CHAPTER 8

INCOME FROM BUSINESS · PART 2

Tax **depreciation**, **initial allowance**, **amortisation of intangibles**, **pre-commencement expenditure**, and the rules for **disposal, cost and consideration** of assets. All figures are on **tax** values — accounting revaluation and impairment never count. Law: ITO 2001 · tax year 2027.

CHAPTER ROADMAP

1 Depreciation s.22
2 Initial allowance s.23
3 Intangibles s.24
4 Pre-commencement expenditure s.25
5 Disposal, cost, consideration ss.75 – 77

DEFINITION

Depreciable asset [s.22(15)]: tangible movable property, immovable property (**other than unimproved land**) or structural improvement, owned by the person, with a **useful life above one year**, likely to lose value by wear and tear or obsolescence, and **used wholly or partly to earn taxable business income**. Not an asset whose **entire cost** was deducted under another section.

1 DEPRECIATION RATES

Third Schedule

Asset	Rate on WDV
Building (all types)	10%
Furniture and fittings, machinery and plant (not otherwise specified), motor vehicles (all types), ships, technical or professional books	15%
Computer hardware incl. printer, monitor and allied items; machinery and equipment for manufacture of IT products; aircraft and aero engines	30%
Mineral oil concerns: offshore platform and production installations	20%
Ramp for persons with disabilities, up to Rs. 250,000 each	100%

DEFINITION

Structural improvement includes any building, road, driveway, car park, railway line, pipeline, bridge, tunnel, runway, canal, dock, wharf, retaining wall, **fence**, power lines, water or sewerage pipes, drainage, landscaping or dam. An asset jointly owned with an Islamic financial institution under **musharika / diminishing musharika** is treated as wholly owned by the taxpayer.

2 RULES OF DEPRECIATION

section 22

1 BASE

On the **written-down value (WDV)** at the start of the year; in the year of acquisition WDV = cost less initial allowance.

2 TIMING

Full year in the year of acquisition; **none** in the year of disposal.

3 PRIVATE USE

Allowed on a **proportional** basis. WDV is reduced by the **full** depreciation; on disposal the **disallowed part is added back** to WDV.

4 EXEMPT YEARS

Depreciation during years when business income was **exempt** is treated as allowed.

5 TOTAL LIMIT

Depreciation + initial allowance cannot exceed **cost**.

6 NO WITHHOLDING

Depreciation is disallowed in **all years** if required withholding on the purchase payment was not deducted and deposited.

7 REVALUATION · IMPAIRMENT

Ignored for tax: depreciation follows tax WDV.

8 IDLE OR DISCARDED

An asset that **ceases to be used** in business is treated as **disposed of**: no depreciation.

3 INITIAL ALLOWANCE

section 23

WHO GETS IT

An **eligible depreciable asset placed into service in Pakistan for the first time**, in the year first used or the year commercial production starts, whichever is **later**. Rate: **25% of cost** for plant and machinery.

NOT ELIGIBLE

Road transport vehicles not plying for hire · **furniture** and fittings · plant **used before in Pakistan** · assets fully expensed elsewhere · **immovable property** and structural improvements.

LESSORS

A lessor's initial allowance and depreciation are deductible **only against lease rental income** from those assets.

INDUSTRIAL UNDERTAKING · s.2(29C)

10+ persons with power or **20+ without power** engaged in manufacture, ship-building, power generation, mining; construction (plant imports, from 1 May 2020); **hotels** (from 1 July 2020); **PTA-licensed telecoms**.

4 DISPOSAL RULES

gain or loss against WDV

GAIN OR LOSS

Consideration > WDV → excess is business income. **Consideration < WDV** → difference is a deduction. No depreciation in the year of disposal.

PASSENGER VEHICLE

Cost for depreciation capped at **Rs. 7.5 million**. Consideration on sale = **7.5m ÷ actual cost × amount received**.

BUILDING AND EXPORTS

Building sold above cost, or asset **exported** from Pakistan: consideration treated as **cost** → gain = **depreciation allowed**. Cost of a building excludes land.

5 WORKED EXAMPLES

fresh numbers

Plant and machinery · depreciation + initial allowance	Rs.	Working
Opening tax WDV	2,000,000	
Less: WDV of disposals (no depreciation in year of disposal)	(300,000)	
Balance A	1,700,000	
Addition eligible for initial allowance	800,000	
Initial allowance 25%	200,000	25% × 800,000
Balance B (800,000 − 200,000)	600,000	
WDV for normal depreciation (A + B)	2,300,000	
Normal depreciation 15%	345,000	15% × 2,300,000
Total: initial allowance + depreciation	**545,000**	

PRIVATE USE · COMPUTER

WDV Rs. 200,000; 70% business. Depreciation 30% × 200,000 = 60,000; **allowed 42,000**; WDV c/f **140,000** (reduced by the full 60,000).

