CAF-6
Taxation
Past Papers and their Suggested Solution
2014-2019

Developed By:

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The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examination

2 September 2019
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Saeed, a citizen of Pakistan, was working on a foreign vessel belonging to Delta Shipping Company (DSL) based in Spain for the past three years. His monthly salary was USD 15,000 which was remitted to his Pakistani bank account through normal banking channel. The amount received during the tax year 20X9 was converted to Pak Rupees at an average exchange rate of USD 1 = PKR 131.

On 1 October 20X8, he resigned from DSL and joined Haris Pharma Limited (HPL) in Pakistan as a General Manager. He was offered following monthly salary and allowance in HPL:

	Rupees
Basic salary	600,000
Medical allowance	66,000

In addition to the above, he was also provided the following:

(i) Bonus equal to two monthly basic salaries. However, bonus amount was adjusted in proportion to the duration of his stay in the company. The bonus amount was paid to him on 5 July 20X9.

(ii) Two company maintained cars. Both cars were purchased on 1 October 20X8. The car costing Rs. 3,500,000 was used for official purposes whereas the car costing Rs. 1,900,000 was used for personal purposes.

(iii) Free lunch from the restaurant owned by one of HPL's directors. The fair market value of food provided to him during the year was Rs. 125,000.

(iv) A special allowance of Rs. 20,000 per month to meet expenses wholly and necessarily incurred in the performance of his official duties. Actual expenses incurred by him during the year were Rs. 150,000.

(v) Provident fund contribution of Rs. 60,000 per month. An equal amount per month was also contributed by Saeed to the fund.

Other information relevant to tax year 20X9 is as under:

(i) On 1 December 20X8, Saeed obtained a loan of Rs. 25 million from a scheduled bank at 15% mark-up per annum to acquire a residential house.

(ii) During the year, he received dividends of Rs. 575,000 from a listed company. The amount was net of withholding income tax at the rate of 15% and Zakat of Rs. 62,500 deducted under the Zakat and Usher Ordinance, 1980.

(iii) Withholding tax deducted by HPL from Saeed's salary during the tax year 20X9 amounted to Rs. 1,300,000.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute under the appropriate head of income, the total income, taxable income and net tax payable by or refundable to Saeed for the tax year 20X9. **(17)**

Q.2 (a) Explain the term 'Rent' with relation to 'Income from property'. **(02)**

(b) During the tax year 20X9, Amjad carried out the following transactions in respect of his properties:

(i) On 1 July 20X8, Amjad purchased a factory building in Sukkur along with the installed machinery at the price of Rs. 9 million and Rs. 3 million respectively. To manage the shortage of funds of Rs. 2,000,000, he borrowed the same on 1 July 20X8 from his friend Shamshad through a crossed cheque. The loan carries interest at the rate of 18% per annum.

On 1 January 20X9, he let out this building along with the machinery to Basit at a monthly rent of Rs. 500,000 payable in advance.

(ii) On 1 July 20X8, Amjad let out his residential property situated in DHA Karachi to Mirza Limited at a monthly rent of Rs. 300,000. Rent for the two years was received in advance on 1 August 20X8.

(iii) On 1 July 20X8, Amjad also entered into an agreement with Zeeshan for the sale of his plot situated in Quetta for Rs. 50 million. The plot had been purchased for Rs. 40 million in 20X4. Under the terms of sale agreement, he received Rs. 5 million at the time of signing the agreement and the balance was to be received on 30 September 20X8. However, due to financial difficulties, Zeeshan failed to pay the balance amount on the due date and consequently, Amjad forfeited the advance in accordance with the terms of the agreement.

On 10 April 20X9, he finally sold the plot to Jamshed for Rs. 65 million.

(iv) Following expenditures were incurred by Amjad in respect of his properties in Sukkur and Karachi:

Details of expenditures	**Property situated in**	
	Sukkur	**Karachi**
Repair & maintenance - building	270,000	70,000
- machinery	50,000	-
Ground rent	50,000	10,000
Insurance - building	150,000	20,000
Total	**520,000**	**100,000**

Required:
In view of the provisions of the Income Tax Ordinance, 2001 compute under appropriate head of income, taxable income of Amjad for the tax year 20X9. **(10)**

Q.3 Respond to the following independent scenarios, under the provisions of the Income Tax Ordinance, 2001:

(a) Jean Francois, a French designer, often visits to Pakistan for promotion of his products. During his last visit he stayed in Pakistan from 10 July 20X8 to 25 February 20X9. ***Determine the residential status of Jean Francois for tax year 20X9, assuming that the Commissioner has granted him permission to use calendar year as special tax year.*** **(02)**

(b) Haris sold two of his personal vehicles during the current year and earned profit of Rs. 550,000. ***Discuss the taxability of profit earned by Haris in the context of capital gain/loss.*** **(02)**

(c) Sikandar has revalued his factory building in accordance with International Financial Reporting Standards and consequently charged depreciation on the revalued amount. ***Explain the tax implication of the revaluation.*** **(02)**

(d) Shahbaz has acquired machinery for his new factory against a loan repayable in USD. ***Discuss what would be the cost of machinery for the purpose of depreciation deduction.*** **(02)**

(e) Farhan and Imran jointly own a building in Quetta. The building has been rented out to a company. ***Discuss the tax treatment of income from such property.*** **(02)**

Q.4 Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, briefly explain the following:

(a) Requirement of books of account to be maintained by a taxpayer who has business income upto Rs. 500,000. **(04)**
(b) General provisions/rules which may apply to income subject to Final Tax Regime. **(06)**
(c) Provisions regarding Special Audit Panel. **(05)**

Q.5 (a) Identify any **three** situations in which the fair market value of the assets shall be treated to be the cost of the asset. **(03)**

(b) During the tax year 20X9, Salman Shahid sold the following assets:

(i) A vehicle used by manager-in-charge of his garment factory for Rs. 2.8 million. The vehicle was purchased for Rs. 3.1 million in tax year 20X6. **(03)**

(ii) A machine for Rs. 350,000 on 1 June 20X9, which he had imported from Malaysia for Rs. 1,900,000 on 1 May 20X9, to start a new business. The machine was badly damaged during the shipment from Malaysia, rendering it unfit for use. He received insurance claim of Rs. 1,840,000 as damages on 15 May 20X9. Charges incurred in connection with the submission of claim with insurance company were Rs. 38,000. **(03)**

Required:
Under the provisions of the Income Tax Ordinance, 2001 compute under the appropriate head of income, the amount to be included in the taxable income of Salman Shahid for the tax year 20X9.

Q.6 (a) Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, briefly describe the treatment of the following:

(i) Recording of partial payments received in advance during a tax period in respect of both taxable and exempt supplies. **(02)**
(ii) Change in rate of tax during a tax period . **(04)**

(b) There are certain goods returned by the customer as they are unfit for consumption and the seller has no option but to destroy them.

Specify the procedure which must be followed by a registered person under the Sales Tax Rules, 2006 for the destruction of such goods. **(02)**

(c) Who is required to file the following sales tax returns? Also mention the due date of filing of these returns.

(i) Monthly return (ii) Special return
(iii) Final return (iv) Annual return **(04)**

Q.7 MH Associates (MHA) is registered under the Sales Tax Act, 1990 as a manufacturer, distributor and retailer. Following information has been provided by MHA for the month of August 20X9:

	Rupees
Supplies	
Taxable goods to registered persons	7,850,000
Taxable goods to unregistered persons	815,000
Exempt goods to unregistered persons	800,000
Purchases	
Taxable goods from registered persons	5,400,000
Exempt goods from registered persons	1,500,000
Taxable goods from unregistered persons	1,100,000

Additional information:

(i) Supplies of taxable goods to registered persons include an invoice erroneously issued to Rasheed for Rs. 270,000 whereas the correct amount of invoice was Rs. 720,000.

(ii) Supplies of taxable goods to unregistered persons include sale of Rs. 365,000 to end consumers.

(iii) Purchases from registered suppliers of taxable goods include:
- an amount of Rs. 1,800,000 paid for purchase of raw material. However, only 40% of the goods were supplied during August 20X9.
- goods worth Rs. 1,200,000 against which a discrepancy has been indicated by the CREST.

(iv) Two machines A and B costing Rs. 900,000 and Rs. 1,200,000 respectively were acquired and commissioned into operation on 15 August 20X9. Machine A has been used for taxable supplies only whereas Machine B has been used for exempt supplies only.

(v) Input tax amounting to Rs. 120,000 was paid on 15 March 20X9 but inadvertently it could not be claimed in the return for March 20X9 and thereafter.

(vi) An electricity bill of Rs. 670,000 was paid in cash which included sales tax amounting to Rs. 95,000.

(vii) Taxable supplies of Rs. 90,000 were returned by the registered customers during the period. Proper debit/credit notes were issued within the specified time.

(viii) Sales tax credit brought forward from previous month amounted to Rs. 255,000.

Except where otherwise specified, all figures are exclusive of sales tax. Rate of sales tax is **17%**.

Required:
In the light of the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by or refundable to MHA and input tax to be carry forward, if any, for tax period August 20X9. **(16)**

Q.8 (a) Briefly discuss **three** broad principles for levy of taxes. **(04)**

(b) Briefly explain any **three** indirect taxes applicable in Pakistan. **(05)**

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001

Tax Rate for Every Individual

S. No.	Taxable income	Rate of tax
1.	Where the taxable income does not exceed Rs. 400,000	0%
2.	Where the taxable income exceeds Rs. 400,000 but does not exceed Rs. 800,000	Rs. 1,000
3.	Where the taxable income exceeds Rs. 800,000 but does not exceed Rs. 1,200,000	Rs. 2,000
4.	Where the taxable income exceeds Rs. 1,200,000 but does not exceed Rs. 2,400,000	5% of the amount exceeding Rs. 1,200,000
5.	Where the taxable income exceeds Rs. 2,400,000 but does not exceed Rs. 4,800,000	Rs. 60,000 + 10% of the amount exceeding Rs. 2,400,000
6.	Where the taxable income exceeds Rs. 4,800,000	Rs. 300,000 + 15% of the amount exceeding Rs. 4,800,000

Depreciation Rates under Third Schedule

3.	Building (all types)	10%
4.	Plant and machinery, Vehicles (all types)	15%

Initial Allowance and First Year Allowance

The rate of initial allowance shall be 25% for plant and machinery and 15% for building.

Capital Gains on Disposal of Immovable Property

S. No.	Period	Rate of tax
6.	Where holding period of immovable property is up to three years	5%
7.	Where holding period of immovable property is more than three years	0%

Suggested Solution of September 2019 is still not Published By ICAP. It will be uploaded here, As soon as it is Published by ICAP.

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The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examination

4 March 2019
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 (a) Mustafa, Ali and Zain are partners of a resident firm in Pakistan, under the name and style MAZ Enterprises (MAZE) which is engaged in manufacturing and local supply of auto spare parts. All partners have equal share of profits and losses in the firm.

Following information has been extracted from accounting records of MAZE for the tax year 20X9:

	Rs. in '000
Sales	140,400
Cost of goods sold	(91,260)
Gross profit	49,140
Administrative and selling expenses	(21,430)
Financial charges	(15,740)
	(37,170)
Other income	1,900
Profit before tax	13,870

Additional information:

(i) The above accounts have been prepared on cash basis and stock-in-trade has been valued on the prime-cost method. However, the partners want to change the method of accounting from cash basis to accrual basis. In this respect, following information has been gathered:

	Opening balances	**Closing balances**
	--------- **Rs. in '000** ---------	
Stock-in-trade using prime-cost method	5,200	7,500
Stock-in-trade using absorption-cost method	5,900	8,800

(ii) Cost of goods sold includes cost of used machinery imported from China on 31 July 20X8 amounting to Rs. 2,110,000. The cost includes payment of custom duty of Rs. 90,000 and income tax of Rs. 110,000 to the Collector of Customs.

(iii) Administrative and selling expenses include:

- payment of Rs. 380,000 to a local hotel for holding annual eid-milan party for the employees, key customers and their families.
- payment of a fixed monthly remuneration of Rs. 150,000 to each partner.
- payment of Rs. 180,000 for purchase of accounting software on 1 January 20X9. The software is expected to be used for fifteen years.

(iv) Financial charges are net of interest income of Rs. 360,000 (net of tax @ 10% deducted by the bank), earned by the firm on its savings accounts.

Required:
Under the provisions of Income Tax Ordinance, 2001 and Rules made thereunder, compute the total income, taxable income and tax payable by MAZE using accrual basis of accounting. **(10)**

Note: ▪ ***Show all the relevant exemptions, exclusions and disallowances.***
▪ ***Tax rates are given on the last page.***

(b) Besides the share of income from MAZE, Zain has received the following amounts from his employment with Hasan Pakistan Limited (HPL) during the tax year 20X9:

(i) A monthly salary of Rs. 200,000.
(ii) Reimbursement of Rs. 350,000 for actual cost of medical services for him and his dependents, from an insurance company, under the health insurance policy.

On 31 March 20X9, he purchased a car from HPL for Rs. 110,800. The market value of this car on 31 March 20X9 was Rs. 250,000.

Required:
Compute the total income, taxable income and tax liability of Zain for the tax year 20X9. ***(Tax rates are given on the last page)*** **(07)**

Q.2 (a) Haider, a filer, was carrying on business as a cloth trader. On 28 October 20X7 there was a fire in his shop and the entire stock of clothes costing Rs. 1,550,000 was destroyed. The insurance company refused to pay the claim. Consequently, Haider ceased his business on 31 January 20X8.

After cessation of business, Haider filed an appeal against the insurance company and was able to recover Rs. 1,300,000 as full and final settlement from the insurance company in tax year 20X9.

Required:
Under the Income Tax Ordinance, 2001:

(i) state the requirements that Haider should comply with, on cessation of his business on 31 January 20X8. **(03)**
(ii) briefly discuss the treatment of the recovered amount in the tax year 20X9. **(02)**

(b) Mohsin has been working at the head office of Lewis Consulting, Inc. (LCI) situated in New York, USA. On 1 January 20X8, LCI had established its branch office in Pakistan and had sent Mohsin for two years as Country Manager for looking after the Pakistan operations.

During the tax year 20X9, apart from salary income, Mohsin earned/received the following amounts:

- On 15 December 20X8, he conducted a seminar in USA for a fee of USD 18,000. On his request, the event manager transferred the amount (net of tax) directly to his personal bank account in Islamabad on 10 January 20X9.
- On 31 May 20X9, he earned income from his business established in USA and brought 40% of the income to Pakistan.

Required:
Under the Income Tax Ordinance, 2001:

(i) state the residential status of Mohsin for the tax year 20X8. **(01)**
(ii) discuss the taxability of his foreign source incomes for the tax year 20X9. **(04)**

Q.3 (a) Imran, a resident person, is filing the return of his business income for the first time. He has been informed by his friend that he will also be required to file a wealth statement. In this respect, he seeks your advice about the particulars which he should disclose in his wealth statement. **(04)**

(b) Following transactions pertain to Salam Limited (SL) which took place during the tax year 20X9:

(i) A machine costing Rs. 1,800,000, being used in SL's Karachi factory was transferred to its subsidiary in Ghana. The fair market value and tax written down value of the machine on the date of transfer were Rs. 2,500,000 and Rs. 600,000 respectively. **(02)**

(ii) On 1 January 20X9, SL entered into a forward contract for the purchase of raw materials to be used in its business to guard against loss through price fluctuations. On the date of maturity of the forward contract, SL did not take the delivery of the raw materials but the contract was settled by making a payment of Rs. 500,000. **(03)**

Required:
Explain the taxability of the above transactions.

(c) On 1 July 20X8, Zahid rented out his properties as follows:

(i) An apartment was rented to Abdul Qadir at a monthly rent of Rs. 40,000. Zahid received a non-adjustable security deposit of Rs. 300,000 which was partly used to repay the non-adjustable security deposit amounting to Rs. 175,000 received from the previous tenant in July 20X3. He also spent Rs. 20,000 on repairs of the apartment in February 20X9.

(ii) A bungalow was rented to a bank. Zahid and his younger brother are joint owners of the bungalow in the ratio of 60:40 respectively. The annual rent agreed with the bank was Rs. 6,000,000 which is inclusive of Rs. 100,000 per month for utilities, cleaning and security. Zahid paid Rs. 35,000 per month for providing these services.

Required:
Under the provisions of Income Tax Ordinance, 2001 compute total and taxable income of Zahid for the tax year 20X9 under appropriate heads of income. **(07)**

Q.4 (a) Under the Income Tax Ordinance, 2001 identify **four** situations under which an appeal may be filed with the Commissioner (Appeals). **(04)**

(b) Sadiq Ali has received an ex-parte assessment order from the income tax department under which he is required to pay Rs. 5.2 million on account of tax not withheld from certain payments. He does not agree with the contention of the income tax department and would like to file an appeal to the Commissioner (Appeals).

Required:
State the procedure that he should follow for filing of appeal to the Commissioner (Appeals). **(03)**

(c) Abid is the legal representative of his grandfather since his death on 10 July 20X7 and manages his estate worth Rs. 28 million. On 22 January 20X9, he received a notice from the Income Tax Department requiring him to make payment of Rs. 0.8 million against his grandfather's income for the tax year 20X7. The notice also required him to submit details of his grandfather's income for the tax year 20X8.

Required:
Advise Abid about his obligations relating to the tax assessment proceedings pending/arising against his grandfather. **(05)**

Q.5 (a) Briefly discuss the difference between a public company and a private company, within the meaning of Income Tax Ordinance, 2001. **(04)**

(b) Certain types of payments by a private company to its shareholders can be treated as 'dividend' under the Income Tax Ordinance, 2001. State the conditions necessary for the application of this rule and the exceptions to such rule. **(05)**

Q.6 (a) Briefly discuss the situations under which the following are required to be registered under the Sales Tax Act, 1990 and Rules made thereunder:

(i) Cottage industry **(02)**
(ii) Retailer **(01)**

(b) Under the provisions of Sales Tax Act, 1990 and Rules made thereunder, identify the circumstances in which a registered person may be liable for deregistration. **(03)**

(c) Bashir (Private) Limited (BPL) was incorporated on 1 January 2019 and registered with sales tax department on 1 February 2019. BPL is in process of submitting its first sales tax return for the month ended 28 February 2019. The finance department has identified following transactions which took place before registration:

(i) Goods costing Rs. 5 million were purchased from a registered supplier. 80% of the goods remained unsold as at 1 February 2019. The supplier charged sales tax at the rate of 17%. **(03)**

(ii) Advance payment of Rs. 2.5 million was received on 15 January 2019 for the supply of taxable goods to a registered person. The goods were delivered in February 2019. **(02)**

Required:
Advise the finance department about the sales tax implications of the above transactions on BPL's first sales tax return.

Q.7 Following information has been extracted from the records of four registered persons for the month of February 2019:

	Registered Persons			
	A	**B**	**C**	**D**
	-------------------- Rupees --------------------			
Purchases				
Taxable supplies from registered persons	1,500,000	1,500,000	-	-
Taxable supplies from un-registered persons	-	-	1,500,000	1,500,000
Fixed assets (machinery) from a registered supplier	-	-	-	2,500,000
Supplies				
Taxable supplies to registered persons	1,200,000	-	1,000,000	1,000,000
Exempt supplies to registered persons	300,000	-	-	800,000
Taxable supplies to un-registered persons	-	-	800,000	-
Zero rated supplies	300,000	1,800,000	-	-

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of 17%.

