TAMSAAL
ISSN Print: 3007-5939
ISSN Online: 3007-5947
Volume 4, Number 7, 2026, Pages 431 – 457
Journal Home Page
https://tamsaal.pk/index.php/tamsaal/index

The Withholding Dilemma: Revenue Necessity or Compliance Nightmare? A Critical Legal Analysis of Pakistan's Withholding Tax Regime

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ARTICLE INFO

Article History:

Received:	*June*	*08, 2026*
Revised:	*July*	*11, 2026*
Accepted:	*July*	*20, 2026*
Available Online:	*July*	*27, 2026*

Keywords:

Withholding Tax, Taxation, Federal Board of Revenue, Tax Regime, Final Tax

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DOI: *https://doi.org/10.59075/tamsaal.v4i7.115*

ABSTRACT

Taxation System plays a significant role in the economy of Pakistan and Withholding tax regime is undoubtedly the backbone of FBR tax revenue on yearly basis. In this research I will examine the role and importance of Withholding Tax in Pakistan and the prevailing laws in this regard. Majorly I have examined how in previous years revenue generated by Withholding Taxes has significantly increased. In addition to all these details regarding the withholding tax I have discussed the dark side of extreme reliance on Withholding Tax System by the government by neglecting other indirect and direct ways of collection of taxes.

Introduction

Taxation is the ultimate way to promote public welfare and regulate the governmental affairs. For developing countries, it is pertinent to make effective taxation plans as there is no other opinion to admit that the taxes are the backbone to Pakistan's economy. (Sherani, 2025) Effective taxation policies ensure the well-being of country. As Pakistan is a developing country and there is always quest for effective revenue generating mechanism. (NASIR, 2020)

The term Withholding means to "Refuse to give the due or desired" while on the other hand, withholding tax is known as "Retention tax". It is referred to the deduction or collection of tax at source which means it is a sort of tax being deducted automatically at source by the payer of the Income. (Tax, 2026) The payer directly sends the tax withheld to the government treasury. This means that the withholding agent deducts the Withholding Tax according to the set percentage from the payment received and directly sends it to the government reserves. (Babar, 2024) The withholding tax can be refunded or claimed afterwards. Somehow, they are considered as an Advance tax or Receipts that can be taken back from the government against their Annual Tax liability. On National level it is an effective and a major source of revenue for FBR. (FBR, 2025)

"The real reason for withholding taxes is the unwillingness of workers to share their incomes with the government and the consequent difficulties of collection. To overcome this handicap, the government has simply impressed employers into its service as involuntary and unpaid tax collectors" (Chodorov, 1954)

In Pakistan around 41% of total tax amounts to the Withholding tax. Intentionally or unintentionally, everyone is paying the Withholding tax. Under the Income Tax Act 1922, there were three heads for Withholding tax deduction; salaries, dividends and the interest on securities. But in Income Tax Ordinance, 2001 there are around 24 sections and sub-sections that provide numerous heads for the deduction and collection of Withholding taxes along with the prescribed rates. (TaxationPk, 2024)It is deducted on numerous cash flows; salary, dividends, phone calls, sale purchase of property or vehicles and the list goes on. The withholding agents are responsible to reduce the governmental expenses of collecting taxes with the help of their administrative powers. It reduces the tax burden of masses by allowing them to get rid of bulk of taxes. (Kagan, 2025)

The mechanism of collection of withholding tax ensures to the streamed collection of taxes throughout the year. The withholding taxes are considered as adjustable taxes against the total tax liability at the time of final taxation. But everything has its pros and cons, similarly Withholding taxes also expose the taxpayers and the government to various challenges and advantages as well. This research explores the legal status of Withholding Tax in Pakistan and navigates the major challenges faced in this regard along with possible reforms and solutions. (Ahmed, 2020)

Research Gap of the Study

The research gap identified in this study lies on fundamental level in between the how the withholding tax is studied and how it actually operates in Pakistan as a legal institution. After the review of existing literature, withholding tax is reviewed as a legal institution and fiscal policy. These works touch the areas of legal concern such as constitutional propriety of delegating tax powers to the executive through SRO's. This research is doctrinal in nature and this is precisely absent in many of the literatures that allows it to engage with the law in depth.

As the withholding tax at its core is a legal creation and this deficiency if find in maximum literatures. It is a legal concept because the Income Tax Ordinance, 2001 defines its scope at its core and prescribes its consequences. This law decides all of the aspects means who must will deduct it, how much will be deducted and what will be consequences in case of non-compliance. Every obligation regarding the withholding tax in regard of penalty or refund or filing of appeal comes directly from the statute. Withholding tax cannot be understood without been studied properly and these kinds of research work is missing from the existing research on Pakistan's withholding tax.

This gap is translated into four objectives first is the examination of the legal position of the withholding tax it responds to the absence of any detailed doctrinal analysis of the Income Tax Ordinance, 2001 and clearly defines the Withholding tax. The second objective is the analysis of contribution of withholding tax in direct tax base net and this concern is answered by studying how the withholding tax is treated as a fiscal achievement rather than a legislative manner for revenue generation. The third objective deals with the administrative, procedural and financial challenges faced by the taxpayers faced due to the compliance to the Withholding taxes and fourthly, a way forward is introduced that comply the benefit theory of taxation and in accordance with the rule of law and compared with the international jurisdictions

These four objectives scrutinize the statutory and constitutional framework and to observe whether the withholding tax regime applicable in Pakistan is correct or not. This research aims to study the unaddressed questions in the available literature. This research not only answers the concerns that how much revenue is generated by withholding taxes or how efficiently it is collected on yearly basis as it seeks the legal and constitutional validity of the of the withholding taxes and analyze whether they are judicially coherent or not.

Administrative, Procedural, and Financial Challenges Faced in Withholding Tax Compliance – Data Analysis and Results

This chapter presents the legal and factual data that forms the basis of this chapter. The data is organized into three categories; the relevant legal framework, revenue data available on the FBR portal in between the period 2019 to 2025 and the decisions of judicial authorities.

The Relevant Legal Framework

In this research, the legal framework is discussed at three levels; the constitutional provisions for tax, the statutory level which includes the Income Tax Ordinance, 2001and the regulatory level operating in Pakistan that comprises the Rules and SROs issued under the Income Tax Ordinance, 2001.

