Example: 8.16

A company has rented out its bungalow. Compute its taxable property income from the following information:

1. Monthly rent of the house – Rs. 30,000
2. Security deposit received at the beginning of the year – Rs. 200,000
3. Repair and maintenance charges – Rs. 96,000
4. Property related taxes – Rs. 7,200
5. Rent collection charges – Rs. 26,400
6. Legal charges (including Rs. 5,000 due but not paid) – Rs. 15,000

Solution:

Rent Chargeable to Tax (RCT)

- Rent of the property (Rs. 30,000 × 12) = Rs. 360,000
- 1/10th of deposit received (200,000 ÷ 10) **[N-1]** = Rs. 20,000
- **Total RCT** = Rs. 380,000

Less: Allowable Deductions:

- Repair allowance – 1/5th of RCT (i.e., 380,000 ÷ 5) = Rs. 76,000
- Property related taxes = Rs. 7,200
- Rent Collection Charges – Lesser of:
    - Actual rent collection charges = Rs. 26,400
    - OR
    - 4% of RCT = (380,000 × 4%) = Rs. 15,200
    - **Allowed amount** = Rs. 15,200
- Legal Charges **[N-2]** = Rs. 15,000

Total deductions: Rs. (113,400)

Taxable income from property = Rs. 266,600

Notes:

N-1: Assumed that the deposit is not adjustable against rent.

N-2: The deductions are allowed according to the method of accounting adopted by the taxpayer. It is assumed that ‘accrual basis’ has been adopted.

CHAPTER-9

INCOME FROM BUSINESS

BUSINESS [2(10)]

‘Business’ is an activity undertaken with a motive to earn profits. According to the Income Tax Ordinance, the ‘business’ includes any:

1. Trade;
2. Commerce;
3. Manufacture;
4. Profession;
5. Vocation; or
6. Adventure or concern in the nature of trade, commerce, manufacture, profession or vocation.

However, it does not include employment.

The law does not define the terms used in the definition. Under such a condition, the meanings which are generally attached to or understood from the use of such terms shall be adopted.

INCOMES CHARGEABLE UNDER ‘BUSINESS’ [18(1) & (2)]

The following incomes are chargeable to tax under the head "Income from Business":

1. Profits and gains of any business carried on during the tax year.
2. Profits and gains of any business treated to have been carried on during the tax year.
3. Income from the sale of goods or provision of services to its members by any trade, professional or similar association. Examples of such associations may be Lahore Chamber of Commerce and Industries (LCCI), All Pakistan Textile Mills Association (APTMA), ICAP, and ICMAP.
4. Fair market value of any ‘benefit’ or perquisite arising from the past, present, or prospective business relationship. It may or may not be convertible into money.

‘Benefit’ includes any benefit derived by way of waiver of profit on debt or the other debt itself under the State Bank of Pakistan, Banking Policy Department’s Circular No. 29 of 2002 or in any other scheme issued by the SBP. *(This circular of SBP provides guidelines on write-off of irrecoverable loans and advances).*

5. Income from the hire or lease of tangible movable property.
6. Management fee derived by a management company (e.g., modaraba management company).
7. Profit on debt, in the case of a person whose business is to lend money and earn profit on debt (e.g., banks, financial institutions). **‘Profit on debt’** received by any other person may be taxable as **‘Income from Other Sources’.**

Incomes subject to tax under sections 5A, 5AA, 6, 7, and 7A shall not be taxable as ‘Income from Business’.

INCOMES OF CO-OPERATIVE SOCIETIES [Explanation to 18(2)(b)]

The following income of a co-operative society shall be taxable as income from business:

1. Sale of goods;
2. Sale of immovable property; or
3. Provision of services to its members.

AMOUNT RECEIVED AGAINST LEASE [18(3)]

Where a lessor has leased out any asset to any other person (lessee), then any amount paid or payable by the lessee in connection with the lease shall be taxable as **'Income from Business'.**

The 'lessor' may be any of the following persons:

1. A scheduled bank,
2. An investment bank,
3. A development finance institution,
4. A modaraba, or
5. A leasing company.

Note: Whether or not the asset is owned by the lessor, the amount received or receivable in connection with the leased asset shall be taxable as **'Income from Business'.**

INCOME FROM MUTUAL FUNDS [18(4)]

Any amount received by a banking company or a non-banking finance company shall be chargeable to tax as **'Income from Business'** and not as **'Income from Other Sources'** if the following conditions are satisfied:

1. The amount has been distributed by a mutual fund or a Private Equity and Venture Capital Fund; and
2. It is distributed by such funds out of their income on account of **'profit on debt'.**

SPECULATION BUSINESS [19]

Where a taxpayer carries on **'speculation business'**, it shall be treated as a distinct and separate head of income. Incomes, gains, or losses from such business shall be kept separate from other business incomes. Incomes from business are dealt with separately under the following heads:

1. Income from non-speculation business; and
2. Income from speculation business.

'Speculation business' means a business in which a contract for the purchase and sale of any commodity (including stocks and shares) is periodically or ultimately settled otherwise than by actual delivery or transfer of the commodity. [19(2)]

However, the following businesses are **not** included in **'speculation business'**:

1. A business in which a contract is entered into by a person to guard against loss through future price fluctuations in respect of other contracts entered into by him for actual delivery of goods.
2. A business in which a contract in respect of stocks and shares is made by a dealer or investor to guard against loss in his holdings through price fluctuations.
3. A business in which a contract is entered into by a member of a forward market or a stock exchange.

Exchange in any transaction of **'jobbing'** or **'arbitrage'** to guard against loss which may arise in the ordinary course of his business.

- **'Jobbing'** is the function of buying and selling financial securities on the stock market by a dealer who acts as a principal in making a market in these securities.
- **'Arbitrage'** is the buying and selling of products, financial securities, or foreign currencies between two or more markets in order to take profitable advantage of any differences in the price quoted in those markets.

ADMISSIBLE DEDUCTIONS [20]

While computing the income under the head **'Income from Business'**, certain expenses and allowances are allowed as deductions. These deductions may broadly be categorized into the following four groups:

A) Expenses incurred for the purposes of business;
B) Animals used for business;
C) Depreciation and amortization on assets, intangibles, etc.; and
D) Amalgamation expenses incurred by an amalgamated company.

A) Expenses Incurred for the Purposes of Business [20(1)]

Any expenditure incurred by a person during the tax year **'wholly and exclusively'** for the purpose of business generating taxable income is allowed as a deduction while computing such income. Where expenditure is not incurred wholly for the business, then only such proportion of it shall be allowed as a deduction, which fairly relates to the business.

Some of the examples of expenditures that may be allowed as a deduction are given below:

1. Cost of the goods purchased and utilized for the business.
2. Cost of goods manufactured and sold.
3. Rent for premises used for the business.
4. Any tax, cess, charge, or rate (other than income tax) paid in connection with the business or any of its assets.
5. Repair charges of any asset used for the business.
6. Insurance premium paid for insuring the assets.
7. Any **sum** paid to an employee as **bonus** or **commission** for services rendered. The amount should be reasonable by considering:
    - i) The pay of the employee;
    - ii) The conditions of the employee's service;
    - iii) The profits of the business during the year; and
    - iv) The general practice in similar businesses.

The above payments should be allowed as a deduction only if these are not payable to the employee as profit or dividend. If these are payable as a distribution of profits, they should not be allowed as a deduction.

8. Actual amount of bad debts.
9. Any expenditure incurred by an employer on any educational institution or hospital for the benefits of the employees or their dependents.
10. Any expenditure incurred on a recognized institute meant for training of industrial workers.
11. Expenditures incurred on a Pakistani for his training under an approved scheme.
12. Annual subscription paid to a registered trade organization (such as, LCCI, APTMA, PSMA, etc.).
13. Expenditure on a foreign visit undertaken with a trade delegation sponsored by the Federal Government.
14. Any expenditure incurred wholly and exclusively for the business.

Note: While computing income, the deductions and allowances shall be allowed according to the method of accounting regularly used by the taxpayer. Where incomes are recognized on an accrual basis, the expenses shall also be allowed accordingly.

B) Animals Used for Business [20(1A)]

Where a person is using animals for the purposes of business (otherwise than as stock-in-trade) and the animals have died or become permanently useless for business, then the person shall be allowed a deduction against business income. The deduction shall be equal to an amount calculated as below:

- **Actual cost of the animal**: XXXX
- **Less: Amount realized in respect of carcass or animal**: (XXXX)
- **Amount to be allowed as deduction**: XXXX

C) Depreciation and Amortization on Assets [20(2)]

A person is allowed a deduction on account of depreciation or amortization in respect of the following assets used for the business:

1. Depreciable assets;
2. Intangibles with a useful life of more than one year; and
3. Pre-commencement expenditures.

The depreciation and amortization are allowed according to the provisions laid down in sections 22 through 25 and the Third Schedule to the Income Tax Ordinance, which is sufficiently discussed in the chapter **'Assets & Depreciation'.**

D) Amalgamation Expenses [20(3)]

An amalgamated company is allowed a deduction in respect of any expenditure connected with the amalgamation. These expenses may be:

1. Legal expenses;

2. Financial advisory services; and
3. Other administrative costs relating to planning and implementation of amalgamation.

DEDUCTION ON ACCOUNT OF FINANCIAL COSTS [28(1)]

While determining **'Income from Business'** of a person, the following deductions shall be allowed on account of **'financial costs'**:

1. Any expenditure in the nature of **profit on debt**, if the debt has been utilized for the purposes of business.
2. Lease rentals for a business asset acquired on lease. The lease amount should have been paid to:
   - i) A scheduled bank;
   - ii) A financial institution;
   - iii) A modaraba;
   - iv) A leasing company; or
   - v) A Special Purpose Vehicle on behalf of the Originator.
   - **Lease rental comprises of two parts**, i.e., principal amount and lease charges. The total amount of lease rentals is allowed as a deduction. However, for deduction on account of a passenger transport vehicle not plying for hire, the amount of deduction shall not exceed Rs. 2,500,000. [Proviso to 28(1)(b)]
   - The **Finance Act, 2022** amended section 22(13)(a) of the ITO whereby words **'two and a half million'** were substituted by words **'seven and a half million'**. Corresponding amendment in section 28(1)(b) is overlooked.
   - **This mistake has created confusion** regarding the maximum amount to be allowed as a deduction on account of lease rentals paid in respect of a leased passenger transport vehicle not plying for hire.
   - **Considering the rules for interpretation of statutes,** we are of the opinion that the maximum amount available to the lessee for deduction on account of lease rentals paid should be taken as **Rs. 7,500,000** and **not Rs. 2,500,000**, which was before amendment by the Finance Act, 2022.
3. Profit on debt incurred on capital borrowed for business.
4. Any sum paid to a **Modaraba** or to a **Participation Term Certificate holder** for any funds borrowed for the business.
5. Any payment made by a **Scheduled bank** on a profit and loss sharing account or a deposit with such a bank. (This payment should have been made by way of distribution of profits in respect of such deposits).
6. Any payment made by the **House Building Finance Corporation (HBFC),** the **National Development Leasing Corporation Limited (NDLC),** or **Small and Medium Enterprises Bank (SME Bank)** to the **State Bank of Pakistan (SBP)** as a share in profit for investments made by SBP in HBFC, NDLC, or SME Bank respectively.

7. Any amount payable by a **Musharika** to its certificate holder or to a bank as a share in the profits of the Musharika.
8. The financial cost of **securitization** incurred by an **Originator** from a **Special Purpose** 9**Vehicle (SPV)** being the difference between the amount received by the Originator and the amount of receivables securitized to an SPV.
   - **Note:** Irrespective of the method of accounting adopted by the Originator, where as a result of securitization or issuance of **sukuks**, any assets are transferred by the Originator to SPV, it shall be treated as a **financing transaction**. [28(2)]

DEDUCTIONS NOT ADMISSIBLE [21]

The following expenses/payments are not allowed as deductions while calculating the income under the head "Income from Business":

1. Any tax, cess, or rate (including income tax) levied on the profits or gains of the business.
2. Any amount of tax deducted or collected at source from the person under various sections of the Income Tax Ordinance, 2001.
3. Any expenditure in respect of which a person is **required** to deduct or collect tax at source and the person has either not deducted it or has deducted but not paid such tax.

Notes:

- **i)** Recovery of any amount of tax u/s 161 or 162 shall be considered as tax paid; and
- **ii)** Maximum amount of expenditure to be disallowed in respect of purchases of raw materials and finished goods shall be **20%** of such purchases.

4. Any amount of **commission** paid or payable in respect of the supply of products listed in the **Third Schedule of the Sales Tax Act, 1990**, if:
   - **i)** The amount of commission paid or payable exceeds **0.2%** of gross amount of supplies of those products;
   - **ii)** The person to whom commission is paid or payable is **not appearing in the Active Taxpayers' List** under the Income Tax Ordinance, 2001.
5. In case of **pharmaceutical manufacturers**, any expenditure for **sale promotion, advertisement, and publicity** exceeding **10%** of the turnover.
6. Any payment made by an **association of persons** to its partners or members on account of:
   - **i)** Profit on debt;
   - **ii)** Brokerage;
   - **iii)** Commission;
   - **iv)** Salary; or
   - **v)** Any other remuneration.
7. Expenditure of a **non-resident business** on account of **"Head Office Expenditure"** which exceeds the allowable limits. The allowable deduction shall be calculated as below:

Total Head Office Expenditure × (Total Turnover in Pakistan / Total World Turnover)

8. Any expenditure incurred on **entertainment** except those which are incurred:
    - **i)** Abroad in connection with the business;
    - **ii)** In Pakistan on entertainment of **foreign or local customers and suppliers**;
    - **iii)** At the **meetings of members, agents, directors, and employees**;
    - **iv)** On **refreshment of employees**;
    - **v)** At the **opening of branches**; and
    - **vi)** On **entertainment of persons related directly to business**. [Rule-10]

Notes:

- **A) "Entertainment"** means the provision of **meals, refreshments, and reasonable leisure facilities** in accordance with the tradition of business and subject to overall norms and customs of business in Pakistan.
- **B)** The **FBR may prescribe conditions** for allowing an entertainment expense. The **violation of such conditions** shall also render the expense **inadmissible**.

9. Any expenditure under a single account head exceeding Rs. 250,000 in aggregate shall be inadmissible if the payment is not made through a banking channel. It does not apply to the following payments/expenditures:

i) Single transactions not exceeding Rs. 25,000; ii) Utility bills; iii) Freight charges; iv) Travel fare; v) Postage; vi) Payments made to discharge any statutory obligation (such as duties, taxes, octroi, export tax, fines, fee, cess, etc.); and vii) Any amount credited by direct transfer to an employee's bank account for reimbursement of expenses incurred on behalf of the taxpayer.

1. Transaction through banking channel should be verifiable from the bank statements of the respective payer and the payee.
2. Obligation to make payment through banking channel does not apply to purchase of agricultural produce directly from the grower, if the grower provides a certificate (in a prescribed format) to the withholding agent. [Clause (12) of Part-IV of Second Schedule]
3. 'Payment through Banking Channel' means:- a) Any payment made through crossed cheque, bank draft, pay order or any other crossed banking instrument showing transfer of amount from the business bank account; and b) Online transfer of payment from the business account of the payer to the business account of the payee and payment through credit card, if such transactions are verifiable from the bank statements of the respective payer and the payee.
4. 'Business Bank Account' means a bank account utilized by the taxpayer for business transactions declared to the CIR through original or modified registration form u/s 181. [210(A)]
5. Notwithstanding the existence of an independent clause (ia) in section 21, (which deals with companies separately and is yet to be implemented), the above-discussed provision

of payment through banking channel shall continue to apply on companies till that time when that clause is made effective by FBR.

6. Expenditure by company under a single account head exceeding Rs. 250,000 in aggregate if not paid by digital means from business bank account notified to CIR u/s 114A. It does not apply to the following expenditures:

i) Expenditure upto Rs. 25,000; ii) Utility bills; iii) Freight charges; iv) Travel fare; v) Postage; and

vi) **Taxes, duties, fees, fines or any other statutory obligation.**

1. **'Digital Means'** refers to digital payments and financial services, including but not limited to the following:

i) Online portals or platforms for digital payments/receipts; ii) Online Interbank Fund Transfer services; iii) Online bill or invoice presentment and payment services; iv) Over the Counter (OTC) digital payments services/facilities; v) Card payments using Point of Sale (POS) terminals, QR codes, mobile devices, ATMs, Kiosk, and/or any other digital payments-enabled devices; and vi) Any other digital/online payment modes. *(As per SBP's PSD & OD Circular Letter No. 05 of 2021, dated 15-10-2021)*

2. **Payment through 'digital means' in case of companies shall be effective from such date as the FBR may notify.**
3. Any payment on account of salary exceeding Rs. 32,000 per month must be made through a crossed cheque or transfer to the employee's bank account or through a digital mode; otherwise, it will not be considered valid.
4. Any contribution to a provident fund, pension fund, superannuation fund, or gratuity fund that is not recognized or approved under income tax law is not allowed.
5. Any contribution to any provident or other fund, if the person has not made effective arrangements for deduction of tax at source at the time of payments out of such fund, is not allowed.
6. Any amount in excess of 50% of the contribution made to an approved gratuity fund, an approved pension fund, or an approved superannuation fund is not deductible.
7. Any donation to an unapproved institution is not deductible.

Note: Donations to approved institutions are also not allowed as a deduction. Instead, a tax credit at the average rate of tax is allowed for such donations. *(For further details, refer to the chapter on 'Tax Credits').*

16. Any provision against the profits of the business, e.g., provision for bad debts, is not allowed.
17. Any appropriation of profit, such as dividends, transfers to reserves, or capitalization in any way, is not deductible.
18. Any expenditure in the nature of a fine or penalty for the violation of any law, rule, or regulation is not allowed.

19. Any expenditure of a capital nature (e.g., purchase of assets) is not allowed as a deduction.
20. Any personal expenditure incurred by the person is not deductible.
21. Any expenditure attributable to sales is not deductible if the person was required to integrate his business with the FBR through an approved fiscal electronic device and software and failed to do so. However, the disallowance of expenditure shall not exceed eighty percent (80%) of the allowable deduction.

Sales by Industrial Undertaking to Persons Not Registered under Sales Tax

From 01-10-2020, an industrial undertaking is not allowed to deduct any expenditure attributable to sales made to persons required to be registered but not registered under the Sales Tax Act, 1990. The inadmissible deduction shall be computed as per the following formula:

(A/B) × C

Where:

- **A** = Total amount of deductions claimed under this part;
- **B** = Turnover for the tax year; and
- **C** = Total amount of sales (excluding sales tax and federal excise duty) to persons required to be registered but not registered under the Sales Tax Act, 1990 where sales equal or exceed rupees one hundred million per person.

Notes:

1. Disallowance of expenditure on this account shall not exceed ten percent of total deductions claimed under this Part-IV of Chapter-III of Income Tax Ordinance, 2001 (sections 18 to 36).
2. FBR may notify the persons or classes of persons who are exempt from this provision. While exempting persons, the FBR may impose the notified conditions and limitations.

Example: 9.1

ABC & Company is a partnership firm. For the tax year ended on 30th June 200X, the firm declared a net profit of Rs. 400,000. The scrutiny of the profit and loss account revealed that the following deductions were also made while preparing the financial statements:

1. Income tax for previous year - Rs. 30,000
2. Tax at source deducted by the customers - Rs. 15,000
3. Salary paid to an employee without deduction of tax - Rs. 200,000
4. Salary paid to partner A - Rs. 60,000
5. Interest paid to partner B - Rs. 5,000
6. Salary per month paid in cash to an employee (Tax at source was deducted) - Rs. 40,000
7. Contribution to unrecognized provident fund - Rs. 30,000
8. Donations to unapproved institutions - Rs. 10,000
9. Donations to approved institutions - Rs. 20,000
10. Manager of the firm was paid the following amounts:

- **i)** Salary - Rs. 80,000
- **ii)** Perquisites and allowances - Rs. 50,000

11. Accounting depreciation - Rs. 55,000

Required:
Compute the taxable income of the firm considering that the depreciation under the Income Tax Ordinance comes to Rs. 45,000.
Answer:
Computation of Taxable Income
Tax at source (N-3) - 15,000
Salary paid without deduction of tax (N-4) - 200,000
Salary paid to Mr. 'A' (N-5) - 60,000
Interest paid to Mr. 'B' (N-5) - 5,000
Salary paid in cash (40,000 × 12) (N-6) - 480,000
Contribution to unrecognized Provident Fund - 30,000
Donations to unapproved institutions - 10,000
Donations to approved institutions (N-7) - 20,000
Salary and allowances to Manager (N-8) - Nil
Accounting depreciation (N-9) - 55,000
Total - 1,305,000
Less: **Tax depreciation (N-9)** - 45,000

Particulars	**Amount (Rs.)**
Net profit as per profit and loss account	400,000
Add: Deduction not admissible (N-1)	
Income tax (N-2)	30,000

Total taxable income - 1,260,000
Notes:
N-1 The expenses/payments which are inadmissible under the Income Tax Ordinance shall be added back to the profit or loss computed under the accounting principles.
N-2 Income tax paid is not an expense rather, it is an appropriation of profit, so should not be allowed as a deduction.
N-3 Tax deducted at source by the customers is an advance payment of tax on behalf of the firm and not an expense.
N-4 Any payment made without deduction of tax, if applicable, is inadmissible.
N-5 Any payment to a partner on account of salary, interest, etc., is not allowed as a deduction. It is immaterial that the tax at source has been deducted or not.
N-6 Salary exceeding Rs. 32,000 per month should be paid through cheque or direct transfer to the employee's bank account otherwise, it will be inadmissible.

N-7 Donation to an approved institution is not allowed as a direct deduction; rather, a tax credit is allowed at the average rate of tax.
N-8 Any payment made to employees on account of salary and allowances, etc., is allowed as a deduction against business income.
N-9 Accounting depreciation is not allowed as a deduction. The depreciation computed as per the Third Schedule (termed as Tax or Statutory Depreciation) is allowed as a deduction.

AMOUNTS SUBSEQUENTLY RECOVERED [70]

Where in any subsequent year a taxpayer has received an amount of such expenditure or loss, which was allowed as a deduction against the income from business in any tax year, such amount shall be deemed as income from business in the year of receipt.

ABNORMAL LOSSES [72(2)]

Where a business asset is destroyed, lost, or stolen, the amount representing the loss shall be charged to the profit and loss account and shall be allowed as a deduction while computing the "Income from Business." The amount of loss is determined as follows:

Value of the asset - XXX

Less: **Any amount received as salvage value, etc., if any.** - XXX

XXX

Any compensation, indemnity or damages received under: i) An insurance policy, indemnity or other agreement: XXX ii) A settlement; or: XXX iii) A judicial decision.: XXX

EXPENSES ON SCIENTIFIC RESEARCH [26]

A person shall be allowed a deduction under the head "Income from Business" if the following conditions are satisfied:

1. It is a **scientific research expenditure** incurred in Pakistan.
2. The expenditure is wholly and exclusively incurred for the purpose of deriving income from a business, which is chargeable to tax.

'**Scientific research expenditure**' means any expenditure on **scientific research** undertaken in Pakistan for the purpose of developing the person's business. It also includes any contribution to a **'scientific research institute'** to undertake research for the purposes of the person's business. However, it does not include expenditure in respect of the: i) Acquisition of a depreciable asset; ii) Acquisition of an intangible; iii) Acquisition of immovable property; or iv) Ascertaining the existence, location, extent, or quality of a natural deposit.

'**Scientific research**' means any activity in the field of natural and applied science for the development of human knowledge.

'**Scientific research institute**' means any institution certified by FBR as conducting scientific research in Pakistan.

EXPENSES ON EMPLOYEES' WELFARE AND TRAINING [27]

A person deriving income from business shall be allowed a deduction in respect of any expenditure incurred by him during the tax year on:

1. Any educational institution in Pakistan established for the benefit of his employees and their dependents;
2. Any hospital in Pakistan established for the benefit of the employees and their dependents;
3. Any institution meant for the training of industrial workers, if it is recognized, aided, or run by the Government (Federal, Provincial, or Local); and
4. Training of any Pakistani in connection with a scheme specially approved by FBR for this purpose.

BAD DEBTS [29]

A person shall be allowed a deduction on account of bad debts if:

1. The debt was previously included in his income. In case of a financial institution, it was an amount lent for deriving taxable income;
2. The amount of debt is written off during the tax year; and
3. There are reasonable grounds to believe that the debt cannot be recovered.

Note: The amount of deduction should not be more than the actual amount written off as bad debts. The amount allowed as deduction may be less than the actual bad debts.

Subsequent Recovery of Bad Debts

Where a person has been allowed a deduction on account of bad debts and in subsequent tax year he receives any amount in respect of that debt or loan, the amount so received shall be dealt with in the year in which it is received as below:

1. Where recovered amount is more than the difference between the actual bad debt and the bad debt allowed as deduction, then the excess amount shall be included in the business income for the year.
2. Where recovered amount is less than the difference between the actual bad debt and the bad debt allowed as deduction, then the shortfall shall be allowed as deduction against the business income for the year.

Example: 9.2

M/s. Lyallpur Cotton Mills Limited was allowed a deduction on account of bad debts amounting to Rs. 60,000 as against the actual bad debts of Rs. 100,000. After two years the company receives an amount from the debtors rendered as bad. Determine the amount to be included in total income or allowed as deduction if the amount so received is:

1. Rs. 100,000; or
2. Rs. 35,000

Answer:

1. Recovery of Rs. 100,000

- Amount recovered from bad debts: **Rs. 100,000**
- Less: Total bad debts: **(100,000)**
- Less: Amount allowed as deduction: **(60,000)**
- **Amount to be included in total income: Rs. 60,000**

2. Recovery of Rs. 35,000

- Amount recovered from bad debts: **Rs. 35,000**
- Less: Total bad debts: **(100,000)**
- Less: Amount allowed as deduction: **(60,000)**
- **Amount to be allowed as deduction: Rs. (5,000)**

CONSUMER LOANS BY BANKING COMPANIES, ETC. [29A]

The Income Tax Ordinance, 2001 contains a mechanism for allowing deduction in respect of anticipated bad debts arising out of **consumer loans**. The legal provisions in this regard are discussed below:

1. A Non-banking finance company or House Building Finance Corporation shall be allowed a deduction for a **reserve created** to offset the bad debts arising out of the consumer loans.
2. **Maximum deduction** on account of reserve shall be **3% of the income** for the tax year arising out of the consumer loans. It means a reserve can be created only if the institution has an **income** arising out of consumer loans.
3. On actual occurrence of a **bad debt**, the amount shall **not** be allowed as deduction, rather it shall be **set-off** against the reserve created for this purpose.
4. Where the amount of bad debts is **more than the reserve created**, then the… (text cut off in the image).

Additional amount of bad debts (which could not be set-off against the reserve) shall be carried forward to following years for setting it off against the reserves for those years.

"Consumer Loan" means a loan of money or its equivalent made by a non-banking finance company or the House Building Finance Corporation to a debtor (consumer) and the loan is entered primarily for personal, family or household purposes and includes debts created by the use of a lender credit card or similar arrangement as well as insurance premium financing.

PROFIT ON NON-PERFORMING LOANS [30]

Any interest/profit accruing on a non-performing loan credited to suspense account by a banking company, a development finance institution (DFI), Non-Banking Finance Company (NBFC) or modaraba in accordance with the **Prudential Regulations for Banks** or Non-Banking Finance Companies (NBFC) or modarabas, issued by the State Bank of Pakistan or SECP, shall be allowed as deduction.

Where a deduction has been allowed as above and thereafter any part of such amount is received during the tax year, then receipt shall be treated as **income from business** in the year in which any such amount is received.

TRANSFER TO PARTICIPATORY RESERVE [31]

Any amount transferred by a company to a **"Participatory Reserve"** created under section 66 of the **Companies Act, 2017** shall be allowed as deduction in the tax year in which it is transferred. For this purpose, the following conditions are to be fulfilled:

1. The reserve has been created in accordance with an agreement regarding **participatory redeemable capital** between the company and a banking company (as defined in the **Financial Institutions (Recovery of Finances) Ordinance, 2001**).
2. Maximum **5% of the participatory redeemable capital** is transferred to the reserve in a tax year.
3. Maximum **up to 10%** of the participatory redeemable capital may be claimed as **admissible deduction** on account of participatory reserve.

Any part of the amount accumulated in the participatory reserve, allowed as deduction, shall be **included in the Income from Business** in the tax year in which it is applied towards:

i) Any purpose **other than** payment of share of profit on the participatory redeemable capital; or

ii) Any purpose **not allowable** as deduction or exemption under the income tax law.

APPORTIONMENT OF COMMON EXPENDITURE, DEDUCTION AND ALLOWANCE [67]

It may happen that a **common expenditure, deduction and allowance** is incurred for different purposes. Such expenditure, etc., shall be **apportioned** amongst all such activities to which it relates. The apportionment shall be on some **reasonable basis** taking into account the nature and size of the subject matter for which expenditure, etc., is incurred. Apportionment of expenditure is necessary if it is incurred for:

1. **More than one head of income**, such as:
   - Income taxable under **normal tax regime (NTR)** and income taxable as a **separate block of incomes** (u/s 5, 6 & 7); or
   - Income, which is taxable under the **Income Tax Ordinance** and **some other purpose** (e.g., personal expenses).

Rules for Apportionment of Common Expenditure, Deduction and Allowance [Rule-13]

The provision relating to the apportionment of expenditures, etc., are summarized below:

1. Any expenditure, etc., that is incurred for a **particular class of income** shall be allocated to that class only.

2. Any expenditure, etc., that is incurred for **particular classes of income** shall be apportioned to those classes only.
3. Any **common expenditure, etc.** (excluding financial expenses) shall be apportioned amongst each class of income **according to the following formula**:

Amount of Expenses, etc. × Gross Receipts for the Class of Income
Gross Receipts for All Classes of Income

4. **'Gross receipt'** means **net of receipts or turnover** of **sales tax** and **federal excise duty paid**.
5. While allocating **common expenditure, etc.**, (particularly site renting expenses) the **nature and source** of each class of income must be taken into account.
6. The **basis determined for allocation of expenditure, etc.**, should be certified by a **Chartered Accountant** or a **Cost and Management Accountant**. This certificate would be accepted by **CIR** unless there is a significant variation (i.e., **10% ± beyond the limits**) from allocation under these rules.

Notes:

1. In the formula **'gross receipts'** means **all receipts without deduction of expenditures**.
2. Where in case of a certain transaction **net gain, brokerage, commission and other income** is taken as turnover, then the **gross profit from business** shall be taken as **gross receipts** (for the purpose of apportionment of expenditure).
    - The term **'Gross Receipt'** means **net of receipts or turnover of Sales Tax or Federal Excise Duty paid**.
3. For the purposes of **apportionment of expenditures**, etc., a person may have the following **classes of incomes**:

i) Pakistan-source incomes. These are further classified as incomes chargeable to tax under the head:

- a) Salary;
- b) Income from property;
- c) Income from business – non-speculation;
- d) Income from business – speculation;
- e) Capital gains; and
- f) Income from other sources.

ii) Foreign-source incomes. These are further classified as incomes chargeable to tax under the head:

- a) Salary;
- b) Income from property;
- c) Income from business – non-speculation;
- d) Income from business – speculation;
- e) Capital gains; and

- f) Income from other sources.

iii) Income exempt from Tax.
iv) Income chargeable to tax under separate tax regime – STR (u/s 5, 6 and 7).
v) Income chargeable to tax under final tax regime – FTR (u/s 169).

4. **“Common expenditure, deduction and allowance”** means an expenditure, deduction and allowance that are **not clearly allocable** to any **particular class or classes** of income (e.g., general administrative expenses).

NON-PAYMENT OF A LIABILITY [34(5) & (6)]

Where a person has been allowed a **deduction** on account of an **expenditure and liability** in respect of such expenditure is **not paid within three (3) years** of the end of the tax year in which it was allowed, such a **liability shall be treated as income from business** after the expiry of the above-said three (3) years.

If the taxpayer **pays the liability after the year** in which it is treated as **income**, it will be **allowed as a deduction** against the income from business for the tax year in which **payment is made**.

BENEFIT FROM A TRADING LIABILITY [34(5A)]

Where a deduction has been allowed in respect of **any trading liability** and subsequently the taxpayer has **derived any benefit** in respect of such trading liability, the **value of such benefit shall be chargeable to tax**, as **"Income from Business"** for the tax year in which **benefit has been received**.

One example of a **benefit from a trading liability** is a **cash discount** (i.e., **discount on earlier payment of a debt**).

Note:

Considering the definition referred above, a large number of assets may be termed as **‘Eligible Depreciable Asset’**. However, this classification of assets is meant **only for the purpose of some special depreciation allowance** u/s 23 or 23B of the Income Tax Ordinance.

According to the currently applicable provisions of the law (i.e., **Part-II of the Third Schedule**), only the following assets may fall under this category of assets:

1. **Plant and machinery**; and
2. **Plant, machinery & equipment installed for generation of alternate energy** by an **industrial undertaking**.

INTANGIBLE [2(30) & 24(11)]

Intangible means asset or expenditure of the following types if it provides an advantage or benefit for a period of **more than one year**:

1. Patent;
2. Invention;

3. Design or model;
4. Secret formula or process;
5. Copy right;
6. Trade mark;
7. Scientific or technical knowledge;
8. Computer software;
9. Motion picture film;
10. Export quotas;
11. Franchise;
12. Licence;
13. Intellectual property;
14. Other like property or right;
15. Contractual rights; or
16. Any other expenditure that provides **benefit for a period of more than one year**.

Notes:

1. 'Intangible' does **not include** self-generated goodwill or any adjustment arising on account of accounting treatment in the manner as may be prescribed.
2. Expenses relating to the above items shall be **amortized** according to **section 24** of the **Income Tax Ordinance** instead of allowing them as a **straight deduction**. (**FBR's Circular No. 7 of 2003, dated 11-07-2003**)

PRE-COMMENCEMENT EXPENDITURE [24(3) & 25(5)]

Broadly speaking **'Pre-Commencement Expenditure'** is **not an asset**; rather, it is an **expense**. But as it **provides benefit for more than one year**, it is **amortized over a period of five (5) years**. It is sometimes termed as **'deferred revenue expenditure'** or **'fictitious asset'**.

