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# COMMENTS ON INCOME TAX (AMENDMENT) ORDINANCE, 2022

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## ➤ PROLOGUE:

Tax Incentive Schemes have been introduced time and again to encourage and promote tax culture and documentation of economy. Recently, general amnesty schemes were offered such as Foreign Assets (Declaration & Repatriation) Act, 2018 and Voluntary Declaration of Domestic Assets Act 2018. Moreover, the Benami Transaction (Prohibition) Act, 2017 became operational in 2019 on issuance of relevant Rules, whereby, benami assets were declared illegal. It was therefore imperative to bring a transitional declaration mechanism for providing an opportunity to bring these assets into the documented economy. Therefore, another amnesty scheme was given in the form of Asset Declaration Ordinance, 2019. A number of other amnesty schemes were also introduced earlier in 1958, 1969, 1976, 1997, 2000, 2008, 2012, 2013 and 2015.

The main parking venue for the informal economy in Pakistan is the construction sector in Pakistan, and it is also the driver of major economic activity. Therefore, a specific amnesty to this sector was given in Section 100D of the ITO. However, it was criticized that a specific sector was given a favour and other industries were not given such incentive. So, to incentivize capital investment to all geographic areas and to encourage entrepreneurs to invest in industrial undertakings out of their undisclosed assets, so that employment is generated and Sick units are revived, a Promotion Package for Industry (PPI) is now being introduced through certain amendments in the Income Tax Ordinance, 2001 ("ITO").

A document has been circulating on social media today i.e 2<sup>nd</sup> March 2022, setting forth the PPI/amendments proposed to be made by the Federal Government. These comments are based on the document being circulated on social media, hence, we disclaim the accuracy of our comments made and the proposed amendments stated herein. We also disclaim any discrepancies that may arise between the proposed amendments stated herein and the actual Ordinance that will be promulgated by the President of Pakistan.

Nevertheless, should you have any queries in relation to this document, do not hesitate in contacting us.

This document has been prepared exclusively for the use of our staff, clients and intended readers, based on public information available with us. This Memorandum should not be published or printed in any manner without seeking written consent from us. Our comments in this document should not be construed as definite and should, therefore, be used only as a guidance.

Warm Regards

**TOLA ASSOCIATES**

**Dated: Wednesday, March 2, 2022**

## COMMENTS ON INCOME TAX (AMENDMENT) ORDINANCE, 2022

### 1. CARRY FORWARD OF BUSINESS LOSSES OF SICK INDUSTRIAL UNITS – SECTION 59C

A new Section 59C has been inserted to the Income Tax Ordinance 2001 (“ITO”), whereby, an incentive has been provided to the companies acquiring ‘sick industrial units’ to revive them. This incentive has been provided in form of adjustment of business losses by acquiring company.

#### 1.1 SICK INDUSTRIAL UNIT

The “sick industrial unit” has been defined as a company being an industrial undertaking, which –

- has accumulated losses equal to or exceeding its entire capital and reserves at the time of acquisition, for a continuous period of three years prior to 1st July, 2022; or
- has defaulted towards repayment of outstanding debts owing to banking companies or non-banking financial institutions for a consecutive period of three years immediately before acquisition, or
- has been declared as such by the Federal Government in a notification published in the official Gazette.

#### 1.2 LOSS ADJUSTMENTS

Where a company acquires more than 50% share capital of another company being a sick industrial unit,

- the acquiring company shall be entitled to adjust loss for the latest tax year and brought forward assessed business losses (excluding capital loss of the acquired company)
- The loss will be allowed to be adjusted by the acquiring company for a period of three years.
- Where the losses surrendered by the acquired company are not adjusted against income of the acquiring company in the said three tax years, the acquired

company shall carry forward the unadjusted losses in accordance with section 57. The maximum carry-forward time period under section 57 has been provided as 10 years for banking company, 8 years for hotel company and 6 years for others.

#### 1.3 CONDITIONS FOR LOSS ADJUSTMENT

The above benefits are subject to fulfilment of below conditions:

- there is continued ownership for five years starting from the 30<sup>th</sup> June, 2023 and there is no change in share capital of the acquiring company;
- the assets of the acquired company shall not be sold upto 30<sup>th</sup> June, 2026; and
- the acquired company continues the same business till 30<sup>th</sup> June, 2026.