Constitutional Provisions

The Article 77 of the Constitution of Pakistan, 1973 says: -

“No tax shall be levied for the purposes of the Federation except by or under the authority of Act of Majlis-e-Shoora (Parliament).” (Constitution of Pakistan, 1973)

In simple words, the government cannot collect tax until unless it is allowed by the proper backing of law. Under the fourth Schedule, the Federal Government is authorized to make laws on Income Tax except in agricultural matters.

The Article 142 read with the Fourth Schedule to the Constitution explains the legislative competence between the Federation and the provinces in Pakistan. The entry 47 of the Federal Legislative List confers the taxes other than the agricultural income. The entry 50 deals with the capital value of assets but excluding the taxes on immovable property. (Constitution of Pakistan, 1973)

The Article 23 of the Constitution of Pakistan 1973 says that every citizen has the right to acquire, hold and dispose off the property but with subject to reasonable restrictions imposed by the law.

The Article 25 guarantees that every person is equal before the law and owns equal protection of law and is also engaged with the provisions of the withholding tax where the taxpayers are classified as filer and non-filers.

The Article 10A guarantees the right to fair trial and due process and also includes the administrative and quasi-judicial proceedings in regard of withholding tax assessments. (Consitution of Pakistan, 1973)

Statutory Provisions of the Income Tax Ordinance, 2001

The Income Tax Ordinance 2001 is the main statutory instrument used to govern the taxation matters in Pakistan. It was promulgated on 13 September, 2001 and was enforced on 1st July 2022, it was a replacement of Income Tax Ordinance, 1979 which was itself replaced by the Income Tax Act, 1922. The Income Tax Ordinance, 2001 is the most comprehensive instrument for restructuring the Taxation regime in Pakistan since 1947 the Income Tax law was undertaken as part of a broader tax reform agenda supported by the International Monetary and the World Bank which had made the taxation a complex one and administratively inefficient. (Alagappan, 2020)

The Income Tax Ordinance 2001 was heavily influenced by the International best standards. the Ordinance revolves around the principle of self-assessment means that the taxpayers should compute and declare their tax liability on their own and the tax authorities play the role of supervision and play the role of audit rather than determining the tax liability at the first instance. This philosophy was a major departure from the 1979 Ordinance's assessor-based system. At that time the department was independently responsible for the assessment of liability of each taxpayer. (Inam & Khan, 2008)

The Income Tax Ordinance 2001 being enforced in July 2002 has been amended nearly twenty-three time through the Finance Acts and by mid-year amendments through SROs. The constant and frequent amendments have altered the character of the Ordinance from the original form to a point where its foundational principles including the self-assessment and the preference for the assessed income over the presumptive taxation have been immensely diluted. (Tariq, 2018)

Concept of Income

The concept of Income is the foundation in the system of income tax because the income tax is imposed on the income that the law recognizes. The Oncome Tax Ordinance, 2001 explains the concept of Income as it does not provide a single definition but explains its concept. (Areej & Iqbal, 2023)

The Section 2 of the Income Tax Ordinance, 2001 contains the foundational definitions on which the regime of withholding taxation in Pakistan is based. The Section 2 defines the Income in a broad manner. (Shouzab, Yasin, & Sultan) It covers the amount on which the tax is charged under the Income Tax Ordinance, 2001 at which the collect is collected and deducted at source including import, dividends, payments to non-residents etc. It also includes anything that the law considers as income. Income is indeed wider comparative to the regular earning. (Khan, 2020)

The income is not limited to the salary of business profit as the Ordinance provides a broader approach to it. As Income under the Ordinance refers to any economic benefit that a person receives other than the exemptions. As different heads of income such as wages, rental income, dividends, profit on debt etc. all constitute the taxable income by depending on the circumstances prescribed by the law itself. (Amir, 2011)

Each of the Income head is subjected to different computational rules, deductions and exemptions and withholding tax provisions. The understanding of legal meaning of Income helps to analyze the withholding tax regime in Pakistan.

The concept of income is well linked with the principle of taxability. Before subjecting to the deductions and collections under the withholding tax regime, the very first thing that must exist is whether the amount qualifies under the taxable income or not. (AHMED, 469–516)

Tax Year and its Legal Significance (Section 74)

In the income tax regime, the concept of tax year plays a significant role as it determines the period for which the income of the person is assessed, computed and taxed. Under the Section 74 of the Income Tax Ordinance, 2001 the taxable income is calculated and assessed with respect to the specified tax year. The applicability of the tax rates, filing deadlines and withholding taxes are subjected to the tax year. As the withholding taxes are deducted throughout a tax year, in this case the tax year plays a significant role. (Malik, 2025)

Normal Tax Year

According to the Section 74 of the Income Tax Ordinance, 2001 the basic rule is that the tax year is of twelve months and end on 30th June of each year. This tax years refers as a Normal Tax Year. The normal tax year is a standard accessing year in the income tax. It upheld consistency in compliance and enables the uniform administration by the FBR. It serves as a standard year within which the withholding taxes are accessed, collected and deducted against the taxpayer’s liability. (Bukhari & Haq, Tax Reforms in Pakistan Historic & Critical View, 2020)

Special Tax Year

As certain taxpayers do not follow the normal tax year as their records are maintained according to a different accounting cycle. This is also a twelve-month consecutive period but not ending on June 30th of the year. The special tax year is identified on the closing date of filing. Although the special tax years end different to the normal tax year but the withholding taxes are deducted and collected at source as per the approved tax year. (Ilyas, 2020)

Transitional Tax Year

Transitional tax year refers to the intervening period between the new and old accounting year when the taxpayer changes from one tax year to another. This transactional tax year ensures that the income earned during this changeover period is properly assessed and no income is left untaxed. (Streimikiene, Ahmed, Vveinhardt, Ghauri, & Zahid, 2018)

Th withholding tax deducted and collected during the transitional period is referred to that tax year so that the adjustments and credits are done in accordance to the provisions of Income Tax Ordinance, 2001. (Ahmed, Ashfaq, & Malik, 2024)

Withholding Tax Regime in Pakistan

The withholding taxation is the most effective and quick mean of collecting income tax as withholding tax is deducted and collected at source. It is the most commonly used mean for the purpose of tax collection. It provides the most reliable and streamlined income to the government for revenue generation. (Amin, Nadeem, Parveen, Kamran, & Anwar, 2014)

It is not a distinct mean of income tax as it does not create any independent fiscal obligation, it determines the manner and point at which the existing income tax liability is discharged. This distinction holds importance to understand the legal character of the withholding tax mechanism.

