Taxation of Non-Resident Individuals and Expatriates in Pakistan

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Reliance Restricted

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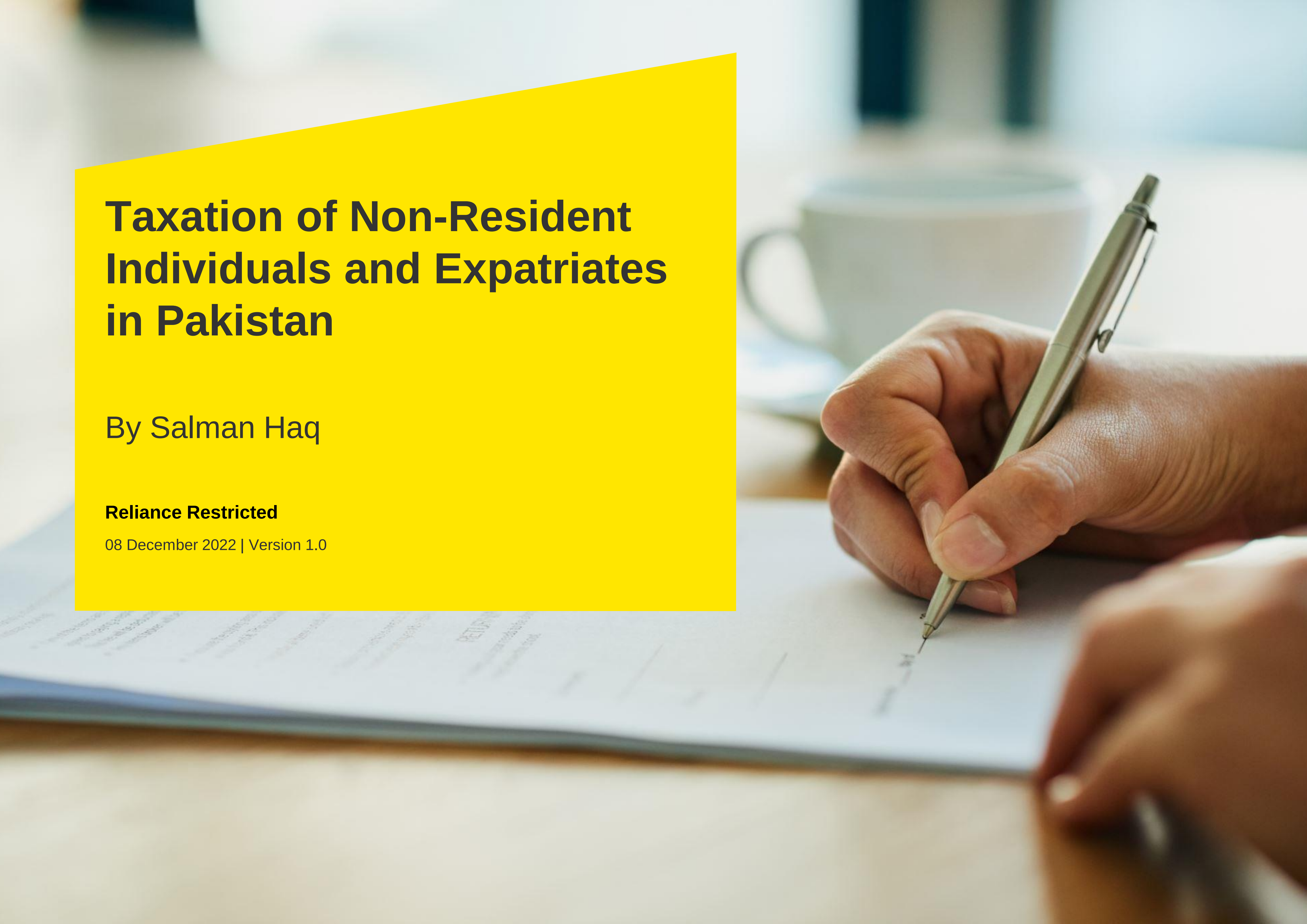


Table of Contents

Presentation Objectives

The objective of this presentation is to discuss the dynamics governing taxability of foreigners and expatriates in Pakistan

The presentation takes into account various incomes earned by foreigners and expatriates that may be taxed as their Pakistan sourced income.

