CHAPTER 12

TAXATION OF INDIVIDUALS & AOPs

How an **individual** is classified and taxed (**salaried vs non-salaried**), special cases (**deceased persons, authors**), the full **taxation of an association of persons** and its members (**rate purposes**), and **income splitting** on changes, dissolution and succession. Law: ITO 2001 · tax year 2027.

CHAPTER ROADMAP

1. **Taxation of individuals** — s.86
2. **Deceased persons and authors** — ss.87 · 89
3. **Association of persons** — s.2(2) · 92
4. **Member's share and rate purposes** — formula (A ÷ B) × C
5. **Tax rates** — First Schedule
6. **Income splitting** — ss.98A – 98C

PRINCIPLE

Section 86: the taxable income and tax liability of **each individual are determined separately**. An **AOP** (firm, HUF, artificial juridical person, LLP, foreign body — **not a company**) is a **separate taxable entity** from its members.

1 SALARIED OR NON-SALARIED?

the 75% test

SALARIED

Taxable **salary is more than 75%** of taxable income → salaried slabs. No surcharge.

NON-SALARIED

No salary, or salary **not above 75%** of taxable income → non-salaried slabs; **10% surcharge** if taxable income exceeds **Rs. 10 million**.

SURCHARGE

10% of the income tax, on **non-salaried individuals and AOPs** above Rs. 10m. The 9% surcharge on salaried individuals has **ended from tax year 2027**.

Fresh examples	Mr P	Mr Q	Mr R	Mr S
Taxable salary	800,000	80,000	600,000	900,000
Other taxable income	100,000	900,000	400,000	250,000
Total taxable income	900,000	980,000	1,000,000	1,150,000
Salary as % of total	88.9%	8.2%	60%	78.3%
Status	Salaried	Non-salaried	Non-salaried	Salaried
Tax	3,000	57,000	60,000	5,500

Salaried slabs (salary above 75% of taxable income):

Taxable income (Rs.)	Tax
Up to 600,000	Nil
600,001 – 1,200,000	1% of the excess over 600,000
1,200,001 – 2,200,000	6,000 + 11% of the excess over 1,200,000
2,200,001 – 3,200,000	116,000 + 20% of the excess over 2,200,000

Taxable income (Rs.)	Tax
3,200,001 – 4,100,000	316,000 + 25% of the excess over 3,200,000
4,100,001 – 5,600,000	541,000 + 29% of the excess over 4,100,000
5,600,001 – 7,000,000	976,000 + 32% of the excess over 5,600,000
Above 7,000,000	1,424,000 + 35% of the excess over 7,000,000

Non-salaried individuals and AOPs (a professional firm that cannot incorporate: top rate **40%** instead of 45%):

Taxable income (Rs.)	Tax
Up to 600,000	Nil
600,001 – 1,200,000	15% of the excess over 600,000
1,200,001 – 1,600,000	90,000 + 20% of the excess over 1,200,000

Taxable income (Rs.)	Tax
1,600,001 – 3,200,000	170,000 + 30% of the excess over 1,600,000
3,200,001 – 5,600,000	650,000 + 40% of the excess over 3,200,000
Above 5,600,000	1,610,000 + 45% of the excess over 5,600,000

2 DECEASED PERSONS AND AUTHORS

sections 87 and 89

LEGAL REPRESENTATIVE · s.87

Liable for **tax the deceased would have owed** and tax on the **income of the estate** — **limited to what the estate can meet**. Proceedings against the deceased continue against the representative; new ones may be started.

AUTHORS · s.89

If a literary or artistic work took **more than 24 months**, the author may elect to treat a **lump-sum royalty** as received **equally in that year and the preceding two years**.

3 ASSOCIATION OF PERSONS

basic principles

SEPARATE ENTITY

Taxed separately from its members. **Resident** if control and management are **wholly or partly in Pakistan** at any time in the year; taxed on **worldwide** income.

MEMBER'S SHARE

If the AOP has paid tax, a member's share is **exempt** — but **included in his income for rate purposes** (profit **after tax**). Turnover of **Rs. 300 million or more**: exemption only if **audited financial statements** (CA / CMA) are filed with the return.

COMPANY AS MEMBER

Its share is **excluded** from the AOP's income and taxed **separately at company rates**.

LOSSES

The AOP sets off and carries forward **its own** losses. A member's share of loss is **not** adjustable against his income and is **not** counted for rate purposes.

ADD BACK TO AOP INCOME

Profit on debt, brokerage, commission, salary or other remuneration paid by the AOP to a **member** is not deductible.

OTHER POINTS

FTR income of the AOP is not added to members' income. An exempt **LLP** share is included in the member's income. Professional firms: top rate **40%**.

4 MEMBER OF AN AOP · TAX ON HIS OWN INCOME

formula (A ÷ B) × C

FORMULA

A = tax if the exempt AOP share were taxable; **B** = taxable income including the share; **C** = his **actual taxable income** (excluding the share). Tax = (A ÷ B) × C. The share raises the **rate** but is not itself taxed.

