

Tax on
Salary

2011

"This tax guide is for the use of CLIENTS and STAFF only and covers the taxability aspects of the salary as per Pakistani income tax laws applicable to Tax Year 2011"

Income Tax
Law &
Calculation

A. Salam Jan & Co. - Chartered Accountants – is a member of AFFILICA International – a network of independent accountancy firms.

INTRODUCTION

This tax guide gives information for arriving at the taxable income of a salaried person and computation of tax liability thereof under the Income Tax Ordinance, 2001. It is equally informative and useful from the employers' perspective to determine the amount of tax to be withheld every month from the salary paid to the employees.

It contains the provisions relating to the tax of a resident salaried person only.

WHAT IS SALARY?

Salary means amount received by an employee from any employment, whether of a capital or revenue nature. It includes pay and perquisites.

Pay means wages or other remuneration like leave pay, payment in lieu of leave, overtime payment, bonus, commission, fees and gratuity.

Perquisite means benefit whether convertible to money or not given to employee over and above pay and wages, e.g. - utilities allowance, conveyance allowance, provision of vehicle and accommodation etc.

WHO IS A SALARIED PERSON?

An individual is treated as a salaried person if more than 50% of his total income comprises of salary income or he/she derives income entirely from salary. Every salaried person is obliged to pay tax on salary, if salary exceeds prescribed limits.

TAXABILITY OF SALARY

While computing the taxable salary income of a person, all perquisites, allowances or benefits, except exempt items are to be included in the salary and such gross figure shall be treated as the taxable salary income of a taxpayer.

Following allowances are exempt from tax subject to the following conditions:

Medical Allowance

Exempt upto 10% of basic salary, if free medical treatment or hospitalization or re-imburement of medical or hospitalization charges is not provided.

[See Clause (139)(b) of Part I of Second Schedule of ITO 2001]

Special Allowance

Exempt if granted to meet expenses for the performance of official duties.

[See Clause (39) of Part I of Second Schedule of ITO 2001]

RATES OF TAXATION

The tax on salary income is calculated at the rates prescribed in Income Tax Ordinance, 2001. Through Finance Bill 2010 different rates are proposed.

The proposed rates for **Tax Year 2011** are as follows:

S.No	Taxable Income	Rate of Tax
1	Where the taxable income does not exceed Rs.300,000.	0%
2	Where the taxable income exceeds Rs.300,000 but does not exceed Rs.350,000.	0.75%
3	Where the taxable income exceeds Rs.350,000 but does not exceed Rs.400,000.	1.5%
4	Where the taxable income exceeds Rs.400,000 but does not exceed Rs.450,000.	2.5%
5	Where the taxable income exceeds Rs. 450,000 but does not exceed Rs.550,000.	3.5%
6	Where the taxable income exceeds Rs. 550,000 but does not exceed Rs.650,000.	4.5%
7	Where the taxable income exceeds Rs. 650,000 but does not exceed Rs.750,000.	6.0%
8	Where the taxable income exceeds Rs. 750,000 but does not exceed Rs.900,000.	7.5%
9	Where the taxable income exceeds Rs. 900,000 but does not exceed Rs.1,050,000.	9.0%
10	Where the taxable income exceeds Rs. 1,050,000 but does not exceed Rs.1,200,000.	10.0%
11	Where the taxable income exceeds Rs. 1,200,000 but does not exceed Rs.1,450,000.	11.0%
12	Where the taxable income exceeds Rs. 1,450,000 but does not exceed Rs.1,700,000.	12.5%
13	Where the taxable income exceeds Rs. 1,700,000 but does not exceed Rs.1,950,000.	14.0%
14	Where the taxable income exceeds Rs. 1,950,000 but does not exceed Rs.2,250,000.	15.0%
15	Where the taxable income exceeds Rs. 2,250,000 but does not exceed Rs.2,850,000.	16.0%
16	Where the taxable income exceeds Rs. 2,850,000 but does not exceed Rs.3,550,000.	17.5%
17	Where the taxable income exceeds Rs. 3,550,000 but does not exceed Rs.4,550,000.	18.5%
18	Where the taxable income exceeds Rs. 4,550,000.	20.0%

MARGINAL RELIEF

Through Finance Act 2008 a new provision for marginal relief in the tax rates was introduced to remove anomaly in the tax rates. The marginal relief is available on amount in excess of maximum limit of the preceding slab relative to slab in which the taxable income fall. The marginal amount will be taxed at the following rates:

S.No	If taxable income of the tax payer is	Percentage of incremental income taxable at next applicable tax rate
1	Where the taxable income does not exceed Rs.550,000.	20%
2	Where the taxable income exceeds Rs. 550,000 but does not exceed Rs.1,050,000.	30%
3	Where the taxable income exceeds Rs. 1,050,000 but does not exceed Rs.2,250,000.	40%
4	Where the taxable income exceeds Rs. 2,250,000 but does not exceed Rs.4,550,000.	50%
5	Where the taxable income exceeds Rs. 4,550,000.	60%

Special Notes:

1. For withholding tax purposes these rates shall apply to salary paid on or after first day of July 2010.
2. When the relief worked out through this provision ceases to exist then it would not be applicable and tax shall be computed normally without marginal relief.