Scenario

After the presentation, we should be able to identify tax incidence arising under each of the following scenarios.

- ABC private limited is a 100% subsidiary of a German based company XYZ GmbH which is a multinational conglomerate. XYZ GmbH has deputed Mr. YG as the Finance Director of ABC private limited. Mr. YG is a German citizen. Mr. YG receives portion of his salary in Pakistan from ABC private limited and a portion in the Germany from XYZ GmbH. Mr. YG has been in Pakistan for 1 year now.
- Mr. YG, as in 1 above, has opened a bank account in Pakistan and receives profit on such bank account.
- Mr. YG, as in 1 above, has invested in listed shares of both Pakistani companies and foreign companies.
- Mr. YG derives dividend income and capital gains both from Pakistani companies and foreign companies.
- One of the customers of ABC private limited, as in 1 above, has filed a suit against ABC private limited in the court of England and Whales. ABC private limited has engaged Mr. DF as a Lawyer in the UK and pays him fee for defending its case in the UK Court. Mr. DF conducts all his soliciting and advisory activity in the UK and is not present in Pakistan.
- PQR limited, a renowned TV channel in Pakistan has held its Yearly Awards in Dubai. For, this purpose it invited two Indian Artists to perform during the award ceremony. These artists were paid by PQR limited.

1

Some Basic Concepts of Taxation

A brief introduction to residency status and taxation of resident and non-resident individuals is provided in the ensuing slides.

Some Basic Concepts of Taxation

Principles of Taxation in Pakistan

The tax laws in Pakistan recognize taxation based on residence status

Taxation of Income

Resident individuals are taxed on both Pakistan sourced income and foreign sourced income.

Non-resident individuals are taxed on Pakistan sourced income only.

Every tax year is a separate and distinct unit. An individual may be a resident in a particular year and be a non-resident in the next depending on his stay in Pakistan.

Absolute and Fictional Income

It is imperative to note that income may be classified as Pakistan source either as:

a) Absolute – meaning that the income has actual source in Pakistan; or

b) Fictional – meaning that it becomes Pakistan sourced income based on the status of the payer in Pakistan.

Any income that is not classified as Pakistan source would be treated as foreign source income for the purposes of taxation.

Resident Individual is a person who is:

- ❖ **Present in Pakistan for more than 183 days or more in a tax year**
- ❖ **Employee of federal / provincial government posted abroad for the year**
- ❖ **being a citizen of Pakistan is: i) not present in any other country for more than one hundred and eighty-two days during the tax year; or ii) who is not a resident taxpayer of any other country**

Principles of Taxation in Pakistan

Absolute Income

Section	Character of Income	Comment
101(1)	Salary	From employment exercised in Pakistan; or paid to a Government employee wherever such employment is exercised
101(2)	Business Income of a resident person	When income is derived from business carried on in Pakistan
101(3)	Business Income of a non-resident person	When income is directly or indirectly attributable to a permanent establishment or any other business connection in Pakistan
101(5)	Gains on disposal of business assets	Disposal of business assets in Pakistan
101(6)	Dividend Income	When paid by a resident company; or remittance of after tax profit by a branch of a foreign company operating in Pakistan
101(9)	Rental Income	When it is derived from the lease of immovable property in Pakistan or from any other interest in or over immovable property, including a right to explore for, or exploit, natural resources in Pakistan.
101(10)	Alienation or disposal of immovable property	Referred to in 101(9)
101(13)	Disposal of shares	Gain on disposal of shares of a resident company