Required:
In the light of the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by or refundable to each of the above registered persons and input tax to be carry forward, if any, for the tax period February 2019. **(15)**

Q.8 (a) National Finance Commission has the duty to make recommendations to the President with regard to finance related matters. You are required to list such recommendations. **(04)**

(b) State the taxes and duties which may be raised under the authority of Parliament. Also state **four** types of taxes which are covered:

(i) under the scope of legislation of the Federation
(ii) under the scope of legislation of the Provinces. **(06)**

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001

Tax Rate for Every Individual

S. No.	Taxable income	Rate of tax
1.	Where the taxable income does not exceed Rs. 400,000	0%
2.	Where the taxable income exceeds Rs. 400,000 but does not exceed Rs. 800,000	Rs. 1,000
3.	Where the taxable income exceeds Rs. 800,000 but does not exceed Rs. 1,200,000	Rs. 2,000
4.	Where the taxable income exceeds Rs. 1,200,000 but does not exceed Rs. 2,400,000	5% of the amount exceeding Rs. 1,200,000
5.	Where the taxable income exceeds Rs. 2,400,000 but does not exceed Rs. 4,800,000	Rs. 60,000 + 10% of the amount exceeding Rs. 2,400,000
6.	Where the taxable income exceeds Rs. 4,800,000	Rs. 300,000 + 15% of the amount exceeding Rs. 4,800,000

Tax Rate for Association of Persons

S. No.	Taxable income	Rate of tax
1.	Where the taxable income does not exceed Rs. 400,000	0%
2.	Where the tax able income exceeds Rs. 400,000 but does not exceed	5% of the amount exceeding Rs. 400,000
3.	Where the taxable income exceeds Rs. 1,200,000 but does not exceed Rs. 2,400,000	Rs. 40,000 + 10% of the amount exceeding Rs. 1,200,000
4.	Where the taxable income exceeds Rs. 2,400,000 but does not exceed Rs. 3,600,000	Rs. 160,000 + 15% of the amount exceeding Rs. 2,400,000
5.	Where the taxable income exceeds Rs. 3,600,000 but does not exceed Rs. 4,800,000	Rs. 340,000 + 20% of the amount exceeding Rs. 3,600,000
6.	Where the taxable income exceeds Rs. 4,800,000 but does not exceed Rs. 6,000,000	Rs. 580,000 + 25% of the amount exceeding Rs. 4,800,000
7.	Where the taxable income exceeds Rs. 6,000,000	Rs. 880,000 + 30% of the amount exceeding Rs. 6,000,000

Depreciation Rates under Third Schedule

3.	Plant and machinery	15%

Initial Allowance and First Year Allowance

The rate of initial allowance shall be 25% for plant and machinery.

Ans.1 (a)

MAZ Enterprises
Computation of total income, taxable income and net tax payable/refundable
For tax year 20X9

		Rupees
Profit before taxation (W-1)		15,170,000
Add: Inadmissible expenses/admissible income		
Cost of machinery included in the cost		2,110,000
Payment for holding annual eid-milan party		-
Remuneration to each partner (150,000×3×12)		5,400,000
Cost of accounting software		180,000
Interest income - separate block of income (360,000÷0.9)		400,000
		8,090,000
Less: Admissible expenses/inadmissible income		
Cost of machinery as per books	2,110,000	
Less: Income tax paid at import stage	(110,000)	
Depreciable value of machinery	2,000,000	
Depreciation - Initial allowance (2,000,000×25%)		500,000
- Normal [(2,000,000–500,000)×15%]		225,000
Amortization of the Computer software		
[From 1 January 20X9 to 30 June 20X9 (180,000/10×182/365)]		8,975
Increase in financial charges (To reserve the impact of netting off of interest income)		360,000
		1,093,975
Total income		**22,166,025**
Less: Interest income - separate block of income		(400,000)
Taxable income for the year		**21,766,025**
Tax liability		
Tax on 6,000,000		880,000
@ 30% on amount exceeding 6,000,000		4,729,807
Tax on interest income (10%)		40,000
		5,649,807
Less :Withholding tax on import of machinery		(110,000)
Less :Tax deducted by the bank		(40,000)
		5,499,807

W-1: Computation of profit under accrual basis of accounting	**Rupees**
Profit as given in the question - on cash basis	13,870,000
Adjustment on account of:	
- Closing Stock under Absorption Cost Method	8,800,000
- Closing Stock under Prime Cost Method	(7,500,000)
	1,300,000
Profit under accrual basis of accounting	**15,170,000**

(b) **MAZ Enterprises**
Computation of the taxable income of Zain
For tax year 20X9

	Rupees
Salary (200,000×12)	2,400,000
Reimbursement for actual cost of medical services	-
Purchase of car at less than market value (250,000 – 110,800)	139,200
Taxable income without share of AOP	2,539,200
Share of profit from AOP **(W-1)**	5,385,406
Taxable income including share of AOP	7,924,606
Tax liability for Zain	
Tax on Rs. 4,800,000	300,000
15% on amount exceeding Rs. 4,800,000	468,691
Tax liability	768,691
Tax rate to be charged (768,691÷7,924,606)	9.70%
Tax liability of Zain (2,539,200×9.70%)	**246,302**

W-1: Determination of Zain's share of profit from MAZE	**Rupees**
Partners divisible income (21,766,025–5,609,807)	16,156,218
1/3 share of Zain (5,385,406–1,800,000)	3,585,406
Monthly remuneration received from MAZE (150,000×12)	1,800,000
	5,385,406

Ans.2 (a) (i)

- Haider should give to the Commissioner a notice in writing regarding the discontinuance of business within fifteen days of the discontinuance i-e by 15 February 20X8.
- He is also required to furnish the return of income under the provisions of the ITO 2001 or on being required by the Commissioner by notice in writing.
- The return should cover the period commencing from 1 July 20X7 to 31 January 20X8.

(ii) Under the ITO-2001, if there is any income that has been derived by a person in a tax year from a business that has ceased before the commencement of that year and if that income would have been taxable had there been no cessation, then the provision of the tax statute would apply as if there was no cessation.

In the light of above provision, the receipt of Rs. 1,300,000 shall be included in his income from business for the tax year 20X9, provided that the write off has been claimed/allowed in the previous year(s).

(b) (i) Mohsin is not a resident individual as he spent less than 183 days in Pakistan during the tax year 20X8.

(ii) Under the ITO-2001 the foreign-source income of a short term resident individual shall be exempt from tax if he/she is:

- a resident individual solely by reason of the individual's employment; and
- present in Pakistan for a period or periods not exceeding three years.

However, the above rule is not applicable to any foreign-source income brought into or received in Pakistan.

Mohsin is a short term resident individual as he is in Pakistan for employment and his stay is less than three years. Based on the above rule:

- Receipt of US$ 18,000 in equivalent Pak Rupees for conduction the seminar session in USA shall be taxable as it has been received in Pakistan. However, he can claim the foreign tax credit of the amount paid as income tax in USA.
- 40% of his foreign source income which he brought into Pakistan is taxable whereas 60% of his foreign source income which he kept outside Pakistan is exempt from tax.

Ans.3 (a) Particulars to be disclosed in the wealth statement:

Imran would be required to disclose following particulars in his wealth statement:

- Total assets and liabilities as on 30 June;
- Total assets and liabilities of his spouse, minor children, and other dependents as on 30 June;
- Any assets transferred by him to any other person during the tax year 20X9 and the consideration for the transfer;
- Total expenditure incurred by him, his spouse, minor children and other dependents during the tax year and the details of such expenditure; and
- The wealth reconciliation statement.

(b) (i)

	Rs.in 000
Consideration received (equal to the cost of the asset)	1,800
WDV at the time of disposal	600
Gain on disposal	1,200

(ii) The forward contract entered into by SL for the purchase of raw materials is in the nature of a hedging contract which was entered into to guard against loss from future price fluctuations. Such contracts have specifically been excluded from the definition of speculative business. Therefore, Rs. 500,000 paid to settle the forward contract is an expenditure incurred in the normal course of business and is a deductible expenditure.

(c)

Income from property	**Rupees**
Rental income (40,000 × 12)	480,000
Rental income from joint property (4,800,000 **(W-1)** × 60%)	2,880,000
Less: Repair charges	-
Add: Un-adjustable security deposits (Rs. 212,500 **(W-2)** × 1/10)	21,250
	3,381,250
Income from other sources	
Income from utilites, cleaning and security [(1,200,000 – 420,000)×60%]	468,000
Total income	3,849,250
Less: Income from property – separate block of income	(3,381,750)
Taxable income	468,000

W-1: Determination of Income from joint property (bungalow)	**Rupees**
Total rental income	6,000,000
Less: Amount relating to utilities, cleaning and security	(1,200,000)
Income from property	4,800,000

W-2: Computation of unadjustable security deposit	**Rupees**
Received from new tenant	300,000
Less: Amount charged to tax in July 2013 to June 2018 (175,000 × 5/10)	(87,500)
	212,500

Ans.4 **(a)** An appeal may be filed with the Commissioner if a person is dissatisfied with the order passed as follows:

(i) A best judgment assessment (ex-parte assessment) based on any available information or material to the best of the Taxation Officer's / Commissioner's judgment.
(ii) An amendment of assessment issued by the Commissioner
(iii) An order holding an individual personally liable to pay the amount of tax, which was required to be collected or deducted by him/her or because of failure to pay the collected or deducted amount as required by the law.
(iv) An order declaring or treating a person as a representative of a non-resident person.

(b) Sadiq Ali shall file the appeal in the prescribed form, verified in the prescribed manner, be accompanied by the prescribed fee and shall precisely state the grounds upon which the appeal is made.

The appeal should be filed within 30 days of the service of intimation of the order. However, Commissioner (Appeals) may condone the delay in filing of an appeal upon application in writing by the appellant.

(c) As a legal representative, any proceedings pending against Abid's grandfather shall continue against Abid from the stage at which it stood on the date of his grandfather death. Further, any proceedings which could have been initiated against the deceased if he had survived, may now be initiated against Abid.

Abid is also liable for any tax, which would have been payable by his deceased grandfather. However, such liability is limited to the extent of Rs. 28 million i.e.

value of his deceased grandfather's estate.

Ans.5 **(a)** "Public Company" means

- a Company in which not less than fifty percent of the shares are held by the Federal Government or Provincial Government;
- a Company in which not less than fifty percent of the shares are held by a foreign Government, or a foreign Company owned by a foreign Government;
- a Company whose shares were traded on registered stock exchange in Pakistan at any time in the tax year and which remained listed on that exchange at the end of that year; or
- a unit trust whose units are widely available to the public and any other trust as defined in the Trusts Act, 1882 (II of 1882).

'Private company' means a company that is not a public company.

(b) The following type of payments made by a private company may be treated as "dividend" under the ITO 2001, to the extent to which the company possesses accumulated profits:

- payment by way of advance or loan to a shareholder, or
- any payment for the individual benefit of any shareholder

EXCEPTIONS:

- any distribution made to any shareholder in respect of liquidation or reduction in capital or redemption of debentures.
- any advance or loan made to a shareholder in the ordinary course of the business, where lending of money is a substantial part of the business of the company.
- any dividend paid which is set off by the company against any amount previously paid and treated as dividend to the extent to which it is set off.

Ans.6 **(a)** (i) Cottage industries are required to be registered when their:

- annual turnover from taxable supplies made in any tax period during the last twelve months ending any tax period does exceed Rs. 10 million or
- annual utility bills for the same period exceed Rs. 800,000.

(ii) Those retailers are required to register under the Sales Tax Act who are liable to pay sales tax except such retailers who are required to pay sales tax through their electricity bill.

(b) A registered person may be liable for deregistration due to any of the following reasons:

(i) He ceases to carry on his business;
(ii) His supplies become exempt from tax;
(iii) He transfers or sells his business;
(iv) Merger with another person; or
(v) Failure to file tax return for six consecutive months.

(c) (i) The tax paid on goods purchased by a person who is subsequently registered under this Act or the rules made thereunder, shall be treated as input tax, provided that such goods were purchased by him from a registered person against a tax invoice issued under section 23 during a period of thirty days before making the application for registration and constitute his verifiable unsold stock on the date of application for registration.

Considering the above, BPL can claim input tax subject to availability of tax invoice and verifiability of unsold stock.

(ii) Under the STA-1990, time of supply in relation to supply of goods means the time at which the goods are delivered or made available to the recipient of the supply or the time when any payment is received by the supplier in respect of that supply, whichever is earlier.

However, in respect of exempt supply , it shall be accounted for in the return for the tax period during which the exemption is withdrawn from such supply.

Considering the above, BPL has to include advance payment of Rs. 2.5 million received from a registered person in its sales tax return for the month ended February 2019.

Ans.7

	Taxable amount	Sales tax @ 17%
	-------- Rupees --------	
Registered person (A)		
Input tax		
Supplies from registered persons	1,500,000	255,000
Less: Inadmissible input tax/adjustable input tax (255,000×600,000/1,800,000)		(85,000)
Input tax for the month		170,000
Output tax		
Taxable supplies to registered persons	1,200,000	204,000
Exempt supplies to registered persons	300,000	-
Zero rate supplies	300,000	-
Output tax for the month		204,000
Admissible credit [Lower of 170,000 or 183,600 (90% of 204,000)]		170,000
Sales tax payable (204,000 – 170,000)		34,000
Sales tax refundable (300,000/1,800,000×255,000)		42,500
Registered person (B)		
Since all supplies are zero rated and all purchases are made from registered suppliers, the registered person can claim the refund of all input tax i.e. 255,000 (1,500,000×17%).		
Registered person (C)		
Input tax		
Supplies from un-registered persons	1,500,000	-
Output tax		
Taxable supplies to registered persons	1,000,000	170,000
Taxable supplies to un-registered persons	800,000	136,000
Output tax for the month		306,000
Further tax on supplies to unregistered persons (800,000×3%)		24,000
Sales tax payable [306,000+24,000]		330,000
Registered person (D)		
Input tax		

Supplies from un-registered persons	1,500,000	-
Fixed assets (machinery)	2,500,000	425,000
Inadmissible input tax (800,000÷1,800,000×425,000)		(188,889)
		236,111
Output tax		
Taxable supplies to registered persons	1,000,000	170,000
Taxable exempt supplies	800,000	-
Output tax for the month		170,000
Less: Input tax on fixed assets		(236,111)
Sales tax refundable/carry forward		66,111

Ans.8 **(a)** The duties of the National Finance Commission to make recommendations to the President with regard to finance related matters include:

(i) the distribution between the Federation and the Provinces of the net proceeds of the taxes.
(ii) the making of grants-in-aid by the Federal government to the Provincial Governments.
(iii) the exercise by the Federal Government and the Provincial Governments of the borrowing powers conferred by the Constitution;
(iv) any other matter relating to finance, referred to the Commission by the President.

(b) Following taxes may be raised under the authority of the Parliament:

(i) taxes on income, including corporation tax, but not including taxes on income consisting of remuneration paid out of the Federal Consolidated Fund;
(ii) taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed;
(iii) export duties on cotton, and such other export duties as may be specified by the President;
(iv) such excise duties as may be specified by the President; and
(v) such other taxes as may be specified by the President.

(i) Taxes which can be imposed by the Federation:
Following are the types of taxes which can be imposed by the Federation as provided in the Federal legislative list under the Constitution of Pakistan:

- Duties of customs, including export duties.
- Duties of excise, including salt, but not including alcoholic liquors, opium or other narcotics;
- Taxes on income other than agricultural income;
- Taxes on corporations.

(ii) Taxes which can be imposed by the Provinces:
Following taxes are covered in the scope of legislation of Provinces:

- Agriculture income tax
- Sales tax on services
- Taxes on transfer of immoveable property
- Professional tax

(The End)

The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examination

3 September 2018
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Ahmer Ghazi has been working as director production in Delta Pakistan Limited (DPL) for last three years. He received following monthly emoluments from DPL during the year ended 30 June 20X8:

	Rupees
Basic salary	650,000
House rent allowance	95,000
Medical allowance	70,000

In addition to the above, the employer also provided following to Ahmer Ghazi:

(i) Health insurance for him and his family members. The amount of annual premium paid by DPL was Rs. 50,000.
(ii) Return air ticket for Dubai worth Rs. 180,000 for him and his family as a reward for achieving the production target.
(iii) Loan of Rs. 5 million was given to him on 1 August 20X7 at 6% per annum.
(iv) Withholding tax of Rs. 1,500,000 deducted from his salary was reimbursed to him.

Other information relevant to the tax year 20X8 is as under:

(i) Under an employee share scheme 10,000 shares of DPL were allotted to Ahmer Ghazi on 1 January 20X6. According to the scheme, he was not allowed to sell/transfer the shares up to 31 December 20X6. On 1 April 20X8, he sold 6,000 shares of DPL for Rs. 33 per share. The face value of each share is Rs. 10. Fair market values of each share on different dates were as follows:

- Rs. 20 per share on 1 January 20X6
- Rs. 23 per share on 1 January 20X7
- Rs. 29 per share on 30 June 20X8

(ii) On 30 October 20X7 Ahmer Ghazi let out his apartment at a monthly rent of Rs. 30,000 to his friend. The fair market rent of the apartment is Rs. 40,000 per month.
(iii) He is a part time singer and earned Rs. 225,000 by allowing a private TV channel to use his song in a TV drama.
(iv) He purchased Sukuks of a listed company amounting to Rs. 1,400,000 as an original allottee, on 30 June 20X8.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the following for the year ended 30 June 20X8:

(a) Total income **(10)**
(b) Taxable income **(01)**
(c) Net tax payable or refundable **(05)**

Note:
- ***Ignore minimum tax under section 113.***
- ***Show all the relevant exemptions, exclusions and disallowances.***
- ***Tax rates are given on the last page.***

Q.2 Kaleem Limited (KL) is a listed company and its accounting year ends on 30 June. KL is now considering to change its accounting year from 30 June to 30 September.

Under the provisions of the Income Tax Ordinance, 2001:

(a) briefly describe normal , special and transitional tax year. **(06)**

(b) state the requirements regarding change in tax year from normal to special. **(02)**

(c) state the tax year corresponding to the income year ended 30 September 20X8 and the due date for filing the return of income. **(02)**

Q.3 (a) Hirani & Company (HC), a resident AOP, is engaged in the manufacturing of various consumer products and is assessed under normal tax regime. During the year ended 30 June 20X8, HC's sales was Rs. 14,000,000. It includes sales tax of Rs. 1,000,000 and excise duty of Rs. 500,000. The taxable income for the year is Rs. 1,170,000.

Compute HC's tax liability for tax year 20X8, under the provisions of the Income Tax Ordinance, 2001. ***(Tax rates are given on the last page)*** **(03)**

(b) The accounting profit before tax of Bashir Associates (BA) for the year ended 30 June 20X8 is Rs. 1,200,000.

Last year, BA had written off balances outstanding from two of its debtors namely Pulse International (PI) and Hussain Global (HG) which were partly allowed by the tax authorities. Details are as follows:

	PI	**HG**
	--------- Rupees ---------	
Amounts written off	1,150,000	925,000
Allowed by tax authorities	825,000	240,000

During the current tax year, BA received Rs. 652,000 from PI and Rs. 346,000 from HG, in full settlement of their debts.

In the light of the Income Tax Ordinance, 2001 compute BA's taxable income for the tax year 20X8. **(05)**

(c) Jamil and Company (JC) is the sole trader of a branded tea in Pakistan. In addition to the trading business, JC is also engaged in forward purchasing and selling of tea to reap the benefits of price fluctuation in local and international markets. Following information has been extracted from the records of JC for the year ended 30 June 20X8:

(i) Detail of trading and speculation businesses (forward purchase and sale) were as follows:

	Trading business	**Speculation business**
	------ Rs. in million ------	
Gross revenue	400	200
Gross profit	20	10

(ii) Total administrative and general expenses for the year amounted to Rs. 7.2 million. This amount includes a penalty of Rs. 0.4 million paid to the custom authorities.

(iii) Assessed carried forward losses from previous years are as follows:

	Rs. in million
Losses from trading business	12.8
Losses from speculation business	9.6
Capital losses (incurred in 20X2)	2.0

Under the Income Tax Ordinance, 2001 and Rules made thereunder, compute JC's taxable income / (loss) and the amount of loss to be carried forward, if any, for the tax year 20X8. **(06)**

Q.4 (a) On 25 August 20X8, the Officer of Inland Revenue has issued a notice to Rahat Foods (Private) Limited (RFPL) to deposit withholding income tax of Rs. 1,950,000 in respect of loan amounting to Rs. 13,000,000 given to Nadeem Ahmad, a shareholder of RFPL, by treating the amount of loan as dividend. The notice was served to the company on 30 August 20X8.

