divisible taxes for each year.

Explanation:- With the arrangements contained in Articles 3 and 7 above, the overall provincial share in the net Divisible Pool Taxes would not be less than 45% in the first financial year and 50% in the last financial year.”.

General
Pervez Musharraf
President

Justice (R) Mansoor Ahmad
Secretary

Annex-VI

Provincial Share in the Divisible Pool Taxes Net
A comparison of Actual with the projection of 1996 Award

		1997-98	1998-99	1999-2000	2000-01	2001-02
Punjab	Actual	57.9	61.6	70.1	78.8	80.8
	1996 Projection	80.8	95.5	113.0	133.9	158.8
	Difference	-22.9	-33.9	-42.9	-55.1	-78.0
Sindh	Actual	23.3	24.8	28.2	31.7	32.6
	1996 Projection	32.5	38.4	45.4	53.8	63.9
	Difference	-9.2	-13.6	-17.2	-22.1	-31.3
NWFP	Actual	13.6	14.4	16.4	18.4	18.9
	1996 Projection	18.9	22.3	26.4	31.3	37.1
	Difference	-5.3	-7.9	-10.0	-12.9	-18.2
Balochistan	Actual	5.3	5.6	6.4	7.2	7.4
	1996 Projection	7.4	8.7	10.3	12.2	14.5
	Difference	-2.1	-3.1	-3.9	-5.0	-7.1
Provinces (Combined)	Actual	100.1	106.5	121.1	136.2	139.7
	1996 Projection	139.6	164.9	195.1	231.2	274.3
	Difference	-39.5	-58.4	-74.0	-95.0	-134.6

Annex-VII

TO BE PUBLISHED IN THE GAZETTE OF PAKISTAN
(EXTRAORDINARY)

GOVERNMENT OF PAKISTAN
FINANCE DIVISION
(NFC SECRETARIAT)
****

Islamabad, the 21st July, 2005

NOTIFICATION

S.R.O.739(I)/2005.- In pursuance of Article 160 (1) of the Constitution of the Islamic Republic of Pakistan, the President is pleased to constitute National Finance Commission consisting of the following namely:-

(1)	Minister for Finance Government of Pakistan	Chairman
(2)	Minister for Finance Government of the Punjab	Member
(3)	Minister for Finance Government of Sindh	Member
(4)	Minister for Finance Government of NWFP	Member
(5)	Minister for Finance Government of Balochistan	Member
(6)	Advisor to the Prime Minister on Finance	Member
(7 to 10)	One Member from each Province to be notified in consultation with the Governors of the Provinces.	
(11)	Finance Secretary Government of Pakistan	Official Expert

TERMS OF REFERENCE

2. The terms of reference for the Commission are as under:-

(a) the distribution between the Federation and the Provinces of the net proceeds of the following taxes:

(i) taxes on income, including corporation tax, but not including taxes on income consisting of remuneration paid out of the Federal Consolidated Fund;

(ii) taxes on the sales and purchases of goods, imported, exported, produced, manufactured or consumed;

(iii) GST on services

(iv) Export duties on cotton

(v) Consider the inclusion of other Federal Taxes including Customs Duties and Federal Excises, but not including taxes on income paid out of Federal Consolidated Fund.

(b) the making of grants-in-aid by the Federal Government to the Provincial Governments;

(c) the exercise by the Federal Government and the Provincial Governments of the borrowing powers conferred by the Constitution;

(d) examine the question of rationalization of payment of royalties on crude oil and of surcharge on natural gas collected by the Federal Government to the Provincial Governments;

(e) to consider review of the distribution of share of taxes between the Federal Government and Provincial Governments; and

(f) to develop and enforce a mechanism for setting parameters to achieve fiscal discipline at the Federal and Provincial levels and for ensuring consistency in maintaining an appropriate fiscal balance at the consolidated level.

(g) any other matter relating to finance referred to the Commission by the President.