Principles of Taxation in Pakistan

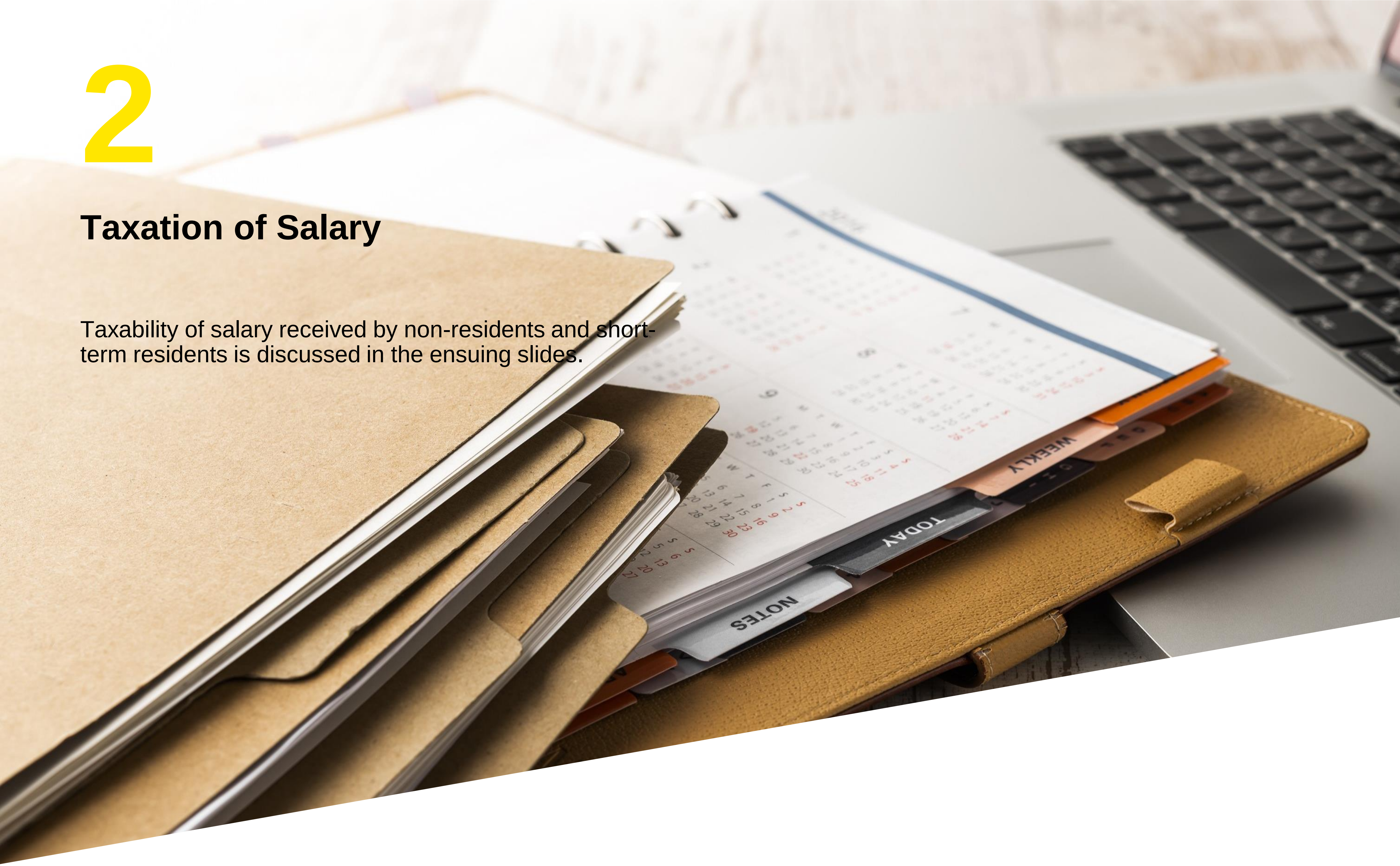
Fictional Income

Section	Character of Income	Comment
101(4)	Independent Services rendered by a nonresident person	If paid by a resident person or born by the permanent establishment of a nonresident person
101(7)	Profit on Debt	If paid by a resident person or born by the permanent establishment of a nonresident person
101(8)	Royalty	If paid by a resident person or born by the permanent establishment of a nonresident person
101(11)	Pension or annuity	If paid by a resident person or born by the permanent establishment of a nonresident person
101(12)	technical fee	If paid by a resident person or born by the permanent establishment of a nonresident person
101(12A)	fee for offshore digital services	If paid by a resident person or born by the permanent establishment of a nonresident person
101(13A)	Insurance/reinsurance Premium	Paid by an insurance company to an overseas insurance or re-insurance company.
101(14)	Any other amount	Paid by a resident person or borne by a permanent establishment in Pakistan of a non-resident person

Some Basic Concepts of Taxation

Various Sources of Income for Non-Resident Individuals

Salary	Income from Business	Capital Gains
Dividends	Profit on Debt	Others



2

Taxation of Salary

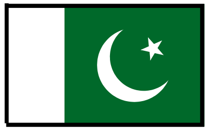
Taxability of salary received by non-residents and short-term residents is discussed in the ensuing slides.

2 Taxation of Salary

What is salary?

Salary is any amount received by an employee from exercise of his/her employment.

When does salary become Pakistan sourced?



Irrespective of where the salary is paid or whether or not the employer has a presence in Pakistan, salary shall be Pakistan sourced if it is received from exercise of employment in Pakistan.

All allowances received by an employee in relation to his employment are fully taxable.

All perquisites (benefits in kind) provided to an employee in relation to his employment are taxable at fair market value (FMV).