5 WORKED EXAMPLE

fresh numbers · tax year 2027

AOP "Alpha & Co" · partners X : Y = 60 : 40	Rs.		
Accounting profit	1,800,000		
Add: salary to partner X	300,000		
Add: profit on debt to partner Y	100,000		
Taxable income of the AOP	**2,200,000**		
Tax: 170,000 + 30% × (2,200,000 − 1,600,000)	(350,000)		
Divisible income	**1,850,000**		
Balance after member payments: 1,850,000 − 300,000 − 100,000	1,450,000	X 60% = 870,000	Y 40% = 580,000
Income in members' hands (incl. salary / profit on debt)	1,850,000	X 1,170,000	Y 680,000

EXAMPLE

Mr Y also earns business income of Rs. 1,000,000. Including the exempt share: 680,000 + 1,000,000 = 1,680,000; tax as non-salaried = 170,000 + 30% × 80,000 = **194,000** (A). Tax on his actual taxable income = 194,000 ÷ 1,680,000 × 1,000,000 = **Rs. 115,476**.

6 INCOME SPLITTING

sections 98A – 98C

CHANGE IN CONSTITUTION · 98A

The firm's income is apportioned among partners on a **time basis**. The partners **at the date the return is due** file it.

DISSOLUTION · 98B

Tax of the firm is recoverable from **any person who was a partner at dissolution** or discontinuance, and from the **legal heirs** of deceased partners.

SUCCESSION NOT ON DEATH · 98C

Predecessor pays tax for the year up to the date of succession and earlier years; **successor** for the rest. If the predecessor **cannot be found**, or tax cannot be recovered from him, the successor is liable (with a right of recovery).

7 EXAM FOCUS · MCQ TRAPS

what examiners test

1 75% test
Salaried only if salary is **more than 75%** of taxable income; exactly 75% is non-salaried.

2 Surcharge
10% for non-salaried individuals and AOPs above Rs. 10m; none for salaried (the 9% ended in tax year 2027).

3 Rate purposes
The member's **after-tax** share is exempt but included for the **rate**.

4 Add back
Salary, profit on debt, brokerage, commission paid to members.

5 Share of loss
Not set off against the member's income; **not counted for rate**.

6 Company member
Taxed **separately at company rates**; excluded from the AOP's income.

7 Rs. 300 million
Turnover of **Rs. 300m or more**: share is exempt only if **audited accounts** are filed.

8 FTR income
An AOP's **final-tax income** is not added to members' taxable income.

CLASSIFY IT · SALARIED OR NOT?

1	Salary 900,000; other income 100,000	SALARIED
2	Salary 100,000; other income 1,000,000	NON-SALARIED
3	Salary 600,000; other income 400,000 (60%)	NON-SALARIED
4	Salary 900,000; other income 250,000 (78%)	SALARIED
5	Salary exactly 75% of taxable income	NON-SALARIED
6	No salary income at all	NON-SALARIED
7	Non-salaried individual, taxable income Rs. 12m	10% SURCHARGE
8	Salaried individual, taxable income Rs. 12m	NO SURCHARGE

CLASSIFY IT · AOP: WHAT HAPPENS?

1	Salary paid to a partner	ADD BACK
2	Profit on debt paid to a partner	ADD BACK
3	Brokerage or commission to a member	ADD BACK
4	Salary to a non-member employee	ALLOWED
5	Member's share of AOP profit (tax paid)	EXEMPT · RATE ONLY
6	Company member's share	TAXED SEPARATELY
7	Member's share of the AOP's loss	NOT SET OFF
8	AOP's final-tax income in a member's hands	NOT ADDED

LISTS TO KNOW

Salaried test	Surcharge	Audit rule	Author election	Professional firm
salary above 75%	10% above Rs. 10m (non-salaried)	AOP turnover Rs. 300m	24 months → 3 years	top rate 40%

REVISION MAP

1 · INDIVIDUALS
Taxed separately · salaried if salary above 75% of taxable income · slabs · surcharge on non-salaried above Rs. 10m · deceased: legal representative · authors: 24 months, three years

2 · AOP
Separate entity · resident if controlled wholly or partly in Pakistan · member's share exempt but for rate purposes · company member taxed separately · Rs. 300m turnover: audited accounts

CHAPTER 12
INDIVIDUALS & AOPs

3 · COMPUTATION
Add back member payments → taxable income → tax → divisible income → shares · member tax = (A ÷ B) × C · loss share ignored · FTR income not added · professional firm 40%

4 · CHANGES
Change in constitution: time basis · dissolution: recover from partners and heirs · succession: predecessor to the date, successor after; successor liable if predecessor not found

Salaried
More than 75% salary.

AOP
Own tax, then members.

Rate purposes
Share raises the rate only.

Splitting
Time basis and succession.