PASSENGER CAR

Cost Rs. 9,000,000. Year 1: 15% × 7,500,000 = 1,125,000 → WDV 6,375,000. Sold next year for 8,100,000: consideration 7.5/9 × 8,100,000 = 6,750,000 → **gain 375,000**.

EXPORTED MACHINE

Cost Rs. 35m, WDV Rs. 28m, export proceeds Rs. 45m: consideration = cost 35m → **gain 7m** (= depreciation allowed).

6 INTANGIBLES AND AMORTISATION

section 24

WHAT IS AN INTANGIBLE

Patent, design, secret formula, copyright, trade mark, **computer software**, film, **franchise**, licence, contractual rights, and any expenditure giving a benefit for **more than one year** — but not depreciable assets, unimproved land or **self-generated goodwill**.

AMORTISATION

A ÷ B: cost ÷ normal useful life in **whole years**. No ascertainable life → **15 years**. Partly business → **fair proportion**. Part of year → **× days used ÷ days in the year** (available-for-use days count, even non-working).

DISPOSAL

No amortisation in the year; consideration above WDV is business income, below is a deduction. Total deductions cannot exceed cost.

EXAMPLE · SOFTWARE

Rs. 7,300,000, life 20 years, available from 1 March 2027: 7,300,000 ÷ 20 = 365,000 × **122/365** = **Rs. 122,000** (Mar 31 + Apr 30 + May 31 + Jun 30 days).

EXAMPLE · FRANCHISE

Rs. 4,500,000, no ascertainable life, 60% business use: 4,500,000 ÷ 15 = 300,000 × 60% = **Rs. 180,000**.

7 PRE-COMMENCEMENT EXPENDITURE

section 25

WHAT QUALIFIES

Expenditure **before the business starts**, wholly and exclusively to earn taxable income — feasibility studies, **prototypes**, trial production.

NOT INCLUDED

Cost of **land**; anything depreciated or amortised under ss.22 / 24.

DEDUCTION

20% a year, straight line; total cannot exceed the expenditure; nothing if the entire amount was deducted elsewhere.

8 DISPOSAL, ACQUISITION AND BANKING CHANNEL

sections 75, 75A

DISPOSAL · s.75

Parting with ownership: sold, exchanged, transferred, cancelled, redeemed, **destroyed, lost**, expired, surrendered. Also **succession or will**; **business asset to personal use**; asset **discarded or no longer used**; part of an asset.

ACQUISITION

When the person begins to own the asset or is granted a right. A **personal asset applied to business** is an acquisition at that time.

BANKING CHANNEL · s.75A

Immovable property above Rs. 5 million and **any other asset above Rs. 1 million** must be bought by crossed instrument or **digital means**. Otherwise: **no depreciation, initial allowance, amortisation or pre-commencement deduction** and the amount is **not cost**.

9 COST OF AN ASSET

section 76

1 PURCHASED ASSET

Cash paid + **FMV of anything given in kind** + **incidental expenditure** (acquiring and disposing) + expenditure to **alter or improve**.

2 PRODUCED ASSET

Total costs of producing or constructing it (materials, wages, consumables, power, factory overheads) + later improvements and disposal costs.

3 PERSONAL ASSET TO BUSINESS

FMV on the date it is applied to business use.

4 FINANCE LEASE

Lessee: on maturity or early termination, cost is the **residual value or bargain purchase price**; during the lease, rentals are deducted.

5 FOREIGN-CURRENCY LOAN

Increase or decrease in the rupee liability before full repayment is **added to or deducted from cost** (taking hedges into account).

6 GRANTS AND SUBSIDIES

Deducted from cost, except to the extent chargeable to tax.

7 PART DISPOSAL

Apportion cost by the **FMV at the time of acquisition**.

8 OTHER

Asset received as taxed income: amount taxed + amount paid. Exempt receipt: exempt amount + amount paid. Inherited immovable property: **FMV**.

EXAMPLE

Worked example: plant cost Rs. 150,000,000; voluntary government subsidy (not taxable) Rs. 10,000,000; exchange loss on its foreign-currency loan Rs. 300,000 → cost = **140,300,000**. Initial allowance 25% = 35,075,000; WDV 105,225,000; depreciation 15% = **15,783,750**; WDV carried forward **89,441,250**.

10 CONSIDERATION RECEIVED

section 77

GENERAL RULE
Higher of the amount received and the **FMV**, plus the FMV of anything received in kind.

LOST OR DESTROYED
Includes **insurance, indemnity, settlement or court compensation** received.

PERSONAL USE · DISCARDED
FMV at the time applied to personal use or discarded.