3. The National Finance Commission notified vide Gazette of Pakistan Extraordinary SRO 529(1)/2000, dated 22ND July, 2000 and SRO 895(1)/2000, dated 18th December, 2000 and SRO 1043(I)/2003, dated 13h November, 2003, shall stand dissolved with immediate effect.

Sd/-

No.F.2(1)-NFC/2005

(Mian Muhammad Younis)
Joint Secretary (PF)
Secretary
National Finance Commission

Annex-VIII

TO BE PUBLISHED IN THE GAZETTE OF PAKISTAN (EXTRAORDINARY)

GOVERNMENT OF PAKISTAN
FINANCE DIVISION
(NFC SECRETARIAT)
****

Islamabad, the July 24, 2009

NOTIFICATION

S.R.O. 693(I)/2009.- In partial modification of Notifications SRO.739(1)2005 dated 21st July, 2005, SRO.950(1)2005, dated 12th September, 2005 and SRO.900(1)2008, dated 26th August, 2008 and in pursuance of Article 160(1) of the Constitution of the Islamic Republic of Pakistan, the President is pleased to reconstitute National Finance Commission consisting of the following members, namely:-

(1)	Minister for Finance Government of Pakistan		Chairman
(2)	Minister for Finance Government of the Punjab		Member
(3)	Minister for Finance Government of Sindh		Member
(4)	Minister for Finance Government of NWFP		Member
(5)	Minister for Finance Government of Balochistan		Member
(6)	Mr. Abdul Ghafoor Mirza	(Punjab)	Member
(7)	Mr. Kaiser Bengali	(Sindh)	Member
(8)	Senator Haji Muhammad Adeel	(NWFP)	Member
(9)	Dr. Gulfaraz Ahmed	(Balochistan)	Member

2. The Commission shall, in addition to matters referred in para 2 of SRO.739(1)2005, dated 21st July, 2005, make recommendations on the following matters, namely:-

(i) Sales Tax on Services (CE Mode);

(ii) examine the question of rationalization of payment of royalties on crude oil and of surcharge on natural gas collected by the Federal Government; and

(iii) to develop and enforce a mechanism for setting of parameters to fiscal discipline at the Federal and Provincial levels.

3. The Finance Division shall, as per the Rules of Business, 1973, provide the Secretariat support to the Commission.

Sd/-

(Mian Muhammad Younis)

No.F.2(1)-NFC/2005-

Senior Joint Secretary/
Secretary
National Finance Commission

Annex-IX [Table-1]

Fiscal Position of the Federal and Provincial Governments

[Prov. share 56% 1st year and 57.5% remaining years with no Grants & Collection Charges at 1% & tax 15% of GDP]

