Income Tax Ordinance 1979 and the Salaried Class

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The aim of the taxation is to reduce the private consumption and private investment so that the government can provide social goods and merit goods and subsidize the poor without causing inflation or balance of payments difficulties.[1] Of course taxation must not be set so high as to reduce private activity to such an extent that unemployment exists. Income Tax as the name suggests is a tax on income and is the most important direct tax; which reduces the real income of tax payer that is his savings, leisure or consumption of other goods is reduced.[2] This is because it does not provide an escape to the tax payers. The Income tax also lends itself to a greater degree of the sophistication in the application of progressive principle than any other tax. It may be graduated, lower rates being charged upon the first bands of taxable income and higher rates thereafter.

Income could be derived from various sources but here I would be discussing the income earned through salaries and the provision with regard to it in the Income Tax Ordinance of 1979.[3] Without going into the details of salary income, which includes any wages, annuity, pension or gratuity, I will concentrate on the rate structure of income tax affecting the salaried persons.

Under the Ordinance 1979, the tax shall be levied on the excess of income over Rs. 12 000/- by giving a straight line deduction of this amount without having to compute various allowances. The income exceeding Rs. 12,000/- and up to Rs. 21,000/- shall, subject to marginal adjustment, be Rs. 120/- without investment allowance and Rs. 84/- if full investment allowance is availed.[4]

The rate structure has been so designed that for income exceeding Rs. 21,000/- and up to Rs. 40,000/- tax payable will be more or less the same as before. On incomes beyond Rs. 60,000/- per annum the rates have been made more progressive.[5]

Relief on account of investments and donations will now be given as a rebate computed at the average rate of tax, as against straight line deduction allowed in the past.[6] Although the method of tax relief has been changed tax rates have been so devised that incidence of tax after investment remains more or less the same as before. The following table describes the tax burden at the different levels of income.

Tax Burden at Different levels of Salaried Income[7]

Total Salary Income	Investment 30%	Tax Liability under New Rules		Tax Liability under Old Rules	
		With Investment	Without Investment	With Investment	Without Investment
Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
21,000/-	6,300/-	84/-	120/-	190/-	1,140/-
40,000/-	12,000/-	2,534/-	3,620/-	2,700/-	6,900/-
60,000/-	18,000/-	8,484/-	12,120/-	8,300/-	14,500/-

The above table gives the tax liability under new and old rules for three different arbitrary levels of income to show the effect of the burden of tax. It may be clearly observed that the amount of tax paid in all three cases after the allowance of full investment is more or less the same, whereas the tax without investment significantly differs. If we take into account the amount of investment plus the amount of tax paid by the tax payer it works out to be 30.4%, 36.3% and 44.1% respectively in the three cases. Barring the first case of Rs. 21,000/- where the difference in the amount of tax before and after investment is not significant, the ratio is very

high. Keeping in view the family liabilities of a tax payer of salaried class it would be demanding heavily on him. The saving of 36.3% and 44.1% in both the cases respectively is definitely too high.

This suggests that the present provisions are superior to the old ones up to the income of Rs. 21,000/- as there is less burden on the tax payer. The saving capacity of the salaried class is very low, specifically in the face of rising prices, which erode their real incomes. But in case of other two cases incidence is more or less the same though the present money income in real terms is much less.

The provision of deduction at source in case of salaried people is of immense advantage not only from the view point of the collection of revenues, but it also gives them a little feeling about the tax burden.[8] Contrary deduction at source also makes them sacrifice not only the immediate use of the money but also deprives them of the interest otherwise earned on such savings.

Summary, Conclusion and Suggestions

It may be summarized that as far as the income levels up to Rs. 21,000/- are concerned the present income system is superior, as it does not fall heavily on the salaried class tax payers. But it has not brought any remarkable advantages to the tax payer with the exception that it is easier to assess. I, therefore, suggest that keeping in view the rising cost of living the nominal amount of tax may be levied on the salaried income up to Rs. 50,000/- (it may be mentioned that it can safely be assumed that each salaried person has at least 4 dependents), and beyond Rs. 50,000/- to Rs. 1,00,000/- the share of tax plus investment should be 20% of the real income i. e. deflating the income accordingly. Secondly, keeping in view the sacrifice involved, the deduction at source may be stopped but it may not look practicable hence some concession in tax may be allowed, after all he is an honest tax payer, who neither avoids nor evades the tax.

Appendix

Income Tax Rates under new Ordinance– Sections 9, 10 and 50

In case of every Individual, unregistered firm, an Association of persons, Hindu undivided family and every artificial Judicial person the following rates are applicable on taxable Income:–

	Tax Rate
Where Taxable Income does not exceed Rs. 10,000	15%
,, ,, exceeds Rs. 10,000 but does not exceed Rs. 15,000	Rs. 1500+20% on exceeding Rs. 10,000/–
,, ,, Rs. 15,000 ,, Rs. 20,000	Rs. 2500+25% on exceeding Rs. 15,000/–
,, ,, Rs. 20,000 ,, Rs. 25,000	Rs. 3750+35% on exceeding Rs. 20,000/–
,, ,, Rs. 25,000 ,, Rs. 30,000	Rs. 5500+40% on exceeding Rs. 5,000/–
,, ,, Rs. 30,000 ,, Rs. 60,000	Rs. 7500+50% on exceeding Rs. 30,000/–
,, ,, Rs. 60,000 ,, Rs. 1,00,000	Rs. 22500+55% on exceeding Rs. 60,000/–

(No tax is payable by an assessee whose income is less than Rs. 12,000)

Tax Rates for Resident as per Assessment Year 1977-78 Onwards

Taxable Income Rs.	*Tax Rates*
1 to 5,000	10%
5,001 to 10,000	500+20% on exceeding Rs. 5,000
10,001 to 20,000	1500+30% on exceeding Rs. 10,000
20,001 to 30,000	4500+40% on exceeding Rs. 20,000
30,001 to above	8500+50% on exceeding Rs. 30,000

References

1. Allan, Charles M., The Theory of Taxation, Penguin Modern Economics Texts, Penguin Books, 1971, p. 23.
2. Ibid, p. 33.
3. Government of Pakistan, Central Board of Revenue, Income Tax Ordinance, 1979 (XXI of 1979), pp. 22–23.
4. Ibid, p. 91.
5. Government of Pakistan, Central Board of Revenue, open circular No. 4 of 1979 titled Income Tax Ordinance 1979–Important Provisions–Instruction regarding, p. 31.
6. Ibid, p. 31.
7. The Table is prepared by the author by taking into consideration three different hypothetical but of much practical significance, levels of income.
8. Mehta, J. K. & Agarwala, S. N., Public Finance—Theory and Practice, Kitab Mahal, Allahabad, 1960, p. 275.