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International Tax
Pakistan Highlights 2020

Updated January 2020

Recent developments:

For the latest tax developments relating to Pakistan, see Deloitte tax@hand.

Investment basics:

Currency – Pakistan rupee (PKR)

Foreign exchange control – Foreign exchange regulations are issued and administered by the state bank of Pakistan. There generally are no restrictions on the repatriation of income or capital.

The Tax Laws (Second Amendment) Ordinance 2019 introduced amendments to encourage investment in the local debt market and simplify the tax regime for nonresident companies.

Accounting principles/financial statements – IFRS and the Companies Act 2017 apply. All public companies and private limited companies with paid-up capital of PKR 10 million or more must file annual financial statements with the Securities and Exchange Commission of Pakistan.

Principal business entities – These are the limited liability company, partnership, and branch of a foreign entity.

Corporate taxation:

Rates	
Corporate income tax rate	29% (in general)
Branch tax rate	29% (in general), plus 15% withholding tax on remittances of profits to head office
Capital gains tax rate	See under “Capital gains,” below

Residence – A company is resident if it is incorporated under the laws of Pakistan or if its management and control are situated wholly in Pakistan.

Basis – A resident company is taxed on Pakistan-source and foreign-source income at the corporate tax rate. Nonresidents are taxed only on Pakistan-source income.

Branches of foreign companies are treated as nonresidents for Pakistan tax purposes and are subject to tax on income attributable to the Pakistan branch. The tax rates are same as for a subsidiary; however, branches can claim a deduction for head office expenses, but may not claim a deduction for certain amounts paid to the head office or associates of the head office, such as interest, royalties, and technical service fees.

Taxable income – Income generally is taxed under five "heads of income," i.e., business income, rental income, capital gains, salary income, and income from other sources. Business income of a resident entity or a permanent establishment (PE) of a nonresident entity is taxed on a net taxable income basis.

The final tax regime applicable with respect to various streams of income has been replaced with the "minimum tax regime" (with the exception of exports, dividends, prizes and winnings, and sales of petroleum products, etc.). See "Alternative minimum tax," below.

Rate – The corporate tax rate is 29% for the 2020 tax year and is imposed on the net taxable income of a company. Small companies, however, are taxed at a 23% rate that gradually will be reduced by 1% annually until tax year 2023.

Surtax – There is no surtax.

Alternative minimum tax – A minimum tax on turnover of 1.5% applies on the declared turnover of a resident company and other specified taxpayers. The minimum tax is applicable where taxpayers suffer losses or the tax yield on income is less than 1.5% of turnover.

An alternative corporate tax of 17% of "accounting income" applies. The tax liability of a company is calculated as the higher of the alternative corporate tax or the total corporate tax payable (including the tax on net taxable income, minimum tax, and final taxes).

Taxation of dividends – A resident entity pays tax at a rate of 15% on dividend income, with following exceptions:

- The rate is 7.5% for dividends paid by "independent power purchasers, where the dividend is a pass-through item and is to be reimbursed under the agreement; and
- The rate is 25% if no income tax is payable by the payer company due to a tax exemption, the use of carried-forward losses, or the use of tax credits.

Intercorporate dividends are exempt if group taxation relief is available.

Capital gains – Capital gains derived from the sale of immovable property are taxed under the normal tax regime at rates that depend on the amount of the gains, and to the extent of a prescribed percentage of the gains that is computed based on the length of time the property was held. The capital gains tax rates for sales of immovable property are as follows:

- 5% for gains up to PKR 5 million;
- 10% for gains exceeding PKR 5 million and up to PKR 10 million;
- 15% for gains exceeding PKR 10 million and up to PKR 15 million; and
- 20% for gain exceeding PKR 15 million.

The percentage of the gains that is taxable at these rates is based on the holding period of the property:

Capital gains from immovable property

Holding period for open plots	**Holding period for constructed property**	**Portion of gain taxable**
Up to one year	Up to one year	100%

Between one and eight years	Between one and four years	75%
More than eight years	More than four years	0%

Capital gains on the sale of shares of public companies, "modaraba" certificates, and other specified "securities" are taxable at a standard rate of 15%; however, such gains are exempt from tax if the shares were acquired before 1 July 2013 or they were held for more than 24 months.