Rs. Billion

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Provincial Share in the Div Pool	45%	56%	57.5%	57.5%	57.5%	57.5%	
Federal Receipts	1,997.23	2,337.58	2,724.91	3,138.49	3,651.81	4,223.98	16.2%
FBR Revenues	1,380.00	1,710.50	2,048.26	2,442.60	2,890.90	3,387.10	19.7%
Surcharges	133.53	132.08	146.30	146.30	146.30	146.30	1.8%
Non-tax receipts	483.70	495.00	530.35	549.59	614.60	690.58	7.4%
Divisible Pool Net	1,266.27	1,616.42	1,925.36	2,296.04	2,717.45	3,183.87	
Div pool net as % of Gross		94%	94.0%	94.0%	94.0%	94.0%	
1% to NWFP for war on terror		16.16	19.25	22.96	27.17	31.84	
Divisible Pool Net (after subtracting 1% for War on Terror)	1,266.27	1,600.26	1,906.11	2,273.08	2,690.27	3,152.03	20.0%
Yearly growth in Div pool net		26.4%	19.1%	19.3%	18.4%	17.2%	
Provincial Share in the Div Pool	569.82	899.35	1,096.01	1,307.02	1,546.91	1,812.42	26.0%
Grants in Aid (Special Grant)	52.90	-	-	-	-	-	
Total	622.72	899.35	1,096.01	1,307.02	1,546.91	1,812.42	23.8%
Straight Transfers	85.40	129.17	147.08	167.48	190.35	215.59	20.3%
out of which GST on Services	-	51.32	61.45	73.28	86.73	101.61	
Total Federal Transfers incl. war on terror transfers	708.12	1,044.67	1,262.35	1,497.46	1,764.43	2,059.85	23.8%
As % of GDP	4.8%	6.3%	6.9%	7.4%	7.8%	8.1%	
Federal Receipts Net	1,289.11	1,292.91	1,462.56	1,641.03	1,887.38	2,164.13	10.9%
As % of GDP	8.7%	7.8%	8.0%	8.1%	8.3%	8.5%	-0.5%
Total Expenditure	2,094.27	2,204.50	2,364.02	2,579.52	2,876.71	3,215.21	9.0%
As % of GDP	14.1%	13.4%	12.9%	12.7%	12.6%	12.6%	-2.3%
Current Expenditure	1,736.27	1,800.00	1,886.70	2,027.90	2,191.54	2,430.00	7.0%
Development Expenditure	358.00	404.50	477.32	551.62	685.17	785.21	17.0%
PSDP As % of GDP	2.4%	2.5%	2.6%	2.7%	3.0%	3.1%	
Budget Deficit/Surplus	(805.16)	(911.59)	(901.45)	(938.49)	(989.33)	(1,051.08)	
As % of GDP (Federal)	5.4%	5.5%	4.9%	4.6%	4.3%	4.1%	
OFD (MEF)	4.9%	4.2%	3.3%	3.1%	2.9%	2.8%	
Adjustment required		1.3%	1.6%	1.5%	1.4%	1.3%	
Provincial Total Resources	914.33	1,341.41	1,614.63	1,905.63	2,238.84	2,600.56	23.3%
Federal Transfers	708.12	1,044.67	1,262.35	1,497.46	1,764.43	2,059.85	23.8%
Provincial Own Receipts	163.20	206.42	256.00	305.30	364.23	447.47	22.4%
Tax Receipts	74.20	107.32	146.30	183.20	227.63	293.97	31.7%
Non-tax receipts	89.00	99.10	109.70	122.10	136.60	153.50	11.5%
Other Transfers	43.01	90.32	96.28	102.87	110.18	93.23	16.7%
NHP & Fed Dev Assistance	43.01	47.31	52.04	57.25	62.97	69.27	10.0%
Arrears of NHP+GDS+Grant for OZT	-	43.01	44.23	45.63	47.21	23.96	
Provincial Expenditures	981.04	1,341.41	1,614.63	1,905.63	2,238.84	2,600.56	21.5%
As % of GDP	6.6%	8.1%	8.8%	9.4%	9.8%	10.2%	
Current Expenditure	661.35	753.94	859.49	979.82	1,116.99	1,273.37	14.0%
As % of GDP	4.5%	4.6%	4.7%	4.8%	4.9%	5.0%	
Development Expenditure	319.70	587.47	755.14	925.81	1,121.85	1,327.19	32.9%
As % of GDP	2.2%	3.6%	4.1%	4.5%	4.9%	5.2%	
Provincial surplus/(deficits)	(66.71)	-	-	-	-	-	
As % of GDP	0.4%	0.00%	0.00%	0.00%	0.00%	0.00%	
GDP (market price)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

Federal Current expenditures in addition to normal expenditures following are also added

NHP @ Rs.25 billion for four years

GDS @ Rs.12 billion for five years

Grants in lieu of OZT to Sindh @ Rs.0.66% of the provincial share in the divisible pool

Rs.6 billion Grants to Balochistan for repayment of OFD

Rs.6 billion Punjab on account of NHP

Rs.52.9 billion grants-in-aid in benchmark year also includes Rs.6 billion grants to Balochistan for repayment of OFD

Annex-IX [Table-3]

Fiscal Position of the Provinces [Punjab]