Under the **Income Tax Ordinance, 2001**, **'Pre-Commencement Expenditure'** means **any expenditure incurred before the commencement of such business**, the **income of which is chargeable to tax**. It includes:

1. Incorporation expenses;
2. Cost of feasibility studies;
3. Cost of construction of prototypes; and
4. Cost of trial production activities.

However, **any expenditure, which is incurred for acquiring any land, depreciable asset or intangible, shall not be included in 'pre-commencement expenditure'.** The expenses shall form part of such **asset** for which these were incurred.

STOCK-IN-TRADE [2(62) & 35(7)]

'Stock-in-Trade' means anything **produced, manufactured, purchased, or otherwise acquired** for **manufacture, sale, or exchange**. It also includes **any material or supplies** that are to be consumed in the **production or manufacturing process**.

However, **stocks or shares do not form part of the 'stock-in-trade'**. This means that **shares, etc., will never be treated as stock-in-trade** even if these are held for **business and sale purposes**.

ACQUISITION OF AN ASSET [75(5) & (6)]

A person shall be treated as having **acquired an asset** at any of the following times:

1. When he begins to **own an asset**;
2. When he is **granted any right** to own an asset; or
3. When a **personal asset is applied for business use**.

DISPOSAL OF AN ASSET [21(8) & 75(1) to (4)]

Disposal of an asset means to **pass over an asset** to some other person. In general, it denotes a **change in ownership** of an asset. Under the **Income Tax Ordinance, 2001**, a disposal may take place when an asset is:

1. **Sold**;
2. **Exchanged**;
3. **Transferred**;
4. **Distributed**;
5. **Cancelled**;
6. **Redeemed**;
7. **Relinquished** (to abandon, give up or renounce some right or thing);
8. **Destroyed**;
9. **Lost**;
10. **Expired**;
11. **Surrendered**.

Additionally:

- **Transmitted by succession** or **under a will**;
- In case of a **business asset, applied to personal use**; or **[75(3)]**
- In case of a **business asset, discarded or ceased to be used in business**. **[75(3A)]**

Notes:

1. In case of **transmission by succession** or **under a will**, the **time of disposal** of an asset shall be the time **at which it is transmitted**. **[75(2)]**
2. An asset may be **disposed of in full or in parts**. **[75(4)]**
3. **'Business asset'** means an **asset** (including stock-in-trade and a depreciable asset), which is held **wholly or partly** for use in a business. **[75(7)]**
4. **'Personal asset'** means an asset, which is held **wholly for personal use**. **[75(7)]**

PURCHASE OF ASSETS THROUGH BANKING CHANNEL [75A]

The **Income Tax Ordinance, 2001** provides that no person shall purchase **any immovable property or any other asset** having **FMV greater than Rs. 5,000,000** or **Rs. 1,000,000**, respectively, unless the **payment is made through** a **crossed cheque, crossed demand draft,**

crossed pay order, or any other crossed banking instrument showing **transfer of an amount from one bank account to another bank account**.

Further, in case of **immovable property**, means the **higher of**:

- The **value notified by the FBR** under **8(4)**; **or**
- The **value fixed by the provincial authority** for **stamp duty purposes**.

COMPUTATION OF TAXABLE BUSINESS INCOME

While computing the taxable **'Business Income'**, two situations may arise, i.e., where the **profit and loss account is provided** and where instead of a profit and loss account, **such information** is provided from which the **profit or loss** may be determined. The method adopted for computation of taxable income shall depend upon the given situation.

Where Profit and Loss Account is Given

Where in a particular case the **profit and loss account** or the **result of profit and loss account** (i.e., profit or loss) is given, the profit or loss is to be adjusted **according to the available information**. All **errors (both accounting as well as tax)** are to be **rectified** in order to compute the taxable income.

This process may be done as below:

Net profit/(loss) as per profit and loss account

XXX

Add:

- **Inadmissible expenses** – **XXX**
- **Income not included in P/L A/c** – **XXX**
- **Rectification of accounting errors, which result in an increase of income** – **XXX**
- **Expenses for such income, which is not taxable under this head** – **XXX**

Less:

- **Admissible allowance not recorded** – **XXX**
- **Expenditures not included in P & L A/c** – **XXX**
- **Rectification of accounting errors, which result in a decrease of income** – **XXX**
- **Incomes not taxable under this head** – **XXX**

Total Income from Business – **XXX**

Where Profit and Loss Account is Not Given

Where in a particular case, instead of providing the **profit and loss account** or the **result of profit and loss account** (i.e., profit or loss), the **information for determining** the amount of **profit or loss** is provided, then we will have to **prepare the profit and loss account** by taking into account the **accounting principles** as well as the **taxation rules**. Under such a case, **only such expenses shall be deducted** from the incomes, which are **permitted under the Income Tax Ordinance**.

ASSETS AND DEPRECIATION

ASSETS

The term **'asset'** has been defined in different ways by accounting and legal experts. Some selected definitions are given below:

- **"Asset means any resource, tangible or intangible, from which future benefits are expected and the rights to which have been acquired as a result of a past or present transaction."** (Macmillan Dictionary of Accounting).
- **"Asset means economic property or legal right owned by an individual or a company to which a money value can be assigned."** (Dictionary of Accounting & Finance).
- **Black's Law Dictionary defines assets as**:
  "Property of all kinds, real and personal, tangible and intangible, including, inter alia, for certain purposes; patents and causes of action which belong to any person including a corporation and the estate of a decedent. The entire property of a person that is applicable or subject to the payment of his debt."

The **Income Tax Ordinance, 2001** recognizes the following types of **assets**:

1. **Capital asset**
2. **Depreciable asset**
3. **Eligible depreciable asset**
4. **Intangible asset**
5. **Pre-commencement expenditure**
6. **Stock-in-trade**

CAPITAL ASSET [2(10) & 37(5)]

Refer to Chapter **"Capital Gains"**

DEPRECIABLE ASSET [2(17) & 22(15)]

Briefly, **any tangible movable or immovable property** having **normal useful life** of **more than one year** and is **being used by the owner for his business purposes** is a **depreciable asset**. (For detailed definition, see the part of this chapter which deals with **Depreciation**).

ELIGIBLE DEPRECIABLE ASSET [23(5)]

'Eligible Depreciable Asset' means a **depreciable asset** other than the following assets:

1. **Any road transport vehicle unless the vehicle is plying for hire.**
   (A vehicle which is plying for hire will be considered as an eligible depreciable asset.)
2. **Any furniture or fittings.**
3. **Any plant or machinery that has been used previously in Pakistan.**
4. **Any plant or machinery whose entire cost has been allowed as a deduction under another section of the ITO in the tax year in which it is acquired.**
5. **Immovable property or structural improvement to the immovable property.**

1. The following shall be the consequences if the transaction is not undertaken in the manner specified above:
    - Such asset shall not be eligible for any depreciation allowance u/s 22, 23, 24, and 25 of the Income Tax Ordinance; and
    - Such amount shall not be treated as cost in terms of section 76 of the Income Tax Ordinance for computation of any gain on sale of such asset.

COST OF AN ASSET [76]

The cost of an asset acquired by a person shall be determined in accordance with the following rules.

Purchase of an Asset [76(2)]

Where a person purchases an asset, its cost of acquisition shall include the following amounts:

1. Consideration paid for the asset. The consideration may be in cash or in kind. Where the consideration is in kind, the fair market value of an asset given as consideration (on the date when the new asset is acquired) shall be taken as consideration for the new asset.
2. Expenses incurred on acquisition of an asset.
3. Expenses incurred for alteration or improvement of an asset.
4. Expenses incurred on disposal of an asset.

Note: Inclusion of 'disposal expenses' in cost is against the basic definition of the term 'cost' as these expenses are incurred at the time of disposal of an asset and not at the time of acquisition. However, it seems that in order to render the tax law compatible with International Accounting Standards, the law makers have included disposal expenses in the definition of 'cost of acquisition'. In this way, disposal expenses are allowed as a deduction while computing the gain or loss on disposal of an asset.

Example: 10.1

Usama Limited purchased a vehicle for Rs. 1,900,000 and incurred Rs. 100,000 on its registration, etc. After three (3) years, the company sold out the vehicle for Rs. 1,600,000. The total accumulated depreciation till the time of disposal (as per tax record) was Rs. 771,750. An amount of Rs. 50,000 was paid as commission on the disposal.

Required: Compute the gain / (loss) on disposal of the vehicle.

Answer:

Disposal Consideration: Rs. 1,600,000

Less: Written down value at the time of disposal

- **Cost:**
    - Purchase Price: Rs. 1,900,000
    - Expenses on Registration: Rs. 100,000
    - Commission on Disposal: Rs. 50,000

- **Total:** Rs. 2,050,000

- **Less: Accumulated Depreciation:** Rs. (771,750)
- **Written Down Value:** Rs. (1,278,250)

Gain on Disposal of Vehicle: Rs. 321,750

Personal Asset Treated as Business Asset [76(3)]

Where a personal asset is applied for business and treated as acquired by the business, then the fair market value at the time the asset is applied for business shall be taken as the cost of the asset to the business.

Asset Produced or Constructed by a Person [76(4)]

Where a person has himself produced or constructed an asset, then the following amounts shall be included in the cost of such asset:

1. Total costs incurred in producing or constructing the asset.
2. Expenses incurred on bringing the asset in useable condition.
3. Expenses incurred for alteration or improvement of an asset.
4. Expenses incurred on disposal of an asset.

Example: 10.2

Progressive Limited purchased a machine for Rs. 1,350,000. The company incurred the following expenses in respect of the machine:

- Freight and other charges - Rs. 15,000
- Loading and unloading charges - Rs. 2,000
- Spares purchased for erection of the machine - Rs. 3,000
- Labour and other expenses connected with erection - Rs. 5,000
- Wages paid to the worker during the month of erection of the machine - Rs. 5,000
- Oil and lubricants during the month - Rs. 500

Required: Compute the cost of the machine.

Answer:

Cost of the Machine

Particulars	**Rs.**
Purchase Price	1,350,000
Add: Expenses on bringing the machine in useable condition:	
Freight and other charges	15,000
Loading and unloading	2,000
Spares	3,000
Labour charges	5,000
Total Cost of the Machine	**1,375,000**

Note: Expenses incurred after the erection of the machine (e.g., wages to workers and oils & lubricants) are ignored while computing the cost of an asset.

Asset Acquired with a Foreign Currency Loan [76(5) & (6)]

Where an asset is acquired with a loan in foreign currency and exchange rate fluctuation increases or decreases the liability of the person in Pak rupees, then any increase or decrease in the liability, before full and final repayment of the loan, shall also be added to or deducted from the cost of the asset.

Notes:

1. For the purpose of depreciation, the difference on account of foreign currency fluctuation, if any, shall be taken into account in the year of occurrence.
2. The terms and conditions of any hedging agreement shall be considered in determining whether the exchange rate fluctuation has any effect on the increase or decrease in a person's liability. [7(6)].
3. Where an asset is acquired against a foreign currency loan and, as a result of hedging agreement, there is no change in the liability of the person in local currency, then there will be no change in the cost of the asset.

Example: 10.3

Lalazar Limited acquired a foreign currency loan amounting to US$ 40,000 in the beginning of the year 20x1. The loan was repayable in eight (8) half-yearly installments of US$ 5,000. The loan was utilized for import of a plant valuing equal to the amount of the loan. At the time of obtaining the loan and importing the plant, one US Dollar was equal to Rs. 100. The company incurred the following expenses in connection with the plant:

- Insurance and sea freight: Rs. 20,000
- Port expenses: Rs. 5,000
- Customs duty and excise duty on import: Rs. 55,000
- Inland freight and octroi charges: Rs. 10,000
- Expenses on installation of plant: Rs. 10,000

After payment of four installments, the exchange rate fluctuated, and the next two installments were paid @ Rs. 105 and Rs. 110, respectively, per one US$.

Required: Compute the cost of the plant prior to and after the change in exchange rate (i.e., in year 20x1 and 20x3 respectively). Also, compute the depreciation for the years 20x1, 20x2, and 20x3 assuming that the depreciation is charged @ 15% on WDV (Ignore the 'initial allowance' u/s 23).

Answer:

Cost of plant prior to change (i.e., in year 20x1)

- Purchase price (US $ 40,000 @ Rs. 100) = Rs. 4,000,000

Add: Other Costs:

- Insurance and sea freight = Rs. 20,000
- Port expenses = Rs. 5,000

- Customs duty and excise duty = Rs. 55,000
- Inland freight and octroi = Rs. 10,000
- Installation expenses = Rs. 10,000
- **Total Cost** = Rs. 4,100,000

Cost of Plant after Change (i.e., in year 20x3)

- Total cost prior to change (as above) = Rs. 4,100,000
- **Add: Increase in liability due to the change in exchange rate [N-1]**
    - Increase in 5th installment $5,000 × Rs. 5 (i.e., Rs. 105 – Rs. 100) = Rs. 25,000
    - Increase in 6th installment $5,000 × Rs. 10 (i.e., Rs. 110 – Rs. 100) = Rs. 50,000
    - **Total increase in liability** = Rs. 75,000
- **Total cost after change** = Rs. 4,175,000

Income Tax – Assets & Depreciation

Depreciation for the Year:

Year 20X1

Total cost of plant: Rs. 4,100,000

Depreciation (Rs. 4,100,000 × 15%): Rs. 615,000

Year 20X2

Total cost: Rs. 4,100,000

Less Depreciation for Year 20X1: Rs. 615,000

Written down value: Rs. 3,485,000

Depreciation (Rs. 3,485,000 × 15%): Rs. 522,750

Year 20X3

Total cost: Rs. 4,175,000

Less Accumulated Depreciation (Rs. 615,000 + Rs. 522,750): Rs. 1,137,750

Written down value: Rs. 3,037,250

Depreciation (Rs. 3,037,250 × 15%): Rs. 455,588

Example: 10.4

Using the data of Example-10.3, compute the total cost and depreciation for the year 20X4, assuming that on the first day of the year 20X4, the exchange rate became Rs. 96 per US$. The remaining two installments were paid at this rate.

Answer:

Total cost prior to change in year 20X4: Rs. 4,175,000

Less Decrease in Liability due to change [N-1]: Rs. 40,000

Total cost after change: Rs. 4,135,000

N-1 Decrease in Liability due to Change in Exchange Rate:

Total loan repaid in 20X4 (5,000 × 2): US$ 10,000

Liability in Pak Rupees already booked (10,000 × 100): Rs. 1,000,000

Liability in Pak Rupees already paid (10,000 × 96): Rs. 960,000

Decrease in liability: Rs. 40,000

Depreciation for Year 20X4

Total cost: Rs. 4,135,000

Less Accumulated Depreciation:

- Year 20X1: Rs. 615,000
- Year 20X2: Rs. 522,750
- Year 20X3: Rs. 455,588

Total Accumulated Depreciation: Rs. 1,593,338

Written down value: Rs. 2,541,662

Depreciation (Rs. 2,541,662 × 15%): Rs. 381,249

Asset Acquired from Any Subsidy, etc. [76(10)]

The amount of any grant, subsidy, rebate, commission, or any other assistance received or receivable in respect of acquisition of an asset shall not be included in the cost of such asset. However, where the amount of grant, etc., is chargeable to tax under the Income Tax Ordinance 2001, then such an amount shall also be included in the cost of the asset.

Income Tax – Assets & Depreciation

Example: 10.5

A charitable institution received a grant of Rs. 150,000 for purchasing some equipment. The required asset was purchased at Rs. 170,000. Compute the cost of the asset where:

1. The grant is not chargeable to tax; and
2. The grant is chargeable to tax.

Answer:

1. Grant Not Chargeable to Tax

Purchase value of equipment: Rs. 170,000

Less Grant received for equipment: Rs. 150,000

Cost of the asset: Rs. 20,000

2. Grant Chargeable to Tax

In this case, Rs. 170,000 will be the cost of the equipment as the grant received is chargeable to tax. The amount of the grant shall be included in the income of the institution, and the total amount paid for the asset shall be the cost of the asset.

Where Acquisition of an Asset is Derivation of an Amount Chargeable to Tax [76(8)]

When the acquisition of an asset is derived from an amount chargeable to tax, the cost of the asset shall be the amount or chargeable plus any amount paid by the person for the asset.

Where Acquisition of an Asset is Derivation of an Amount Exempt from Tax [76(9)]

When the acquisition of an asset is derived from an amount exempt from tax, the cost of the asset shall be exempt, excluding any amount paid by the person for the asset.

Explanation

The above two cases lay down the procedure for determining the cost of an asset acquired under different situations:

1. Chargeable to tax
2. Exempt from tax

In both cases, the amount to be taken as the cost is the same. The provisions determine that the source of income from which the asset is acquired rather than the consideration determines the cost of the asset.

For example, if a taxpayer has both taxable and exempt sources of income (such as an agricultural business which is exempt from tax and another business which is chargeable to tax) and acquires an asset using either, the cost is determined accordingly.

It should be noted that if an asset is acquired from exempt income and the cost is partly paid, the amount spent shall form part of the cost of the asset. However, in cases where the source is a grant, subsidy, etc., that amount is exempt from tax.

Disposal of an Asset in Parts [76(7)]

If an asset is disposed of in parts, the cost shall be apportioned between the disposed part and the retained part based on the fair market value of both at the time of acquisition.

Income Tax – Assets & Depreciation

FBR's Power to Prescribe Rules [76(11)]

FBR is empowered to prescribe rules for the determination of the cost of any asset. In that case, the cost of such assets shall be determined in light of such rules.

Asset Acquired on Disposal of an Asset under Compulsory Acquisition [79(4)]

When a person acquires an asset in exchange for another asset that was disposed of due to compulsory acquisition under any law, the cost of such an asset shall be determined as follows:

Cost of the asset disposed of: **XXX**

Add: Consideration given for replacement asset: **XXX**

Less: Consideration received for disposal of asset: **(XXX)**

Total cost of the replacement asset: **XXX**

This method of cost determination shall be adopted only if the consideration received is reinvested in acquiring an asset of a similar kind within one year of disposal.

Example: 10.6

An asset of a taxpayer (costing Rs. 450,000) was acquired by the Government for Rs. 600,000. The taxpayer then purchased another asset of the same nature for Rs. 650,000. Determine the cost of the replacement asset.

Answer:

Cost of the asset disposed: **Rs. 450,000**

Add: Consideration for replacement asset: **Rs. 650,000**

Less: Consideration received for disposal: **Rs. 600,000**

Cost of the replacement asset: **Rs. 500,000**

Note: Although the replacement asset is purchased for Rs. 650,000, its cost for tax purposes shall be taken as Rs. 500,000.

Example: 10.7

Considering the information in Example 10.6, compute the cost of the replacement asset if the new asset is purchased for Rs. 550,000.

Answer:

Cost of the asset disposed: **Rs. 450,000**

Add: Consideration for replacement asset: **Rs. 550,000**

Less: Consideration received for disposal: **(Rs. 600,000)**

Cost of the replacement asset: **Rs. 400,000**

Consideration on Disposal of an Asset [77]

At the time of disposal of an asset, the gain or loss is computed and charged to the profit & loss account to determine the actual income of a person. A key element in this regard is the value of the consideration received on disposal of an asset. Below is a summary of the relevant provisions of the Income Tax Ordinance, 2001.

Income Tax – Assets & Depreciation

Disposal Consideration on Sale of an Asset [77(1)]

When an asset is sold, the higher of the total amount received for the asset or its fair market value shall be the consideration. Where the consideration is received in kind, then the fair market value of the asset or thing received (at the time of disposal) shall be the consideration.

Disposal Consideration in Case of a Lost or Destroyed Asset [77(2)]

When an asset has been lost or destroyed, the disposal consideration for such an asset shall consist of the following amounts:

1. Any amount received as salvage value, etc., if any.
2. Any compensation, indemnity, or damages received under:
    - An insurance policy, indemnity, or other agreement;
    - A settlement; or
    - A judicial decision.

Consideration of an Asset Applied for Personal Use [77(3)]

When a business asset is applied for personal use, then its fair market value at the time it is so applied shall be taken as disposal consideration.

Consideration of a Discarded Asset [77(3)]

When a business asset is discarded or ceases to be used in business, then its fair market value at the time it is discarded, etc., shall be taken as disposal consideration.

Consideration of a Leased Asset [77(4)]

The residual value received by a *leasing company* on the maturity of a lease agreement shall be taken as consideration for the disposal of such an asset.

However, it should be noted that the residual value plus the total amount received by the leasing company towards the cost of the asset (i.e., the principal part of the lease rentals realized by the leasing company) should not be less than the original cost of the asset to the leasing company.

A *Leasing Company*, for this purpose, means any of the following institutions, if approved by the Commissioner:

1. Schedule banks;
2. Financial institutions;
3. Modarabas; or
4. Leasing companies.

Example: 10.8

A leasing company purchased an asset for Rs. 800,000. The company leased out the asset on the following terms:

1. Advance deposit of Rs. 80,000 to be adjusted against an equal amount of residual value.
2. Rs. 1,000,000 payable in 40 monthly installments of Rs. 25,000.

Required:

Compute the disposal consideration under each of the following cases where the installment is divided between principal repayment and financial charges, respectively, as below:

A) **80% : 20%**

B) **75% : 25%**

C) **70% : 30%**

Answer:

Disposal consideration in each case shall be as below:

Income Tax – Assets & Depreciation

Division of Installment and Disposal Consideration

Division of Installment	**Residual Value**	**Residual Value plus Principal**	**Disposal Consideration**
Principal	**Lease Charges**	**Residual Value**	**Residual Value plus Principal**
A	800,000	200,000	80,000

B	750,000	250,000	80,000
C	700,000	300,000	80,000

Notes:

1. Under situations A & B, the amount of residual value plus the principal part of the lease rentals (installments) is more than the original cost of the asset (i.e., Rs. 800,000), so the residual value shall be taken as disposal consideration.
2. Under situation C, the amount of residual value plus the principal part of the lease rentals (i.e., Rs. 780,000) is less than the original cost of the asset. In this case, the difference between the original cost (i.e., Rs. 800,000) and the total of residual value and the principal part of the lease rentals (i.e., Rs. 780,000) shall be added to the residual value in order to determine the disposal consideration. Disposal consideration under this case is computed as below:
   - **Residual value** = Rs. 80,000
   - **Add:**
     - Original cost of asset = Rs. 800,000
     - Less: Residual value plus principal part = (Rs. 780,000)
     - **Difference** = Rs. 20,000
   - **Disposal consideration** = Rs. 100,000

Consideration of Assets Sold in Bulk [77(5)]

When different assets are disposed of through a single transaction and the consideration of each asset is not determined or specified separately, the total consideration received shall be apportioned among all assets so disposed. This apportionment shall be on the basis of the fair market value (FMV) of assets at the time of the transaction. In other words, the disposal consideration shall be computed using the following formula:

Total Consideration Received×FMV of an assetFMV of all assets\text{Total Consideration Received} \times \frac{\text{FMV of an asset}}{\text{FMV of all assets}}Total Consideration Received×FMV of all assetsFMV of an asset

Example: 10.9

A company sold the following assets in a single transaction for Rs. 500,000. The written down value (WDV) and the fair market value (FMV) of the assets are given below:

Required:

Asset	**WDV (Rs.)**	**FMV (Rs.)**
Vehicle	100,000	160,000
Furniture & Fixture	50,000	45,000
Office Equipment	80,000	140,000
Miscellaneous Assets	70,000	55,000
Total	**300,000**	**400,000**

Consideration for each class of assets and gain on disposal of the assets.

Answer:

Consideration of Assets Sold

Vehicle=500,000400,000×160,000=200,000\text{Vehicle} = \frac{500,000}{400,000} \times 160,000 = 200,000Vehicle=400,000500,000×160,000=200,000
Furniture=500,000400,000×45,000=56,250\text{Furniture} = \frac{500,000}{400,000} \times 45,000 = 56,250Furniture=400,000500,000×45,000=56,250
Office Equipment=500,000400,000×140,000=175,000\text{Office Equipment} = \frac{500,000}{400,000} \times 140,000 = 175,000Office Equipment=400,000500,000 ×140,000=175,000 Other Assets=500,000400,000×55,000=68,750\text{Other Assets} = \frac{500,000}{400,000} \times 55,000 = 68,750Other Assets=400,000500,000 ×55,000=68,750

Gain/(Loss) on Disposal of Asset

Asset	Consideration Received (Rs.)	WDV (Rs.)	Gain/(Loss) (Rs.)
Vehicle	200,000	100,000	100,000
Furniture	56,250	50,000	6,250
Office Equipment	175,000	80,000	95,000
Other Assets	68,750	70,000	(1,250)
Total	**500,000**	**300,000**	**200,000**

FBR's Powers to Prescribe Rules [77(6)]

The FBR is empowered to prescribe rules for the determination of consideration received for any assets. If so prescribed, the disposal consideration shall be determined in accordance with such rules.

COST AND DISPOSAL VALUE IN NON-ARMS LENGTH TRANSACTIONS [78]

The fair market value of the asset at the time of the transaction shall be taken, respectively, as cost and disposal consideration to the buyer and the seller, if the asset is purchased or sold in non-arm's length transactions.

FAIR MARKET VALUE [68]

For the purposes of the Income Tax Ordinance, *fair market value* (FMV) is determined in relation to a property or rent, asset, service, benefit, or perquisite. Fair market value means the price at which a particular property, etc., would ordinarily fetch on sale or supply in the open market at a particular time. [68(1)]

Notes:

1. The FMV shall be determined irrespective of whether there is any restriction on transfer of the asset or if it is not otherwise convertible into cash. [68(2)]
2. The CIR may determine the price in a case where it is not ordinarily ascertainable. The CIR shall not determine the price of immovable property. [68(3)]
3. The FBR shall determine the FMV of immovable properties of the area or areas. Such value shall be notified in the official Gazette. [68(4)]
4. The FBR has notified FMV of properties for various parts of Pakistan. While determining the capital gain on the disposal of properties, the notified value shall be taken into account.
5. In areas where the FBR has not notified the FMV, the value fixed for stamp duty by the District Officer (Revenue) or any other authorized authority shall be deemed as the FMV for properties of those areas. [68(5)]
6. In respect of an immovable property, the value for the following purposes shall not be less than the FMV as notified by the FBR or as fixed by the District Officer (Revenue), etc., as the case may be. [68(6)]

Income Tax – Assets & Depreciation

Consideration Received for Various Purposes

i) Consideration received to be used for computation of capital gain u/s 37 on disposal of immovable property.

ii) Consideration received to be used for levy of advance tax u/s 236C on transfer of immovable property.

iii) Value for collection of advance tax u/s 236K on purchase of immovable property.

iv) Value to be taken as income u/s 111 in respect of unexplained asset.

Note: Under all these cases, if the FMV (as determined above) is different from the *auction price*, the higher of the FMV and the auction price shall be taken as value.

NON-RECOGNITION OF GAIN OR LOSS ON DISPOSAL OF AN ASSET [79]

Normally, the gain or loss on disposal of an asset is taken into account. However, in the following cases, no gain or loss shall be taken to arise if the person acquiring the asset is a resident person:

1. Where disposal is between spouses under an agreement to live apart.
2. Where disposal is by reason of the transmission of the asset to an executor or beneficiary on the death of a person.
3. Where disposal is by reason of a gift of the asset to a *relative*.
4. Where disposal is by a company to its members on its liquidation.
5. Where disposal is by an association of persons to its members on its dissolution. However, under this case, the assets should be distributed in accordance with the interest of members in the capital of AOP.

Notes:

A) If the person acquiring the asset is a non-resident person, the gain or loss on disposal of assets shall be computed as per normal procedure.

B) Under all the above cases, it shall be treated that:

i) The person is acquiring the asset of the same character as the person disposing of the asset, and

ii) The person is acquiring the asset at a cost that is equal to the cost of the asset at the time of disposal to the person disposing it off.

C) **'Relative'** in relation to an individual means:

i) An ancestor, a descendant of any of the grandparents, or an adopted child, of the individual, or of a spouse of the individual; or

ii) A spouse of the individual or of any person specified above. [85(5)]

6. Where the disposal is by reason of the compulsory acquisition of the asset under any law. In order to avail this benefit, the consideration received on disposal shall be reinvested (within one year of the disposal) in an asset of similar kind.

DEPRECIATION

Depreciation has been defined as a measure of the wearing out, consumption, or other loss of the value of a *Fixed Asset* arising from use, effluxion of time, or obsolescence. Depreciation as a term is sometimes restricted to fixed tangible assets but is usually regarded as a general term that also includes the amortization of intangible assets and assets such as leases whose useful life is limited.

DEPRECIATION UNDER INCOME TAX

A business house is at liberty to adopt any of the depreciation methods for charging the cost of an asset to its profit and loss account for financial reporting purposes. However, **Section 22(2)** renders it mandatory for a person who acquires a depreciable asset or an intangible with a useful life of more than one year or incurs pre-commencement expenditure to depreciate or amortize the asset, as per **Sections 22, 23 (also 238), 24, and 25**. It further specifies that while computing income under the head *'Income from Business'*, an allowance for depreciation shall be allowed as a deduction **only if it is calculated in accordance with the Third Schedule** to the **Income Tax Ordinance, 2001**. Thus, while computing the income from business, any depreciation charged to the profit and loss account without adopting the provisions of the Third Schedule shall be treated as inadmissible and shall be added back to the profit as per the profit and loss account. This depreciation is generally termed as **"Accounting Depreciation."**

The amount of depreciation computed as per the Third Schedule (commonly known as **'Statutory Depreciation'** or **'Tax Depreciation'**) is an admissible deduction against the Income from Business.

Example: 10.10

Ehzabd Limited shows a profit of **Rs. 3,500,000** after charging **Rs. 1,450,000** as depreciation on its assets. The company consistently follows a well-defined system of depreciation. However, the depreciation for the year, as per **Income Tax Ordinance,** comes to **Rs. 1,600,000**. Assuming other things are in conformity with the law, compute the taxable income of the company.

Computation of Taxable Income	**Rs.**
Profit as per Profit and Loss Account	3,500,000
Add: Accounting depreciation	1,450,000
Total	4,950,000
Less: Statutory depreciation	1,600,000
Taxable income of the company	**3,350,000**

DEPRECIATION RULES

The **Third Schedule to the Income Tax Ordinance, 2001** specifies rates at which the depreciation shall be allowable under the law. These rules are briefed in the following paragraphs.

ASSETS ON WHICH DEPRECIATION IS ALLOWED [2(17) & 22 (1), (2) & (15)]

Depreciation under Income Tax is allowed on **"depreciable assets"**, used by a person for his business. Depreciation is computed by applying the depreciation rates specified in the Third Schedule to the **Income Tax Ordinance, 22(1) & (2).**

A **"Depreciable asset"** means a property that fulfills the following conditions:

1. It is owned by the person whose taxable income is being determined.
2. It should be any:

   i) **Tangible moveable property**

   ii) **Immovable property** (other than unimproved land)

   iii) **'Structural Improvement'** to immovable property

Income Tax – Assets & Depreciation

'Structural Improvement'

Structural Improvement means any **building, road, driveway, car park, railway line, pipeline, bridge, tunnel, airport runway, canal, dock, wharf, retaining wall, fence, power lines, water and sewerage pipes, drainage, landscaping, or dam.**

Conditions for Depreciable Asset

A property is considered a **depreciable asset** if:

1. It has a **normal useful life exceeding one year**.
2. It is **likely to lose value** due to normal wear and tear or **obsolescence**.
3. It is used **wholly or partly** by the owner in deriving **income from business chargeable to tax**.

However, where the total cost of any asset has been **allowed as a deduction** in the year of its acquisition, such an asset **shall not be included** in "depreciable assets."

Categories of Depreciable Assets

A depreciation allowance is **admissible only if the assets** are **owned and used** by a taxpayer for business. The depreciable assets may fall under any of the following **categories**:

1. **Buildings**
2. **Machinery**
3. **Plant**
4. **Furniture, fixtures, and fittings**
5. **Ships**
6. **Computer hardware, allied accessories, and machinery and equipment** used in the manufacture of I.T. products
7. **Technical or professional books**
8. **Vehicles**
9. **Aircraft, etc.**
10. **Below ground installations**
11. **Offshore platforms and production installations** in mineral oil concerns

ASSET USED PARTLY FOR BUSINESS [22(3)]

Where an asset is used **partly for business** and **partly for other purposes**, then only that **proportion of the depreciation** shall be allowed as a **deduction** that **fairly relates** to the **business**.

Example: 10.11

Mr. Saif owns a building in which he carries on **his business** and **also resides with his family**. Only **1/4th** of the building is used for his business. Compute the **depreciation allowance chargeable to business** if the **cost** of the building is **Rs. 4,000,000**. (*Ignore provisions relating to reduced depreciation for the year of acquisition.*)

Computation of Depreciation Allowance	**Rs.**
Written down value (WDV) at the beginning (i.e., Cost)	4,000,000
Depreciation rate as per Third Schedule	**10% of WDV**
Depreciation for the building (4,000,000 × 10%)	400,000
Depreciation chargeable to business (400,000 ÷ 4)	**100,000**

ASSET NOT USED FOR WHOLE YEAR

Where an asset is **not used for the whole tax year**, **depreciation for such an asset shall be charged for the whole year**. In other words, **full depreciation shall be charged** for the year of acquisition. However, **no depreciation shall be charged in the year when the asset is disposed of**.

Income Tax – Assets & Depreciation

TREATMENT OF DEPRECIATION WHERE BUSINESS IS EXEMPT

(*Explanation to 22(5)*)

Business is Permanently Exempt:

Where income from a business is **permanently exempt from tax**, the person is **not obliged** to follow the rules for **depreciation allowance** under the **Income Tax Ordinance, 2001**. The person may charge **depreciation as per accounting policies** adopted for this purpose.

