Tax on corporate transactions in Pakistan: overview

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Country Q&A | Law stated as at 01-May-2020 | Pakistan

A Q&A guide to tax on corporate transactions in Pakistan.

The Q&A gives a high level overview of tax in Pakistan and looks at key practical issues including, for example: the main taxes, reliefs and structures used in share and asset sales, dividends, mergers, joint ventures, reorganisations, share buybacks, private equity deals and restructuring and insolvency.

To compare answers across multiple jurisdictions, visit the tax on corporate transactions *Country Q&A tool*.

The Q&A is part of the global guide to tax on transactions. For a full list of jurisdictional Q&As visit *global.practicallaw.com/taxontransactions-guide*.

Tax authorities

1. What are the main authorities responsible for enforcing taxes on corporate transactions in your jurisdiction?

A number of taxes may apply to corporate transactions, depending on the nature of the transaction. Under the Constitution of the Islamic Republic of Pakistan, taxes on income (personal and corporate), sales tax on goods and customs, regulatory and excise duty are within the exclusive domain of the federal government. The Federal Board of Revenue (FBR) (*www.fbr.gov.pk/*) is the revenue collection agency of the federal government.

Agricultural income tax, sales tax on services and tax on immovable property are provincial levies. The revenue collection agencies for sales tax on services are the:

- Sindh Revenue Board.
- Punjab Revenue Authority.
- Balochistan Revenue Authority.
- Khyber Pakhtunkhwa Revenue Authority.

Sales tax on services in the Islamabad Capital Territory is collected by the FBR.

Taxes on immovable property are collected by the provincial boards of revenue mentioned above and by local authorities. Agricultural income tax is collected by collectors appointed by the respective provincial governments of Pakistan.

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Pre-completion clearances and guidance

2. Is it possible to apply for tax clearances or obtain guidance from the tax authorities before completing a corporate transaction?

There is no mandatory requirement to apply for tax clearances from the tax authorities before completing a corporate transaction.

Advance rulings can only be sought by non-residents. The procedure for the issuance of an advance ruling is set out in Rule 231A of the Income Tax Rules 2002. A non-resident person wishing to seek an advance ruling must make an application to the FBR in the prescribed form. This application is considered by a committee set up under the Income Tax Rules 2002. The relevant Commissioner Inland Revenue (appointed in accordance with the provisions of the Income Tax Ordinance 2001) may provide comments to the committee regarding the application and, if he deems necessary, provide the advice of a legal expert on the application and decide the issue in a joint sitting or by circulation amongst its members. The advance ruling will be binding on the Commissioner only in respect of the specific transaction on which the advance ruling is issued. Note that the advance ruling will continue to remain in force unless there is a change in facts or in the law on the basis of which the advance ruling was pronounced.

The advance ruling will cease to be binding on the Commissioner if it is subsequently found to have been obtained by fraud or misrepresentation of the facts about the nature of the transaction on which the advance ruling was issued. An application filed under this rule is disposed of within 90 days of its receipt. The applicant can withdraw the application at any time before the advance ruling is issued.

Any taxpayer can apply to the Commissioner Inland Revenue for the issuance of an exemption or lower rate certificate. The certificate will be issued if the Commissioner is satisfied that an amount is one of the following:

- Exempt from tax under the Income Tax Ordinance 2001 (ITO).
- Subject to tax at a rate lower than the prescribed rate.
- Subject to a 100% tax credit under the ITO.

Furthermore, while it is possible to seek clarification or guidance from representatives of tax authorities via informal means (such as telephone conversations or email communications), such clarification or guidance is not legally binding.

Disclosure of corporate transactions

3. Is it necessary to disclose the existence of any corporate transactions to the tax authorities?

There is no specific requirement to disclose the existence of corporate transactions to tax authorities.

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If any tax must be collected or withheld from any amount payable in connection with a corporate transaction, the withholding or collection agent (as the case may be) must disclose the nature of the payment and the particulars of the payer, or recipient, in the bi-annual statements that must be filed with the FBR.

Furthermore, these transactions may, depending on their nature, need to be disclosed in the taxpayer's income tax return that must be filed annually. The income tax return must be accompanied by:

- Applicable documents.
- Statements.
- Certificates.
- Annexes.
- In the case of companies, the income tax return must be accompanied by audited accounts and reconciliation of profits as per the accounts and taxable income as declared in the return.

At the time the income tax return is filed, it may be necessary to disclose certain corporate transactions to the tax authorities under the first and last bullet points listed above.

Main taxes on corporate transactions

Transfer taxes and notaries' fees

> 4. What are the main transfer taxes and/or notaries' fees potentially payable on corporate transactions?

Stamp duty

Key characteristics. Instruments through which property (movable or immovable) is transferred are subject to stamp duty under the Stamp Act, 1899.

Triggering event. Stamp duty is payable on or before the execution of the instrument in Pakistan. Where an instrument is executed outside Pakistan, stamp duty is payable within three months of the instrument being brought into Pakistan.