The Part V of the Income Tax Ordinance, 2001 comprising of Sections 147 to 169. This part holds complete details regarding the source-based tax mechanism. It holds complete identification of the transactions that attract the withholding, the persons who are under obligation to file the withholding taxes and the consequences in regard of default. (H.Sial & Ahmad, 2016)

The government exercises the most pervasive form of fiscal power, the private individuals and businesses are conscript into the role of unpaid tax collector and they are required to intercept income at the moment it changes the hands and before the access of recipient, it is remit to the government. This mechanism is based on the legal principle that the tax is collected from the payer who is considered accountable entity such as employer, a bank or any registered entity who is administratively more reliable as compared to collecting it from the individual recipient who receives the income. The burden is transferred from state to the private withholding agent. (Hassan, Naeem, & Gulzar, 2021)

Who is the Withholding Tax Agent?

Withholding tax Agent is the one who collects and deducts tax under the provisions of Income Tax Ordinance, 2001. (FBR, Income Tax Ordinance, 2001) There is no explicit explanation of Withholding agent in the Income Tax Ordinance, 2001 but the term "Prescribed Person" represents the same. It is defined in the Section 153(7) of the Income Tax Ordinance. (IRS, 2025)

In Tax Reference N0-10-P/2014 the prescribed person is referred to Withholding Agent in following words: -

"The Amendment expands the scope of a "prescribed person", as a "withholding agent", to collect advance tax on payments made. The Amendment, therefore, not only imposes an additional obligation upon the taxpayer to act as a "withholding agent" of collecting advance tax but it also imposes a pecuniary liability on him for failing to act and collect the same." (M/S Shaukat Khan & Co v Commissioner of Land Revenue, 2014)

Duties of Withholding Agents

The Withholding Agent has to perform following duties:-

- The Withholding Agents are required to deduct/ collect the withholding tax on the concerned transaction. (Associates, 2025)
- The Withholding Agents are responsible to deposit the deducted/collected taxes into the government treasury. (Academy, 2024)
- The Withholding Agents are required to keep track of the Withholding taxes as such record is required to be produced during audits. (OLY, 2019)

SWAPS - Synchronized Withholding Administration and Payment System

Under the Withholding tax regime under the Income Tax Ordinance, 2001 the "SWAPS" refers to the exchange of legislative exchange of one form of tax treatment to another.

FBR introduced the system of SWAP through Finance Act 2022 to deal with the concerns regarding delayed or non- payment of Withholding taxes. The Section 164 deals with this. In this system the FBR can notifies certain people or individuals to deduct/collect Withholding Taxes, they are referred as SWAPS agents. (TaxationPK, 2024) They are obligated to deposit tax to FBR without delay by using SWAPS payment receipt instead of computerized payment receipt and it acts as a solid proof of Withholding Tax deduction. As this system is directly linked with FBR so it is really effective. (Association, 2022)

It is the automated and real-time digital system to streamline the monitoring, collection and documentation of the withholding taxes. It resolves the concern of non-payment or late-payment of tax by the withholding agents through the Synchronized Withholding Administration and Payment System Agent. (Vatupdate, 2024) The SWAP agents are integrated with the FBR and withholding tax is deposited in the government treasury on real-time basis at the time of making the third-party payment processed by the SWAPS agents. In case of non-compliance penalties are imposed. It reduces time and cost of compliance for the businesses by auto generating the withholding statements. (FBR, Income Tax Ordinance , 2001)

Statutory Provisions Regarding Withholding Tax Under the Income Tax Ordinance, 2001

The Part V of the Income Tax ordinance, 2001 contains the charging provisions which create the primary withholding obligations represented by the provisions of Division II and Division III, principally Sections 148, 149, 150, 151, 152, 153, 155, 156, 236C, 236G, and 236H. In each of these provisions taxable event is identified. Than the classification provisions that determine the legal character of the deductions represented by Sections 168 and 169 of Division IV, these provisions identify whether the tax is characterized as final tax or adjustable tax and the enforcement provisions that ensure proper compliance represented by Section 161 (personal liability of the withholding agent for failure to collect or deduct), Section 165 (biannual statement filing obligation), Section 182 (penalty for non-compliance), and Section 205 (default surcharge). With the help of these sections the State ensures that the withholding obligations are fulfilled properly. (Shakeel, 2023)

In order to understand the specific legal problems generated in between the period of 2019 to 2025 it is necessary to understand the interaction and structure of the three mechanisms of the withholding tax.

The Charging Provisions

Imports – Section 149

The Section 148 of the Income Tax Ordinance, 2001 is the sole provision of the Division II that requires the Collector of Customs to collect the advance tax from the good's importer at the time od clearance and that is computed on the value of goods determined for the custom purposes as per the prescribed rates under the Part II of the First Schedule where the categories of importers and items are differentiated. (Waseem, 2019) There are no private withholding agents stands in between the payee and the payer so it is not understood as a withholding provision in the strict sense. It is a collection at source mechanism as the state itself perform the functions under the Section 149 through the Custom authorities, delegate the powers to the private persons. The tax collected under the Section 148 for the extreme majority for commercial importers. This is treated as the minimum tax or final tax under the Section 148 with the consequence that the import stage withholding tax is the largest contributor in the income tax net. (Shabir, 2023)

Income through Salary – Section 149

The Section 149 of the Income Tax Ordinance, 2001 deals with this head. In case of salaried persons, the employers are obligatory to deduct Withholding Tax. The rate of Withholding Tax for all salaried individual is not same as everyone is subjected to different rates depending on their Income. (Chohan & Mujtaba, 2024) Tax slabs being mentioned in the Income Tax Ordinance are considered in this regard. Being a filer or a non-filer, impacts less in case of the income through salary as compared to the business transactions. Through Finance Act 2024, following tax rates were introduced: -

Taxable Income PKR	Tax Rate %
up to 600,000	0%
600,00 to 1,200,00	5% of the amount exceeding 600,000
1,200,00 to 2,200,00	15% of the amount exceeding 1,200,00 + 30,000
2,200,00 to 3,200,000	25% of the amount exceeding 2,200,00 + 180,000
3,200,000 to 4,100,000	30% of the amount exceeding 3,200,000 + 430,000
More than 4,100,000	35% of the amount exceeding 4,100,000 + 700,000

Source: Compiled by the researcher

In July to December 2024, there was increase of 59.2% (Rs.98.8 billion) in Withholding Tax collected under Section 149 of the Income Tax Ordinance, 2001. (FBR Year Books)

Income Through Dividend – Section 150

The Section 150 deals with the income through dividends. When a company shares profit with its stakeholders, this is considered as Income through Dividend. Income through dividend is also subject to Withholding Tax. (Khan A., 1999).

