

White Paper on

E-Commerce Payment Infrastructure in Pakistan

***Contributed by***

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**Disclaimer**

The information and views set out in this White Paper are those of the members of Working Group on E-Commerce Payments Infrastructure and do not necessarily reflect the official opinion of their respective organizations.

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# Introduction

The objective of this paper is to analyze current E-Commerce landscape, issues, challenges and provide recommendations for the development and establishment of payment infrastructure in Pakistan. This paper is a contribution to the work being undertaken by Ministry of Commerce (MoC) for devising a National E-Commerce Policy for providing the citizens of Pakistan with an enabling infrastructure which connect buyers and sellers to make digital/cashless transactions. It is also vital to formalize and record the transactions that in most cases may go unreported due to unlawful import of goods or off the books trading. It is expected that a National Policy on E-Commerce shall support and work towards building E-Commerce market and ecosystem, which will also encourage local trade and foreign investment in the country. This paper is prepared in the light of the feedback shared by the MoC Working Group[[1]](#footnote-1) members of Payments Infrastructure.

# E-Commerce in Pakistan

Pakistan’s E-Commerce industry is currently estimated at $100 million with 41 million broadband subscriptions. More than 38 million people use internet on mobile phones and yet E-Commerce has not reached to a level where mobile money is used for E-Commerce transactions. With a population of nearly 190 million, growing base of 38 Million Next Generation Mobile Services users and financial inclusion solutions in terms of branchless banking, Pakistan offers one of the largest untapped markets in the world for E-Commerce.

Statistics below show the E-Commerce penetration in Pakistan and across region and world:

1. E-Commerce Industry is estimated at $100 million with more than 41 million internet users i.e. 16.5% with per capita spend of $0.55.
2. Consumer Electronics/Mobile Phones are the most bought items in Pakistan at 9%.
3. Most activity on E-Commerce is seen in Lahore region at 21% followed by Karachi (20%) and then Islamabad/Rawalpindi (15%)[[2]](#footnote-2).
4. Regional E-Commerce Industry: India – $12.6 billion with 15.1% penetration and per capita spend of $11.2 whereas Bangladesh is estimated to be $45 million with 6.5% internet penetration and per capita spend of $0.29. A table indicating the E-Commerce transactions globally and regionally is attached at Annexure A.

# Key Findings of Working Group

Key findings of Working Group on existing Payment Infrastructure for E-Commerce are summarized below:

1. Adequate Payments infrastructure for E-Commerce exists in Pakistan which includes:
   1. E-Commerce Gateway facility being provided by following five (5) banks and two (2) microfinance banks (MFBs) at present:
      1. MCB Bank Limited
      2. Habib Bank Limited
      3. United Bank Limited
      4. Bank Alfalah Limited
      5. Tameer Microfinance Bank (EasyPay)
      6. Mobilink Microfinance Bank (JazzCash)
      7. Bank Al-Habib Limited (Keenu)
   2. At present, 496 E-Commerce merchants have been on-boarded by banks as of March 31, 2017. These merchants processed approximately 0.81 million transactions worth PKR 6.4 billion during the first three quarters of FY 2016-17. It is expected that the volume and value of E-Commerce transaction to reach at 1.1 million and PKR 8.25 billion respectively for the FY 2016-17. However, this number is significantly less compared to a large retail market of approximately 2,000,000 merchants that exists nationwide[[3]](#footnote-3).
   3. For digital payments, 37.1 million plastic cards, that include international schemes cards such as VISA/MasterCard/JCB /CUP, are issued by banks. Among these 37.1 million cards, only 1.2 million are credit cards whereas 17.5 million are debit cards. The remaining cards comprise of social disbursement, prepaid and ATM only cards.
   4. Domestic Payment Scheme PayPak exists in Pakistan and could be instrumental for promoting local E-Commerce.
   5. Internet Merchant Accounts can be opened in local currency or in USD (F.E. Circular No. 06 of 2000).
   6. People have options to use Branchless Banking/Mobile Banking for E-Commerce Payments.
2. According to certain estimates there are over 200 online web stores selling merchandise of different brands in Pakistan.[[4]](#footnote-4)
   1. Merchandise value of all E-Commerce stores is estimated to have crossed $100Mn a year.
   2. Average order size on every E-Commerce store is reported to be PKR 5,000 (USD 50),
3. SBP has issued the Rules for Payment System Operators and Payment Service Providers (PSOs/PSPs) under which non-bank private entities are encouraged to set up payment processing infrastructure for various purposes including ecommerce. Under these Rules SBP has given in-principle approval to few entities who are under process of setting up E-Commerce payment gateways.
4. New Fintechs offering services like Cab rides, food delivery etc also provide option of online payment for providing services through mobile apps and thus present exciting business opportunities for Pakistani payment companies. However, some of these new ventures though accept payments through cards, use acquiring services from offshore banks which results in unnecessary outflow of foreign exchange from the country.
5. Companies such as Payoneer, Skrills etc. are providing online money transfer and E-Commerce payment services for importers through verified Paypal accounts. However, people using these services have to settle for lower foreign exchange rates.