According to RFPL's records, the loan was given to Nadeem Ahmad on 25 May 20X7 when accumulated profit of the company was Rs. 12,000,000.

In the light of the provisions of the Income Tax Ordinance, 2001 explain whether you agree with the notice issued to RFPL by the Officer of Inland Revenue. **(03)**

(b) Specify the circumstances under which the Commissioner of Income Tax has powers to issue notice demanding a return of income from certain person(s) for a period of less than twelve months. Also state the powers of the Commissioner if such person fails to furnish the return as required, within the specified time. **(06)**

Q.5 Saleem is a resident taxpayer and runs a fitness centre in DHA Karachi. He files his return of income regularly. Following information pertains to his business for the tax year 20X8:

(i) Accounting profit before tax amounted to Rs. 2,350,000.

(ii) Administrative expenses include annual rent of the premises used for fitness centre amounting to Rs. 1,560,000. Withholding tax of Rs. 144,000 was deducted from the rent payment but was not deposited in the government treasury.

(iii) A passenger transport vehicle used for pick and drop of employees of fitness centre was disposed of for Rs. 3,500,000. The vehicle was purchased for Rs. 4,500,000 in tax year 20X7. No accounting depreciation was provided during the year 20X8. Accounting gain of Rs. 200,000 has been recorded in the profit or loss account.

(iv) On 1 July 20X7, a car was acquired on finance lease for Rs. 3,000,000. Advance tax paid at the time of acquisition and registration of vehicle aggregated Rs. 85,000. The vehicle has been used 70% for business purposes and 30% for Saleem's personal use.

Accounting depreciation of Rs. 600,000 and financial charges of Rs. 462,000 were recorded in the profit or loss account. Lease rentals paid during the year amounted to Rs. 857,000.

(v) During the year, Saleem recorded gain of Rs. 50,000 on disposal of shares. Details are as under:

Name of investee company	Sold on	Purchased on	Gain/(loss) on disposal (Rs.)
Sun (Private) Limited	1 Aug 20X7	1 Sep 20X3	500,000
Moon Limited - a listed company	15 Sep 20X7	1 Jan 20X5	(700,000)
Planet Limited - a listed company	1 Feb 20X8	1 Jan 20X6	250,000
			50,000

Required:
Compute Saleem's taxable income under appropriate head of income and tax liability for the tax year 20X8. ***(Tax rates are given on the last page)*** **(12)**

Q.6 (a) Under the Sales Tax Act, 1990 and Rules made thereunder, briefly describe:

(i) temporary sales tax registration and rights, obligations and responsibilities of a person holding temporary registration. **(05)**

(ii) differences between rules applicable to exempt and zero rated supplies. **(04)**

(iii) the provisions related to excess/additional amount of sales tax collected by a registered person. **(03)**

(b) Where a Commissioner of Inland Revenue, having jurisdiction, is satisfied that a registered person has issued fake invoices, evaded tax or committed tax fraud, he may suspend the registration of such person without prior notice, pending further inquiry.

Under the Sales Tax Act, 1990 and Rules made thereunder, state any ***four*** basis of such satisfaction which allow the Commissioner to suspend the registration as described above. **(03)**

Q.7 (a) Briefly explain indirect taxes applicable in Pakistan. **(04)**

(b) State **one** objective of tax laws in each of the following cases:

(i) High tax rate on high income
(ii) Higher taxes on import of luxury goods
(iii) Tax credit on donations to approved institutions
(iv) Tax credit on investments
(v) Creation of tax free zones
(vi) Tax on income of individuals and companies
(vii) Tax on transactions not made through normal banking channel
(viii) Zero rating under the Sales Tax Act, 1990 **(06)**

Q.8 Abid Khan is registered for sales tax purposes and is engaged in the manufacturing of electrical appliances in Multan. His sales and purchases for the month of August 20X8 are summarized below:

	Rupees
Supplies	
Taxable goods to registered customers	15,118,000
Taxable goods to un-registered customers	10,150,000
Exports	5,000,000
Exempt supplies	4,500,000
Purchases	
Taxable goods from registered suppliers - for taxable supplies	25,000,000
- for exempt supplies	1,500,000
Packing materials from un-registered suppliers	9,500,000

Additional information:

(i) Supplies of taxable goods to registered customers include:
- an amount of Rs. 4,225,000 against sale of electric toasters at a trade discount of 35%. As per normal business practice, he allows a discount of 10% only.
- goods supplied against which advance payment of Rs. 2,500,000 had been received in June 20X8.

(ii) Taxable supplies returned by different registered customers amounted to Rs. 900,000. Proper debit and credit notes were raised within the specified time.
(iii) A plant costing Rs. 2,700,000 was commissioned into operation on 15 August 20X8. The plant is being used for taxable supplies only.
(iv) An electricity bill of Rs. 2,600,000 was paid in cash which includes sales tax amounting to Rs. 350,000.
(v) Input tax brought forward from July 20X8 is Rs. 595,000.

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of 17%.

Required:
Compute sales tax payable by or refundable to Abid Khan along with input tax to be carried forward/refundable, if any, in the sales tax return for the month of August 20X8.
Note : Show all relevant exemptions, exclusions and disallowances. **(14)**

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001

Rates of Tax for Salaried Individuals

S. No.	Taxable income	Rate of tax
10.	Where the taxable income exceeds Rs. 3,500,000 but does not exceed Rs. 4,000,000	Rs. 472,000 + 25% of the amount exceeding Rs. 3,500,000
11.	Where the taxable income exceeds Rs. 4,000,000 but does not exceed Rs. 7,000,000	Rs. 597,000 + 27.5% of the amount exceeding Rs. 4,000,000
12.	Where the taxable income exceeds Rs. 7,000,000	Rs. 1,422,000 + 30% of the amount exceeding Rs. 7,000,000

Tax Rates for Every Individual and Association of Person Except for Salaried Taxpayer

S. No.	Taxable income	Rate of tax
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,500,000	Rs. 32,000 + 15% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 144,500 + 20% of the amount exceeding Rs. 1,500,000
6.	Exceeds Rs. 2,500,000 but does not exceed Rs. 4,000,000	Rs. 344,500 + 25% of the amount exceeding Rs. 2,500,000
7.	Exceeds Rs. 4,000,000 but does not exceed Rs. 6,000,000	Rs. 719,500 + 30% of the amount exceeding Rs. 4,000,000
8.	Exceeds Rs. 6,000,000	Rs. 1,319,500 + 35% of the amount exceeding Rs. 6,000,000

Tax Rates for Income from Property

S. No.	Taxable income	Rate of tax
1.	Where the gross amount of rent does not exceed Rs. 200,000.	Nil
2.	Where the gross amount of rent exceeds Rs. 200,000 but does not exceed Rs. 600,000.	5% of the gross amount exceeding Rs. 200,000.
3.	Where the gross amount of rent exceeds Rs. 600,000 but does not exceed Rs. 1,000,000.	Rs. 20,000 plus 10% of the gross amount exceeding Rs. 600,000.
4.	Where the gross amount of rent exceeds Rs. 1,000,000 but does not exceed Rs. 2,000,000.	Rs. 60,000 plus 15% of the gross amount exceeding Rs. 1,000,000.
5.	Where the gross amount of rent exceeds Rs. 2,000,000.	Rs. 210,000 plus 20% of the gross amount exceeding Rs. 2,000,000.

Tax Rates for Capital Gains on Disposal of Listed Securities

S. No.	Period	Tax year 20X5	Tax year 20X6	Tax year 20X7	Tax year 20X8
3.	Where holding period of a security is twelve months or more but less than twenty-four months.	10%	12.5%	12.5%	12.5%
4.	Where holding period of a security is twenty-four months or more but the security was acquired on or after 1st July 20X3.	0%	7.5%	7.5%	7.5%

Minimum tax under section 113

S. No.	Person(s)	Minimum Tax as percentage of the person's turnover for the year
3.	In all other cases.	1.25%

Depreciation Rates Under Third Schedule

3.	Motor vehicles (all types)	15%

Note:
The suggested answers are provided for the guidance of the students. However, there are alternative solution(s) to the questions which are also considered by the Examination Department while marking the answer scripts.

Ans.1

Mr. Ahmer Ghazi
Computation of income tax liability
For the tax year 2017

	Rupees
Income from Salary	
Basic Salary (650,000×12)	7,800,000
House rent Allowance (95,000×12)	1,140,000
Medical allowance (70,000×12)	840,000
Health insurance	-
Award for meeting sales target	180,000
Grant of concessional loan by DPL [Rs. 5 million @ 4% (10–6)]	*183,334
Tax of Ghazi paid by DPL	1,500,000
	11,643,334
Income from property	
Rent of apartment (40,000×8)	320,000
Income from capital gain	
Sale of 6,000 shares @ Rs.33–23 =10	60,000
Income from other sources	
Amount received for his song (Royalty)	225,000
Total income for the year from all sources	12,188,334
Less: Separate block of income	
Property income	320,000
Capital gain	60,000
	380,000
Taxable income under NTR	11,808,334
Tax liability under	
Normal tax regime	
on 7,000,000	1,422,000
exceeding 7,000,000 at the rate of 30%	1,442,500
	2,864,500
Separate block – Income	
Property income tax @ 5%	6,000
Capital gain tax @ 7.5%	4,500
Total tax payable	2,875,000
Less: Tax credit for investment in Sukuks (2,864,500/11,808,334×1,400,000)	(339,616)
	2,535,271
Less: Tax paid by DPL	(1,500,000)
Income tax payable	1,035,271

Ans.2 (a) Normal tax year

Normal tax year is a period of twelve months ending on the 30th day of June and is denoted by the calendar year in which the said date falls.

Special tax year

Where a person's income year is different from the normal tax year, or where, by an order, a person has been allowed by the Commissioner to use a twelve months' period different from normal tax year, such income year or such period shall be that person's special tax year and shall be denoted by the calendar year relevant to the normal tax year in which the closing date of the special tax year falls.

Transitional tax year

Where the tax year of a person changes as a result of an order by the Commissioner of Income tax either from the normal tax year to special tax year or vice versa, the period between the end of the last tax year prior to change and the date on which the changed tax year commences shall be treated as transitional tax year. (Also called separate tax year)

(b) Change of tax year from normal to special

- A person shall apply in writing to the Commissioner for change in tax year from normal to special.
- The Commissioner should grant permission only if he is satisfied that the company has a compelling need to use special tax year.
- While giving the permission, the Commissioner may impose such conditions as he may deem fit.

(c)
- Tax year is 20X9.
- Due date for filing of return is 30 September 20X9.

Ans.3 (a)

		Rupees
Income tax payable under normal tax regime		
Taxable income	**A**	1,170,000
Income tax (Rs. 32,000 + 15% of 420,000)		95,000
Income Tax payable under minimum tax regime		
Gross sales (14,000,000–1,000,000–500,000)		12,500,000
Turnover tax u/s 113 @ 1.25% on Rs. 12,500,000	**B**	156,250
Tax liability of HC (higher of **A** and **B**)		156,250

(b)

	Rupees
Accounting profit before adjustments	1,200,000
Less: Amount received from Pulse International	(652,000)
Less: Amount received from Hussain Global	(346,000)
Bad debts amount previously allowed but recovered by PI	327,000
Bad debts short allowed	(339,000)
Taxable income	190,000

	Pulse International (PI)
Amount received	652,000
Bad debts claimed	1,150,000
Less: Bad debts allowed as deduction	825,000
	325,000
Excess income to be added in the income for the tax year 2018	327,000

	Hussain Global (HG)
Amount received	346,000
Bad debts claimed	925,000
Less: Bad debts allowed as deduction	240,000
	685,000
Amount short received to be allowed as deduction for the TY 20X8	(339,000)

(c)

Particulars	**Trading business**	**Speculation business**	**Total**
	-------- **Rs. in million** --------		
Gross revenue	400.00	200.00	600.00
Gross profit	20.00	10.00	30.00
Administrative and general expenses [7.2m–0.4m×400m÷600m]	4.53	2.27	6.80
Net income	15.47	7.73	22.80
brought forward losses	12.80	9.60	
Taxable income/(loss) carried forward for the year	2.67	*(1.87)	

****Loss carried forward to next year***

Capital loss of Rs. 2 million cannot be carried forward to next year as the period of six years lapsed in tax year 20X8.

Ans.4 (a) Under the Income Tax Ordinance, 2001 the definition of dividend includes any payment by a private company by way of advance or loan to a shareholder or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company, possesses accumulated profit.

Considering the above definition of dividend, the tax officer is correct to the extent of treating the loan payment as dividend. However, he made error in treating the entire amount of Rs. 13 million as dividend because the amount of accumulated profit was Rs. 12 million on that date. Therefore, only Rs. 12 million can be treated as dividend.

(b) The Commissioner may, by notice in writing, require the following persons or their representatives to furnish a return of income for a period of less than twelve months:

- a person who has died;
- a person who has become bankrupt or gone into liquidation;
- a person who is about to leave Pakistan permanently;
- where the Commissioner otherwise considers it appropriate to require such a return to be furnished.

If a person fails to furnish the return, the Commissioner may, based on any available information or material and to the best of his judgment, make an assessment of the taxable income of the person and the tax due thereon. Under such a case, the assessment, if any, treated to have been made on the basis of return or revised return filed by the taxpayer shall be of no legal effect.

Ans.5 Saleem
Computation of taxable income for the year 20X8

	Rupees
Income from business	
Accounting profit before adjustment	2,350,000
Add: Inadmissible expenses/admissible income	
Rental charges - withholding tax deducted but not deposited	1,560,000
Depreciation on leased assets	600,000
Financial charges on leased assets	462,000
	2,622,000
	4,972,000
Less: Admissible expenses/inadmissible income	
Accounting profit on sale of vehicle	200,000
Lease rental (857,000×70%)	599,900
Accounting gain on the sale of shares	50,000
Loss on disposal of a passenger transport vehicle **(Note 1)**	180,556
	1,030,456
	3,941,544
Income from capital gain	
Gain on the sale of share of Sun (Private) Limited (Holding period is more than 12 months and therefore only 3/4 is taxable 500,000×3/4)	375,000
Gain on the sale of securities	
Moon Limited	(700,000)
Planet Limited	250,000
	(450,000)
Total income	3,866,544
Add: Loss on sale of shares of listed companies - Separate block of income	450,000
Taxable income under NTR	4,316,544
Computation of tax liability	
Tax on 4,000,000	719,500
Tax on income exceeding 4,000,000 @ 30% (316,544×30%)	94,963
Tax payable under NTR	814,463
Advance tax collected at the time of vehicle purchased	(85,000)
Income tax payable	729,463

Note 1: Loss on disposal of a passenger transport vehicle

Consideration received on disposal of passenger transport vehicle not plying for hire A×B/C Where (3.5×2.5/4.5) *(A is the amount received on disposal of the vehicle Rs. 3.50 million; B is the amount referred to in clause (a) of sub-section (13) Rs. 2.5 million; and C is the actual cost of acquiring the vehicle Rs. 4.5 million.)*	1,944,444
Written down value of vehicle (2.5×85%)	(2,125,000)
Loss on disposal	(180,556)

Ans.6 (a) (i) Where a person files application for sales tax registration as a manufacturer prior to installation of machinery, for the purpose of import of machinery to be installed by him, temporary registration as manufacturer shall be allowed to him for a period of sixty days.

After receiving temporary registration, the person shall be allowed to import plant, machinery and raw materials, etc. as a manufacturer, subject to submission to the customs authorities of a post-dated cheque equal to the difference in duties and taxes to be availed as a manufacturer.

In case the list of machinery is not provided within sixty days of issuance of the temporary registration, such temporary registration shall be disabled and the post-dated cheques submitted shall be encashed.

A person holding temporary registration shall file monthly return, but shall not issue a sales tax invoice and if such invoice is issued, no input tax credit shall be admissible against such invoice.

No sales tax refund shall be paid to the person during the period of temporary registration, however, the amount of input tax may be carried forward to his returns for subsequent tax periods.

(ii) Features distinguishing the concept of 'Zero rating' from 'Exempt supply':

Distinction points	Zero Rated Supply	Exempt Supply
Taxability	Zero rated supply is charged to tax at the rate of zero per cent.	Exempt Supply means a supply which is exempt from tax.
Products covered	Goods exported as notified by FBR or listed in the Fifth Schedule are charged to sales tax at the rate of zero per cent.	Goods specified by Federal Government and FBR and goods listed in Sixth Schedule are exempt supplies.
Invoicing Sales Tax Requirements	Invoice has to be raised for the goods supplied	No sales tax invoice shall be raised.
Registration	A person engaged in zero rated supplies has to be registered with the Sales tax department.	A person engaged exclusively in supply of exempt goods is not liable to be registered.
Input tax credit	Input tax paid related to zero rated supplies is refundable.	Input tax paid related to exempt supplies is inadmissible, therefore, it is neither adjustable nor refundable.

(iii) Collection of excess sales tax

- Any person who has collected or collects any tax or charge which was not payable as tax or charge or which is in excess of the tax or charge actually payable and the incidence of which has been passed on to the consumer, shall pay the amount of tax or charge so collected to the Federal Government.
- Any amount payable to the Federal Government shall be deemed to be an arrear of tax or charge payable under this Act and shall be recoverable accordingly and no claim for refund in respect of such amount shall be admissible.

- The burden of proof that the incidence of tax or charge has been or has not been passed to the consumer shall be on the person collecting the tax or charge.

(b) The basis for such satisfaction may inter alia include the following:

(i) non-availability of the registered person at the given address;
(ii) refusal to allow access to business premises or refusal to furnish records to an authorized Inland Revenue Officer;
(iii) abnormal tax profile, such as taking excessive input tax adjustments, continuous carry-forwards, or sudden increase in turnover;
(iv) making substantial purchases from or making supplies to other blacklisted or suspended person;
(v) non-filing of sales tax returns;
(vi) on recommendation of a commissioner of any other jurisdiction;
(vii) any other reason to be specified by the Commissioner;

Ans.7 (a) Following are the indirect taxes under the Pakistani Taxation System.

(i) **Custom Duty**
Goods imported and exported from Pakistan are liable to custom duties as prescribed in Pakistan Custom Tariff.

(ii) **Federal Excise Duty**
Generally, federal excise duty is charged on the basis of excise value or retail price. However, some items are chargeable to duty on the basis of weight or quantity. All exports are liable to Zero per cent Federal Excise Duty.

(iii) **Sales Tax**
Sales tax is levied on

- Import of goods into Pakistan, payable by the importers;
- Taxable supplies made in Pakistan by a registered person in the course of furtherance of any business carried on by him;

A registered person can make adjustment of tax paid at earlier stages against the tax payable by him on his supplies. For most of the goods sales tax is payable @ 17%.