Type of Dividend Payment	Filer/non-Filer
Independent power projects	7.5/15%
Real Estate Investment Trust/ Mutual Funds	15/30%
Real Estate Investment Trust/ Mutual Funds - In case of 50% or more Income derived from profit on debt	25/50%
Exemption to Company or carry forward business loss	25/50%

Source: Compiled by the researcher.

In July to December 2024, there was increase of 51.1% (Rs.31.4 billion) in Withholding Tax collected under Section 150 of the Income Tax Ordinance, 2001. (FBR Year Books)

Profit on Debt – Section 151

Profit on debt is discussed in section 151 of the Income Tax Ordinance, 2001. It refers to the amount gained as a profit or interest when a person deposits money in any financial Institution or gets through investment. The profit through debt is also liable to Withholding Tax. (Hassan, Mahmood, Tahir, Alkhateeb, & Wajid, 2021)

Profit on Debt by:	Filer/non-Filer
Individual/AOP	15/35%
Company	15/35%

Source: Compiled by the researcher.

In July to December 2024, there was increase of 16.2% (Rs.35.6 billion) in Withholding Tax collected under Section 151 of the Income Tax Ordinance, 2001. (FBR Year Books)

Payment to Non-Residents – Section 152

The section 152 deals with the payments made to non-residents. When any individual or any business organization makes payment to a non-resident person, withholding tax is applied on dividends, interests or any other sort of fees. (Siddique, 2014) As Pakistan has signed Double taxation Agreements with many countries, so in case of this the rates can be reduced. (Siddique, Taxation of Non-Residents under Income Tax Law of Pakistan, 2016) The core purpose is to serve people by preventing the same income to be subjected to taxation in both countries. They is a quite favorable scenario. (FBR, Standard Operating Procedure For Monitoring of Withholding Taxes , 2011)

Payment to non-residents	Tax Rate %
Dividends	15
Interest	10
Royalties	15

Source: Compiled by the researcher.

Payments For Goods and Services – Section 153

The treatment with the payment for goods and services falls under the section 153. Withholding tax is deducted on the payment made by any individual or any company either for the payment of goods or services. As in this scenario the person being a filer has to pay less tax as compared to the non-filer. (Malik, Effectiveness of Withholding Taxes in Expanding Pakistan's Tax Base: A Focus on the informal and Undocumented Sectors, 2025)

Payment By	Filer/non-Filer
Company for Other Goods	5/10%
Company (Toll manufacturing)	9/18%
Individual/AOP for Other Goods	5.5/11%
Individual/AOP(Toll manufacturing)	11/22%
Sales of cotton, rice, seeds, edible Oils	1.5/3%

Source: Compiled by the researcher.

In July to December 2024, there was increase of 25.2% (Rs.60.3 billion) in Withholding Tax collected under Section 153 of the Income Tax Ordinance, 2001. (QuratulAin, 2024)

Income from Property (Rent of Immovable Property) – Section 155

Under the Section 155 of the Income Tax Ordinance, 2001 obligates the Federal Government, Provincial Government, local authorities, associations of persons and other organizations to deduct tax on the rent paid on the lease of immovable properties including the lease of items including furniture and fixtures and other allied services at progressive rates set by the authorities. The individuals and associations receiving rent as their sole and principal source of income, it is generally treated as a final tax under Section 169 but for companies it is treated as a minimum or adjustable tax, thereby the income being a source of rent is removed from the ordinary computation of business or other income and subjected to tax as gross. (Akhtar, Safdar, Baig, Ahmad, & Khan, 2022) On the basis of the progressive slabs without the reference to the deductible allowances of the landlords beyond what the slab structure implicitly assumes. The history of the Section 155 is narrower in practice in comparison to what the drafting in principle suggests. (Cyan, Koumpias, & Martinez-Vazquez, 2016)

Prize Money – Section 156

The section 156 deals with the prize money or winning amounts. This Section requires every person to pay prize on the prize bonds. The tax deduction under the Section 156 is treated as final tax. The revenue generated under the Section 156 is comparatively modest as compared to the revenue generated under the Sections 148, 149, and 153. (Shah, 2025)

They can be from quiz, lottery or prize bond. This is also subjected to Withholding Tax.

Payment By	Filer/non-Filer
Prize Bond/Puzzles	15/30%
Lottery/Quiz	20/40%

Source: Compiled by the researcher.

Debit and Credit Card Transactions – 236y

The section 236Y deals with the payment through debit and Credit cards. If a person makes payment somewhere outside Pakistan through debit card, credit card or any prepaid card, that payment is also subjected to the Withholding Tax. The core purpose of this is to reduce the outflow of dollars. (Ali, Muhammad, & Khushro, 2022)

Payment Method	Filer/Non-Filer
International Card	5/10%

Source: Compiled by the researcher.

Cash Withdrawal – Section 231a

The section 231A deals with the cash withdrawals. If any person withdraws cash from any bank more than Rs 50,000/-, the bank deducts Withholding Tax from the account holder. The ultimate purpose of this is to encourage people to use other banking channels like online banking and cheque system as this helps in record keeping and eliminates the risk of untracked flow of transactions. (Mughal & Akram, 2012)

Amount	Filer/non-Filer
More than 50,000	Exempt/0.6%

Source: Compiled by the researcher.

Among the ways mentioned in the ***Income Tax Ordinance, 2001*** for the collection of taxes, the collection of Income Tax at source means Withholding tax is the most profitable way.

The Classification and Enforcement Provisions

Normal Withholding Rule - Section 168

The Section 168 lays down the general rule for the treatment of tax withheld on payments. It assumes in two ways; firstly, it is deducted in way it treated as the part of the income as the government gets it directly and secondly the deduced amount is treated as tax that is already paid. (Ahmed & Talpur, 2016)

The law pretends you earned the full amount and already paid tax on it although it never passed through your hands.

