



TAX UPDATE

An Update on
Taxability of Salary

*Under the Income Tax Ordinance, 2001 & Income Tax Rules, 2002
(Applicable w.e.f. July 1, 2012, as amended vide the Finance Act, 2012)*



Table of contents

	Page
What this document aims at?	1
Significant changes vide the Finance Act, 2012	1
Exempt allowances & benefits	2
Taxable allowances & benefits	2
Allowable deductions	3
Tax credits	3
Annual return & wealth statement	4
Exemption limit	4
Tax rates	4
Reduction in tax liability	4
Worked examples – Comparison of tax liability as per new and previous rates	5

What this document aims at?

The purpose of this document is to briefly summarize the concept of computation of income from salary and computation of tax thereon under the Income Tax Ordinance, 2001 and Income Tax Rules, 2002, taking into account the amendments vide the Finance Act, 2012 (the Act).

The information and elaborations as contained herein are general in nature and based on our interpretation of the applicable statute and significant amendments vide the Act, becoming effective for the Tax Year 2013.

As such nothing contained herein should be taken as legal advice in a given case and Tariq Abdul Ghani Maqbool & Co. does not accept any responsibility for any loss arising from any action taken or not taken based on this document.

July 2, 2012

Significant changes vide the Finance Act, 2012

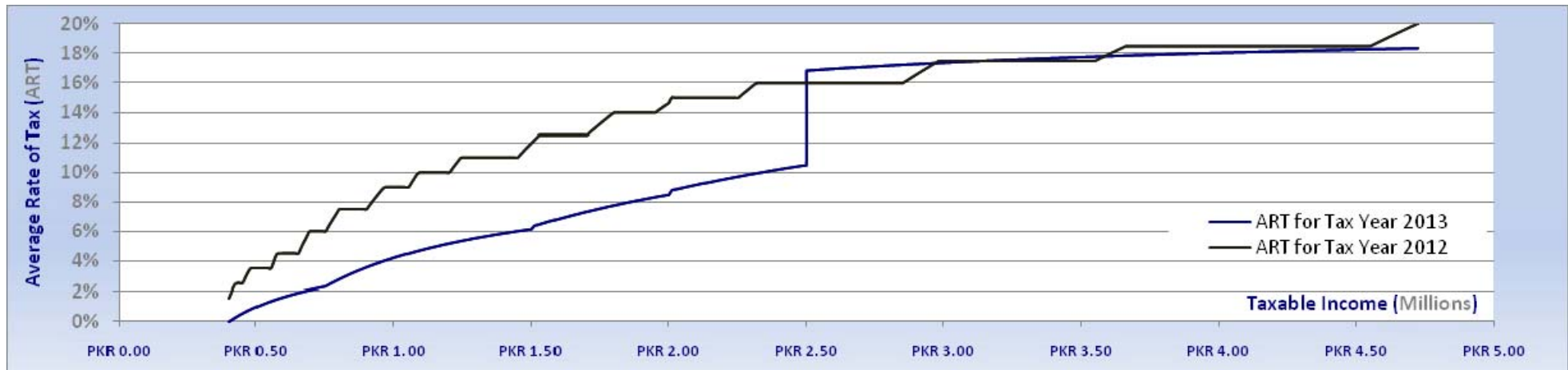
Relief Measures

Basic Exemption Limit for salaried taxpayers has been increased to Rs. 400,000 from existing Rs. 350,000.

The table of tax rates has been revised generally yielding a **General Reduction in Tax Incidence**.

Deemed income on concessional loan to employees not to be computed for loans up to Rs.500,000. Further, the **benchmark rate** for computing such deemed income has been fixed at 10%.

Limits for **tax credit in respect of investment in shares and life insurance premia** relaxed from existing 15% to 20% of taxable income and monetary threshold increased to Rs.1,000,000 from existing Rs.500,000.