Liable party/parties. The person liable for stamp duty can vary, depending on the province in which the instrument is executed. Generally, stamp duty is payable by the following parties:

- The person drawing, making or executing any of the following instruments:
    - administration bond;
    - agreement relating to deposit of title deeds;

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    - pawn or pledge;
    - bill of exchange;
    - bond;
    - bottomry bond;
    - customs bond;
    - debenture;
    - further charge;
    - indemnity bond;
    - mortgage deed;
    - promissory note;
    - release;
    - respondentia bond;
    - security bond;
    - settlement;
    - transfer of shares in an incorporated company or other body corporate;
    - transfer of debentures (being marketable securities, whether the debenture is liable to duty or not);
    - transfer of any interest secured by a bond, mortgage deed or policy of insurance.
- The person effecting the insurance in the case of a policy of insurance (other than fire insurance).
- The person issuing the policy in the case of a policy of fire insurance.
- The lessee, or intended lessee, in the case of a lease or agreement to lease.
- The grantee in the case of a conveyance (including a re-conveyance of mortgaged property).
- The lessor in the case of a counterpart of a lease.
- The parties in equal shares in the case of an instrument of exchange.
- The purchaser of the property to which a certificate of sale relates in the case of a certificate of sale.
- The parties to an instrument of partition in proportion to their respective shares in the whole property partitioned, or, when the partition is made in execution of an order passed by a revenue authority, civil court or arbitrator, in such proportion as such authority, court or arbitrator directs.

Applicable rate(s). Stamp duty is a provincial levy, and the rates are revised from time to time by means of provincial legislation. Prescribed rates under the relevant provincial stamp schedule apply.

Capital value tax (CVT)

Key characteristics. CVT is charged on the capital value of the immovable property, motor vehicles, shares in listed companies, modaraba certificates and instruments of redeemable capital. The tax is payable on the purchase of such an asset,

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or the purchase of a right to the use the asset for more than 20 years. CVT on immovable property is a provincial levy, whereas CVT on all the other assets mentioned above is a federal levy. CVT on immovable property is no longer applicable in Punjab.

Triggering event. CVT is payable at the time of registering or attesting the transfer of the assets.

Liable party/parties. CVT is payable by the transferee of the assets.

Applicable rate(s). The prescribed rates of CVT vary. For example, the following rates of CVT apply:

- For commercial and industrial immovable property situated in the province of Sindh, the rate is either:
  - a standard rate of 1.5% of the value of the immovable property, as ascertained in the applicable valuation table (where the immovable property's value in the transfer document matches, or is less than, the value attributed to it in the valuation table); or
  - where the immovable property's value exceeds the value determined in the valuation table, CVT is charged at a floating rate, which is calculated as the value determined in the valuation table, divided by the actual value of the immovable property, multiplied by the standard CVT rate (1.5%).
- The floating rate of CVT is only charged where the actual value of the immovable property (that is, the value of the immovable property as recorded in the transfer document) exceeds the value determined in the valuation table.
- 0.02% of the purchase value is charged on the purchase of modaraba certificates of any instrument of redeemable capital.
- 0.01% of the purchase value is charged on the purchase of shares of a public company listed on the stock exchange.

Registration fee

Key characteristics. Instruments of transfer used to transfer an interest in immovable property must be registered under the Registration Act 1908 to effectuate the transfer, and are subject to a registration fee.

Triggering event. The registration fee must be paid within four months of the execution of the instrument.

Liable party/parties. The transferee/lessee/beneficiary of the instrument of transfer must pay the registration fee.

Applicable rate(s). The registration fee is equal to 1% of the value of the property transferred (in the relevant jurisdiction).

Corporate and capital gains taxes

5. What are the main corporate and/or capital gains taxes potentially payable on corporate transactions?

Capital gains tax on a disposal of securities

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Key characteristics. Capital gains tax is chargeable on the disposal of securities, which are defined under the Income Tax Ordinance 2001 (ITO) as:

- A share of a public company.
- A voucher of the Pakistan Telecommunications Corporation.
- A modaraba certificate.
- An instrument of redeemable capital.
- Debt securities and derivative products.

For the purposes of calculating the gain arising on the disposal of a security by a person, the cost of acquisition of the security is deducted from the consideration received by the person on disposal of the security.

Triggering event. A disposal of securities triggers the tax.

Liable party/parties. The party disposing of the securities is liable to pay the capital gains tax.

Applicable rate(s). A capital gain arising on or after 1 July 2010 from a disposal of securities (other than a gain that is exempt under the ITO) is subject to capital gains tax at the following rates for the 2019-2020 tax year (depending on the duration of the period for which the securities have been held):

- For securities acquired before 1 July 2016 where the holding period of a security is less than 12 months: the rate is 15%.
- For securities acquired after 1 July 2016 where the holding period of a security is less than 12 months: the rate is 15%.
- For securities acquired before 1 July 2016 where the holding period of a security is 12 months or more but less than 24 months: the rate is 12.5%.
- For securities acquired after 1 July 2016 where the holding period of a security is 12 months or more but less than 24 months: the rate is 15%.
- For securities acquired before 1 July 2016 where the holding period of a security is 24 months or more but the security was acquired on or after 1 July 2013: the rate is 7.5%.
- For securities acquired after 1 July 2016 where the holding period of a security is 24 months or more but the security was acquired on or after 1 July 2013: the rate is 15%.
- Where the security was acquired before 1 July 2013: the rate is 0%.

Capital gains tax on a disposal of immovable property

Key characteristics. The gain arising on the disposal of immovable property is subject to capital gains tax.

The gain arising on the disposal of immovable property which constitutes an open plot, where the holding period of that open plot does not exceed one year, is calculated by deducting the cost of acquiring that property from the consideration received by the person on the disposal of that property.

The gain arising on the disposal of immovable property which constitutes an open plot, where the holding period of that open plot exceeds one year but does not exceed eight years, is calculated by deducting the cost of acquiring that property from the consideration received by the person on the disposal of that property and multiplying that amount by 0.75.