As a result, you typically have the opportunity to use the withheld amount as a credit against your annual tax liability. (Aazim, 2017) For partners in a partnership-like entity, known as an "association of persons" or AOP, there is a specific calculation: if a company is a partner in such an entity and tax has been deducted from the entity's income, the company is entitled to claim its proportional share of that credit. This share is determined by the percentage of the entity's profit that the company owns. After the company makes this claim, the entity itself is not permitted to claim the same amount again, preventing any duplication of claims. (Mughal U. A., 2026)

One category of tax doesn't qualify for this normal credit treatment: amounts treated as final tax under Section 236Z(7), those are handled separately under Section 169 instead. If your credit ends up bigger than what you actually owe, you don't lose the difference you get it refunded.

(Rasheed, 2025) Two extra rules protect the integrity of this system: nobody is allowed to deduct a "service charge" or handling fee from tax money before handing it to the government, that money belongs entirely to the state. And if anyone does skim money off in this way, they become personally on the hook to pay it back, and the tax department can chase them down using all its normal recovery powers, just like unpaid tax. (Jamal, 2026)

Final Tax – Section 169

Section 169 is the section dealing with an exception to the rule which is Section 168. In practice, however, it applies to a major portion of the taxes that have been withheld. Section 169 only comes into play where there is a clear provision in the law that states that the withholding of taxes on a certain type of payment is "final" such as the case of certain payments made to nonresidents, certain services exported, prize winnings and petroleum products. (Reporter, 2026) In fact, over time, Parliament has deliberately taken several types of income including dividends and rent from certain taxpayers from this list of "final" payments and put them back to the regular Section 168 arrangement. (Munir, 2019)

Where the income falls under the category of Section 169's "final tax," then the following harsh consequences will apply to the taxpayer:

The income is not included in your income computation at all. It is excluded from your total income. (KPMG, 2025)

No actual expense that you incurred in earning that income will be deducted.

It cannot be reduced by using other allowances such as Zakat or in relation to any losses suffered.

Any other tax credits cannot be set against this amount withheld.

There will be no refund even if one feels they have been overtaxed unless it is proven that the tax withheld is indeed more than the amount that should have been withheld in accordance with the law in which case the only excess would be refunded. (Daudpota, 2025)

However, in case the payer should have withheld tax and hasn't done so, the tax authority can proceed to recover the tax.

If a person's income for the year is fully subject to this taxation, there would be no need for an additional assessment because the tax return filed itself would act as the assessment.

This is the reason why individuals whose incomes fall under final tax (many importers/exporters of services) find filing easy. (Aazim, 2017)

Significance of the issue:

The divide between Sections 168 and 169 is the key divide in the withholding tax regime of Pakistan. In Section 168, the process of withholding is the one that withholding was supposed to be; it is just a method of pre-payment of tax, which is adjusted against the final tax liability. In Section 169, however, withholding ceases to be an income tax and starts resembling a flat rate tax on gross revenue; it is fixed in amount, not refundable normally and does not take into account the actual expenditures of the taxpayer. That so many kinds of payments are still governed by Section 169 after years of reductions is indicative of how much the withholding tax system of Pakistan has moved away from the principle of taxation of net income. (Shouzab, Yasin, & Sultan, ISSUES IN PAKISTAN'S DIRECT TAXES: AN EXAMINATION OF THE RECENT PROBLEMS IN THE INCOME TAX ORDINANCE, 2001 , 2022)

Failure to Pay Tax Collected or Deducted – Section 161

Section 161 is primarily the provision that subjects the withholding agent to personal liability for failing in its responsibilities. If the withholding agent fail to withhold the tax, or if he withhold the tax but not turn it over to the tax authorities, then he will be personally liable for paying the tax himself along with interest charges as if he had himself become liable for the tax. The liability arises independent of what the actual taxpayer may owe in taxes. (Bukhari & Haq, Tax Reforms in Pakistan Historic & Critical View, 2020)

Tax authorities can collect this tax from the withholding agent without proving that the taxpayer failed to pay or report his tax with the single exception of the case when it transpires that the taxpayer paid his tax personally. Section 161 has been the cause of most of the litigations regarding the enforcement provisions. This is due to the fact that the withholding agent is made to bear the responsibility for failure of another party to comply with the tax laws in contradiction to common legal principles that punish people only for their failures. (Piracha & Moore, 2015)

Statements – Section 165

Section 165 requires every withholding agent to regularly submit reports to the tax department listing how much tax they deducted, from whom, and other required details. Since 2020, most agents have had to switch from filing these reports twice a year to filing them every month. A related rule (165A) also makes banks report bulk information about deposits and withdrawals. If an agent fails to file these reports, they get penalized under Section 182, and repeat offenders can end up on an official list of non-compliant agents maintained by FBR's dedicated Directorate General of Withholding Taxes. (Akhtar, Safdar, Baig, Ahmad, & Khan, Broadening of Tax Base in Pakistan: Legislative and Prospects, 2021)

Penalties and Default Surcharge

Section 182 prescribes penalties to the amount of the greater of Rs. 5,000 or 0.1% of the amount payable in taxes, per day that the report is not filed by an agent, which increases cumulatively for every day that it goes unfiled. Section 205 prescribes interest, referred to as a "default surcharge," to be paid on any tax that has not been collected and remitted on time, at the annual rate of KIBOR plus 3%, or any other rate that is set in the law for that period. (Ahmed & Mangla, Economic Challenges Facing Pakistan in the Regional and Global Environment, 2019)

Sections 161, 165, 182, and 205, together, ensure that a withholding agent making even a single mistake will incur four distinct penalties simultaneously, consisting of personal liability for payment of the taxes, compound interest thereon, fine for the late submission, and, in severe cases, even criminal prosecution for the same failure. This combination of penalties imposed upon a private individual performing an unpaid service for the benefit of the State and receiving no reward for this task, is precisely what is considered unjust. (Kleven & Waseem, 2011)

Claim of Withholding Tax

If any individual, Association or any company has paid Withholding Tax more than their actual tax liability they can claim return. As the Withholding Tax can be referred to Advance Tax or any sort of bills in shape of Income Tax. They can be refunded back at the end of the year by the government. As if certain conditions are fulfilled, the Withholding Tax can be claimed at the end of the year. Among the conditions to be eligible for refund claim, one must be a filer. (Khan S. A., 2011)