Losses – Business losses (except losses from a speculative business) may be set off against taxable income earned during the same tax year under any head of income. Excess losses may be carried forward for up to six years following the tax year. Losses from a speculative business and capital losses may be carried forward to the following tax year for set off against speculative business income and capital gains for that year. Losses relating to the disposal of specific securities, including listed shares, may be carried forward and set off against future capital gains for a period of up to three tax years. Business losses cannot be offset against income that is taxed under the final taxation regime.

Losses attributable to tax depreciation and amortization may be carried forward indefinitely but may be offset against only 50% of taxable business income each year where that income is at least PKR 10 million.

Foreign tax relief – A resident entity may claim a credit for income tax paid outside Pakistan on its foreign-source income against its tax liability in Pakistan. The amount of the credit is the lesser of the income tax paid abroad or the Pakistan tax payable on the foreign-source income.

Participation exemption – There is no participation exemption.

Holding company regime – There is no holding company regime, but see under "Consolidated returns," below.

Incentives – To encourage investment in alternative energy power generation, a first-year allowance of 90% of the cost of plant, machinery, and equipment is available. In addition, profits and gains from power generation projects in Pakistan may be exempt from tax in certain cases.

Accelerated depreciation is available for industrial undertakings in rural and under-developed areas.

A tax credit is available to companies for employing new graduates, equal to the lesser of the amount of annual salary paid or 5% of taxable income.

A tax credit equal to 10% of the amount invested for the replacement or modernization of plant and machinery is available for investments made between 1 July 2010 and 30 June 2019.

A credit equal to 20% of the tax liability for the year of listing and the following tax year, and a credit equal to 10% of the tax liability for the two subsequent tax years, is granted to companies that opt to be listed on a registered stock exchange in Pakistan.

A tax credit equal to the equity-financed investment proportion of tax payable is available to a new corporate industrial undertaking set up with at least 70% equity raised through the issuance of new shares for cash consideration. This credit is available for companies incorporated and industrial undertakings established between 1 July 2011 and 30 June 2021, provided certain conditions are fulfilled.

Industrial undertakings established before 1 July 2011 also are allowed a tax credit for investment relating to the modernization or replacement of plant and machinery, or where they expand using 70% equity financing between 1 July 2011 and 30 June 2021. The credit is granted against tax payable based on the ratio of equity investment to total investment.

Incentives apply to income from exports of computer software, information technology (IT) services, or IT enabled services until 30 June 2025, where 80% of the export proceeds are brought into Pakistan.

Other – A Federal Workers Welfare Fund (WWF) assessment equal to 2% of taxable profit is levied on every industrial undertaking, with the exception of industrial undertakings doing business in the province of Sindh. Sindh WWF is levied under provincial legislation at a rate of 2% of taxable income or accounting profit.

Compliance for corporations:

Tax year – The law provides for two types of tax year: a normal tax year (for the period ending 30 June) and a special tax year (i.e., a tax year other than the normal year that has been approved by the tax authorities).

Consolidated returns – Holding companies and subsidiaries of a wholly owned group may opt to be taxed as a single fiscal unit under the group taxation concept.

Filing and payment – For a company whose tax year ends between 1 January and 30 June, the tax return is due by 31 December. In all other cases, the return is due by 30 September following the end of the tax year.

Penalties – The penalty for failure to file a tax return is 0.1% of the amount of the tax payable for each day of default. The minimum penalty is PKR 40,000, and the maximum is 50% of the amount of tax payable.

Rulings – A nonresident may obtain an advance ruling on the tax implications of any transaction or contract.