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No gain will arise on the disposal of immovable property which constitutes an open plot where the holding period of that open plot exceeds eight years.

The gain arising on the disposal of immovable property which constitutes a constructed property, where the holding period of that constructed property does not exceed one year, is calculated by deducting the cost of acquiring that property from the consideration received by the person on the disposal of that property.

The gain arising on the disposal of immovable property which constitutes a constructed property, where the holding period of that constructed property exceeds one year but does not exceed four years, is calculated by deducting the cost of acquiring that property from the consideration received by the person on the disposal of that property and multiplying that amount by 0.75.

No gain will arise on the disposal of immovable property which constitutes a constructed property where the holding period of that constructed property exceeds four years.

Triggering event. The disposal of immovable property triggers the tax.

Liable party/parties. The party disposing the immovable property is liable to pay the tax.

Applicable rate(s). For the purposes of calculating the gain, the consideration received on a disposal of immovable property cannot be less than the fair market value of the immovable property. The fair market value of the immovable property at the time of the disposal is determined with reference to valuation tables that are notified by the FBR, and where the valuation tables are not notified, by the valuation tables notified by the District Officer (Revenue) or the provincial or any other authority authorised in this regard for the purposes of stamp duty.

The capital gain on a disposal of immovable property is subject to the following rates of capital gains tax:

- Where the gain does not exceed PKR5 million: 5%.
- Where the gain exceeds PKR 5 million but does not exceed PKR10 million: 10%.
- Where the gain exceeds PKR10 million but does not exceed PKR15 million: 15%.
- Where the gain exceeds PKR15 million: 20%.

The capital gains tax due is payable in the same year as the disposal occurs.

Capital gains tax on a disposal of capital assets (other than securities or immovable property)

Key characteristics. A “capital asset” means property of any kind held by a person (whether or not that property is connected with a business), but does not include:

- Any stock-in-trade, consumable stores or raw materials held for a business purpose.
- Any property with respect to which the person holding the property is entitled to a depreciation deduction or amortisation deduction under the law.
- Any movable property held for personal use by the person holding the property, or held for personal use by any member of the person’s dependent family.

Shares in private limited companies are capital assets for the purposes of calculating capital gains tax on a disposal of capital assets.

Any gain arising on the disposal of a capital asset is subject to capital gains tax. Gains on capital assets are calculated by

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deducting the cost of acquiring the asset from the consideration received by the person disposing of that asset.

Where a capital asset has been held by a person for more than one year, the amount of gain arising on the disposal of the asset is calculated by first determining the gain (by calculating the difference between the consideration received by the person on the disposal of the asset and the cost of the asset) and then multiplying the calculated gain by three quarters.

Triggering event. The disposal of a capital asset triggers the tax.

Liable party/parties. The party disposing of the capital asset is liable to pay the tax.

Applicable rate(s). The gains calculated (as outlined above) are added to the corporate income of companies, which is subject to the corporate rate of tax payable by companies at the end of the tax year. The rate of corporate tax imposed on the taxable income of a company (other than a banking company) is:

- 32% for the tax year 2016.
- 31% for tax year 2017.
- 30% for tax year 2018.
- 29% for tax year 2019 and subsequent tax years.

Gain on disposal of assets outside Pakistan

Key characteristics. Any gain arising from the disposal or alienation outside Pakistan of any asset located in Pakistan of a non-resident company is chargeable to tax in Pakistan. Where the asset is any share or interest in the non-resident company, the asset will be treated as located in Pakistan if the share or interest derives its value principally from the assets located in Pakistan and shares or interest of 10% or more of the share capital of the non-resident company are disposed or alienated.

The share or interest will be treated to have derived its value principally from the assets located in Pakistan if on the last day of the tax year preceding the date of transfer of the share or interest, the value of such assets exceeds PKR100 million and represents at least 50% of the value of the assets owned by the non-resident company.

Where the entire assets of the non-resident company are not located in Pakistan, the income of the non-resident company, from disposal or alienation outside of Pakistan of a share or interest in the non-resident company will be treated as located in Pakistan to the extent it is reasonably attributable to assets located in Pakistan and determined in the prescribed manner.

Triggering event. The disposal of assets outside Pakistan triggers tax.

Liable party/parties. The party disposing of the capital asset is liable to pay the tax.

Applicable rate(s). Tax in respect of the above will be charged at either 20% of the fair market value less cost of the acquisition of the asset or 10% of the fair market value of the asset, whichever is higher.

Advance tax payable by the purchaser or transferee of immovable property

Key characteristics. Persons responsible for registering, recording or attesting the transfer of immovable property must collect advance tax from the purchaser or transferee on behalf of the federal government. The advance tax is adjustable against the final tax liability for the purchaser or transferee for the tax year.

Triggering event. The registration, recording or attestation of a transfer of immovable property triggers the advance tax.

Liable party/parties. The purchaser or transferee of the immovable property is liable to pay the tax.

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Applicable rate(s). The following rates of advance tax are applied:

- 1% of the fair market value for taxpayers appearing in the Active Taxpayers' List.
- 2% of the fair market value for persons not appearing in the Active Taxpayers' List (in effect, the rate of tax applicable to taxpayers appearing on the Active Taxpayers' List is increased by 100% for those taxpayers not appearing on the Active Taxpayers' List).

The fair market value is calculated using the valuation tables which are applied on a disposal of immovable property (*see above, Capital gains tax on a disposal of immovable property*).