SEVERAL ASSETS
Not separately priced: **apportion by FMV** at the time of sale.

11 WORKED EXAMPLES · LEASE AND BUILDING DISPOSAL

fresh numbers

Finance lease: vehicle cost Rs. 2,000,000 — stage	Cost for depreciation (lessee)
Before payment of the 6th instalment	Rs. 2,000,000
After the 6th, before the 12th	Rs. 1,500,000
After the 12th, before the 18th	Rs. 1,000,000
After the 18th, before the 24th	Rs. 500,000
On maturity (after the 24th): residual value	**Rs. 100,000**

EXAMPLE

Building sold above cost: cost Rs. 60m, depreciation allowed to date Rs. 18m, sold for Rs. 90m. Because the price exceeds cost, consideration is treated as **cost (Rs. 60m)**. WDV = 60 − 18 = 42m → gain = 60 − 42 = **Rs. 18m**, i.e. exactly the depreciation allowed.

12 QUICK RULINGS

from the Study Text situations

REVALUED BUILDING
Depreciation on **tax WDV**; accounting revaluation is irrelevant.

OVERSEAS OFFICE
No initial allowance (not placed in service in Pakistan); normal depreciation allowed.

IMPAIRMENT CHARGE
Not deductible; WDV is not reduced.

IDLE MACHINERY
Not used in business → **no depreciation**.

CAR NOT PLYING FOR HIRE
Depreciation yes; **initial allowance no**.

SOFTWARE BOUGHT 1 APRIL
Amortise for **91 days**, not the full year.

LEASED ASSET TRANSFERRED AT MATURITY
Full-year depreciation on the **residual value**; no initial allowance (previously used).

UNREALISED EXCHANGE GAIN
Notional, not taxable; realised gains are.

13 EXAM FOCUS · MCQ TRAPS

what examiners test

1 Tax WDV only
Revaluation and impairment are ignored; depreciation uses tax WDV.

2 Year rules
Full year on purchase; **none** on disposal; initial allowance only for assets **first used in Pakistan**.

3 IA exclusions
Non-hire **vehicles**, **furniture**, previously used plant, buildings.

4 Partly private
Business share allowed; WDV reduced by the **full** depreciation; disallowed part **added back** on disposal.

5 Car cap
Cost capped at **Rs. 7.5m**; sale proceeds scaled by 7.5m ÷ cost.

6 Gain on buildings and exports
Consideration = **cost**, so gain = depreciation allowed.

7 Amortisation
Days, not months; **15 years** if life unknown; self-generated goodwill excluded.

8 s.75A
Immovable > Rs. 5m or other asset > Rs. 1m not paid via banking: **no allowances, not cost**.

CLASSIFY IT · WHICH RATE?

1	Factory building	10%
2	Office furniture and fittings	15%
3	Delivery van	15%
4	Computer printer and monitor	30%
5	Aircraft and aero engines	30%
6	Technical or professional books	15%
7	Ramp for persons with disabilities (up to Rs. 250,000)	100%
8	Initial allowance on new plant	25%

CLASSIFY IT · ALLOWED OR NOT?

1	Initial allowance on a new machine used in Pakistan	ALLOWED
2	Initial allowance on office furniture	NOT ALLOWED
3	Initial allowance on a car not plying for hire	NOT ALLOWED
4	Initial allowance on plant used before in Pakistan	NOT ALLOWED
5	Depreciation on the revalued amount	NOT ALLOWED
6	Depreciation in the year of disposal	NOT ALLOWED
7	Depreciation on idle machinery	NOT ALLOWED
8	Full-year depreciation in the year of purchase	ALLOWED

LIMITS TO KNOW

Car cap	Pre-commencement	Unknown life	s.75A	Initial allowance
Rs. 7.5m	20% straight line	15 years	Immovable Rs. 5m · other Rs. 1m	25% plant

REVISION MAP

1 · DEPRECIATION
Tax WDV basis · rates 10 / 15 / 30 / 100% · full year on purchase, none on disposal · private use proportional · revaluation and impairment ignored

2 · INITIAL ALLOWANCE
25% on plant and machinery placed in service in Pakistan for the first time · not for furniture, non-hire vehicles, previously used plant, buildings, fully expensed assets

CHAPTER 8
BUSINESS PART TWO

3 · INTANGIBLES AND PRE-COMMENCEMENT
Amortisation A ÷ B × days used ÷ days in year · 15 years if no life · pre-commencement 20% straight line, no land

4 · DISPOSAL AND COST
Gain / loss vs WDV · cost = price + kind + incidental + improvements ± FX − grants · consideration: higher of price / FMV + kind · s.75A banking rule

Depreciation
On tax WDV only.

IA
Plant first used in Pakistan.

Intangibles
Days, 15-year default.

Assets
Cost and consideration.