Individual taxation:

Rates

Individual income tax rate (salaried individuals)	Taxable income	Rate
	Up to PKR 600,000	0%
	Over PKR 600,000 and up to PKR 1.2 million	5% of amount exceeding PKR 600,000
	Over PKR 1.2 million and up to PKR 1.8 million	PKR 30,000 plus 10% of amount exceeding PKR 1.2 million
	Over PKR 1.8 million and up to PKR 2.5 million	PKR 90,000 plus 15% of amount exceeding PKR 1.8 million
	Over PKR 2.5 million and up to PKR 3.5 million	PKR 195,000 plus 17.5% of amount exceeding PKR 2.5 million
	Over PKR 3.5 million and up to PKR 5 million	PKR 370,000 plus 20% of amount exceeding PKR 3.5 million

	Over PKR 5 million and up to PKR 8 million	PKR 670,000 plus 22.5% of amount exceeding PKR 5 million
	Over PKR 8 million and up to PKR 12 million	PKR 1.345 million plus 25% of amount exceeding PKR 8 million
	Over PKR 12 million and up to PKR 30 million	PKR 2.345 million plus 27.5% of amount exceeding PKR 12 million
	Over PKR 30 million and up to PKR 50 million	PKR 7.295 million plus 30% of amount exceeding PKR 30 million
	Over PKR 50 million and up to PKR 75 million	PKR 13.295 million plus 32.5% of amount exceeding PKR 50 million
	Over PKR 75 million	PKR 21.42 million plus 35% of amount exceeding PKR 75 million
Individual income tax rate (non-salaried individuals and associations of persons)	**Taxable income**	**Rate**
	Up to PKR 400,000	0%
	Over PKR 400,000 and up to PKR 600,000	5% of amount exceeding PKR 400,000
	Over PKR 600,000 and up to PKR 1.2 million	PKR 10,000 plus 10% of amount exceeding PKR 600,000
	Over PKR 1.2 million and up to PKR 2.4 million	PKR 70,000 plus 15% of amount exceeding PKR 1.2 million
	Over PKR 2.4 million and up to PKR 3 million	PKR 250,000 plus 20% of amount exceeding PKR 2.4 million
	Over PKR 3 million and up to PKR 4 million	PKR 370,000 plus 25% of amount exceeding PKR 3 million
	Over PKR 4 million and up to PKR 6 million	PKR 620,000 plus 30% of amount exceeding PKR 4 million
	Over PKR 6 million	PKR 1.22 million plus 35% of amount exceeding PKR 6 million
Capital gains tax rate	Applicable individual income tax rate (in general)	

Residence – Individuals are considered resident for a tax year if they are present in Pakistan for 183 days or more in the tax year, or if they are present in Pakistan for 120 days or more in the tax year and present in the aggregate for 365 days or more in the four preceding tax years.

Basis – Resident individuals are taxed on their worldwide income; nonresidents are taxed only on Pakistan-source income.

Taxable income – As with corporations, taxable income is divided into five heads of income, which include income from employment (i.e., salary), income from the exercise of a profession, income from property, capital gains, and other income.

Rates – "Salaried individuals" (i.e., cases where salary income exceeds 75% of taxable income) and non-salaried individuals are subject to tax at progressive rates ranging from 0% to 35%. The specific rates and brackets are shown in the tables above.

Capital gains – Capital gains are taxed at the applicable personal income tax rate. Capital gains on the disposal of listed shares and securities are taxed in the same manner as for companies.

Deductions and allowances – Deductions and allowances are available for individuals, including those for zakat and interest paid on home loans and tuition fees paid for their children, subject to certain conditions. The deductions are restricted to the amounts specified in the law.

Foreign tax relief – Residents may claim a credit for income tax paid outside Pakistan on their foreign-source income against their tax liability in Pakistan. The amount of the credit is the lesser of the income tax paid abroad or the Pakistan tax payable on the foreign-source income.

Compliance for individuals:

Tax year – The tax year is the financial year.

Filing status – Joint returns are not permitted; each individual must file a separate return.

Filing and payment – The tax return must be filed by 31 August after the tax year ending on 30 June. Resident individuals are also required to file a statement of wealth and a wealth reconciliation statement as at 30 June.