#### 1.4 CALCULATION FOR AVAILABLE ADJUSTMENT OF LOSS

The loss of the acquired company shall be adjusted against income under the head “income from business” of the acquiring company as per following formula, namely:-

$$(A/100) \times B$$

where—

**A** is the percentage share capital held by the acquiring company of the acquired company; and

**B** is the loss of the acquired company.

For example, Company X acquires 60% shares of Company Y being a sick business unit having accumulated business losses of 100 million. The losses available to Company X for adjustment will be (Rs. 100 million x 60/100) Rs. 60 million only.

Moreover, if the acquiring company fails to revive the acquired company by tax year 2026,

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the acquiring company shall, in tax year 2027 offer the amount of profit on which taxes have not been paid due to adjustment of losses surrendered by the acquired company. For e.g. if, by 2026, the Company Y is still in the definition of Sick Unit, then all the losses adjusted will become taxable in Tax Year 2027.

### 2. TAX CREDIT FOR FOREIGN INVESTMENT FOR INDUSTRIAL PROMOTION – SECTION 65H

A new Section 65H has been inserted in the ITO, whereby a one-time 100% tax credit against tax liability will be available against foreign investments to the following:

#### 2.1 ELIGIBLE PERSONS

- (a) a non-resident Pakistani citizen having continued non-residential status for more than five years; or
- (b) a resident individual **having foreign assets declared** in terms of section 116 or 116A by the 31st December, 2021, (meaning it is not an amnesty for undeclared assets).

#### 2.2 CONDITIONS FOR THE CREDIT:

- Investment is required in equity of a company incorporated on or after the 1st March, 2022;
- The company shall be an industrial undertaking in Pakistan;
- Equity shall be at least Rs 50 million with funds remitted into Pakistan through proper banking channel as per the procedure to be prescribed by the State Bank of Pakistan, at any time up to the 31st December, 2022,
- the company shall be entitled to a one-time tax credit equal to 100% of the amount remitted and credited in rupees in the bank account of such company against tax liability for the tax year in which commercial production commences.
- Commercial production should commence by the 30th June, 2024.

- The credit will not be applicable to a company or an industrial undertaking established by splitting up or reconstitution of a company or an industrial undertaking already in existence or by transfer of machinery or plant from an industrial undertaking established at any time before 1st March, 2022.

#### 2.3 CARRYFORWARD OF TAX CREDIT

Where no tax is payable by the taxpayer in respect of the tax year in which the commercial production has commenced or where the tax payable is less than the amount of credit, the amount of the credit or so much of it as is in excess thereof, shall be carried forward and deducted from the tax payable by the taxpayer in respect of the following tax year and so on, but no such amount shall be carried forward for more than five tax years.

#### 2.4 REVOCATION OF TAX CREDIT

Where any credit is allowed under this section and subsequently it is discovered by the Commissioner Inland Revenue that any one or more of the conditions specified in this section was or were not fulfilled, the credit originally allowed shall be deemed to have been wrongly allowed and the Commissioner shall re-compute the tax payable by the taxpayer for the relevant year.

### 3. AMNESTY SCHEME THROUGH INVESTMENT IN NEW INDUSTRIES/EXISTING INDUSTRIES – SECTION 100F

#### 3.1 AMNESTY TO INVEST IN NEW INDUSTRIAL UNDERTAKING

A general amnesty is given to all persons to declare assets by paying a general tax rate of 5% by investment in new industries.

##### 3.1.1 PERSONS NOT ELIGIBLE FOR AMNESTY

- Holders of public office (a person as defined in the Voluntary Declaration of Domestic Assets Act, 2018. See Annexure A), their spouses and dependent children;

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- A public company;
- A person who has filed a declaration under the Voluntary Declaration of Domestic Assets Act, 2018, the Foreign Assets (Declaration and Repatriation) Act, 2018, or the Assets Declaration Act, 2019;
- a person that has been declared a bank loan defaulter by a bank or a financial institution within the last three years; or
- a director of a company who has been declared a bank loan defaulter by a bank or a financial institution within the last three years.