Exempt allowances & benefits

Description	Condition/ Limit
Medical benefit or reimbursement*	Medical facility or hospital charges* are fully exempt, if provided in accordance with the terms of employment. * Exemption is available only when NTN of the hospital or clinic is disclosed and the employer certifies and attests the bills.
Medical Allowance (without medical facility)	Exempt up to 10% of basic salary.
Special allowance or benefit (other than entertainment or conveyance allowance)	If granted to meet expenses wholly and necessarily incurred in the performance of duties is fully exempt.
Employer's contribution to provident fund	Exempt up to lower of Rs.100,000 and 10% of salary, such that the amount does not exceed employee's contributions.
Gratuity/ superannuation/ Commutation of Pension (received in Pakistan by residents)	On retirement/ death
	Receipts from
	Treatment
	Approved Funds Fully Exempt
	Approved Schemes Exempt up to Rs.200,000
	Other cases
	Exempt up to lower of 50% of the amount or Rs. 75,000. Residual amount to be taxed at the current rate of tax.
Pension	Fully exempt, where the person does not continue to work for the same employer or an associate of the employer. In case of pensions from more than one source, the pension representing the highest amount would be exempt.

Taxable allowances & benefits

Few of the prominent and common items in this list include:

Description	Remarks
Utilities allowance (water, gas, electricity allowance)	Fully Taxable
House rent allowance	Fully Taxable
Accommodation (whether furnished or not)	45% of basic salary to be included in taxable salary.
Leave fare assistance	Fully Taxable
Salary of domestic servant (house-keeper, gardener, etc.)	Fully Taxable
Capital receipt on termination of employment	Fully chargeable to tax
Tax paid by the employer	Salary is to be grossed-up by tax paid by the employer on behalf of the employee.
Interest-free loans to employees or loans at concessional rates	The concession, being the difference between the benchmark rate and the lower rate charged, is taxable. The benchmark rate has been fixed at 10% w.e.f July 1, 2012. However, the concession is not taxable in case: a. the amount of loan is up to Rs.500,000; or b. where the employee waives interest on his account with the employer.
Conveyance allowance	Fully taxable
Motor vehicle (owned and maintained by employer)	Partly for private use: Taxable at 5% of cost/ FMV at the time of commencement of lease. Wholly for private use: Taxable at 10% of cost/ FMV at the time of commencement of lease.

Taxable allowances & benefits (Contd.)

Description	Remarks
Waiver of loan by the employer	Fully taxable
Discharge of debt by employer	Fully taxable
Transfer of assets or property	To be included in income of the employee at fair market value less value of consideration paid.
Employee share scheme	<p>Value of right/ option under an Employee Share Scheme is not chargeable to tax until:</p> <p>(a) the right/ option is disposed; or</p> <p>(b) shares are acquired.</p> <p>Amount taxable against disposal of right/ option is the difference between:</p> <p>(a) consideration for right/ option; and</p> <p>(b) cost in respect of said right/ option.</p> <p>Amount taxable at acquisition of shares is difference between:</p> <p>(a) fair value of shares; and</p> <p>(b) sum paid against acquisition of shares.</p> <p>If shares acquired are under restriction as to transfer, the amount is taxable only at the earlier of:</p> <p>(a) acquisition of transfer rights; or</p> <p>(b) at the time of actual disposal of shares.</p>

Allowable deductions The following payments are exempt from tax by way of reduction of taxable income:

Description	Eligibility Criteria	Limit
Donations	Paid to institutions, foundations, societies, boards, trusts and funds as per Clause (61) Part-I of 2nd Schedule to the Income Tax Ordinance	Up to 30% of taxable income
Zakat	Paid or deducted under the Zakat and Ushr Ordinance	100% (i.e. the full amount of zakat)

Tax credits

Certain tax credits are also available against specified items as per the following formulae:

$$\text{Applicable Amount}^* \times \frac{\text{Tax before allowing tax credit(s)}}{\text{Taxable income for the tax year}}$$

Specified Items for Tax Credit				
* Applicable Amount (lower of)	Charitable donations - Note1	Investment in shares & Insurance premium - Note2	Contribution to approved pension fund	
	Profit on debt on loans for purchase or construction of house - Note4			
	Amount of donation or fair value of property donated	Cost of acquisition 20% of taxable income	Actual annual contribution made	Amount paid 50% of taxable income
	30% of taxable income	Rs. 1,000,000/-	20% of taxable income - Note3	Rs. 750,000/-

Note1: Includes donations not covered under 2nd Schedule if made to:

- local education boards/ universities established under Federal/ Provincial law;
- educational institution/ hospital/ relief fund established/ run in Pakistan by Federal/ Provincial Govt. or local authority; or
- approved non-profit organizations.