Example:

If a taxable salary income, of a person is Rs. 362,000, the tax on the salary income will be lower of (a) and (b):

<u>(a) Tax with Marginal Relief</u>		Rs.
Tax on first 350,000	350,000 x 0.75%	2,625
Tax on marginal amount of 12,000	12,000 x 20%	2,400
		5,025
 <u>(b) Tax without Marginal Relief</u>		Rs.
Tax on total amount of Rs. 362,000	362,000 x 1.5%	5,430

Therefore, tax on **Rs. 362,000** is **Rs. 5,025**, being the lower of **(a)** and **(b)**.

TAX REDUCERS

The tax calculated above can be reduced to a prescribed limit if the salaried person is a senior citizen or a full time researcher or teacher. The gross tax calculated as per applicable rates of tax is subject to reduction for **senior taxpayers** and **full time teacher or researcher**.

Teacher or Researcher

A reduction of 75% of tax on income from salary is available to a full time teacher or researcher, employed in a non-profit education or research institution duly recognized by HEC, any university or board and government training and research institution.

[See Clause (2) of Part III of Second Schedule of ITO 2001]

Senior Taxpayers

If the age of the taxpayer on the first day of a tax year is 60 years or more and taxable income does not exceed Rs.1,000,000 the gross tax qualifies for a reduction of 50%.

[See Clause (1A) of Part III of Second Schedule of ITO 2001]

FILING OF TAX RETURN / EMPLOYER'S CERTIFICATE

When income exceeds the taxable limit in a tax year and is exclusively derived from "salary" being less than Rs. 500,000, one may file an Employer's Certificate in lieu of a return of income by the due date.(i.e. August 31 next following the tax year) if the employer has not furnished the Annual Statement of Deduction of Income Tax from Salary. The salaried taxpayer is not required to even furnish Employer's Certificate if his/her taxable salary income is less than Rs. 500,000 and his/her employer has filed an Annual Statement of Deduction of Income Tax from Salary as prescribed under the Income Tax Rules.

However, if a person exclusively deriving income from salary and the salary income for the tax year is Rs. 500,000 or more, the taxpayer shall file return of income electronically in the prescribed form and it shall be accompanied by the proof of deduction or payment of tax and wealth statement as required under section 116.

The deduction of tax at source by an employer from the salary is a final discharge of employee's obligation in case if the employee's salary is less than Rs. 500,000 ,his/her employer has deducted proper tax due from him/her and filed an annual statement of deduction of tax from salary. In other cases such a deduction of tax should not be the final discharge of employee's obligation and such an employee is liable to file the employer's certificate on prescribed form or e-file his/her return of income on due date as the case may be.

WEALTH STATEMENT

A salaried taxpayer is obliged to file a Wealth Statement and wealth reconciliation statement if his or her last declared or assessed taxable income or declared income for the year is Rs. 500,000 or more. Wealth statement should be filed in all cases whether the annual statement has been filed or not by his / her employer.

Wealth statement is a statement of:

- total assets and liabilities of the taxpayer as on a closing date of financial year (i.e. *June 30 each year*);
- total assets and liabilities of the taxpayer's spouse, minor children, and other dependants on the same date;
- any assets transferred by the taxpayer to any other person during the year; and
- the detail of such total expenditures incurred by taxpayer and his or her spouse, minor children, and other dependants during the year.
- the reconciliation statement of wealth.

EMPLOYER'S RESPONSIBILITIES AS WITH HOLDING TAX AGENT

Every employer paying salary to an employee shall, at the time of payment, deduct tax from the amount paid at the employee's average rate of tax computed at the prescribed rates on the estimated salary income of the employee for the tax year in which the payment is made. While making deduction of tax from an employee, the employer shall make an adjustment for the following on production of documentary evidence:

Tax withheld from employee under other heads like:

- On payment of landline telephone bills (if connection is in the name of employee);
- On payment of mobile bills (if connection is in the name of employee);
- On payment of vehicle registration/renewal token (if vehicle is registered in the name of employee); and
- On cash withdrawal from bank (if the bank account is in the name of employee).

Allow tax credits available to an employee on:

- (a) donations to approved NPOs (section 61 of ITO 2001);
- (b) investment in shares (section 62 of ITO 2001);
- (c) contribution to approved pension funds (section 63 of ITO 2001); and
- (d) profit on debt (section 64 of ITO 2001).

The tax so deducted shall be deposited in the government treasury within seven days from the end of each fortnight.

The salaried person shall submit declaration to the employer regarding his/her sources of income and tax credits claimed on prescribed form IT-3. This shall be kept by the employer in his record for a period of five years.

Every employer is required to file / e-file a quarterly* statement on prescribed form regarding the deduction of tax from salaries of employees within the twenty days of the end of the relevant quarter. The quarterly statement is required to be filed even if there is no withholding tax deduction during the relevant quarter.

Every employer is also required to file / e-file an Annual Statement of Deduction of Tax from Salary on prescribed form within two months of the end of the financial year.

Employer responsible for deducting tax from salary shall issue a certificate to the employee, in the prescribed form with in forty-five days after the end of the financial year.

*Quarterly statement is required w.e.f July 2010, up to year June 2010 only monthly statement was required to be filed.

NATIONAL TAX NUMBER

National tax number NTN should be mentioned on all returns, employer's certificate, wealth statement etc. A taxpayer can obtain NTN by submitting an application in the prescribed form along with a photo copy of Computerized National Identity Card (CNIC) and other required documents.