Rs. Billion

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Provincial Total Resources	444.77	636.58	776.29	923.55	1,092.60	1,290.51	23.7%
Divisible Pool transfers	326.19	464.52	567.08	676.25	800.37	937.75	23.5%
Straight Transfers incl. GST	5.63	31.68	37.44	44.13	51.71	60.09	60.6%
Straight Transfers	5.63	5.13	5.65	6.21	6.83	7.52	5.9%
★ *GST on Services*	-	26.55	31.79	37.91	44.87	52.57	
Other Grants/Transfers	15.02	16.52	18.17	19.99	21.99	24.19	10.0%
FDA/NHP	15.02	16.52	18.17	19.99	21.99	24.19	10.0%
Arrears of NHP/GDS/Grants for OZT	-	-	-	-	-	-	
War on Terror (1% of Div Pool)	-	-	-	-	-	-	
Provincial Own Receipts	97.92	123.85	153.60	183.18	218.54	268.48	22.4%
Tax Receipts	44.52	64.39	87.78	109.92	136.58	176.38	31.7%
Non-tax receipts	53.40	59.46	65.82	73.26	81.96	92.10	11.5%
Provincial Expenditures	489.87	636.58	776.29	923.55	1,092.60	1,290.51	21.4%
As % of GDP	3.3%	3.9%	4.2%	4.5%	4.8%	5.0%	
Current Expenditure	314.87	358.96	409.21	466.50	531.81	606.26	14.0%
As % of GDP	2.1%	2.2%	2.2%	2.3%	2.3%	2.4%	
Development Expenditure	175.00	277.62	367.08	457.05	560.80	684.25	31.4%
As % of GDP	1.2%	1.7%	2.0%	2.2%	2.5%	2.7%	
GDP (market price)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

Annex-IX [Table-4]

Fiscal Position of the Provinces [Sindh]

Rs. Billion

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Provincial Total Resources	264.36	359.16	432.44	509.98	598.82	702.68	21.6%
Divisible Pool transfers	153.72	220.49	269.07	320.87	379.77	444.95	23.7%
Straight Transfers incl. GST	52.98	60.89	68.21	76.43	85.57	95.65	12.5%
Straight Transfers	52.98	48.30	53.12	58.44	64.28	70.71	5.9%
★ *GST on Services*	-	12.60	15.09	17.99	21.29	24.95	
Other Grants/Transfers	7.07	13.79	15.79	18.04	20.57	23.35	27.0%
FDA/NHP	7.07	7.78	8.56	9.42	10.36	11.39	10.0%
Arrears of NHP/GDS/Grants for OZT	-	6.01	7.23	8.63	10.21	11.96	
War on Terror (1% of Div Pool)	-	-	-	-	-	-	
Provincial Own Receipts	50.59	63.99	79.36	94.64	112.91	138.72	22.4%
Tax Receipts	23.00	33.27	45.35	56.79	70.57	91.13	31.7%
Non-tax receipts	27.59	30.72	34.01	37.85	42.35	47.59	11.5%
Provincial Expenditures	288.40	359.16	432.44	509.98	598.82	702.68	19.5%
As % of GDP	1.9%	2.2%	2.4%	2.5%	2.6%	2.7%	0.0%
Current Expenditure	213.40	243.27	277.33	316.16	360.42	410.88	14.0%
As % of GDP	1.4%	1.5%	1.5%	1.6%	1.6%	1.6%	0.0%
Development Expenditure	75.00	115.89	155.10	193.83	238.40	291.80	31.2%
As % of GDP	0.5%	0.7%	0.8%	1.0%	1.0%	1.1%	0.0%
GDP (market price)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

★ The indicative share of GST on Services are strictly provisional at this stage. These shares would be revised in the light of decision taken after discussion with the provinces. The final share so determined would take effect from 1st July, 2011.