Tax credits (Contd.)

Note2: In case of **investments**, the entitlement is restricted to original allotments of listed shares and acquisition of shares from the Privatization Commission of Pakistan and being held for a period of 24 months. In case of **insurance premium**, the benefit is restricted to life insurance premium paid to insurance companies registered with SECP.

Note3: Additional contribution allowed to persons joining a fund up to June 30, 2016, if the age at joining is 41yrs or above. The said additional contribution is allowed at 2% for each year exceeding the age of 40 years such that the applicable amount does not exceed 50% of last year's taxable income.

Note4: Profit on debt means profit/ share in rent and appreciation in value of house paid to banks, financial institutions, government, local authority, statutory body or listed company. This implies that loan from employer is also covered if it is a listed company or statutory body.

Annual return & wealth statement

Case	Filing Requirement	Timeline for Filing
Where salary income is less than Rs.500,000 and there is no other source of income	No need for any tax filing, since the Annual Statement filed by the employer constitutes the tax return	N/A
Where salary income is less than Rs.500,000 and the taxpayer also has income/ loss from any other source	(A) In case the total income is less than Rs.1Million, the taxpayer needs to file annual tax return manually (B) In case the total income is Rs.1Million or more, the taxpayer needs to file annual tax return manually and a wealth statement	30 th day of September falling next to the tax year
Where salary income is Rs.500,000 or more (irrespective of the fact whether or not there are some other income sources)	The taxpayer needs to electronically file the annual tax return along with a wealth statement	31 st day of August falling next to the tax year

Exemption limit

Income up to **Rs. 400,000** is exempt from tax.

Tax rates

Taxable Income (Rupees)		Rate of Tax	
From	To		
Up to 400,000			0%
400,001	750,000		5% of the amount exceeding Rs. 400,000
750,001	1,500,000	17,500	10% of the amount exceeding Rs. 750,000
1,500,001	2,000,000	95,000 *	15% of the amount exceeding Rs. 1,500,000
2,000,001	2,500,000	175,000 *	17.5% of the amount exceeding Rs. 2,000,000
Above 2,500,000		420,000 *	20% of the amount exceeding Rs. 2,500,000

* These amounts are shown as appearing in the Finance Act, 2012 and, accordingly, we have worked our examples based on these amounts. It is, however, noticeable that these amounts are higher than those worked-out by applying related rates to higher bracket as per previous slab. The difference in amounts is given as under:

