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TAXATION OF INCOME FROM SALARY

SALARY:

Any amount received by an employee from any employment in a tax year, whether of a revenue or capital nature.

Salary includes:

- Any pay, wages, or other remuneration, including leave pay, overtime bonus, commission, fees, gratuity, work condition supplements (such as for unpleasant or dangerous working conditions)
- Any perquisite whether convertible to money or not;
- Any allowance provided to an employee including cost of living, rent, utilities, education, entertainment, traveling, etc., excluding allowance solely expended in the performance of duties of employment;
- Any personal expenditure reimbursed by employer other than personal expenditure incurred solely in the performance of duties of employment
- Any pension or annuity

Note: Commission paid to a person is taxable under minimum tax regime but in case of employee/ employer relation, the same will be taxable as salary

BASIS OF CHARGEABILITY:

Salary is taxable on receipt basis i.e. any salary received by an employee in a tax year shall be chargeable to tax.

SALARY WHEN CONSIDERED PAKISTAN SOURCE:

Salary shall be Pakistan source income to the extent to which the salary is received from

- Any employment exercised in Pakistan, wherever paid
- Is paid by, or on behalf of, the Federal Government, a Provincial Government, or a Local Government in Pakistan, wherever the employment is exercised.

VALUATION OF PERQUISITES:

Section 13 of the Income Tax Ordinance, 2001 states the different provisions relating to determination of value of perquisites.

However, in order to facilitate the understanding to these methods, we divided them under the following headings:

CONVEYANCE:

Motor Vehicle provided by an employer to any employee (including director) wholly or partly for personal use, the amount chargeable to tax under the head salary shall include:

Partly for personal and official use	5% of the cost of vehicle to the employer or Fair market value (FMV) of motor vehicle at the commencement of lease
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For personal use only	10% of the cost of vehicle to the employer or FMV of motor vehicle at the commencement of lease
For office use only	No addition

Note 1: The above notional figure will always be calculated on original cost even if old car is given to employee. Proportionate figure will be added in salary in case vehicle is not used for the whole tax year. Any amount given by employee for use of car shall be deducted from above notional figure.

Note 2: Running and maintenance cost is not a separate perquisite and included in the said nominal value @ 10% or 5%. However, driver's salary if paid by employer is a separate perquisite and fully taxable. Further, any conveyance allowance given shall also be fully taxable.

Note 3: Where vehicle is provided to an employee for personal purpose or partly for personal and partly for business purpose, then full depreciation will be allowed to company provided 5% or 10% amount has been added in salary of the employee and employer has deducted withholding tax accordingly.

ACCOMMODATION:

Accommodation or housing, the amount chargeable to tax under the head "Salary" shall include higher of the following:

- Amount that would have been paid in case such accommodation was not provided; and
- 45% of the minimum of time scale (MTS) of the basic salary or the basic salary where there is no MTS.

Minimum of time scale is the amount from where the salary scale of a particular employee starts e.g. (4900-800-8500) means salary of the employee 4900 with increment of Rs. 800 per annum/qtr. etc. subject to maximum increased salary up to Rs. 8,500.

UTILITIES AND SERVICES OF DOMESTIC SERVANTS:

Utilities:

"Utilities" includes electricity, gas, water and telephone.

The amount chargeable to tax under the head salary shall include the FMV of utilities as reduced by any payment made to the employer for such utilities.

Domestic servants

In case services of housekeeper, gardener, driver, or other domestic assistant is provided by an employer to the employee, the amount chargeable to tax under the head salary shall include the amount of total salary paid to the domestic assistants as reduced by any payment made to the employer for such services.

INTEREST FREE LOAN:

Where a loan is given to an employee after 1.7.2002 (e.g. tax year 2003) than any of the following two amounts shall be added to the salary income of the employee

- The amount of interest computed at the benchmark rate, if no interest is payable by the employee
- The amount computed at the benchmark rate less the actual amount of interest paid by the employee, if lower rate is applicable on loan.

OBLIGATIONS WAIVER/SETTLEMENTS:

- Any obligation waived of which an employee owed to the employer shall be included in the salary income of the employee.
- Any repayment by the employer to another person on account of an obligation of the employee shall be included in the salary income of the employee equal to the amount repaid.

SELF HIRING OF PROPERTY:

Where an employee or his spouse is the owner of any such building that is given on rent to the employer and the employer has provided the same building to the employee against his entitlement for a rent-free accommodation, then it will have following effect:

- Receipt of rent of building is chargeable to tax under the head income from property. Any rent received by the employee or his spouse shall be property income of the recipient and be treated accordingly.
- The building is provided by the employer to his employee as a rent-free accommodation. It will be a perquisite and added in the salary income of the employee as per the above rule.

TRANSFER OF PROPERTY OR PROVISION OF SERVICES TO EMPLOYEES:

The amount chargeable to tax to the employee under the head salary for that shall include:

"The fair market value of the property or services determined at the time property is transferred or the services are provided, as reduced by any payment made by the employee for the property or services".

If any property is not transferred to an employee but it is given only for the use, then specific rules are there for vehicles and accommodation.

ANY OTHER PERQUISITE:

The amount calculated as below shall be included in the salary income of the employee:

Fair market value of the perquisite	XXX
Less: payment made by the employee if any	<u>(XXX)</u>
Amount to be included in salary income	<u>XXX</u>

EXEMPTIONS:

CERTAIN PERQUISITES WITHOUT MARGINAL COST BY VIRTUE OF EMPLOYMENT:

The following perquisites received by an employee by virtue of his employment are exempt from tax:

- Free or subsidized food provided by hotels and restaurants to its employees during duty hours
- Free or subsidized education provided by an educational institution to the children of employees
- Free or subsidized medical treatment provided by a hospital or clinic to its employees
- Any other perquisite for which the employer does not have to bear any marginal cost as notified by the Board.

MEDICAL ALLOWANCE AND REIMBURSEMENT:

- In case only medical reimbursement is provided by an employer to employee or its family and dependents, the same will be fully exempt where such provision or reimbursement is in accordance with the terms of employment and NTN of the hospital or clinic is provided and employer also certifies and attests the medical bills.
- In case only medical allowance is provided, the same will be exempt up to 10% of basic salary
- If both medical reimbursement and allowance are provided to employee, medical allowance will be fully taxable whereas medical reimbursement will be exempt provided NTN of hospital is provided and employer attests the bills.
- If both medical allowance and reimbursement are provided, but reimbursement is not according to the terms of employment, in that case medical allowance will be exempt upto 10% of basic salary and medical reimbursement will be fully taxable

LEAVE ENCASHMENT:

Any amount received on account of leave encashment/leave fare assistance is fully taxable. However, any amount received on encashment of leave preparatory to retirement is exempt, if it is received by a government employee.

WORKER'S PROFIT PARTICIPATION FUND (WPPF):

Amount received from WPPF as worker is fully exempt.

SCHOLARSHIP:

Any scholarship granted by employer to employee to meet the cost of person's education is exempt from tax provided employer and employee are not associates.