

# Taxation of Foreign Income and Jurisdiction of AEOI

By

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## Principle of Taxation

- Law recognizes taxation on residence status
  - accepted internationally
- Resident's income- section 11(5)
  - Pakistan source and foreign source
  - Based on Principle of WORLD INCOME
- Non resident's income- section 11 (6)
  - Pakistan source income only

# Who is non- resident?

- An Individual is resident – section 82
  - if he remains in Pakistan for more than 183 Days in a tax year
- If he lives less than 183 days in Pakistan
  - He is non-resident for that tax year
- Every tax year is a separate, distinct and self contained unit
- Individual may be resident in one tax year and he may be non-resident in next year and may be resident in third year
  - This all depends upon his stay in Pakistan in a tax year

# illustration

Particulars	A	B
Stay in Pakistan	110 days	186 days
Property income from UAE	One Million	One Million
Commission income from PSO	2 million	2 million
Business income from UK	3 million	3 million
Whether resident in Pakistan	?	?
Property income from UAE taxable in Pakistan	?	?
Whether commission income is taxable in Pakistan	?	?
Whether business income is taxable in Pakistan	?	?

## Special status in Pakistan

- 25<sup>th</sup> amendment abolishes special status for FATA and PATA
- Business income in previous area of FATA and PATA are exempt up to 2023 under clause 146 of Part 1 of second schedule
- [AJK and Gilgit Baltistan are not Pakistan for tax purposes](#)
- Income Tax Ordinance, 2001 doesn't apply at AJK and GB
- AJK and GB have separate legislation on taxes.
- They have adopted Income Tax Ordinance, 2001 to be applied in their jurisdiction by their tax administration

## Differential tax rate?

- Tax rates for non –resident individuals are same as are applicable for resident individuals
- Non discrimination provision of Treaty
- If treaty provides for higher tax rates then non-resident of Treaty country may invoke Non Discrimination provision of the Treaty and may pay tax equal to tax rates paid by the resident individuals
- If Treaty rates are lower than the rates applicable to resident individuals, then non- resident of the Treaty country may get benefit of Treaty rates notwithstanding higher tax rate to resident individuals

## Wealth statement u/s 116

- Non resident person shall not oblige to file wealth statement along with return of income under sub section (2)
- Non resident individual shall furnish wealth statement if he earns income from Final Tax Regime under sub section (4)
- Commissioner shall issue notice to non resident individual to furnish wealth statement under sub section (1)

## Foreign income and assets statement u/s 116A

- Resident individual having :
  - Foreign Income more than \$ 10,000., or
  - Foreign assets more than \$ 100,000
- Shall file statement u/s 116A declaring
  - Foreign assets and liabilities
  - Foreign assets transferred and consideration received
  - Complete particular of foreign income and expenditure
- He shall file return u/s 114 (2) (f)
- Commissioner may call for statement
- Non filing may attract penalty proceedings

## Non recognition of rules- Section 79

- Gain or loss shall be recognized on disposal of following assets in the hands of NON RESIDENT
  - By transmission of asset to an executor or beneficiary on the death of a person
  - By reason of gift
  - Between spouse living a part on agreement
  - By reason of compulsory acquisition of asset under any law
  - By company to its shareholders on liquidation of company
  - By an AOP to its members

## Royalty, FTS , offshore digital services

- Section 6 provides for special taxation on following payments to NR
  - Royalty
  - Fee for technical services
  - Fee for offshore digital services ( F.A. 2018)
- Taxation on the basis of gross receipts
  - Final taxation
  - No deduction of expenditure is admissible
  - No set off any loss
  - To tax credit is permissible
- Tax withholding : 15% on royalty or FTS , 5% on offshore digital service

Withholding U/S 152 on payments to non- resident

Sub-section	Nature of payment	Final or adjustable	Filer	Non filers
(1)	Royalty and Fee for Technical services	Final	15%	15%
(1A)	A contract or sub contract under a construction, assembly or Installation project	Final	7%	13%
	A contract for supply of supervisory activities to above project	Final	7%	13%
	Any other contract for construction or services rendering	Final	7%	13%
	A contract for advertisement services rendered by T.V Satellite Channel	Final	7%	13%
4A	Commissioner may issue exemption certificate having P.E			
(1AA)	Insurance premium or re-insurance premium	Final	5%	5%
(1AAA)	Advertisement services to NR media person relaying outside Pakistan	Adjustable	10%	10%
1C	Offshore digital services	Final	5%	5%