In case of salary persons and must fall into the Income Slot where there is no tax liability. The only way is to adjust the excess tax is to do so against the salary tax deductions. The core aim of government behind collecting Withholding Tax throughout the year and then providing the opportunity at the end to get refund is to make people filer and come under the scrutiny of Federal Board of Revenue. In case of refund amount, an online application can be filed on portal of FBR and it after scrutiny FBR finds the claim to be a legitimate one, the amount is refunded. If any person's falls under the Income slot exposed to tax and the income is properly declared in the Income Tax Return along with the Withholding Tax throughout the year, in this case the Withholding Tax will be adjusted in annual income tax return. (Ansari, 2025)

Refund Procedure

To get refund of withholding tax, it is necessary to keep track of all the bills and receipts throughout the year. To get the refund, the person has to fill the application available on the FBR portal and the evidence for deduction of Withholding tax are required. Once it is scrutinized by the concerned department, refund will be given to the person. (Mughal & Akram, Reasons of Tax Avoidance and Tax Evasion: Reflections from Pakistan, 2012)

Withholding Tax Contribution (2018 To 2025)

The Withholding Tax contributes a larger chunk in the Revenue of FBR on yearly basis. From 2018 to 2024 there is significant increase in Withholding Tax in Pakistan. The significant contribution of Withholding Tax since past years has reflected the continues reliance of government on this tool of collection of tax to strengthen fiscal stability. The following data sheds light on the significant contribution of Withholding Tax in each year. (FBR, Biannual/Quarterly Review, 2025)

Year	FBR Revenue	Revenue Generated	Growth
2019-2020	3,996.7 billion	1,091.5 billion	13.70%
2020-2021	4,734.2 billion	1,237.1 billion	13.30%
2021-2022	6,148.5 billion	1,534.4 billion	24.00%
2022-2023	7,164 billion	1,874.2 billion	32.20%
2023-2024	9,299.1 billion	2,740 billion	36.50%

Source: Compiled by the researcher.

Role of Filer, Non-Filer and Late Filer

The status of person's registration with Federal Board of Revenue has a significant impact on the Withholding taxes. The Federal Board of Revenue maintains a Active taxpayers list and the person or entity who has filed the Income Tax Return is included in Active Taxpayers List while the other one is considered as a non-Filer and if the Income Tax Return is filed after due date the person is known as a Late filer. non- filers have to pay comparatively double Withholding charges. For instance, if company has a filer status, the Withholding tax will be 9% and 18% in case of non-filer and in case of Individuals/AOP the filer has to pay 11% Withholding tax on services while the non-filer has to pay 22%. (Mudassir, 2024) Filing of Income Tax Return has become more under considerable with time. The person filing the Income Tax Return has to mention all the Withholding tax paid with respect to the different heads. As in last twenty years, the increase in Withholding Tax is evident. (BACC, 2026)

General Treatment with Withholding Tax

In Pakistan there are three ways to tackle the Withholding tax;

The Withholding Tax can be treated as a complete discharge for the Final Tax liability. This works in a way that there is no further tax liability left on the transaction. This is called Final Tax Regime. The deduction of Withholding Tax on the payment of divided is the example of this way of working. (FBR, The Directorate General of Withholding Taxes, 2025)

In second scenario, the Withholding Tax is adjusted at the end of the financial year. When the financial year end, the total income is calculated and the already paid tax is adjusted accordingly. This is known as Normal Tax Regime. For instance, when a person sale or purchases any property, tax is deducted and later on adjusted from the salary. (Pwc, 2026)

The third scenario, is referred as Minimum Tax Regime. In this case the tax deducted is treated as the minimum tax, no matter is the person has lower income. Means if the Withholding Tax being deducted is more than the tax liability calculated in normal manner, the already deducted Withholding tax is final. For instance, on commercial imports, tax is deducted before regardless of the profit they make as if they get less profit, still they have to pay the tax deducted at import. (Zafar, 2024)

Procedural, Administrative, and Financial Challenges Faced by Taxpayers under the Withholding Tax Regime

Procedural Challenges

Procedural challenges are those that arise from the legal processes through which withholding tax obligations are created, enforced, and disputed. They concern the fairness and adequacy of the procedures available to withholding agents and dedicatees, whether they are given adequate notice of their obligations, a genuine opportunity to be heard before adverse action is taken against them, and effective access to remedies when the law is misapplied. (ASB, 2025)

Complexity of Withholding Provisions

The most fundamental procedural challenge faced by withholding agents in Pakistan is the sheer number and complexity of the withholding tax provisions with which they must comply. As the Income Tax Ordinance, 2001 contains more than fifty distinct withholding tax provisions, spanning Sections 148 to 156G, the 231 series, the 233 series, and the 236 series. Each provision identifies a different category of payment, a different withholding agent, a different rate, and a different compliance deadline. The Finance Acts of 2019, 2020, 2021, 2022, 2023, 2024, and

2025 each introduced further amendments adding new provisions, revising rates, and expanding definitions often with limited transition time for withholding agents to adjust their compliance systems. (Taimur, 2025)

The legal consequence of this complexity is significant and directly documented in Pakistani litigation. A withholding agent who incorrectly classifies a payment — for example, treating a composite transaction as a payment for goods under Section 153(1)(a) rather than a payment for services under Section 153(1)(b) — deducts tax at the wrong rate and thereby exposes itself to full personal liability for the shortfall under Section 161(1), together with a default surcharge at the rate of KIBOR plus 3% per annum under Section 205. This liability arises not from any dishonest intent but from the genuine legal difficulty of correctly applying a complex statutory framework that has been amended more than twenty times since 2002. (Bhatty, 2020)

The withholding tax system in Pakistan has evolved into a fundamental legal issue. It not only imposes a heavy load on taxpayers but also weakens the Rule of Law by turning legal compliance into a task requiring specialized legal knowledge instead of being a standard civic duty. (ASB, 2025)