(b) Objectives of tax laws in each case are specified below:

(i) Fair distribution of wealth
(ii) Reduction in imports of unnecessary goods and balance of trade.
(iii) To promote culture of payment of donation to only organised and regulated institutions
(iv) Promote investment in listed companies
(v) To give incentives to underdeveloped areas.
(vi) Revenue collection
(vii) Documentation of economy
(viii) Promotion of Exports

Ans.8

Mr. Khan
Computation of sales Tax payable / Refundable
For the tax period August 20X8

	Taxable Value	Sales Tax Rate	Sales Tax
	---------------- Rupees ----------------		
Sales tax credits - input tax			
Purchases from registered suppliers	25,000,000		4,250,000
Purchases from unregistered suppliers - packing material	9,500,000	inadmissible	-
Purchases goods used exclusively for making exempt supplies	1,500,000	inadmissible	-
Cash payment of electricity bill inclusive of sales tax	-		350,000
Fixed assets (Machinery)	2,700,000		459,000
Total input tax	38,700,000		5,059,000
Less: Inadmissible/unadjusted input tax **(Note 1)**			(887,762)
Input tax for the month			4,171,145
Add: Input tax brought forward from previous month			595,000
Accumulated credit			4,766,238
Sales tax debits - output tax			
Local taxable supplies - registered suppliers (15,118,000–4,225,000–2,500,000)	8,393,000		1,426,810
Local taxable supplies - registered suppliers (4,225,000×0.9÷0.65)	5,850,000		994,500
- unregistered persons	10,150,000		1,725,500
	24,393,000		-
Export (zero rated)	5,000,000		-
Exempt supplies (Rs. 4,500,000)	-		-
Output tax for the month	29,393,000		4,146,810
Less: Sales return - taxable supplies	(900,000)		(153,000)
Total supplies / Output tax for the month	28,493,000		3,993,810
Admissible credit (90% of output tax i.e. Rs. 3,594,429 (3,993,810 ×0.9) or input tax excluding Fixed Assets (4,766,238 – 378,454 = 4,387,784) which ever is lower.			(3,594,429)
			399,381
Input tax on fixed assets			(378,454)
			20,927
Further tax on supplies to unregistered persons = 10,150,000×2			203,000
Sales tax payable			223,927
Sales tax to be carried forward (4,766,238–3,594,429 – 378,454)			**793,355**
Sales tax refundable (5,059,000×5,000,000/28,493,000)			**887,762**
Note 1: Apportionment of input tax			
Residual input tax			5,059,000
Total supplies			28,493,000
Inadmissible input tax i.e. Export [(5,000,000/28,493,000)×5,059,000]			887,762

(THE END)

The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examination

5 March 2018
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Mr. Qateel, a resident individual, is engaged in the manufacture of various consumer goods under the name and style 'Qateel Enterprises (QE)'. The following information has been extracted from the records of QE for the financial year ended 30 June 20X8.

	Rupees
Total turnover	28,500,000
Cost of sales	(26,155,000)
Gross profit	2,345,000
Operating expenses	(4,500,000)
Operating loss	(2,155,000)
Finance charges on lease of machinery	(35,703)
Other income	5,000,000
Profit before tax	2,809,297

Additional information:

(i) Cost of sales includes:
- Rs. 45,000 paid as fine for violation of contract with a customer for delay in supply of goods.
- accounting depreciation of Rs. 1,900,000 (including depreciation on leased assets).

(ii) Operating expenses include:
- Rs. 450,000 paid for renewal of a manufacturing licence for fifteen years.
- vehicle tax paid in cash amounting to Rs. 55,000 for eight office cars.
- Rs. 200,000 paid as security deposit to K-Electric (KE) for replacement of transformer at the factory.
- Rs. 300,000 collected by KE as advance tax through monthly electricity bills.
- cash donation to poor families amounting to Rs. 64,600 and donation of Rs. 2,000,000 paid through cheque to Edhi Foundation, which is listed in Part 1 of the Second Schedule of the Income Tax Ordinance, 2001.
- penalty of Rs. 25,000 imposed by the Commissioner Inland Revenue for late filing of annual return of income for the tax year 20X7.
- entertainment expenditure of Rs. 128,000 incurred on arrival of foreign customers for business purposes.

(iii) Other income includes:
- dividend of Rs. 580,000 received from listed companies. The amount is net of income tax at the rate of 15% and Zakat of Rs. 100,000 deducted under the Zakat and Usher Ordinance, 1980.
- Capital gain of Rs. 1,200,000 from sale of shares of a private limited company. Shares were acquired on 1 August 20X3.

(iv) On 30 June 20X8, leased machinery was transferred to Qateel on maturity of lease. The leasing company was asked to adjust the amount of security deposit against the residual value of Rs. 100,000. The date of commencement of lease was 1 July 20X3.

Lease rentals paid during the year amounted to Rs. 270,000.

On the date of maturity, the accounting written down value and market value of the machinery was Rs. 590,490 and Rs. 800,000 respectively.

(v) During the year, a warehouse was constructed for storage of goods at a cost of Rs. 1,040,000. No accounting depreciation has been recorded on it.

(vi) Tax depreciation for the tax year 20X8 without considering the effect of para (iv) and (v) above, amounted to Rs. 1,560,000.
(vii) Advance income tax paid during the year amounted to Rs. 480,000.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the total income, taxable income and net tax payable by or refundable to QE for the year ended 30 June 20X8. **(18)**

Note:
- ***Ignore minimum tax under section 113.***
- ***Show all the relevant exemptions, exclusions and disallowances.***
- ***Tax rates are given on the last page.***

Q.2 Under the provisions of the Income Tax Ordinance, 2001 compute taxable income or loss under correct head of income for tax year 20X8, in each of the following cases:

(a) Mrs. Raees separated from her spouse due to certain disagreements. Under an agreement to live apart, her spouse provided her a house and paid cash of Rs. 150,000 per month as support payment. The fair market rent of the house is Rs. 50,000 per month. **(02)**

(b) Shaoor is the sole proprietor of Shaoor Enterprises (SE). On 31 January 20X8 SE sold a factory building including land for Rs. 10 million. At the time of disposal, the fair market values of the land and building were Rs. 3 million and Rs. 5 million respectively.

The land and building were acquired on 1 July 20X6 at a cost of Rs. 2 million and Rs. 6 million respectively. The tax WDV of the building on 1 July 20X7 was Rs. 5.4 million. **(05)**

(c) Hasrat has been working as Director HR in Shakir Limited (SL) for many years. During the tax year 20X8 he received basic salary of Rs. 6 million. SL also contributed Rs. 50,000 per month towards a recognized provident fund. An equal amount was contributed by Hasrat. Interest income of Rs. 3,391,000 at the rate of 20% of accumulated balance of the fund was credited to Hasrat's account. **(04)**

Q.3 (a) Under the provisions of the Income Tax Ordinance, 2001 briefly discuss the following:
(i) The term 'Concealed assets'. **(02)**
(ii) The powers of Commissioner relating to the concealed assets of any person when these are impounded by the Federal Government. **(03)**

(b) Anwar had filed his return of income for the tax year 2013 on 31 August 2013. Discuss the following in the light of provisions of the Income Tax Ordinance, 2001:

(i) By which date the Commissioner of Income Tax could make the first amendment of the assessment, if required. **(02)**
(ii) By which date any further amendment can be made if the first amendment was made on 15 February 2017. **(02)**

(c) On 1 December 20X7 Bruce Lee was appointed by a Chinese company as a Technical Director for Pakistan. He has provided you the following details:

Arrival in Pakistan	15 December 20X7
Joined office in Pakistan	20 December 20X7
Visit to Dubai on an official trip	21-30 March 20X8
Visit to South Korea for vacations	12-21 April 20X8
Visit to northern areas of Pakistan for personal trip	4-9 June 20X8

In view of the provisions of the Income tax Ordinance, 2001 and related Rules thereunder, comment on the residential status of Bruce Lee for the tax year 20X8. **(03)**

(d) Under the provisions of the Income Tax Rules, 2002 list the records to be kept by a taxpayer in respect of his income from:
- (i) Salary **(01)**
- (ii) Property **(1.5)**
- (iii) capital gain **(1.5)**

Q.4 (a) Nadeem has agricultural land in Thatta which is being used for the cultivation of sugarcane. During the year, he cultivated 200,000 tonnes of sugarcane. Out of total cultivation, 140,000 tonnes of sugar cane was sold to a sugar mill at a price of Rs. 4,550 per ton whereas the remaining quantity was utilized in his own sugar mill. During the year, there were no other purchases of sugar cane by his sugar mill.

The sale of his sugar mill stood at Rs. 310 million whereas total expenses other than the raw material amounted to Rs. 19 million. There was no opening and closing stock of sugarcane.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the taxable income of Nadeem for the tax year 20X8. **(04)**

(b) Identify due date of filing of tax return in each of the following cases, under the provisions of the Income Tax Ordinance, 2001:

- (i) An individual who's entire income falls under final tax regime **(0.5)**
- (ii) An individual who derives his income from business which falls under normal tax regime. **(0.5)**
- (iii) An individual filing return in response to a notice received from the Commissioner who believes that he is likely to discontinue his business. **(01)**
- (iv) An individual filing return in response to a notice received from the Commissioner for not filing return of income of the previous tax year. **(01)**
- (v) A company. **(01)**

(c) Discuss the provisions of the Income Tax Ordinance, 2001 regarding set off and carry forward of losses under the following heads:

- (i) Income from business **(05)**
- (ii) Income from speculation business **(04)**

Q.5 (a) Taxes are primary revenue yielding tools of the Government of modern ages. You are required to state any **three** non-revenue objectives which the Government achieves by imposing taxation. **(03)**

(b) List any **five** taxes which can be imposed by the Federal Government. **(05)**

Q.6 Under the provisions of the Sales Tax Act, 1990:

(a) List the exceptions to the following general rule:

- (i) Where the taxable supplies are made to a person who has not obtained registration number, there shall be charged, levied and paid a further tax at the rate of 2% of the value in addition to the normal rate of 17%. **(03)**
- (ii) Goods exported shall be charged to tax at the rate of zero percent. **(03)**

(b) Explain the term 'Temporary registration'. Briefly discuss the rights, obligations and responsibilities of a person who has obtained temporary registration. **(06)**

Q.7 Faiz Associates (FA) is a partnership concern and registered under the Sales Tax Act, 1990 as manufacturer-cum-distributor. Following information has been provided by FA for the month of January 2018:

	Rupees
Supplies	
Taxable goods to registered customers	3,450,000
Taxable goods to un-registered customers	1,000,000
Consumable goods supplied on PIA's international flight	500,000
Export	700,000
Purchases	
Taxable goods from registered suppliers	2,000,000
Taxable goods from un-registered suppliers	450,000
Exempt goods from registered suppliers	600,000
Input tax brought forward from December 2017	265,000

Additional information:

(i) Supply of taxable goods to registered customers include the following:
- Goods amounting to Rs. 80,000 sold to Hafiz Brothers (HB) on 31 January 2018. HB started business in January 2018 and had filed an application for registration under the Sales Tax Rules 2006 on 30 January 2018. However, no sales tax registration number was issued till 31 January 2018.
- Goods having market value of Rs. 600,000 which were supplied to Parveen Limited, an associated company, for Rs. 500,000.
- An invoice erroneously issued for Rs. 450,000 whereas the correct amount of the invoice was Rs. 540,000.
- Sale to Ghalib Corporation of goods worth Rs. 225,000. The contract for sale has been signed but neither invoice was issued nor any delivery and payment was made in January 2018.

(ii) Purchases from registered suppliers include:
- purchase of two air-conditioners amounting to Rs. 150,000 for FA's new office.
- an invoice of Rs. 500,000 dated 22 January 2018 issued by Taqi Corporation (TC). However, TC was blacklisted by the Commissioner on 6 February 2018.

(iii) FA destroyed certain goods worth Rs. 45,000 after following the due process under the Sales Tax Rules, 2006. Input tax on these goods was claimed in December 2017.

(iv) Free replacement of defective parts costing Rs. 400,000 relating to goods which were sold under 1-year warranty. The market value of such parts was Rs. 550,000.

(v) A debit note for Rs. 100,000 issued by a customer in respect of goods returned was duly settled and the relevant credit note has been issued within the stipulated time.

(vi) During the month, FA paid Sindh Sales Tax worth Rs. 8,500 on franchise services. Under the Sindh Sales Tax Laws, such tax is not an admissible credit.

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of 17%.

Required:
Compute sales tax payable by or refundable to Faiz Associates along with input tax to be carried forward, if any, in the sales tax return for the month of January 2018. **(18)**
Note : Show all relevant exemptions, exclusions and disallowances.

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001
THE FIRST SCHEDULE
Tax Rates for Every Individual and Association of Person Except for Salaried Taxpayer

S. No.	Taxable income	Rate of tax
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 7,000 + 10% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,500,000	Rs. 32,000 + 15% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 144,500 + 20% of the amount exceeding Rs. 1,500,000
6.	Exceeds Rs. 2,500,000 but does not exceed Rs. 4,000,000	Rs. 344,500 + 25% of the amount exceeding Rs. 2,500,000
7.	Exceeds Rs. 4,000,000 but does not exceed Rs. 6,000,000	Rs. 719,500 + 30% of the amount exceeding Rs. 4,000,000
8.	Exceeds Rs. 6,000,000	Rs. 1,319,500 + 35% of the amount exceeding Rs. 6,000,000

THE THIRD SCHEDULE
Part I
Depreciation Rates

1.	Building (all types)	10%
2.	Furniture and fittings	15%
3.	Plant and machinery	15%
4.	Motor vehicles (all types)	15%
5.	Computer hardware	30%

Part II
Initial Allowance and First Year Allowance

The rate of initial allowance shall be 25% for plant and machinery and 15% for building.

Ans.1

Qateel Enterprises
Computation of income tax liability
For the tax year 2017

		Rupees
Accounting profit before taxation		**2,809,297**
Add: Inadmissible expenses/admissible income		
Fine paid – violation of the contract		-
Vehicle tax		-
Accounting depreciation		1,900,000
Renewal of license fee		450,000
Replacement of transformer (KESC) – security deposit		200,000
Advance tax collected (KESC)		300,000
Donation paid in cash		64,600
Donation paid		2,000,000
Penalty paid to CIR for late filing of return		25,000
Entertainment expenditures – foreign customer		-
Dividend income - Gross		800,000
Gain on sale of a private limited company shares Rs. 1,200,000. Since holding period is > one year gain would be reduced to 75%		900,000
Finance charges on lease machinery		35,703
		6,675,303
Less: Admissible expenses & inadmissible/FTR income		
Renewal of license fee [450,000/10]		45,000
Gain on sale of a private limited company shares		1,200,000
Tax depreciation as given		1,560,000
Tax depreciation on warehouse constructed	**N-1**	244,400
Lease rental paid		270,000
Dividend income		580,000
Tax depreciation on leased machinery acquired by paying residual value		15,000
		(3,914,400)
Total income for the year		5,570,200
Less: Dividend income (FTR income)	**N-2**	(800,000)
		4,770,200
Zakat deducted on dividend		(100,000)
		4,670,200
Deductible allowances		
Donation paid – allowed upto 30% of the taxable income		(1,401,060)
Taxable income under NTR		3,269,140
Computation of tax liability		
Tax on 2,500,000		344,500
Tax on income exceeding 2,500,000 @ 25%		192,285
Tax payable under NTR		536,785
Tax on dividend – FTR (15%)		120,000
Total tax liability		656,785
Advance tax collected on electricity bill		(300,000)
Advance tax paid		(480,000)
Advance tax on dividend		(120,000)
		(900,000)
Income tax refundable		**(243,215)**

		Rupees
N-1:	Warehouse constructed	**1,040,000**
	Initial allowance @ 15% (1,040,000×15%)	156,000
	Tax depreciation @ 10% [(1,040,000–156,000)×10%]	88,400
	Total depreciation	**244,400**

N-2:	Dividend received	
	Add: Zakat paid (Rs.4,000,000)	580,000
		100,000
		680,000
	Add: Advance tax deducted	120,000
	Grossed up with amount of tax deducted @ 15%	**800,000**

Ans.2 **(a)** Head of income: Income from other sources

According to Income tax Ordinance, any income received by a spouse as support payment under an agreement to live apart shall be exempt from tax.

(b)

Computation of taxable income
Mujahid Enterprises
For the year ended 30 June 2017

	Rupees
Income from business	
From sale of building	
Sale proceeds (equivalent to cost)	6,000,000
Tax WDV of building (6,000,000–600,000)	(5,400,000)
Taxable income (under NTR)	600,000
Capital gain	
From sale of land	
Sale proceeds (cost of the assets)	3,750,000
Cost of land	(2,000,000)
Taxable income (separate block of income)	1,750,000

Accordingly, the sale proceeds of the building and land are computed as under:
Land = 10×3/8 = Rs. 3.75 million
Building = 10×5/8 = Rs. 6.25 million

(c) Head of income: Income from salary

	----------- Rupees -----------	
Salary		6,000,000
Provident fund contribution by SL (50,000×12)	600,000	
Tax exemption up to 150,000 or 10% of salary	(150,000)	450,000
Interest credited to provident fund		
Amount credited	3,391,000	
Exempt higher of:		
- 2,712,800 (3,391,000×16%÷20%); or		
- 1/3rd of salary i.e. 2,000,000 (6,000,000÷3)	2,712,800	678,200
Taxable income of Hasrat		7,128,000

Ans.3 **(a)** (i) Under the Income Tax Ordinance, 2001 if in the opinion of the Commissioner, an asset is acquired from any income chargeable to tax but could not be charged to tax, it is considered to be a concealed asset.

(ii) Where a concealed asset of any person is impounded by any department or agency of the Federal Government, the Commissioner may at any time, before making a best judgement or any amended assessment order, issue to the person a provisional assessment order or provisional amended assessment order, as the case may be, for the last completed tax year during which the concealed asset was accounted for.

(b) (i) The Commissioner of income tax is empowered to amend the assessment of the taxpayer within five years from the end of the financial year in which the Commissioner has issued or treated to have issued the assessment order to the taxpayer Accordingly, in this case amendment can be made by 30 June 2019.

(ii) Where the Commissioner has issued the amended assessment order to the taxpayer, the limitation period should be later of:

- five years from the end of the financial year in which the original assessment order is issued or treated as issued by the Commissioner; or
- one year from the end of the financial year in which the amended assessment order is issued or is treated as issued to the tax payer.

The time limitation for the next assessment will therefore to be by 30 June 2019.

(c) Mr. Bruce Lee is not a resident for the tax year 2017 as he was present for less than 183 days in Pakistan i-e 178 days as follows:

Months	Days
December 2016 (15-12-16 is also included)	17
January 2017	31
February 2017	28
March 2017	31
April 2017	30
May 2017	31
June 2017	30
	198
Less: Number of days visited to Dubai – March	(10)
Less: Number of days visited to South Korea – April	(10)
	178

For not considering the days spent on personal trip within Pakistan.

(d) Under the provisions of the Income Tax Rules 2002, following are the records to be kept by a tax payer in respect of his income from:

(i) Salary

- Salary certificate indicating the amount of salary and tax deducted therefrom.

(ii) Property

- Tenancy agreement, if executed
- Tenancy termination agreement, if executed
- Receipt for amount of rent received
- Evidence of deductions claimed in respect of premium paid to insure the building, local rate, tax, charge or cess, ground rent, profit/interest or share in rent on money borrowed, expenditure on collecting the rent, legal services and unpaid rent.

(iii) Capital gain
- Evidence of cost of acquiring the capital asset
- Evidence of deduction for any other costs claimed
- Evidence in respect of consideration received on disposal of the capital asset.

Ans.4 (a)

Income from business:	**Rs. in million**
Sale – Sugar	310
Less: Operating expenses	(19)
Market value of agricultural produce used as raw-material (60,000×4,550)	(273)
	18
Exempt income:	
Sale of Sugar cane worth of Rs. 910 million (200,000×4,550) received from agricultural land	-
Taxable income	18

(b) (i) On or before 31 August next following the end of tax year.
(ii) On or before 30 September next following the end of the tax year.
(iii) Due date fixed for submission of tax return by the Commissioner.
(iv) Due date specified in the notice for submission of tax return or thirty days from the date of issuance of notice.
(v)

▪	If tax year ends between 1 January to 30 June	On or before 31 December next following the end of tax year.
▪	If tax year ends between 1 July to 31 December	On or before 30 September next following the end of tax year.

(c) Business Loss

(i) Where a person sustains a loss for a tax year under the head "income from business", the said loss can be fully offset against the person's income, if any, chargeable to tax under any other head of income except income from salary and income from property.
(ii) Where such loss cannot be fully offset against the income of any other head for that year, so much of the loss that has not been offset fully, may be carried forward to the following tax year and set off against the person's chargeable income under the head "income from business" for that year.
(iii) No loss can be carried forward for more than six tax years immediately succeeding the tax year for which the loss was first computed.
(iv) Where the business loss includes deductions allowed under depreciation and amortization that have not been set off against income, the amount not set off, may be added to the deductions allowed under these heads in the subsequent years and so on until completely set off.

Speculation Losses

(i) If a person sustains a loss in a tax year from any speculation business, he can set off such loss only against profits of any other speculation business carried on by him during the same tax year.
(ii) In the subsequent years too, the speculation loss can be set-off against income of any speculation business only. It means that loss from speculation business cannot be adjusted against income under any other head.
(iii) If a person has a speculation loss carried forward for more than one tax years, the loss of earliest tax year shall be set-off first.