Business is Exempt for a Certain Period:

Where the income from business is **subject to a tax holiday** (*i.e., exempt from tax for a specific period*), the **depreciation allowance** (including **"initial allowance"** u/s **23**) shall be provided **as per normal procedure**. The following **procedure** shall be adopted in this case:

1. The **depreciation for the exempted period** shall be deemed to have been **allowed** for the tax years **during which the income was exempt**; and
2. After the **exemption period**, the **depreciation** shall be **allowed on the WDV at the prescribed rate**. The **WDV** shall be calculated by **deducting the depreciation deemed to have been allowed** from the **actual cost of the asset**.

Example: 10.12

A company was **incorporated on 1st day of tax year 20X1**. It **purchased plant and machinery immediately after incorporation** at a price of **Rs. 1,000,000**. The company is **exempt from tax for five years** (*i.e., up to tax year 20X5*). (*Ignore the Initial Allowance*).

Required:

Compute the **amount of depreciation allowance allowable** for the **tax year 20X6**.

Answer:

WDV at the beginning of the tax year 20X6 [N-1]

WDV = Rs. **443,705**

Rate of depreciation = **15%**

Depreciation for tax year 20X6 = Rs. **66,556**

N-1: WDV for the tax year 20X6:

Details	**Amount (Rs.)**
Actual cost of the plant and machinery	1,000,000
Less: Depreciation deemed to have been allowed [N-2]	(556,295)
WDV for tax year 20X6	**443,705**

N-2: Depreciation deemed to have been allowed during five tax years, i.e., up to 20X5:

Tax Year	Opening WDV	Depreciation @ 15%	WDV After Depreciation
20X1	1,000,000	150,000	850,000
20X2	850,000	127,500	722,500
20X3	722,500	108,375	614,125
20X4	614,125	92,119	522,006
20X5	522,006	78,301	443,705
Total Depreciation Deemed Allowed	**556,295**		

ASSET WITH USEFUL LIFE UPTO ONE YEAR [22(6)]

Where the **useful life** of an asset is **one year or less**, **no depreciation allowance** shall be allowed. Instead, the **renewal or replacement cost** shall be **allowed as revenue expenditure**.

RATES FOR DEPRECIATION ALLOWANCE
(*Part I of Third Schedule*)
The **depreciation allowance** in respect of **assets used for the purpose of business** shall be **computed at the rates specified** in the table given below:
Income Tax – Assets & Depreciation
Depreciation Rates on Written Down Value (WDV)

S. No.	Description	Rate on WDV
1	Buildings (all types)	10%
2	Furniture (including fittings)	15%
3	Machinery and Plant (not otherwise specified)	15%
4	Technical or professional books	15%
5	Motor vehicles (all types)	15%
6	Ships	15%
7	Computer hardware, including printer, monitor, allied items and machinery and equipment used in manufacture of I.T. products	30%

8	Aircrafts, aero-engines and aerial photographic apparatus	30%
9	Offshore platforms and production installations in mineral oil and concerns	20%
10	A ramp built to provide access to persons with disabilities not exceeding Rs. 250,000 each	100%

Initial Allowance for Depreciation [23 & Part I of Third Schedule]

In addition to a **normal depreciation allowance**, an **additional depreciation allowance** (*termed as initial allowance*) shall be **allowable** as a **deduction against the "Income from Business"**. The following conditions apply to the **initial allowance**:

1. The **initial allowance** is allowable on **"eligible depreciable assets"** only.
2. The **asset** should be **newly constructed, erected, or installed** (*i.e., it is placed into service in Pakistan for the first time in a tax year*).
3. The **initial allowance** shall be **admissible** in **respect of the later of** the **tax year** in which the **asset is used for the first time in Pakistan** or the **tax year in which commercial production is commenced**.
4. The **allowance** shall be **allowed @ 25% of the cost of the plant and machinery** as determined under the **Income Tax Ordinance, 2001**.
5. In case of a **leasing company**, the **deduction on account of initial allowance** in respect of **assets leased** by it shall be **restricted up to lease rental income** for the **tax year only**. **Any unabsorbed depreciation** may be **carried forward for deduction in coming years**. **Leasing Company** means **any leasing company, investment bank, modaraba, scheduled bank or development financial institution** that has **leased its assets to another person**.

Accelerated Depreciation to Alternate Energy Projects

(*23B & Part-I of Third Schedule*)

An **"accelerated depreciation"** shall be **allowed** in **respect of plant, machinery, and equipment** if the **following conditions** are satisfied:

1. It shall be **allowed in respect of plant, machinery, and equipment installed for generation of alternate energy**.
2. The **plant, etc., is installed by an industrial undertaking**.
3. The **industrial undertaking should be set up anywhere in Pakistan** and **owned and managed by a company**.

Income Tax – Assets & Depreciation

Accelerated Depreciation Allowance

1. **Accelerated depreciation** shall be **admissible** in respect of the **'eligible depreciable asset'** put to use **after July 01, 2009**.

2. The **rate of accelerated depreciation** shall be **90% of the cost of the asset**.
3. Other provisions of the **'Initial Allowance'** shall **mutatis mutandis apply** to this allowance.

Note:

"Where in respect of an eligible depreciable asset any special depreciation is admissible u/s 23, 23B (i.e., initial allowance), then only one of these allowances shall be allowed in respect of that asset."

Asset Leased by a Leasing Company, Bank, etc. [22(1)(2) & (13)(c)]

An asset leased by **any of the following institutions** shall be **treated as used by it** for its **own business**:

1. Leasing company
2. Investment bank
3. Modaraba
4. Scheduled bank
5. Development financial institution

Depreciation on an asset given on lease shall be allowed to the lessor on such an asset.

Limit on Depreciation [22(1)]

The **amount of depreciation** allowed to above-mentioned institutions **against assets given on lease** shall **not exceed** the **lease rental income** derived in respect of such assets during the tax year.

Example: 10.13

A **leasing company** leased out a **plant** costing **Rs. 1,000,000** in the **tax year 20x1**. The **annual lease rentals** were agreed at **Rs. 240,000**, **spread over five (5) years**. Compute the amount of **depreciation** to be allowed over the **tax years 20x1, 20x2, 20x3, 20x4, and 20x5**.

Answer: Depreciation Schedule

Tax Year	Unabsorbed Depreciation B/F	Depreciation for the Year	Total Depreciation	Lease Rentals	Admissible Depreciation	Unabsorbed Depreciation C/F

20x1	-	362,500	362,500	240,000	240,000	122,500
20x2	122,500	95,625	218,125	240,000	218,125	-
20x3	-	81,821	81,821	240,000	81,821	-
20x4	-	69,089	69,089	240,000	69,089	-
20x5	-	58,726	58,726	240,000	58,726	-

Computation of Depreciation for the Tax Year

1. **20x1:**
   - **Initial Depreciation = (1,000,000 × 25%) = 250,000**
   - **Normal Depreciation = (1,000,000 – 250,000) × 15% = 112,500**
   - **Total Depreciation = 362,500**
2. **20x2:**
   - **WDV × Depreciation Rate = (1,000,000 – 362,500) × 15% = 95,625**
3. **20x3:**

- **WDV × Depreciation Rate** = **(1,000,000 – 458,125) × 15%** = **81,821**

4. **20x4:**
    - **WDV × Depreciation Rate** = **(1,000,000 – 539,946) × 15%** = **69,089**
5. **20x5:**
    - **WDV × Depreciation Rate** = **(1,000,000 – 608,495) × 15%** = **58,726**

Asset Owned by Islamic Financial Institution [22(15)]

It shall be **treated** that a **depreciable asset is wholly owned by a taxpayer** if the **following conditions** are satisfied:

(*Note: Further explanation/details might be in the next page.*)

Income Tax – Assets & Depreciation

Asset Owned by Islamic Financial Institution [22(15)]

1. The asset is **jointly owned** by the **taxpayer** and an **Islamic financial institution**.
2. The institution is **licensed** by the **State Bank of Pakistan** or the **SECP**.
3. The asset is held **pursuant to an arrangement** of **Musharaka financing** or **diminishing Musharaka financing**.

Conditions for Depreciation Allowance [Rule-12]

An **allowance for depreciation** is **conditional** upon the **following information**:

1. The **asset has been used** during the tax year.
2. The particulars **prescribed** in **Rule-12** of the **Income Tax Rules, 2002** and the information/documents required by the Commissioner are **duly furnished**.

Particulars to be Furnished [Rule-12]

The **following particulars** should be furnished to the **tax authorities** in respect of an asset:

1. **Description** of the asset (**depreciable asset or intangible**) for which **depreciation** is claimed.
2. The **part allocable to business**, if the asset has **not been used wholly** for the business.
3. The **date of acquisition**.
4. **WDV** (Written Down Value) of the asset at the **beginning of the tax year**.
5. **Amount of capital expenditure** incurred on:
    - **Additions**
    - **Alteration**
    - **Improvements**
    - **Extensions**
6. **Sale proceeds** of **any asset disposed of** during the tax year.
7. **WDV of the asset disposed** of during the tax year.

Total Value of Each Asset

When depreciation is **allowable**, the **total value of the asset** shall be determined as follows:

Formula:

sql

CopyEdit

WDV at the beginning of the tax year XXX

Add: Capital expenditure during the tax year XXX

Less: Initial depreciation allowed, if any XXX

Total Value XXX

Example: 10.14

A company **purchased a machine** for **Rs. 400,000** on the **first day of the tax year**. Compute the amount to be allowed as **depreciation** on the machine for the **tax year**.

Answer:

Computation	Amount (Rs.)
Cost of the machine	400,000
Initial Depreciation *(as per Third Schedule, 400,000 × 25%)*	100,000
WDV for Normal Depreciation *(400,000 – 100,000)*	300,000
Normal Depreciation *(300,000 × 15%)*	45,000
Total Depreciation for the Year	**145,000**

Prescribed Rate of Depreciation

1. **Initial Depreciation** (also includes **first year allowance & accelerated depreciation**)
2. **Normal Depreciation**

Income Tax – Assets & Depreciation

Depreciation Allowance Considerations

10. **Normal useful life** for each intangible asset.
11. **Amount of depreciation allowable** on account of:

- **Initial depreciation**, **first-year allowance**, or **accelerated depreciation**
- **Normal depreciation**
- **Amortization**

12. **Total depreciation and amortization** allowed for the tax year.
13. **WDV (Written Down Value)** of each **depreciable asset** and the **cost of intangible** at the end of the tax year along with its **remaining normal useful life**.

Particulars for Assets Disposed During the Year

1. **Sale proceeds** of the assets **disposed** during the tax year.
2. **WDV at the beginning** of the tax year of such **disposed assets**.
3. **The excess or deficit** on the **disposal** of assets.

General Provisions

1. The **total amount of depreciation allowance** shall **not exceed** the **original cost of the asset**. In other words, the **maximum depreciation allowable** under the **Income Tax Ordinance** is **restricted** to the **cost of the asset**. **[22(7)]**

Class of Assets	WDV as Per Tax Records (Rs.)
Land	8,000,000
Building	15,000,000
Plant & Machinery	20,000,000
Motor Vehicle	2,500,000
Computers	450,000
Furniture	100,000

2. Where a **taxpayer disposes of an asset** at **any time** during the tax year, **no depreciation allowance** shall be **deductible for the year of disposal**. **[22(8)]**

Gain or Loss on Disposal of Asset [22(8)]

Any **gain or deficit** on the **disposal of an asset** shall **respectively be taken as profit or loss** from the business and **charged to the profit and loss account**.

Example: 10.15

Riaz Limited has the following assets at the **start of the tax year**:

During the tax year, the company disposed of the following assets:

Assets	WDV (Rs.)	Sale Proceeds (Rs.)
Motor Vehicles	100,000	120,000
Computers	75,000	64,000
Furniture	10,000	6,000

The company also purchased the following assets during the tax year:

- **Office Furniture**
- **Computer**

Amount Paid:

- **Office Furniture:** Rs. 20,000
- **Computer:** Rs. 50,000

Income Tax – Assets & Depreciation

Required:

Compute the **amount of depreciation allowance** for the tax year and the **amount of gain or loss** from the disposal of assets.

Depreciation Allowance for the Year

Assets	WDV Beginning (Rs.)	Addition (Rs.)	Deletion (Rs.)	WDV for Depreciation (Rs.)	Rate (%)	Depreciation Allowance (Rs.)

Land	8,000,000	-	-	8,000,000	-	-
Buildings	15,000,000	-	-	15,000,000	10%	1,500,000
Plant & Machinery	20,000,000	-	-	20,000,000	15%	3,000,000
Motor Vehicles	2,500,000	-	100,000	2,400,000	15%	360,000
Computers	450,000	50,000	75,000	425,000	30%	127,500
Furniture	100,000	20,000	10,000	110,000	15%	16,500
Total	**46,050,000**	**70,000**	**185,000**	**45,935,000**		**5,004,000**

Gain or Loss on Disposal of Assets

Assets	**Sale Proceeds (Rs.)**	**WDV (Rs.)**	**Gain/(Loss) (Rs.) *(2) - (3)***
Motor Vehicle	120,000	100,000	20,000
Computers	64,000	75,000	(11,000)
Furniture	6,000	10,000	(4,000)
Total	**190,000**	**185,000**	**5,000**

WRITTEN DOWN VALUE (WDV) [22(5)]

The **WDV of the assets** shall be determined in light of the following principles:

Asset Acquired During the Tax Year

Where an **asset is acquired** during the tax year, its **WDV shall be computed** as below:

- **Total cost of the asset** = **XXX**
- **Less: Initial allowance or accelerated depreciation, if any** = **XXX**
- **WDV at the beginning of the tax year** = **XXX**

Example: 10.16

A company **purchased a new machine** on the **first day of the tax year** for **Rs. 100,000**. Compute the **WDV of the asset** at the beginning of the tax year and the **total amount to be allowed as depreciation**.

Solution:

- **Cost of the machine** = Rs. **100,000**
- **Less: Initial Allowance** (**@ 25% of cost**) = Rs. **25,000**
- **WDV at the beginning of tax year** = Rs. **75,000**
- **Less: Depreciation Allowance** (**@ 15% of WDV**) = Rs. **11,250**
- **WDV at the end of tax year** = Rs. **63,750**

Depreciation Allowed for the Year:

- **Initial Allowance** = Rs. **25,000**
- **Normal Depreciation** = Rs. **11,250**
- **Total Depreciation** = Rs. **36,250**

Synopsis of Taxes

Income Tax – Assets & Depreciation

WDV of Any Asset which is Partly Used for Business [22(6)]

Where an asset is partly used for business and partly for another use, the WDV for depreciation purposes shall be computed on the basis that the asset has been solely used for business.

Example: 10.17

Considering the already discussed example under the title **"Asset Partly Used for Business"** (Example 10.11), the **WDV for the second tax year** shall be computed as below:

- **Cost of the building** *(1/4th being used for Business)* = **Rs. 4,000,000**
- **Total Depreciation (@ 10% of WDV) for first year** = **Rs. 400,000**
- **WDV at the end of first year (and at the beginning of the second year)** = **Rs. 3,600,000**
- **Total Depreciation (@ 10% of WDV) for second year** = **Rs. 360,000**
- **WDV at the end of second year** = **Rs. 3,240,000**

Total Depreciation Allowed as Deduction

1. **For first tax year** *(1/4th of Rs. 400,000)* = **Rs. 100,000**
2. **For second tax year** *(1/4th of Rs. 360,000)* = **Rs. 90,000**

Total = **Rs. 190,000**

Depreciation Not Allowed as Deduction

1. **For first tax year** *(Rs. 400,000 - Rs. 100,000)* = **Rs. 300,000**
2. **For second tax year** *(Rs. 360,000 - Rs. 90,000)* = **Rs. 270,000**

   Total = **Rs. 570,000**

   Gain or Loss on Disposal of an Asset which is Partly Used for Business [22(9)]

   The **gain or loss** on disposal of an asset is computed by deducting the **WDV** out of the consideration received against the asset.

   If an asset is **partly used for business**, the **WDV may be computed** in any of the following ways:

1. **Cost of the asset**
   - **Less:** Total depreciation allowed on the asset till its disposal
   - **WDV** = **XXX**

   OR

2. **WDV computed for depreciation purposes**
   - **Add:** Total depreciation not allowed
   - **WDV** = **XXX**

Example: 10.18

Assume that the **building discussed in Example 10.17 is disposed of during the third year** for **Rs. 3,900,000**. The **gain or loss on its disposal** shall be computed as below:

- **Disposal Consideration** = **Rs. 3,900,000**
- **Less:** WDV at the time of disposal **(4,000,000 - 190,000)** OR **(3,240,000 + 570,000)** = **Rs. 3,810,000**
- **Gain on disposal** = **Rs. 90,000**

Asset Acquired Prior to the Tax Year

Where an **asset was acquired at any time before the tax year**, the **WDV shall be determined** as follows:

1. **Actual cost of the asset at the time of acquisition** = **XXX**
2. **Less:** Total depreciation **(normal and special allowance)** before the tax year = **XXX**
3. **WDV at the beginning of the tax year** = **XXX**

Income Tax – Assets & Depreciation

EXCEPTIONS REGARDING COST INCURRED AND CONSIDERATION RECEIVED [22(11) & (13)]

While determining the **cost of acquisition** of an asset, **amount of depreciation, disposal consideration, and gain or loss on disposal** of an asset, the rules discussed in earlier paragraphs of the chapter are generally applicable. These rules are contained in **Part-III of Chapter-IV** *(i.e., sections 75 to 79)* of the **Income Tax Ordinance**.

However, under certain cases, these general principles are **not applicable**, which are:

1. Passenger transport vehicle not plying for hire.
2. Assets given on lease by a leasing company, etc.

3. Disposal of immovable property.
4. Export of depreciable asset.

Provisions regarding all the above cases are separately discussed in this chapter at their appropriate places.

Passenger Transport Vehicle Not Plying for Hire [22(13)(a)]

Cost of the Vehicle [22(13)(a)]

The cost of such a vehicle shall be the **lesser of the actual cost of the vehicle or Rs. 7,500,000**. In other words, the **maximum cost for depreciation purposes shall be Rs. 7,500,000** if the vehicle is purchased at a price higher than this amount.

Example: 10.19

Ms. Sarfraz Limited is a **manufacturing company**. It purchased a **bus worth Rs. 7,850,000** at the **start of the tax year** and **expended Rs. 150,000** on its **registration, etc.** The bus is used for the **transportation of the employees** of the company. **Compute the depreciation** to be allowed as a **deduction while computing the income** of the company.

Answer:

- **Total Actual Cost** *(Rs. 7,850,000 + Rs. 150,000)* = **Rs. 8,000,000**
- **Cost of the bus for depreciation purposes** = **Rs. 7,500,000**
- **Depreciation** *(Rs. 7,500,000 @ 15%)* = **Rs. 1,125,000**

For gain or loss on disposal of a passenger transport vehicle not plying for hire, the "Consideration Received on Disposal" shall be computed according to the following formula:

A×BC\frac{A \times B}{C}CA×B

Where:

- **A** = Amount received on disposal of vehicle
- **B** = Cost determined for depreciation purposes *(i.e., lesser of actual cost of vehicle or Rs. 7,500,000)*
- **C** = Actual cost of acquiring the vehicle

Example: 10.20

Ms. Sarfraz Limited **disposes of the bus** in the **next tax year** against **Rs. 8,500,000**. The bus was purchased **at the beginning of the previous tax year** *(as in Example 10.19)* at a cost of **Rs. 8,000,000**. Compute the **gain or loss on disposal** of the bus under the **Income Tax Ordinance**.

Answer:

Amount of Disposal Consideration:

Disposal Consideration : Cost for Depreciation Purpose

Actual Cost of the Bus

(Rs. 8,500,000 x Rs. 7,500,000) ÷ Rs. 8,000,000 = 7,968,750

Less: Written down value at the time of disposal

Cost U/S 22 = 7,500,000

Less: Depreciation as per Third Schedule (7,500,000 x 15%) = **1,125,000**

6,375,000

Gain on disposal of the vehicle = **1,593,750**

COST AND DISPOSAL CONSIDERATION OF IMMOVABLE PROPERTY

Rules regarding cost and disposal consideration of immovable property differ from other assets. Legal provisions are discussed below.

Cost of Immovable Property, etc. [22(13)(b)]

The cost of land shall not be included in the cost of an immovable property or structural improvement to immovable property. Thus, the cost of the land and cost of immovable property on such land shall be shown separately.

Disposal of Immovable Property [22(13)(d)]

Tax treatment of an immovable property differs in each of the following situations:

A) Where consideration is more than the original cost of the asset; and

B) Where the consideration received is less than the original cost of the asset.

Provisions of the Income Tax Ordinance dealing with the tax treatment under both cases are discussed below.

(A) Consideration more than the Original Cost

Any consideration received on disposal of an immovable property shall be treated as cost of the property if the consideration exceeds the original cost of the asset. Under such a case, the total amount allowed as deduction on account of depreciation allowance (accumulated depreciation) on such asset shall become the gain on disposal of the asset.

Example: 10.21

An office building costing Rs. 1,000,000 has been disposed of by a company. The written down value at the time of disposal is Rs. 750,000. Compute the gain or loss on disposal if the property is disposed of for Rs. 1,200,000.

Answer:

Gain on Disposal of Building

Consideration received on disposal = **1,200,000**

Less: Written down value:

Cost of the asset [N-1] = **1,200,000**

Less: Accumulated depreciation [N-2] = **(250,000)**

Gain on disposal of asset = **950,000**

N-1: The disposal consideration is treated as cost of the immovable property if the consideration received is more than the original cost of the asset.

N-2 Accumulated depreciation charged to the business till disposal is as below:

- **Original cost of the building**: Rs. 1,000,000
- **Less: Written Down Value**: Rs. 750,000
- **Accumulated depreciation**: Rs. 250,000

(B) Consideration less than the Original Cost

Section 22(13)(g) lays down the provisions regarding such an immovable property which is disposed of at a consideration which is more than the original cost of the asset. The law does not provide any special treatment for an immovable asset whose disposal consideration is less than the original cost. Under such a case, the general provisions of the law shall be applied. Thus, where an immovable property is disposed of at consideration which is less than the cost of the asset, then the gain or loss on its disposal shall be accounted for as per normal procedure.

Example: 10.22

A building with a written-down value of Rs. 1,000,000 has been disposed of during the tax year. The building cost was Rs. 1,500,000. Compute the gain or loss on its disposal if the sale consideration is:

1. Rs. 1,250,000; or
2. Rs. 900,000.

Answer:

Gain or loss on disposal

	Disposal Consideration
Disposal Consideration	Rs. 1,250,000
Less: WDV	Rs. 1,000,000
Gain/(loss) on disposal	Rs. 250,000

EXPORT OF A DEPRECIABLE ASSET [22(14)]

The cost of the asset shall be treated as the consideration received on disposal of an asset if:

1. It is a depreciable asset;
2. It has been used in Pakistan by the person; and
3. It is exported or transferred by the person out of Pakistan.

Note: Under this case, there will always be a gain on the disposal of the asset. The gain will be equal to the accumulated depreciation charged to the accounts.

AMORTIZATION OF INTANGIBLES [24]

An intangible is an asset that has no physical form. Examples of such assets are patents, copyrights, goodwill, design, model, secret formula, or process, etc. The law allows a deduction on account of amortization of such assets. The legal provisions in this regard are summarized below:

1. A deduction on account of amortization shall be allowed if the following conditions are satisfied: [24(1)]

   i) The asset is wholly or partly used for the purpose of business, the income of which is chargeable to tax; and

   (ii)

   The intangible has a normal useful life of more than one year.

   (2)

   The amortization shall be allowed only if, at the time of computing the income of the person, the total cost of the intangible has not been claimed and allowed as a deduction under any other provision of the Income Tax Ordinance. [24(2)].

   (3)

   The amortization deduction shall be allowed for each tax year. The amount is computed as below:

   Total cost of the assetNormal useful life of the asset\frac{\text{Total cost of the asset}}{\text{Normal useful life of the
   asset}}Normal useful life of the assetTotal cost of the asset

   In other words, the deduction shall be allowed during the normal useful life of the asset on a straight-line method. [24(3)].

   (4)

   An intangible that does not have an ascertainable useful life shall be treated as if it had a normal useful life of twenty-five (25) years. [24(4)].

   (5)

   A fair proportional part of the amortized amount shall be allowed as a deduction if, during the tax year, the intangible is partly used for business chargeable to tax. [24(5)].

   (6)

   Where such an asset is not used for the whole of the tax year, then the amount of deduction shall be computed as below: [24(6)]

   Total Amortization Amount×No. of days the intangible is used for businessNo. of days in t
   ax year\text{Total Amortization Amount} \times \frac{\text{No. of days the intangible is used for business}}{\text{No. of days in tax
   year}}Total Amortization Amount×No. of days in tax yearNo. of days the intangible is use
   d for business

   Note: It shall be treated that an intangible has been used on the day (including a non-working day) on which it is available for use. [24(10)]

   (7)

   The amortization amount, in any case, cannot exceed the total cost of the intangible. [24(7)]

   (8)

In the year of disposal, no amortization deduction shall be allowed. [24(8)]

(9)

Any gain or loss on disposal of an intangible shall be treated as income or deduction under the head "Income from Business." [24(8)]

(10)

In order to calculate the gain or loss on disposal of an intangible, the WDV shall be computed as below: [24(9)]

(i) Where Intangible is Wholly Used for Business

- **Cost**: XXX
- **Less: Total amortization allowed till disposal**: XXX
- **WDV**: XXX

(ii) Where Intangible is Partly Used for Business

- **Cost**: XXX
- **Less: Total amortization that would have been allowed, if the intangible were wholly used for business**: XXX
- **WDV**: XXX

It is to be noted that the WDV under both cases (i.e., wholly used for business or partly used for business) will not change in case of an intangible.

(11) Cost of an Intangible

Cost of an intangible means any expenditure incurred by a person for:

i) Acquiring or creating the intangible;

ii) Improving the intangible; or

iii) Renewing the intangible.

AMORTIZATION OF PRE-COMMENCEMENT EXPENDITURES [25]

A person shall be allowed a deduction on account of amortization of pre-commencement expenditure @ 20% of the total expenditure. In this regard, the following points should be kept in mind:

1. Pre-commencement expenditures are amortized on a straight-line method.
2. Total amortization shall be restricted up to the actual expenditure.
3. Where the entire amount of pre-commencement expenditure has been allowed as a deduction under any other provision of the law, then the amortization shall not be allowed.

CHAPTER-11

METHOD OF ACCOUNTING & RECORDS

POWER OF BOARD TO PRESCRIBE METHOD, ETC. [32(1) & (2)]

Section 32 of the Income Tax Ordinance deals with the method of accounting to be employed by a business for computing its financial results. This section provides that incomes, profits, and gains shall be computed in accordance with the method of accounting regularly employed by the taxpayer. [32(1)]

Thus, more or less, it is the taxpayer who has to decide whether to adopt the mercantile (accrual) system of accounting or the cash system of accounting. Whichever method has regularly been employed by a taxpayer is acceptable for the computation of taxable income.

Apart from the above-referred general rule, the law specifies that a person shall account for its transactions under the head "Income from Business" as below: [32(2)]

1. In the case of a company, on an **accrual basis**; and
2. In the case of other persons, on **accrual or cash basis**, at the option of the taxpayer.

Note: A salaried taxpayer has to pay tax on his salary income on an actual receipt basis. However, under certain cases, he may opt for the **accrual basis**.

POWER OF BOARD TO PRESCRIBE METHOD, ETC. [32(3)]

In the case of any business or any class of persons, the **Federal Board of Revenue** is empowered to:

1. Require that the accounts shall be maintained in such form and in such manner as prescribed by the Board; and
2. Prescribe the manner in which the payments of business transactions shall be recorded (i.e., on an **accrual basis or on a cash basis**).

CHANGE IN METHOD OF ACCOUNTING [32(4) & (5)]

A person may apply to the concerned **Commissioner** for a change in his method of accounting. This change is possible **only if** the Commissioner is satisfied that the change is necessary in order to clearly reflect the person's **Income from Business**. Where a method of accounting is changed, the person shall ensure that necessary **adjustments** are incorporated so that:

1. No transaction is omitted from the record; and
2. No item is taken into account more than once.

CASH-BASIS ACCOUNTING AND ACCRUAL-BASIS ACCOUNTING [33, 34]

The Income Tax Ordinance 2001 defines the both methods of accounting (i.e., the **Cash-Basis Accounting** and the **Accrual-Basis Accounting**). Coming paragraphs contain the meaning assigned to these terms by the Ordinance.

Cash-Basis Accounting [33]

"**Cash-basis accounting**" means such method under which a person in respect of his **Income from Business** derives income when it is **actually received** and incurs expenditure when it is **actually paid**.

ynopsis of Taxes

Accrual-Basis Accounting [34]

"Accrual-basis accounting" is that method under which a person, in respect of his **"Income from Business"**, derives income when it becomes **due** and incurs expenditure when it becomes **payable**.

Notes:

1. An amount shall be **due** to a person when he **becomes entitled** to receive it. It is immaterial that the amount is payable in **installments** or the time for discharge of the entitlement is postponed. [34(2)]
2. An amount shall be **payable** by a person when all the events that determine the **liability** have occurred, and it is **possible** that the amount of liability can be determined with **reasonable accuracy**. [34(3)]

COST OF STOCK-IN-TRADE [35]

The cost of **stock-in-trade disposed of** during a tax year shall be determined as below:

Opening value of stocksXXXAdd: Cost of the stocks acquired during the yearXXXLess: Closing value of stocks(XXX)Cost of Stock-in-Trade DisposedXXX\begin{aligned} \text{Opening value of stocks} & \quad XXX \\ \text{Add: Cost of the stocks acquired during the year} & \quad XXX \\ \text{Less: Closing value of stocks} & \quad (XXX) \\ \hline \text{Cost of Stock-in-Trade Disposed} & \quad XXX \\
\end{aligned}Opening value of stocksAdd: Cost of the stocks acquired during the yearLess: Closing value of stocksCost of Stock-in-Trade DisposedXXXXXX(XXX)XXX

Notes:

1. Where a person has **commenced the business** during the tax year, the **opening value of stocks** shall be the **fair market value** at the time when the stock-in-trade is ventured into the business. [35(2)(b) & (3)]
2. The **closing value** shall be the **lower** of the **cost** or **net realizable value** of the stock-in-trade on hand at the end of the year. [35(4)]

Computation of Cost [35(5) & (6)]

Cost of stock-in-trade is an **important factor** while determining the **cost of goods sold**. The law specifies that a **taxpayer** may compute the cost of stock-in-trade according to any of the methods **applicable** to him on the basis of the **method of accounting** adopted by him. The methods applicable to **different persons** (based on the method of accounting) are specified in the **table** given below:

S. #	Basis of Accounting	Cost Method
1.	**Cash basis**	Prime cost method or Absorption cost method.
2.	**Accrual basis**	Absorption cost method.
3.	**Where particular items of stock-in-trade are not readily identifiable**	First-in-First-Out (FIFO) method or Average cost method.

Change of Method for Cost Computation [35(6)]

Where a person has **adopted a specific method** for cost computation (i.e., **FIFO method** or **Average Cost Method**), he **may change** the same **only with the approval of the Commissioner**. The **Commissioner** may impose **certain conditions** while allowing the change.

TERMS USED IN COST OF STOCK-IN-TRADE [35(7)]

Certain terms have been used while determining the **cost of stock-in-trade**. Below are the definitions of those terms.

Absorption-Cost Method

It means the generally accepted accounting principle under which the cost of an item of stock-in-trade is the sum of **direct material costs, direct labour costs, and factory overhead costs**.

Average-Cost Method

It means the generally accepted accounting principle under which the **valuation of stock-in-trade** is based on the **weighted average cost of units on hand**.

Direct Labour Costs

It means the **labour costs directly related** to the manufacture or production of stock-in-trade.

Direct Material Costs

It means the **cost of materials** that become an **integral part** of the stock-in-trade manufactured or produced, or which are **consumed** in the manufacturing or production process.

Factory Overhead Costs

It means the **total costs of manufacturing or producing stock-in-trade**, including the **direct material costs** and **direct labour costs**.

First-In-First-Out Method (FIFO)

FIFO method means the generally accepted accounting principle under which the valuation of stock-in-trade is based on the **assumption that stock is sold in the order of its acquisition**.

Prime-Cost Method

It means the generally accepted accounting principle under which the **cost of stock-in-trade** is the **sum of direct material costs, direct labour costs, and variable factory overhead costs**.

Variable Factory Overhead Costs

It means those **factory overhead costs which vary directly** with changes in the **volume of stock-in-trade manufactured or produced**.

INCOME FROM LONG-TERM CONTRACTS [36]

A **'long-term contract'** means a **contract** that is **not completed within the tax year** in which work is commenced. However, if it is **estimated to be completed within six (6) months** of its commencement, then it **will not** be treated as a **long-term contract**.

The contract may be for **manufacture, installation, or construction**. It may also be for the **performance of related services** in relation to manufacture, installation, or construction.

The **income arising out of long-term contracts** shall be **computed on the basis of the 'percentage of completion method'**. Under this method, the **revenues and expenses** of a long-term contract are **recognized with reference to the stage of completion**.

While applying this method, the **percentage of completion** shall be **determined** by **comparing** the total costs **allocated to the contract** and **incurred before the end of the year** with the **estimated total costs** as determined at the **beginning of the contract**.

RECORD TO BE KEPT BY A TAXPAYER [174]

The law requires that a **taxpayer** shall **maintain** such **accounts, documents, and records** in Pakistan as may be **prescribed by the Board**. However, the **Commissioner may authorize a person** to maintain records differently.

A taxpayer is required to keep books of accounts, records, and documents for a period of **six (6) years** after the end of the tax year to which they relate. If any **proceedings** are **pending** before any authority or court, the taxpayer **must maintain** the record till the **final decision** of the proceedings.

However, the **six (6) year limitation** shall **not** apply to records pertaining to **income, assets, expenses, or transactions** specified in **section 111(2)(c) of ITO** (e.g., investment, money, valuable article, or expenditure discovered by CIR and situated or incurred **outside Pakistan** or **concealed** foreign-source income).

Where **without a reasonable cause**, a person **fails to provide documentary evidence** in favor of a **deduction** claimed by him, the **Commissioner** may **disallow** or **reduce** such **deduction**.