# Issues and Challenges

* 1. **Infrastructure**

E-Commerce in Pakistan faces the following issues and challenges in the existing environment:

1. **Low Banking Penetration:** Pakistan is home to 5% of the world’s unbanked population which translates not only into low financial inclusion but also undermines efforts to increase E-Commerce through formal channels.
2. **Tax on Banking Transactions:** In recent years, the imposition of tax on banking transaction has lead to reduction in its usage due to which both merchants and consumers refer to physical cash for transactions. Merchants are reluctant to accept electronic payments because of fear of FBR and other tax authorities. Further the tax for non filers’ transactions has proved to be a deterrent for not only merchant acquisition but also for customers to prefer to transact in cash.
3. **Low penetration of Debit & Credit Card:** In the developed world, credit cards have traditionally been the key drivers of commerce and recently E-Commerce. Unfortunately, credit and debit card penetration in Pakistan is very low with only 1.2 million credit cards and 17 million debit cards issued. However, even the usage of these cards for E-Commerce purposes is still much lower as most of these are not activated for online sessions (E-Commerce) due to security reasons and risks associated with these transactions and customers have to call the helpline of their respective banks to activate online sessions.
4. **Merchant Acquiring is still very low:** Card acquiring business in Pakistan is still a loss making
5. **E-Commerce Merchant On-boarding:** Due to the high risk of merchant fraud, International payment schemes require acquiring bank to adopt strict merchant onboarding criteria. The strict KYC and documentary requirements from payment schemes and banks deters merchants, especially smaller ones, to become part of the existing payment infrastructure. Even Branchless Banking (BB) players have to sign up merchants as BB level 2 merchant accounts. Currently merchants are signed up as Branchless Banking Level 2 Merchants which requires stringent KYC and significant time for E-Commerce players to come onboard. In Pakistan, the large number of merchants or prospective E-Commerce businesses are smaller players who may not be able to fulfill strict merchant on-boarding criteria.
6. **Online Collection of Taxes:** At present, there is no mechanism in place to collect online tax/custom duty from importers and exporters. SBP and Pakistan Customs are working together on WeBoc System which shall be able to provide platform for online collection of duties/taxes to facilitate both importers and exporters
7. **International Payments: Int**ernational payment wallets/schemes such as PayPal are not available in Pakistan and Pakistani customers have to use other channels by paying extra to settletheir transactions. In case of exports, the situation is even worse as exporters, especially of digital content, resort to availing these foreign services and repatriate funds to Pakistan through illegal channels.

**4.2. Others**

1. **Cash on delivery:** Approximately 80% of all E-Commerce transactions are cash on delivery, where customers pay for products using cash at the time of delivery.
2. **Consumer Protection & Privacy concerns**: Consumer protection is generally weak and the customer typically has no recourse available in case of disputes over the goods/services delivered.
3. **Foreign Exchange Issues.** Currently, it is observed that local offline merchants buy products from online stores such as EBay, Aliexpress etc. and then sell these merchandize and other smuggled products in local markets which results in flight of capital and create pressure on foreign exchange reserves. SBP has a clear stance to discourage imports and increase exports as well as inward remittances to stabilize foreign exchange reserves.

# Cross-Border Transactions

Globally, cross-border E-Commerce is booming, especially in the Asia and Pacific region. The Asia and Pacific region contributes to approximately one-third of the global total and has outperformed North America in which China alone is responsible for 60% of APAC E-Commerce transactions. E-Commerce giants like Amazon and Alibaba use state of the art technology and quick processes to work in the regions they invest in for which an enabling environment is required.[[5]](#footnote-5)

Private sectors discussion on challenges and recommendations on cross border transactions can be found in **Appendix D** of this document.

##### **Challenges for Cross Border Transactions**

The issues currently being faced in imports and exports through proper channel are as follows:

#### Imports

The long process of importing products hampers the rise and interest of cross-border trade in the region.

1. Shipments are detained for a maximum of 30 days from the date of arrival. If proper documentation (NOC) is not received during this time, the shipment will either be destroyed or confiscated, and subjected to fines and penalties.
2. Duty and taxes can be applied to all shipments at approximately 53% of the assessed value of the shipment. This means it is not the value written on the shipment that is charged to the customer but what the custom’s officer perceives it to be.
3. Proper documentation must be provided by the consignee for all shipments weighing over 5 kg (11 lb) and valued at US $100 or more for clearance. Packages assessed at 200 USD or less are only accepted as gifts and not marked for duties / taxes. Otherwise the person will be responsible for clearing all the dues and taxes.