Ans.5 **(a)** The taxation system may also be utilized to achieve the following non revenue objectives as follows:

- To strengthen anemic enterprises by granting them tax exemptions or other conditions or incentives for growth;
- To protect local industries against foreign competition by increasing local import taxes;
- As a bargaining tool in trade negotiations with other countries;
- To counter the effects of inflation or depression;
- To reduce inequalities in the distribution of wealth;
- To promote science and invention, finance educational activities or maintain and improve the efficiency of local forces;
- To implement laws which eliminate discrimination among various elements in the markets/businesses.
- To discourage certain undesirable sectors and activities.
- To promote documentation in the economy.
- To promote export of the country.
- To promote investment in listed companies.
- To promote information technology specially software houses.
- To promote culture of payment of donation to only organized and regulated institutions.

(b) Following taxes can be imposed by the Federal Government

(i) Taxes on income other than agricultural income.
(ii) Taxes on corporations.
(iii) Taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed, except sales tax on services.
(iv) Taxes on the capital value of the assets, not including taxes on immovable property.
(v) Taxes on mineral oil, natural gas and minerals for use in generation of nuclear energy.
(vi) Taxes on the production capacity of any plant, machinery, undertaking, establishment or installation in lieu of any one or more of them.
(vii) Terminal taxes on goods or passengers carried by railway, sea or air; taxes on their fares and freights.

Ans.6 **(a)** (i) 2% further tax is not payable in the following cases even if the supplies are made to unregistered persons:

- Electricity energy supplied to domestic and agricultural consumers.
- Natural gas supplied to domestic consumers and CNG stations.
- Motor oil, diesel oil, jet fuel, kerosene oil and fuel oil.
- Goods sold by the retailers to end customers.
- Supply of goods directly to end customers including food, beverages, fertilizers and vehicles.
- Items listed in Third Schedule to the Sales Tax Act, 1990.
- Second hand worn clothing and other worn articles falling under PCT heading 6309.0000.
- Fertilizers.
- Supplies by steel melters, re-rollers and ship breakers operating under Chapter XI of Sales Tax Special Procedure Rules, 2007.
- Supplies covered under the Fifth Schedule to the Sales Tax Act, 1990.

(ii) Following is the list of goods which are exported but shall not be charged at the rate of zero percent:

- Goods exported but have been or are intended to be re-imported into Pakistan; or
- Goods which have been entered for export under section 131 of the Customs Act, 1969 (IV of 1969), but are not exported; or
- Have been exported to countries specified by the Federal Government, by notification in the official Gazette in this regard.

(b) Where a person files application for sales tax registration as a manufacturer prior to installation of machinery, for the purpose of import of machinery to be installed by him, temporary registration as manufacturer shall be allowed to him for a period of sixty days.

After receiving temporary registration, the person shall be allowed to import plant, machinery and raw materials, etc. as a manufacturer, subject to submission to the customs authorities of a post-dated cheque equal to the difference in duties and taxes to be availed as a manufacturer.

In case the list of machinery is not provided within sixty days of issuance of the temporary registration, such temporary registration shall be disabled and the post-dated cheques submitted shall be encashed.

A person holding temporary registration shall file monthly return, but shall not issue a sales tax invoice and if such invoice is issued, no input tax credit shall be admissible against such invoice.

No sales tax refund shall be paid to the person during the period of temporary registration and the amount of input tax may be carried forward to his returns for subsequent tax periods.

Ans.7

Faiz & Faraz Associates
Computation of sales tax payable/refundable
For the tax period January 2018

	Taxable Value	**Sales Tax Rate**	**Sales Tax**
	------------------ Rupees ------------------		
Sales tax credits - Input Tax			
Purchases from registered suppliers	2,000,000		
Purchases of air conditioners for office use	150,000		
	1,850,000		314,500
Purchases from unregistered suppliers	450,000	**inadmissible**	-
Purchases exempt goods from registered suppliers	600,000	**exempt**	-
Invoice issued by Taqi Corporation which was declared blacklisted in next period			-
Sindh sales tax paid on franchise service	-	**inadmissible**	-
Total input tax			314,500
Less: Inadmissible/unadjusted input tax			(68,431)
Input tax for the month			246,069
Opening balance			265,000
Less: Input tax on goods destroyed (45,000×0.17)			7,650
			257,350
Accumulated credit			503,419
Sales tax debits - Output Tax			
Local taxable supplies	3,450,000		
Local taxable supplies - *to Hafiz Brothers	(80,000)		
Local taxable supplies - to Ghalib Corporation	(225,000)		
Local taxable supplies - to Parveen Limited – associated undertaking (600,000–500,000)	100,000		
Local taxable supplies - correction of invoice (540,000–450,000)	90,000		
	3,335,000		566,950
- unregistered persons	1,000,000	**U.R**	170,000
Local taxable supplies - to Hafiz Brothers*	80,000	**U.R**	13,600
	4,415,000		
Export (zero rated)	700,000	**Z.R**	-
Consumer goods supplied to PIA international flight	500,000	**Z.R**	-
	1,200,000		
Output tax for the month	**5,615,000**		750,550
Less: Sales return	(100,000)		(17,000)
Total supplies/Output tax for the month	**5,515,000**		733,550
Free replacement of defective parts	-		-
Admissible credit [90% of output tax i.e. Rs. (733,550×0.9 = 660,195) or input tax Rs. 503,419 whichever is lower]			(503,419)
			230,731
Further tax on supplies to unregistered persons (1,000,000+80,000)=1,080,000×2%			21,600
Sales tax payable			251,731
Sales tax to be carried forward (503,419–503,419)			**-**
Sales tax refundable [314,500×(700,000+500,000)/5,515,000]			**68,431**

W-1: Apportionment of input tax	**Rupees**
Residual input tax	314,500
Export and zero rated sales (500,000+700,000)	1,200,000
Total supplies	5,515,000
Inadmissible input tax [(700,000+500,000)/5,515,000×314,500]	68,431

(THE END)

The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examination

6 September 2017
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Taqi Ahmed is working as Director Marketing with Zee Textiles Limited (ZTL) for the last twenty five years. Details of his monthly emoluments during the year ended 30 June 20X7 are as under:

	Rupees
Basic salary	440,000
Conveyance allowance	44,000
Medical allowance	44,000

In addition to the above, Taqi Ahmed has provided the following information:

(i) He and his family members are covered under the health insurance policy in accordance with the terms of employment. The amount of annual premium paid by ZTL was Rs. 200,000.

(ii) During the year, daily allowance of Rs. 400,000 was received to meet the expenses for working on assignments at ZTL's factories located in Lahore and Multan.

(iii) On 31 July 20X7, the HR Committee approved a performance bonus for all employees for the year ended 30 June 20X7. Taqi received Rs. 1,200,000 as performance bonus on 15 August 20X7.

(iv) On 31 March 20X7, in recognition of completion of twenty five years of his service with ZTL, the board of directors approved to waive the outstanding amount of loan taken by Taqi Ahmed. This interest free loan of Rs. 2,500,000 was taken on 1 January 20X5 and was repayable in fifty equal monthly instalments commencing from May 20X5. The prescribed benchmark rate is 10% per annum.

(v) During the year, he received Rs. 100,000 for attending board meetings of ZTL. No tax was withheld from this amount.

(vi) Amount of tax withheld by ZTL from his salary amounted to Rs. 2,000,000.

Other information relevant to tax year 20X7 is as under:

(i) Salary is transferred to the bank account on 10th of the following month.

(ii) 10% annual increase was given to him effective 1st July in each of the last three years.

(iii) Taqi has given his house on rent to his cousin at annual rent of Rs. 1,500,000. The rent was inclusive of amenities and utilities of Rs. 25,000 per month. However, annual rent for a similar house with same amenities and utilities, in the vicinity, is Rs. 1,800,000.

(iv) He acquired 15,000 shares of a listed company from Privatization Commission of Pakistan at a price of Rs. 60 per share on 15 January 20X6. He claimed tax credit of Rs.90,000 on such investment, against the tax payable for the tax year 20X6. On 15 June 20X7 he sold all the shares at the rate of Rs. 85 each.

(v) On 31 August 20X6, he was entitled to receive 5,000 interim bonus shares from Arian Limited (AL) a listed company. The market value of these shares on that date was Rs. 22 per share.

(vi) He also received Rs. 150,000 as cash dividend declared by AL. The share registrar incorrectly treated Taqi as non-filer and deducted withholding tax accordingly.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute under correct head of income, the total income, the taxable income and net tax payable by or refundable to Taqi Ahmed for the year ended 30 June 20X7. **(16)**

Q.2 Under the provisions of Income Tax Ordinance, 2001 and rules made thereunder:

(a) Discuss the residential status for tax year 2017 in each of the following situations:

(i) On 21 September 2016 Asif proceeded to Dubai to join his new job. Due to certain professional issues with his employer in Dubai, he resigned on 1 May 2017 and came back to Pakistan. On 16 May 2017 he got a new job in Pakistan which he continued till 30 June 2017. **(02)**

(ii) Sami Associates is an association of persons and provides accounting services in Dubai. On 2 January 2017, the entire management and control of its affairs was shifted from Karachi to Dubai. **(02)**

(b) Explain the treatment of foreign source income for tax year 2017 under each of the following independent situations:

(i) Joseph, a South African cricket coach is working in Pakistan under an employment contract since 20 July 2014. During the tax year 2017, he earned foreign source income from his business established in South Africa and brought 25% of the income to Pakistan. **(04)**

(ii) On 15 January 2016 Farhan returned to Pakistan from London after 10 years and has been living in Pakistan since then. During the tax year 2017, he received GBP 5,000 as return from his investment in London. **(02)**

(c) Determine the amount of deductible allowance that a resident individual can claim on account of education expenses, if his taxable income for the year was Rs. 800,000 and he paid monthly fee of Rs. 6,000 per child for his three children. **(02)**

Q.3 Under the provisions of the Income Tax Ordinance, 2001 compute taxable income or loss, under the correct head of income for tax year 2017, in each of the following cases:

(a) Under an employee share scheme, 30,000 shares of Dawood Limited were issued to Qamar, on 1 August 2013 for Rs. 30 each. According to the scheme, he was not allowed to sell/transfer the shares before completion of three years from the date of issue. The face value of each share is Rs. 10 per share. Fair market value of each share on different dates was as follows:

1 August 2013	**30 June 2016**	**31 July 2016**
Rs. 40	Rs. 30	Rs. 50

He sold 10,000 shares on 31 May 2017 for Rs. 65 per share. **(04)**

(b) Zaheer sold a painting to his brother on 10 April 2017 for Rs. 2,000,000. Zaheer had purchased this painting for his residence, in an auction on 14 August 2013 for Rs. 1,800,000. **(02)**

(c) Sarwar Enterprises sold an immovable property for Rs. 50 million. The cost of the immovable property was Rs. 30 million. Tax depreciation of Rs. 6 million had been allowed on the immovable property up to the tax year 2016. **(2.5)**

(d) Shams Industries Limited (SIL) sold and exported one of its plants to a Nigerian Company. The sale proceeds received in SIL's account amounted to Rs. 25 million. The cost and tax written down value of the plant was Rs. 20 million and Rs. 7 million respectively. **(2.5)**

Q.4 (a) Under the provisions of the Income Tax Ordinance, 2001, state the situations where expenditure is required to be apportioned for the purpose of claiming a deduction. **(03)**

(b) List the situations under which an original assessment can be amended or an amended assessment can be further amended by the Commissioner of Income Tax. Also state the time period within which the original or the previously amended assessment order can further be amended. **(07)**

Q.5 Under the Income Tax Ordinance, 2001 certain persons are required to pay minimum tax amounting to 1% of their turnover from all sources.

(a) Explain the term 'Turnover' for the purpose of determining the minimum tax. **(05)**

(b) List the persons who are required to pay minimum tax. **(03)**

(c) Discuss the provisions relating to carry forward of minimum tax paid to the subsequent years. **(02)**

Q.6 Cyma Associates (CA) is registered under the Sales Tax Act, 1990, as manufacturer-cum-distributor-cum-retailer. Following information has been extracted from its records for the month of August 2017:

	Rupees
Supplies	
Taxable goods to registered persons	15,000,000
Taxable goods to unregistered persons	2,800,000
Exports	1,500,000
Exempt supplies	1,700,000
Purchases	
Taxable goods from registered suppliers	20,000,000
Taxable goods from unregistered suppliers	1,800,000
Exempt goods from registered suppliers	400,000
Fixed assets (machinery) from a registered supplier	1,000,000

The following additional information is available for August 2017:

(i) Supply of taxable goods to registered persons include the following:
- Goods invoiced at Rs. 325,000 (net of special discount of Rs. 125,000) sold to a government official.
- On 1 August 2017, CA launched 'Halloween Tooth Brush' which is covered under 3rd schedule. The retail price of the tooth brushes is Rs. 100 each. However, being the first month of launching, it was sold at a discounted price of Rs. 75 each. 4,000 tooth brushes were sold in August 2017.

(ii) Exports include supply of taxable goods of Rs. 500,000 to a retailer in Export Processing Zone.

(iii) Exempt supplies include distribution of free samples of exempt goods among the vendors. Value of such goods amounted to Rs. 80,000.

(iv) Purchases from registered suppliers include:
- material worth Rs. 350,000 the payment of which was made by depositing cash directly in the business bank account of the supplier.
- material worth Rs. 800,000 against which a discrepancy has been indicated by the CREST.
- an amount of Rs. 2,000,000 paid for purchase of raw material. However, only 30% of the goods were supplied during August for which sales tax invoice has been issued by the supplier.

(v) On 1 August 2017, CA executed an agreement with Majeed Sons (MS) for sale of locally purchased goods worth Rs. 225,000. The agreement empowers MS to obtain delivery of these goods anytime it likes.

(vi) Supplies returned by different registered persons amounted to Rs. 756,000. Proper debit and credit notes were raised within the specified time.

(vii) The auditors have proposed a provision against obsolete and expired stock of Rs. 285,000 which is lying in CA's warehouse since January 2016.

(viii) Machinery purchased during the month was commissioned into operations on 31 August 2017.

(ix) Excess of input tax over output tax in July 2017 amounted to Rs. 75,000.

Except where otherwise specified, all figures are exclusive of sales tax. Rate of sales tax is 17%.

Required:
Compute the sales tax liability of CA for the month of August 2017. **(17)**

Q.7 Zubair has recently been registered under the Sales Tax Act, 1990. You are required to advise him on the following matters:

(a) Type of exports which are outside the purview of zero rating. **(03)**
(b) Eligibility for a refund if input tax is paid in excess of output tax payable for the month. **(03)**
(c) The conditions required to be fulfilled for filing a revised return. **(02)**
(d) Concept of provisional and final adjustment in relation to 'Apportionment of input tax'. **(02)**
(e) How to deal with change in rate of tax during a tax period. **(04)**

Q.8 (a) Briefly describe the pillars/principles of tax administration which are meant to safeguard the interest of taxpayers and avoid abuse of powers by the tax administrators. **(04)**

(b) Differentiate between the terms 'Tax evasion' and 'Tax avoidance'. Give **one** example in each case. **(03)**

(c) List any **six** ethical issues that which administrators may face while discharging their duties. **(03)**

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001

SECTION 236M

Bonus shares issued by companies quoted on stock exchange

Every company, quoted on stock exchange, issuing bonus shares to the shareholders of the company, shall withhold five percent of the bonus shares to be issued.

THE FIRST SCHEDULE

Rates of Tax for Salaried Individuals

9.	Where the taxable income exceeds Rs. 3,000,000 but does not exceed Rs. 3,500,000	Rs. 359,500 + 22.5% of the amount exceeding Rs. 3,000,000
10.	Where the taxable income exceeds Rs. 3,500,000 but does not exceed Rs. 4,000,000	Rs. 472,000 + 25% of the amount exceeding Rs. 3,500,000
11.	Where the taxable income exceeds Rs. 4,000,000 but does not exceed Rs. 7,000,000	Rs. 597,000 + 27.5% of the amount exceeding Rs. 4,000,000
12.	Where the taxable income exceeds Rs. 7,000,000	Rs. 1,422,000 + 30% of the amount exceeding Rs. 7,000,000

Rate of Dividend Tax

(a) 7.5% in the case of dividends declared or distributed by purchaser of a power project privatized by WAPDA or on shares of a company set up for power generation or on shares of a company, supplying coal exclusively to power generation project; and
(b) 12.5% for filers other than mentioned in (a) above;
(c) 20% for non-filers other than mentioned in (a) above

Income from Property

The rate of tax to be paid under section 15, in the case of individual and association of persons, shall be as follows:

3.	Where the gross amount of rent exceeds Rs. 600,000 but does not exceed Rs. 1,000,000.	Rs. 20,000 plus 10% of the gross amount exceeding Rs. 600,000.
4.	Where the gross amount of rent exceeds Rs. 1,000,000 but does not exceed Rs. 2,000,000.	Rs. 60,000 plus 15% of the gross amount exceeding Rs. 1,000,000.
5.	Where the gross amount of rent exceeds Rs. 2,000,000.	Rs. 210,000 plus 20% of the gross amount exceeding Rs. 2,000,000.

Capital Gains on Disposal of Securities

The rate of tax to be paid under section 37A shall be as follows:

S. No.	Period	Tax year 2015	Tax year 2016	Tax year 2017
(1)	(2)	(3)	(4)	(5)
2.	Where holding period of a security is twelve months or more but less than twenty-four months.	10%	12.5%	12.5%
3.	Where holding period of a security is twenty-four months or more but the security was acquired on or after 1st July, 2012.	0%	7.5%	7.5%

Ans.1

Taqi Ahmed
Computation of total income, taxable income and net tax payable/refundable
For the tax year 2017

	Rupees
Income from Salary:	
Basic Salary [(400,000+(440,000×11)]	5,240,000
Conveyance allowance [(40,000+(44,000×11)]	524,000
Medical allowance [(40,000+(44,000×11)]	524,000
Daily allowance (Special allowance)	-
Performance bonus for tax year 20X7 but received in 20X8	-
Director's fees for attending board meeting - ZTL	100,000
Loan waived by ZTL (50,000×28)	1,400,000
Imputed/deemed interest on loan (1,800,000×10%) from July 20X6 to Mar 20X7	135,000
	7,923,000
Income from property	
Rental amount (1,800,000–300,000)	1,500,000
	1,500,000
Income from other sources	
Bonus shares received [5,000×22)	110,000
Dividend received (150,000/0.80)	187,500
Value of amenities and utilities included in rent	300,000
	597,500
Capital gain	
Consideration received on disposal [15,000×85]	1,275,000
Less: cost of acquisition [15,000×60]	(900,000)
Gain on disposal of 15,000 shares	375,000
Total income for the year from all sources	**10,395,500**
Less:	
Property income-Separate block income (1,800,000–300,000)	(1,500,000)
Bonus shares - FTR income	(110,000)
Dividend received - FTR income	(187,500)
Gain on disposal of 15,000 shares-Separate block	(375,000)
	(2,172,500)
Taxable income under NTR	8,223,000
Tax liability	
NTR-Income	
Tax on Rs. 7,000,000	1,422,000
exceeding Rs. 7,000,000 at the rate of 30%	366,900
	1,778,900
Property income-Separate block income	
Rent upto Rs. 1,000,000	60,000
Amount exceeding Rs. 1,000,000 i.e. Rs. 500,000 @ 15%	75,000
	135,000
Capital Gain - Separate block income	
Holding period is more than twelve months but less than 24 months (Rs. 375,000@12.5%)	46,875
Bonus shares (Rs. 110,000 @ 5%)	5,500
Dividend - FTR income (Rs. 187,500 @ 12.5%)	23,438
Tax payable	1,999,713
Less: Tax deducted by ZTL	(2,000,000)
Tax deducted on dividend @ 20%	(37,500)
Tax paid/deducted on bonus shares	(5,500)
Net tax payable	43,287
Add: Tax credit previously allowed, now added back	90,000
Total tax payable	46,713

Ans.2 (a) (i) The number of days Asif spent in Pakistan during tax year 2017 is 144 as shown below:

Month	Days
July 2016	31
August 2016	31
September 2016	21
May 2017	31
June 2017	30
Total	**144**

Asif is a non- resident person as his total stay in tax year 2017 is less than 183 days.