The **Commissioner** may require any person to **install and use an Electronic Tax Register** for the purpose of **storing and accessing information** regarding any transaction that has a bearing on the tax liability of such a person. The **type and description** of the **Electronic Tax Register** shall be prescribed by the **Board**.

Notes:

1. **"Deduction"** means **any amount debited** to the trading account, manufacturing account, receipts, and expenses account, or profit and loss account.
2. The **books of accounts** and **other records** may be kept on **electronic media**, provided that the **sanctity and safe-keeping** of the records are ensured. **[Rule-32(1)]**

3. In case of a **company**, the books of accounts and other records shall be maintained **in accordance** with the **International Accounting Standards** as required under the **Companies Act, 2017**. **[Rule-32(2)]**

PLACE WHERE BOOKS ARE TO BE KEPT [Rule-33]

A taxpayer shall keep the books of accounts at a place **specified below**:

S. #	Taxpayer	Place for Keeping Books
1	Person deriving income from business.	Where the taxpayer is carrying on his business.
2	Person having business in more than one place.	At the **principal place of business**. If the business is **spread over different places**, separate books of accounts are maintained in respect of **each place**, at each of such places.
3	Person having income other than business.	Where the taxpayer resides or **such other place** as declared by him.

Note: The place **or places** where books of accounts, etc., are to be kept shall be **clearly stated** in the **tax return form**.

PRESCRIBED BOOKS OF ACCOUNTS

Rule-28 through Rule-33 deal with the **books of accounts, records, and documents** to be maintained by **different classes of taxpayers**. The books **prescribed under the Income Tax Rules, 2002** are the **minimum** level of records to be **maintained by a taxpayer**. **[Rules-28(2)]**

The books prescribed by the Rules do **not** prevent a person deriving **Income from Business** from: **[Rule-28(3)]**

1. Maintaining **additional** books of accounts, etc.;
2. **Adding columns** or particulars in the prescribed forms according to his own requirements; or
3. Maintaining the record, etc., in the **prescribed manner**, keeping in view the **nature of his business**.

Below is the list of certain **books and records** to be maintained by a taxpayer.

GENERAL PROVISIONS [Rule-29]

A person deriving **Income from Business** shall have to **maintain** a proper record in respect of the following:

1. **All amounts received**;
2. **All amounts expended**;
3. **All sales**;

4. **All purchases**;
5. **All assets** of the taxpayer;
6. **All liabilities** of the taxpayer; and
7. In a case where the taxpayer is engaged in **assembly, production, processing, manufacturing, mining, or like activities**, he will have to further maintain **complete information** in respect of **all input costs**.

Notes:

1. The **above-referred prescribed record** is to be **maintained** by **all persons** deriving **Income from Business**.
2. A person who has **computerized his record** may **issue** cash memos/invoices/receipts generated by his **computer system**.
3. The **books, etc.**, required to be maintained shall be **maintained for six (6) years** after the end of the **tax year** to which they relate.
   However, where **any proceeding** under the **Income Tax Ordinance, 2001** is **pending** before any **authority or court**, the record **shall be maintained** till the **final decision** of the proceedings.
   SPECIFIC PROVISIONS [Rule-30]
   Taxpayer with Business Income Up to Rs. 500,000 or a New Taxpayer [Rule-30(1)]
   Where a person's **business income** is **up to Rs. 500,000** or he is a **new taxpayer** having business income, he shall have to **maintain** the following **additional record**:
   i) **Cash memo/invoice/receipt** for each transaction of **sale or receipt**. It should contain the following **information**:

- **Serial number and date**;
  b) Name of the person or of his business, address, NTN or CNIC and Sales Tax Registration Number, if any;
  c) The description, quantity, and value of goods sold or services rendered.
  ii) **Daily record** of receipts, sales, payments, purchases, and expenses.
  iii) **Vouchers** of purchases and expenses.

  Notes:

1. Where each transaction does **not exceed Rs. 100**, **one or more cash memos** per day for all such transactions may be issued.
2. The above **provisions are not applicable to companies**.

   2. Taxpayer with Business Income Exceeding Rs. 500,000 [Rule-30(2)]

Where a person's **business income exceeds Rs. 500,000** or he is a **wholesaler, distributor, dealer, or commission agent**, then he will have to **maintain the following specific records**:

i) Cash memo/invoice/receipt for each transaction of sale or receipt containing the following information:

a) **Serial number and date**;

b) **Name of the taxpayer** or of his **business, address, NTN or CNIC, and Sales Tax Registration Number**, if any;

c) **The description, quantity, and value of goods sold or services rendered**; and

d) **The name and address of the customer**. (*This is applicable only if the person is a wholesaler, distributor, dealer, or commission agent and the transaction exceeds Rs. 10,000*.)

ii) Cash book/bank book or daily record of receipts, sales, payments, purchases, and expenses.

iii) General ledger or annual summary of business transactions under distinctive heads.

iv) Vouchers of purchases and expenses. (*Where a single transaction exceeds Rs. 10,000, it should contain the name and address of the payee*.)

v) Quarterly inventory of stock-in-trade, showing its description, quantity, and value, if a person deals in purchases and sales of goods.

3. Professionals [Rule-30(3)]

Where the taxpayer is a **medical practitioner, legal practitioner, accountant, auditor, architect, engineer, etc.**, then he will have to **maintain the following record**:

i) Patient-slip/invoice/receipt for each transaction or receipt containing the following information:

a) **Serial number and date**;

b) **Name of the taxpayer** or of his **business, address, NTN or CNIC, and Sales Tax Registration Number**, if any;

c) **Details of the goods supplied or services rendered** and **the amount charged**. (*It is to be noted that confidential details are not required.*)

d) **The name and address of the patient or client**. (*This point does not apply to a general medical practitioner.*)

4) Daily appointment and engagement diary in respect of clients or patients. (Not applicable to general medical practitioners).

- Daily record of receipts, sales, payments, purchases, and expenses.
- Vouchers of purchases and expenses.

Manufacturers Having Turnover More Than Rs. 2.5 Million (Rule-30(4))

A manufacturer who has a turnover exceeding Rs. 2.5 million shall have to maintain the following records:

1. Cash memo/invoice/receipt for each transaction containing the following information:
    - a) Serial number and date;
    - b) Name of the taxpayer or of his business, address, NTN or CNIC, and Sales tax registration number, if any;
    - c) Description, quantity, and value of goods sold;
    - d) Name and address of the customer, if a single transaction exceeds Rs. 10,000.
2. Cash book and/or bank book.
3. Sales day book and sales ledger, if applicable.
4. General ledger.
5. Vouchers of purchases and expenses.
6. Stock register, in respect of raw material and finished goods, duly supported by gate record. Further, quarterly inventory of all items of stock-in-trade (including work-in-progress) showing description, quantity, and value.

ELECTRONIC TAX REGISTER (ETR) [Rule-30A]

A person required to use Electronic Tax Register (ETR) shall:

1. Install the electronic tax register (ETR) within seven days of its authentication by the Commissioner holding jurisdiction over such case and obtain a register identification number (RIN) for permanent affixture on the Electronic Tax register;
2. Use the electronic tax register to record only his own sales and ensure that each sale is made through it and print the receipt of each sale containing the information in accordance with sub-rules (3) and (4) of rule 29 and rule 30, and to deliver the original receipt to the purchaser;
3. In case of non-availability for use of the electronic tax register, the sales may be recorded with the use of a substitute electronic tax register, duly authenticated by the Commissioner;
4. Prepare a daily and a monthly Accounting report containing the information as prescribed in Chapter VII of these rules;
5. Ensure that the electronic tax register operates correctly with particular regard to correct programming of the names of goods and services and the correct allocation of their tax rates;
6. Promptly report any malfunctioning of the electronic tax register to the person responsible for its servicing.

vi) On demand by an authorized person, produce the electronic tax register for inspection;

vii) Ensure the inspection of the electronic tax register before the authorized service management after six months;

viii) Keep copies of electronic tax register reports for a period of five years and produce the same for inspection by the Commissioner whenever required;

iv) Safely keep the electronic tax register ledger in the electronic tax register's casing and produce it whenever required by the Commissioner to do so; and

v) Ensure the inspection before further use of an electronic register which has been or is suspected to have been interfered or tampered with.

NON-BUSINESS TAXPAYERS [Rule-31]

All taxpayers (other than deriving income from business) shall have to maintain at least such documents and records as has been specified in the table given below:

S. No.	Source of Income	Documents to be Maintained
1.	Salary	Salary certificate issued by the employer indicating the amount of salary and tax deducted therefor.
2.	Property	i) Rent deed, if executed. ii) Tenancy termination agreement, if any. iii) Receipts of amount received as rent.
3.	Capital gains	Evidence of the following transactions: i) Cost of acquisition; ii) Deduction claimed on account of any other costs; iii) Consideration on disposal.
4.	Dividends	Dividends warrant.
5.	Royalty	Royalty agreement.

6.	Profit on debt	Evidence and details of the debt along with the amount of profit and tax and zakat withheld.
7.	Ground rent or other rental incomes taxable under the head "Income from Other Sources"	Lease agreement and lease termination.
8.	Annuity or pension	Evidence of amount received.
9.	Prizes, etc.	Evidence (i.e., certificate, etc.) of income and tax deduction at source.
10.	Loan, advance, deposit, or gift	Evidence of the mode of receipt of loan, allowance, deposit, or gifts.
11.	Miscellaneous	Evidence of the income and deductions claimed.

RECORD OF BENEFICIAL OWNERS [181E & 2(7A)]

Every company and association of persons shall electronically furnish particulars of its *beneficial owners* in the prescribed form and manner.

A company and an association of persons shall update the particulars of its beneficial owners, if there is any change in such particulars.

Beneficial owner means a natural person who:

1. Ultimately owns or controls an AOP, whether directly or indirectly, at least twenty-five percent (25%) shares or voting rights; or
2. Exercises ultimate effective control, through direct or indirect means, over the AOP including control over the finances or decisions or other affairs of the AOP.

ELECTRONIC RECORD [237A]

FBR may require any person to use its information system and electronic resource, in order to replace or supplement its manual business processes by automated business processes and substitute its paper-based records by electronic records.

Electronic record generated, maintained, issued, served, received, filed, or requisitioned through the electronic resource of the FBR shall by itself sufficiently and conclusively prove its validity, authenticity, and integrity and shall be treated to have been done according to the provisions of the ITO.

In case of an integrated enterprise, no sale shall be made or service shall be rendered without generating prescribed fiscal invoices.

Electronic Record [2(18C)]

"Electronic record" includes the contents of communications, transactions, and procedures under this Ordinance, including attachments, annexes, enclosures, accounts, returns, statements, certificates, applications, forms, receipts, acknowledgements, notices, orders, judgments, approvals, notifications, circulars, rulings, documents, and any other information associated with such communications, transactions, and procedures, created, sent, forwarded, replied to, transmitted, distributed, broadcast, stored, held, copied, downloaded, displayed, viewed, read, or printed, by one or several electronic resources and any other information in electronic form.

Electronic Resource [2(19D)]

"Electronic resource" includes telecommunication systems, transmission devices, electronic video or audio equipment, encoding or decoding equipment, input, output or connecting devices, data processing or storage systems, computer systems, servers, networks and related computer programs, applications and software including databases, data warehouses, and web portals as may be prescribed by the FBR from time to time, for the purpose of creating electronic records.

ONLINE INTEGRATION OF BUSINESSES

INTEGRATED ENTERPRISE [2(30B)]

"Integrated enterprise" means a person integrated with the FBR through approved fiscal electronic device and software, and who fulfills prescribed obligations and requirements for integration.

Rules 33 to 33G deal with the matters connected with "Integrated enterprise". Provisions of those rules are discussed in the coming paragraphs.

APPLICATION [R-33A & The Schedule]

These rules are applicable to all persons specified in the below table. These persons are called as "integrated enterprise" and are required to be online integrated.

S. No.	Description	Exclusion, if any
1.	Restaurants	Where the facility of air-conditioning is not installed.
2.	Hotels, motels, guest houses, marriage halls, marquees, clubs including race clubs	Where the facility of air-conditioning is not installed.
3.	Inter-city travel by road.	Where – i) The taxpayer is

		only providing non-air conditioned travel service; ii) Travel service maintaining a fleet of less than ten vehicles.
4.	Courier services and cargo services.	
5.	Services provided for personal care by beauty parlours, clinics and slimming clinics, massage centres.	Where the facility of air-conditioning is not installed.
6.	All medical service providers including dentists, physiotherapists, plastic surgeons, hair implant surgeons, and veterinary doctors.	Where the fee charges are less than Rs. 500.
7.	Pathological laboratories, medical diagnostic laboratories including X-Rays, CT Scan, M.R. Imaging etc.	
8.	Private hospitals or medical care centres providing medical consultation, hospitalization or other ancillary services.	
9.	Health clubs, gyms, physical fitness centres, swimming pools and multipurpose clubs such as Lahore gymkhana, Islamabad club, Chenab Club, Karachi gymkhana, Royal Palm Lahore, Polo club etc. operated by any civilian/non-civilian administration.	
10.	Photographers, videographers and event managers.	Where the fee charges are less than Rs. 50,000 per event.
11.	Accountants defined as: (a) A Chartered Accountant within the meaning of the Chartered Accountants Ordinance, 1961 (of 1961); or	

(b) A Cost and Management Accountant within the meaning of the Cost and Management Accountants Act, 1966 (XIV of 1966).		
S. No.	**Description**	**Exclusion, if any**
12.	Retailers including manufacturer-cum-retailer, wholesaler-cum-retailer, importer-cum-retailer or such person who combines the activity of retail sale with another business activity.	A retailer who does not fall in any of the following categories, namely: i) A retailer operating as a unit of national or international chain of stores; ii) A retailer operating in an air-conditioned shopping mall, plaza or center, excluding kiosks; iii) A retailer whose cumulative electricity bill during the immediately preceding twelve consecutive months exceeds rupees twelve hundred thousand; iv) A wholesale-cum-retailer, engaged in bulk import and supply of consumer goods on wholesale basis to retailers as well as on retail basis to the general body of consumers; v) A retailer whose shop measures one thousand square feet in area or more.
13.	Foreign Exchange Dealers / Exchange Companies.	

14.	Private schools, colleges, universities, professional institutes/vocational training centers.	Where the fee per child is less than Rs. 1,000 per month.

OBLIGATIONS AND REQUIREMENTS [R-338]

1. **An "integrated enterprise" shall install and integrate FBR's approved fiscal electronic** device and software through a licensed integrator available on its website with complete technical instructions for installation, configuration, and integration.
2. **The person shall notify to FBR (on or after 01-07-2024), through the Computerized** System, all of the establishments from which he intends to carry on business and shall register each point of sale (POS) to activate the integration duly providing the following information:

   i) POS Registration Number (to be provided by the System)
   ii) Name of business
   iii) Branch name
   iv) Branch address
   v) POS identification number
   vi) Registration date; and
   vii) License number of licensed integrator.
3. **No sale or service from the notified establishment shall be rendered without being** recorded by the electronic fiscal device (EFD), which means a system composed of one Sale Data Controller (SDC) and at least one Point of Sale (POS) connected together, that has the following characteristics and requirements:

i) **It can perform the following tasks, i.e.,**

a) Receive, record, analyze, and store fiscal data;
b) Format fiscal data into fiscal invoices or bills;
c) Transmit the fiscal data to the FBR's Computerized System through secure means; and
d) Print invoice or bill.

ii,) **Sales Data Controller (SDC)** is the component of an EFD that:

a) Receives transaction data from a POS component of the EFD;
b) Analyzes the transaction data into fiscal data;
c) Formats the fiscal data as a fiscal invoice or bill, creates the digital signature for the EFD, and records the digital signature on the fiscal invoice or bill;
d) Transmits the fiscal invoice or bill number to the POS;
e) Encrypts and preserves the transaction data and fiscal data in an irrevocable and secure manner;
f) Transmits the fiscal data to the FBR's Computerized System.

iii,) **External SDC (E-SDC)** is hardware set up as a separate component of the EFD used by integrated enterprises.

iv,) **Virtual SDC (V-SDC)** is software attached to the POS system.

v,) An integrated enterprise must integrate each and every POS of the business to any of the SDC.

vi,) **An EFD must comply with the following, namely:**

a) Each POS is accredited;

b) Each POS transmits to the SDC a bill on which is recorded the transaction data specified in sub-rule (6), for each transaction of the business;

c) The SDC receives the transaction data, analyzes the data, verifies calculated taxes to produce fiscal data for the transaction, records the invoice or bill data, and transmits the fiscal invoice or bill number to the POS;

d) POS prints the fiscal invoice or bill with the fiscal invoice or bill number and QR code;

e) The SDC transmits the fiscal data to the FBR's system; and

f) A fiscal invoice or bill is produced for each invoice.

vii,)**The point of sale should have the following functionalities, namely:**

a) Provide mechanism to connect to SDC;

b) Send each invoice or bill to SDC for the issuance of fiscal invoice or bill;

c) Generate the QR Code on the base of fiscal invoice or bill number generated by the SDC and print the QR Code on bill;

d) Must perform closing on the close of day, week, and month.

Send the summary report with the following fields to FBR periodically (daily, weekly or monthly):

A) Total sale; and

B) Total number of invoices or bills for the period.

Every adjustment, modification, or cancellation must be recorded duly maintaining logs for each activity; and

System events need to be recorded.

4. **The invoice or bill for each transaction shall be transmitted to EFD specifying the following particulars:**

i) POS Registration Number;

ii) Unique sequential invoice number;

iii) Date and time of sale invoice or bill;

iv) Name of customer or service recipient, where recorded;

v) Item-wise description of service and price exclusive of sales tax, if any;

vi) Rate for each item, if applicable;

vii) Total amount inclusive of sales tax, if any;

viii) Discount, if any; and

ix) Mode of payment, cash or credit card. In case of credit card, the name of client and other relevant details thereof.

5. **POS shall print a clear and legible invoice or bill for each transaction, a copy of which shall be provided to the customer, containing the following particulars in addition to those as in the preceding sub-rule:**

i) QR Code (Generated based on FBR Fiscal Invoice Number);

ii) FBR Fiscal Invoice Number;

iii) Name of the business;

iv) National tax number; and

v) Name or location of the notified establishment.

6. **The EFDs installed at each notified establishment shall be tamper-proof and all the data recorded thereon shall be backed up at an offline site.**
7. **In case of sale returns or exchange, a proper credit note or supplementary invoice with prescribed particulars shall be issued containing the reference of original invoice and the detail of amount refunded or additionally charged, along with sales tax involved, if any.**
8. **All the transactions made from the notified establishment shall be communicated to the FBR's Computerized System through EFD.**
9. **The SDC shall be capable of generating and sending alert messages resulting from any malpractice or error or any inconsistent action noticed in the system and keeping a log thereof.**
10. **The transactions on each point of sales in the notified establishment shall be recorded** by a CCTV camera and the recording thereof shall be retained for a period of at least three months. Such recordings shall be provided to the Commissioner concerned as and when demanded and for the time as specified.
11. **In case ancillary services or sale of goods are made from the notified establishment, the** transactions thereof shall also be recorded and the invoice or bill issued in the same manner. Such data shall also be communicated to the FBR's Computerized System in the same manner.
12. **The cost for integration, including the cost of equipment and fiscalization, shall be borne** by the taxpayer itself.
13. **The taxpayer shall prominently display at each establishment that the POS or the** establishment is accredited by FBR to issue invoice or bill and that the registration number of each POS is verifiable through the FBR's verification services.

CHAPTER-12
CAPITAL GAINS

Profit and gain arising from the 'disposal' of 'capital assets' is taxable under the head 'Capital Gains' [37(1)].
The term 'Capital Asset' has been defined as follows:

CAPITAL ASSET [2(11) & 37(5)]

Capital asset means property of any kind held by a person excluding the following assets:

1. Any stock-in-trade, consumable stores or raw materials;
2. Any depreciable assets;
3. Any intangible asset on which amortization is allowed u/s 24; and
4. Any movable property held for personal use by the person or his family member dependent upon him. However, the following assets shall be treated as capital assets:
   i) A painting, sculpture, drawing or other work of art;
   ii) Jewelry;
   iii) A rare manuscript, folio or book;
   iv) A postage stamp or first day cover;
   v) A coin or medallion; or
   vi) An antique.

Note: The property may or may not be held for the purpose of business.

Examples of Capital Assets:

1. Modaraba Certificates.
2. Participation Term Certificates.
3. Term Finance Certificates.
4. Musharika Certificates.
5. Shares of companies.
6. PTC vouchers issued by Government of Pakistan.
7. Leasehold rights.
8. Partner's share in an AOP.
9. Immovable property.

COMPUTATION OF CAPITAL GAIN [37(2), (3) & (4)]

'Capital gain' on disposal of a capital asset is determined as below:

Consideration received on disposal of asset: XXX

Less: Cost of the asset: XXX

Gain/(Loss) on disposal of asset: XXX

Notes:

1. As per section 76(2) of the Income Tax Ordinance, the incidental expenditure incurred on the disposal of an asset also forms a part of the cost of the asset. Thus, any expenses on disposal shall also be deducted in order to compute the gain or loss.
2. While determining the cost of capital asset, the following amounts shall not be included: [38(4)]
   - (i) Any expenditure that is or may be deducted under any other head of income; and
   - (ii) Any expenditure that is rendered inadmissible under section 21 of the Income Tax Ordinance.

Example 12.1

Mr. Raza purchased 10,000 shares of ABC Limited (a non-listed company) @ Rs. 15 per share. He incurred Rs. 1,000 on the acquisition/transfer of shares. During the year, he disposed of all of the shares @ Rs. 20 per share and paid Rs. 1,500 as commission to the broker.

Required: Compute the amount of capital gain of Mr. Raza.

Answer:

- **Consideration received** (10,000 × Rs. 20) = Rs. 200,000
- **Less: Cost of Shares**
  - Paid on purchase of shares (10,000 × Rs. 15) = Rs. 150,000
  - Expenses on purchase = Rs. 1,000
  - Expenses on disposal = Rs. 1,500
  - **Total cost** = Rs. 152,500
- **Gain on disposal of shares** = Rs. 47,500

CAPITAL GAIN ON IMMOVABLE PROPERTY

(Section 37(1A) & Division-VIII, Part-I of First Schedule)

The gain on the disposal of immovable property is taxable as a separate block of income. For charging income tax on capital gains, immovable properties are divided into the following three categories:

1. **Open plots**
2. **Constructed properties**
3. **Flats**

Taxing capital gain on immovable property shall be as below:

Tax on Disposal of Properties Acquired on or Before 30-06-2024

The tax liability shall be determined by applying the following tax rates to the capital gain:

S. No	Holding Period	Rate of Tax
		Open Plots
1	Upto one year	15%
2	Exceeds one year but does not exceed two years	12.5%
3	Exceeds two years but does not exceed three years	10%

4	Exceeds three years but does not exceed four years	7.5%
5	Exceeds four years but does not exceed five years	5%
6	Exceeds five years but does not exceed six years	2.5%
7	Exceeds six years	0%

2. Tax on Disposal of Property Acquired on or After 01-07-2024

- **Persons in ATL on Date of Acquisition and Date of Disposal: 15%**
- **Persons Not in ATL on Date of Acquisition and Date of Disposal:**
  - Tax rate applicable to Individuals, AOPs, and Companies on taxable income under NTR shall apply.
  - Although normal tax rate shall apply to capital gains but in case of Individuals and AOPs tax rate shall not be less than 15%.

Capital Gain [37(2)]

Capital gain on immovable property shall be determined as below:

- **Disposal consideration** .... **XXX**
- **Less: Cost of acquisition** .... **XXX**
- **Gain / (Loss) on disposal** .... **XXX**

FMV and Disposal Consideration [37(2) & 68(6)(i)]

While computing capital gain on disposal of an immovable property it shall be considered that disposal consideration is not less than the FMV notified by FBR or value fixed by District Officer (Revenue).

Reduction in Tax Liability [Clause (9A), Part-III of Second Schedule]

1. Amount of tax payable on capital gain on disposal of immovable property shall be reduced by **fifty percent (50%)** on the first sale of immovable property acquired or allotted to ex-servicemen and serving personnel of Armed Forces or ex-employees or serving personnel of Federal and Provincial Governments, being original allottees of the immovable property, duly certified by the allotment authority.
2. Amount of tax payable shall be reduced by **seventy-five percent (75%)** for capital gains arising after **completion of three years** from the date of acquisition of immovable property.

Property Allotted to Dependents of Shaheed, etc. [236C(4)]

Gain on disposal of immovable property shall not be taxable under the following cases:

1. The seller is dependent on:
   - **i)** A **shaheed** belonging to **Pakistan Armed Forces**;
   - **ii)** A person who dies while in service of the **Pakistan Armed Forces** or the **Federal and Provincial Governments**; or
2. First sale of immovable property which has acquired or allotted as an original allottee, duly certified by the official allotment authority.

TAX WITHHOLDING ON SHARES OF A COMPANY (Other than Securities) [37(6) to (10)]

The acquirer of shares of any company (other than securities covered under **37A**) is obligated to deduct tax while making payment for shares. Relevant provisions are as below:

1. Tax shall be withheld from the gross amount paid or payable as consideration for the shares.
2. Time for tax withholding shall be earlier of the time of:
    - **i)** Payment for the shares; or
    - **ii)** Registration of shares by the **SECP** or the **SBP**.

1. Tax shall be deducted @ **10% of FMV of shares**. Tax withheld shall be adjustable. *[Provisions of Tenth Schedule do not apply to tax deductible under section 37A.]*
2. Tax deducted shall be paid to **CIR within fifteen (15) days** of the payment for shares.
3. The **FMV shall be determined under 101A of ITO & Rule-19H of ITR**.
4. The person acquiring the shares may apply to CIR for payment without deduction of tax or deduction of tax at a reduced rate. The CIR, after necessary inquiry, may allow accordingly.
5. Following actions may be taken in a case where default is made in deduction or payment of tax on acquisition of shares:
    - **i)** Action under **§ 161 and 162** of ITO may be taken for recovery of tax not deducted or paid;
    - **ii)** Penalty may be imposed under **§ 182** of ITO;
    - **iii)** Prosecution proceedings may be initiated under **§ 191(1)(c)** of ITO for fine or imprisonment; and
    - **iv)** Default surcharge under **§ 205** of ITO may be imposed.
6. The person disposing the shares shall, within **thirty (30) days** of the disposal, furnish to CIR the prescribed information, documents, and statements. The CIR may, by a notice, require such information, etc., within a period of less than 30 days.
7. **SBP shall not allow transfer or registration of repatriable shares** unless tax liability under **§ 37(6) to (10)** is discharged. CIR shall issue a certificate which is to be submitted to SBP by the person selling the shares.

Fair Market Value of Shares [R-19H(2)(c) & (d) & (7)]

Shares are Equity Shares and Not Traded on Stock Exchange

FMV shall be determined as per the following formula:

(A+B+C−D)/E/F(A + B + C - D) / E/F(A+B+C−D)/E/F

Where:

- **A** = Book value of all assets, other than those mentioned in component B.
- **B** = FMV under **§ 68** of ITO in respect of:
    - **(i)** Immovable property; and

    - **(ii)** Assets mentioned in section **38(5)**.
      [These are painting, sculpture, drawing or other work of art, jewellery, rare manuscript, folio or book, postage stamp or first day cover, coin or medallion or an antique.]
- **C** = FMV of shares and securities as computed above.
- **D** = Book value of liabilities shown in the balance sheet excluding contingent liabilities, provisions made for meeting liabilities, paid-up capital regarding equity shares, reserves and surpluses, amount set apart for dividends where such dividends (regarding equity as well as preference shares) have not been declared and required income tax for taxation.
- **E** = For FMV under **§ 37(7)**, value of **'D'** shall be taken as zero.
- **F** = Paid-up value of equity shares.
- **E/F** = Paid-up equity share capital.

Shares Are Not Equity Shares and Not Traded on Stock Exchange:

FMV shall be estimated to be price it would fetch if sold in the open market on the date of transaction. Where CIR is not satisfied with the valuation, he may appoint an expert for valuation u/s 222.

Penalty for Non-Compliance of Income Tax General Order [37(6) & 182(1)-Sr.12A]

Where any person fails to pay tax at the time of making payment as consideration of shares or at the time of registration of shares by the Securities and Exchange Commission of Pakistan or the State Bank of Pakistan, whichever is earlier, the person shall pay penalty equal to 50% of the amount of tax involved.

CAPITAL GAIN ON DISPOSAL OF SECURITIES [37A]

'Securities' is a category of 'capital assets' introduced through the Finance Act, 2010. 'Security' means the following capital assets:-

1. Share of a public company;
2. Voucher of Pakistan Telecommunication Corporation;
3. Modaraba certificate;
4. An instrument of redeemable capital;
5. Debt securities;
6. Unit of exchange traded fund; and
7. Derivative products (e.g., treasury bonds).

Notes:

1. 'Shares of a public company' shall be considered as security if such company is a public company at the time of disposal of such shares.
2. FBR may prescribe rules to carry out purposes of section 37A.

'Debt Securities' means:- [37A(3A)]

1. 'Corporate Debt Securities' such as Term Finance Certificates (TFCs), Sukuk Certificates (Shariah Compliant Bonds), Registered Bonds, Commercial Papers, Participation Term Certificates (PTCs) and all kinds of debt instruments issued by any Pakistani or foreign company or corporation registered in Pakistan; and
2. 'Government Debt Securities' such as Treasury Bills (T-Bills), Federal Investment Bonds (FIBs), Pakistan Investment Bonds (PIBs), Foreign Currency Bonds, Government Papers, Municipal Bonds, Infrastructure Bonds and all kinds of debt instrument issued by Federal Government, Provincial Government, Local Authorities and other statutory bodies.

Note: The 'derivative products' include future commodity contracts entered into by the members of Pakistan Mercantile Exchange whether or not settled by physical delivery. 'Derivatives' is a general term for financial assets that are 'derived' from other financial assets. For example, an option to buy a treasury bond or the option (one financial asset) is derived from the bond (another financial asset). The value of the option depends on the performance of the bond. This can be taken a stage further. For example, the value of an option on a futures contract depends on the performance of the futures contract, which, in turn, will vary with the value of the underlying contract of security. Derivatives exist for assets (like equities or bonds) as well as for interest rates, currency exchange rates and stock market indices. The main advantage of derivatives is that they give investors leverage in the market in which they are trading. This can either enhance their returns or help to hedge risks.

Computation of Capital Gain [37A(1A)]:

Capital gain / (Loss) on disposal of a security shall be computed as below:

Disposal consideration	XXX
Less: Cost of acquisition	XXX
Capital gain / Loss	XXX

Taxation of Gain on Securities [37A (1), (4) & (6) and Division-VII of Part-I of First Schedule]

Tax on Individuals and Association of Persons:

Capital gain arising from disposal of 'securities' shall be treated as a separate block of income under STR. The FBR may prescribe rules for this purpose. The applicable tax rates shall be as below:

1. **Tax on Disposal of Securities Acquired Before 01-07-2013**

Capital gain shall not be taxable.

2. **Tax on Disposal of Securities Acquired between 01-07-2013 & 30-06-2022**

Capital gain shall be taxable @ 12.5%.

3. **Tax on Disposal of Securities Acquired between 01-07-2022 & 30-06-2024**

S. #	Holding Period of Security [Reckoned from the date of acquisition to the date of disposal]	Rate of Tax on Gain
1.	Upto one (1) year	15%

2.	Exceeding one (1) year & up to two (2) years	12.5%
3.	Exceeding two (2) year & up to three (3) years	10%
4.	Exceeding three (3) year & up to four (4) years	7.5%
5.	Exceeding four (4) year & up to five (5) years	5%
6.	Exceeding five (5) year & up to six (6) years	2.5%
7.	Exceeding six (6) years	0%

4. **Tax on Disposal of Securities Acquired on or After 01-07-2024**

Persons in ATL on Date of Acquisition and Date of Disposal: 15% Persons Not in ATL on Date of Acquisition and Date of Disposal:

- Tax rate applicable to Individuals, AOPs and Companies on taxable income under NTR shall apply.
- Although normal tax rate shall apply to capital gains but in case of individuals and AOPs tax rate shall not be less than 15%.

5. **Tax on Gain on Disposal of Future Commodity**

Capital gain on disposal of future commodity shall be taxable @ 5%. It may be acquired between 01-07-2022 & 30-06-2024 or on or after 01-07-2024.

Tax on Companies:

Tax payable by a company on gain on disposal of securities (including debt securities) falls under NTR and shall be charged at the general rates applicable to the companies:

- Small company 20%
- Banking company 39%
- Any other company 29%

Deduction of Capital Gain Tax [Provisos to the Tax Table in Division VII]

On redemption of securities, a mutual fund or a collective investment scheme or a REIT scheme shall deduct Capital Gains Tax at the following rates:

i) Individual & AOP	**15% for stock funds 15% for other funds**
ii) Company	15% for stock funds 25% for other funds

1. In case of a stock fund, if dividend receipts of the fund are less than capital gains, the rate of tax deduction shall be [1] 15%.
2. No capital gain tax shall be deducted, if the holding period of the security acquired on or before 30-06-2024 is more than six (6) years. This shall be applicable only in case of a mutual fund, collective investment scheme or a REIT scheme.
3. Rate for capital gain tax shall base on whether the investor is or is not appearing in ATL at the time of transaction.
4. NCCPL shall adjust the capital gain tax liability based on status of investor is appearing in Active Taxpayers' List at the end of tax year.

Non-Application of Section 37A [Provisos to 37A (1) & Rule 19I]

Capital gain on disposal of 'securities' shall not be taxable u/s 37A (i.e., STR) where disposal is:

1. By a banking company or an insurance company;
2. Of 'shares of a listed company' without involving the stock exchange and not settled through NCCPL; and
3. Through IPO during listing process. However, where detail of such disposal is furnished to NCCPL for computation of capital gains and tax, then it shall be taxable as a separate block of income.

Under Point No. 2 & 3 above:

1. Capital gain shall be taxable u/s 37 of ITO (i.e., NTR);
2. 'Shares of a listed company' do not include units of a mutual fund, collective investment scheme of a REIT scheme or derivative products. Capital gain on disposal of such units, schemes or products shall be taxable u/s 37A of ITO.
3. Transactions of shares of listed companies recorded in the system of NCCPL and reported as per Eighth Schedule shall be taxable u/s 37A of ITO.