#### Exports

1. Pakistani companies are also not able to compete for the global B2C cross-border E-Commerce market which will balloon in size to $1 trillion in 2020 because of the export duties.
2. Presently the value of items shipped through couriers is often not captured in export data because they are categorized as samples or gifts. These are labeled as samples because under the normal export channel exporters have to file shipping bills and are subject to checks by custom officials, which are cumbersome, especially for small exporters with low-value shipments.
3. Pakistani companies are also unable to offer refunds for items received by foreign customers that are not as expected due to payment legislation that does not authorize such transfers.
4. Although the provision of Internet Merchant Account is available but the quantum of transactions through these accounts is not encouraging. A comprehensive mechanism/modus operandi to channelize the export proceeds by using these accounts in consultation with all stakeholders may be devised.

##### **SBP Initiatives for Cross Border E-Commerce**

1. SBP in collaboration with Customs is working on integrating WeBoc system with 1Links bill payments system which will enable the traders/taxpayers for making online payment of duty/taxes by the customers/importers to SBP BSC (Customs A/c) through their respective commercial banks.
2. The present payments infrastructure in the country is adequate to carry out E-Commerce transactions~~.~~ At present, the provision of Internet Merchant Accounts is available and few banks are also accommodating the incoming proceeds from exports by local merchants through International Card Schemes such as VISA, MasterCard etc (see Annexure B).
3. SBP has initiated work on a National Payment Gateway (NPG) which will incorporate a core switch for general interoperability along with a Micro Payment Gateway (MPG) for m-wallet interoperability. The focus of NPG is more on inter-switch settlement of domestic PKR transaction with enhanced integrated monitoring and risk management.

# Recommendations of Working Group for Infrastructure

Following action items/recommendations are being proposed by the Working Group on Payments Infrastructure with responsible stakeholder for promotion of E-Commerce and Payments Infrastructure in Pakistan.

##### **Stakeholder: SBP & Banking Industry**

1. SBP should work with the industry to enhance the role of private sector payment gateways (PSOs/PSPs) and encourage new entrants to enter the market of ecommerce. This will result in enhanced competition and further introduce innovative products and services in the country for both consumers and merchants.
2. Standardized Merchant On-boarding criteria/mechanism may be established for payment gateways and be made flexible.
3. Local card scheme like PayPak may be enabled to start Card Not Present (CNP) acquiring in addition to Card Present (CP) environment transactions. Further, M-wallet holders may be given the option of low cost domestic Virtual Debit Cards (VDCs) for online purchases and other services.
4. Steps need to be taken for enhancing the security on E-Transactions, consumer trust and consumer protection in the sphere of E-Commerce. SBP has already issued Regulations for Payment Card Security which require banks to implement authentication measures like Two/Three Factor authentication etc (3D Secure) for Payment Card transactions to authenticate the identity of cardholders and to address the non-repudiation risk. SBP and Banks may further take steps for enhancing consumer awareness about their rights during and after the completion of transaction including dispute resolution.
5. Transaction Monitoring System (TMS) may be established at banks’ end for debit cards (*the mechanism for credit cards already exists*) to track payments on E-Commerce transactions (*local as well as international*) through merchants using customer IDs and Mobile accounts that are linked to their NICs.
6. Banks shall allow debit and credit cards usage or provide their customers with the option to pre-select at time of issuance for E-Commerce transactions with due enforcement of security measures and Transaction Monitoring System (TMS).
7. The WG is of the view that the existing payment gateways have high charges (such as 3% on card transactions, 2% on OTC and 1% on mobile wallets) without offering complete service profile especially fraud risk management. Therefore, these high charges, both in Card Present and Card Not Present (CNP) environments, need to be rationalized in a manner that should incentivize both the merchants and consumers for E-Commerce.
8. As discussed above, the scope of proposed NPG is limited to domestic payments only. However, depending on the use cases and recommendations by stakeholders, SBP may explore the option of including the functionality of incoming remittances from E-Commerce transactions in the proposed National Payment Gateway via automation of Pakistan Remittance Initiative (PRI). The working group feels that the expectation for this arrangement needs to be clearly laid down. It is therefore recommended that MoC and MOITT shall work with the exporters, including providers of digital content and other relevant stakeholders to determine exact requirement to make existing process more efficient and communicate the same to SBP for consideration to incorporate this functionality in NPG.

##### **Stakeholder: FBR**

* Federal and Provincial governments may establish e-payment portals for government receipts and payments to increase use cases for mobile accounts and drive E-Commerce adoption. For example provincial and federal tax collection and payment, Fees for obtaining National IDs, Traffic tickets, driving license fee etc. These portals shall be integrated with the centralized payment gateways.
* Electronic payments may be incentivized by reducing tax on e-payments.