For the purposes of the ITO, the Active Taxpayers' List means the list instituted by the board under the ITO and includes such lists issued by the Azad Jammu and Kashmir Central Board of Revenue or the Gilgit-Baltistan Council Board of Revenue (the "Active Taxpayers' List"). The ITO empowers the FBR to institute an Active Taxpayers' List. As such, the Finance Act 2019 has replaced the concept of a distinction between filers and non-filers (introduced by the Finance Act, 2014) with the concept of a distinction between taxpayers that appear in the Active Taxpayers' List and persons that do not appear in the same. As regards persons not appearing in the Active Taxpayers' List, the collection or deduction of advance income tax, the calculation of income and the tax payable thereon will be determined in accordance with the rules appearing in the Tenth Schedule to the ITO. That schedule provides that where tax is required to be deducted or collected under the ITO from persons not appearing in the Active Taxpayers' List, the rate of tax required to be deducted or collected, as the case may be, will be increased by 100% of the relevant rate otherwise specified in the ITO.

Advance tax payable by the seller or transferor of immovable property

Key characteristics. Persons responsible for registering, recording or attesting the transfer of immovable property must collect advance tax from the seller or transferor on behalf of the federal government. The advance tax is adjustable against the final tax liability of the seller or transferor for the tax year. However, advance tax does not need to be collected if the immovable property has been held for more than five years.

Triggering event. The registration, recording or attestation of a transfer of immovable property triggers the advance tax.

Liable party/parties. The seller or transferor of the immovable property is liable to pay the tax.

Applicable rates. Advance tax is charged at the following rates:

- 1% of the gross amount of consideration received for taxpayers in the Active Taxpayers' List.
- 2% of the gross amount of consideration received for persons not appearing in the Active Taxpayers' List (the rate of tax set out for taxpayers appearing in the Active Taxpayers' List is effectively increased for persons not appearing in the Active Taxpayers' List by 100%).

For the purposes of calculating the advance tax, the value of the immovable property (that is, the consideration received on the disposal of the immovable property) cannot be less than the fair market value that is calculated using the valuation tables which are applied on a disposal of immovable property (*see above, Capital gains tax on a disposal of immovable property*).

Corporate tax

There are no corporate taxes specifically applicable to corporate transactions. The income of companies is subject to the corporate rate of tax payable by companies at the end of the tax year. The rate of corporate tax imposed on the taxable income of a company (other than a banking company) is:

- 32% for the tax year 2016.

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- 31% for tax year 2017.
- 30% for tax year 2018.
- 29% for tax year 2019 and subsequent years.

Value added and sales taxes

6. What are the main value added and/or sales taxes potentially payable on corporate transactions?

Sales tax on goods

Key characteristics. Under the Sales Tax Act 1990 (STA), a sales tax is charged on:

- Taxable supplies made by a registered person in the course or furtherance of any taxable activity carried on by that person.
- Goods imported into Pakistan.

Triggering event. A “taxable supply” is defined under the STA as a supply of taxable goods made by an importer, manufacturer, wholesaler (including dealer), distributor or retailer, other than a supply of goods which is exempt or chargeable to tax at a rate of 0% under the STA.

Liable party/parties. In the case of a supply of goods, the liable party is the person making the supply of goods. In the case of goods imported into Pakistan, the liable party is the person importing the goods.

Applicable rate(s). The applicable rate is 17% of the value of the taxable supplies made by a person registered under the STA in the course of, or the furtherance of, any taxable activity carried on by that person, and on the value of the goods imported into Pakistan.

The applicable rate is 19% where taxable supplies are made to a person not registered under the STA. For certain goods, reduced rates are specified by the FBR from time to time.

Sales tax on services

Key characteristics. Sales tax on services is a provincial tax levied in Pakistan. It is levied as a value added tax. The following provincial laws are currently in force:

- Sindh Sales Tax on Services Act 2011.
- Punjab Sales Tax on Services Act 2012.
- Balochistan Sales Tax on Services Act 2011.
- Khyber Pakhtunkhwa Sales Tax on Services Act 2013.

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- Islamabad Capital Territory (Tax on Services) Ordinance 2001.

Sales tax is payable where:

- A service is provided by a resident registered person from his registered office or place of business in the respective province, in the course of an economic activity (including in the commencement or termination of the activity).
- A service is provided to a resident person (being a resident of the respective province) by a non-resident person in the course of an economic activity (including the commencement or termination of the activity).

Triggering event. The provision of a service triggers the tax.

Liable party/parties. Where the services are provided by a resident registered person, the liability to pay the tax is on the resident registered person providing the service. Where the services are provided by a non-resident person, the liability to pay the tax is on the resident person receiving the service.

Applicable rate(s). Taxable services are listed in the Second Schedule to each of the above Acts. The rates vary from 5% to 19.5%.

Other taxes on corporate transactions

7. Are any other taxes potentially payable on corporate transactions?

Other taxes may be applicable, depending on the nature of the corporate transaction.

Taxes applicable to foreign companies

8. In what circumstances will the taxes identified in *Questions 4* to *7* be applicable to foreign companies (in other words, what "presence" is required to give rise to tax liability)?

Establishing "presence" for non-resident companies in Pakistan

A non-resident is only liable to pay income tax on Pakistan-source income. A person is a non-resident person for a tax year if the person is not a resident person for that year. An individual is considered a resident individual for a tax year if the individual is either:

- Present in Pakistan for a period of, or periods amounting in aggregate to, 183 days or more in the tax year.
- Present in Pakistan for a period of, or periods amounting in aggregate to, 120 days or more in the tax year and, in the

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four years preceding the relevant tax year, has been in Pakistan for a period of, or periods amounting in aggregate to, 365 days or more.