### 3.1.2 FUNDS NOT ELIGIBLE FOR AMNESTY

- any proceeds of crime, corruption, money laundering and terror financing;
- any amount which is subject of any departmental or court proceedings;

### 3.1.3 SECTORS NOT ELIGIBLE FOR INVESTMENT

- arms and ammunitions;
- explosives;
- sugar;
- cigarettes;
- aerated beverages;
- flour mills;
- vegetable ghee; and
- cooking oil manufacturing excluding extraction units.

### 3.1.4 CONDITIONS AND BENEFITS OF AMNESTY

- The person may file a statement by the 30th September, 2022, (to be notified by FBR later) declaring therein the amount of funds (which have not been declared in any of the returns of income upto tax year 2021 filed by the 31st December, 2021) for investment in a new company formed

for establishing and operating an industrial undertaking.

- The amount shall be deposited in rupees in a dedicated bank account in Pakistan as equity of the newly formed company, incorporated under the Companies Act, 2017, before the filing of the statement and such funds shall only be used for purchase or import of plant and machinery through letter of credit or for construction of building and structure for the industrial undertaking.
- The minimum amount of investment shall be Rs 50 million.
- Investment should be in equity and does not include borrowed funds and investment in land.
- The tax to be paid on the above amount invested shall be 5% (non-refundable, non-adjustable) and source of such funds cannot be investigated under Section 111.
- The new industrial undertaking in which such investment is made shall commence commercial production by the 30th June, 2024 and a certificate to that effect, duly issued by Engineering Development Board, is submitted to the Commissioner along with the return filed for tax year 2024.
- The amount declared shall be confidential and cannot be disclosed to any authority or court, FIA or NAB by FBR.
- There shall be no change of ownership of industrial undertaking company prior to the 30th June, 2026
- There shall be no disposal of assets prior to 30th June, 2026

### 3.1.5 INCORPORATION IN BOOKS

The declarant shall be entitled to incorporate the amount of investment and tax paid thereon in his wealth statement in case of individual, and in financial statements or books of accounts in case of companies.

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### 3.2 AMNESTY TO INVEST IN EXISTING INDUSTRIAL UNDERTAKING

The amnesty shall also be available for investment in existing Industrial Undertaking through mode of investment in expansion and modernization from amount of funds.

This benefit was also available in Section 65B for investment made in BMR upto Tax Year 2019, in the form of a tax credit at the rate of 10% upto Tax Year 2018 and 5% for Tax Year 2019.

#### 3.2.1 Conditions and benefits of the amnesty

- The amounts of investment have not been declared in any of the returns of income up to Tax year 2021 and filed by 31st December 2021.
- Such company opens a dedicated bank account to deposit the said funds before the filing of the statement and such funds shall only be used for expansion and modernization by way of purchase or import of plant and machinery including IT hardware through letter of credit, or software and IT services or for construction of building and structure for the manufacturing premises of the existing industrial undertaking.
- That the expansion and modernization shall be completed by the 30th June, 2024, and a certificate to that effect, duly issued by the Engineering Development Board, is submitted to the Commissioner along with the return filed for tax year 2024.
- The person may file a statement by 30th September, 2022, (to be notified by the FBR later) declaring therein the amount of funds for investment.
- “modernization” includes acquisition or upgradation of IT hardware, software and IT services.

- The minimum amount shall be Rs 50 million.
- The tax to be paid on above amount invested shall be 5% (non-refundable, non-adjustable) and source of such funds cannot be investigated under Section 111 of the ITO.
- The amount declared cannot be disclosed with any authority or court, FIA or NAB by the FBR.
- There shall be no change of ownership of industrial undertaking company prior to the 30th June 2026
- There shall be no disposal of assets prior to 30th June 2026

### 4. POINTS TO PONDER

Following are some points which require some explanation or reconsideration to avoid unnecessary litigations in the future:

- The newly inserted Section 59C of the ITO provides for adjustment of losses of the acquired company for 3 three years and provides that remaining losses to be adjusted in accordance with Section 57 of the ITO. However, Section 57 provides that losses cannot be adjusted for more than 6 years. An explanation will, therefore, be required whether the periods provided under Section 57 are **in addition** to the period available in section 59C or is the total period inclusive of the period under Section 59C.
- The period allowed to acquiring company for the revival of the sick unit is also very short and suggest the same should be atleast till 2028.
- Moreover, it has also been provided that in case the acquiring company fails to revive the sick unit by Tax Year 2026, the adjusted losses will become taxable in TY 2027. This provision should also cater for the opportunity of being heard for the acquiring company.