Unlawful Issuance of Notices Under Section 161

Section 161(1) of the Income Tax Ordinance, 2001 empowers the Commissioner to issue an order holding a withholding agent personally liable for tax not deducted or deposited. Section 161(1A) provides that no such recovery shall be made unless the withholding agent has been given an opportunity of being heard. These provisions create a clear two-stage procedural requirement: first, the Commissioner must establish that a specific default has occurred; second, the withholding agent must be given a genuine hearing before any recovery order is passed. (Mahboob, 2025)

During the research period of 2019 to 2025, the most persistently documented procedural challenge in Punjab's withholding tax jurisprudence is the practice of FBR field officers issuing Section 161 notices without first establishing any specific, documented instance of default — what the Lahore High Court has repeatedly described as 'fishing inquiries.' These notices are typically issued on the basis of a general comparison between the withholding agent's filed statement under Section 165 and some independently generated estimate of the agent's expected withholding liability, without identifying any specific payment on which tax was not deducted. This practice forces withholding agents to disprove a presumed default — a reversal of the burden of proof that has no statutory basis and directly violates the due process guarantee of Article 10-A of the Constitution. (Khan A. I., 2025)

Sui Northern Gas Pipelines Ltd. v. Deputy Commissioner Inland Revenue

The Lahore High Court held that Section 161 of the Income Tax Ordinance, 2001 can only be invoked where the Commissioner has incontrovertible evidence of an actual, specific failure to deduct or deposit withholding tax. The Department cannot issue notices under Sections 161 and 205 through generalized fishing inquiries without first establishing a specific documented instance of default. This principle establishing the right of withholding agents to be proceeded against only on the basis of specific evidence was consistently cited and applied before the Lahore High Court and ATIR throughout the 2019–2025 research period, yet field officers continued to issue blanket notices in disregard of this authoritative judicial pronouncement. (Sui Northern Gas Pipelines Ltd. v. Deputy Commissioner Inland Revenue, 2014)

The persistence of this practice despite clear judicial authority to the contrary is itself one of the most significant legal findings of this research. It illustrates the gap between the law as declared by the courts and the law as applied by the administration a gap that imposes a very real procedural burden on withholding agents, who must spend time and resources challenging unlawful notices before the Commissioner Appeals, the ATIR, and sometimes the Lahore High Court, even when the underlying legal position is well-settled in their favor.

Inadequacy of the Appeal Process

The procedural challenge of challenging wrongful withholding tax demands is compounded by the inadequacy of the appeal process available to taxpayers in Punjab. Under the Income Tax Ordinance, 2001, a taxpayer aggrieved by an order under Section 161 may appeal to the Commissioner Inland Revenue (Appeals) under Section 127, then to the Appellate Tribunal Inland Revenue under Section 131, and then on a question of law to the Lahore High Court under Section 133. In principle, this three-tier appeal structure provides adequate legal protection. (Global, 2024) In practice, however, the delays within this structure during the research period have been substantial with ATIR proceedings routinely taking two to four years to conclude and High Court references remaining pending for even longer periods. During this entire period, the withholding agent against whom a demand has been raised may be required to pay the disputed tax or provide security, imposing a significant financial burden even before the legal merits of the case are determined. (Khan M. Z., 2024)

Administrative Challenges

Administrative challenges are those that arise from the institutional design and operational practice of the FBR and its field formations in administering the withholding tax regime. They concern not the procedural rights of individual taxpayers but the systemic features of the administrative apparatus that make compliance difficult, inconsistent, and unpredictable.

Frequent Legislative Changes Through Finance Acts and SROs

One of the most serious administrative challenges faced by withholding agents during the research period is the frequency with which the withholding tax regime has been amended. Between 2019 and 2025, every annual Finance Act introduced changes to one or more withholding tax provisions revising rates, expanding definitions, inserting new provisions, or amending existing sub-sections. In addition to these annual Finance Act changes, the FBR issued numerous Statutory Regulatory Orders, circulars, and general orders throughout each fiscal year, further amending rates and procedures in real time. (Robert, 2026)

The impact of legislative instability on legal matters is considerable. Businesses acting as withholding agents are required to annually, and occasionally mid-year, revise their accounting and payroll systems to align with the most recent withholding rates and classifications. These modifications necessitated prompt updates to systems and communication with employees. Research by Waseem (2017) and Brockmeyer et al. (2024) highlights that such instability deters formal compliance and promotes informality, as businesses find it more cost-effective to remain outside the documented economy than to continually update their withholding systems. (Ahmed, Ashfaq, Ali, Nawaz, & Nasreen, 2024). The key amendments and administrative impacts of finance Acts from 2019 to 2025 are represented in the table below.

Finance Act	Key WHT Amendments	Administrative Impact
Finance Act, 2019	Higher non-filer rates across all major heads; expanded definition of 'prescribed person' under Section 153	Withholding agents required to verify ATL status of every payee before each payment
Finance Act, 2020	COVID-19 relief — reduced rates on certain heads; suspension of enhanced non-filer rates	Mid-year rate changes required immediate system updates with minimal notice
Finance Act, 2021	Section 236H expanded to wider range of goods; Section 100D builder tax regime introduced	Manufacturers and distributors acquired new WHT obligations requiring new compliance infrastructure
Finance Act, 2022	Section 7E introduced; Section 236C expanded; Section 153 rates revised; non-filer restrictions strengthened under Section 114B	Property-related WHT generated massive litigation; non-filer restrictions created compliance panic
Finance Act, 2023	Salary tax slabs revised upward; Section 151 rates increased; Section 231AB reintroduced cash withdrawal tax	Employers required to recalculate monthly salary deductions mid-year for all employees
Finance Act, 2024	Section 153 services rate increased from 11% to 15%; Section 149 slabs further revised; default surcharge increased to KIBOR+3%	Increased compliance cost for service sector withholding agents; penalty risk elevated
Finance Act, 2025	Section 153(2A) inserted — withholding on digital commerce payments; Section 165C inserted — quarterly digital statements; Section 149 slabs revised upward; Sections 236C and 236K amended following Section 7E invalidation	Digital commerce sector acquired new WHT obligations; employers required to recalculate salary deductions; property WHT framework overhauled to fill Section 7E revenue gap