Salary is taxed on a receipt basis.

Taxation of Short Term Resident Individuals

The foreign sourced income of an individual who is a resident solely because of his employment and is present in Pakistan for a period not exceeding three years is exempt from tax.

Foreign Sourced Income of Returning Expats

Foreign-source income of returning expatriates (citizens of Pakistan who were not resident in Pakistan during any of the preceding four tax years) shall be exempt from tax in the tax year of return and the succeeding tax year.

Foreign Sourced Salary Derived by Individuals

Where a citizen of Pakistan leaves Pakistan during a tax year and remains abroad during that tax year, any income chargeable under the head “Salary” earned by him/her outside Pakistan during that year is exempt from tax.

2 Taxation of Salary

Rate of tax applicable on salary income is provided below.

Income Tax Rates for Salaried Individuals

Serial No.	Amount	Rates
1	Up to PKR 600,000	Nil
2	PKR 600,001 – PKR 1,200,000	2.5% of the amount exceeding PKR 600,000
3	PKR 1,200,001 to PKR 2,400,000	PKR 15,000 +12.5% of the amount exceeding PKR 1,200,000
4	PKR 2,400,001 – PKR 3,600,000	PKR 165,000 +20% of the amount exceeding PKR 2,400,000
5	PKR 3,600,001 – PKR 6,000,000	PKR 405,000 + 25% of the amount exceeding PKR 3,600,000
6	PKR 6,000,001 – PKR 12,000,000	PKR 1,005,000 +32.5% of the amount exceeding PKR 6,000,000
7	PKR 12,000,001 and above	PKR 2,955,000 +35% of the amount exceeding PKR 12,000,000

3

Taxation of Income from Business

An overview of income from business for non-residents and expatriates is provided in the ensuing slides.

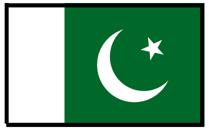
3 Income from Business

Discussion on when an individual may be considered to derive Pakistan source business income is discussed hereunder

What is "Income from Business"?

Income from Business includes profits and gains of any business carried on by a person at any time in a year.