- Is an employee or official of the federal government or a provincial government posted abroad in the tax year.

A company is a resident company for a tax year if any of the following apply:

- It is incorporated or formed by or under any law in force in Pakistan.
- The control and management of the affairs of the company is situated wholly in Pakistan at any time in the year.
- It is a provincial government or local government in Pakistan.

A non-resident company may also be subject to income tax in Pakistan if it has a permanent establishment in Pakistan. A permanent establishment is defined in the Income Tax Ordinance 2001 as a fixed place of business through which the business of the person is wholly or partly carried on, and includes, among other things:

- A place of management, branch, office, factory or workshop.
- The furnishing of services, including consultancy services, by any person through employees or other personnel engaged by the person for such a purpose.
- The installation of any substantial equipment, or any other asset or property, capable of activity giving rise to income.

Double tax treaties can also specify the nature of the presence required to give rise to the existence of a permanent establishment of a non-resident company in Pakistan. A permanent establishment is treated as a distinct entity for the purposes of income tax.

Business income

The following business incomes are classified as Pakistan-source income:

- Business income derived from any business carried on in Pakistan.
- Business income of a non-resident person will be Pakistan-source income to the extent to which it is directly or indirectly attributable to:
  - a permanent establishment of the non-resident person in Pakistan;
  - sales in Pakistan of goods merchandise of the same or similar kind as those sold by the person through a permanent establishment in Pakistan;
  - other business activities carried on in Pakistan of the same or similar kind as those effected by the non-resident through a permanent establishment in Pakistan; or
  - any business connection in Pakistan; or
  - import of goods, whether or not the title to the goods passes outside Pakistan, if the import is part of an overall arrangement for the supply of goods, installation, construction, assembly, commission, guarantees or supervisory activities and all or principal activities are undertaken or performed either by the associates of the person supplying the goods or its permanent establishment, whether or not the goods are imported in the name of the person, associate of the person or any other person.
- Where the business of a non-resident person comprises the rendering of independent services (including professional services and the services of entertainers and sports persons), the Pakistan-source business income of the person will

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include any remuneration derived by that person where the remuneration is paid by a resident person, or borne by a permanent establishment in Pakistan of a non-resident person.

Capital gains

Any gain from the disposal of any asset or property used in deriving any business income referred to above is treated as Pakistan-source income.

Controlled foreign company

Income attributable to controlled foreign company will be included in the taxable income of a resident person for a tax year.

Controlled foreign company means a non-resident company if:

- More than 50% of the capital or voting rights of the non-resident company are held, directly or indirectly, by one or more persons resident in Pakistan or more than 40 persons resident in Pakistan or more than 40% of the capital or voting rights of the non-resident company are held, directly or indirectly, by a single resident person in Pakistan.
- Tax paid, after taking into account any foreign tax credits available to the non-resident company, on the income derived or accrued, during a foreign tax year, by the non-resident company to any tax authority outside Pakistan is less than 60% of the tax payable on the said income under the ITO.
- The non-resident company does not derive active business income.
- The shares of the company are not traded on any stock exchange recognised by law of the country or jurisdiction of which the non-resident company is resident for tax purposes.

Income of a controlled foreign company is an amount equal to the taxable income of that company determined in accordance with the provisions of the ITO as if that controlled foreign company is a resident taxpayer, and will be taxed at 15%.

The amount of attributable income for a tax year will be computed by multiplying the income of a controlled foreign company by the percentage of capital or voting rights, whichever is higher, held by the person, directly or indirectly, in the controlled foreign company.

The attributable income will be treated as zero, if the capital or voting rights of the resident person is less than 10%. Income of a controlled foreign company will be treated as zero, if it is less than PKR10 million.

Dividends

9. Is there a requirement to withhold tax on dividends or other distributions?

Dividends

Under the Income Tax Ordinance 2001 a dividend includes, among other things:

- Any distribution by a company of accumulated profits to its shareholders.

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- Any distribution by a company on the reduction of its capital to its shareholders.
- Remittance of after tax profit of a branch of a foreign company operating in Pakistan.

Every person paying a dividend must deduct tax from the gross amount of the dividend paid at the following rates if such tax is being deducted from persons that appear in the Active Taxpayers' List:

- 7.5% where the dividend is paid by Independent Power Purchasers where such dividend is a pass-through item under an Implementation Agreement, or Power Purchase Agreement, or Energy Purchase Agreement and is required to be reimbursed by the Central Power Purchasing Agency (CPPA) or its predecessor or successor entity.
- 15% in all cases other than those mentioned in the bullet point above.

Every person paying a dividend must deduct tax from the gross amount of the dividend paid at the following rates if such tax is being deducted from persons that do not appear in the Active Taxpayers' List:

- 15% where the dividend is paid by Independent Power Purchasers where such dividend is a pass-through item under an Implementation Agreement, or Power Purchase Agreement, or Energy Purchase Agreement and is required to be reimbursed by the CPPA or its predecessor or successor entity (this is effectively the rate applicable to taxpayers appearing on the Active Taxpayers' List, increased by 100%).
- 30% in all cases other than those mentioned in the bullet point above.

These tax rates may be reduced if a double tax treaty applies, provided that the conditions specified in the treaty are met. Generally, these treaties provide for a ceiling in the applicable withholding rate of 10% or 15% of the gross amount paid, provided the conditions provided for in the treaty are met.