##### **Stakeholders: MoC, MOITT & E-Commerce Gateways/Marketplaces**

1. To make existing process for realization of export proceeds more efficient, MoC and MOITT shall work with the exporters, including providers of digital content and other relevant stakeholders to determine exact requirement and communicate the same to SBP for consideration to incorporate this functionality in NPG.
2. E-Commerce players (especially Marketplaces and Auction places) should set up customer support and complaint/dispute resolution mechanism rather than relying on Payment Gateways Customer Resolution Mechanism (CRM).
3. E-Commerce Gateways shall make investments in centralized data analytics to reduce fraud, which is an effective mechanism for payment gateways to secure their transactions like linking validated cards to customers up to their expiry which shall reduce processing costs and delays.
4. A list of credible international financial market places and processers may be considered to integrate with local market places.
5. Credit scoring of banked individuals such as Equifax in Canada ([www.equifax.ca](http://www.equifax.ca)) may be introduced whereby using data collection and integration both the customer and banks can each review the profile of that customer to determine risk level of any particular banking transaction (or otherwise).

# Others Recommendations

1. Over the counter (OTC) limits to be annulled for reversal of transactions especially to assist with refunding of prepayments made by customers. Enabling refund processing in the same direction as how customers make their payments is essential in building trust for customers to transact online and use OTC as a valid prepayment method.
2. Relevant provisions may be introduced to enable individual accounts as a merchant account. Provisions such as “Doing Business As” (DBA) may be allowed to lower end customers who already maintain account with the bank and the same account may be used for business transactions.
3. All merchants originated in Pakistan should open “Merchant Account” in any local bank and/or foreign bank operating in Pakistan for the purpose of collecting sales proceeds of goods and services sold in Pakistan as permissible under SBP rules. It shall be mandatory for all retail merchants, Market places, Auction places etc. to sign up any Principle Acquirer and/or Payment Facilitator in Pakistan, duly authorized by SBP to ensure that all E-Commerce transactions originated domestically must be settled in PKR. SBP will work with local payment gateways to make their offering more attractive from an onboarding and service perspective to incentivize local ecommerce merchants to integrate with local gateways as their preferred prepayment processing solutions. These measures will ensure that there is a cheap and scalable solution available for the ecommerce merchant.

# Key Activities

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **S.No.** | **Issues** | **Recommendations** | **Actions** | **Implementing Agency** | **Time Frame** |
| 1 | Standardized merchant on-boarding criteria is not available especially for small merchants | * Standardized and flexible merchant on-boarding criteria/mechanism shall be established for flexible-Commerce retailers | SBP shall establish and implement the standardized merchant on-boarding criteria for small merchants and E-Commerce players | SBP, Banking Industry, Card Schemes | 30th June, 2018 |
| 2 | Non availability of Domestic Payment Card Scheme, PayPak, for E-Commerce transactions | * Domestic card scheme (PayPak) shall be enabled to start Card Not Present (CNP) acceptance in addition to Card Present (CP) transactions | SBP shall work with 1LINK and the banks to start work in this area | SBP, 1LINK, Banking Industry | 30th June, 2018 |
| 3 | Absence of online collection of duties and taxes | * SBP and FBR (Customs) shall work together to enable online collection of duties/taxes to facilitate both importers and exporters | SBP, FBR and banking industry shall work on integrating WeBoc system with online payment system of the country | SBP, FBR and banking industry | 30th Dec, 2018 |
| 4 | Non Availability of Risk management of online payments through Debit cards | * + - * Proactive Transaction Monitoring System (TMS) shall be established at banks’ end for debit cards (the mechanism for credit cards already exists) to track payments on E-Commerce transactions (local as well as international) | SBP shall enforce applicability of maximum limit on debit cards to be used for CNP transactions based on customer’s consent. | SBP, Banking Industry | 30th June, 2018 |
| 5 | Lack of Consumer Awareness and product offerings by financial institutions | * E-Commerce players (especially Marketplaces) shall set up customer support and complaint/dispute resolution mechanism rather than relying on Payment Gateways Customer Resolution Mechanism (CRM). * A list of credible international financial market places (Amazon etc) shall be considered to integrate with local market places |  | SBP, MoC, MOITT & E-Commerce Gateways/Marketplaces  MoC, MOITT & E-Commerce Gateways/Marketplaces | 30th June, 2018  30th June, 2018 |
| 6 | High cost of interchange | * Interchange shall be rationalized for E-Commerce which is currently higher due to higher risk exposure at card issuing bank’s end. | SBP shall rationalize the card interchange fee | SBP, Banking Industry | 30th June, 2018 |
| 7 | Tax on banking transactions | * Electronic payments shall be incentivized in the forthcoming budget by reducing tax on e-payments |  | FBR | 30th June, 2018 |
| 8 | Lack of Data Analytics tools | * Credit scoring of banked individuals such as Equifax in Canada ([www.equifax.ca](http://www.equifax.ca)) shall be introduced * Payment Gateways shall be encouraged to make investments in centralized data analytics to reduce fraud which is an effective mechanism for payment gateways to secure their transactions |  | SBP, MoC, MOITT & E-Commerce Gateways/Marketplaces  SBP, MoC, MOITT & E-Commerce Gateways/Marketplaces | 30th June, 2018  30th June, 2018 |
| 9 | Absence of Cross Border Transactions mechanism for exporters of goods and services (domestic handicrafts, Digital content etc) for realization of export proceeds | * MoC and MOITT shall work with the exporters, including providers of digital content and other such entities to determine requirements to make existing process for realization of export proceeds more efficient and communicate the same to SBP for consideration to incorporate this functionality in NPG. |  | MoC, MOITT, SBP | 30th June, 2018 |