(ii) An AOP is treated as a resident if the management and control of its affairs is situated in Pakistan at any time during the year. Hence Sami Associates would be considered a resident irrespective of the fact that its entire management and control of affairs was subsequently shifted from Karachi to Dubai.

(b) (i) Joseph is considered as a short term resident individual as he is:

- in Pakistan solely by reason of his employment
- present in Pakistan for a period not exceeding three years.

Under the Income Tax Ordinance, 2001, the foreign source income of a short term individual is exempt from tax if it is not brought into Pakistan. Therefore, 25% of his foreign source income which he brought into Pakistan is taxable whereas 75% of his foreign source income which he kept outside Pakistan is exempt from tax.

(ii) Since Farhan, being a citizen of Pakistan, was not resident in any of the four tax years preceding the tax year in which he became a resident his foreign source income is exempt from tax in the tax year in which he became resident and following one tax year.

(c) The amount allowed as educational expense should be the lesser of:

		Rupees
(i)	5 % of the total tuition fee paid (6,000×12×3×5%)	10,800
(ii)	25% of the person's taxable income (800,000×25%)	200,000
(iii)	An amount equal to 60,000 × 3 children	180,000

Therefore, the amount allowed is Rs. 10,800.

Ans.3 (a)

Share of DL - Employees share scheme	**Taxable Income Rupees**
Fair market value of shares on 31 July 2016 (30,000× 50)	1,500,000
Purchase price (30000×30)	900,000
Income from salary	600,000

Share of DL - Employees share scheme	**Rupees**
Sale proceeds of shares on 31 May 2017 (10,000×65)	650,000
Purchase price (10,000×50)	500,000
Capital Gain	150,000

(b)

Sale of painting	**Taxable Income Rupees**
Consideration received	2,000,000
Less: Cost of painting	(1,800,000)
Capital gain	200,000
The taxable gain would be 75% of 200,000 = Rs. 150,000 as the painting was disposed of after more than one year.	

(c)

	Rs. in million
Sale proceeds (equivalent to cost)	30
Less: Cost of land and WDV of immovable property (30 - 6)	(24)
Gain on disposal (Income from business)	6

(d)

	Rs. in million
Cost (equivalent to sale proceeds)	20
Less: WDV of plant	(7)
Gain on disposal (Income from business)	13

Ans.4 (a) Expenditures, deductions and allowances are required to be apportioned where these relate to:

(i) the derivation of more than one head of income.

(ii) derivation of income comprising of taxable income and any class of income on which the tax collected at source is treated to be the final tax liability of the person.

(iii) the derivation of income chargeable to tax under a head of income and to some other purpose also.

(b) When the Commissioner has definite information acquired from an audit or otherwise, the Commissioner is satisfied that:

- Any taxable income has escaped assessment;
- Total income has been under assessed or assessed at too low tax rate or has been the subject of excessive relief or refund; or
- Any amount under a head of income has been misclassified.

The Commissioner considers that the assessment order is erroneous in so far as it is prejudicial to the interest of revenue.

Time period within which assessment can be amended:

The Commissioner is empowered to amend the assessment order within the later of:

- Five years from the end of financial year in which the original assessment order is issued or treated as issued by the Commissioner; or
- One year from the end of financial year in which the amended assessment order is issued or treated as issued.

Ans.5 (a) For the purpose of minimum tax liability, turnover is defined as:

(i) The gross sales/gross receipts, exclusive of sales tax and federal excise duty or any trade discounts shown on invoices or bills, derived from the sale of goods and also excluding any income taken as deemed.
(ii) The gross fees for the rendering of services, including commissions.
(iii) The gross receipts from the execution of contracts.
(iv) The company's share of the above stated amounts of an association of persons of which the company is a member.

In case of (i), (ii) and (iii) above, it does not include any amount covered by final discharge of tax liability for which tax is separately paid or payable.

(b) Following persons are required to pay minimum tax:

(i) a resident company
(ii) an individual having turnover of Rs. 10 million or above in the tax year 2017 or in any subsequent tax year
(iii) an association of persons having turnover of Rs. 10 million or above in the tax year 2017 or in any subsequent tax year

(c) Where minimum tax exceeds the actual tax payable, the excess amount of tax paid shall be carried forward for adjustment against normal tax liability of the subsequent tax year.

However, the amount shall be carried forward and adjusted against tax liability for a maximum of five tax years immediately succeeding the tax year for which the amount was paid.

Ans.6

Cyma Associates
Computation of Sales Tax Payable/Refundable
For the tax period August 2017

	Taxable value	Sales tax rate	Sales Tax
	------------------ Rupees ------------------		
SALES TAX CREDITS (INPUT TAX)			
Purchases from registered suppliers (20,000,000−350,000−800,000)	18,850,000	17%	3,204,500
Purchases from unregistered suppliers	1,800,000	inadmissible	
Purchases of exempt goods from registered suppliers	400,000	inadmissible	
Purchases against which cash deposited in bank account	350,000	inadmissible	
Purchases against which discrepancy indicated by CREST	800,000	inadmissible	
Fixed assets (Machinery)	1,000,000	17%	170,000
Total input tax	23,200,000		3,374,500
Less: Inadmissible/unadjusted input tax **(W-1)**			(424,762)
Input tax for the month			2,949,738
Add: Excess of input tax over output tax of July 2017			75,000
Accumulated credit			3,024,738
SALES TAX DEBIT (OUTPUT TAX)			
Local taxable supplies - to registered suppliers (15,000,000+500,000−325,000−300,000)	14,875,000	17%	2,528,750
Local taxable supplies - to unregistered persons	2,800,000	17%	476,000
Local taxable supplies - according to agreement with Majeed Sons	225,000	17%	38,250
Local taxable supplies - to government official (325,000+125,000)	450,000	17%	76,500
Local taxable supplies - sale of tooth brushes	400,000	17%	68,000
	18,750,000		-
Exempt supplies - no effect of free samples given	1,700,000		-
Export (zero rated) (1,500,000−500,000)	1,000,000		
Output tax for the month	21,450,000		3,187,500
Less: Sales return	(756,000)	17%	(128,520)
Total supplies/Output tax for the month	20,694,000		3,058,980
		2,753,082	
Admissible credit (90% of output tax i.e. Rs. 2,753,082 (3,058,980×0.9) or input tax excluding Fixed Assets (3,024,738−148,601=2,876,137) whichever is lower.		2,876,137	(2,753,082)
			305,898
Input tax on fixed assets (170,000 x 18,750,000 / 21,450,000)			(148,601)
			157,297
Further tax on supplies to unregistered persons = 2,800,000×2%			56,000
Sales tax payable			213,297
Sales tax to be carried forward (3,024,738−2,753,082-148,601)			123,055
Sales tax refundable (3,374,500×1,000,000/21,450,000)			157,319
W-1: Apportionment of input tax			
Residual input tax			3,374,500
Exempt supplies and export sales (1,700,000+1,000,000)			2,700,000
Total supplies			21,450,000
Inadmissible input tax [(2,700,000/21,450,000)×3,374,500]			424,762

Ans.7 **(a)** Following exports are outside the purview of zero rating:

(i) Goods which are intended to be re-imported into Pakistan
(ii) Goods which have been entered for export under the Customs Act, 1969 but are not exported
(iii) Goods exported to a country specified by the Federal Government, by Notification in the official gazette.

(b) There are two types of refunds

(i) Refund of input tax in excess of 90% of output tax ; and
(ii) Refund of input tax related to zero ratings and exports.

In case of (i) a registered person would be required to submit a statement along with annual audited accounts, duly certified by the auditors, showing value additions less than the limit prescribed.

The refund of input tax shall be made on yearly basis in the second month following the end of the financial year of registered person.

In the case of (ii) the refund claim shall have to file in such manner and subject to such conditions as the Board may, by notification in the official gazette specify.

(c) A revised return may be filed to correct any omission or wrong declaration made in a return subject to approval of the Commissioner Inland revenue having jurisdiction within 120 days of filing of return.

(d) Monthly adjustment of input tax claimed by a registered person is treated as a provisional adjustment and at the end of each financial year, a final adjustment is made on the basis of taxable and exempt supplies made during the course of that year.

(e) If there is a change in the rate of tax,

- a taxable supply made by a registered person shall be charged to tax at such rate as in force at the time of supply.
- imported goods shall be charged to tax at such rate as is in force:

  - in case the goods are entered for home consumption, on the date on which a goods declaration is presented.
  - in case the goods are cleared from warehouse, on the date on which a goods declaration for clearance of such goods is presented.

- where a goods declaration is presented in advance of the arrival of the conveyance by which the goods are imported, the tax shall be charged as is in force on the date on which the manifest of the conveyance is delivered.
- where the tax is not paid within seven days of the presenting of the goods declaration the tax shall be charged at the rate as is in force on the date on which tax is actually paid.

If there is a change in the rate of tax during a tax period, a separate return has to be furnished in respect of each portion of the tax period showing the application of different rates.

Ans.8 (a) Pillars of tax administration

Pillars of tax administration which safeguard the interest of taxpayers and avoid abuse of powers by the tax administration are as follows:

(i) **Fairness**
Strive to be impartial, fair, neutral and consistent in administering the law without regard to race, social or economic circumstances.

(ii) **Transparency**
All proceedings must be transparent and must be seen as transparent.

(iii) **Equity**
Treating all tax payers fairly. Refraining from unduly pressurising a tax payers or a body of tax payers merely to achieve tax targets.

(iv) **Accountability**
There must be a strong system of accountability for wrong doers which should curb corruption, nepotism and maladministration.

(b)

Tax Evasion	Tax Avoidance
Attempts to minimise a taxpayer's liability through illegal means is called Tax Evasion.	Attempts to minimise a tax payer's liability through legal means and without violating tax laws is called Tax Avoidance.
Example of tax evasion include deliberately concealing the true state of affairs to the tax authorities to reduce tax liability and dishonest tax reporting.	Examples of tax avoidance involve using tax deductions, changing one's business structure through incorporation. Establishing companies in tax heavens through legal means.

(c) Ethical issues facing tax administration in the discharge of their duties are:

(i) Acceptance of gifts
(ii) Conflict of interest
(iii) Selective application of the law/ or inconsistency in applying the law
(iv) Political influence
(v) Confidentiality/secrecy
(vi) Discretion
(vii) Corruption
(viii) Lack of autonomy

(THE END)

The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examinations

6 March 2017
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Mushtaq is a sole proprietor of Mushtaq Enterprises (ME) engaged in the business of manufacturing of different products. ME's profit and loss account shows profit before taxation of Rs. 1.8 million for the year ended 30 June 20X7. A review of ME's records has revealed the following information.

(i) ME employs five salesmen. Rs. 22,000 per month were paid to each salesman in cash which includes reimbursement of Rs. 6,000 per month incurred on entertainment of customers at the business premises.

(ii) Administrative expenses include Rs. 150,000 which were paid to a research institute in China for the purpose of developing a new product.

(iii) Accounting loss on the sale of patents was Rs. 65,000. The tax written down value of these patents at the beginning of the year was Rs. 430,000 and these were sold for Rs. 524,000. Amortization charged to the profit and loss account on these patents for the current year was Rs. 25,000.

(iv) Receivables from Atif and Aslam which had been written off in the previous year were recovered. Details are as follows:

	Atif	**Aslam**
	------ Rupees ------	
Claimed bad debts in last tax return	800,000	1,200,000
Allowed by tax authorities last year	550,000	600,000
Amount recovered during the year	700,000	400,000

(v) ME has opened a sales office in Dubai. In this respect, furniture costing Rs. 850,000 with written down value (WDV) of Rs. 650,000 was shifted to Dubai office. The tax WDV of the furniture at the beginning of the year was Rs. 610,000.

(vi) Accounting depreciation for the year is Rs. 580,450. However, no depreciation has been provided on the following fixed assets purchased on 1 March 20X7:

	Rupees
Furniture	200,000
Used machinery imported from Germany	500,000

(vii) Tax depreciation for the year, prior to the adjustments mentioned in (vi) above, amounted to Rs. 456,400.

(viii) Advance tax paid u/s 147 was Rs. 200,000.

(ix) The assessed business losses of tax year 20X1 brought forward in year 20X7 are Rs. 830,000. These include unabsorbed tax depreciation amounting to Rs. 705,000.

Other transaction of Mushtaq

On 1 June 20X7, he sold 6,000 shares for Rs. 432,000 out of 15,000 shares which he received on 1 May 20X4, on the death of his father. The fair market value of shares on the date of transfer to Mushtaq was Rs. 25 per share.

Required:

Under the provisions of Income Tax Ordinance, 2001 and rules made thereunder, compute taxable income and net tax payable by or refundable to Mushtaq for the year ended 30 June 20X7. **(16)**

Q.2 (a) Explain the term 'disposal of assets' as referred to in the Income Tax Ordinance, 2001. **(05)**

(b) Saleha is a resident person. She disposed of the following assets during the tax year 20X7.

(i) A painting which she inherited from her father was sold for Rs. 1,250,000. The market value of the painting at the time of inheritance was Rs. 1,550,000. The painting was purchased by her father for Rs. 1,000,000. **(02)**

(ii) She sold jewellery for Rs. 2,300,000 which was purchased by her husband in March 20X5 for Rs. 1,300,000 and gifted to her on the same date. **(02)**

(iii) She disposed of her car for Rs. 1,800,000. The car was being used for the purposes of her business. The tax written down value of the car at the beginning of tax year 20X7 was Rs. 1,600,000. The rate of depreciation for tax purposes is 20%. **(02)**

(iv) On 20 October 20X6 she sold a dining table to Faheem for Rs. 18,000 which she had purchased on 15 May 20X5 for Rs. 15,000 for her personal use. **(02)**

Required:
Under the provisions of the Income Tax Ordinance, 2001, discuss the taxability of each of the above transactions in the context of capital gain/loss.

Q.3 (a) On 1 June 20X6 Dawood and Dewan jointly purchased a bungalow for Rs. 35 million. They paid the amount in the ratio of 65:35 respectively. To arrange funds for the deal, Dawood borrowed Rs. 3,000,000 in cash from Shameem who is in the business of lending money. The rate of interest is agreed @ 20% per annum.

On 1 July 20X6, the house was let out to a company at annual rent of Rs. 4,500,000 inclusive of an amount of Rs. 75,000 per month for utilities, cleaning and security. For providing these services Dawood and Dewan paid Rs. 35,000 per month. During the tax year 20X7 they also paid Rs. 10,000 as collection charges and Rs. 230,000 for administering the property.

Required:
Compute taxable income of Dawood and Dewan under appropriate heads of income for the tax year 20X7. **(08)**

(b) Najam had purchased a house in 20X2 for Rs. 20 million.

On 1 July 20X6, Najam entered into an agreement with Zameer for sale of the house for Rs. 25 million. As per the terms of the agreement, Najam received Rs. 5 million on the day the contract was signed and balance amount was to be paid on 30 September 20X6. However, due to financial difficulties, Zameer failed to pay the balance amount on the due date and consequently, Najam forfeited the advance in accordance with the terms of the agreement.

On 15 February 20X7 Najam sold the house to Farid for Rs. 30 million.

Required:
Advise Najam about the taxability of the above transaction under the Income Tax Ordinance, 2001. **(04)**

Q.4 (a) State the duties of National Finance Commission. **(04)**

(b) List the taxes and duties which may be raised under the authority of Parliament. Also list various types of taxes which are covered under the scope of legislation of the Provinces. **(06)**

Q.5 (a) List the persons who are required to file a tax return under the provisions of the Income Tax Ordinance, 2001. **(06)**

(b) In the light of the provisions of the Income Tax Ordinance, 2001:

(i) Identify the circumstances under which the Commissioner of Income Tax may require a person to furnish a return of income for a period of less than twelve months. **(03)**

(ii) State the consequences if a person fails to furnish the return as required in (i) above. **(03)**

Q.6 Zahid, the sole proprietor of FG and company, is a resident individual and is in the process of filing his wealth statement for the tax year 20X7. The relevant information is as under:

(i) Assets and liabilities disclosed in the wealth statement for the tax year 20X6 were as follows:

	Rupees
Assets	
Agriculture land in Hyderabad	5,000,000
Residential property in DHA Karachi	3,000,000
Investment in shares of listed companies	1,100,000
Business capital – FG & Co.	4,000,000
Motor vehicle	1,540,000
Cash at bank	600,000
Cash in hand	300,000
	15,540,000
Liabilities	
Bank loan	(1,500,000)
Net assets	**14,040,000**

(ii) Details relating to FG & Co. are as follows:

	Rupees
Income from business for the tax year 20X7	2,540,000
Drawings during the year	450,000

(iii) Balance of cash in hand and at bank, as on 30 June 20X7 amounted to Rs. 157,500 and Rs. 730,000 respectively.

(iv) Transactions carried out by Zahid during the year were as follows:

- Paid an advance of Rs. 1,000,000 against purchase of a bungalow for Rs. 10,000,000.
- Sold shares of a listed company for Rs. 350,000. The shares were purchased on 1 May 20X6 for Rs. 50,000. Capital gain tax collected by NCCPL amounted to Rs. 37,500.
- Gifted shares of a listed company to his brother. The shares were purchased by Zahid in 20X2 at a cost of Rs. 100,000 whereas market value of the shares at the time of gift was Rs. 150,000.
- Paid Rs. 200,000 towards principal amount of the bank loan.
- Personal expenses amounted to Rs. 2,075,000.
- Net receipts against agricultural income amounted to Rs. 2,500,000.

Required:
Prepare Zahid's wealth statement and wealth reconciliation statement for the tax year 20X7. **(07)**

Q.7 Jahangir Ali (JA) is registered under the Sales Tax Act 1990. JA runs multiple businesses. Following information has been extracted for the month of February 2017:

	Rupees
Supplies	
Taxable goods exported to Qatar	100,000
Taxable goods to registered customers	750,000
Taxable goods to unregistered customers	550,000
Purchases	
Taxable goods from registered suppliers	3,000,000
Exempt goods from registered suppliers	70,000
Taxable goods from unregistered suppliers	95,000

The following further information is available:

(i) Taxable goods supplied to registered customers include goods amounting to Rs. 300,000 supplied to an associated company at a special discount of 25%.

(ii) Taxable goods supplied to unregistered customers include goods worth Rs. 100,000 supplied to Saleem Brothers (SB). JA did not charge any sales tax from SB as it has submitted an undertaking that it is a cottage industry and exempt from sales tax under the Sixth Schedule of the Sales Tax Act, 1990.

(iii) Taxable goods purchased from registered suppliers include:
- goods worth Rs. 320,000 purchased from Akram Limited who was blacklisted on 25 February 2017 due to issuance of flying invoices.
- goods purchased from ZA Traders amounting to Rs. 30,000. ZA Traders did not declare this amount in its tax return for the month of February 2017.
- a new machine purchased for Rs. 500,000 which was commissioned into operation during February 2017.
- office equipment of Rs. 200,000, purchased for the warehouse.

(iv) Goods pledged with a bank were sold by the bank in an auction for Rs. 1,000,000. The normal selling price of these goods was Rs. 1,200,000.

(v) Excess of input tax over output tax brought forward from January 2017 was Rs. 110,000.

Rate of sales tax is **17%**. All figures are exclusive of sales tax.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by or refundable to JA and the amount of sales tax to be carried forward, if any, for the tax period February 2017. **(17)**

Q.8 (a) Under the provisions of Sales Tax Act, 1990 and Rules made thereunder, identify the circumstances in which:

(i) a registered person is not allowed to reclaim or deduct input tax paid. **(06)**

(ii) a registered person may be liable for deregistration. **(03)**

(b) On 2 June 2016, Abid Limited inadvertently issued a tax invoice with an incidence of sales tax amounting to Rs. 25,000 as against the applicable tax of Rs. 45,000. The error was detected on 15 February 2017 i.e. after expiry of 180 days.