Withholding U/S 152 on payments to non- resident

Sub-section	Nature of payment	Final or adjustable	Filer	Non filers
2A	For sales of goods <u>by a company</u> to PE of NR	As Resident	4%	7%
	For sales of goods <u>by non company</u> to PE of NR	As Resident	4.5%	7.75%
	For rendering or providing <u>by a company</u> services to PE of NR	minimum	8%	14%
	For rendering or providing <u>by non company</u> services to PE of NR	minimum	10%	17.5%
	On the execution of contract to PE of NR	As Resident	7%	13%
	Sport persons		10%	10%
4A	Commissioner may issue exemption certificate			

## Withholding U/S 152 on payments to non- resident

Sub- section	Nature of payment	Final or adjustable	Filer	Non filers
3	Same WHT on salary 149, dividend 150, prize bond 156, commission of Resident			
	NO WHT IF TAX PAID BY AN AGENT OF NR U/S 172			
	NO WHT IF NR IS NOT CHARGEABLE TO TAX IN RESPECT OF THE AMONUT			
5	NR may seek exemption certificate from Commissioner			
5A	Commissioner may decide within 30 days NR request			
6	If decided against NR, withholding shall apply			
122B	NR may seek revision from Chief Commissioner against refusal			
Article 199	NR may file writ before High Court against refusal			

## Withholding U/S 152 on payments to non- resident

- NR shall not apply to CIR for exemption if title passed outside Pakistan
  - **EXCEPT:** Overall arrangement for supply of goods, installation, construction, assembly, commission, guarantees, supervisory and all or
    - principal activities performed by associate or its PE
    - Supply of goods is made by Resident or PE in Pakistan
- Educational or medical expenses as per SBP regulation
- Case law: 2010 PTD 1159 (Karachi H.C) EFU Insurance v/s Federation

## Exemption from WHT

- Section 152 imposes responsibility upon **PAYER** to deduct WHT or seek exemption from Commissioner
- In case Commissioner declined exemption request to payer
- And Chief Commissioner also decline interference u/s 122B
- Can NR itself seeks direct exemption from his Commissioner ?

## Case study 2

- Mr. A is non resident in Pakistan and earns five months salary income from Turkey entity for transmitting research data from Pakistan. Turkey entity remitted salary after deducting tax under Turkish Tax law.
- Whether Turkish Tax law applies?
- Whether such net salary is exempt from Pakistan tax?
- Whether salary is Pakistan source income?



## Case study 3

- Mr. A is non resident in Pakistan and earns five months salary income from Turkey entity for transmitting research data from Pakistan.
- He has made request to his foreign employer to pay his salary to his three kids who are getting education in Turkish University. Turkey entity made payments to his kids after deducting tax under Turkish Tax law.
- Whether Turkish Tax law applies?
- Whether such net salary is exempt from Pakistan tax?
- Whether salary is Pakistan source income?

## Case study 4

- Mr. A is a Chinese non resident individual entered into an agreement with Chinese firm and earns consultancy income of US\$ 25,000 from Chinese firm on KDA project. He completed this task within 35 days and left Pakistan
- He has subsequently entered into another agreement with another Chinese entity in China on Gawadar Project which was carried out for 125 days in China and 130 days in Pakistan. He earned consultancy income US\$ 120,000 and payments were remitted from Pakistan office of Chinese entity
- Tax Officer Quetta issued notice for taxing his Gawadar Income and Taxman at Karachi issued notice for Karachi income only
- How you will defend your client?

## Case study 5

- Mr. A is a Chinese non resident individual entered into an agreement with Chinese firm and earns consultancy income of US\$ 225,000 from Chinese firm on KDA project. He has sent his employee in Pakistan for 130 days in aggregate. Employee received salary of US\$ 30,000 in China. After getting consolidated data from his employee, he has completed this task within 35 days
- Tax Officer in Pakistan issued notice for taxing income of employee and employer.
- How you will defend your client?