Profit on debt

The payer of interest or profit on debt on an instrument of any kind (other than a loan agreement between a borrower and a banking company or a development finance institution) to any person other than a financial institution must deduct tax at the following rates:

- Where the person receiving such profit on debt appears in the Active Taxpayers' List, the rate is:
  - 15% on the yield or profit, where that yield or profit exceeds PKR500,000;
  - 10% on the yield or profit, where that yield or profit is PKR500,000 or less.
- Where the person receiving such profit on debt does not appear in the Active Taxpayers' List, the rate is:
  - 30% on the yield or profit, where that yield or profit exceeds PKR500,000;
  - 20% on the yield or profit, where that yield or profit is PKR500,000 or less.
- The rate of tax applicable to persons appearing on the Active Taxpayers' List is effectively increased by 100% for those persons not appearing on the Active Taxpayers' List.

Share acquisitions and disposals

Taxes potentially payable

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10. What taxes are potentially payable on a share acquisition/share disposal?

The following taxes are payable on a share acquisition/share disposal:

- Stamp duty (*see Question 4, Stamp duty*).
- Capital gains tax (*see Question 5, Capital gains tax on a disposal of securities*).

Exemptions and reliefs

11. Are any exemptions or reliefs available to the liable party?

Stamp duty

Any instrument executed outside of Pakistan is not chargeable to stamp duty. If such an instrument is brought into Pakistan after execution, the applicable stamp duty must be paid within three months after the instrument has been first received in Pakistan. However, if the instrument in respect of such a transaction is executed in electronic form, no stamp duty is payable.

Capital gains tax

The liability to pay capital gains tax on a disposal of securities does not apply to banking and insurance companies.

No gains arise on, among other things, the issuance or receipt of shares as a result of a scheme of arrangement and reconstruction under the applicable law and approved by either the High Court, the State Bank of Pakistan, or the Securities and Exchange Commission of Pakistan (as the case may be) on or after 1 July 2007.

Tax advantages/disadvantages for the buyer

12. Please set out the tax advantages and disadvantages of a share acquisition for the buyer.

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Advantages

Transfer taxes on a share acquisition are generally lower than transfer taxes on the acquisition of immovable property. Sales tax is not applicable on a sale of shares.

Disadvantages

The seller may not be willing to provide appropriate warranty/indemnity protection to the buyer in the event of any unknown tax liabilities arising.

Tax advantages/disadvantages for the seller

13. Please set out the tax advantages and disadvantages of a share disposal for the seller.

Advantages

There are no particular advantages.

Disadvantages

The seller may be required to provide extensive tax warranties or indemnities to the buyer in relation to any future tax liabilities.

In the event the seller sustains a loss on the disposal of securities in a tax year, the loss can only be set off against the gain of the seller from any other securities chargeable to tax under the provisions on the disposal of securities, and no loss is carried forward to the subsequent tax year.

However, if the seller sustains a loss on the disposal of securities in a tax year:

- The loss can only be set off against the gain of the seller from any other securities chargeable to tax under the provisions on the disposal of securities.
- No loss is carried forward to the subsequent tax year, as long as the amount of the loss sustained on disposal of securities in the tax year 2019 and onwards has not been set off against the gain of the person from disposal of securities chargeable to tax will be carried forward to the following tax year and set off only against the gain of the person from disposal of securities chargeable to tax.
- No such loss shall be carried forward to more than three tax years immediately succeeding the tax year for which the loss was first computed.

Transaction structures to minimise the tax burden

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14. What transaction structures (if any) are commonly used to minimise the tax burden?

The transaction structures commonly used in Pakistan to minimise the tax burden are overseas holding companies incorporated in low tax jurisdictions which have favourable tax treaties with Pakistan. However, where the tax authorities establish that such a structure lacks substantial economic substance, it is possible for the tax authorities to disregard the structure.

Asset acquisitions and disposals

Taxes potentially payable

15. What taxes are potentially payable on an asset acquisition/asset disposal?

An asset can either be movable or immovable property. The applicable taxes on an asset acquisition/asset disposal are outlined below.

Movable property

The following taxes can apply to an acquisition of movable property:

- Stamp duty (*see Question 4, Stamp duty*).
- Capital value tax (*see Question 4, Capital value tax (CVT)*).

Immovable property

The following taxes can apply to an acquisition of immovable property:

- Stamp duty (*see Question 4, Stamp duty*).
- Capital value tax (*see Question 4, Capital value tax (CVT)*).
- Registration fee (*see Question 4, Registration fee*).
- Advance tax (*see Question 5, Advance tax payable by the purchaser or transferee of immovable property* and *Question 5, Advance tax payable by the seller or transferor of immovable property*).

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Exemptions and reliefs

16. Are any exemptions or reliefs available to the liable party?

Stamp duty

Any instrument executed outside of Pakistan is not chargeable to stamp duty. If such an instrument is brought into Pakistan after execution, the applicable stamp duty must be paid within three months after the instrument has been first received in Pakistan. In the event the instrument in respect of such a transaction is executed in electronic form, no stamp duty is payable.

Movable property (except shares, vehicles and ships) can be transferred by delivery. In that event, since no instrument of transfer is executed, stamp duty will not be payable.