Source: Compiled by the researcher with the assistance of AI

Filer and Non-Filer Distinction – BURDEN on WITHHOLDING AGENTS

A distinctive and administratively burdensome feature of Pakistan's withholding tax regime is the dual-rate structure that applies to virtually every withholding provision — with one rate for 'filers' appearing on the Active Taxpayers List and a significantly higher rate for 'non-filers.' This structure, progressively expanded since 2014 and extended to almost every major withholding head during the research period, requires the withholding agent to determine the ATL status of every payee before making each payment and applying the correct withholding rate accordingly. (Gangl, Kirchler, Lorenz, & Torgler, 2015)

This verification obligation places a real administrative burden on withholding agents. The FBR's online ATL portal accessible through the IRIS system does not always update in real time, meaning that a payee who has recently filed their return may not yet appear on the ATL at the moment the payment is made. If the withholding agent deducts at the non-filer rate when the payee is in fact a filer or vice versa it exposes itself to either a Section 161 demand or an adjustment dispute. (Tariq, Income Tax Planning: A Case Study of Tax Saving Instruments in Pakistan (Under Income Tax Ordinance 2001x`), 2020)

Digital Compliance Barriers

he FBR's IRIS online tax portal through which withholding tax statements under Section 165, income tax returns, and refund applications must be filed has been a persistent source of administrative difficulty for taxpayers during the research period. Despite significant investment in IRIS 2.0, launched in late 2023, and the subsequent IRIS-ADX upgrade, the system has experienced recurrent technical failures particularly during peak filing periods. (Khurram & Arshad, 2024)

The legal consequence of IRIS failures is particularly acute for withholding agents because Section 182(1)(d) of the Ordinance imposes a penalty of Rs. 2,500 per day for failure to file the withholding statement within the prescribed deadline, subject to a minimum of Rs. 10,000. Where a withholding agent is unable to file due to a system failure rather than any failure on their own part the statutory penalty still accrues unless the FBR exercises its administrative discretion to condone the delay. The FBR has issued circulars on several occasions extending filing deadlines due to system failures, but this relief has been ad hoc and inconsistent, leaving taxpayers uncertain about their legal position when the system fails near a filing deadline. (Shair, Tayyab, Nawaz, & Ahmed, 2023)

Inconsistent Enforcement by FBR Field Formations

The persistent problem of administrative nature in this regard during the research period has been the non-uniformity of enforcement by the FBR regional formations in the Punjab province. While there is a Lahore High Court interpretation of Section 161 which has laid down uniform standards regarding the issuance of withholding tax recovery notices, the field officers do not follow this jurisprudence in many cases, where they have continued to issue recovery notices without showing any defaults, disregard the six-year statute of limitations set out by the Supreme Court in 2025, and recover money under Section 205 on an inaccurate computation of the default surcharge. Such non-uniformity in enforcement has resulted in the legal liability of the withholding agent being dependent upon the Regional Tax Office as well as the specific officer dealing with the withholding agent's case, thus violating the Rule of Law principle of uniformity in enforcement as a core theoretical criterion of this study. (Tarar, 2017)

Financial Challenges

Financial challenges are those that impose direct monetary burdens on taxpayers and beyond the tax they are legally required to pay and that arise from the structural features of the withholding tax regime itself.

Excess Withholding and Delayed Refunds

One of the major problems in the withholding tax system in Pakistan and one of the most important in terms of its legal implications is the over-deduction of withholding taxes and delays in the refunds. The problem is due to the fact that the withholding tax system operates on a flat rate applied to all gross payments regardless of whether the individual has income or expenses or whether the actual tax liability is higher than the flat withholding tax rate. In situations where the flat withholding tax rate is higher than the actual tax rate, which happens very often to lower-income individuals and companies with low-profit margins, there is a right to receive the excess amount back after filing an income tax return. (Hanif, 2025)

According to Section 170 of the Income Tax Ordinance, 2001, taxpayers are legally entitled to receive a refund of excess tax within forty-five days after submitting their refund application to the Commissioner. However, during the research period, it has been observed that refund claims have experienced significant delays beyond this legal timeframe. Taxpayers and tax professionals in Punjab have reported that processing refund claims, especially those related to excess deductions under Section 151 on bank profits and Section 153 on business receipts, has taken anywhere from six months to several years. (Haque, 2026)

The impact on the finances of this delay is serious. If there has been a considerable amount of deduction of withholding tax out of the sale proceeds during the year in accordance with Section 153 and the business is due an overpayment, the retention of such funds by the state for any more time means that the business does not have the money that could be used by it in its business. It is not just an inconvenience to the company but it is also a violation of its rights as a citizen because it means retention of the taxpayer's property illegally by the State in disregard of the provisions of Article 23 of the Constitution of Pakistan 1973. (Aleem, 2026)

The Non-Filer Penalty as a Financial Burden

The system of withholding taxes in Pakistan, having the concept of dual rates for filers and non-filers, creates a huge burden on those taxpayers who, for some reason, have not found themselves on the list of active taxpayers. Thus, a non-filer who sells any property in the province of Punjab will be subject to a withholding rate of around double the withholding rate payable by a filer, that is, he will have two times fewer money from the sale of his property than a filer will have in the same situation. Also, a non-filer who receives profit from the bank according to Section 151 will pay withholding tax at the rate of 35%, while a filer – only 15%. (Penalty: non-filers)

The reliance on the filer/non-filer approach by the Pakistani authorities as the main tool for enforcing compliance resulted in an imposition of the burden of financial penalty of non-filer status on those who could not afford to have professional help in filing their income tax returns and sustaining the filer status due to lower incomes and small businesses who lack the help of professional tax advisers to maintain their status and enjoy lower rates of the withholding tax in comparison with taxpayers and companies from the upper classes of the economy. Thus, it imposes higher burdens on those who are less able to comply with this requirement. (ASB, 2025)

Concluding Remarks

As from the above discussion, it is clear that Withholding Taxes are the largest contributor in government's treasury. Collection of tax has always been a huge problem for government and Withholding Tax are no less than a blessing in disguise. On one side they are giving numerous benefits to government but on the other hand sincere and honest tax payers are bearing the burden of Withholding Taxes. It is necessary to have proper information regarding its working and its effect in order to claim refund. It is the largest contributor in tax regime so it cannot be eliminated but if government keeps on relying entirely on it will surely cause adverse impacts. In order to bring reforms in the Withholding tax Regime, it is necessary to first bring institutional changes to the Federal Board of Revenue. Such reforms should be introduced that increase the capabilities of Officials so that they became much more independent and capable to broaden the tax net.

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