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KPMG Taseer Hadi & Co.
Chartered Accountants

ANALYZING FINANCIAL STATEMENTS, WITHHOLDING OF TAXES & INCOME TAX RETURN FILING REQUIREMENTS

[*PRESENTED BY:*
KHALID MAHMOOD (FCA)

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Plan of presentation : topics to be covered

1. *Reading & relating financial statements for preparation of return*
2. *IFRS / IAS relating to the return of income*
3. *Tax adjustments – admissible & inadmissible tax deductions etc.*
4. *Withholding of taxes under various heads*
5. *Filing of returns (Basics)*
6. *Filing of wealth statement (Basics)*
7. *E-filing of statutory statements*

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What does it mean and what is its purpose?

Return of income is to be based on the figures covered in the financial statements, hence, the significance of the financial statements from tax point of view is much important.

Reading and relating the financial statements for return of income means analyzing the financial Statements with the perspective of Income Tax Ordinance 2001

- Basic components of audited financial statements:
  - Auditors' report to the members
  - Balance Sheet
  - Income Statement
  - Cash Flow Statement
  - Statement of Changes in Equity
  - Notes to the financial statements

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What does it mean and what is its purpose?

- Review of the fairness and appropriateness: Reading audit report to identify qualifications / emphasis covered in audit report (if any).

- Review of the financial statements to identify the following:
  - Business income,
  - Other income,
  - Accounting Depreciation, amortization,
  - Additions and disposals of fixed assets,
  - Taxes paid, by reviewing the Cash flow statement,
  - Penalties, provisions, and other inadmissible deductions for tax purposes, etc.

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IAS 12 – INCOME TAXES

As such, there is not any IFRS/IAS that relates directly to the preparation of return of income. However, IAS 12 is relevant for the recording and reconciling of income tax expense in the financial statements.

The objective of this standard is to address the differences in the amount of revenues and expenses recognized in a given period for taxation purposes and the corresponding amounts reported in the financial statements. The principle issue is how to account for the current and future tax consequences of transaction and other events of the current period that are recognized in the financial statements.

Relevant terms:

- Accounting Profit & Taxable income
- Deferred Tax
- Temporary differences
- Deferred Tax Assets & Deferred Tax Liabilities.

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IAS 12 – INCOME TAXES

Accounting Profit & Taxable Profit

Accounting profit is the profit disclosed by an entity in its financial statements prepared on the basis of accounting standards, whereas taxable income is the profit that is determined applying the relevant tax laws/rules.

Deferred Tax

Deferred Tax is any amount of tax that will be payable or deductible in future period when the carrying amount of an assets or liability will be settled in accordance with the prescribed rules relating to accounting items.

Temporary differences

These are the differences between the tax and financial reporting bases of assets and liabilities which will result in taxable or deductible amounts in future periods.

Taxable temporary Difference:

Taxable temporary differences result in a deferred tax liability i.e. future taxable amount.

Deductible temporary Difference:

Deductible temporary differences result in a deferred tax asset i.e. future on-taxable amount

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IAS 12 – INCOME TAXES

Identifying temporary differences

Balance sheet items	Taxable Temporary difference	Deductible temporary difference
Asset	Carrying amount greater than tax base	Tax base greater than carrying amount
Liability	Tax base greater than carrying amount	Carrying amount greater than tax base

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IAS 12 – INCOME TAXES

Deferred tax assets and Deferred tax liabilities

- A deferred tax asset is the amount of income tax recoverable in future periods in respect of deductible temporary differences. The most common form of deferred tax asset arises because of unused tax losses which are carried forward by the reporting entity.
- A deferred tax liability is the amount of income tax payable in future periods in respect of taxable temporary differences
- Deferred tax liability shall be recognized on all taxable temporary differences except to the extent that it arises from
  - Initial recognition of Goodwill
  - Initial recognition of an asset or liability in a transaction that:
    - Is not a Business combination; and
    - At the time of the transaction, affects neither accounting nor taxable profit (tax loss

  Such differences are known as permanent differences.