Loss on Disposal of Security [37A (5)]

Set-Off of Loss: Loss on disposal of 'securities' shall be set-off only against any taxable gain of the person from disposal of any other 'securities' in the same tax year.

Carry-Forward of Loss:

1. Upto Tax Year 2018: Any unadjusted loss cannot be carried forward to the subsequent tax year.
2. Tax Year 2019 and Onwards: Any unadjusted loss shall be carried forward for adjustment against taxable gain of the person from any other 'securities' during the subsequent tax years. It may be carried forward upto three (3) tax years immediately succeeding the tax year for which the loss was first computed.

CAPITAL GAIN TAX [100B & Eighth Schedule]

Capital gain on listed securities covered u/s 37A (including super tax u/s 4C of ITO) is taxed under separate tax regime (STR). Capital gain and tax on such securities shall be computed, determined, collected and deposited according to the rules specified in the Eighth Schedule.

The above provisions are not applicable to the following persons:

1. A mutual fund;
2. A banking company;
3. A non-banking finance company;
4. An insurance company subject to tax under the Fourth Schedule;
5. A modaraba;
6. Any other person or class of persons notified by the FBR; and

7. A person who intends not to opt for determination any payment of tax under Eighth Schedule. Such a person shall file an irrevocable option to NCCPL after obtaining prior approval from Commissioner. Under such a case exemption from enquiries regarding source of investment shall not apply. [R-5]

'NCCPL' means the National Clearing Company of Pakistan Limited incorporated under the Companies Act, 2017 and licensed as "Clearing House" by the SECP or any subsidiary of NCCPL notified by the FBR for this purpose. [2(35AA)]

'Clearing House' means a clearing house by whatever name or designation established or arranged to be established by a Stock Exchange for the registration of dealing in securities or settlement of trading in future contracts. [Section 2 (f) of the SECP Act, 1997]

RULES FOR COMPUTATION OF CAPITAL GAIN ON LISTED SECURITIES [8th Schedule]

Manner and Basis of Computation of Capital Gain and Tax Thereon [R-1]

1. Capital gain on listed securities shall be computed as per Eighth Schedule and tax on it shall be collected and deposited on behalf of the person earning the income by National Clearing Company of Pakistan Limited (NCCPL) in the manner prescribed in the Income Tax Rules, 2002. For this Purpose the NCCPL shall develop an automated system.
2. Central Depository Company of Pakistan Limited (CDC) shall furnish the required information to NCCPL for discharging it obligations. If the said information is not provided, NCCPL shall forward the details to CIR who shall exercise the powers to enforce furnishing the information, etc.
3. The Asset Management Companies, Pakistan Mercantile Exchange and any other person shall furnish the information when required by NCCPL for discharging its obligations.
4. Capital gain on disposal of units of open end mutual funds and gain or loss on trading of future commodities contracts on Pakistan Mercantile Exchange shall be determined as per Eighth Schedule and tax thereon be collected and deposited on behalf of taxpayer by NCCPL.
5. NCCPL shall issue an annual certificate to the taxpayer of taxable capital gain for the financial year. A certificate for a shorter period may be issued by NCCPL as requested by the taxpayer or required by the Commissioner. This certificate shall be considered as conclusive evidence in respect of such income and shall be filed by the taxpayer along with his return of income.
6. Within forty-five (45) days of the end of each quarter the NCCPL shall furnish to the FBR a prescribed statement of capital gain in that quarter and tax computed on such income. Tax shall be computed by applying the rates specified in Division-VII, Part-I of First Schedule.
7. The 'Super Tax' u/s 4B shall also apply to the taxpayer subject to tax under Eighth Schedule. Super Tax shall be charged at the rates specified in Division-IIA of Part-I of the First Schedule.

Sources of Investment [R-2]

Being redundant now, the provisions of this rule are not being discussed.

Non-applicability of Certain Provisions of Income Tax Ordinance, 2001 [R-3]

Respective provisions for collection and recovery of tax, advance tax and deduction of tax at source laid down u/s 137 through 158 of the Income Tax Ordinance, 2001 shall not apply on the capital gains subject to tax under Eighth Schedule. There is only one exception, i.e., the NCCPL may refer to the FBR a particular case for recovery of tax where it is unable to recover the amount of tax. Under such a case the provisions relating to recovery of tax shall apply.

Payment of Tax Collected by NCCPL [R-4]

The amount collected by NCCPL under the Eighth Schedule shall be deposited in a separate bank account maintained in National Bank of Pakistan. This amount (along with interest accrued thereon) shall be paid to the FBR on yearly basis by 31st day of July next following the financial year in which collection was made.

Computation, Collection and Payment of Tax u/s 4C [R-4A]

In addition to capital gains tax, NCCPL shall also compute and collect tax under section 4C at applicable tax rates on the amount of capital gains computed under Eighth Schedule.

Responsibility and Obligation of NCCPL [R-6]

1. An authorized authority shall conduct regular system and procedural audits of NCCPL on quarterly basis to verify the implementation of applicable rules. The authorities entitled to conduct such audit may be:

   i) Pakistan Revenue Automation Limited (PRAL);

   ii) A company incorporated under the Companies Act, 2017;

   iii) Any other company or firm approved by the FBR; and

   iv) Any authority appointed u/s 209 of the Income Tax Ordinance, 2001, not below the level of an Additional Commissioner Inland Revenue.

2. The recommendations of audit report as approved by the Commissioner shall be implemented by NCCPL, who shall also make necessary adjustments for short or excessive deductions of tax. Under this case no penal action shall be taken against NCCPL on account of any error, omission or mistake that has occurred from application of the system.
3. NCCPL shall refer a particular case to the FBR for recovery of tax if it is unable to recover the amount of tax.

For detailed rules in this regard the reader is advised to refer to Rules 13A through 13P of the Income Tax Rules, 2002.

TREATMENT OF CAPITAL LOSSES [38]

While computing the income chargeable to tax under the head "Capital Gains", any losses on disposal of capital asset (taxable under NTR) shall be dealt with as below.

1. Any capital loss shall be deducted from capital gain on disposal of any other capital asset. [38(1)]
2. Where a gain on disposal of a capital asset is not chargeable to tax, the loss in respect of such asset cannot be deducted while computing income under the head "Capital Gain". [38(2)]
3. Loss on disposal of capital asset is computed by deducting the consideration received on disposal out of the cost of the asset. [38(3)]
4. Any loss on disposal of the following assets is not recognized under the Income Tax Ordinance, 2001: [38(5)] i) A painting, sculpture, drawing or other work of art; ii) Jewelry; iii) A rare manuscript, folio or book; iv) A postage stamp or first day cover; v) A coin; vi) A Medallion; and vii) An antique.

Notes:

1. Non-recognition of a loss means that such a loss cannot be set-off or carried forward against other incomes.
2. Section 38(5) prohibits the recognition of certain capital losses. However, it is silent about the gains in respect of above-referred assets. It means any such gain will be recognized and chargeable to tax.
3. Loss on disposal of a 'security' shall not be covered under this section (i.e., section 38), rather, shall be treated as discussed under section 37A.

COST OF ACQUISITION [Rule-13K(d)]

'Cost of Acquisition' of any security means the market price of the security which the investor pays or would have paid to purchase such security. Besides this general rule, the following principles shall apply while the cost of securities acquired:

S. #	Transaction	Cost of Acquisition
1.	Purchase of shares	The market price of the security paid by the investor.
2.	Right shares	Discounted price at which the right shares are issued. It also includes cost of acquisition of letter of rights (LoR).
3.	Acquisition through bequest or inheritance	Market price of the security at which the deceased person paid or would have paid to purchase such security.
4.	Bonus shares	Market price of bonus shares immediately following the bonus issue which the investor would have paid to purchase such shares. Section 236Z renders total value of bonus shares as income and subject to tax withholding @ 10% as final tax on issue of bonus shares.

		In that case cost of acquisition shall be the value taken for tax withholding u/s 236Z and not zero.
5.	Initial public offering	Actual price paid to the issuer

EXEMPTION OF CAPITAL GAINS

Refer to Chapter "Exemptions and Concessions"

CHAPTER-13

INCOME FROM OTHER SOURCES

SCOPE OF OTHER INCOMES [39]

Any income, which is chargeable to tax under any of the provisions of the Income Tax Ordinance and is not included under any other heads of income, [i.e., salary, income from property, income from business and capital gains] shall be taxed under the head "Income from Other Sources". [39(1)]

The following incomes shall be chargeable to tax under this head:

1. **Dividend. [N-1]**
2. **Royalty.**
3. **Profit on debt. [N-2]**
4. **Additional payment received by a taxpayer on delayed refund under any tax law.**

5. **Ground rent. [N-3]**
6. **Rent from sub-lease of a property, land or building by the tenant (lessee).**
7. **Income from hire of machinery, plant or furniture together with the building in which it is installed.**
8. **Income from provision of amenities, utilities or any other service connected with renting of building.**
9. **Any annuity or pension. [1] It is to be noted that pension and annuity are already chargeable to tax under the head "salary" vide section 12(2)(f), so it cannot be taxed under this head. However, if the relationship between the recipient and payer is not of employee and employer then it may be taxed under "Income from Other Sources".**
10. **Any prize-on-prize bond, raffle, lottery or cross-word puzzle, prize on winning a quiz and prize offered by companies for sales promotion. [N-4]**
11. **Amount of any unexplained income, investment or expenditure treated as income u/s 111 (for further details, see the heading "un-explained income or assets" included in this Chapter).**
12. **Any consideration received for the provision, use or exploration of property.**
13. **Any consideration received against the grant of a right to explore for, or exploit, natural resources.**
14. **Income of a shareholder arising from issuance of bonus shares by a company. [N-5]**
15. **Fair market value of any benefit received in connection with the provision, use or exploitation of property.**
16. **Any amount received by the tenant as consideration for vacating the possession of a building less the amount paid by him at the time of acquiring possession of such building.**
17. **This excess amount received shall be charged to tax on equal basis in ten (10) years starting from the year in which it is received. [39(2)]**
18. **Any amount received by a person from Approved Income Payment Plan or Approved Annuity Plan under Voluntary Pension System Rules, 2005. [1]**
19. **Any amount or fair market value of any property received without consideration or received as gift other than from a 'relative' as defined in section 85(5) of the Income Tax Ordinance, 2001.**
20. **Any amount of loan, advance, deposit for issuance of shares or gift received from another person (other than a banking company or financial institution). However, it shall not be treated as income if:**

i) The payer is a person who holds a National Tax Number and the amount is received through a crossed cheque or through a normal banking channel. [39(3)]; or

ii) The amount is received as an advance for the sale of goods or supply of services. [39(4)]

Notes:

N-1 In case of dividend it is to be noted that as per section 8 it shall be taxed as a separate block of income. Practically, the companies are bound to deduct tax at source at the time of distribution of dividend. The tax deducted at source is considered as full and final discharge of tax liability in respect of the dividend income. Thus dividend income shall not be included in the taxable income under NTR; rather, shall be shown as a footnote. [39(5)]

N-2 Profit on debt may be treated as 'income from business' or 'income from other sources'. Where the prime business of a person is to earn profit on debt (e.g., banks, financial institutions, leasing companies, etc.), then it will be 'income from Business'. Under other cases it will be 'income from Other Sources'.

N-3 In order to understand the taxability of 'ground rent' the following provisions of the Income Tax Ordinance need combined study:

1. **Section 15(2): Definition of 'rent'; which means "any amount received or receivable by the owner of land or building as consideration for its use or occupation......".**
2. **Section 15(1): Charging provision of rent; which specifies that 'rent' is chargeable to tax as "Income from Property".**
3. **Section 39(1)(d): Which lays down that 'ground rent' is chargeable to tax as "Income from Other Sources".**
4. **Section 39(1): Only such incomes are chargeable as 'income from other sources' as are not chargeable under any other head of income.**

Perusal of above provisions reveals that 'ground rent' is now part of the definition of 'rent'; hence, shall be taxable as 'income from property' and not as 'income from other sources'.

N-4 These incomes are covered under FTR. Tax deducted at source shall be final discharge of tax on such incomes; hence, will not fall under this head.

N-5 It falls under FTR; hence, cannot be taxed as IFOS. [236Z]

N-6 Following incomes shall not be taxable as 'income from Other Sources': [39(5)]

(i) Dividend u/s 5;

(ii) Return on investment on sukuks u/s 5AA;

(iii) Royalty, fee for money transfer operations, card network services, payment gateway services, interbank financial telecommunication services [1] and fee for technical services to non-resident u/s 6; and

(iv) Shipping and air transport income of a non-resident u/s 7.

PROFIT ON DEBT RECEIVED IN ARREARS [39 (4A) & (4B)]

In case a profit on debt is received in arrears, a person may opt that the amount of profit on debt be taxed at a rate that would have been applicable if the profit had been paid to him in the tax year to which it relates. This option may be exercised if the following conditions are satisfied:

1. **The profit on debt is derived from National Savings Deposit Certificates or Defence Saving Certificates.**
2. **The amount received includes profit chargeable to tax in the tax year preceding the year of receipt.**
3. **As a result of this accumulated receipt a person is chargeable at a higher rate of tax than what would have been applicable if the profit had been paid in the relevant tax year.**

The above option shall be exercised in writing. It shall be furnished to CIR by the due date for furnishing of return of income for the tax year in which amount is received. The CIR may extend the time period for furnishing the option.

AMOUNT RECEIVED FOR VACATING THE POSSESSION OF A PROPERTY

Where a taxpayer receives any amount for vacating the possession of any building, such income less the amount paid by him for taking the possession of that building shall be deemed as his income. This will be charged to tax under the head "Income from Other Sources" in ten (10) years (starting from the year in which it is received) in equal proportion. [39(1)(k) & 39(2)]

Example: 13.1

Amount paid as advance Rs. 80,000 Amount received at the time of vacating the property 120,000 Excess amount received 40,000 Amount to be charged to tax every year [upto (10) years] = 40,000 ÷ 10 4,000

DEDUCTIONS [40]

While computing taxable income under the head "Income from Other Sources", any expenditure (other than a capital expenditure) incurred wholly and exclusively for the purposes of earning such income shall be deducted from the income. These expenditures and allowances may be the followings:

1. Collection and realization charges.
2. Repair and maintenance charges.
3. Insurance charges.
4. Depreciation allowance and initial allowance as per Third Schedule, in case of income from lease of any building together with plant or machinery.
5. Interest on borrowed capital.
6. Zakat paid on profit under the Zakat and Ushr Ordinance, 1980, if the income is profit on debt chargeable to tax under this head (i.e., Income from Other Sources).
7. Any other expenditure incurred for the earning of such income.

Notes:

1. The deductions shall be admissible according to the method of accounting regularly used by the taxpayer while computing his income. Where incomes are recognized on accrual basis the expenses shall also be allowed accordingly.
2. Any expenditure which is deductible in computing the income under any other head of income shall not be allowed as deduction under this head. [40(4)]
3. While determining income under this head, such expenditure that is rendered as inadmissible under section 21 of the Income Tax Ordinance shall not be allowed as deduction under this head. [40(5)]
4. An expenditure shall be treated as "capital expenditure" if it has a normal useful life of more than one year. [40(6)]
5. Any income, which is taxable under the "Final Tax Regime" (FTR) or as a separate block of income, shall not be included in the total income of the taxpayer rather, shall be shown as a footnote to[1] the tax computations.

The amount received under FTR is presumed as income and the amount of tax deducted or collected at source is treated as full and final discharge of the tax liability of the recipient, in respect of such income.

ASSESSMENT OF ROYALTIES OR COPY-RIGHT FEE [89]

Any lump-sum receipt by an author on account of royalties or copy-right fee of a literary or artistic work shall be deemed to be the income of the tax year in which it is received and the two immediately preceding years. This treatment shall be possible only if the author claims that he took more than 24 months to complete this work. Otherwise the income shall be taxed in the year of receipt.

In order to understand the above provision, consider the following example:

Example: 13.2

Mr. Altaf is a non-professional writer. During the tax year 20x3 he received a lump-sum amount of Rs. 600,000 on account of royalty of a book. He claims that he spent 30 months in completing the book.

Compute his tax liability for the tax year 20x3 assuming that:

1. He has no other source of income; and
2. He has rented out certain machinery from which he has a regular annual taxable income of Rs. 1,500,000 every year.

Answer:

1. Tax Liability with No Other Income of the Taxpayer

Under this case the taxpayer may, upon his own discretion, claim that his income be deemed to be the income of the year in which it is received and two preceding years. In this way his tax liability for tax year 20x3 shall be determined as follows:

Total Income received as royalty 600,000

Income for each year (i.e., 20x1, 20x2, 20x3) Rs. 600,000 ÷ 3 200,000

Note: As the income is below the threshold, there shall be no tax liability for any of the **tax years.**

2. Tax Liability with Other Taxable Income

Total amount received as royalty	600,000
Income chargeable to tax year 20x1, 20x2, 20x3	200,000
Taxable Income and Tax Liability for Tax Year 20x3	
Income from hire of machinery	1,500,000
Royalty income	200,000
Taxable Income	1,700,000
Tax Liability for the Year	
Tax on Rs.1,600,000	170,000
Tax on balance of Rs. 100,000 @ 30%	30,000
Total for the current tax year	200,000

Add: Adjustment for previous tax years (100,000 x 2) [N-1] 100,000

Total tax payable 300,000

N-1 Adjustment for previous tax years

Tax on adjusted income (including-royalty)	200,000
Less: Tax already paid for that year [N-2]	150,000
Further tax payable for one year	50,000

Adjustment of tax for two years (Rs. 40,000 x 2) 100,000

N-2 Tax on Rs. 1,500,000:

Tax on Rs. 1,200,000 90,000

Tax on balance of Rs. 300,000 @ 20% 60,000 150,000

N-3 While computing the tax liability of Mr. Altaf, the following assumptions are made:

1. There is no change in the tax-free limit of income; and

2. The rates applicable to the current year are also applicable to previous tax years.

Practically, those rates and exemption limits shall be applied which were actually applicable to the relevant tax years.

UNEXPLAINED INCOMES, EXPENDITURES OR ASSETS [111]

The value of any income, expenditure, investment, article or asset, etc., shall be chargeable to tax under the head "Income from Other Sources" if the following conditions are met:

1. It is any:

i) Amount which is credited in a person's books of account;

ii) Investment made by a person;

iii) Money or valuable article owned by a person; iv) Expenditure incurred by a person; or

v) Concealment of any income or furnishing of inaccurate particulars of income, which includes:

a) the suppression of any production, sales or any amount chargeable to tax; or

b) the suppression of any item of receipt liable to tax in whole or in part;

2. The person offers no explanation about the nature or source of the transaction, concealment of income or furnishing of inaccurate particulars of income or the explanation offered by him is not, in the opinion of the Commissioner, satisfactory; and [111(1)]

3. Where a person claims the 'agricultural income' as his source of investment, expenditure, etc., then it shall be accepted only to the extent of agricultural income worked back on the basis of agricultural income tax paid under the relevant provincial law.

Heads of Income [111 (1) (ii)]

The inadequately explained amount treated as income may be chargeable to tax as below:

Income from Business:

The suppressed amount of production, sales or any amount or any item of receipt liable to tax as business income shall be chargeable to tax under the head "Income from Business".

Income from Other Sources:

All other amount credited, value of the investment, money, value of the article, or amount of expenditure shall be chargeable to tax under the head "Income from Other Sources".

Tax Year for Taxing Such Income [111 (2)]

The amount shall be included in person's income chargeable to tax in the tax year as per the following:

Situation	**Tax Year in which Income is Included**
The amount representing investment, money, valuable article or expenditure is situated or incurred in Pakistan or concealed income is Pakistan-source.	Tax year to which such amount relates.
The investment, money, valuable article or expenditure is discovered by the CIR and is situated or incurred outside Pakistan or concealed Income is foreign-source.	Tax year immediately preceding the tax year in which investment, etc. is discovered by CIR.
The investment, money, valuable article or expenditure is acquired or incurred outside Pakistan in a prior tax year and is liable to be included in the income of tax year 2018 and onwards on the basis of discovery made by the CIR during tax year 2019 and onwards and the explanation given by the person...	Tax year in which, according to explanation of the person, the investment, money, valuable article or expenditure is acquired or incurred outside Pakistan. Under this case the explanation given by...

If a person explains the acquisition of an asset or expenditure from sources relating to the tax year in which such asset was acquired or expenditure was incurred	the person shall not be rejected on the basis that the source does not relate to the tax year in which the amount chargeable to tax is to be included.
The "Year of discovery of foreign assets or expenditure or concealed income" means the year in which the CIR (Chief Income Tax Officer) has issued a notice requiring the person to explain the nature and source of such foreign assets, expenditure, or concealed income.	

Short Declaration of Value [111(3)]

The Commissioner may include the difference in the actual cost and declared cost of any investment, valuable article or expenditure in a case where the declared cost is less than the actual cost. Such amount shall be chargeable to tax under the head "Income from Other Sources" in the tax year to which the investment, valuable article or the expenditure relates.

Notes:

1. Where a Commissioner discovers any non-declaration or short declaration of income, the same shall be charged to tax in the tax year to which it relates. [111(2) & (3)]
2. An unexplained income, expenditure or asset shall not be taxable if the following conditions are satisfied: [111(4)]

i) It is an amount of foreign exchange remitted from outside Pakistan through normal banking channels;

ii) Such amount should not exceed five million rupees in a tax year;

iii) It is encashed into rupees by a scheduled bank; and

iv) The bank has issued a certificate for encashment and the same has been presented to the tax authorities.

Remittance through money service bureaus (MSBs), exchange companies (ECs) or money transfer operators (MTOs) shall be deemed as remittance through normal banking channels.

3. The amount representing the value recorded by the authority registering or attesting the transfer of immovable property shall remain subject to tax under section 111.
4. Where a person has paid the tax on purchase or transfer of immovable property under section 236W of the Income Tax Ordinance, the person shall have a right to incorporate in his books of accounts the amount computed as above in tangible form.
5. While explaining the nature and source of any amount, a person is entitled to take credit of a sum equal to imputable income, if his source of income falls under FTR. [111(4A)]

A taxpayer may claim credit of a sum as in excess of imputable income only if the excess amount is reasonably attributed to the business activities subject to final tax and financial statements and accounts audited by a chartered accountant are furnished.

"Imputable Income" has been defined in relation to an amount which is subject to "final tax" and means the income which would have resulted in the same tax, had this amount not been subject to final tax. [2(28A)]

6. The Board is empowered to make necessary rules regarding valuation, etc., of the assets. [111(5)]
7. There is no need to issue a separate notice if the explanation regarding nature and sources of the following transactions has been confronted to the taxpayer through a notice under section 122(9) of the ITO: [111(5)]
i) Any amount credited in a person's books of account;
ii) Any investment made or ownership of money or valuable article;
iii) Funds from which expenditure was made;
iv) Suppression of any production, sales, or any amount chargeable to tax; or
v) Suppression of any item of receipt liable to tax in whole or in part.
8. A separate notice under section 111 is not required to be issued if the explanation regarding nature and sources of amount credited or the investment of money, valuable article, or the funds from which expenditure was made has been confronted to the taxpayer through a notice under section 122(9) of the Income Tax Ordinance, 2001.
9. While exercising its powers, the Board has included Rule 228 in the Income Tax Rules, 2002. According to this rule, the assets shall be valued as follows:

S. #	Sub-Rule	Type of Asset	Value
1	(1)(a)	Immovable property – FMV is notified by FBR	The fair market value of the area notified by the FBR under S 68(4) shall be the value.
2	(1)(b)	Immovable property – FMV is not notified by FBR	Where the FBR has not notified the fair market value or any area, the value fixed by the District Officer (Revenue) or the provincial or other authorized authority for the purpose of stamp duty shall be treated as fair market value.
3	(1)(c)	Agricultural land	Average sale price of the sales recorded in the revenue record of the estate in which the land is situated for the relevant period or time.
4	(1)(d)	Where sale price is higher than the FMV	Higher of the sale price recorded in the instrument of sale of property or the value determined under S. Nos. 1, 2 and 3 above.
5	(1)(e)	Auctioned property	Higher of the auctioned price or the value determined under S. Nos. 1, 2 and 3 above.
6	(2)(a)	New imported car or jeep	C.I.F. value plus the amount of all charges, duties, taxes, and costs etc., incurred till its registration.
7	(2)(b)	New car or jeep purchased from the manufacturer, assembler or dealer in Pakistan	The price paid by the purchaser including the amount of all charges, duties, taxes and costs etc., till its registration.

8	(2)(c)	Used car or jeep imported into Pakistan.	Import price adopted by the customs authorities for customs duty plus freight, insurance, and all charges, duties, taxes, and costs incurred till its registration.
9	(2)(e)	Used car or jeep locally purchased by the taxpayer.	Original value determined as in the case of S. No. 5, 6, or 7 above, less ten percent (10%) of the original value for every year following the year in which it was imported or purchased from a manufacturer.

Notes:

1. In case of a car or jeep used for the first time in Pakistan (S. No. 6, 7, & 8), the value for each successive year shall be reduced by 10% of the original value. This reduction is to be made up to a maximum of five (5) years. [Rule 228(2)(d)]
2. The value of a car or jeep shall never be determined at an amount less than fifty percent (50%) of the value as determined under S. No. 6, 7, or 8 above or the purchase price, whichever is more. [Rule-228(3)]

EXEMPTION OF PROFIT ON DEBT

Refer to Chapter “Exemptions and Concessions”

CHAPTER - 14
INSURANCE BUSINESS

Section 99 and Fourth Schedule of the Income Tax Ordinance, 2001 specify special provisions relating to the taxation of insurance business. The relevant parts of the Ordinance are reproduced below.

SPECIAL PROVISIONS FOR INSURANCE BUSINESS
[99 & Fourth Schedule]

SEGREGATION OF INCOME FROM BUSINESS

Profits and gains of an insurance company shall be computed separately as income from:

1. Life insurance business; and
2. Income from other insurance business.

LIFE INSURANCE BUSINESS

Income from Life Insurance Business

The profits and gains of a life insurance business shall be the current year's surplus appropriated to profit and loss account prepared under the Insurance Ordinance, 2000, as per advice of the Appointed Actuary, so as to exclude from it any expenditure other than expenditure which is allowed as a deduction in computing profits and gains of a business to the extent of the proportion of surplus not distributed to policy holders.

The profits shall be net of adjustments under sections 22(8), 23(8) and 23(11) of the Insurance Ordinance, 2000.

Computation of Surplus

The following provisions shall apply in computing the surplus for life insurance business:

1. The amounts paid to, or reserved for, or expended on behalf of policy-holders shall be allowed as a deduction.

I) In the first computation of the surplus, no account shall be taken of amounts to the extent to which they are paid out, or in respect of any surplus brought forward from a previous inter-valuation period; and

II) If any amount reserved for policy-holders ceases to be so reserved, and is not paid to, or expended on behalf of policy-holders, the sums previously allowed as a deduction shall be treated as part of the respective statutory fund for the tax year in which the amount ceased to be so reserved.

2. Any amount either written off or reserved in the accounts, or through the actuarial valuation balance sheet to meet depreciation, or loss on the realization of investments shall be allowed as a deduction, and any sums taken credit for in the accounts or actuarial valuation balance sheet on account of appreciation, or gains on the realization, of investments shall be included in the surplus.

If, after consultation with the SECP, it appears to CIR that the rate of profit on debt or other factors employed in determining the liability in respect of outstanding policies is inconsistent with the valuation of investments so as artificially to reduce the surplus, the CIR may make such adjustment to the allowance for depreciation, or in respect of appreciation, of such investment as the CIR thinks reasonable.

3. Profit on debt accrued in the inter-valuation period in respect of any securities of FG which have been issued or declared to be income tax-free shall not be excluded, but shall be exempt from tax.

GENERAL INSURANCE

1. Income from business other than life insurance business shall be profit or loss before tax as per profit and loss account prepared under the Insurance Ordinance, 2000, excluding any surplus appropriation made during the year.

2. The profits and gains of any business of insurance shall be taken to be the balance of the profits disclosed by the annual accounts required under the Insurance Ordinance, 2000, to be furnished to the SECP subject to the following adjustments:

i) Any expenditure or allowance, or any reserve or provision for any expenditure, or the amount of any tax deducted at source from dividends or profit on debt received which is not admissible under the head 'Income from Business' shall be excluded;

ii) Any amount of investment written off shall be allowed as a deduction, but any amount taken to reserve to meet depreciation of investments shall not be allowed as a deduction, and any sums taken credit for in the accounts on account of appreciation of investment shall not be treated as part of the profits and gains, unless these have been crystallized as gains or losses on the realization of investments;

iii) No deduction shall be allowed for any expenditure, allowance, reserve, or provision in excess of the limits laid down in the Insurance Ordinance, 2000, unless the excess is allowed by the SECP and is incurred in deriving income chargeable to tax; and

iv) No deduction shall be allowed for any expenditure incurred on account of insurance premium or reinsurance premium paid to an overseas insurance or re-insurance company or a local agent of an overseas insurance company until tax at the rate of 5% is withheld on the gross amount of insurance or re-insurance premium.

MISCELLANEOUS

1. The above rules sha ll also apply to the assessment of the profits and gains of any business of insurance carried on by a mutual insurance association. Such profits and gains shall be taxable as 'Income from Business'.

2. While computing income of insurance business, capital gains on disposal of shares and dividend of listed companies, PTC vouchers, modaraba certificate or instruments of redeemable capital and derivative products shall be included. These incomes shall be taxable at the rates applicable to companies.

3. Where loss on disposal of securities is sustained in a tax year, the loss shall be set off Only against the gain from any other securities chargeable to tax as in point No. 2 above. Any such unabsorbed loss shall be carried forward to the subsequent tax year.

4. Capital gain on disposal of securities earned by an insurance company shall not be taxable under section 37A. [37A(1)]

5. The CIR is authorized to examine and amend the amount of income as disclosed in the financial statement presented to the SECP with respect to commission paid and claimed for losses.

6. Provisions of the Eighth Schedule regarding computation of capital gains and tax on disposal of listed securities shall not apply to an insurance company. [100B(2)]

SUPER TAX ON HIGH EARNING PERSONS
[4C & Division IIB, Part-I, First Schedule & Rule 6DA of Fourth Schedule]
Super tax is imposed on 'income' of every person for the tax year 2022 and onwards.

[For details, refer to the chapter "Scope of Tax"]

ADDITIONAL TAX
[9D & Rule 6DB of Fourth Schedule]
Additional tax on certain income, profits, and gains u/s 9D shall not apply to insurance companies.

CHAPTER-15
OIL, NATURAL GAS AND OTHER MINERAL DEPOSITS

SCOPE OF THE CHAPTER (Ito & Fifth Schedule)
This chapter deals with the computation of the profits and gains from the business of exploration, extraction, and production of:
1. Petroleum, oil, and natural gas; and
2. Mineral deposits (other than petroleum or natural gas).

Certain Definitions
The ITO and certain other laws referred in the ITO define some terms connected with this topic. For better understanding of the topic, those definitions are reproduced below:
Petroleum:
1. "Petroleum" means crude oil, natural gas, and case-head petroleum spirits as defined in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986, but does not include refined petroleum products.
2. "Petroleum" includes any mineral oil or relative hydrocarbon and natural gas existing in its natural condition in strata, but does not include coal or bituminous shales or other stratified deposits from which oil can be extracted by destructive distillation. [Pakistan Petroleum (Production) Rules, 1949]
3. "Petroleum" means all liquid and gaseous hydrocarbons existing in their natural condition in the strata, as well as all substances, including sulphur, produced in association with such hydrocarbons, but does not include basic sediments and water. [Pakistan Petroleum (Exploration and Production) Rules, 1986]
Casing-Head Petroleum Spirit
• "Casing-head petroleum spirit" means any hydro-carbon obtained from natural gas (before crude oil from which it is derived has been measured for royalty) by separation or by any chemical or physical process. [Pakistan Petroleum (Production) Rules, 1949]
Crude Oil
1. "Crude Oil" means oil in its natural state before the same has been refined or otherwise treated, but excluding water and foreign substances. [Pakistan Petroleum (Production) Rules, 1949]
2. "Crude Oil" means all petroleum other than natural gas, and which at standard atmospheric conditions of pressure and temperature is in a fluid phase, including condensates and distillates. [Pakistan Petroleum (Exploration and Production) Rules, 1986]

Natural Gas

1. **"Natural gas"** means gas obtained from bore-holes and wells and consisting primarily of hydro-carbons. [Pakistan Petroleum (Production) Rules, 1949]
2. **"Natural gas"** means all hydrocarbons which at standard atmospheric conditions of pressure and temperature are in a gaseous phase, including non-hydrocarbon gas which is in association with and produced together with such gaseous hydrocarbons. [Pakistan Petroleum (Exploration and Production) Rules, 1986]

PETROLEUM, OIL AND NATURAL GAS

[1001) (8) & (2) and Part-I of Fifth Schedule]

1. **Profits and gains and tax liability** of the following businesses shall be computed as provided in Part I of the Fifth Schedule:
   i) Exploration and production of petroleum including natural gas and from refineries set up at the Dhodak and Bobi fields;
   ii) Pipeline operations of exploration and production companies; or
   iii) Manufacture and sale of liquefied petroleum gas or compressed natural gas.
2. **Tax under special procedure** (as above) shall not apply to:
   i) Profits and gains attributable to the production of petroleum including natural gas discovered before 24-09-1954;
   ii) Profit and gains derived from Sui Gas Field.

SEPARATE BUSINESS

1. A business of a person shall be treated as a **separate business undertaking** if it is carried on under an "agreement" with FG and consists of or includes:
   i) Exploration or production of petroleum in Pakistan;
   ii) Setting up refineries at Dhodak and Bobi fields;
   iii) Pipeline operations; and
   iv) Manufacture and sale of liquefied petroleum gas or compressed natural gas.
2. **Profits and gains of such undertaking** shall be computed separately from the income, profits or gains from any other business carried on by the person.