Penalties – The penalty for failure to file a tax return is 0.1% of the amount of the tax payable for each day of default. The minimum penalty is PKR 40,000 and the maximum is 50% of the amount of tax payable.

Rulings – A nonresident that is not operating in Pakistan through a PE may obtain an advance ruling on the tax implications of any transaction or contract.

Withholding tax:

Rates

Type of payment	Residents		Nonresidents	
	Company	Individual	Company	Individual
Dividends	7.5%/15%/25%	7.5%/15%/25%	15%	15%
Interest	10%/15%	10%/15%	10%	10%
Royalties	15%	15%	15%	15%
Fees for technical services	3%/8%	3%/10%	15%	15%

Dividends – A resident generally is subject to withholding tax at a rate of 15% on dividend income; a rate of 7.5% or 25% may apply under certain circumstances (see "Taxation of dividends," above).

A nonresident pays a 15% withholding tax on Pakistan-source dividends, or a reduced rate if provided under an applicable tax treaty.

Interest – Interest accruing on deposit accounts, bonds, certificates, debentures, securities issued by the government, etc. that is payable to a resident entity or individual is subject to withholding tax at a rate of 10% if the interest is up to PKR 500,000, and 15% where the interest exceeds PKR 500,000.

The withholding tax rate on interest paid to a nonresident company without a PE in Pakistan or a nonresident individual is 10%, unless the rate is reduced under a tax treaty.

Royalties – Royalties payments to a resident or nonresident are subject to a 15% withholding tax.

Fees for technical services – Fees for technical services paid to a nonresident are subject to a 15% withholding tax, unless the rate is reduced under a tax treaty. Technical service fees paid to a resident are subject to withholding tax at rates that vary depending on the nature of the service.

Branch remittance tax – The remittance of profits to a head office abroad is treated as dividends, attracting a 15% withholding tax on the remittance.

Other – A 7% withholding tax is imposed on payments made under a construction contract to a resident company; the rate is 7.5% on payments to other resident persons. A 3% withholding tax is imposed on payments made for advertising services (other than services relating to print or electronic media). Certain other payments to residents are subject to withholding tax at a rate of 8% for payments to a company and 10% for payments to persons other than a company.

A 10% withholding tax applies to advertising services provided by a nonresident media company; and a 5% tax applies on the payment of insurance premiums. These rates generally apply to income subject to the final taxation regime. For other payments to nonresidents, a general withholding tax of 20% applies.

Anti-avoidance rules:

Transfer pricing – Under the anti-avoidance rules, the tax authorities are authorized to distribute, apportion, or allocate income, deductions, or tax credits between associated companies to reflect income that would have been realized in accordance with the arm's length principle. Pakistan tax law provides four methods for determining the arm's length result.

Taxpayers are required to prepare a master file, a local file, and a country-by country-report containing information on transactions with related parties, as well as to provide and maintain such other information and documents as may be prescribed.

Interest deduction limitations – Where a foreign controlled resident company or branch of a nonresident (other than a bank or financial institution) has a foreign debt-to-equity ratio exceeding 3:1 at any time during a tax year, no deduction will be allowed in respect of the interest on the portion that exceeds the 3:1 ratio.

Controlled foreign companies – Controlled foreign company (CFC) legislation attributes income of a CFC to a greater-than-10% shareholder resident in Pakistan. A CFC is defined as a nonresident company for which all of the following apply:

- More than 50% of the nonresident company's capital or voting rights are directly or indirectly held by one or more Pakistan residents, or more than 40% of the company's capital or voting rights are directly or indirectly held by a single Pakistan resident;

- Tax paid by the nonresident company for the taxable year, after taking into account foreign tax credits, to any tax authority outside Pakistan is less than 60% of the Pakistan tax that would have been payable on the company's income if the company were resident in Pakistan;
- The foreign company derives more than 80% of its income from dividends, interest, property, capital gains, royalties, or annuities; supplies of goods or services to a related party; sales or licenses of intangibles; or the management, holding, or investment in securities and financial assets; and
- The shares of the company are not traded on a stock exchange recognized under the laws of the country in which the company is tax resident.