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IAS 12 – INCOME TAXES

A deferred tax asset shall be recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized, unless the deferred tax asset arises from the initial recognition of an asset or liability in a transaction that:

- Is not a business combination
- At the time of the transaction affects neither accounting profit not taxable profit (tax loss)

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Tax adjustments – admissible tax deductions

ADMISSIBLE DEDUCTIONS

- Section 20 provides that any expenditure incurred during the year wholly and exclusively for the purpose of business, will be an admissible expenditure.
- Whereas sections 22 to 31 lay down the rules for admissibility of following specific expenses / allowance:

Section	Expense / allowance
22	Depreciation
23	Initial allowance
23A	First year allowance
23B	Accelerated depreciation to alternate energy projects
24	Intangibles
25	Pre-commencement expenditure @ 20%
26	Scientific research expenditure
27	Employee training and facilities
28	Profit on debt, financial costs and lease payments
29	Bad debts
29A	Provision regarding consumer loans
30	Profit on non-performing debts of a banking company or development finance institution
31	Transfer to participatory reserve

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Tax adjustments – inadmissible tax deductions

INADMISSIBLE DEDUCTIONS

Section-21

- Cess, rate or tax levied on the profits or gain or assessed as percentage or otherwise of the profit or gain. S.21 (a)
- Amount of tax deducted from the amount derived by the person, sales of goods, services, execution of contract, export etc. s.21(b)
- Salary, rent, brokerage, Commission, profit on debt, payment to non-resident, payment for services or fee due to default of deduction or payment of tax S.21(c)
- Entertainment expenses in excess of prescribe limit or violation of conditions. S.21(d), Rule 10
- Contribution to unrecognized provident fund, unapproved pension fund, superannuation fund, gratuity fund. S 21(e)
- Contribution to employee beneficial fund and failure to make effective arrangement to secure tax deduction u/s 149 on the payment out of fund to the employee chargeable to tax S. 21(f)
- Fine, penalty paid or payable by the persons for the violation of law, rule or regulation S. 21(g)
- Personal expenditure incurred by the person. S.21(h)

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Tax adjustments – inadmissible tax deductions … *continued*

- Any amount carried to reserve fund or capitalized in any way S.21(i)
- Any profit on debt, brokerage, commission, salary or other remuneration paid by AOP to any member of the association. S.(21) (j)
- Expenditure paid or payable under single account head in aggregate exceeding Rs. 50,000 paid other than:
  - Cross Cheque payment
  - Cross bank Draft payment
  - Cross pay order payment
  - Other cross banking instruments,
  - Verifiable transfer of payment or
  - Verifiable credit card payment

  This clause not to apply in case of:
  - Expenditure not exceeding Rs. 10,000/-
  - Expenditure on account of utility bills, freight charges, travel fare, postage; and payment of taxes, duties, fee, fines or any other statutory obligation.

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Tax adjustments – inadmissible tax deductions … *continued*

- Any salary paid or payable exceeding Rs. 15,000/-per month other than cross cheque or direct transfer of fund to the employee's bank account S.21 (m)
- Any capital expenditure paid or payable other than allowed under the law. S.21 (n)
- Expenditure relating to FTR income. [S. 169, S. 67, Rule 13].
- Expenditure relating to exempt income.
- Expenditure in violation of section 174(2).
- Capital losses other than allowed by the law, damage or destruction of capital assets, premium on redemption of debt, discount on issue of shares, loss on the sale of business, expenditure or losses before the commencement or after the closure or discontinue.

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STEPS OF WITHHOLDING

- Determine nature of payment / receipt
- Determine applicable withholding tax provision including applicable rate and treaty provisions (if applicable)
- Determine status of payer as ‘withholding agent’ (prescribed person) – Section 153 and 152
- Determination of status of recipient – liable or exempt from withholding tax
- Deduction / collection (or non-deduction / collection), payment of tax
- Timing of deduction / collection – Section 158
- Deposit of tax and issuance of certificate – Sections 160 & 164 (Rules 42 and 43)
- Reporting through filing of statutory statements – Section 165 (Rule 44)
- Monitoring – Section 176

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CONSEQUENCES FOR DEFAULT IN WITHHOLDING TAX

- Disallowance of expense – Section 21(c)
- Recovery of tax not deducted from recipient – Section 162
- In case the amount is not recoverable from the recipient, recovery of tax not deducted from the payer, – Section 161
- Default surcharge for delayed deposit of tax deducted / collected - Section 205(3)
- Penalty – Section 182(1)