Annex-IX [Table-5]

Fiscal Position of the Provinces [NWFP]

Rs. Billion

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Provincial Total Resources	125.25	216.36	255.20	297.09	344.77	373.62	24.4%
Divisible Pool transfers	92.09	131.33	160.24	191.09	226.16	264.98	23.5%
Straight Transfers incl. GST	9.19	15.88	18.20	20.85	23.84	27.13	24.2%
Straight Transfers	*9.19*	*8.38*	*9.22*	*10.14*	*11.16*	*12.27*	5.9%
★ *GST on Services*	-	*7.50*	*8.98*	*10.71*	*12.68*	*14.86*	
Other Grants/Transfers	14.17	56.76	61.40	66.83	72.93	54.67	31.0%
FDA/NHP	14.17	15.59	17.15	18.87	20.75	22.83	10.0%
Arrears of NHP/GDS/Grants for OZT	-	25.00	25.00	25.00	25.00	-	
War on Terror (1% of Div Pool)	-	16.16	19.25	22.96	27.17	31.84	-
Provincial Own Receipts	9.79	12.38	15.36	18.32	21.85	26.85	22.4%
Tax Receipts	4.45	6.44	8.78	10.99	13.66	17.64	31.7%
Non-tax receipts	5.34	5.95	6.58	7.33	8.20	9.21	11.5%
Provincial Expenditures	131.16	216.36	255.20	297.09	344.77	373.62	23.3%
As % of GDP	0.9%	1.3%	1.4%	1.5%	1.5%	1.5%	
Current Expenditure	80.00	91.20	103.97	118.52	135.12	154.03	14.0%
As % of GDP	0.5%	0.6%	0.6%	0.6%	0.6%	0.6%	
Development Expenditure	51.16	125.16	151.24	178.56	209.66	219.58	33.8%
As % of GDP	0.3%	0.8%	0.8%	0.9%	0.9%	0.9%	
GDP (market price)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

Annex-IX [Table-6]

Fiscal Position of the Provinces [Baluchistan]

Rs. Billion

	2009-10 (Benchmark)	2010-11 (1st year)	2011-12 (2nd year)	2012-13 (3rd year)	2013-14 (4th year)	2014-15 (5th year)	ACGR
Provincial Total Resources	79.95	129.31	150.69	175.01	202.64	233.75	23.9%
Divisible Pool transfers	50.72	83.00	99.63	118.81	140.61	164.75	26.6%
Straight Transfers incl. GST	17.59	20.70	23.23	26.07	29.23	32.72	0.0%
Straight Transfers	*17.59*	*16.04*	*17.64*	*19.41*	*21.35*	*23.48*	*0.0%*
★ *GST on Services*	-	4.66	5.59	6.66	7.88	9.24	*0.0%*
Other Grants/Transfers	6.74	19.42	20.16	20.97	21.87	22.86	0.0%
FDA/NHP	6.74	7.42	8.16	8.97	9.87	10.86	-
Arrears of NHP/GDS/Grants for OZT	-	12.00	12.00	12.00	12.00	12.00	-
War on Terror (1% of Div Pool)	-	-	-	-	-	-	-
Provincial Own Receipts	4.90	6.19	7.68	9.16	10.93	13.42	22.4%
Tax Receipts	2.23	3.22	4.39	5.50	6.83	8.82	31.7%
Non-tax receipts	2.67	2.97	3.29	3.66	4.10	4.61	11.5%
Provincial Expenditures	71.61	129.31	150.69	175.01	202.64	233.75	26.7%
As % of GDP	0.5%	0.8%	0.8%	0.9%	0.9%	0.9%	0.0%
Current Expenditure	53.08	60.51	68.98	78.64	89.64	102.20	14.0%
As % of GDP	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.0%
Development Expenditure	18.54	68.80	81.72	96.37	113.00	131.56	48.0%
As % of GDP	0.1%	0.4%	0.4%	0.5%	0.5%	0.5%	0.0%
GDP (market price)	14,837	16,510	18,288	20,355	22,763	25,563	11.5%

★The indicative share of GST on Services are strictly provisional at this stage . These shares would be revised in the light of decision taken after discussion with the provinces. The final share so determined would take effect from 1st July, 2011.