# Appendix A: E-Commerce Transactions

**Table 1:** Overview of E-Commerce Transactions

|  |  |
| --- | --- |
| **E-Commerce Industry** | **Value** |
| World | $1.5 trillion |
| China | $466 billion |
| North America | $450 billion |
| EU | $487 billion |
| India | $12 billion |
| Bangladesh | $45 million |
| Pakistan | $100 million |

*\* Source – Cracking E-Commerce 2.0, Plant N & Karandaaz Pakistan*

**Table 2:** PS Infrastructure in Pakistan

|  |  |
| --- | --- |
| **Indicators** | **2016** |
| No of Branches | 14,219 |
| No of Online Branches | 13,926 |
| No of ATMs | 12,352 |
| POS Machines | 52,062 |
| Cellular Subscriber (millions) | 137 |
| 3/4G users (millions) | 38.3 |
| No. Active Branchless Banking Agents | 210,536 |
| Plastic Cards (millions) | 36 |
| E-Commerce merchants | 398 |
| Number of E-Commerce Transactions (Oct-Dec 16) ( in 000) | 263 |
| Value of E-Commerce Transactions (Oct-Dec 16) (in millions) | 2,041 |

**Table 3:** Percentage -wise usage of payment options

|  |  |
| --- | --- |
| **E-Commerce Industry** | **Value** |
| Cash on Delivery | 80% |
| IBFT | 10% |
| Internet Payment Gateway | 3% |
| Wallets / Deposit in bank branches / Cheque payments / Card swipe on delivery | 7% |

**Table 4:** Current Pricing Model for onboarding various E-Commerce

Merchants in Pakistan

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Joining Fee** | **Annual Fee** | **Per Transaction MDR\*** |
| **UBL** | 40,000 | 40,000 | 3.5% |
| **HBL** | 35,000 | 35,000 | 2.6- 3.2% |
| **MCB** | 45,000 | 48,000 | 3.5% |

*\*Note: Prices are approximate figures, and vary merchant to merchant based on transaction volume.*

**Table 5:** Online/Webstores

|  |  |
| --- | --- |
| 1.      Daraz.pk | 21.  BuyBest.pk |
| 2.      TCSConnect.com | 22.  OnlineStorePk.com |
| 3.      Symbios.pk | 23.  bnbAccessories.com |
| 4.      Kaymu.pk | 24.  SaqisCity.com |
| 5.      ShopHive.com | 25.  FashionSouk.com |
| 6.      FoodPanda.pk | 26.  MyWatches.pk |
| 7.      Tohfay.com | 27.  VividShop.pk |
| 8.      SentimentsExpress.com | 28.  ApnaDress.com |
| 9.      HealthSupplementsPk.com | 29.  Savers.pk |
| 10.  2ShopDaily.pk | 30.  ShopNShop.pk |
| 11.  eBazaarPk.com | 31.  ShopTime.pk |
| 12.  iShopping.pk | 32.  BuyOn.pk |
| 13.  360bin.com | 33.  ComputerPoint.com.pk |
| 14.  Scentiment.pk | 34.  JabronDeals.com |
| 15.  StoreNStore.pk | 35.  GoShopping.pk |
| 16.  HamarieShop.pk | 36.  Hub.com.pk |
| 17.  vMart.pk | 37.  AaramShop.pk |
| 18.  Mega.pk | 38.  MyTabletPC.pk |
| 19.  OnlyShopping.pk | 39.  BuyPakistan.com |
| 20.  Liberty.pk | 40.  FineStore.pk |
|  | 41.  RoyalZone.pk  42. techcity.pk |
|  |  |