When does business income for a non-resident become Pakistan sourced?



For sale of goods

Business income is Pakistan sourced to the extent it is directly or indirectly attributable to:

a) **A PE of a non-resident**

b) **Sale of goods or rendering of services similar to those being sold or rendered by the PE in Pakistan**

c) **Any business connection in Pakistan**

d) **Cohesive business operations**

For rendering of independent services:

Rendering of independent services (including professional services and the services of entertainers and sports persons), when the remuneration is paid by a resident person or borne by a PE of a non-resident person in Pakistan.

3 Income from Business

Rate of tax applicable on business income is provided below.

Income Tax Rates for Non-salaried Individuals		
Serial No.	Amount	Rates
1	Up to PKR 600,000	Nil
2	PKR 600,001 – PKR 800,000	5% of the amount exceeding PKR 600,000
3	PKR 800,001 to PKR 1,200,000	PKR 10,000 +12.5% of the amount exceeding PKR 800,000
4	PKR 1,200,001 – PKR 2,400,000	PKR 60,000 + 17.5% of the amount exceeding PKR 1,200,000
5	PKR 2,400,001 – PKR 3,000,000	PKR 270,000 + 22.5% of the amount exceeding PKR 2,400,000
6	PKR 3,000,001 – PKR 4,000,000	PKR 405,000 + 27.5% of the amount exceeding PKR 3,000,000
7	PKR 4,000,001 – PKR 6,000,000	PKR 680,000 + 32.5% of the amount exceeding PKR 4,000,000
8	PKR 6,000,001 and above	PKR 1,330,000 + 35% of the amount exceeding PKR 6,000,000

4

Taxation of Capital Gains

An overview of capital gains for non-residents and expatriates is provided in the ensuing slides.

3 Capital Gains

An overview of when capital gains may become Pakistan sourced is provided below

What are “Capital Gains”?

Gains arising on disposal of capital assets are capital gains.

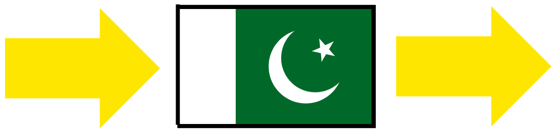
“Capital Asset” means property of any kind held by a person, whether or not connected with a business, but does not include:

- **Stock in trade;**
- **Assets entitled to depreciation and amortization; and**
- **Movable property for personal use, with certain exceptions**

Gains arising on disposal of securities including traded shares are taxed at differing rates depending on holding period.

“Security” means share of a public company, voucher of Pakistan Telecommunication Corporation, Modaraba Certificate, an instrument of redeemable capital, debt Securities, unit of exchange traded fund and derivative products.

When do capital gains become Pakistan sourced?



Property

Any gains from alienation of any property or right from immoveable property or from any shares in a company which consists directly or indirectly of immoveable property is deemed as Pakistan sourced income.

Shares

Disposal of shares in a resident company is Pakistan sourced income.

The taxability for various categories of assets is provided on the next slide.

3 Capital Gains

An overview of when capital gains may become Pakistan sourced is provided below

Taxability of Gains on Various Categories of Assets

Type of Asset	Taxability
Securities including listed shares	Capital gains on disposal of securities are taxed depending on holding period of securities. Capital gains are calculated as: A – B A = consideration received on disposal B = cost of acquisition
Immoveable Property	The gain arising on disposal of immovable properties is to be charged to tax at various rates depending on the following categories: open plots, constructed property, and flats. No gains are taxed when the holding period exceeds six years for open property, four years for constructed property, and two years for flats.
Capital assets (including shares of private company) not being securities and immovable property	Capital gains on disposal of capital assets and shares of private company are taxed at slab rates discussed on slide 15, the gains are calculated as: A – B A = consideration received on disposal B = cost of acquisition
Disposal of assets outside Pakistan	Please see the next slide.