## Case study 6

- Mr. A is a Chinese non resident individual entered into an agreement with Chinese firm and earns consultancy income of US\$ 25,000 from Chinese firm located at Karachi on KDA project. After getting consolidated data from consultancy firm in Pakistan on making payment of US\$ 7,000, he has completed this task within 35 days
- Tax Officer in Pakistan issued notice for taxing income.
- How you will defend your client?

## Case study 7

- Mr. A is an AJK resident and non resident individual in Pakistan entered into an agreement with Chinese firm and earns consultancy income of US\$ 25,000 from Chinese firm located at Karachi on KDA project.
- After getting consolidated data through internet from consultancy firm in Karachi on making payment of US\$ 7,000, he has completed this task within 35 days in AJK. Payments were paid to him in China
- He has however didn't deduct tax while making payment of US\$ 7000 to Pakistan firm
- Tax Officer in Pakistan issued notice for taxing income of Mr. A.

## Case study 8

- Mr A is dealing in stock exchange at Singapore. He has clients world over. His few clients were interested in Pakistan stock market. Mr. A on behalf of his clients entered into a business contract with Mr. B in Pakistan
- Mr. B on the instructions of Mr. A made number of dealings in Pakistan stocks and in this arrangement portfolio bank accounts were opened.
- Mr. B remitted commission income to Mr. A after deduction of tax u/s 233.
- Mr. A filed return in Pakistan and asked for refund of tax deduction
- Taxman intended to reject refund claim. How you will defend Mr. A?

## Case study 9

- Mr. A has three sons XYZ. Mr. X lives in USA and Mr. Y and Mr. Z are living in Pakistan. Mr. A has flat in USA and gifted the same to MR.Y
- Mr. A has a house at DHA Karachi and gifted to Mr. X and shop at Lahore to Mr. Z
- All events took place on 20-12-2016 in tax year 2017
- Mr. X came to Pakistan for registration for property only
- Meanwhile Mr. Z left Pakistan on 26Dec 2016 for business trip and export deals to UAE and Europe and came back after June 2017
- How you will file their return on the transaction of gift

## Case study 10

- Mr. A has two sons and both are living in USA. Son Mr. B came to Pakistan to look after his ailing father while Mr. C continued to live in USA. Mr. B stayed here from July 2016 to January 2017 and left Pakistan when his father expired on 25<sup>th</sup> Jan 2017
- Mr. A was owner of two plots at DHA Karachi
- Both plots were subsequently transferred in the name of both brothers
- Taxman issued notice to both heir for levy of tax on inheritance of assets
- How you will defend them?

## Case study 11

- Two brothers have domicile of Zob Baluchistan. But their CINC carried two residential addresses, one at Nazimabad Karachi and other at Zob. They bought house in Karachi for education purposes of their children
- Both have formed an AOP and got registered at Queeta showing place of business at Zob
- AOP won contract for road construction in the area of Zob from NHA through documents carrying postal address of Karachi
- AOP applied for exemption certificate which was refused by CIR Queeta
- Meanwhile they got correction and now CNIC shows Zob address only
- Whether CIR Queeta justified? How you will defend before CCIR?

## Case study 12

- Mr A lives in UAE and made supply of plant and machinery to M/s XYZ and title of goods was passed on in UAE. M/s XYZ incurred freight and insurance expenses and cleared port documents in its name as an importer
- M/S XYZ entered into another agreement with Mr.B, the brother of A who is resident in Pakistan for installation and commissioning of plant and machinery
- Whether M/S XYZ incurred any liability on import of plant and machinery ?
- Whether remittances of price of plant is chargeable to tax
- Whether Mr A and Mr. B are chargeable to tax as an AOP when both are not interface with each other. M/s XYZ has two separate agreements with them

## JURISDICTION OF AEOI

### **Information exchange Agreement- section 107**

The Federal Government may enter into

(i) Tax Treaty, (ii) Tax information exchange agreement, (iii) Multilateral convention, (iv) An inter-governmental agreement, (v) or similar agreement

**(a) for the avoidance of double taxation**

**(b) for the exchange of information for the prevention of fiscal evasion or avoidance of taxes**

**(c ) including automatic exchange of information with respect to taxes on income imposed under this Ordinance or any other law and under the corresponding laws in force in that country**

# Tax evasion and Avoidance

- Tax heaven
- Corporate re-structuring
- Merger
- De-merger
- Split of contracts
- Paper subsidiary
- Drug money
- Panama leak