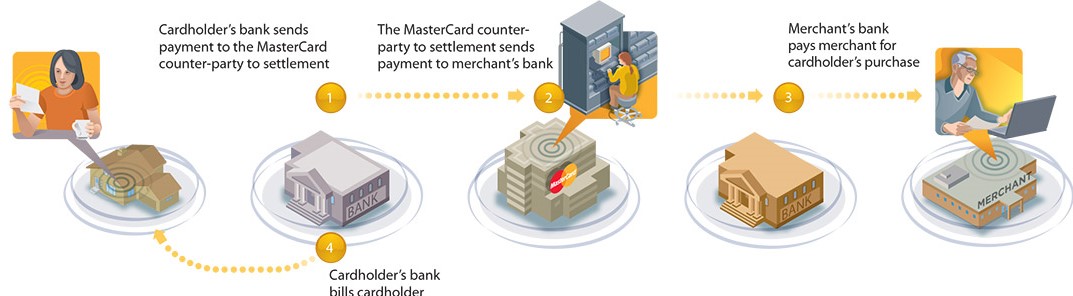
# Appendix B: Transaction Flow for Export Proceeds

**Transaction Authorization**

* 1. A local merchant’s website is enabled with Bank A’s Internet Payment Gateway
  2. Customer, sitting abroad, purchases products from this website and pays through VISA/MasterCard issued by any international bank.
  3. Merchant website displays product pricing in PKR, whereas customer billing currency can be any foreign currency.
  4. Bank A identifies this as an Off-Us transaction and sends to respective payment scheme (VISA or MasterCard) with PKR amount.
  5. Payment Scheme converts PKR into USD with their international rates and then converts USD into issuer billing currency and sends all three amounts PKR, USD and Issuer billing currency amount for authorization.
  6. Card issuing bank authorize payment and sends the response back to payment scheme.
  7. Payment scheme sends it back to Bank A
  8. Bank A informs the merchant website/system
  9. Merchant website inturn informs customer of successful transaction

1. **Transaction Settlement**
   1. Merchant submits batch settlement file to Bank A
   2. Bank A host generates Outgoing files for payment schemes (VISA/MasterCard)
   3. Merchant payment file is also generated simultaneously
   4. Bank A settle with Merchant in PKR (transaction currency)
   5. Bank A submits outgoing files to payment schemes for settlement of funds with transaction currency amount (PKR)
   6. Payment Scheme converts PKR into USD with their international rates and then converts USD into issuer billing currency and sends all three amounts PKR, USD and Issuer billing currency amount for transaction posting into customer account.
   7. Payment Scheme does settlement with Bank A in USD by crediting Bank A Nostro Account maintained in New York.
   8. FX gain & loss is determined against Buying vs Treasury Rate on daily basis.

# Appendix C: Transaction Flow

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# Appendix D: Private Sector Recommendations

**Imports**

Owing to existing legislation and process challenges, Pakistani Online marketplaces are not able to list foreign sellers on their platforms. A Pakistani consumer currently uses foreign websites like EBay, Alibaba or Amazon to import items for personal use while using local credit cards to make payments. Alternatively, non-custom duty paid items also enter the country via a grey channel to serve the high local demand and can be purchased from the offline market. This pushes local Pakistani online marketplaces to be in a disadvantageous position compared to foreign platforms.

To enable local online marketplaces to legalize these transactions, the challenges listed below will need to be addressed

1. Online marketplaces are unable to provide visibility to customers with respect to customs duties assessed upon entry at time of purchase. This is primarily due to differences in item valuation upon time of assessment (invoice value vs previously assessed value in FBR records) or inconsistent application of HS codes for customs duties. Poor visibility and inconsistent application of customs duties encourages mistrust in local Online marketplace platforms.
2. Online Marketplaces are not authorized to apply for PTA approvals on behalf of importers for items that require PTA approvals. A PTA approval can only be obtained by the buyer which in this case would appear after the item is displayed online for purchase by sellers and will result in a processing delay.

Factors given above results in legislation causing local businesses to be in a disadvantageous position compared to businesses that do not exist within Pakistan’s borders. Ebay’s CEO recently [claimed](https://propakistani.pk/2017/01/17/ebay-ceo-pakistan-among-fastest-growing-e-commerce-markets-world/) that Pakistan was an ‘exploding’ market for their business despite the fact that Ebay has no presence locally in Pakistan.

The country’s economy is already facing huge trade deficit where imports are approximately double than exports resulting into pressure on country’s foreign exchange reserves. Therefore, import regime may require special care to avoid associated risks such as trade deficit (for example placing value caps or authorizing only certain online marketplaces to have imports).

**Exports**

1. Presently the value of low value items shipped through couriers for personal use is often not captured in export data because they are categorized as samples or gifts. This is a simpler and faster way to get through customs as compared to the a normal export channel exporters have to file shipping documents that include airway bill, invoice, packing list, request letter to assistance collector of custom AFU export, letter authorizing clearing agent to clear export, copy of passport, copy of airline ticket and personal presence of passenger at time of clearance and these documents are subject to checks by custom officials, making the process cumbersome, costly and time consuming, especially for small exporters with low-value shipments.
2. There is no regulation in customs laws that permit an online marketplace to ship items on behalf of the seller. If an online marketplace facilitates the transaction on behalf of the seller and ships it out on their behalf, they will automatically be deemed the seller of this item with the associated risks and rewards transferred to the online marketplace
3. Exports from Pakistan are, interalia, governed under the foreign exchange rules and regulations framed by the Federal Government and State Bank of Pakistan. In order to boost exports through E-Commerce, the following rules and regulations may need to be modified
4. Federal Government’s Notification No. I (6)-ECS/ 48 and No. I(7)- ECS/48 both dated July 01, 1948;
5. SBP Notification No. F.E.1/2016-SB dated July 26, 2016;
6. Chapter 12 (Exports) of the Foreign Exchange Manual-2016;
7. Chapter 13 (Imports) of the Foreign Exchange Manual-2016.