"Agreement" means an agreement entered into between the Federal Government and a taxpayer for the exploration and production of petroleum in Pakistan.

COMPUTATION OF PROFITS

1. Profits and gains of the undertaking shall be computed in the like manner as is computed under the head 'Income from Business'.
2. Any expenditure incurred on searching or discovering and testing a petroleum deposit or winning access thereto but the search, exploration, enquiry is given up before the commencement of commercial production, the expenditure allocable to a surrendered area or to the drilling of a dry-hole shall be treated as lost at the time of the surrender of the area or the completion of the dry-hole.

3. Where the expenditure is treated as lost and is allowed as deduction to the undertaking, it shall be allowed in either of the following ways as provided in the agreement:

i) The loss in any tax year shall be set off against any income of the undertaking under any head (other than income from dividends) for that tax year.

Where the loss cannot be wholly set off, it shall be carried forward to the following six (6) years and set off against income under any head (other than income from dividends) for those tax years.

ii) Loss in any year shall be set off against the income of the undertaking of the tax year in which commercial production has commenced.

Where the loss cannot be wholly set off against the income of the undertaking, it shall be carried forward to the following ten (10) years.

'Surrender' means the termination of rights with respect to an area including the expiration of rights according to the terms of an agreement;

'Surrendered area' means an area with respect to which the rights of the person have terminated by surrender or by assignment or by termination of the business;

4. After the commencement of commercial production, all expenditure incurred prior thereto shall be dealt as below:

i) Expenditure treated as lost shall be dealt as discussed above;

ii) Expenditure represented by physical assets in use at the time the commercial production shall be capitalized and depreciated as per normal procedure; and

iii) Any other expenditure shall be allowed as a deduction. However, such deduction in any tax year shall be restricted up to the following:

a) 10% of the aggregate amount deductible in respect of onshore areas; and

b) 25% of the aggregate amount deductible in respect of offshore areas.

5. Any expenditure, including a 'royalty' paid to FG by an onshore petroleum exploration and production undertaking expended after commencement of commercial production wholly and exclusively for its business shall be allowed as a deduction. This deduction is subject to the following conditions:

i) Expenditure incurred in the acquisition of depreciable assets or intangibles shall not be allowed as deduction; rather, depreciation or amortization under sections 22 to 24 shall be admissible in respect of such assets;

ii) Expenditure incurred on acquisition of the physical assets acquired before the commencement of commercial production and were being used by the undertaking on and after that date shall be treated as acquired at the time of the commencement of commercial production.

These shall be taken at their original cost, as reduced by the depreciation deduction, if any, previously allowed to be deducted under the ITO. Depreciation under section 22 shall be allowed on this value.

6. If, in any year, the deductions allowed (under the head 'Income from Business' and point Nos. 3 and 4 above) exceed the gross receipts from the sale of petroleum produced in Pakistan, the loss shall be set off against other income (other than dividends).

Un-adjusted loss shall be carried forward up to six (6) tax years in the manner and subject to the limitations as provided in section 57 of ITO.

However, the limitation of six years shall not apply to depreciation allowed to a person carrying on the business of offshore petroleum exploration and production, in respect of any machinery, plant or other equipment used in such exploration or production. It may be carried forward up to an indefinite period.

7. Where any asset used by a person in the exploration and production of petroleum is exported or transferred out of Pakistan, the person shall be treated as having made a disposal of the asset for a consideration received equal to the cost of the asset as reduced by any depreciation deductions allowed under the ITO (other than an initial allowance under section 23).

'Payments to the Federal Government' means amounts payable to the Federal Government or to any Federal Governmental authority in Pakistan

(a) in respect of royalties as specified in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986; and

(b) in respect of any tax or levy imposed in Pakistan peculiarly applicable to oil production or to extractive industries or any of them and not generally imposed upon all industrial and commercial activities.

'Commercial production' means production as determined by the Federal Government.

DEPLETION ALLOWANCE

While determining income of the undertaking after commencement of commercial production, an allowance for depletion shall be made subject to the following limitations:

1. It shall be 15% of the gross receipts representing the well-head value of the production; and
2. It shall not exceed 50% of the profits or gains of the undertaking before deduction of depletion allowance.

Well-Head Value

1. 'Well-head value' shall have the meaning assigned to it in the agreement between the Federal Government and the taxpayer, and in the absence of any such definition in the agreement, the meaning assigned to it in the Pakistan Petroleum (Production) Rules, 1949, or the Pakistan Petroleum (Exploration and Production) Rules, 1986.

2. 'Well-head value' of crude oil shall be the price of the competitive non-Pakistani crude oil, suitably adjusted to the same gravity and quality at the same destination as the actual ultimate destination of Pakistani crude oil, reduced by costs incurred from the point of production within Pakistan to such destination. [Pakistan Petroleum (Production) Rules, 1949]

3. 'Well-head Value' means the market value of the Petroleum less gathering, processing, treatment and transportation costs from the well-head to the place at which the market value is determined, and in the case of natural gas shall also include compression, dehydration and liquefaction costs. [Pakistan Petroleum (Exploration and Production) Rules, 1986]

LIMITATION ON PAYMENT TO FEDERAL GOVERNMENT AND TAXES

1. The limit of 'taxes on income' and other payments excluding a 'royalty' paid by an onshore petroleum exploration and production undertaking to the Government in respect of its profits or gains shall be governed by the 'agreement'.

2. The aggregate of taxes, etc., on the undertaking shall not exceed the limits provided for in the agreement. However, it shall not be less than the following limits:

Onshore Petroleum Exploration and Production Undertaking:

50% of the profits or gains derived by the undertaking before deduction of payment to FG. From tax year 2003 onwards, it shall not be less than 40% of the profits and gains before deduction of payment (excluding royalty) to FG.

Offshore Petroleum Exploration and Production Undertaking:

40% of the profits or gains derived by the undertaking before deduction of payment to FG. Where in a tax year the aggregate of taxes on income and payments to FG is greater or less than the amount provided for in the agreement, necessary adjustment (as below) shall be made to equal it to the limits provided in the agreement:

3. i) An additional amount of tax shall be payable by the taxpayer, if it is less than the amount as per the agreement; and

ii) An abatement of tax shall be allowed to the taxpayer, if it is greater than the amount as per the agreement.

4. Where in a tax year 'payments to FG' exceed the amount provided for in the agreement, the excess amount shall be carried forward and treated as payments to the Federal Government for the succeeding year. It may be carried forward as below:

i) The whole of the excess amount shall be carried forward if so provided for in an agreement made before 01-07-1970. It may be on account of royalty or any peculiar tax or levy; and

ii) In all other cases, only so much of the excess amount shall be carried forward as relates to any peculiar tax or levy applicable to oil production or to extractive industries only.

'Taxes on income' and 'tax' includes income tax, but does not include payments to the FG.

Option to Pay Tax under Special Regime

An undertaking may opt to pay tax @ 40% of its profits and gains, net of royalty.

This option shall be available if appeals, references and petitions on the issue of tax rate pending before any appellate forum are withdrawn. This option is available only for one time and shall be irrevocable.

Decommissioning Cost

'Decommissioning Cost' is an estimate of costs of dismantling and removing a fixed asset and restoring the site on which it is located.

'Decommissioning Cost' as certified by a Chartered Accountant or a Cost Accountant (as prescribed in Rule 12A of ITR) shall be allowed over a period of ten years or the life of the development and production or mining lease whichever is less, starting from the year of commencement of commercial production.

MINERAL DEPOSITS (OTHER THAN OIL AND NATURAL GAS) [100 (3) & Part - ll of Fifth Schedule]

The profits and gains of any business which consists of, or includes, the exploration and extraction of such mineral deposits of a wasting nature (other than petroleum or natural gas) carried on by a person in Pakistan shall be computed as below.

SEPARATE BUSINESS

1. A business of a person shall be treated as a separate business undertaking if it consists of or includes the exploration or extraction of mineral deposits of a wasting nature (other than petroleum) in Pakistan.

2. Profits and gains of such undertaking shall be computed separately from the income, profits or gains from any other business carried on by the person.

COMPUTATION OF PROFITS

1. Profits and gains of the undertaking shall be computed in the like manner as is computed under the head 'Income from Business'.

2. All expenditure on prospecting and exploration incurred up to the date of commercial production shall be, to the extent to which it cannot be set off against any other income of such undertaking, treated as a 'loss'.

3. The 'loss' shall be carried forward and set off against the income of such undertaking after the commencement of commercial production. If it cannot be wholly set off against the income of such undertaking of the tax year in which the commercial production had commenced, the portion not so set off shall be carried forward up to ten (10) years beginning with the year in which commercial production commenced.

4. After the commencement of commercial production, depreciation in respect of machinery and plant for extracting the ore shall be allowed as a deduction from the profits and gains of the tax year in which they are used for the first time in an amount equal to the original cost of such asset.

DEPLETION ALLOWANCE

1. In determining the profits and gains, depletion allowance shall be made equal to 20% of the taxable income of such undertaking (before the deduction of depletion allowance).

2. Depletion allowance shall be allowed only if an amount equal to the depletion allowance is set apart and left as a reserve to be utilized for the development and expansion of the undertaking.

3. Where a depletion allowance is made in any tax year and subsequently it is utilised for any purpose other than for development and expansion of the undertaking, the amount originally allowed shall be treated as having been wrongly allowed and the Commissioner may recompute the taxable income of the taxpayer for the relevant tax years and make the amended assessment under section 122.

In this case, the period of five years (for amendment in assessment) shall be reckoned from the end of the tax year in which the amount was so utilised.

SUPER TAX ON HIGH EARNING PERSONS [4C & Division IIB, Part-I, First Schedule & Rule 4AB of Fifth Schedule]

Super tax is imposed on 'income' of every person for the tax year 2022 and onwards.

[For details, refer to the chapter "Scope of Tax"]

ADDITIONAL TAX [99D & Rule 4AC of Fifth Schedule]

Additional tax on certain income, profits and gains under section 99D shall not apply to taxpayer deriving income from exploration and production of petroleum and exploration and extraction of mineral deposits.

CHAPTER - 16

BANKING BUSINESS

BANKING COMPANIES

BANKING COMPANY [2 (7) & Banking Companies Ordinance, 1962-5 (b) & (c)]

'Banking company' means any company which transacts the business of banking in Pakistan and includes their branches and subsidiaries functioning outside Pakistan of banking companies incorporated in Pakistan.

It includes any body corporate, which transacts the business of banking in Pakistan.

'Banking' means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft or otherwise.

Any company which is engaged in the manufacture of goods or carries on any trade and which accepts deposits of money from the public merely for the purpose of financing its business shall not be deemed to transact the business of banking.

INCOMES AND TAX LIABILITY OF BANKING COMPANIES [100A & First Schedule] Incomes, Gains and Profits

The income, profits and gains and tax payable by a 'banking company' shall be determined as below: [100A]

1. Incomes and tax liability of a banking company shall be computed in accordance with the rules in the Seventh Schedule.

2. Computation of incomes and tax is subject to the limitations and provisions of Chapters VII and VIII of the ITO (i.e., sections 101 to 112).

Tax Rates

Income Tax [Division - II, Part - I of First Schedule & Rule 6 of Seventh Schedule]

Income of a banking company, computed as per Seventh Schedule, shall be 'Income from Business' and subject to tax @ 39% taxable income.

Super Tax for TDP [4B & Division - IIA of Part - I of First Schedule & Rule 7C of Seventh Schedule]

Super tax for the tax year 2022 under section 4B of the ITO was payable @ 4% on 'income' as defined under section 4B (2) of ITO. While determining income for this purpose, brought forward losses, if any, shall be excluded.

Super Tax on High Earning Persons [4C & Rule 7CA & Division - IIB of Part - I of First Schedule]
Super tax for the tax year 2023 and for all subsequent tax years under section 4C of the ITO shall be payable @ 10% on income as defined under section 4C (2) of ITO.

Tax on Dividend and Capital Gains [Rule 7B]

Income from Dividend and Capital Gains shall be taxable at the normal rate, i.e., @ 39%.

Tax on Additional Advances for Micro, Small and Medium Enterprises [Rule 7D]

Tax for the tax years 2020 to 2023 on taxable income arising from additional advances to micro, small and medium enterprises shall be taxable at 20% instead of the normal rate of 39%.

Tax on Additional Advances for Low Cost Housing [Rule 7E]

1. Tax for the tax years 2020 to 2023 on taxable income arising from additional advances for low-cost housing shall be taxable at 20% instead of the normal rate of 39%.

Taxable income arising from additional advances to Naya Pakistan Housing and Development Authority for low-cost housing schemes shall be taxable at 10%.

2. Tax on Additional Advances as Farm Credit [Rule 7F]

Tax for the tax years 2020 to 2023 on taxable income arising from additional advances as Farm Credit in Pakistan shall be taxable at 20% instead of the normal rate of 39%.

Reduced rate of 20% for income arising from additional advances to micro, small and medium enterprises & for low-cost housing and Farm Credit was valid up to tax year 2023. For tax year 2024 onwards such income shall also be taxable at the normal rate of 39% applicable to banking companies.

ADDITIONAL TAX [99D, Rule 7CB of Seventh Schedule & SRO 1558(I)/2023, dated 21-11-2023]

In addition to any tax charged or chargeable, paid or payable under any provision of ITO, every banking company shall be liable to an additional tax subject to the following conditions:

1. It is imposed for any of the last three tax years preceding the tax year 2023 and onwards and notwithstanding anything contained in any law (including ITO) in force for the time being.

2. The company has any income, profit or gains that have arisen due to any economic factor or factors that resulted in windfall income, profits or gains.

3. FG may, by a notification:

i) Specify sector or sectors subject to additional tax;

ii) Determine windfall income, profits or gains and economic factor or factors including but not limited to international price fluctuation having bearing on any commodity price in Pakistan or any sector of the economy or difference in income, profit or gains on account of foreign currency fluctuation;

iii) Provide the rate not exceeding fifty percent of such income, profits or gains;

iv) Provide for the scope, time and payment of tax payable in specified manner and with applicable conditions; and

v) Exempt any person or classes of persons, any income or classes of income from additional tax with applicable condition, if any.

4. FG has notified the following provisions for levying tax on windfall income, profit and gains:

i) Sector: Banking companies shall be subject to tax under section 99D.
ii) Income Covered: Windfall income from foreign exchange.
iii) Rate of Tax: 40% of the windfall income, profits and gains.
iv) Period Covered: Calendar years (CY) 2021 & 2022.
v) Tax years: 2022 & 2023.
vi) Payment Date: 30-11-2023, extendable by CIR for fifteen days on application by taxpayer.
vii) Mode of Payment: Tax shall be paid in federal treasury through prescribed challan or CPR.
viii) Method for Computing Windfall Income:
Tax Year 2023 (i.e., CY 2021):
Foreign exchange income as per Financial Statements for CY 2021 = XXX
Less: Average of foreign exchange income of last 6 calendar years (2015 to 2020) = XXX
Windfall income for CY 2021 (i.e., tax year 2022) = Taxable @ 40% = XXX

Tax Year 2023 (i.e., CY 2022):
Foreign exchange income as per Financial Statements for CY 2022 = XXX
Less: Foreign exchange income of five specified calendar years (2016 to 2020) = XXX

Add: Windfall income for CY 2021 (as computed for tax year 2022) = XXX
Foreign exchange income to be used for average income = XXX
Foreign exchange income for last six CY years (as above) + 6 = XXX
Windfall income for CY 2022 (i.e., tax year 2023) = Taxable @ 40% = XXX

Notes:

1. For computing average foreign exchange income to be used in determining the windfall income, the following shall be noted:
   i) For CY 2021 (i.e., tax year 2022), foreign exchange incomes of the immediately preceding six calendar years (CY 2015 to 2020) are added and then divided by 6; and
   ii) For CY 2022 (i.e., tax year 2023), foreign exchange incomes of five specified calendar years (i.e., CY 2016 to 2020) and windfall income for CY 2021 (i.e., tax year 2022) are added and divided by 6.
2. If windfall income for CY 2021 (i.e., tax year 2022) is negative, then its value (to be used in the formula for CY 2022) shall be taken as zero.
3. Where there is a foreign exchange loss in any calendar year, then that calendar year and its loss shall be ignored while computing average foreign exchange income.
   It simply means that foreign exchange income of the remaining years shall be divided by the number of the remaining calendar years.

SPECIAL PROVISIONS UNDER SEVENTH SCHEDULE

COMPUTATION OF INCOME [Rule 1 & 2]

Total of all incomes, profits and gains, before tax, from all sources as disclosed in the annual accounts furnished to the SBP shall be taken as income of a banking company. This income shall be subject to the following provisions:

Depreciation:

1. Statutory depreciation shall be allowed as a deduction whereas accounting depreciation shall be added to the income. No allowance or deduction shall be admissible on assets given on finance lease.
2. ITO’s provisions relating to inadmissible deductions (u/s 21), gain or loss on disposal of depreciable assets (u/s 22(8)) and assets (u/s 75 to 79) shall, **mutatis mutandis**, apply.

Provisions for Advances and off Balance Sheet Items:

1. Deduction is allowed for **actual provision for advances and off balance sheet items** subject to the maximum of the following limits:

i) **Banking companies**: 1% of total advances; and
ii) **Consumers and SMEs**: 5% of total advances.

2. A banking company shall furnish a certificate from the external auditor to the effect that such provisions are based upon and are in line with the Prudential Regulations.
3. Provisioning in excess of the above-referred limits shall be carried over to succeeding years.
4. Provision allowed as deduction shall be exclusive of reversals of such provisions, if any.
5. Reversal of **bad debts** classified as "doubtful" or "loss" are taxable as the respective provisions have been allowed as deduction.
    - **Bad debts** classified as 'sub-standard' or 'doubtful' under the Prudential Regulations issued by the SBP or provisions for advances, off-balance sheet items or any other financial asset classified in stage I, II or III as performing, under-performing or non-performing under any applicable accounting standard including IFRS 09 shall not be allowed as expense.

    - Only **bad debts** classified as "loss" pertaining to non-performing assets under the Prudential Regulations issued by the SBP shall be allowed as expense.

6. Provisions or Expected Credit loss for Advances and off balance sheet items or any other financial asset existing before or after 01-01-2024 under IFRS 09 shall not be allowed as an expense or deduction.
7. Where in a tax year **bad debts** is reclassified as "loss" or "recoverable", then it shall be allowed as an expense in that tax year (as per above-discussed provisions).
8. Adjustment made in the annual accounts, on account of any applicable accounting standard or policy or any guidelines or instructions of SBP shall be excluded in arriving at taxable income.
   This adjustment shall be made in the year of disposal of such item or asset or the discharge of the liability.

Additional Notes:
• **Any notional loss or notional gain on any investment shall not be allowed as expense or charged to tax unless all the events that determine such gain or loss have occurred and the gain or loss can be determined with reasonable accuracy.**
• **The Seventh Schedule does not restrict power of CIR, while conducting audit u/s 177, to call for record, information and documents as he may deem appropriate for the purpose.**

Unpaid Liability:

1. Where a deduction is allowed for any expenditure and the liability or a part of the liability in respect of that expense is not paid within three (3) years of the end of the tax year in which the deduction was allowed, the unpaid liability shall be taxable as "Income from Business" in the first tax year following the end of three years.

2. Where, subsequently, such liability or its part is paid, a deduction shall be allowed for the amount paid in the tax year in which it is paid.

Loss on Disposal of Securities:

1. Loss on sale of shares of listed companies, disposed within one year of their acquisition, shall be adjustable against **business income** of the tax year.
2. Unadjusted loss for the tax year shall be carried forward for set-off against **capital gains only**. Loss shall be carried forward upto six (6) years immediately succeeding the tax years.

SHARIAH COMPLIANT BANKING [Rule 3]

1. Any special treatment for "Shariah Compliant Banking" approved by the SBP shall not be provided for any reduction or addition to income and tax liability. Income and tax shall be computed as per Seventh Schedule.
2. A statement, certified by the auditors, disclosing the comparative position of transaction as per Islamic mode of financing and as per normal accounting principles shall be attached to the return of income. Adjustment to the income of the company shall be made according to the accounting income as per Seventh Schedule.

TRANSFER OF ASSETS IN DIVERSIFIED PAYMENT RIGHTS [Rule 3A]

Where any assets are transferred by an Authorized Dealer, as a consequence of a Diversified Payment Rights transaction, to a Special Purpose Vehicle, it shall be treated as a financing transaction irrespective of the method of accounting adopted by the Authorized Dealer.

Diversified Payment Rights, **Special Purpose Vehicle** and **Authorized Dealer** shall mean the 'Diversified Payment Rights', 'Special Purpose Vehicle' and 'Authorized Dealer' respectively, in each case, as referred in the State Bank of Pakistan’s Circular(s) or Regulations on Diversified Payment Rights.

HEAD OFFICE EXPENDITURE OF FOREIGN BANKS [Rule 4]

1. A foreign bank shall be allowed a deduction for head office expenditure as per the following formula:

(A/B) × C

Where:
A = The gross receipts of permanent establishment in Pakistan;
B = The world gross receipts; and
C = The total head office expenditure.

The term 'head office expenditure' is defined in section 105(3) & (4) of ITO. The definition is discussed in the chapter Permanent “Establishment & Non-Residents.”

2. This deduction is subject to the following conditions:

i) Head office expenditure is charged in the books of accounts of the PE; and
ii) A certificate from auditors is provided to the effect that the claim of such expenditure:
a) Has been made in accordance with the above-discussed rule; and
b) Is reasonable in relation to the operation of the PE in Pakistan.

ADVANCE TAX [Rule 5]

1. Advance tax u/s 147 of ITO shall be paid by 15th of every month.
2. At any time before the installment payable on 15th June, a banking company shall estimate its tax liability for the relevant tax year. Where tax payable is likely to be more than the amount it is required to pay, it shall:
   i) Furnish to the CIR an estimate of the amount of tax payable for the year;
   ii) Pay so much amount as installment due on 15th June that 50% of estimated tax liability is paid as advance tax by 15th June of the relevant tax year; and
   iii) Remaining 50% shall be paid equal in remaining six installments.

Other provisions of advance tax u/s 147 of ITO shall also apply to a banking company.

EXEMPTION FROM TAX WITHHOLDING [Rule 5(2)]
Tax shall not be withheld from a banking company where it is recipient of an amount subject to tax withholding under any provision of the ITO.

TAX ON INCOME FROM GOVERNMENT SECURITIES [Rule 6C]
Tax Years 2020 and 2021:

1. **'Additional income earned'** from **'additional investment'** in FG securities shall be taxed @ 37.5% instead of normal rate of 39%.
2. A certificate from auditors shall also be furnished while e-filing return of Income certifying the amount of the money invested in Federal Government securities in preceding tax year, additional investments made for the tax year and mark-up income earned from the additional investments for the tax year.
3. In order to determine the applicability of the enhanced rate of tax, CIR may require the banking company to furnish details of the investments in FG securities.
4. The taxable income arising from additional investment shall be determined through this formula:
   A x B/C
   Where:
   A = Taxable income of the banking company;
   B = Mark-up income earned from the additional investment for the tax year; and
   C = Total of the mark-up income and non-mark-up income of the banking company as per accounts.

'Additional investments' means average investment made by the bank in FG securities during the tax year, in addition to the average investments held during the tax year 2019.
'Additional income earned' means mark-up income earned from additional investments for the tax year.

Tax Years 2022 & 2023: [Rule 6C(6A)]

Taxable income attributable to investment in FG securities shall be taxed at the following rates:

- 55% instead of 39% if the gross advances to deposit ratio as on the last day of the tax year is up-to 40%;
- 49% instead of 39% if the gross advances to deposit ratio as on last day of the tax year exceeds 40% but does not exceed 50%; and
- 39% if gross advances to deposit ratio as on last day of the tax year exceeds 50%.

Notes:

1. The above tax rates shall be applicable to total income attributable to total investment in Federal Government securities.
2. This provision shall not apply to a banking company for tax year 2024. [Rule 8(5)]
3. For tax years after 2024 Rule 6 (providing for enhanced rate of tax on taxable income from FG securities) shall become functional. In that case the normal provisions applicable to companies under ITO shall also apply to banking companies on income from FG securities.

APPLICATION OF SECTION 113 [Rule 7A]

Just like other resident companies, section 113 shall apply to banking companies.

DIVIDEND AND CAPITAL GAINS [Rule 7B]

Income from Dividend and Capital Gains shall be taxable at the normal rates, i.e., @ 39%.

TAX ON ADDITIONAL ADVANCES FOR MICRO, SMALL AND MEDIUM ENTERPRISES [Rule 7D]

1. Tax for the tax years 2022 to 2023 on taxable income arising from additional advances to micro, small and medium enterprises shall be charged @ 20% instead of normal rate of 39%. For tax year 2024 this income shall also be taxable @ 39%.
2. A certificate from auditors certifying the amount of such advances made in preceding tax year, additional advance made for the tax year and net mark-up earned from additional advances for the tax year shall also be furnished while e-filing return of income.
3. In order to determine the applicability of the enhanced rate of tax, the CIR may require the banking company to furnish details of the advances to micro, small and medium enterprises.
4. Taxable income arising from additional advances shall be determined according to the formula:

A x B/C

Where:

A = Taxable income of the banking company;

B = Net mark-up income earned from such additional advances for the tax year as declared in the annual accounts; and

C = Total of the net mark-up and non-mark-up income of the banking company as per accounts.

The term " micro, small and medium enterprises shall have the same meaning as provided in Prudential Regulations issued by the SBP.
" Additional advances " means any average advances disbursed in addition to average amount of such advances made in such sector by the bank for the tax year.

TAX ON ADDITIONAL ADVANCES FOR LOW-COST HOUSING [Rule 7E]

1. Tax for the tax years 2020 to 2023 on taxable income arising from additional advances for low-cost housing shall be charged 20 % instead normal rate of 39 %.

For tax year 2024 this income shall also be taxable @ 39 %.

2. Taxable income arising from additional advances to Naya Pakistan Housing and Development Authority for low-cost housing schemes shall be taxable @ 10 %.
3. A certificate from auditors certifying the amount of such advances made in preceding tax year, additional advance made for the tax year and net mark - up earned from additional advances for the tax year shall also be furnished while e - filing return of Income.
4. In order to determine the applicability of the reduced rate of tax, the CIR may require the banking company to furnish details of the advances made for low-cost housing.
5. Taxable income arising from additional advances shall be determined according to the following formula:

A x B / C

Where: A = Taxable income of the banking company; B = Net mark - up income earned from such additional advances for the tax year as declared in the annual accounts; and C = Total of the net mark - up and non - mark - up income of the banking company as per accounts.

1. The term " low-cost housing " shall have the same meaning as provided in Prudential Regulations issued by the SBP.
2. " Additional advances " means any average advances disbursed in addition to average amount of such advances made in such sector by the bank for the tax year 2019.

TAX ON ADDITIONAL ADVANCES AS FARM CREDIT (Rule 7F)

1. Tax for the tax years 2020 to 2023 on taxable income arising from additional advances as Farm Credit in Pakistan shall be charged @ 20 % instead normal rate of 39 %.

For tax year 2024 this income shall also be taxable @ 39 %.

2. A certificate from auditors certifying the amount of such advances made in preceding tax year, additional advance made for the tax year and net mark - up earned from additional advances for the tax year shall also be furnished while e - filing return of income.
3. In order to determine the applicability of the reduced rate of tax, the CIR may require the banking company to furnish details of the advances made for Farm Credit.

   Taxable income arising from additional advances shall be determined according to the following formula: A x B / C

   Where:

   A = Taxable income of the banking company;

   B = Net mark - up income earned from such additional advances for the tax year as declared in the annual accounts; and

   C = Total of the net mark - up and non - mark - up income of the banking company as per accounts.

The term " Farm Credit " shall have the same meaning as provided in Prudential Regulations issued by the SBP for agriculture financing, excluding advances made to a company as defined in section 80 of ITO.
" Additional advances " means any average advances disbursed in addition to average amount of such advances made in such sector by the bank for the tax year 2019.

EXEMPTIONS [Rule 8]

1. Exemptions and tax concessions under the Second Schedule to ITO shall not apply to income of banking company computed under Seventh Schedule.

2. The accumulated business loss (other than speculation losses) of an amalgamating banking companies shall be set off or carried forward against the business profits and gains of the amalgamated company and vice versa, up to six (6) tax years immediately succeeding the tax year in which the loss was first computed.

3. Group relief u / s 59B of ITO shall be available provided the holding and subsidiary companies are banking companies. The accounts of the group companies shall be audited by the chartered accountants, firm on the panel of auditors of SBP. The surrender and claim of loss would be subject to approval of SBP.

4. The holding and subsidiary companies of 100 % owned group of banking companies may opt to be taxed as one fiscal unit u / s 59AA relating to group taxation subject to the approval of SBP.

5. Profit on debt and capital gains from FG's sovereign debt and debt instruments derived by any non - resident banking company shall be exempt from income tax.

For the purpose of this exemption, the debt, debt instrument and the company should be approved by FG under a sovereign agreement.

PROVISIONS OF ITO [Rule 9]

In respect of the matters not specifically dealt with in the Seventh Schedule, the provisions of the ITO shall apply, mutatis mutandis, to the banking company.

CHAPTER - 17
TAX CREDITS

TAX CREDITS [4 (3)]

Part - X of Chapter - III of the Income Tax Ordinance, 2001 deals with the matters relating to the different tax credits available to a taxpayer. While computing the tax liability of a person under the Income Tax Ordinance, 2001 different types of tax credits are allowed to a taxpayer. These tax credits may broadly be classified under the following categories: [4 (3)]

Category ' A ' REBATE IN TAX LIABILITY

Rebate means a reduction in tax liability. Certain rebates or tax credits are allowed to a taxpayer, if specified conditions are satisfied. Rebates may be classified into the following two groups:

1. Foreign Tax Credit

Tax Credit for such foreign - source income of a resident taxpayer which is taxable under the Income Tax Ordinance, 2001. [103]

2. Tax Credit for Donations and Investments, Etc.

Tax Credits allowed under sections 61 to 65E (Part - X of Chapter - III) and section 100C, which are for:

i) Charitable donations;
ii) Contribution to approved pension fund;
iii) Employment generation by manufacturers;
iv) Point of sale machine;
v) Investment by companies on purchase of plant and machinery;
vi) Industrial undertakings established before 01-07-2011;
vii) Mining projects in Sindh and startups;
viii) Specified industrial undertakings;
ix) Tax credit for foreign investment for industrial promotion; and x) Charitable organizations.

Category ' B ' CREDIT FOR TAX ALREADY PAID

Tax Credit for the amount of tax already deposited by or on behalf of the taxpayer. These payments may fall under any or all of the following:

1. Amount recovered by the Commissioner from any other person on account of the taxpayer;
2. Advance payment of tax by the taxpayer;
3. Tax deducted or collected at source; and [168 (2)]
4. Any amount of refund for previous tax years.

Coming paragraphs contain the details of all the above - stated categories of the tax credits.

FOREIGN TAX CREDIT [103]

Provisions regarding the taxation of foreign-source income and tax credit of a resident taxpayer are summarized below:

1. Any foreign-source income (other than the salary income) of a resident taxpayer shall be chargeable to tax under the Income Tax Ordinance, 2001. However, he shall be allowed a tax credit in respect of the foreign-source income. The credit shall be of an amount which is lesser of the following two amounts:
   i) The foreign income tax paid; or
   ii) The Pakistan income tax payable in respect of net foreign-source income computed at the average rate of Pakistan income tax. [103(1) & (2)]

Example: 17.1

Mr. Asim, a resident, derived an income of Rs. 2,400,000 from his business in Pakistan. He also earned an amount of Rs. 600,000 from different sources in UAE. He paid Rs. 96,000 as income tax in UAE in respect of his income from there. Compute the tax liability of Mr. Asim under the Income Tax Ordinance, 2001.

Answer:

Income from Business

- Pakistan-source income: Rs. 2,400,000
- Foreign-source income (assuming business): Rs. 600,000
- **Taxable income** = Rs. 3,000,000

Tax Liability

- Tax on Rs. 1,600,000 = Rs. 170,000
- Tax on Rs. 1,400,000 @ 30% = Rs. 420,000
- **Less:** Foreign Tax Credit, i.e., lesser of:
  A) Foreign income tax paid = Rs. 96,000
  OR
  B) Pakistan income tax:
  Tax on Taxable Income × Foreign Source Income
  = (Rs. 590,000 ÷ Rs. 3,000,000) × Rs. 600,000
  = Rs. 118,000
    - **Total Tax Liability** = Rs. 590,000 - Rs. 96,000 = Rs. 494,000

2. Where the foreign income falls under different heads of income, it shall be charged to tax under their respective heads. The tax credit shall also be allowed separately for each head. [103(3)]

Example: 17.2

Considering the same information as in the above example, further assume that the segregation of UAE income and tax thereon is as below:

Source of Income	**Income**	**Tax**
Income from business	Rs. 300,000 @ 24%	Rs. 72,000
Income from other sources	Rs. 300,000 @ 8%	Rs. 24,000
Total	Rs. 600,000	Rs. 96,000

Compute Mr. Asim's tax liability

Answer:

Computation of Taxable Income

- **Income from Business:**
  - Pakistan-source: 2,400,000
  - Foreign-source: 300,000
- **Income from other sources (foreign source):** 300,000
- **Taxable income:** 3,000,000

Tax Liability

- Tax on taxable income – as per First Schedule (as in Example 17.1): 590,000
- **Less:** Foreign tax credit (see working): (83,000)
- **Total tax liability:** 507,500

Computation of Foreign Tax Credit

A) **In respect of Income from Business:**

- Lesser of:
  i) Foreign income tax paid: 72,000
  OR
  ii) Pakistan income tax: (590,000 ÷ 3,000,000) × 300,000 = 59,000
- **Amount for Business:** 59,000

B) **In respect of Income from Other Sources:**

- Lesser of:
  i) Foreign income tax paid: 24,000
  OR
  ii) Pakistan income tax: (590,000 ÷ 3,000,000) × 300,000 = 59,000
- **Amount for Other Sources:** 24,000
- **Total amount of tax credit:** 83,500

3. Average rate of Pakistan income tax is computed on the basis of tax on taxable income (without allowing any other tax credit). [103(8)]

4. Just like Pakistan-source income, income from foreign-source speculation business is treated as a separate head of income. [103(4)]

5. Foreign tax credit is allowed maximum up-to the total income tax liability under the Income Tax Ordinance, 2001. Any excess amount of tax credit shall not be refunded, carried forward or carried back to the following or preceding tax years. [103(6)]

6. The foreign income tax must be paid within two (2) years after the end of the tax year in which the income is earned. If the payment is not made within the prescribed period, the tax credit shall not be allowed. [103(7)]

Actually, the tax credit had already been allowed during the tax year in which income was earned. Now, because of non-payment of foreign tax, it has become inadmissible. Under such a case the amount allowed as tax credit shall become payable to the tax authorities.