The taxable income of a CFC is determined as if the CFC were a resident taxpayer, and converted into PKR at the State Bank of Pakistan rate applying on the last day of the tax year. The amount included in the taxable income of the resident shareholder is based on the percentage of capital or voting rights, whichever is higher, directly or indirectly held by the resident in the CFC. No income of the CFC is attributed to a resident shareholder where the capital or voting rights held by the shareholder is less than 10% or is less than PKR 10 million. Where income of a CFC is taxable to a shareholder in Pakistan under the CFC rules, the income is not taxed again when distributed.

Hybrids – There are no hybrid rules applicable in Pakistan tax law.

Economic substance requirements – The tax authorities may recharacterize a transaction that was entered into for tax avoidance purposes or where the transaction lacks substance, or may disregard a transaction that has no economic substance.

Disclosure requirements – Corporate taxpayers are required to submit audited financial statements along with the income tax return.

Transfer pricing reporting requirements apply (see under "Transfer pricing," above.)

Exit tax – A notice of discontinuance of business must be provided, along with filing a final income tax return and discharging any outstanding tax liability.

General anti-avoidance rule – See "Transfer pricing" and "Economic substance requirements," above.

Sales tax:

Rates	
Standard rate	17% for goods; for services, the rates are 13% to 16%, depending on the province
Reduced rate	Various

Taxable transactions – Sales tax is levied on the supply and import of goods, and the rendering or provision of specified services. The federal government normally levies sales tax only on the supply of goods, whereas provincial governments levy sales tax on services rendered in their provinces. The federal government also levies sales tax in respect of services rendered in the Islamabad Capital Territory.

Federal Excise Duty (FED) is chargeable in a similar manner to VAT on certain services.

Rates – The standard sales tax rate is 17% for goods and 13% to 16% for services, depending on the province where the services provider is located or where the services are used. The rate is 13% in Sindh, 16% in Punjab and the Islamabad Capital Territory, and 15% in Balochistan and Khyber Pakhtunkhwa.

Various reduced rates apply, depending upon the nature of goods and services and the tax jurisdiction. Exports generally are zero-rated.

Under federal and provincial sales tax laws, all purchasers of taxable goods or recipients of taxable services are required to withhold sales tax when making payment to the supplier or service provider, as specified in the legislation.

Registration – All suppliers of taxable goods or providers of taxable services are required to register with the relevant tax authority. For goods, this is the Federal Board of Revenue; for services, registration is at the provincial level.

Filing and payment – Sales tax returns and payments generally must be made on a monthly basis. Payments are due by the 15th day of the following month and returns must be filed by the 18th day of the following month.

Other taxes on corporations and individuals:

Social security contributions – The employer contributes up to 6% of wages to the Social Security Institution on behalf of the employee. No contribution is due on wages in excess of PKR 600 per day or PKR 15,000 per month.

Payroll tax – There is no specific payroll tax, but the employer withholds tax from the salary payment and remits the tax to the government on behalf of the employee. Taxable income of employees is bifurcated into salaried and non-salaried employee classes (see "Rates" under "Individual taxation").

Capital duty – A capital authorization fee is levied at varying rates, depending on the authorized capital.

Real property tax – Property tax is levied at the provincial level.

Transfer tax – Subject to certain conditions, a 5% tax is levied on the gross sales price of property or goods sold by auction.

Stamp duty – Stamp duty is payable on the issuance and transfer of shares at rates of 0.5% and 1.5%, respectively, of the face value of the shares, subject to a minimum of PKR 1. If the shares are transferred to or through a central depository company (CDC), the duty is applied under the CDC's rules.

Net wealth/worth tax – There is no net wealth/net worth tax.

Inheritance/estate tax – There is no inheritance/estate tax.

Tax treaties: Pakistan has concluded 69 tax treaties. Pakistan signed the OECD multilateral instrument (MLI) on 7 June 2017.

Tax authorities: Federal Board of Revenue, Provincial tax authorities

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