However, the above rules have been identified in the absence of any formal model/mechanism of E-Commerce. SBP will need to propose amendments in their foreign exchange rules and regulations specifically for Ecommerce to support local platforms to list foreign sellers.

**Other recommendations to be considered**

**Imports**

1. Introduce de minimis value of USD 250 in order to promote cross-border transactions to make the final cost visible to the consumer at time of purchase and also cut down on delivery time by reducing the time taken in tax and duty assessments. Customs duties are by their very nature trade barriers that hurt job creation, slow down economic growth and drive up costs for companies and consumers. A recent [study](http://www.oecd-ilibrary.org/docserver/download/5k4bw6kg6ws2-en.pdf?expires=1495556418&id=id&accname=guest&checksum=0E913E583243B61E1B75205915D2D09E) by the Organization for Economic Cooperation and Development (OECD) suggests that improved tradefacilitation in developing nations would mean a 15% reduction in the cost of trade.
2. One of the most prevalent and burdensome global trade barriers is the formality of declaring, classifying, valuing and risk assessing low value consignments at the border. Majority of such cases are assessed as low risk. Additionally, in many cases, the cost to authorities for processing low value shipments is greater than the revenue collected by the customs administrations. This is why de minimis regimes were introduced in the revised Kyoto convention and also the WTO trade facilitation agreement to establish a reasonable threshold, below which duties and taxes would not be collected and for which less information will be required for clearance with greater focus being on risk assessment and admissibility.

A number of recent economic [studies](http://www.global-express.org/assets/files/Members%20Library/GEA%20Position%20Paper%20on%20de%20minimis%20FINAL.pdf) have demonstrated the positive impact of de minimis regimes:

* APEC economies concluded that establishing a de minimis threshold of USD 200 could lead to almost USD 12bn in net economic benefits[[6]](#footnote-6)
* A study in the US concluded that raising the de minimis from USD 200 to USD 800 would lead to net gains of USD 17 mn per annum[[7]](#footnote-7)

Importantly, OECD is developing new ways for GST collection on imports. Two collection models are under consideration, the vendor collection model and the intermediary collection model. These models should be studied by Pakistan Customs Authorities and implemented

From the above points it becomes clear why de minimis is essential for the growth of E-Commerce and important for the overall economy of the country. It will provide:

* Easier pricing tools for sellers and portals which in turn create a better customer experience
* Lower costs involved for customs whilst assessing
* Faster clearance times enabling faster deliveries
* Lower costs for end consumers

Already Pakistan has a great inflow of goods from across the globe that come in via the grey channel (zero tax collection) and also lots of products coming in via green channel that are either under invoiced. The products that come in via green channel without any ambiguities also exist, however, the importers add on high margins which in turn make the products costly for customers.

Online Marketplaces on the other hand, typically have standard low commissions and can ensure more favorable prices for the end consumer. Furthermore, the government also gets full visibility in imports and spending patterns of local consumers and can introduce appropriate taxation. Moreover, this will activate the local economy to be more competitive with pricing and may also dishearten grey channel operators since ecommerce portals will be able to provide competitive rates via the green channel.

As far as risk of narcotics and banned substances is concerned, E-Commerce companies will have contracts with shipping providers and sellers that strictly condemn and prohibit movement of banned substances. Shipping companies will also be responsible for screening at ports of exit.

India and Malaysia are two economies that have de minimis values within the range recommended in this document. Worldwide de minimis rates can be found [here](http://www.global-express.org/assets/files/Customs%20Committee/de-minimis/GEA-overview-on-de-minimis_April-2016.pdf)

1. Necessary amendments in the foreign exchange related to allow for payment aggregation and settlement of funds collected from individual consumers across Pakistan to foreign sellers supplying the purchased product or service after the item or service is delivered. Chapter 16 Para 4 of the FE manual may be amended to allow online marketplaces to aggregate and issue payments on the behalf of individual importers as long as the legal requirements are met and complete visibility can be provided on the individuals that are the real importers behind the payments
2. Allow online marketplaces to seek PTA Type approvals for Electronic Sim based devices on behalf of individual buyers. This will eliminate the monopoly of local distributors on mobile devices and create an open market with the necessary control system and visibility. Accelerating smartphone penetration is critical to E-Commerce growth and overall education of the population.