7. Tax credit is allowed on **"net foreign-source income"** which means the total foreign-source income less any deductions allowed under the Income Tax Ordinance. [103(8)]

8. If a resident person sustains a foreign loss, he is allowed to set-off and carry forward such loss. [104]

Compute Mr. Asim's tax liability

Answer:
Computation of Taxable Income
Income from Business:
Pakistan - source 2,400,000
Foreign - source 300,000 2,700,000
Income from other sources (foreign source) 300,000 Taxable income 3,000,000
Tax Liability
Tax on taxable income as per First Schedule (as in Example 17.1) 590,000
Less: Foreign tax credit (see working) (83,000)
Total tax liability 507,500
Computation of Foreign Tax Credit
A) In respect of Income from Business:
Lesser of:
i)Foreign income tax paid 72,000 OR
ii) Pakistan income tax
(590,000 / 3,000,000) × 300,000 = 59,000 59,000
B) In respect of Income from Other Sources: Lesser of:
i)Foreign income tax paid 24,000
OR
ii) Pakistan Income Tax
(590,000 / 3,000,000) × 300,000 = 59,000 24,000
Total amount of tax credit 83,500
3. Average rate of Pakistan income tax is computed on the basis of tax on taxable income (without allowing any other tax credit). [103 (8)]

4. Just like Pakistan - source income, income from foreign - source speculation business is treated as a separate head of income. [103 (4)]
5. Foreign tax credit is allowed maximum up-to the total income tax liability under the Income Tax Ordinance, 2001. Any excess amount of tax credit shall not be refunded, carried forward or carried back to the following or preceding tax years. [103 (6)]
6. The foreign income tax must be paid within two (2) years after the end of the tax year in which the income is earned. If the payment is not made within the prescribed period, the tax credit shall not be allowed. [103 (7)]
Actually, the tax credit had already been allowed during the tax year in which income was earned. Now, because of non - payment of foreign tax it has become inadmissible. Under such a case the amount allowed as tax credit shall become payable to the tax authorities.
7. Tax credit is allowed on " net foreign - source income " which means the total foreign - source income less any deductions allowed under the Income Tax Ordinance. [103 (8)]
8. If a resident person sustains a foreign loss, he is allowed to set - off and carry forward such loss. [104]
9. Foreign Tax Credit shall be allowed prior to any other tax credit allowable under the Income Tax Ordinance. [103 (5)]

TAX CREDIT FOR CHARITABLE DONATIONS, VOLUNTARY CONTRIBUTIONS OR SUBSCRIPTIONS [61]

A tax credit at the average rate of tax shall be allowed to a taxpayer if he has made any donation, voluntary contribution or subscription during the tax year. Tax credit shall be allowable only if the following conditions are fulfilled:
1. The donations are made during the tax year.
2. The taxpayer possesses evidence in respect of the donations made by him.
3. The donations may be made in kind or in cash. The payment of an amount should be through a crossed cheque.
4. A donation has been given to the following institutions:
i) A recognized Board of Education or a University in Pakistan established under a Federal or Provincial law;
ii) Any of the following institutions established or run by the Government (Federal, Provincial or Local):
a) An educational institution,
b) A hospital, or
c) A relief fund.
iii) Any non - profit organization or any person eligible for tax credit under section 100C of the Income Tax Ordinance, or
[List of such NPOs is provided in Table-ll of clause (66) of the Second Schedule, which is available in Chapter "Exemptions and Concessions" of this book.]

iv) Entities, organizations and funds mentioned in the Thirteenth Schedule to the Income Tax Ordinance. [Thirteenth Schedule is available at the end of this Chapter]
5. The tax credit for donations is restricted up-to the lesser of the following amounts: Total amount of donations; or
i) Twenty per cent (20 %) of the taxable income for the year, in the case of a company; or
ii) Thirty per cent (30 %) of taxable income for the year, if the person is an individual or an AOP. Where donation is made to an associated person, the maximum limit shall be 10 % for companies and 15 % for individuals and AOPs.

Notes:

1. Fair market value of a property, at the time when it is donated, shall be the amount of donation in respect of that property.
2. The maximum limit of 20 % or 30 % of taxable income in case of donations made respectively by companies or other taxpayers, shall not apply to donations made to Agha Khan Hospital and Medical College, Karachi. Donations to this institution may be made without any limit and the taxpayer shall be allowed a tax credit on such donations at the average rate of tax.
[Clause (3), Part-IV, Second Schedule]

3. **The taxpayer is allowed a tax credit in the tax payable by him.** Tax credit is computed at the average rate of tax. A straight deduction from the total income shall not be allowed.

Non-Profit Organization [2(36)]

'Non-profit organization' means any person (other than an individual) that fulfills the following conditions:

1. The organization is established for:
   i) The religious, educational, charitable, welfare or development purposes; or
   ii) The promotion of an amateur sport.
2. It is formed and registered by or under any law as a non-profit organization.
3. It is approved by the Commissioner Inland Revenue (CIR) for a specified period; and
4. Its assets and properties cannot be applied for the private benefit of any other person.

Note: The CIR grants approval on a written application submitted to him. The application should be on the prescribed form and it shall contain such particulars and information as are prescribed under Rules 211 through 220 of the Income Tax Rules, 2002.

Example: 17.3

An individual who is running his own business has total income of Rs. 3,200,000. During the year, he donated Rs. 600,000 to approved institutions and Rs. 100,000 to unapproved institutions. Compute his tax.

Answer:

Donations to Approved Institutions

- Total taxable income = 3,200,000
- Tax on Rs. 3,200,000 (as per tax table) = 650,000

- **Less:** Tax credit for donations [(650,000 ÷ 3,200,000) × 600,000] = (121,875)
- **Tax liability for the year** = 528,125

N-1 Donations to approved institutions are within the limit of 30% of taxable income.
N-2 While computing taxable income and tax liability of a person, donations made to unapproved institutions or funds shall be ignored.

TAX CREDIT FOR CONTRIBUTION TO APPROVED PENSION FUND [63]

A tax credit at the average rate of tax shall be allowed to an **'eligible person'** in respect of any contribution or premium paid by him in the tax year in approved pension fund. In order to avail this tax credit, the following conditions should be satisfied:

1. The pension fund should have been approved under the Voluntary Pension System Rules, 2005.
2. The person is deriving income which is chargeable to tax under the head "Salary" or "Income from Business".
3. The tax credit is allowed for such payment which is lesser of the following amounts:

i) Total contribution or premium paid in the tax year; or
ii) Twenty per cent (20%) of taxable income of the eligible person for the relevant tax year (see note below).

Note: The total allowed contribution should not be more than 50% of the total taxable income of the preceding year.

4. Amount of tax credit shall be computed by applying the average rate of tax to the contribution on which it is allowed. The average rate of tax for this purpose is computed as below:

Tax for the Year – Foreign Tax Credit
Taxable Income for the Tax Year.

Note: Where members of approved employment pension or annuity scheme or approved occupational saving scheme transfer their existing balance to their individual pension accounts maintained with one or more pension fund managers, then such transfer shall not qualify for tax credit.

'Individual Pension Account' means an account maintained by an eligible person with a Pension Fund Manager approved under the Voluntary Pension System Rules, 2005. [2(29B)]

Eligible Person [2(19A)]

This term has been defined for the purpose of Voluntary Pension System Rules, 2005. It means an individual who fulfills the following conditions:

1. He is a Pakistani; and
2. He holds a valid NTN or Computerized National Identity Card or National Identity Card for Overseas Pakistanis issued by the National Database and Registration Authority.

Total tax credit for the contribution made to approved pension or annuity scheme and approved pension fund under the Voluntary Pension System Rules, 2005, should not be more than the limit specified in section 63 of the Income Tax Ordinance.

TAX CREDIT FOR EMPLOYMENT GENERATION BY MANUFACTURERS [64B]

A company is allowed a tax credit for generating new employment opportunities. This tax credit is subject to the following conditions:

1. The company is formed for establishing and operating a new manufacturing unit. The company shall have its registered office in Pakistan and is incorporated under the Companies Act, 2017 between 01-07-2015 and 30-06-2018;
2. The manufacturing unit is set up between 01-07-2015 and 30-06-2018;
3. The manufacturing unit is not established by:
   i) Splitting up or reconstruction or reconstitution of an undertaking already in existence; or
   ii) Transfer or machinery or plant from an undertaking established in Pakistan before 01-07-2015;

4.The company employs more than fifty (50) employees in a tax year.

5. The employees are registered with The Employees Old Age Benefits Institution (EOBI) and The Employees Social Security Institutions (ESSI) of the respective Provincial Government;

6. Tax credit shall be equal to two percent (2%) of tax payable for every fifty (50) employees of the company registered with EOBI or ESSI;

7. Maximum tax credit allowable on this account should be ten percent (10%) of the tax payable; and

8. This tax credit shall be admissible for a period of ten (10) years.

Notes:

1. Manufacturing unit shall be treated to have been set-up on the date on which it is ready to go into production, whether trial production or commercial production.
2. Tax credit allowed to a company shall be deemed to have been wrongly allowed if it is subsequently discovered that any of the above-referred conditions were not fulfilled. Under this case the Commissioner shall re-compute the tax payable by the company for the relevant tax year.

TAX CREDIT FOR POINT OF SALE MACHINE [64D]

A tax credit in respect of the amount invested in purchase of point-of-sale machine shall be allowed to a person who is required to integrate with FBR's computerized system for real-time reporting of sale or receipt.

Tax credit is allowed for a tax year in which point of sale machine is installed, integrated and configured with the FBR's computerized system.

Lesser of the following amounts shall be allowed as tax credit:

1. Amount actually invested in purchase of point of sale machine; or

2. Rs. 150,000 per machine.

'Point of sale machine' means a machine meant for processing and recording the sale transactions for goods or services, either in cash or through credit and debit cards or online payments in an internet enabled environment.

IMPORTANT NOTES [65]

1. Where a person who is entitled to tax credit u/s 61-63 (i.e., for donations, investment in shares, investment in health insurance or contribution to approved pension fund) is a member of such an AOP which is chargeable to tax and share from its income is exempt from tax in the hands of the members, the average rate of tax shall be computed on his total income (including exempted share in income of AOP). [65(1)]

Example 17.4

Mr. Ali has the following sources of income:

a) Income from business: Rs. 2,400,000

b) Share from AOP's income: Rs. 400,000

Total Income: Rs. 2,800,000

Further, he donated Rs. 240,000 to approved institutions. Compute the amount of tax credit and tax payable by Mr. Ali considering that AOP has paid the tax liability in respect of its income.

Answer:

- **Income from business**: Rs. 2,400,000
- **Share from AOP (included for rate purposes only)**: Rs. 400,000
- **Taxable income**: Rs. 2,800,000

Tax on taxable income:

- Tax on Rs. 1,600,000: Rs. 170,000
- Tax on Rs. 1,200,000 @ 30%: Rs. 360,000
- **Total tax**: Rs. 530,000
- Tax on actually taxable income [(530,000 + 2,800,000) × 2,400,000] = 454,286
- **Less:** Tax credit for donations [(530,000 + 2,800,000) × 240,000] = (45,429)
- **Tax liability for the year**: Rs. 408,857

2. Where the tax liability (i.e., tax on taxable income) of a person is less than the tax credit on account of donations, investment, contribution to approved pension fund and profit on debts, then the excess amount of tax credit shall not be refunded or allowed to be carried forward or carried back. [65(3)]

However, if the above-referred person is a member of such an AOP which pays tax on its incomes, the excess amount of tax credit of the person may be claimed as tax credit by the AOP. The AOP can claim the tax credit only if the following conditions are satisfied: [65(4)]

i) The member and the AOP agreed in writing on the above arrangement; and

ii) The agreement has been furnished by the AOP along with its return of income.

TAX CREDIT FOR INVESTMENT IN PLANT AND MACHINERY [65B]
Tax credit u/s 65B was available till tax year 2019; hence, it is not discussed here.
TAX CREDIT FOR INDUSTRIAL UNDERTAKINGS ESTABLISHED BEFORE 01-07-2011 [65E]
An already existing company is also allowed to avail tax credit on its new investment in plant and machinery. Legal provisions in this regard are as below:
1. The company is set-up in Pakistan before 01-07-2011.
2. The investment is made with at least seventy percent (70%) new equity raised through issuance of new shares.
3. The investment is made in the purchase and installation of plant and machinery for an industrial undertaking, including corporate dairy farming for:
i) Expansion of the plant and machinery already installed therein, or
ii) Undertaking a new project.
4. Tax credit shall be allowed for a period of five (5) years starting from the date which is later of:
i) The date of setting up; or
ii) The date of commencement of commercial production from the new plant or expansion project.
Tax Credit shall be deducted from tax payable by the company for the tax year in which plant or machinery is installed and for the subsequent four (4) tax years.

5. **Amount of tax credit shall be determined as below:**

i) **Where Separate Accounts Are Maintained:**
Where the company maintains separate accounts for the project (expansion or new), the company shall be entitled to tax credit for an amount which shall be calculated as below:
A × (B + C)

- **A** = Amount of tax attributable to such project (before any tax credit)
- **B** = Equity raised through issuance of new shares for cash consideration
- **C** = Total amount invested in the purchase and installation of plant and machinery for the industrial undertaking

The assessed tax shall include the tax on account of minimum tax and final taxes on the taxable income arising from such industrial undertaking.
Where the company maintains separate accounts of the project (expansion or new), tax credit shall be equal to 100% of the tax payable (including minimum tax and final taxes) attributable to such project.
ii) **In All Other Cases:**
The allowable amount of tax credit, under such cases, shall base on the new equity introduced and total equity of the company. Amount of tax credit shall be computed through the following formula:
[Tax Credit (as in 5(i) above) × Total Equity] ÷ New Equity

6. The plant or machinery is installed on or between 01-07-2011 and 30-06-2021.
7. Where a company is allowed its tax credit and the CIR subsequently discovers that either business has been discontinued in the subsequent five (5) years or any of the above-referred conditions was not fulfilled then it shall be deemed that credit originally allowed was wrongly allowed. Under this case, the CIR shall re-compute the tax liability for the relevant tax year.
8. **New Equity** means the equity raised through fresh issue of shares against cash. It shall not include loans obtained from shareholders or directors.
9. Short-term loans and finances obtained from banking companies or NBFIs for meeting working capital requirements shall not disqualify the company from claiming tax credit.

TAX CREDIT FOR CERTAIN PERSONS [65F]

1. A tax credit equal to 100% of the tax payable under any provisions of the Income Tax Ordinance shall be allowed to the following persons or incomes:

i) Persons engaged in coal mining projects in Sindh supplying coal exclusively to power generation projects; and

ii) This tax credit shall only be available to the income derived from the operations of coal mining projects in Sindh supplying coal to power generation projects.

iii) A **'startup'** for the tax year in which the startup is certified by the Pakistan Software Export Board and the next following two (2) tax years.

2. Tax payable includes minimum, alternate corporate tax and final taxes for the period.

3. The tax credit shall be available if the following conditions, if applicable, are fulfilled:

i) **Return has been filed**

ii) **Applicable withholding tax statements for the relevant tax year have been filed**, where the person is a withholding agent; and

iii) **Sales tax return for the taxes corresponding to relevant tax year have been filed** if the person is required to file Sales Tax Return under any of the Federal or Provincial Sales Tax laws.

Startup [62(2A)]

'**Startup**' means a business of a resident person (individual, AOP or company) which fulfills the following conditions:

1. The business is commenced on or after 01-07-2012;
2. The person is engaged in or intends to offer technology driven products or services to any sector of the economy;
3. The person is registered with and duly certified by the Pakistan Software Export Board (PSEB); and
4. The person has turnover of less than one hundred million in each of the last five tax years.

'**Startup**' may also mean any business of a person or class of persons which fulfills the conditions notified by FBR with the approval of Federal Minister-in-charge in the official Gazette.

TAX CREDIT FOR SPECIFIED INDUSTRIAL UNDERTAKINGS [65G]

An eligible taxpayer shall be allowed to take an investment tax credit for making certain eligible capital investments against tax payable including minimum and final taxes.

Tax credit shall be 25% of the eligible investment amount. Where the tax credit is not fully adjusted during the year of investment, it shall be carried forward to the subsequent tax year. It may be carried forward for a maximum period of two years.

'Eligible investment' means investment made in purchase and installation of new machinery, buildings, equipment, hardware and software, except self-created software and used capital goods.

'Eligible person' means:

1. **Greenfield industrial undertaking engaged in:** i) Manufacture of goods or materials or the subjecting of goods or materials to any process which substantially changes their original condition; or ii) **Ship building**:
    - Provided that the person is incorporated between the 30-06-2019 and the 30-06-2024 and is not formed by the splitting up or reconstruction of an undertaking already in existence or by transfer of machinery, plant or building from an undertaking established in Pakistan prior to commencement of the new business and is not part of an expansion project.
2. An **industrial undertaking** set up by 30-06-2023 and engaged in the manufacture of plant, machinery, equipment and items with dedicated use (no multiple uses) for generation of renewable energy from sources like solar and wind, for a period of five (5) years beginning from the date such industrial undertaking is set up.

'Greenfield Industrial Undertaking' means a new industrial undertaking which is: [2(27A)]

1. Set-up on land which has not previously been utilized for any commercial, industrial or manufacturing activity and is free from constraints imposed by any prior work;
2. Built without demolishing, revamping, renovating, upgrading, remodelling, or modifying any existing structure, facility, or plant;
3. Not formed by the splitting up or reconstitution of an undertaking already in existence or by the transfer of machinery, plant, or building from an undertaking established in Pakistan prior to commencement of the new business and is not part of an expansion project;
4. Using any process or technology that has not earlier been used in Pakistan and is so approved by the Engineering Development Board; and
5. Approved by CIR on an application made in the prescribed form and manner, accompanied by the prescribed documents and any other documents as may be required by the CIR.

NON-APPLICABILITY OF CERTAIN PROVISIONS [65(6)]

In case of tax credit u/s 65E (tax credit for industrial undertakings established before 01-07-2011), the following provisions of the Income Tax Ordinance, 2001 shall not apply:

1. Minimum tax liability if a person has no tax liability due to application of tax credits or rebates [113(1)(d)]; and
2. Considering the tax deducted at source as final tax. Under such a case, tax deducted is not reduced by any tax credits allowed under the Income Tax Ordinance [169(2)(d)].

This means that where a person is entitled to tax credit u/s 65E, the person shall not be liable to pay minimum tax in a case where there is no tax liability due to tax credits. Further, while determining final tax under FTR, tax shall be reduced by any tax credits available to the person under these sections.

TAX CREDIT FOR CHARITABLE ORGANIZATIONS [100C]

A tax credit equal to one hundred percent (100%) of tax payable (including minimum tax and final taxes) under any provision of the Income Tax Ordinance, 2001 shall be allowed to charitable and non-profit organizations subject to the following conditions:

1. Persons eligible for tax credit are:

i) Persons specified in Table-II of clause (66) of Part I of the Second Schedule (list of NPOs is available in the Chapter "Exemptions and Concessions");

ii) A trust administered under a scheme approved by the Federal Government and established in Pakistan for welfare of employees (retired and serving) personnel of the Federal Government or a Provincial Government or armed forces (including civilian employees) and their dependents where the said trust is administered by a committee nominated by the Federal Government or a Provincial Government;

iii) A trust

iv) A welfare institution registered with Provincial or Islamabad Capital Territory (ICT) social welfare department

v) A 'not for profit company' registered u/s 42 of the Companies Act, 201

vi) A welfare society registered under the provincial or Islamabad Capital Territory (ICT) laws related to registration of co-operative societies;

vii) A waqf registered under Mussalman Waqf Validating Act, 1913 or any other law for the time being in force or in the instrument relating to the trust or the institution;

viii) A university or education institution being run by a non-profit organization existing solely for educational purposes and not for the purposes of profit;

ix) A religious or charitable institution for the benefit of the public registered under any law for the time being in force; and

x) International non-governmental organizations (INGOs) approved by the Federal Government.

2. The incomes eligible for tax credit are:

i) Income from donations, voluntary contributions and subscriptions;

ii) Income from house property;

iii) Income from investments in the securities of the Federal Government;
iv) Profit on debt from scheduled banks and microfinance banks;
v) Grant received from Federal, Provincial, Local or foreign Government;
vi) So much of the income chargeable under the head "income from business" as is expended in Pakistan for the purposes of carrying out welfare activities:

- Only so much of income from business shall be eligible for tax credit that bears the same proportion as the said amount of business income bears to the aggregate of income from all sources; and
  vii) Any income of the following persons:
  a) Persons specified in Table-II of clause (66) of Part I of the Second Schedule;
  b) A trust administered under a scheme approved by the Federal Government established for employees of government;
  c) A university or education institution being run by a non-profit organization existing solely for educational purposes and not for the purposes of profit.

3. **Eligibility for tax credit shall be subject to the following conditions, namely:**
   i) Return has been filed;
   ii) Tax required to be withheld has been deducted or collected and paid;
   iii) Withholding tax statements for the relevant tax year have been filed;
   iv) Administrative and management expenditure does not exceed 15% of the total receipts. It shall not apply to a non-profit organization, if-
   a) Charitable and welfare activities have commenced for the first time within last three years; or
   b) Total receipts of the organization during the tax year are less than one hundred million Rupees;
   v) Approval of Commissioner, as required u/s 2 (36), has been obtained.

This condition shall apply to persons in Table-II of clause (66) of Part I of the Second Schedule from 01-07-2023 and shall not be applicable for earlier years:

vi) None of the assets of trusts or welfare institutions confers, or may confer, a private benefit to the donors or family, children or author of the trust or his descendants or the maker of the institution or to any other person.
vii) Where such private benefit is conferred, the amount of such benefit shall be added to the income of the donor; and
A statement of voluntary contributions and donations received in the immediately preceding tax year has been filed in the prescribed form and manner.

Taxation of Surplus Funds of Non-Profit Organization [100C (5) & (6)]

Although non-profit organizations, trusts, or welfare institutions are allowed a tax credit equal to 100% of tax payable, but its ‘surplus funds’ shall be taxable @ 10%.

'Surplus Funds' means the funds or monies which are:

1. Not spent on charitable and welfare activities during the tax year;
2. Received during the tax year as donations, voluntary contributions, subscriptions and other incomes;
3. More than 25% of the total receipts of the organization received during the tax year; and
4. Are not part of 'restricted funds'.

'Restricted Funds' means any fund received by the organization but could not be spent and treated as revenue during the year due to any obligation placed by the donor or funds received in kind.

Example: 17.5

A welfare institution duly approved by the FBR has the following sources of incomes during the tax year:

- Donations: Rs. 1,500,000
- Voluntary Contributions: Rs. 600,000
- Subscription Received from Members: Rs. 150,000
- Income from Property: Rs. 1,125,000
- Income from F.G. Securities: Rs. 375,000
- Business Income: Rs. 3,750,000
- **Total**: Rs. 7,500,000

The trust spent Rs. 6,000,000 for welfare activities in Pakistan. Compute the exempt and taxable income of the trust.

Answer:

Income Sources

Sources of Income	**Total**	**Exempt**	**Taxable**
Donations	1,500,000	1,500,000	-
Voluntary Contributions	600,000	600,000	-
Subscriptions	150,000	150,000	-
Income from Property	1,125,000	1,125,000	-
Income from Securities	375,000	375,000	-
Income from Business (W-1)	3,750,000	3,000,000	750,000
Total	7,500,000	6,750,000	750,000

W-1 Calculation of Exempt Income from Business

- Total income for the year: Rs. 7,500,000
- Amount expended in Pakistan for welfare: Rs. 6,000,000
- Percentage of the amount expended (6,000,000 ÷ 7,500,000 × 100): 80%
- Amount exempt from tax (80% of Rs. 3,750,000): Rs. 3,000,000

Priority of Tax Credits [4(3)]

Where a person is entitled to more than one tax credit, the tax credit shall be allowed in the following order:

1. First all foreign tax credit; then
2. Tax credit for investments, donations, etc., allowable u/s 61-64; and then
3. Tax already deposited by or on behalf of the taxpayer.

Notes:

1. **Foreign tax credit** is allowed prior to any other tax credit. However, tax credit for donations, investments, etc., shall be allowed at the rate computed as below:

Tax on Taxable Income - Foreign Tax Credit

Tax on Taxable Income × 100

2. **Tax credit for category 'A'** shall be restricted to the total amount of tax liability. Any excess amount of tax credit shall not be refunded, carried forward, or carried back. However, in the case of a member of such an AOP (Association of Persons) who pays tax on its taxable income, the excess amount of credit may be claimed by the AOP. [10(3) & 65(3) & (4)]
3. **Tax credit for category 'B'** (i.e., amount of tax collected or deposited on account of the taxpayer, etc.) shall be allowed irrespective of the amount of tax for the tax year. If the amount of tax credit is more than the tax liability, the excess amount shall be refunded to the taxpayer or adjusted against his tax liability for other tax years. [140(9), 147(10) & 168(5)]

Tax Credit to a Company for Tax Withheld from AOP [168(2A) & (2B)]

A company who is a member of an AOP (Association of Persons) which is taxed as per section 92 of the Income Tax Ordinance, 2001 shall be allowed a tax credit in respect of the tax withheld from the AOP subject to the following conditions:

1. **Tax has been deducted or deducted u/s 148 to 158** and **Transitional Advance Tax** provisions from transactions or payments made by the AOP;
2. Tax credit in respect of tax withheld from AOP shall be allowed as per following formula:

(A/B) × C

Where:

A = the amount of share of profits before tax received by the company as a member from the association of persons;

B = the taxable income of the association of persons; and

C = the amount of tax withheld in the name of the association of persons.

Note: The amount for which credit has been allowed to a company (being member of AOP), further tax credit shall not be allowed (to the AOP).

THE THIRTEENTH SCHEDULE

(See section 61)

Institutions and Funds Approved for Donations, Etc.

Sr No.	Name
1.	Any Sports Board or institution recognized, by the Federal Government for the purposes of promoting, controlling or regulating any sport or game.
2.	The Citizens Foundation.
3.	Fund for Promotion of Science and Technology in Pakistan.
4.	Fund for Retarded and Handicapped Children.
5.	National Trust Fund for The Disabled.
6.	Fund for Development of Mazaar of Hazrat Burri Imam.
7.	Rabita-e-Islami's Project for printing copies of the Holy Quran.
8.	Fatimid Foundation, Karachi.
9.	Al-Shifa Trust.
10.	Society for the Promotion of Engineering, Sciences and Technology in Pakistan.
11.	Citizens-Police Liaison Committee, Central Reporting Cell, Sindh Governor House, Karachi.
12.	ICIC Foundation.
13.	National Management Foundation.
14.	Endowment Fund of the institutions of the Agha Khan Development Network (Pakistan) listed in Schedule 1 of the Accord and Protocol, dated November 13, 1994, executed between the Government of the Islamic Republic of Pakistan and Agha Khan Development Network.
15.	Shaheed Zulfiqar Ali Bhutto Memorial Awards Society.
16.	Iqbal Memorial Fund.
17.	Cancer Research Foundation of Pakistan, Lahore.
18.	Shaukat Khanum Memorial Trust, Lahore.
19.	Christian Memorial Hospital, Sialkot.
20.	National Museums, National Libraries and Monuments or Institutions declared to Be National Heritage by the Federal Government.
21.	Mumtaz Bakhtawar Memorial Trust Hospital, Lahore.
22	Kashmir Fund for Rehabilitation of Kashmir Refugees and Freedom Fighters
23	Institutions of the Agha Khan Development Network (Pakistan) listed in Schedule 1 of the Accord and Protocol, dated November 13, 1994, executed between the Government of the Islamic Republic of Pakistan and Agha Khan Development Network
24	Azad Kashmir President’s Mujahid Fund, 1972
25	National Institute of Cardiovascular Diseases, (Pakistan) Karachi

26	Businessmen Hospital Trust, Lahore
27	Premier Trust Hospital, Mardan
28	Faisal Shaheed Memorial Hospital Trust, Gujranwala
29	Khair-un-Nisa Hospital Foundation, Lahore
30	Sind and Balochistan Advocates' Benevolent Fund
31	Rashid Minhas Memorial Hospital Fund
32	Any relief or welfare fund established by the Federal Government
33	Mohatta Palace Gallery Trust
34	Bagh-e-Quaid-e-Azam project, Karachi
35	Tameer-e-Karachi Fund
36	Pakistan Red Crescent Society
37	Bank of Credit and Commerce International Foundation for Advancement of Science and Technology
38	Federal Board of Revenue Foundation
39	The Indus Hospital, Karachi
40	Pakistan Sweet Homes Angels and Fairies Place
41	Al-Shifa Trust Eye Hospital
42	Aziz Tabba Foundation
43	Sindh Institute of Urology and Transplantation, SIUT Trust and Society for the Welfare of SIUT
44	Sharif Trust
45	The Kidney Centre Post Graduate Institute
46	Pakistan Disabled Foundation
47	Sardar Trust Eye Hospital, Lahore
48	Supreme Court of Pakistan–Diamer Bhasha & Mohmand Dams–Fund
49	Layton Rahmatullah Benevolent Trust (LRBT)
50	Akhuwat
51	The Prime Minister's COVID–19 Pandemic Relief Fund-2020
52	Ghulam Ishaq Khan Institute of Engineering, Sciences and Technology (GIKI)
53	Lahore University of Management Sciences
54	Dawat-e-Hadiya, Karachi
55	Baitussalam Welfare Trust
56	Patients' Aid Foundation
57	Alkhidmat Foundation
58	Alamgir Welfare Trust International
59	Prime Minister's Special Fund for victims of terrorism
60	Chief Ministers (Punjab) Relief Fund for Internally Displaced Persons (IDPs) of KPK
61	Prime Ministers Flood Relief Fund 2010 and Provincial Chief Ministers Relief Funds for victims of flood 2010
62	Waqf for Research on Islamic History, Art and Culture, Istanbul

63	All entities mentioned in Table – 1 of clause (66) of Part I of the Second Schedule of the Income Tax Ordinance
64	The Prime Minister's Relief Fund for Flood, Earthquake and Other Calamities with effect on and from the 5th August, 2022
65	Film and Drama Finance Fund

The Federal Government may add, amend or omit any entry in the Thirteenth Schedule.

CHAPTER-18
SET-OFF AND CARRY FORWARD OF LOSSES

SET-OFF OF LOSSES

Income tax is payable on the taxable income of taxpayer as determined under the provisions of the Income Tax Ordinance 2001.

The expression 'taxable income' is the total of the incomes of a taxpayer derived by him under all or any of the heads of income specified in section 11 of the Ordinance as reduced by the 'deductible allowance' admissible under the law.

The 'income' may be a profit, gain or loss from a source [2(29)]. Thus apparently the computation of 'total income' and thereafter, taxable income allows the automatic adjustment of losses under one head against the profits or gains under any other heads of income.

However, the law has specified a procedure for adjustment of losses sustained by a taxpayer during the tax year.

The adjustment of losses against the incomes under any head assessable for the same tax year is known as 'Set-off of Losses'.

Where a loss cannot be fully set-off against the incomes during that tax year is allowed to be adjusted against the incomes of future tax years, it is termed as 'Carry Forward of Losses'.

RULES FOR SET-OFF AND CARRY FORWARD OF LOSSES [56, 57, 58, 37A]

The table given below depicts the summary of the rules relating to set-off and carry forward of losses under the Income Tax Ordinance, 2001.

Heads of Income	Rules for Set-Off & Carry Forward
Salary	1. Section 12(4) specifies that no deduction shall be allowed while computing income under the head "Salary"; hence, there cannot be loss under this head.

	2. Salary income cannot be used to set-off the loss under any other head of income.
Income from Property	1. In is taxable under NTR and loss under this head may be set-off against income under any other head of income of the person for the tax year.
	2. It cannot be set-off against salary income of an individual.
	3. Loss under this head cannot be carried forward.
Business-Non-Speculation	1. Business loss may be set-off against any other income of the person for the year under NTR. However, it cannot be set-off against "Salary".
	2. Unadjusted business loss can be carried forward up to six (6) tax years and adjusted against income under the same head only.
	3. Business losses sustained by a resident company engaged in the hotel business in Pakistan for a tax year commencing on or after 01-07-2020 shall be carried forward for eight (8) years. 4. Adjustment of loss attributable to 'unabsorbed depreciation' has separate and distinct treatment (which is discussed later in this chapter).
Income from Other Sources:	1. Loss under this head may be set-off against any other income of the person for the year under NTR (Normal Tax Regime). However, it cannot be set-off against "Salary" or "Income from Property". 2. Unadjusted loss cannot be carried forward to succeeding tax years for adjustment.
Business - Speculation:	1. Speculative business loss can be set-off only against speculation gains during the tax year. 2. Speculative business loss can be carried forward up to six (6) tax years and shall be adjusted against income under the same head only.
Capital Gains (other than securities and immovable property):	1. Capital loss can be set-off only against capital gains during the tax year. 2. Capital loss can be carried forward up to six (6) tax years and shall be adjusted against income under the same head only.
Capital Gains - Securities:	1. Loss under this head can be set-off only against gain on the disposal of some other security. 2. Loss up to tax year 2018: Cannot be carried forward. 3. Loss for tax years 2019 and onwards: Can be carried forward up to three (3) immediately succeeding tax years and adjusted against gain on the disposal of securities.