Capital gains tax on disposal of assets

No tax is charged on any gain arising on the disposal of an asset:

- Between spouses under an agreement to live apart.
- By reason of the transmission of the asset to an executor or beneficiary on the death of a person.
- By reason of a gift of the asset to a relative.
- By reason of compulsory acquisition of the asset under ay law where the consideration received for the disposal is reinvested by the recipient in an asset of a like kind within one year of the disposal.
- By a company to its shareholders on liquidation of the company.
- By an association of persons to its members on dissolution of the association where the assets are distributed to members in accordance with their interests in the capital of the association.

However, these exemptions do not apply where the person acquiring the asset is a non-resident person at the time of the acquisition.

Where a resident company (transferor) disposes of an asset to another resident company (transferee), no gain or loss will arise on the disposal provided all the following conditions are satisfied:

- Both companies belong to a wholly-owned group of resident companies at the time of the disposal.
- The transferee undertakes to discharge any liability in respect of the asset acquired.
- Any liability in respect of the asset does not exceed the transferor’s cost of the asset at the time of the disposal.
- The transferee is not exempt from tax for the tax year in which the disposal takes place.

No tax is charged on any gain arising on the disposal of asset from one company (transferor) to another company (transferee) by virtue of the operation of a scheme of arrangement and reconstruction under the ITO, provided all the following

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conditions are satisfied:

- The transferee undertakes to discharge any liability in respect of the asset acquired.
- Any liability in respect of the asset does not exceed the transferor's cost of the asset at the time of the disposal.
- The transferee is not exempt from tax for the tax year in which the disposal takes place.
- The scheme is approved by the High Court, the State Bank of Pakistan or the Securities and Exchange Commission of Pakistan (as the case may be) on or after 1 July 2007.

Tax advantages/disadvantages for the buyer

17. Please set out the tax advantages and disadvantages of an asset acquisition for the buyer.

Advantages

Where the buyer acquires a depreciable asset, the applicable tax on that asset acquisition will be subject to a deduction provided such depreciable assets are used in the buyer's business in the tax year. The ITO provides the following incentives in relation to asset acquisition:

- Any industrial undertaking set up in Pakistan installing any plant, machinery and equipment for the generation of alternate energy, and owned and managed by a company, is allowed a deduction (first year allowance) at a rate of 90% against the cost of the eligible depreciation assets used after 1 July 2009.
- Any industrial undertaking owned and managed by a company, set up in specified rural and underdeveloped areas installing plant, machinery and equipment (or engaged in the manufacturing of cellular mobile phones and qualifying for an exemption under the ITO) is allowed a first-year allowance at a rate of 90% against the cost of the eligible depreciable assets used after 1 July 2008.

”Eligible depreciable asset” means a depreciable asset other than:

- Any road transport vehicle, unless the vehicle is plying for hire.
- Any furniture, including fittings.
- Any plant or machinery that has been used previously in Pakistan.
- Any plant or machinery in relation to which a deduction has been allowed under another section of the ITO for the entire cost of the asset in the tax year in which the asset is acquired.

By adding the consideration paid to acquire the asset, the buyer can increase the total cost of a business asset, and as a result, the buyer can offset any expenditure incurred to acquire the business asset when calculating their business profits.

Disadvantages

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The following tax disadvantages apply on an asset acquisition for the buyer:

- Transfer taxes may be significantly higher, particularly if the assets are immovable property.
- The buyer does not acquire the losses of the transferring company.

Tax advantages/disadvantages for the seller

18. Please set out the tax advantages and disadvantages of an asset disposal for the seller.

Advantages

The applicable rate of capital gains tax on immovable property is lower than the rate of capital gains tax on an acquisition of shares (*see Question 5*).

Disadvantages

A deduction is allowed for any loss on the disposal of a capital asset for a tax year. However, no loss can be deducted on the disposal of a capital asset where a gain on the disposal of that asset would not be chargeable to tax.

Transaction structures to minimise the tax burden

19. What transaction structures (if any) are commonly used to minimise the tax burden?

Share transfers, or transfers by schemes of demerger approved by the High Court, are used to minimise the tax burden.

Legal mergers

Taxes potentially payable

20. What taxes are potentially payable on a legal merger?

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A legal merger is a merger sanctioned by the High Court in accordance with section 282L of the former Companies Ordinance 1984, as saved by the Companies Act 2017. The taxes potentially payable on a legal merger are:

- Capital gains tax (*see Question 5*), unless the conditions for exemption listed in *Question 21* apply.
- Stamp duty: a transfer of assets under a scheme of arrangement and reconstruction takes place by virtue of the operation of law. No transfer taxes are applied to the transfer of movable and immovable property under the scheme.

Exemptions and reliefs

21. Are any exemptions or reliefs available to the liable party?

Deduction: costs of merger

Where any expenditure is incurred by an amalgamated company on legal and financial advisory services and other administrative costs relating to the planning and implementation of an amalgamation, that expenditure can be deducted for tax purposes.

Exemption

Subject to the conditions listed below, there is no tax on the gains on the disposal of asset from one company (transferor) to another company (the transferee) under a scheme of arrangement and reconstruction, provided all the following conditions are met:

- The transferee undertakes to discharge any liability in respect of the asset acquired.
- Any liability in respect of the asset does not exceed the transferor's cost of the asset at the time of the disposal.
- The transferee is not exempt from tax for the tax year in which the disposal takes place.
- The scheme is approved by the High Court, the State Bank of Pakistan or the Securities and Exchange Commission of Pakistan on or after 1 July 2007.

Further to the above, there is no tax on the gains from the issuance or receipt of shares as a result of a scheme of arrangement and reconstruction approved by the High Court, the State Bank of Pakistan or the Securities and Exchange Commission of Pakistan on or after 1 July 2007.