Pakistan already has an active customer base that orders/sources Electronic Sim based devices from multiple channels:

* Portals such as AliExpress & Amazon whereby shipments come in via post or express courier
* Paid Gray Channel Carriers
* Friends and Family

Whilst the last 2 channels escape under the radar, orders via portals go through the customs green channel. To aid the clearance the, PTA has devised an [SOP](http://www.pta.gov.pk/media/ta/sop_ta_noc_210915.pdf) of obtaining a personal NOC which is very simple to execute, but can only be executed by the actual individual importer.

Established online marketplaces can facilitate customers (importers) by fulfilling this procedure on the customers’ behalf to make the overall experience better and smoother. Online marketplaces that receive permission for this process can also share real time information about inflows with the PTA and customs to further aid the regulatory authorities.

1. In order for cross border to work successfully there needs to be a simple framework for customs on both export as well as imports. As an example, the Chinese government made a number of amendments to regulations pertaining to Cross Border E-Commerce (CBEC) in Apr 2016 via the Circular on Tax Policies for Retail Import in Cross-Border E-Commerce. These amendments included a new tax policy as well as a comprehensive list of products (with relevant HS codes) to be imported via CBEC.
2. Adjustments were also made to import tax rates of imported articles, which were divided into three categories with tax rates of 15%, 30% and 60%:

* Category I: Books and newspapers, publications, audio and video materials for educational use; computers, video cameras, digital cameras and other IT products; food and beverages; gold and silver; furniture; toys, gaming products, and festive and other recreational products;
* Category II: Sporting goods (excluding golf balls and clubs), fishing tools; textiles and their manufactured goods; TV cameras and other electrical appliances; bicycles; other goods not included in Category I and III;
* Category III: Alcohol and tobacco; valuable accessories, jewelry and gemstones; golf balls and clubs; luxury watches; cosmetics.

This allows for easier classification and assessment of products belonging to a certain category. Such implementation in Pakistan will also be helpful for ecommerce players as well as customs authorities.

Our recommendation is to follow the structure implemented by China in 2016 by allowing import of the products listed [here](http://www.eusmecentre.org.cn/sites/default/files/files/LIST_OF_PRODUCTS_AUTHORIZED_TO_BE_TRADED_VIA_CBEC_EU_SME_CENTRE.pdf). More details on CBEC mechanics can be found [here](https://www.austrade.gov.au/Australian/Export/Export-markets/Countries/China/Doing-business/e-commerce-in-china).

1. A pilot project can be launched to integrate cross border transactions of leading E-Commerce marketplaces directly with Customs’ WeBOC system to boost cross border transactions through E-Commerce. This can be funded through ICT R&D and developed in collaboration with Customs, SBP and leading Ecommerce players as well as logistics companies. For reference, Bank of China released a working paper on processes undertaken to strengthen cross border ecommerce across government institutions. This paper can be found [here](http://pic.bankofchina.com/bocappd/rareport/201604/P020160413370147122111.pdf)

**Exports**

1. Simplifying the process of exports by introducing a minimum value of USD 250 per package within which the item would be considered exports for personal use and would require similar documentation requirements as those items sent overseas as gifts i.e airway bill and invoice. The removal of excessive documentation and requirements for assessments on products below this threshold will encourage exports and speed up deliveries to customers abroad that seek Pakistani products especially textiles and handicrafts
2. Adjust legislation to allow online marketplaces to ship items on behalf of the seller that is listed on its platform. An online marketplace owing to its expertise in digital ecommerce, may be able to generate multiple export orders for a particular seller listed on its platform as opposed to the seller attempting to find these customers on his own. It is essential that the risks and rewards of the product or service are transferred from the seller to the customer upon delivery and not the online marketplace facilitating the transaction.
3. Ministry of Commerce may establish a website for training, education and hand-holding of SMEs that have potential to sell their products internationally. This initiative can be promoted in collaboration with the private sector in order to activate the existing seller base on E-Commerce platforms in the country and integrate the education program for exports through E-Commerce channels. A study published by the University of Southern California for empowering SMEs for cross border E-Commerce can be found [here](http://ncapec.org/docs/ABAC%20Documents/USC%20Marshall%20ABAC%202015%20MSMEs.pdf)
4. Simplify re-export of items imported by consumers that did not arrive in the condition that they were advertised to facilitate customer returns for imports with the following conditions applicable to the re-export
   * Full amount of payment, if any is repatriated
   * Approval from concerned authority / customs is obtained

Conditions such as request letter to deputy / assistant collector of custom AFU exports, export invoice of the items shown in foreign currency in export invoice format, warranty letter, indemnity bond on Rs. 100 bond paper with signature of 2 witnesses and 1 director with NIC copy as well as copy of NTN may be removed to simplify the process.

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