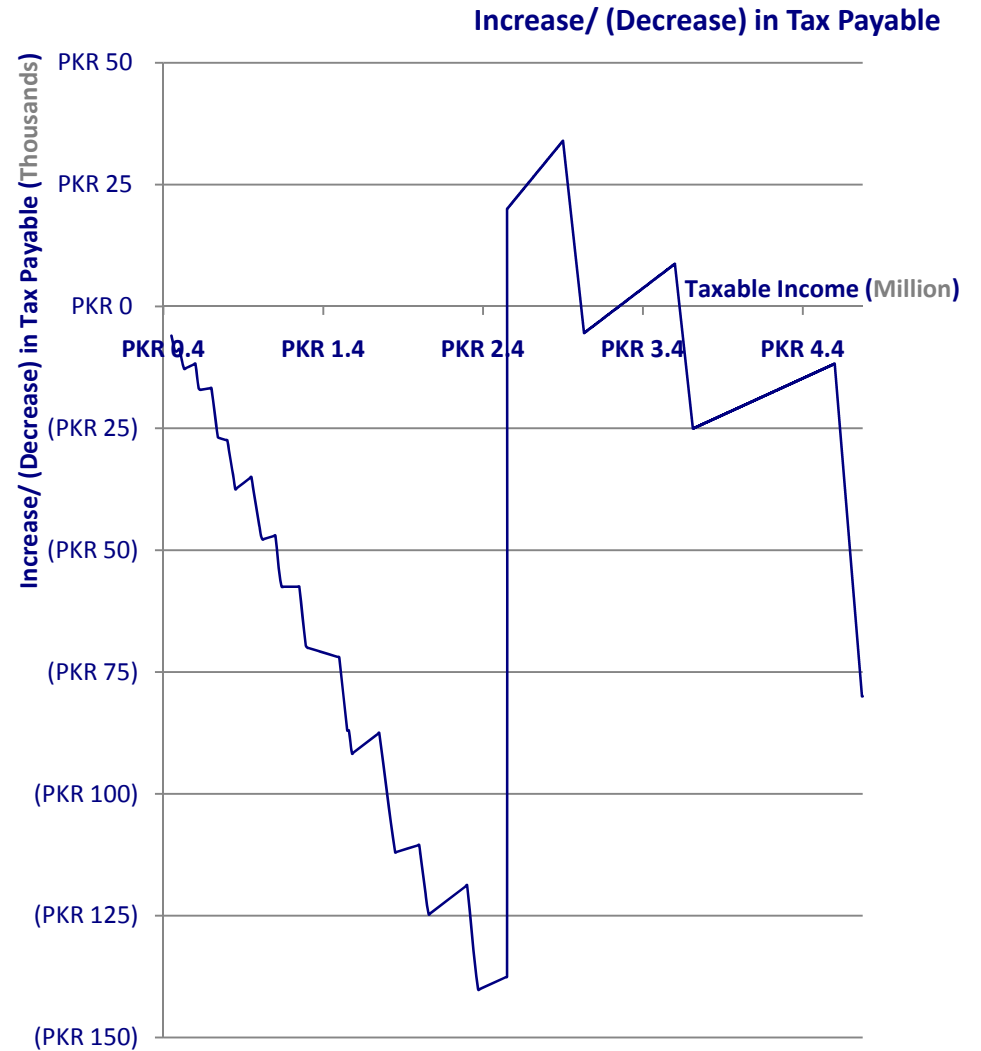
Amount as per Table	Amount Worked-out	Difference
*95,000	92,500	2,500
*175,000	167,500	7,500
*420,000	255,000	165,000

Reduction in tax liability

Applicability	Rate of Reduction	Eligibility criteria
Senior citizens	50%	Age to be 60 yrs or more on the first day of tax year and income does not exceed Rs.1,000,000/-
Full time teachers & researchers	75%	Employed in a recognized non profit education or research institution (including government training & research institutions)

Worked examples – Comparison of tax liability as per new and previous rates

Taxable Income	Tax Payable		
	As per New Rates	As per Previous Rates	Increase/ (Decrease)
	All amounts in Rupees		
400,000	0	6,000	(6,000)
500,000	5,000	17,500	(12,500)
600,000	10,000	27,000	(17,000)
750,000	17,500	45,000	(27,500)
755,000	18,000	46,500	(28,500)
1,100,000	52,500	110,000	(57,500)
1,300,000	72,500	143,000	(70,500)
1,500,000	92,500	179,500	(87,000)
1,600,000	110,000	200,000	(90,000)
1,800,000	140,000	252,000	(112,000)
2,000,000	170,000	293,000	(123,000)
2,010,000	176,750	297,000	(120,250)
2,250,000	218,750	337,500	(118,750)
2,500,000	262,500	400,000	(137,500)
2,525,000	425,000	404,000	21,000
2,575,000	435,000	412,000	23,000
3,400,000	600,000	595,000	5,000
3,500,000	620,000	612,500	7,500
4,000,000	720,000	740,000	(20,000)
4,550,000	830,000	841,750	(11,750)



An Update on Taxability of Salary as Amended vide the Finance Act, 2012

Under the Income Tax Ordinance, 2001 & Income tax Rules 2002 (Applicable w.e.f. July 1, 2012)