Advise Abid Limited in the light of Sales Tax Rules, 2006. **(04)**

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001
THE FIRST SCHEDULE

Tax Rates for Every Individual and Association of Person Except for Salaried Taxpayer

S. No.	Taxable income	Rate of tax
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 7,000 + 10% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,500,000	Rs. 32,000 + 15% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 144,500 + 20% of the amount exceeding Rs. 1,500,000
6.	Exceeds Rs. 2,500,000 but does not exceed Rs. 4,000,000	Rs. 344,500 + 25% of the amount exceeding Rs. 2,500,000

Capital Gains on disposal of Securities

S. No.	Period	Rate of tax
1.	Where holding period of a security is less than twelve months	15%
2.	Where holding period of a security is twelve months or more but less than twenty-four months	12.5%
3.	Where holding period of a security is twenty-four months or more but the security was acquired on or after 1st July, 2012	7.5%

Capital Gains on disposal of Immovable Property

S. No.	Period	Rate of tax
6.	Where holding period of immovable property is up to three years	5%
7.	Where holding period of immovable property is more than three years	0%

THE THIRD SCHEDULE
Part I
Depreciation Rates

1.	Building (all types)	10%
2.	Furniture and fittings	15%
3.	Plant and machinery	15%
4.	Motor vehicles (all types)	15%
5.	Computer hardware	30%

Part II
Initial Allowance and First Year Allowance

The rate of initial allowance shall be 25% for plant and machinery and 15% for building.

Ans.1 Mushtaq Enterprises
Computation of total income, taxable income and net tax payable/refundable
For tax year 20X7

Income from Business:	**Rupees**
Profit before taxation	1,800,000
Add: Inadmissible expenses/admissible income	
Salary paid to salesmen [5×(22,000–6,000)×12]	960,000
Entertainment expenditures	-
Research expenditure incurred outside Pakistan	150,000
Accounting loss on the sale of patents	65,000
Amortisation charged on patents for the year	25,000
Gain on sale of patents (524,000 – 430,000)	94,000
Bad debts recovered: Atif [700,000 – (800,000 – 550,000)]	450,000
Accounting depreciation	580,450
Transfer of furniture to Dubai (850,000–610,000)	240,000
Less: Admissible expenses/inadmissible income	
Bad debts recovered: Aslam [1,200,000–600,000–400,000]	(200,000)
Tax depreciation **(W-1)**	(667,650)
	3,496,800
Less:	
B/f business loss	(125,000)
Unabsorbed tax depreciation – brought forward	(705,000)
	(830,000)
Total business income for the year	2,666,800
Capital Gain (Separate block income)	
Gain on the sale of 6,000 shares [432,000 – (6,000 × 25)]	282,000
Total income for the year	2,948,800
Less: Separate block income	(282,000)
Taxable income for the year under NTR	2,666,800
Computation of net tax liability	
Tax on Rs. 2,500,000	344,500
Tax on income exceeding Rs. 2,500,000 @ 25%	41,700
Income tax payable on separate block income @ 7.5%	21,150
	407,350
Less: Tax paid under	(200,000)
Income tax payable with the return	207,350
W-1: Computation of tax depreciation	
Depreciation on furniture (200,000 × 15%)	30,000
Used imported machine	
Initial allowance (500,000 × 25%)	125,000
Depreciation [(500,000 – 125,000) × 15%]	56,250
Depreciation on additions	211,250
Depreciation for the year	456,400
	667,650

Ans.2 **(a)** A person who holds an asset shall be treated as having made a disposal of the asset at the time the person parts with the ownership of the asset, including when the asset is:

- sold, exchanged, transferred or distributed; or
- cancelled, redeemed, relinquished, destroyed, lost, expired or surrendered.

The transmission of an asset by succession or under a will shall be treated as a disposal of the asset by the deceased at the time asset is transmitted.

The application of a business asset to personal use shall be treated as a disposal of the asset by the owner of the asset at the time the asset is so applied.

Where a business asset is discarded or ceases to be used in business, it shall be treated to have been disposed of.

A disposal shall include the disposal of a part of an asset.

(b) (i) Since Saleha inherited paintings from her father, the fair market value of the painting on the date of its acquisition/transfer would be treated to be its cost. Hence, cost of the painting would be Rs. 1,550,000. and there is a loss of Rs. 300,000. But, according to the ITO-2001, no loss can be recognized on disposal of painting.

(ii) The cost of the Jewellery would be Rs. 1,300,000 i.e. the value thereof at the time of gift. Therefore, the gain of Rs. 1,000,000 should be recognized. However, as the holding period of Jewellery is more than one year, the taxable gain will be restricted to 75% i.e. Rs. 750,000

(iii) The car sold by Saleha was being used by her for business purposes and therefore depreciation was also being charged on it. However, depreciable assets are specifically excluded from the definition of capital assets. Therefore, no capital gain or loss would arise on the disposal of car.

(iv) No capital gain/loss will arise as any movable property held for personal use by the person is excluded from the definition of capital assets.

Ans.3 **(a)**

Taxable income of Dawood	**Rupees**
Income from property (Rs. 3,600,000 **(W-1)** × 65%)	2,340,000
Income from other sources (Rs. 480,000 **(W-2)** × 65%)	312,000
Income from other sources	3,000,000
	5,652,000
Less: Separate block of income - Income from property	(2,340,000)
	3,312,000

Taxable income of Dewan	
Income from property (Rs. 3,600,000 **(W-1)** × 35%)	1,260,000
Income from other sources (Rs. 480,000 **(W-2)** × 35%)	168,000
	1,428,000
Less: Separate block of income - Income from property	(1,260,000)
	168,000

W-1: Computation of joint taxable income under income from property

Income from property:	
Rent received by joint owners for 12 months	4,500,000
Less: Amount received on account of utilities, cleanliness & security (75,000×12)	(900,000)
Rent chargeable to tax	3,600,000
Deduction of expenses against income from property is allowed only for company therefore no deduction is allowed [15A (1)]	

W-2: Computation of income from other sources

Income from other sources	
Amount received on account of utilities, cleanliness & security (75,000×12)	900,000
Less: Actual expenses incurred (35,000×12)	(420,000)
	480,000

(b)

- The amount of Rs. 5 million forfeited by Najam in accordance with the terms of the agreement for the sale of his house to Zameer is to be treated as rent received.

- Najam should recognize the gain of Rs. 10,000,000 (30,000,000 – 20,000,000) on disposal of the house to Farid under the head 'Capital Gain'.

  Since the disposal was made after holding the house for more than three years as it was acquired in 2012, therefore no tax is payable under the law.

Ans.4 (a) The duty of the National Finance Commission is to make recommendations to the President as to:

(i) the distribution between the Federation and the Provinces of the net proceeds of the taxes;
(ii) the making of grants-in-aid by the Federal Government to the Provincial Governments;
(iii) the exercise by the Federal Government and the Provincial Governments of the borrowing powers conferred by the Constitution; and
(iv) any other matter relating to finance referred to the Commission by the President.

(b) Following taxes may be raised under the authority of the Parliament:

(i) taxes on income, including corporation tax, but not including taxes on income consisting of remuneration paid out of the Federal Consolidated Fund;
(ii) taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed;
(iii) export duties on cotton, and such other export duties as may be specified by the President;
(iv) such excise duties as may be specified by the President; and
(v) such other taxes as may be specified by the President.

Powers of the Provinces to legislate on taxes
Following taxes are covered in the scope of legislation of Provinces:

- Agriculture income tax

- Sales tax on services
- Taxes on transfer of immoveable property
- Professional tax
- Tax on luxury houses
- Tax on registration of luxury vehicles
- Property tax

Ans.5 (a) Persons liable to file a tax return

The following persons are required to furnish a return of income for a tax year:

(i) Every company
(ii) Every person (other than a company) whose taxable income for the year exceeds the maximum amount that is not chargeable to tax
(iii) Any non-profit organisation
(iv) Any welfare institution

In addition to the above, return is also required to be filed by a person who,-
(i) has been charged to tax in respect of any of the two preceding tax years;
(ii) claims a loss carried forward for a tax year;
(iii) owns immovable property with a land area of two hundred and fifty square yards or more or owns any flat located in areas falling within the municipal limits existing immediately before the commencement of local government laws in the provinces; or areas in a cantonment; or the Islamabad capital territory.
(iv) owns immoveable property with a land area of five hundred square yards or more located in a rating area;
(v) owns a flat having covered area of two thousand square feet or more located in a rating area;
(vi) owns a motor vehicle having engine capacity above 1000 CC;
(vii) has obtained National Tax Number;
(viii) is the holder of commercial or industrial connection of electricity where the amount of annual bill exceeds rupees five hundred thousand.
(ix) is a resident person registered with any chamber of commerce and industry or any trade or business association or any market committee or any professional body including Pakistan Engineering Council, Pakistan Medical and Dental Council, Pakistan Bar Council or any Provincial Bar Council, Institute of Chartered Accountants of Pakistan or Institute of Cost and Management Accountants of Pakistan.
(x) every individual whose income under the heading 'Income from business' exceeds Rs. 300,000 but does not exceed Rs. 400,000 is also required to file tax return.

(b) (i) The Commissioner may, by notice in writing, require the following persons or their representatives to furnish a return of income for a period of less than twelve months:
- a person who has died;
- a person who has become bankrupt or gone into liquidation;
- a person who is about to leave Pakistan permanently;
- where the Commissioner otherwise considers it appropriate to require such a return to be furnished.

(ii) If a person fails to furnish the return as required in (i) above then the Commissioner may, based on any available information or material and to the best of his judgment, make a provisional assessment of the taxable income of the person and issue a provisional assessment order specifying the taxable income and the tax due thereon.

The provisional assessment order is treated as the final assessment order after the expiry of forty five days from the date of service of order of provisional assessment.

Ans.6 Mr. Zahid
Wealth Statement
For the tax year 20X7

	2017 Rupees
Agriculture land in Hyderabad	5,000,000
Residential property in DHA Karachi	3,000,000
Investment in shares of listed companies (1,100,000–100,000–50,000)	950,000
Business capital FG & Co. (4,000,000+2,540,000–450,000)	6,090,000
Advance against bungalow	1,000,000
Motor Vehicle	1,540,000
Cash at banks	730,000
Cash	157,500
Total	18,467,500
Less: Bank loan – closing balance	(1,300,000)
Wealth as on 30 June 20X7	17,167,500
Wealth reconciliation statement	
Wealth as on 30 June 20X7	17,167,520
Wealth as on 30 June 20X6	14,040,000
Net increase in wealth	3,127,500
Inflows	
Income from business	2,540,000
Agriculture income – Exempt	2,500,000
Capital gain [(350,000 – 50,000 – 37,500)]	262,500
	5,302,500
Outflows	
Gift to brothers – Listed company shares and shares sold	100,000
Personal expenses	2,075,000
	2,175,000
Net increase in wealth	3,127,500

Ans.7

Jawwad Associates (JA)
Computation of Net Sales Tax Liability
For the tax period February 2017

SALES TAX CREDIT (INPUT TAX)		**Taxable value**	**Sales Tax @ 17%**
Taxable goods from registered suppliers (3,000,000–320,000–30,000–500,000–200,000)		1,950,000	331,500
Exempted goods from registered suppliers		70,000	-
Taxable goods from unregistered suppliers		95,000	-
Fixed assets (Machinery)		500,000	85,000
			416,500

Less: Inadmissible/un-adjustable input tax **(W-1)**			(15,426)
Admissible input tax			401,074
Add: Excess of input tax over output tax			110,000
Input Tax for the month (Accumulated credit)			**511,074**
SALES TAX DEBIT (OUTPUT TAX)			
Taxable goods supplied to Qatar (zero rated)		100,000	-
Taxable goods to registered persons (750-300)		450,000	76,500
Taxable goods to an associated undertaking at a special discount (300/0.75)		400,000	68,000
Taxable goods supplied to unregistered customers		550,000	93,500
Goods disposed of by the bank		1,200,000	204,000
Total supplies / Output tax for the month		2,700,000	442,000
Input tax on fixed assets [(2,700,000 – 100,000) /2,700,000] × 85,000)			(81,852)
			360,148
Admissible credit (90% of output tax i.e Rs. 324,133 (360,148 × 0.9) or input tax excluding Fixed Assets (511,074 – 81,852 = 429,222) whichever is lower			(324,133)
Excess of output tax over input tax			36,015
Add: Further tax on supplies made to unregistered person [550,000 × 2%]			11,000
Sales tax payable			47,015
Input tax to be carried forward (429,222 – 324,133)			105,089
Sales tax refund on zero rate supplies **(W-1)**			15,426
W-1: Apportionment of input tax			
Total supplies			2,700,000
Zero rated supplies			100,000
Input tax			416,500
Inadmissible input tax relating to zero rate supplies (100,000/2,700,000×416,500)			15,426

Ans.8 **(a)** (i) A registered person shall not be entitled to reclaim or deduct input tax paid on:

- the goods or services used or to be used for any purposes other than for taxable supplies made or to be made by him;
- the goods on which extra amount of tax is payable under sub-section (5) of section 3;
- any other goods or services which the Federal Government may by a notification in the official Gazette specify;
- the goods or services in respect of which sales tax has not been deposited in the Government treasury by the respective supplier;
- goods which are destroyed with the permission of the collector of sales tax
- purchase from suppliers who are black listed by the Commissioner
- if the payment in case of a transaction on credit is not transferred within 180 days of issue of the tax invoice
- if payment is not made for the supplies in the business bank account of the supplier
- fake invoices;
- purchases made by a registered person in case he fails to provide information relating to his imports, purchases, sales etc. as required by the Board.
- purchases in respect of which a discrepancy is indicated by CREST or input tax of which is not verifiable in the supply chain;
- goods and services not related to the taxable supplies made by the

registered person;

- goods and services acquired for personal or non-business consumption;
- vehicles falling in Chapter 87 of the First Schedule to the Customs Act, 1969.
- services in respect of which input tax adjustment is barred under the respective provincial sales tax law;
- import or purchase of agricultural machinery or equipment subject to sales tax at the rate of 7% under Eighth Schedule to this Act; and
- from the date to be notified by the Board, such goods and services which, at the time of filing of return by the buyer, have not been declared by the supplier in his return or he has not paid amount of tax due as indicated in his return.
- the goods which are subject to extra tax in addition to normal tax payable at 17%.
- gifts and giveaways.

(ii) The following registered persons may apply for deregistration:

- Who ceases to carry on his business
- Whose supplies become exempt from tax

The Commissioner may de-register a person if that person fails to file tax return for six continuous months.

(b) Time limitation of 180 days shall not apply in the given case as it is applicable only in the case of decrease in output tax and increase in input tax. The above increase of output tax may be declared without any time limitations.

Since Abid Limited has already accounted for the output tax in the sales tax return for the supplies, it can issue a debit note in the month of February 2017 when the error was detected, and increase the amount of output tax in the return for February 2017 by Rs. 20,000.

(THE END)

The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examinations

5 September 2016
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Bader is working as General Manager Finance with HiFi Limited (HFL) for the past two years. The details of his monthly emoluments during the year ended 30 June 2016 are as under:

	Rupees
Basic salary	250,000
Medical allowance	28,000
House rent allowance	120,000

In addition to above, Bader was also provided the following:

(i) Rs. 900,000 for signing a bond with HFL. According to the bond Bader would not resign from his employment before the expiry of 30 June 2019.

(ii) Company maintained car for both official and private use. The car was purchased on 1 August 2015 at a fair market value of Rs. 1,500,000.

(iii) On 1 January 2016 HFL sold an item of inventory to Bader for Rs. 12,000. The net realizable value of the item of inventory at the end of 31 December 2015 and 30 June 2016 was Rs. 22,000 and Rs. 24,000 respectively. HFL had acquired it in July 2014 at a cost of Rs. 35,000.

(iv) An option was granted to Bader in August 2014 to acquire 2,500 shares in HFL's parent company, Mamoo plc. (MP), listed on Hong Kong stock exchange. However, the option was exercisable after completion of one year of service with HFL. Bader paid an amount equivalent to PKR 200,000 to acquire the option when the fair market value of the option was PKR 250,000.

On 1 September 2015 he paid an amount equivalent to PKR 300,000 to acquire the shares in MP. The shares were issued to him on 15 September 2015 when the market value of each share was equivalent to PKR 375.

On 15 June 2016 Bader sold 2,000 shares in MP and received net proceeds equivalent to PKR 875,000 in his bank account in Pakistan. This amount was received after deduction of bank charges of PKR 5,000 and brokerage commission equivalent to PKR 10,000.

Other information relevant to tax year 2016 is as under:

(i) On 1 July 2015 Bader received following payments from his previous employer Sultan Hospital Limited:
- Rs. 600,000 in respect of termination benefits under an agreement.
- Rs. 485,000 against gratuity under an unapproved scheme.

(ii) On 1 November 2015 Bader fell ill and was admitted to Sultan Hospital Limited. The hospital incurred Rs. 65,000 on his treatment but did not charge anything to Bader.

(iii) On 1 December 2015 he paid a premium of Rs. 300,000 on a life insurance policy.

(iv) On 1 January 2016 Bader purchased 35,000 listed shares in Muft Limited (ML) at a price of Rs. 25 per share. On 20 March 2016 he fully subscribed 15% right shares offered by ML to its existing shareholders at a price of Rs. 20 per share.

(v) Withholding tax deducted from Bader's salary during tax year 2016 amounted to Rs. 1,105,000.

(vi) His total assessed taxable income and total taxes paid thereon during the three preceding tax years amounted to Rs. 10,500,000 and Rs. 1,260,000 respectively.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the taxable income and net tax payable by or refundable to Bader for tax year 2016. **(15)**
Note: Show all relevant exemptions, exclusions and disallowances. Tax rates are given on the last page.

Q.2 Maroof filed his return of income for tax year 2015 on 30 September 2015. On 15 August 2016 he received a show cause notice from the Commissioner Inland Revenue u/s 122 for amendment of the assessment order issued on self-assessment basis.

Required:
Under the provisions of the Income Tax Ordinance, 2001 briefly describe:
(a) the circumstances under which an assessment order treated as issued on self-assessment basis may be amended by the Commissioner. **(04)**
(b) the situations in which the Commissioner may be barred from amending the original assessment order. **(04)**

Q.3 (a) The Income Tax Department initiating a proceeding against Mobeen, issued a demand note requiring him to pay the outstanding amount of his tax liability for tax year 2015 along with default surcharge. However, before settlement of his tax liability, Mobeen died in a car accident.

Required:
Under the provisions of the Income Tax Ordinance, 2001:
(i) describe whether tax authorities would be able to recover the amount of tax after Mobeen's death and what would be the extent of such recovery. **(03)**
(ii) comment on the status of the proceedings initiated against Mobeen. **(02)**

(b) Under the provisions of the Income Tax Ordinance, 2001 describe the following:

(i) meaning of the term 'Associates'. **(02)**
(ii) circumstances in which a member of an association of persons and the association may be regarded as associates. **(02)**
(iii) situation in which members of an association of persons may not be regarded as associates. **(02)**

(c) List the persons who may be granted immunity from filing of tax return u/s 114 of the Income Tax Ordinance, 2001 solely by reason of owning immovable property with a land area of two hundred and fifty square yards or more or any flat located in areas falling within the municipal limits. **(03)**

Q.4 On 1 July 2015 Farrukh borrowed Rs. 8,000,000 from Star Bank Limited and acquired a plot of land in Hub Industrial Zone for Rs. 6,500,000. He invested the rest of the loan in a business venture with his friend. The above loan carries mark-up at a rate of 12% per annum and is repayable in eight equal quarterly instalments starting from 1 July 2016. On 1 August 2015 Farrukh decided to sell the plot of land to Zulfiqar Motors for Rs. 10,000,000 and received a deposit of Rs. 500,000 from them. On 15 August 2015 Farrukh forfeited the deposit on refusal of Zulfiqar Motors to purchase the plot of land.