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COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
148	**Collection of tax at Imports**			
(a)	Value of goods inclusive of customs duty and sales tax imported by; - Industrial undertaking	5 / Exempt subject to conditions	Adjustable / Minimum in case of edible oil & packing materials	Adjustable / Minimum in case of edible oil & packing materials
	- Other companies	5	-	Final / adjustable subject to conditions
	- Other taxpayers	5.5	Final / adjustable subject to conditions	-

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Withholding of taxes under various heads

COMMON WITHHOLDING TAXES

S.No.	Taxable income	Rate of tax
Section 149 – Salary		
1	Where the taxable income does not exceed Rs.400,000	0%
2	Where the taxable income exceeds Rs.400,000 but does not exceed Rs.750,000	5% of the amount exceeding Rs.400,000
3	Where the taxable income exceeds Rs.750,000 but does not exceed Rs.1,400,000	Rs.17,500 + 10% of the amount exceeding Rs.400,000
4	Where the taxable income exceeds Rs.1,400,000 but does not exceed Rs.1,500,000	Rs.82,500 + 12.5% of the amount exceeding Rs.750,000
5	Where the taxable income exceeds Rs.1,500,000 but does not exceed Rs.1,800,000	Rs.95,000 + 15% of the amount exceeding Rs.1,500,000
6	Where the taxable income exceeds Rs.1,800,000 but does not exceed Rs.2,500,000	Rs.140,000 + 17.5% of the amount exceeding Rs.1,800,000
7	Where the taxable income exceeds Rs.2,500,000 but does not exceed Rs.3,000,000	Rs.262,500 + 20% of the amount exceeding Rs.2,500,000
8	Where the taxable income exceeds Rs.3,000,000 but does not exceed Rs.3,500,000	Rs.362,500 + 22.5% of the amount exceeding Rs.3,000,000
9	Where the taxable income exceeds Rs.3,500,000 but does not exceed Rs.4,000,000	Rs.475,000 + 25% of the amount exceeding Rs.3,500,000
10	Where the taxable income exceeds Rs.4000,000 but does not exceed Rs.7000,000	Rs.600,000 + 27.5% of the amount exceeding Rs.4000,000
11	Where the taxable income exceeds Rs.7000,000	Rs.1,425,000 + 30% of the amount exceeding Rs.7,000,000

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COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
150	**Dividend**			
(a)	Dividend distributed by purchaser of a power project privatized by WAPDA and company set up for power generation.	7.5	Final	Final
(b)	Dividend payment by other companies	10	Final	Final

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Withholding of taxes under various heads

COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
Section 152	**Payments to non-residents**			
(a)	Royalty and technical fee	15	Final	Final
(b)	Execution of a contract or sub-contract under the construction, assembly or installation project in Pakistan including a contract for the supply of supervisory activities in relation to such projects or any other contract for construction or services rendered relating thereto	6	Final subject to option	Final subject to option
(c)	Contract for advertisement services rendered by TV Satellite channel	6	Final subject to option	Final subject to option
(d)	Insurance premium or re-insurance premium	5	Final	Final
(e)	Advertisement services relaying from outside Pakistan	10	Final	Final
(e)	Profit on debt to non-resident person not having a PE in Pakistan	10	Adjustable / Final in specified situations	Adjustable / Final in specified situations
(f)	Other payments (other than Hajj Group Operator)	20	Adjustable	Adjustable
152(2A)	**Payments to PE of a non-resident**			
(a)	Sale of goods	3.5	Adjustable	Adjustable
(b)	Transport services	2	Adjustable	Adjustable
(c)	Other services	6	Adjustable	Adjustable
(d)	Execution of a contract	6	Adjustable	Adjustable

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Withholding of taxes under various heads

COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
153	Goods, services and execution of a contract			
(a)	Sales of rice, cotton seed or edible oils	1.5	Final / adjustable subject to conditions	Final (Adjustable manufacturer / listed company) / subject to conditions
(d)	Sale of any other goods in the case of; - Company	3.5	-	Final / (Adjustable for manufacturer / listed company)/ subject to conditions
	- Other tax payers	4	Final / adjustable subject to conditions	-
(f)	services (other than passenger transport) in the case of:			
	- Company	6	-	Adjustable
	- Other tax payers	7	Minimum	-
(g)	Execution of a contract in the case of; - Company	6	-	Final / Adjustable for listed company
	- Other tax payers	6.5	Final	-

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Withholding of taxes under various heads

COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
154	**Exports**			
(a)	Export proceeds, Proceeds from sales of goods to an exporter under an inland back-to-back letter of credit or any other arrangement, export of goods by an industrial undertaking located in an Export Processing Zone, Collection by a collector of customs at the time of clearing of goods exported	1	Final / adjustable subject to conditions	Final / adjustable subject to conditions
(b)	Indenting commission	5	Final / adjustable subject to filing of option & conditions	Final / adjustable subject to filing of option & conditions
156	**Prize and Winnings**			
(a)	Amount of prize bond winning	15	Final	Final
(b)	Prize on cross-word puzzle	15	Final	Final
(c)	Amount of raffle/lottery winning, prize on winning a quiz, prize offered by a company for promotion of sales	20	Final	Final

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Withholding of taxes under various heads

COMMON WITHHOLDING TAXES

Section	Type of payment	Rate %	STATUS OF TAX COLLECTED / DEDUCTED	
			Ind & AOP	Company
231A	**Cash withdrawal**			
	Cash withdrawal exceeding Rs 50,000	0.3 of the amount withdrawn	Adjustable	Adjustable
233	**Brokerage & Commission**			
(a)	Payment of brokerage and commission	10	Final	Final
(b)	Commission to advertisement agent	5	Final	Final

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FILING OF RETURN OF INCOME – APPLICABILITY - S. 114

- every company;
- every person (other than a company) whose taxable income for the year exceeds the maximum amount that is not chargeable to tax under this Ordinance for the year; or
- non-profit organization
- welfare institution approved
- any person not covered above, who:
  - has been charged to tax in respect of any of the two preceding tax years;
  - claims a loss carried forward under this Ordinance for a tax year;
  - owns immovable property with a land area of two hundred and fifty square yards or more or owns any flat located in areas falling within the municipal limits existing immediately before the commencement of Local Government laws in the provinces; or areas in a Cantonment; or the Islamabad Capital Territory.

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FILING OF RETURN OF INCOME – APPLICABILITY – S. 114 (*Continued*..)

- owns immoveable property with a land area of five hundred square yards or more located in a rating area;
- owns a flat having covered area of two thousand square feet or more located in a rating area;
- owns a motor vehicle having engine capacity above 1000 CC;
- has obtained National Tax Number;
- is the holder of commercial or industrial connection of electricity where the amount of annual bill exceeds rupees five hundred thousand.
- Members of Chamber of Commerce and Industry, trade or any business association, any market committee or any professional body including PEC, PMDC, Bar Councils, ICAP and ICMAP

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Filing of returns (basics)

METHOD OF FILING [s. 118]

Requirement of electronic filing of return of income by every company and an employee where the salary income exceeds Rs. 500,000

REVISION OF RETURN OF INCOME [s. 114 (6)& (6A)]

A person is entitled to revise a return of total income subject to the conditions that:

- the revised return is accompanied by the revised audited accounts,
- the reason for revision are duly filed
- taxable declared income is not less than and loss declared is not more than the declared income or loss, and
- prior approval of the Commissioner for the revision of return has been obtained.

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WEALTH STATEMENT – S. 116

Wealth statement covers the following information:

- the person's total assets and liabilities as on the date or dates specified in the notice;
- the total assets and liabilities of the person's spouse, minor children, and other dependents as on the date or dates specified in such notice;
- any assets transferred by the person to any other person during the period or periods specified in such notice and the consideration for the transfer;
- the total expenditures incurred by the person, and the person's spouse, minor children, and other dependents during the period or periods specified in the notice and the details of such expenditures; and
- the reconciliation statement of wealth.

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FILING OF WEALTH STATEMENT – APPLICABILITY S. 116

- every person required file the return of total income.
- Every person other than company and AoP filing statement under final tax regime under section 115, is required to file wealth statement irrespective of the quantum of tax paid during the year

REVISION OF WEALTH STATEMENT

Revised wealth reconciliation and the reason for revision of wealth statement to be submitted along with revised wealth statement.

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E-filing of withholding tax statement – S. 165 and 118

- Monthly statements – Salary & other than salary – By 15th day following end of month
- Annual statement of tax deduction from salary – By 31st August following end of financial year
- In addition to particulars prescribed, mention of CNIC & NTN would now be mandatory
- Requirement of filing of NIL statement to continue

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THANK YOU

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