3 Capital Gains

An overview of when gain on disposal of assets outside Pakistan is provided below

Gain on Disposal of Assets Outside Pakistan

It is imperative to note that before the introduction of Finance Act 2018, gains arising from an indirect transfer of assets were generally not taxable under the local tax laws. However such gains are now subject to tax in Pakistan.

Gains arising from disposal or alienation of an asset located in Pakistan is Pakistan sourced income of the non-resident.

Assets are deemed to be located in Pakistan if:

- **The shares/interest derive their value, directly or indirectly, wholly or principally, from the assets located in Pakistan, and their value exceed PKR 100 million, and represent at least 50% of the value of all the assets owned by the non-resident company.**
- **The shares/interest disposed or alienated represented 10% or more of the share capital of the non-resident company.**

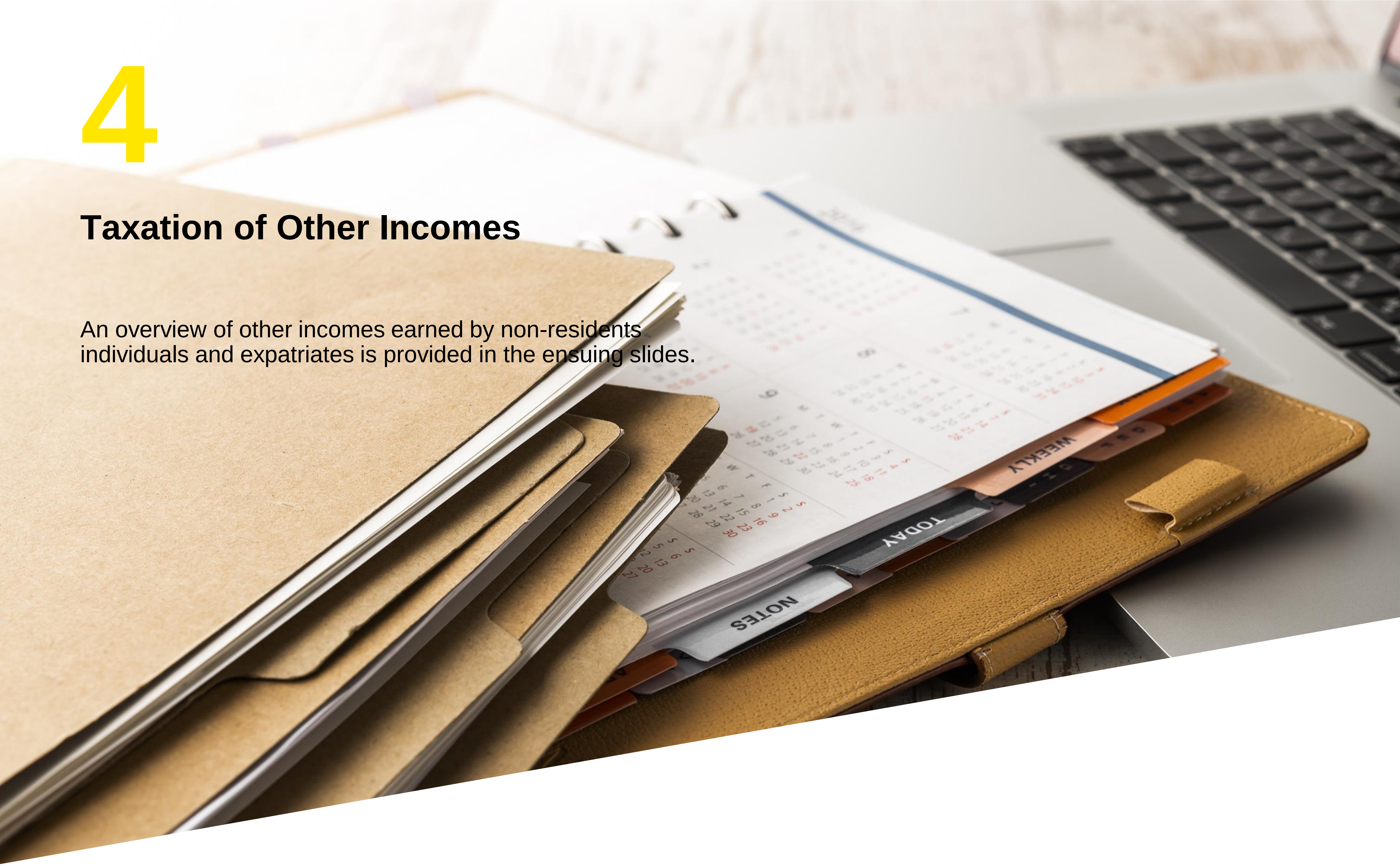
Other requirements for taxation of gain arising on indirect disposal include the following:

- Where the assets of the non-resident company are not wholly located in Pakistan, only income to the extent that is reasonably attributable to such assets located in Pakistan would be taxable;
- Where the assets in Pakistan are held through a resident company, such resident company shall be required to provide the prescribed information to the Commissioner Inland Revenue within 60 days of the date of transaction;
- The buyer would be required to withhold tax at the rate of 10% of the fair market value of the asset;
- Where the buyer has not withheld tax, the resident company is required to collect the requisite advance tax from the non-resident seller;
- The rate of tax applicable on the transaction and to be collected by the resident company shall be the higher of:
  - 20% of the gain (i.e. fair market value less cost of acquisition of the asset); or
  - 10% of the fair market value of the asset; and
- Where the tax has been withheld by the buyer or collected by the resident company, no tax shall be payable by the non-resident company in respect of the gain under the head “Income from Business” or “Capital Gains”.

4

Taxation of Other Incomes

An overview of other incomes earned by non-residents individuals and expatriates is provided in the ensuing slides.

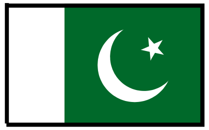


4 Other Incomes

An overview of taxation of dividends, profit on debt, royalty is provided below

Dividends	Profit on Debt	Royalty

When do dividends, profit on debt, royalty become Pakistan sourced?

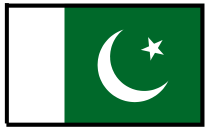


Dividends	Profit on Debt	Royalty
1. Paid by a resident company	1. Paid by a resident person*	1. Paid by a resident person*
2. Remittance of after tax profits of a Branch in Pakistan of a foreign company, with certain exceptions	2. Borne by a PE of a non-resident person in Pakistan	2. Borne by a PE of a non-resident person in Pakistan
	* Except where the profit is payable in respect of any debt used for business of a resident person outside Pakistan through a PE	* Except where royalty is payable in relation to any right, property, information used, or services utilized for business of a resident person outside Pakistan through a PE
The rate of tax for Dividends is 15%	The rate of tax for Profit on Debt is 10%	The rate of tax for Royalty is 15%

4 Other Incomes

An overview of taxation of Rental income, Fee for Technical Services and Fee for offshore digital services is provided below

When do fee for technical services and fee for offshore digital services become Pakistan sourced?



Rental Income

Derived from the lease of immovable property in Pakistan whether improved or not, or from any other interest in or over immovable property, including a right to explore for, or exploit, natural resources in Pakistan.

Taxed on net income basis.

Fee for Technical Services

1. Paid by a resident person*

2. Borne by a PE of a non-resident person

***except where the fee is payable in respect of service utilized in a business carried on by the resident person outside Pakistan through a PE**

The rate of tax for fee for technical services is 15%.

Fee for Offshore Digital Services

1. Paid by a resident person*

2. Borne by a PE of a non-resident person

***except where the fee is payable in respect of service utilized in a business carried on by the resident person outside Pakistan through a PE**

The rate of tax for offshore digital services is 10%.

Questions?

Thank you!