Capital Gains - Immovable Property:	• Loss on the disposal of immovable property cannot be set-off or carried forward.
Capital Gains - (Loss on disposal of painting, sculpture, drawing, work of art, jewellery, rare manuscript, folio, or book, postage stamp, first day cover, coin, medallion or antique):	• Loss is not recognized under the Income Tax Ordinance, 2001. It means there will be no set-off or carry forward of loss on the disposal of such capital assets.
Foreign losses (of all types):	1. All foreign-source losses can be set-off and carried forward. 2. Foreign-source loss can be set-off against income under the same head of income only. 3. Foreign-source loss can be carried forward up to six (6) tax years for adjustment against income under the same head of income only.

Notes:

1. Above-discussed rules regarding set-off and carry forwarded of losses apply only to such incomes which are taxable under Normal Tax Regime (NTR). Any income which falls under Final Tax Regime (FTR) or Separate Tax Regime (STR) cannot be used for adjustment of losses under NTR.
2. The law does not permit any deduction while computing income under FTR or STR; hence, there cannot be loss under these modes of taxation.
3. Losses can be set-off only as provided above. Any loss that cannot be set off under the rules (e.g., loss on disposal of personal assets, etc.) cannot be carried forward. [56(2)]
4. Where a person sustains losses under different heads of income, including "Income from Business", the business loss shall be set off last, i.e., after setting off all other losses [56(3)].
5. The depreciation allowance admissible under the Third Schedule shall be charged up to that portion only which can be absorbed by the incomes. The general rules relating to set-off and carry forward of losses shall not apply to unabsorbed depreciation. Amount of such depreciation shall not be taken as a normal business loss rather, shall be treated separately. Treatment for unabsorbed depreciation is discussed in detail in the later part of this Chapter.

6. If an income from a source is exempt from tax, the loss, if any, from such source cannot be set-off or carried forward.

SET-OFF OF LOSSES OF COMPANIES OPERATING HOTELS [56A]

A public company (as defined in the Companies Act, 2017) shall be entitled to set-off its loss under the head "Income from Business" against its income in Pakistan, Gilgit-Baltistan or Azad Jammu and Kashmir (AJ & K), as the case may be, if the following conditions are satisfied:

1. The company is registered in Pakistan, Gilgit-Baltistan or AJ & K.
2. It is operating hotels in Pakistan, Gilgit-Baltistan or AJ & K, and
3. It sustains a loss in Pakistan, Gilgit-Baltistan or AJ & K for any tax year under the head "Income from Business".

CARRY FORWARD OF LOSSES

Where a loss cannot be set-off during the tax year in which it occurred, then it may be carried forward for adjustment against the incomes of the succeeding years. However, the taxpayer can carry forward only such losses which are assessable under the following heads only:

1. Non-speculation business.
2. Speculation business.
3. Capital gains.

Loss arising under any other head cannot be carried forward for set-off against the income of future years.

RULES FOR CARRY FORWARD

1. **Non-Speculation Business [57(1) & (2)]**

Any unadjusted loss from business can be carried forward for setting it off against the profits and gains under the head "Income from Business". This loss can be carried forward up to six (6) years immediately succeeding the tax year for which the loss was first assessed.

Business losses sustained by a resident company engaged in hotel business in Pakistan for tax year commencing on or after 01-07-2020 shall be carried forward for eight (8) years. [57(2B)]
Where 'business loss' is sustained by PIA during a tax year commencing on or after 01-01-2017, the loss shall be carried forward for ten (10) years. [57(2C)]
Where more than one tax year's losses are being carried forward, loss of the earliest tax year shall be set-off first. [57(3), 58(3) & 59(3)]
Any amount of 'unabsorbed depreciation' shall be allowed as deduction against the incomes of following tax years. And while setting-off the previous years' losses and unabsorbed depreciation, the losses shall be adjusted first and depreciation shall be taken into account last. [57(4) & (5)]

2. **Speculation Losses [58(2)]**

The losses sustained by taxpayer from a speculation business can be carried forward up to six (6) years for set-off against the profits and gains from the speculation business only.

3. **Capital Losses [59(2)]**

Any loss arising out of the disposal of a capital asset (other than 'securities' and immovable property) can be carried forward up to a period of six (6) years for set-off against the capital gains only in those years.

SET-OFF OF LOSSES IN CASE OF AMALGAMATION OF COMPANIES [57A]

1. The assessed loss for the tax year of the amalgamating company or companies shall be set-off against business profit and gains of the amalgamated company in the year of amalgamation. Capital loss and brought forward loss cannot be set-off.
2. Where the loss is not adjusted against the profits and gains for the tax year, then such loss shall be carried forward for adjustment up to a period of six (6) tax years succeeding the year of amalgamation. [57A(1)]
3. The amalgamating company likewise is also entitled to set-off the loss (other than brought forward and capital loss) of the amalgamated company. [57A(1)]
4. All provisions relating to the business losses and unabsorbed depreciation shall also be applicable to the losses of the amalgamating company being adjusted by the amalgamated company or vice versa. [57A(2)]
5. The business losses and unabsorbed depreciation shall be allowed to set-off or carry forward if the amalgamated company continues the business of the amalgamating company for a period of at least five (5) years from the date of amalgamation. [Proviso to 57A(2)]
6. In case of amalgamation of banking company, non-banking finance company, modaraba or insurance company, the accumulated business loss (excluding speculation business losses) of an amalgamating company or companies shall be set off or carried forward against the business income of the amalgamated company or vice versa. This can be done up to six (6) tax years immediately succeeding the tax year in which the loss was first computed.
7. The scheme of amalgamation is approved by the State Bank of Pakistan, SECP or any court. If any of the conditions of the scheme is not fulfilled, the set-off of loss or allowance for depreciation made in any tax year (by the amalgamated company) shall be deemed as its income for the tax year in which default is discovered by the tax authorities. The income shall be deemed of such a company which has set-off or carried forward the losses of another company. [57A (3)]

SET-OFF AND CARRY FORWARD OF LOSSES OF AOPS [59A & 56(2)]

An AOP, being taxable independent of its members, is entitled to set-off and carry forward its losses as other persons (i.e., individuals and companies) are entitled. As the share received by a member out of the incomes of an AOP is exempt from tax, the member is not allowed to set-off and carry forward his respective share in losses of the AOP. Only AOP can set-off and carry forward its losses in accordance with the rules specified in sections 56 to 59 of the Income Tax Ordinance.

LIMITATIONS AS TO SET-OFF OR CARRY FORWARD OF LOSSES [59A(3) & (4)]

1. A member of an association of persons (AOP) is not entitled to set-off or carry forward any share in losses sustained by AOP against his other incomes. This is due to the reason that the share in the income of such an AOP is exempt from tax.
2. Where a person has succeeded the business of any other person, he will not be entitled to carry forward and set-off against his income any loss sustained by that other person.

However, if the succession is by inheritance, then he is allowed to carry forward and set-off such losses.

CARRY FORWARD AND SET-OFF OF DEPRECIATION ALLOWANCE [57(4) & (5) & 59A(5) & (6)]

Depreciation and amortization admissible u/s 22, 23, 23B & 24 shall be taken into account last (i.e., after adjustment of all other deductions). While calculating the amount of loss to be carried forward, the total business loss is split into the following two categories:

1. Loss due to the business transactions; and
2. Loss due to the depreciation allowance as per Third Schedule.

The business loss is carried forward up to a maximum period of six (6) years. Whereas any portion of unabsorbed depreciation allowance shall be carried forward up to an indefinite period. [Circular No. 4 of 1979, dated 23-08-1979]

Whenever a taxpayer earns a profit from his business, it shall be utilized in the following manner:

1. Set-off the current losses from any other head of income which can be set-off, if any;
2. Set-off the carried forward business losses; and
3. Utilize any residual amount of profits for setting-off the unabsorbed depreciation.

Limitation on Adjustment of Unabsorbed Depreciation [57(4) & 59A (5)]

Loss attributable to 'unabsorbed depreciation' (u/s 22, 23, 23B & 24) shall be set off against fifty percent (50%) of the balance 'income from business' after setting off the loss from normal business activities. This procedure will continue until the amount of unabsorbed depreciation is fully set off.

However, where the taxable income of the person for the tax year is less than ten million rupees, the unabsorbed depreciation shall be set off against hundred percent (100%) of the balance income left after adjustment of carried forward business losses.

Example: 18.2

Year	Profit / (Loss) after Dep.	Depreciation For the Year	Profit/(Loss) Before Dep.	Carried Forward Business Loss	Carried Forward Unabsorbed Dep.	Taxable Income for the year
1	(60,000)	(20,000)	(40,000)	(40,000)	(20,000)	
2	(40,000)	(20,000)	(20,000)	(60,000)	(40,000)	
3	10,000	(20,000)	30,000	(50,000)	(40,000)	
4	60,000	(20,000)	80,000		(30,000)	
5	80,000	(20,000)	100,000			50,000

Accumulated loss to be carried forward is calculated as per the following:

Year - 2

Business loss = 40,000 + 20,000 = 60,000

Unabsorbed Depreciation = 20,000 + 20,000 = 40,000

Year - 3

Profit = 10,000

Business loss = 60,000 - 10,000 = 50,000

Unabsorbed Depreciation = 40,000

Year - 4

Profit = 60,000

Business loss = 50,000

Unabsorbed Depreciation = 40,000 - 10,000 = 30,000

Year - 5

Profit = 80,000

Unabsorbed Depreciation = 30,000 - 30,000 = 0

Taxable Income for the year = 80,000 - 30,000 = 50,000

FOREIGN LOSSES [104]

Where a resident person sustains a foreign loss (i.e., loss from a foreign-source income) he may set it off against his income under the same head of income.

If the foreign loss is not fully set-off then the loss shall be carried forward maximum up to six (6) tax years immediately succeeding the tax year during which the loss occurred.

Notes:

1. All foreign losses can be set-off and carried forward up to six (6) years.
2. The foreign losses are adjusted against the same head of income. For this purpose, the speculation business is treated as a separate head of income.
3. Where more than one tax years' losses are simultaneously carried forward, the loss of the earliest year shall be set-off first.

CARRY FORWARD OF LOSSES OF EXEMPT BUSINESS

The business income may be exempt from tax permanently or for a specific period (commonly known as tax holiday). A question arises that if a business has sustained a loss, then how it will be dealt with in taxation. Legal provisions in this regard are discussed in the coming paragraphs:

Business Permanently Exempt from Tax

Where a business is permanently exempt from tax, then there will be no need to determine the incomes under the Income Tax Ordinance. The taxpayer will ignore the provisions regarding the set-off and carry forward of losses. Such a person will maintain books of accounts and prepare the financial statements as per his own requirements.

Business Exempt for a Specific Period

A loss sustained during the exemption period may also be carried forward and set-off after the expiry of the exemption period. Where a business is enjoying a tax holiday, its losses (whether within or after the exemption period) can be carried forward as per normal procedure, i.e., up to a period of six years.

CHANGE IN CONTROL OF AN ENTITY [98]

Where there is a change of fifty percent (50%) or more in the underlying ownership of an entity then any loss incurred for a tax year before the change shall not be allowed as deduction (set-off) in the tax year after change.

However, the above provision shall not apply if the following conditions are fulfilled:

1. The entity continues to conduct the same business until the loss has been fully set off; and
2. The entity does not engage in any new business or investment after the change until the loss has been fully set off.

From the above it is evident that an entity may set-off its losses incurred prior to the change in underlying ownership if it continues to conduct the same business and if it does not engage in any new business or investment.

Entity means a company or an association of persons. [98(2)]

Underlying Ownership means an ownership interest in the entity held, directly or indirectly through an interposed entity or entities, by an individual or by a person not ultimately owned by individuals [98(2)]

Ownership Interest means a share in a company or the interest of a member in an Association of Persons. [98(2)]

LOSSES OF SUBSIDIARY COMPANY [56, 57 & 59B]

The losses of a subsidiary company may be set-off in any of the following ways:

1. Setting-off and carrying forward its losses by the subsidiary; or
2. Surrendering of losses by the subsidiary to its holding company for set-off.

Setting-off the losses by the Subsidiary [56 & 57]

A subsidiary is a separate legal person distinct from its holding company. It may set-off and carry forward its losses in the like manner as other persons are entitled (i.e., it may set-off the loss in the year of its occurrence and carry-forward the unadjusted loss up to a period of six (6) years.

Surrendering the Loss to Holding Company (i.e., Group Relief) [59B]

A subsidiary company may (instead of setting-off its losses against its incomes) surrender its assessed loss (excluding capital loss) for the year in favour of its holding company or another subsidiary or subsidiaries of the holding company. Other provisions in this regard are discussed **below:**

1. The loss which could be surrendered by a subsidiary company shall be in the proportion of the share capital held by the holding company in its subsidiary company. The amount of such loss shall be computed as below:
    - **Assessed Loss of Subsidiary × Percentage Share Capital of Holding in Subsidiary**
2. A subsidiary company cannot surrender its group losses to offset capital losses.
3. The holding company should directly hold at least such percentage of the share capital of the subsidiary company as given below:
    - **Fifty-Five percent (55%)**, where one of the companies in the group is a public company listed on a registered stock exchange in Pakistan; or
    - **Seventy-Five percent (75%)**, where none of the companies in the group is a listed company.
4. The surrendered loss may be claimed by the holding company or a subsidiary company for set-off against its 'Income from Business'.
5. The loss shall be set-off in the tax year of surrender and the following two tax years.
6. The loss can be set-off by the holding company or its subsidiary company if the following conditions are satisfied:

(i) There is a continued ownership for five years, of share capital of the subsidiary company at least 55%, in the case of a listed company, or 75%, in the case of other companies;

(ii) A company within the group engaged in the business of trading shall not be entitled to avail group relief;

(iii) A private limited company, being holding company with 75% of ownership of share capital should be itself listed within three (3) years from the year in which loss is claimed;

(iv) The group companies should be locally incorporated under the Companies Act, 2017;

(v) The loss being surrendered and claimed should be approved by the Board of Directors of the respective companies;

(vi) There should be no change in the business of the subsidiary company. It should continue the same business during the period of three years from the year in which loss is claimed;

(vii) All the group companies in the group should comply with the corporate governance requirements and group designation rules or regulations specified by the SECP, and any designated companies entitled to avail group relief;
(viii) Any other condition as may be prescribed by the Board.

7. A subsidiary company may surrender its losses for a maximum period of three tax years. Circular No. 1 of 2007, dated 02-07-2007 specifies that the three tax years shall be consecutive tax years.
8. In case the surrendered losses are not adjusted against the income of holding company in these three (3) years, the unused losses shall be reverted back to the subsidiary company. The subsidiary company can carry forward and set-off such losses as per normal procedure (i.e., within six years from the tax year to which the loss pertains).
9. Where the holding company's shareholding in the subsidiary is reduced below 75% during the period of five (5) years, the holding company's profit in the year of disposal shall be increased by the amount of losses set-off by it.
10. The company which is claiming the loss shall transfer cash to those surrendering company equal to the amount of tax payable on the profits to be set-off against the acquired loss. Cash shall be transferred after obtaining approval from the Board of Directors.
11. The transfer of cash would not be taken as a taxable event in the case of either of the two companies.
12. Transfer of shares between companies and shareholders in one direction, would not be taken as a taxable event if: (i) The purpose of transfer is to acquire capital for formation of the group; and (ii) Approval of the SECP or SBP, as the case may be, has been obtained.
13. Sale and purchase from third party would be taken as taxable event.

LOSSES UNDER 'GROUP TAXATION' [§9AA]

The concept of 'Group Taxation' was introduced by the Finance Act, 2007. Under this concept holding companies and subsidiary companies of 100% owned group may opt to be taxed collectively instead of individually. For this Purpose companies in the group shall have to give an irrevocable option for taxable as one fiscal unit. This option is available only to such companies which are incorporated under the Companies Act, 2017.

This option shall be available to those companies in the group which comply with the 'corporate governance' requirements and 'group designation rules or regulations' specified by the SECP. The group companies, besides consolidated financial statements (as required under the Companies Act, 2017), shall also compute consolidated income and tax payable by the group for the tax year. The 'Group Taxation' may be regulated through rules made by the Federal Board of Revenue.

If certain companies are allowed to be taxed as one fiscal unit, then for tax purposes all provisions relating to set-off and carry forward of losses shall also be applicable to these companies as one unit.
However, the relief under group taxation would not be available to losses prior to the formation of the group.

CHAPTER-19

PAYMENT OF TAX

The most important function of the tax department is to collect tax from taxpayers. In order to facilitate the authorities in performing this function, the Income Tax Ordinance, 2001 provides various provisions and imposes an obligation on the taxpayers to comply with these provisions. The payment of tax may be categorized under the following headings:

1. Deduction or collection of tax at source;
2. Advance payment of tax;
3. Payment of tax while filing the "return of income";
4. Payment of tax on the demand of the tax authorities; and
5. Recovery through 'tax recovery procedure', if taxpayer fails to pay tax on demand.

The provisions of the Ordinance relating to each category are briefly discussed in the coming paragraphs.

DEDUCTION OR COLLECTION OF TAX AT SOURCE [148 & 158]

'Tax at source' means the collection or deduction of tax at the source from where income or a transaction is being generated or executed. In some countries it is termed as 'pay-as-you-earn' (PAYE). The tax so deducted or collected is also known as 'withholding tax'.
Part-VI of Chapter-X (Advance Tax and Deduction of Tax at Source) and Chapter-XIII (Transitional Advance Tax Provisions) of the Income Tax Ordinance, 2001, which deal with the deduction or collection of tax at source, are the most powerful parts of the Ordinance and are the biggest source of income tax collection under the law. Originally the tax collected or deducted at source was considered as an advance payment of tax on behalf of the taxpayer. But, afterwards, the provisions relating to 'withholding tax' were gradually split into two segments, whereby the tax deducted or collected is:

1. Treated as advance tax and adjustable against tax liability of the taxpayer; and
2. Considered as a full and final discharge of tax liability of the taxpayer in respect of the transaction against which the deduction was made.

All related provisions of the Income Tax Ordinance, 2001 have been summarized in a table appearing in the coming pages.

Deduction or Collection of Tax at Source

(Part-V of Chapter-X and Chapter-XII of the Income Tax Ordinance, 2001)

SEC.	NATURE OF PAYMENT TRANSACTION	TAX RATES	EXEMPTION LIMIT	STATUS OF PAYMENT OR DEDUCTION	TAX WITHHOLDING AGENT	TIME OF DEDUCTION OR COLLECTION
1	Import of goods specified in Twelfth Schedule:					
	Part-I Import by commercial importer	3.5% of the value	Nil	Generally, tax paid on import of goods shall be	Collector of Customs	Clearance of goods
	Part-II Import by other persons	2% of the value	Nil	minimum on income of the goods imported.		
	Part-III Import by commercial importer	5.5% of the value	Nil	Under certain specified cases, tax paid at the		
				import stage shall be adjustable.		
2	Manufacturers of goods specified in mentioned SRO	1% of the value		[See Notes]		

	(SRO 1125/2011 dated 13-12-2011) relating to live					
	livestock, etc., (excluding jute, textiles, cotton, etc.)					
3	Import of finished pharmaceutical products that are not	4%				
	manufactured in Pakistan and certified by DRAP					
4	Import of CKD kits of electric vehicles for small cars or	1%				
	SUVs with 50kW battery or below and LCVs with 150 kW battery					
5	Import of mobile phone by any person					
Tax (in Rs.)						
C&F Value in US $						
Up to 30	700					
31 to 100	1,200					

101 to 300	2,500					
301 to 350	3,000					
351 to 500	5,000					
Exceeding 500	11,500	5,200				

149	**Salary**	Average rate of tax Rs. 600,000		Adjustable	Person responsible for paying salary	Payment
149	**Directorship fee or fee for attending board meeting, etc.**	20% of gross amount payable	Nil	Adjustable	Person responsible for making payment	Payment
150	**Dividends (including dividend in specie):**					
	Dividend Received From:					
	Independent Power Producers	7.5% of gross dividend		Adjustable	Person paying dividend	Payment
	Mutual funds	15% of gross dividend		Adjustable	Person paying dividend	Payment
	Mutual funds deriving 50% or more income from profit on debt	25% of gross dividend		Adjustable	Person paying dividend	Payment
	Real Estate Investment Trusts (REIT)	15% of gross dividend		Adjustable	Person paying dividend	Payment
	Special Purpose Vehicle - Received by REIT Scheme	0%	Nil	Adjustable	Person paying dividend	Payment
	Special Purpose Vehicle - Received by other than REIT Scheme	35% of gross dividend		Adjustable	Person paying dividend	Payment
	In case of a person receiving dividend from a company where no tax is payable due to exemption or carry forward of business losses or tax credits	25% of gross dividend		Adjustable	Person paying dividend	Payment
	Any other person	15% of gross dividend		Adjustable	Person paying dividend	Payment
151	**Profit on Debt**					

	Yield or profit on an account, deposit, or certificate paid to a resident person	15% of gross amount	See Notes	Minimum Tax	Payer	Payment or credit of profit to the account
	Paid to a person not appearing in Active Taxpayer List	35% of gross amount		Minimum Tax	Payer	
	Return on investment in sukuks to a sukuk-holder	25% of gross amount	Nil	Adjustable	SPV or a Company	Payment
	Company					
	Individual or AOP - Return on investment less than Rs. 1,000,000	10% of gross amount	- do -	Minimum Tax	- do -	- do -
	Individual or AOP - Return on investment more than Rs. 1,000,000	12.5% of gross amount	- do -	Minimum Tax	- do -	- do -
152	**Payments to Non-Residents (1)**					
	Royalty & Fees	15% of gross amount	Nil	Final Tax	Prescribed person	Paymen
1A)	Payment for construction, assembly, or installation projects or services relating to advertisement by TV-Satellite Channels	7% of gross amount	Nil	Minimum Tax	Prescribed person	Payment
(1AA)	Payment of insurance premium or re-insurance premium	5% of gross amount	Nil	Minimum Tax	Prescribed person	Payment
(1AAA)	Payment for advertisement services relaying from outside Pakistan	10% of gross amount	Nil	Minimum Tax	Prescribed person	Payment
(1BA)	Payment for foreign produced commercial for advertisement on any television channel or other media	20% of gross amount	Nil	Final Tax	Person responsible for making payment	Payment
(1C)	Remittance outside Pakistan of fee for offshore digital services to a non-resident on behalf of a resident or PE of a non-resident	10% of the gross amount	Nil	Final Tax	Banking company or a financial institution	Remittance abroad

(1D)	Capital gain on disposal of debt instruments and government securities including treasury bills and Pakistan investment bonds invested by a company through special convertible rupee account (SCRA) maintained with banks and financial institutions	10% of capital gain	Nil	Final Tax	Banking company	Disposal of securities
(1DA)	Capital gain on disposal of debt instruments and government securities and certificates	10% of capital gain	Nil	Final Tax	Banking company	Disposal of securities
(1DB)	Return on investment in Sukuks	As mentioned under section 151	Nil	Final Tax	SPV or Company	Payment
(1DC)	Payment (by a licensed exchange company) of service charges or commission or fee to the global money transfer operators, international money transfer operators, or other persons engaged in international money transfers or cross-border remittances for facilitating outward remittances	10%	Nil	Final Tax	Licensed exchange company	Payment
(1DD)	Payment by a banking company to card network company or payment gateway or any other person, of any transaction fee or licensing fee or service charges or commission or fee by whatever name called or interbank financial telecommunication services	10%	Nil	Final Tax	Banking company	Payment
(2)	All other payment to non-resident	20% of the gross amount	Nil	Adjustable	Prescribed person	Payment
(2A)	Payment to PE: For sale of goods	Nil	Minimum tax, but it will be adjustable if received		Prescribed person	Payment

(In case of a company)	-	5% of gross amount	-	-	-

In any other case	-	5.5% of gross amount	-	-	-
For services relating to:	Freight forwarding, air cargo, courier, manpower outsourcing, hotel services, security guard, software development, IT and IT-enabled services, tracking, advertising, share registrar, engineering, car rental, building maintenance, services rendered by Pakistan Stock Exchange Ltd., Pakistan Mercantile Exchange Ltd., inspection and certification, testing, and training services	4% of gross amount	Minimum tax	Prescribed person	Payment
For all other services:	In case of a company	9% of gross amount	-	Prescribed person	Payment
	In any other case	11% of gross amount	-	Prescribed person	Payment
For execution of contracts:	In case of sports persons	10% of gross amount	-	Prescribed person	Payment
	Other persons	8% of gross amount	-	Prescribed person	Payment
153 Sale of Goods (Including Toll Manufacturing)					

(1)(a) Rice, cotton seed oil or edible oil	1.5% of sale value	-	Prescribed person	Payment	
Local sales, supplies, and services provided to taxpayers of the following sectors:	Textile and its articles	1%	Minimum tax	Prescribed person	Payment
	Carpets	1%	Minimum tax	Prescribed person	Payment
	Leather and its articles (including artificial leather footwear)	1%	Minimum tax	Prescribed person	Payment
	Surgical goods	1%	Minimum tax	Prescribed person	Payment
	Sports goods	1%	Minimum tax	Prescribed person	Payment
Local sales, supplies, and services provided by yarn traders to taxpayers of the above five sectors	0.5%	-	Prescribed person	Payment	
Sale of goods (including Toll Manufacturing)					
In case of a company:	For toll manufacturing	9%	-	Prescribed person	Payment
	For other than toll manufacturing	5%	-	Prescribed person	Payment
In any other case	- For toll manufacturing	11%	-	-	-
	- For other than toll manufacturing	5.5%	-	-	-

Supplies by distributors of cigarettes (Clause (24A), Part-II of 2nd Schedule)	2.5% of gross payment	-	-	-	Payment
Supplies by distributors of cigarettes and pharmaceutical products and for large distribution houses (Clause (24A), Part-II of 2nd Schedule)	1% of gross amount	-	-	-	Payment
Dealers and sub-dealers of sugar, cement, and edible oil as recipient (Clause (24C), Part-II of Second Schedule)	0.25% of gross amount	-	-	-	Payment
Payment for sale of gold and silver and articles (Clause (31), Part-II of Second Schedule)	1% of gross amount	-	-	-	Payment
Rendering of Services (For specified services)	4% of gross amount	Less than Rs.75,000 during a financial year	Minimum Tax	-	Payment
For all other services:	-	-	-	-	-
- In case of a company	9% of gross amount	-	-	-	Payment
- In any other case	11% of gross amount	-	-	-	Payment
Payments to electronic and print	1.5%	-	-	-	Payment

media for advertising services					
Oil tanker contractor services (Clause (28F), Part-II of Second Schedule)	2%	-	-	-	Payment
Execution of Contracts	-	-	-	-	-
- In case of a company	7.5%	-	-	-	Adjustable
- In any other case	8%	-	-	-	Adjustable
- In case of sports persons	10%	-	-	-	Adjustable
Payment by exporter or an export house to a resident or PE of a non-resident for services of stitching, dying, printing, embroidery, washing, sizing, and weaving	1%	-	Exporter or an export house	Payment	
Export proceeds realization	1% of the proceeds of Nil	Minimum Tax	Authorized dealer in foreign exchange	Export proceeds realization or at	
Realization of a sale of goods to an exporter under	1% of the proceeds of Nil	Minimum Tax	Banking company	Payment	

(3A)	Export of goods by industrial undertaking in EPZ	1% of the proceeds of export	Nil	Export Processing Zone Authority	The time of export of goods if made by an undertaking in EPZ

(3B)	Making payment for a firm contract to an 'indirect export'	1% of the proceeds of export	Nil	Direct exporter and export house registered under DTRE Rules, 2001 and Export Facilitation Scheme, 2021	Export Facilitation Scheme
(3C)	Clearing of goods exported	1% of the proceeds of export	Nil	Collector of Customs	Realization of foreign exchange proceeds
Commission to an indenting commission agent	5% of the commission due	Nil	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds	
154A	Realization of foreign exchange proceeds on account of following services exported or rendered outside Pakistan:				
i)	Computer software or IT services or IT-enabled services certified by PSEB	0.25% of proceeds	Nil	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds

ii)	Services or technical services	Nil	Final Tax	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds
iii)	Royalty, commission, or fees derived by a resident company from a foreign enterprise for services outside Pakistan	1% of proceeds	Nil	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds
iv)	Construction contracts executed outside Pakistan	1% of proceeds	Nil	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds
v)	Foreign commission due to an indenting agent	1% of proceeds	Nil	Authorized dealer in foreign exchange	Realization of foreign exchange proceeds
Any other services (notified by FBR) rendered outside Pakistan	As given in the notes	Adjustable	-	-	Payment
(155)	Rent of immovable property	15% of gross amount	Nil	Person making the payment	Payment
(156)	Prizes on prize bonds or cross-word puzzle	15% of gross amount	Nil	Person making the payment	Payment
Winnings from a raffle, lottery, quiz,	20% of gross amount	Nil	Person making the payment	Payment	

prize offered by					

156A	Sale of petroleum products to petrol pump operators	12% of the amount or commission/discount	Nil	Person selling the petroleum products	Payment
231A	Cash withdrawal from banks	0.6% of cash withdrawn Rs. 10,000 per day	Adjustable	Banking company	Cash withdrawal
231B	**Motor Vehicles**: Registration of motor vehicle	-	-	-	-
(1)	**Upto 850 cc**	0.5% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(2)	**851 cc - 1000 cc**	1% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(3)	**1001 cc - 1300 cc**	1.5% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(4)	**1301 cc - 1600 cc**	2% of the value	Nil	Government (Federal,	Registration

				Provincial, Local, Diplomatic Mission in Pakistan)	
(5)	**1601 cc - 1800 cc**	3% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(6)	**1801 cc - 2000 cc**	5% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(7)	**2001 cc - 2500 cc**	7% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(8)	**2501 cc - 3000 cc**	9% of the value	Nil	Government (Federal, Provincial, Local, Diplomatic Mission in Pakistan)	Registration
(9)	**Above 3000 cc**	12% of the value	Nil	Government (Federal, Provincial, Local,	Registration

				Diplomatic Mission in Pakistan)	
(1A)	Leasing or ijara of vehicles to non-filer by leasing companies, banks, NBFIs, Investment banks, modarabas or DFIs	4% of the value of vehicle	Nil	Leasing company, bank, DFIs, modaraba	Lease
(2)	Transfer of registration or ownership	-	-	-	-
(1)	**Upto 850 cc**	Rs. 5,000	Nil	Motor Vehicle Registering Authority	Registration of transfer
(2)	**851 cc - 1000 cc**	Rs. 7,500	Nil	Motor Vehicle Registering Authority	Registration of transfer
(3)	**1001 cc - 1300 cc**	Rs. 12,500	Nil	Motor Vehicle Registering Authority	Registration of transfer
(4)	**1301 cc - 1600 cc**	Rs. 18,750	Nil	Motor Vehicle Registering Authority	Registration of transfer
(5)	**1601 cc - 1800 cc**	Rs. 25,000	Nil	Motor Vehicle Registering Authority	Registration of transfer
(6)	**1801 cc - 2000 cc**	Rs. 37,500	Nil	Motor Vehicle Registering Authority	Registration of transfer
(7)	**2001 cc - 2500 cc**	Rs. 50,000	Nil	Motor Vehicle Registering Authority	Registration of transfer

(8)	**2501 cc - 3000 cc**	Rs. 50,000	Nil	Motor Vehicle Registering Authority	Registration of transfer
(9)	**Above 3000 cc**	Rs. 62,500	Nil	Motor Vehicle Registering Authority	Registration of transfer
(2A)	Locally manufactured motor vehicle sold prior to registration	-	-	-	-
(1)	**Upto 1000 cc**	Rs. 10,000	Nil	Motor Vehicle Registering Authority	Registration of transfer
(2)	**1001 cc to 2000 cc**	Rs. 20,000	Nil	Motor Vehicle Registering Authority	Registration of transfer

Sale of vehicles by manufacturer	Rs. 2001cc and above	Rs. 400,000	Nil	Manufacturer	Sale
Foreign national domestic workers (From Agency, sponsor, or person employing worker)	Rs. 20,000	Nil	Visa issuing or renewing authority	Visa issuing or renewing	
Brokerage & Commission					
In case of advertising agents	10% of the amount of payment	Nil	Government (Federal, Provincial, Local), Company, AOP, individual with turnover of Rs. 100 million or more	Payment	
Life Insurance Agents (where annual commission received	8% of the amount of payment	Nil	Government (Federal, Provincial, Local)	Minimum Tax [See Notes]	

is less than Rs. 500,000)					
In all other cases	12% of the amount of payment	Nil	Government (Federal, Provincial, Local)	Minimum Tax [See Notes]	
Person running 'online marketplace'	5% of the amount of payment	Nil	Government (Federal, Provincial, Local)	Adjustable	
Motor Vehicles					
Goods transport vehicles (laden weight of 8,120 Kgs or more, tax after 10 years from first registration)	Rs. 1,200	Nil	Collection of motor vehicle tax	Adjustable	
Passenger transport vehicles (with registered seating capacity)					
Non-Air conditioned:					
- Up to 9 persons	Rs. 200 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 10 to 19 persons	Rs. 500 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 20 and above	Rs. 1,000 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	
Air conditioned:					
- Up to 9 persons	Rs. 375 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 10 to 19 persons	Rs. 750 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	

- 20 and above	Rs. 1,500 per seat p.a.	Nil	Collection of motor vehicle tax	Adjustable	
Other motor vehicles (Annual collection of tax):					
- Up to 1000 cc	Rs. 10,000 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 1000cc to 1199cc	Rs. 15,000 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 1200cc to 1299cc	Rs. 18,000 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 1300cc to 1499cc	Rs. 22,500 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 1500cc to 1599cc	Rs. 37,500 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 1600cc to 1999cc	Rs. 45,000 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
- 2000cc and above	Rs. 100,000 p.a.	Nil	Collection of motor vehicle tax	Adjustable	
Lump sum collection of tax:					
- Up to 1000 cc	Rs. 10,000	Nil	Collection of motor vehicle tax	Adjustable	
- 1000cc to 1199cc	Rs. 16,000	Nil	Collection of motor vehicle tax	Adjustable	
- 1200cc to 1299cc	Rs. 20,000	Nil	Collection of motor vehicle tax	Adjustable	