# Tax heavens

S. No	Name of Tax Heaven	Under controlled	Entry into Force
1	Anguilla	UK	01-03-2014
2	Aruba	Netherland	01-09-2013
3	Bermuda	UK	01-03-2014
4	British Virgin Island	UK	01-03-2014
5	Cayman Island	UK	01-03-2014
6	Cura cao	Netherland	01-09-2013
7	Faroe Island	Denmark	01-06-2011
8	Gibraltar	UK	01-03-2014
9	Greenland	Denmark	01-06-2011
10	Guernsey	UK	01-08-2014
11	Hong kong	China	01-09-2018

# Tax heavens

S.No	Name of Tax Heaven	Under controlled	Entry into Force
12	Isle of Man	UK	01-03-2014
13	Jersey	UK	01-03-2014
14	Macau	China	01-09-2018
15	Montserrat	UK	01-10-2013
16	Sint Maarten	UK	01-09-2013
17	Turk & Caicas Island	UK	01-12-2013
SUMMARY			
	UK	11 Tax Heavens	
	Demark	2	
	Netherland	2	
	China	2	

## Multilateral instrument against offshore tax evasion and avoidance

- The Convention was developed jointly by the OECD and the Council of Europe in 1988
- It responded to G20 London Summit in 2009 to align with international standard on exchange of information
- It opens to all countries, to get benefit from new transparent environment.
- In G20 summit in Buenos Aires in 2018- the communique stated **"All jurisdictions should sign and ratify the multilateral Convention on Mutual Administrative Assistance in Tax Matters."**



## **Multilateral instrument against offshore tax evasion and avoidance**

- The Convention is the most powerful instrument for international tax cooperation.
- It provides for all forms of administrative assistance in tax matters:
  - exchange of information on request,
  - spontaneous exchange,
  - automatic exchange,
  - tax examinations abroad,
  - simultaneous tax examinations and assistance in tax collection.
- It guarantees extensive safeguards for the protection of taxpayers' rights.

## **Multilateral instrument against offshore tax evasion and avoidance- Current status**

- **127 jurisdictions** currently participate in the Convention
- This represents a wide range of countries including all G20 countries, all BRIICS, all OECD countries, major financial centers and number of developing countries.
- In May 2018, China extended the territorial scope of the Convention to the Hong Kong and Macau pursuant to Article 29 of the Convention.

**Multilateral instrument against offshore tax evasion**

- **Pakistan becomes 104th jurisdiction to join most powerful multilateral instrument against offshore tax evasion and avoidance**
- On 14/09/2016 at the OECD Headquarters in Paris, Mohammad Ishaq Dar, Minister of Finance of Pakistan, signed the [Convention on Mutual Administrative Assistance in Tax Matters](#) in the presence of OECD Secretary-General

**Multilateral instrument against offshore tax evasion and avoidance- Current status**

Name of Country	Signature	Deposit of Instrument	Entry into Force
Pakistan	14-09-2016	14-12-2016	01-04-2017
UAE	27-04-2017	21-05-2018	01-09-2018
Saudi Arabia	29-05-2013	17-12-2015	01-04-2016
Switzerland	15-10-2013	26-09-2016	01-01-2017

## Convention applies on Pakistan taxes

- Protocol Article 2, paragraph 1.a.i: **Income Tax.**
- Protocol Article 2, paragraph 1.b.iii.C: **Sales Tax.**
- Protocol Article 2, paragraph 1.b.iii.D: **Federal Excise Duty**

## Jurisdiction of AEOI

- Automatic Exchange of Information (AEOI) Commissioner is created to look after those taxpayers who owns offshore assets
- Jurisdiction is by name
- Six commissioners created, out of which three are functional at Karachi, Lahore and Islamabad
- Source of information
  - Multilateral Convention
  - Bilateral Agreement
  - Dubai property – Supreme Court Sou moto No. 2 of 2018
  - UK- Property and Rental information

## Jurisdiction of AEOI

- Multilateral Convention information is on Common Reporting Standard (CRS)
- 127 signatory countries have started to disseminate information in respect of their non-resident taxpayers
- However 45 signatory countries are receiving above information after qualification of prescribed conditions of OECD
- One of the conditions is to qualify ISO 27001 certificate for Data Security
- Only Two countries in Asia have qualified ISO 27001 – Pakistan- India