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- Moreover, the newly inserted section 65H provides that the credits availed by the taxpayers may be revoked by the Commissioner in case of non-fulfillment of any of the specified conditions. Similar conditions have been provided earlier in sections 65B, 65D, 65E etc., which has resulted in unnecessary litigations between department and the taxpayers. It is therefore, suggested that the revocation of the tax credits may be made subject to approval of Chief Commissioners.
- Furthermore, the threshold of the minimum equity being PKR 50 Million gives a perception that the amnesty has been introduced for the upper class of the society.
- The holder of public office has been referred to be a person as defined under the Voluntary Declaration of Domestic Assets Act, 2018. However, it has not been clarified that from what point in time the period of 10 years (as specified in the referred definition) will be computed.
- Under the newly inserted Section 100F, investment into land has been barred to avail amnesty for the funds invested. This may create practical limitations as the taxpayer will prefer to make investments on their own lands instead of rented plots, etc. Moreover, they might not have enough declared funds to invest separately into land to build industrial undertakings thereon. It is, therefore, suggested that instead to complete restriction, a reasonable percentage of total investment should be allowed to be invested in land also.



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### ANNEXURE A

#### **Definition of Public Officer Holder as provided in** Voluntary Declaration of Domestic Assets Act, 2018

"holder of public office" means a person who is or has been, during the preceding ten years,–

- (i) the President of the Islamic Republic of Pakistan or the Governor of a Province;
- (ii) the Prime Minister, Chairman Senate, Speaker of the National Assembly, Deputy Chairman Senate, Deputy Speaker National Assembly, Federal Minister, Minister of State, Attorney-General for Pakistan and other Law Officers appointed under the Central Law Officers Ordinance, 1970 (VII of 1970), Adviser or Consultant or Special Assistant to the Prime Minister and holds or has held a post or office with the rank or status of a Federal Minister or Minister of State, Federal Parliamentary Secretary, Member of Parliament, Auditor-General of Pakistan, Political Secretary;
- (iii) the Chief Minister, Speaker Provincial Assembly, Deputy Speaker Provincial Assembly, Provincial Minister, Adviser or Consultant or Special Assistant to the Chief Minister and who holds or has held a post or office with the rank or status of a Provincial Minister, Provincial Parliamentary Secretary, Member of the Provincial Assembly, Advocate-General for a Province including Additional Advocate-General and Assistant Advocate-General, Political Secretary
- (iv) the Chief Justice or, as the case may be, a Judge of the Supreme Court, Federal Shariat Court, a High Court or a Judicial Officer whether exercising judicial or other functions or Chairman or member of a Law Commission, Chairman or Member of the Council of Islamic Ideology;
- (v) holding an office or post in the service of Pakistan or any service in connection

with the affairs of the Federation or of a Province or of a local council constituted under any Federal or Provincial law relating to the constitution of local councils, co-operative societies or in the management of corporations, banks, financial institutions, firms, concerns, undertakings or any other institution or organization established, controlled or administered by or under the Federal Government or a Provincial Government or a civilian employee of the Armed Forces of Pakistan:

Provided that a member of the Board, not actively engaged in the business and day-today affairs of the said corporations, banks, financial institutions, firms, concerns, undertakings or any other institution or organization shall not be treated as holder of public office under this sub-clause;

- (vi) the Chairman or Mayor or Vice Chairman or Deputy Mayor of a zila council, a municipal committee, a municipal corporation or a metropolitan corporation constituted under any Federal or Provincial law relating to local councils;
- Explanation.**– For the purpose of this sub-clause the expressions "Chairman" and "Vice Chairman" shall include "Mayor" and "Deputy Mayor" as the case may be, and the respective councilors therein; and
- (vii) a District Nazim or District NaibNazim, Tehsil Nazim or Tehsil *NaibNazim* or *UnionNazim* or *Union NaibNazim*;



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