Transaction structures to minimise the tax burden

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22. What transaction structures (if any) are commonly used to minimise the tax burden?

Transaction structures which comply with the requirements for the exemptions outlined in *Question 21* are used to ensure that the transaction is tax neutral.

Joint ventures

Taxes potentially payable

23. What taxes are potentially payable on establishing a joint venture company (JVC)?

The tax laws of Pakistan do not make any special provisions for the purposes of establishing joint venture companies.

Stamp duty

Stamp duty must be paid on instruments executed for the purposes of the joint venture (*see Question 4, Stamp duty*).

Exemptions and reliefs

24. Are any exemptions or reliefs available to the liable party?

Any instrument executed outside of Pakistan is not chargeable to stamp duty. If such an instrument is brought into Pakistan after execution, the applicable stamp duty must be paid within three months after the instrument has been first received in Pakistan. Further, in the event the instrument in respect of such a transaction is executed in electronic form, no stamp duty is payable.

Transaction structures to minimise the tax burden

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25. What transaction structures (if any) are commonly used to minimise the tax burden?

Transfer taxes and capital gains tax in respect of shares may be mitigated if the investing company is located in a jurisdiction which has a favourable tax treaty with Pakistan.

Company reorganisations

Taxes potentially payable

26. What taxes are potentially payable on a company reorganisation?

There are no other taxes specifically applicable to company reorganisations.

Stamp duty

Stamp duty must be paid on any instrument executed for a company reorganisation in accordance with the rates prescribed under the relevant provincial stamp schedules (*see Question 4, Stamp duty*).

Exemptions and reliefs

27. Are any exemptions or reliefs available to the liable party?

Any instrument executed outside of Pakistan is not chargeable to stamp duty. If such an instrument is brought into Pakistan after execution, the applicable stamp duty must be paid within three months after the instrument has been first received in Pakistan. In the event the instrument in respect of such a transaction is executed in electronic form, no stamp duty is payable.

Transaction structures to minimise the tax burden

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28. What transaction structures (if any) are commonly used to minimise the tax burden?

Specific exemptions may provide tax efficient structures, depending on the nature of business and the commercial objectives. For example, any income (not being the income from trading activity) of a modaraba registered under the Modaraba Companies and Modaraba (Floatation and Control) Ordinance 1980 for any assessment year commencing on or after 1 July 1999 is exempt from income tax.

Restructuring and insolvency

29. What are the key tax implications of the business insolvency and restructuring procedures in your jurisdiction?

Payment of tax

A liquidator of an insolvent company must set aside, out of the proceeds of sale made by the liquidator of any asset, the amount sufficient to provide for any tax which is, or will become, payable by the person whose assets are in the liquidator's possession. The amount of tax due will be notified by the Commissioner Inland Revenue, and the Commissioner can subsequently agree to a lesser amount of tax in certain circumstances.

Shareholders/directors

Where any tax payable by a private company that has been wound up or gone into liquidation during any tax year cannot be recovered from the company, every person who fulfilled any of the following roles will be jointly and severally liable for payment of the tax due by the company:

- A company director (other than an employed director).
- A company shareholder owning not less than 10% of the paid-up capital of the company.

Share buybacks

Taxes potentially payable

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30. What taxes are potentially payable on a share buyback? (List them and cross-refer to *Questions 4* to *7* as appropriate.)

Only listed companies are allowed to buy-back their own shares under the laws of Pakistan. There are no taxes specifically applicable to share buy-backs. The following taxes may apply on a share buy-back:

- Stamp duty (*see Question 4, Stamp duty*).
- Capital gains tax (*see Question 5*.

Exemptions and reliefs

31. Are any exemptions or reliefs available to the liable party?

For the exemptions or reliefs that may apply for the purposes of stamp duty and capital gains tax, see *Question 11*.

Transaction structures to minimise the tax burden

32. What transaction structures (if any) are commonly used to minimise the tax burden?

See *Question 14*

Private equity financed transactions: MBOs

Taxes potentially payable

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33. What taxes are potentially payable on a management buyout (MBO)?

There are no taxes specifically applicable to MBOs. The following taxes may apply on an MBO:

- Stamp duty (*see Question 4, Stamp duty*).
- Capital gains tax (*see Question 5*).

Exemptions and reliefs

34. Are any exemptions or reliefs available to the liable party?

For the exemptions or reliefs that may apply for the purposes of stamp duty and capital gains tax, see *Question 11*

Transaction structures to minimise the tax burden

35. What transaction structures (if any) are commonly used to minimise the tax burden?

See *Question 14*

Reform

36. Please summarise any proposals for reform that will impact on the taxation of corporate transactions.

The Federal Board of Revenue (FBR) has consistently experienced administrative and policy issues. As a result, the current

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government (formed by Pakistan Tehreek-e-Insaf) has frequently emphasised the need for reform in the tax machinery to enhance the narrow income tax base of the country. Pakistan has embarked on an ambitious USD400 million tax reform programme in partnership with the World Bank. At a macro level, the project has two components: the results-based component and the investment financing component. The results-based component is worth USD320 million and is further divided into four main objective areas, namely:

- Controlling taxpayer obligations (USD104.5 million).
- Simple and transparent tax system (USD98 million).
- Facilitation of compliance (USD72 million).
- Institutional development (USD45.5 million).

The investment financing component, worth USD80 million, will be used to upgrade the ICT systems currently being used by the FBR.

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