## Jurisdiction of AEOI

- Multilateral Convention send CRS in respect of following sources of income
  - Financial Institution
  - Insurance
  - Stocks
  - No immovable properties information
- Immovable property information is based on bi-lateral agreement basis OR on voluntarily basis

## Section 111(2)

- (2) The amount referred to in sub-section (1) shall be included in the person's income chargeable to tax:
- (i) in the tax year to which such amount relates if the amount representing investment, money, valuable article or expenditure **is situated or incurred in Pakistan or concealed income is Pakistan-source**; and
- (ii) in the tax year immediately preceding the tax year in which the investment, money, valuable article or expenditure is discovered by the Commissioner and **is situated or incurred outside Pakistan and concealed income is foreign-source**.
- Explanation.—For the removal of doubt, it is clarified that where the investment, money, valuable article or expenditure **is acquired or incurred outside Pakistan in a prior tax year and is liable to be included in the income of tax year 2018 and onwards on the basis of discovery made by the Commissioner during tax year 2019 and onwards** and the person explains the acquisition of such asset or expenditure from sources relating to tax year in which such asset was acquired or expenditure was incurred, such explanation shall not be rejected on the basis that the source does not relate to the tax year in which the amount chargeable to tax is to be included.]

## Section 111(2)(ii)

- Does PRIOR TAX YEAR include any assessment year when Income Tax Act, 1922 was applicable?
- *No. Income Tax Act, 1922 is dead statute by way of repealed provision under section 166 of Income Tax Ordinance, 1979*
- *Word Tax Year was alien in I.T.A, 1922*
- Does PRIOR TAX YEAR include any assessment year when Income Tax Ordinance, 1979 was applicable?
- *No. Income Ordinance 1979 dead statute by way of repealed provision under section-238 of Income Tax Ordinance, 2001*
- *Income Tax Ordinance, 2001 is applicable wef 01—7-2002 in the light of SRO 381(1)/2002 dated 15-06-2002 u/s sub section (3) of section 1 of ITO, 2001*
- *Word Tax Year was alien in I.T.O, 1979*

## Section 111(2)(ii)

- Does PRIOR TAX YEAR include all tax years from tax year 2003 and onwards?
- Does limitation of section 122 apply while applying provision of section 111(2)(ii) on foreign assets?

## Case study-13

- Foreign property worth Rs 20 M was purchased in tax year 2003 but not disclosed in wealth statement. Said asset was discovered on 20-01-2019. Whether provision of section 111(2) (b) applies in T.Y. 2018 ?

2018 ( Taxpayer's view)

Section 111(2)(b) applies to the tax year in which the asset is discovered. Since the asset was discovered on 20-01-2019, the provision of section 111(2)(b) applies in the tax year 2018-19.

2018 (department view)

Section 111(2)(b) applies to the tax year in which the asset is discovered. Since the asset was discovered on 20-01-2019, the provision of section 111(2)(b) applies in the tax year 2018-19.

## CASE STUDY-14

- Taxpayer has filed foreign assets amnesty in respect of property A in Dubai for worth of Rs50M purchased in 2013 and same was rented out to foreign bank. Rental income is deposited in bank.
- He didn't file domestic amnesty
- He received notice for non declaration of foreign rental income from 2013 to June 2018.
- Whether notice was justified?

## Foreign tax credit-103

- Resident of Pakistan in tax year 2018 has earned dividend of Rs 200,000, Interest income of Rs500,000 and business income of 1,000,000 in China. He paid taxes on all types of income in China. He is to be taxed in Pakistan on world income basis:-

Source of Income	Head of income	Income (RS)	Tax rate in China	Tax rate in Pakistan	Results
Foreign source	Dividend	200,000	10	12	Shall he pays 2% in Pakistan
Foreign source	Interest	500,000	10	10	0
Foreign source	Business	1,000,000	35	30	Shall get benefit of 5% in Pakistan
Pakistan source	Business	2,000,000		30	

## Ignored due to Paucity of time

- Section 50- Foreign source of short term resident individual
- Section 51- Foreign source income of returning expatriates
- Section 101- Geographical source of income
- Section 101A-Gain on Disposal of Assets Outside Pakistan
- Chapter IVA of Income Tax Rules, 2002 regarding “ documentation and country –by-country reporting requirements”

Q/A