Non-resident firm: Lahore LTU seeks legal guidance on levy of Super Tax

Large Taxpayer Unit (LTU) Lahore has sought legal guidance from the Federal Board of Revenue (FBR) on whether or not Super Tax under Section 4B of the Income Tax Ordinance, 2001 be imposed on 'income' in addition to 10 percent tax against 'dividend' alone offered by the non-resident beverage company under Avoidance of Double Taxation Agreement (DTA).

Sources told *Business Recorder* here on Tuesday that the LTU Lahore has made a representation to the FBR on the levy of Super Tax u/s 4B of the Income Tax Ordinance, 2001 in the case of an international beverage company (non-resident company).

The LTU Lahore is of the view that dividend is an integral part of income for the purpose of levy of super tax. Since the dividend income as declared by the taxpayer exceeds the threshold of Rs 500 million, the taxpayer company is apparently liable to pay Super Tax @ 3% of the gross dividend. It is evident that super tax is chargeable against every person without any distinction of residential status as specified in section 80 of the Income Tax Ordinance.

According to the LTU Lahore, an international beverage company, a non-resident company incorporated in Netherlands, is assessed to tax in LTU Lahore. It has 99.96% shareholding of another beverage company (resident company). The taxpayer company has declared dividend income of Rs 5,250,000,000 received from Pakistani beverage company (resident company) for the tax year 2016 as its only source of income taxable in Pakistan against which it has paid income tax of Rs 525,000,000 at the rate of 10% of 7dividend under Division III of Part-I of the First Schedule to the Income Tax Ordinance, 2001 (Ordinance) read with the Convention between Netherlands and Pakistan for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (DTA).

It is worth recalling that super tax for rehabilitation of temporarily displaced persons was imposed through Finance Act, 2015 by insertion of Section 4B in the Income Tax Ordinance, 2001, according to which every person having income of Rs 500 million and above is liable to pay the said tax. For facility of reference, subsection (1) of section 4B of the Ordinance is reproduced as under:

4B. Super tax for rehabilitation of temporarily displaced persons.-

(1) A super tax shall be imposed for rehabilitation of temporarily displaced persons, for tax years 2015 and 2016 at the rates specified in Division IIA of Part I of the First Schedule, on income of every person specified in the said Division. (underlined for emphasis.)

Division IIA of Part I of the First Schedule specifying the rate of super tax says:
Division IIA Rates of super tax:

Banking company, rate of super tax is 4% of the income and person, other than a banking company, having income equal to or exceeding Rs 500 million, rate of super tax is 3% of the income.

From the said provisions of law, it is evident that super tax is chargeable against every person without any distinction of residential status as specified in section 80 of the Ordinance, LTU Lahore interpreted the law.

For the purpose of levy of super tax, the expression "income" of a person has specifically been defined in sub-section (2) of section 4B of the Ordinance in the following words:

"(2) For the purposes of this section, - income shall be the sum of the following:-

(i) profit on debt, dividend, capital gains, brokerage and commission;

(ii) taxable income (other than brought forward depreciation and brought forward business losses) under section (9) of this Ordinance, if not included in clause (i);

(iii) imputable income as defined in clause (28A) of section 2 excluding amounts specified in clause (i); and

(iv) income computed under Fourth, Fifth, Seventh and Eighth Schedules.

It thus follows that dividend is an integral part of income for the purpose of levy of super tax. Since the dividend income as declared by the taxpayer exceeds the threshold of Rs 500 (m), the taxpayer company is apparently liable to pay Super Tax @ 3 percent of the gross dividend which works out at Rs 157,500,000, the LTU Lahore said.

The issue has also been examined in the light of the DTA. As per clause 3(a) of Article 2 of the DTA, the Convention shall apply to the following taxes on income imposed on behalf of one of the states:

"3. The existing taxes to which the Convention shall apply are in particular:

(a) in the case of the Netherlands:

-de inkomstenbelasting (income tax),

-de loonbelasting (wages tax),

-de vennootschapsbelasting (company tax),

-de dividendbelasting (dividend tax)

(hereinafter referred to as "Netherlands tax");

(b) in the case of Pakistan:

-the income tax,

-the super tax,

-the surcharge

(hereinafter referred to as "Pakistan tax")

7. Article 10 of the Treaty provides chargeability of dividend income in the following words:

"Article 10"

Dividends: 1. Dividends paid by a company which is a resident of one of the States to a resident of the other State may be taxed in that other State.

2. However, such dividends may also be taxed in the State of which the company paying the dividends is a resident and according to the laws of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed:

(a) 10 percent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly at least 25 percent of the capital of the company paying the dividends;

(b) 20 percent of the gross amount of the dividends in all other cases.

3. The provisions of paragraph 2 shall not affect the taxation of the company in respect of the profits out of which the dividends are paid."

8. Further as per Final Protocol of the DTA the following provisions shall form part

of the DTA:

IV Ad Article 10: The provisions of paragraph 2(a) of Article 10 shall not apply if the company which is a resident of the Netherlands suffers Netherlands company tax on the dividends which it receives from the company which is a resident of Pakistan. In such a case, the provisions of paragraph 2(b) of Article 10 shall apply.

The LTU Lahore said that in this case the taxpayer company has offered dividend income for tax @ 10 percent as per clause 2(a) above as it holds more than 99% shares of Pakistani company (resident beverage company). However, if it is held that paragraph 2(b) of Article 10 of the DTA is applicable in this case instead of paragraph 2(a), we can easily charge the super tax.

Guidance of the Board is solicited whether super tax under Section 4B of the Income Tax Ordinance, 2001 be imposed on "income" in addition to tax @ 10 percent against "dividend" alone offered by the non-resident company as per the DTA, LTU Lahore added.