On 1 September 2015 Farrukh let out the plot of land to his friend Atif at a monthly rent of Rs. 150,000. He received an un-adjustable deposit of Rs. 200,000 from Atif and paid Rs. 80,000 for levelling the ground, Rs. 50,000 as ground rent, Rs. 12,000 as insurance premium against the risk of damage or destruction by water logging and Rs. 140,000 against rent collection charges. Farrukh had paid Rs. 25,000 to a firm of professional valuers which determined the annual rental value of the plot of land at Rs. 2,160,000.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute under the relevant head of income, taxable income of Farrukh for tax year 2016. **(12)**

Q.5 Samaaj Associates (SA) is registered under the Sales Tax Act, 1990 and is engaged in the business of manufacturing, trading and export of electronic, chemical and other consumer goods. Following information has been extracted from SA's records for the month of August 2016:

	Rupees
Supplies:	
To registered persons	2,500,000
To un-registered persons	875,000
To persons registered as exporter	625,000
Purchases:	
Raw material from registered persons	930,000
Finished goods from un-registered persons	725,000
Packing material from registered persons	510,000
Local machinery from un-registered persons	360,000
Imports – finished goods	472,000

Packing material from registered persons include material worth Rs. 150,000 which was used for packing electric motors. On 31 August 2016 these motors were still part of SA's unsold stock.

Following transactions pertaining to August 2016 are not included in the above table:

(i) Sales tax of Rs. 70,000, Rs. 45,000 and Rs. 68,000 was paid in cash on electricity, gas and telephone bills respectively.
(ii) SA purchased high quality cables and wires worth Rs. 250,000 from a registered supplier for the installation of local machinery purchased from un-registered suppliers.
(iii) Three cartons of imported shampoo, falling under third schedule, were supplied to un-registered distributors at a price of Rs. 110,000 per carton. The distributors normally supply such shampoo to retailers at a price of Rs. 135,000 per carton.
(iv) Five electric kettles worth Rs. 75,000 were purchased for use in the offices of factory manager and first line-supervisors of production workers.
(v) On 5 August 2016 SA received advance of Rs. 600,000 against supply of electric shavers to Bari Electronics. SA agreed to deliver the goods in September 2016.
(vi) On 25 August 2016 SA issued discount coupons worth Rs. 450,000 to its customers for participating in grand annual sales exhibition to be held in December 2016.

Other related information is as under:

(i) On 10 February 2016 SA purchased liquid nitrogen worth Rs. 300,000 from Mughal Chemicals (MC), a registered supplier, on credit. On 15 August 2016 SA paid the outstanding amount to MC by way of a crossed cheque drawn on SA's bank account.
(ii) In April 2016 SA inadvertently charged sales tax of Rs. 58,000 instead of 85,000 on supply of chemicals to one of its registered customers. So far, SA has not obtained permission from the Commissioner Inland Revenue for revision of return.
(iii) In July 2016 SA claimed input tax of Rs. 80,000 on purchase of hydrochloric acid from JB Traders. The supplier has not yet deposited the amount of sales tax collected from SA in Government treasury.

In July 2016 the excess of input tax over output tax amounted to Rs. 20,000. Whereas, unadjusted input tax in excess of 90% of output tax amounted to Rs. 10,000.

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of **17%**.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by or refundable to SA and the amount of sales tax to be carried forward, if any, for the tax period August 2016. **(18)**

Note: Show all relevant exemptions, exclusions and disallowances.
Ignore value addition tax payable at import stage.

Q.6 (a) Under the Sales Tax Act, 1990 and Rules made thereunder, briefly describe the concept of 'Residual input tax'. How it differs from 'Residual input tax credit'? **(03)**

(b) Under the provisions of the Sales Tax Act, 1990 enumerate any **four** features distinguishing the concept of 'Zero rating' from 'Exempt supply'. **(04)**

(c) Identify the records which a registered person making taxable/exempt supplies is required to maintain at his business premises or registered office under the Sales Tax Act, 1990. ***(Note: details of contents not required)*** **(04)**

Q.7 (a) List any **seven** responsibilities of tax administrators emanating from best ethical practices. **(07)**

(b) List any **five** types of taxes which can be imposed by the Federation as provided in the Federal legislative list under the Constitution of Pakistan. **(05)**

Q.8 On 1 July 2015 Mehreen joined a local newspaper as an investigative journalist at a salary of Rs. 300,000 per month. Tax deducted u/s 149 from her salary amounted to Rs. 40,000 per month.

Following are the details of her income received from Germany; tax paid thereon and brought forward foreign losses for tax year 2016:

Heads of income	Foreign income/ (loss)	Foreign tax paid	Foreign losses brought forward
	-------------------- Rupees	--------------------	
Speculation business	600,000	110,000	(380,000)
Non-speculation business	1,480,000	187,600	-
Other sources	(1,500,000)	-	-
Capital gain	950,000	76,000	(1,800,000)

On 1 May 2016 Mehreen resigned from her current job and joined Akhbar Merhaba (AM), an Arabic newspaper in Dubai, as editor-in-chief on a monthly salary equivalent to PKR 1,200,000. AM paid 50% of her salary in Dubai and remitted the remaining 50% to her bank account in Pakistan through normal banking channel. Mehreen remained in Dubai during the rest of the tax year 2016.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the taxable income, net tax payable by or refundable to Mehreen for tax year 2016 and the amount of foreign losses or foreign tax credit, if any, to be carried forward. **(10)**
Note: Show all relevant exemptions, exclusions and disallowances. Tax rates are given on the last page.

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001
THE FIRST SCHEDULE
Tax Rates for Every Individual and Association of Person Except for Salaried Taxpayer

S. No.	Taxable income	Rate of tax
1.	Upto Rs. 400,000	0%
2.	Exceeds Rs. 400,000 but does not exceed Rs. 500,000	7% of the amount exceeding Rs. 400,000
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 7,000 + 10% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,500,000	Rs. 32,000 + 15% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 144,500 + 20% of the amount exceeding Rs. 1,500,000
6.	Exceeds Rs. 2,500,000 but does not exceed Rs. 4,000,000	Rs. 344,500 + 25% of the amount exceeding Rs. 2,500,000
7.	Exceeds Rs. 4,000,000 but does not exceed Rs. 6,000,000	Rs. 719,500 + 30% of the amount exceeding Rs. 4,000,000
8.	Above Rs. 6,000,000	Rs. 1,319,500 + 35% of the amount exceeding Rs. 6,000,000

Rates of Tax for Salaried Individuals

S. No.	Taxable income	Rate of tax
1.	Upto Rs. 400,000	0%
2.	Exceeds Rs. 400,000 but does not exceed Rs. 500,000	2% of the amount exceeding Rs. 400,000
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 2,000 + 5% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,400,000	Rs. 14,500 + 10% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,400,000 but does not exceed Rs. 1,500,000	Rs. 79,500 + 12.5% of the amount exceeding Rs. 1,400,000
6.	Exceeds Rs. 1,500,000 but does not exceed Rs. 1,800,000	Rs. 92,000 + 15% of the amount exceeding Rs. 1,500,000
7.	Exceeds Rs. 1,800,000 but does not exceed Rs. 2,500,000	Rs. 137,000 + 17.5% of the amount exceeding Rs. 1,800,000
8.	Exceeds Rs. 2,500,000 but does not exceed Rs. 3,000,000	Rs. 259,500 + 20% of the amount exceeding Rs. 2,500,000
9.	Exceeds Rs. 3,000,000 but does not exceed Rs. 3,500,000	Rs. 359,500 + 22.5% of the amount exceeding Rs. 3,000,000
10.	Exceeds Rs. 3,500,000 but does not exceed Rs. 4,000,000	Rs. 472,000 + 25% of the amount exceeding Rs. 3,500,000
11.	Exceeds Rs. 4,000,000 but does not exceed Rs. 7,000,000	Rs. 597,000 + 27.5% of the amount exceeding Rs. 4,000,000
12.	Exceeds Rs. 7,000,000	Rs. 1,422,000 + 30% of the amount exceeding Rs. 7,000,000

PRINCIPLES OF TAXATION
Suggested Answers
Certificate in Accounting and Finance – Autumn 2016

Ans.1

Bader
Computation of income tax liability
For the tax year 2016

		Rupees
Income from Salary:		
Basic Salary (250,000 × 12)		3,000,000
Medical allowance (28,000 × 12 – 3,000,000 × 10%)		36,000
House rent allowance (120,000 × 12)		1,440,000
Consideration for Bader's agreement to condition of employment		900,000
Perquisite representing car	**W-1**	68,648
Benefit on purchase of item of inventory (22,000 – 12,000)		10,000
Share option scheme [(375 × 2,500)– 200,000 – 300,000]		437,500
Termination benefits		600,000
Unapproved gratuity (485,000 – 75,000 exempt		410,000
Free medical treatment by SHL – exempt		-
Total income under the head salary		6,902,148
Capital Gain:		
Sale of 2,000 shares in MP (875,000 + 5,000 + 10,000)		890,000
Less: Cost of acquisition of shares [(200,000+300,000+437,500) × 0.8]		(750,000)
Net gain on disposal of shares		140,000
Taxable income		7,042,148
Computation of net tax liability:		
Total taxable income		7,042,148
Less: Separate block		
▪ Termination benefits		(600,000)
▪ Unapproved gratuity		(410,000)
(assuming Bader, by notice in writing to the Commissioner, would elect to be taxed on the basis of average rate of tax)		
Taxable income (excluding separate block income)		6,032,148
Tax on Rs. 4,000,000		597,000
Tax @ 27.5% on the amount exceeding Rs. 4,000,000 (6,032,148 – 4,000,000)		558,841
Total gross tax payable under NTR		1,155,841
Tax on termination benefits @ average rate (1,260K /10,500K = 12% × 600,000)		72,000
Tax on unapproved gratuity @ average rate (1,260K /10,500K = 12% × 410,000)		49,200
Total tax liability		1,277,041
Less: Tax credit: either of the following two amounts would be claimed		
Right shares in ML [(35,000 × 15% × 20) × 1,155,841 ÷ 6,032,148]	20,119	-
Investment in life insurance [(300,000 × 1,155,841 ÷ 6,032,148]	57,484	(57,484)
Total tax payable		1,219,557
Less: Taxes withheld at source from salary		(1,105,000)
Net tax payable		114,557

W-1 Perquisite representing car:

The perquisite shall be computed as below:	
FMV of the car	1,500,000
5% of the FMV (1,500,000 × 5%)	75,000
Restricted to the number of days it was used in the tax year (335 ÷ 366)	68,648

Ans.2 (a) Revision of assessment by the Commissioner:

An assessment order shall only be amended by the Commissioner where, on the basis of definite information acquired from an audit or otherwise, the Commissioner is satisfied that:-

(i) any income chargeable to tax has escaped assessment; or
(ii) total income has been under-assessed, or assessed at too low a rate, or has been the subject of excessive relief or refund; or
(iii) any amount under a head of income had been mis-classified.

The Commissioner may also amend the assessment if after making necessary enquiries he considers that the assessment order is erroneous in so far it is prejudicial to the interest of revenue.

(b) Situations in which the Commissioner may be barred from revising the assessment order.

The Commissioner shall not revise any assessment order:-

(i) after the expiry of five years from the end of the financial year in which the order was issued or treated as issued.
(ii) if an appeal against the order lies to the Commissioner (Appeals) or to the Appellate Tribunal and the time within which such appeal may be made has not expired; or
(iii) The order is pending in appeal before the Commissioner (Appeals) or has been made the subject of an appeal to the Appellate Tribunal.

Further an assessment shall not be amended unless the taxpayer has been provided with an opportunity of being heard.

Ans.3 (a) (i) Deceased individual:

Yes, the tax authorities would be able to recover the amount of outstanding liability from the legal representative of Mobeen.
The legal representative is liable for:-

- any tax that Mobeen would have become liable for if he had not died; and
- any tax payable in respect of the income of Mobeen's estate.

The liability of the legal representative shall be limited to the extent to which Mobeen's estate is capable of meeting the liability and such liability shall be the first charge on Mobeen's estate, in preference to any other outstanding liability of the deceased.

(ii) **Comment on the status of the proceedings:**

Any proceeding taken against Mobeen before his death shall be treated as taken against the legal representative and may be continued against him from the stage at which the proceeding stood on the date of Mobeen's death.

(b) (i) **Associates:**

Two persons are associate where the relationship between the two is such that one may reasonably be expected to act in accordance with the intentions of the other, or both persons may reasonably be expected to act in accordance with the intentions of a third person.

(ii) **Circumstances in which a member of an association of persons and the association may be regarded as associates:**

Where the member, either alone or together with an associate or associates under another application of section 85 of the Income Tax Ordinance, 2001, controls fifty per cent or more of the rights to income or capital of the association;

(iii) **Situation in which members of an association of persons may not be regarded as associates:**
Members of an association of persons may not be regarded as associates where the Commissioner is satisfied that neither person may reasonably be expected to act in accordance with the intentions of the other.

(c) Persons not liable to file tax return:
The following persons may be granted immunity from filing of tax return u/s 114 of the Income Tax Ordinance, 2001 solely by reason of owning immovable property with a land area of two hundred and fifty square yards or more or any flat located in areas falling within the municipal limits:
(i) a widow;
(ii) an orphan below the age of twenty-five years;
(iii) a disabled person; or
(iv) a non-resident person.

Ans.4

Farrukh
Computation of taxable income
For the tax year 2016

	Rupees
Income from property:	
Forfeiture of deposit	500,000
Rent of plot of land [higher of (2,160,000 ÷ 12 × 10) or (150,000 × 10)]	1,800,000
Gross rent	2,300,000
Amount not adjustable against the rent	-
(Nothing is to be included in the chargeable income as this provision of law is attracted where the owner of building and not land receives such amount.)	
Less:	
Repairs 1/5th of rent (leveling of ground)	-
(Admissible only against the rent of the building)	
Interest on loan [6,500,000 × 12%] × [10 ÷ 12]	(650,000)
(interest on only that portion of the loan which is utilized for the acquisition of land is admissible)	
Ground rent	(50,000)
Insurance premium *[not available on land]*	-
Rent collection charges (2,300,000 × 6%)	(138,000)
(Lower of actual expenditure or 6% of rent is admissible)	
Fee paid to professional valuer- inadmissible	-
	(838,000)
	1,462,000

Ans.5

Samaaj Associates (SA)
Computation of Net Sales Tax Liability
For the tax period August 2016

SALES TAX CREDIT (INPUT TAX)	**Taxable Value**	**Sales Tax Rate**	**Amount of Sales Tax**
Raw material from registered persons	930,000	17%	158,100
Finished goods from un-registered persons	725,000	inadmissible	-
Packing material from registered persons	510,000	17%	86,700
Local machinery from un-registered persons	360,000	inadmissible	-
Imports – finished goods	472,000	17%	80,240
Sales tax paid on utility bills [70,000+45,000+68,000]	-	-	183,000
Purchase of cables and wires	250,000	17%	42,500
Purchase of electric kettles	75,000	inadmissible	-
Purchase of liquid nitrogen [more than 180 days]	300,000	inadmissible	(51,000)
Input tax claimed on HCL			(80,000)
			419,540
Add: Credit brought forward from previous month	[20,000+10,000]		30,000
Input Tax for the month (Accumulated credit)			**449,540**
SALES TAX DEBIT (OUTPUT TAX)			
Taxable goods to registered persons	2,500,000	17%	425,000
Taxable goods to un-registered persons	875,000	17%	148,750
Taxable goods to registered exporters	625,000	17%	106,250
Self-consumption of packing material	150,000	-	-
Shampoo to un-registered distributors [3 × 110,000]	330,000	17%	56,100
Advance against supply of electric shavers	600,000	17%	102,000
Discount coupons to customers (actionable claims)	450,000	inadmissible	-
Short payment of sales tax in April 2016	-	-	27,000
Output tax for the month			**865,100**
Further tax on supplies to un-registered persons [875,000 × 2%]			17,500
Further tax on supply of shampoo to un-registered distributors [3rd schedule item] [330,000 × 0%]			-
Admissible credit (lower of 449,540 or 90% of 865,100 = 778,590			(449,540)
Sales tax payable			**433,060**
Input tax to be carried forward			**Nil**

Ans.6 (a) **Residual input tax Vs. Residual input tax credit:**

"Residual input tax" means the amount of tax paid on raw materials, components and capital goods being used for making taxable as well as exempt supplies but does not include the input tax paid on raw materials used wholly for making taxable or exempt supplies; Whereas

"Residual input tax credit" is that amount of residual input tax which is apportioned to the value of taxable supplies using the following formula:

$$\textit{Residual Input Tax Credit on taxable supplies} = \frac{\textit{Value of taxable supplies}}{(\textit{Value of taxable + exempt supplies})} \times \textit{Residual Input Tax}$$

(b) **Features distinguishing the concept of 'Zero rating' from 'Exempt supply':**

Distinction points	Zero Rated Supply	Exempt Supply
Definition	"Zero rated supply means a taxable supply which is charged to tax at the rate of zero per cent.	"Exempt Supply means a supply which is exempt from tax.
Products covered	Goods exported as notified by FBR or listed in the Fifth Schedule are charged to sales tax at the rate of zero per cent.	Goods specified by Federal Government and FBR and goods listed in Sixth Schedule are exempt supplies.
Invoicing Requirements	Invoice shall be raised for the goods supplied but sales tax shall be charged at the rate of zero per cent	No sales tax invoice shall be raised.
Registration	A person engaged in zero rated supplies has to be registered with the Sales tax department.	A person engaged exclusively in the exempt supplies is not liable to be registered.
Input tax credit	Input tax paid related to zero rated supplies is refundable.	Input tax paid related to exempt supplies is inadmissible, therefore, neither adjustable nor refundable.

(c) **Records:**

A registered person making taxable/exempt supplies shall maintain the following records of goods (including zero rated and exempt supplies):

(i) records of supplies;
(ii) records of goods purchased;
(iii) records of goods imported;
(iv) records of zero-rated and exempt supplies;
(v) double entry sales tax accounts;
(vi) Following further records is desired:
Tax invoices, Credit notes, debit notes, Bank statements, Banking instruments in terms of section 73, Inventory records, Utility bills, Salary and labour bills, Rental agreements, Sale-purchase agreements, Lease agreements, Record relating to gate passes, inward or outward, and transport receipts.
(vii) Such other records as may be specified by the Board.
(viii) The Board may specify to use such electronic fiscal cash registers as are approved by the Board.

Ans.7 (a) **Responsibilities of the tax implementing authorities:**

A concise code which can enlist responsibilities of Tax Administrators can be as under:

(i) Obey all laws relating to taxation and grant no exemptions, credit or advantage to any taxpayer that is not provided by the law;
(ii) Be dedicated to the highest ideals of honesty and integrity in all matters in order to maintain the respect and confidence of the government and taxpayers;
(iii) Strive to be impartial, fair, neutral and consistent in administering the law without regard to race, social status or economic circumstances;
(iv) Provide prompt, efficient and quality service to all stakeholders in an effort to exceed their expectations;
(v) Refrain from actively participating in partisan political activities;
(vi) Accurately record proceedings and maintain taxpayer information in the strictest confidence and highest level of security;
(vii) Refrain from soliciting gifts for actions and non-actions;
(viii) Make reasonable effort to collect the proper amount of tax revenue due at the lowest possible cost to the state, and in a manner that warrants the highest degree of confidence in our integrity, efficiency, effectiveness and fairness;
(ix) Respond to valid taxpayer refund claims with the same diligence as employed in collection of taxes;
(x) Educate taxpayers on their rights and responsibilities to ensure the highest possible levels of voluntary compliance to the laws.

(b) **Taxes which can be imposed by the Federation:**

Following are the types of taxes which can be imposed by the Federation as provided in the Federal legislative list under the Constitution of Pakistan:

(i) Duties of customs, including export duties.
(ii) Duties of excise, including salt, but not including alcoholic liquors, opium or other narcotics;
(iii) Taxes on income other than agricultural income;
(iv) Taxes on corporations.
(v) Taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed, except sales tax on services.
(vi) Taxes on the capital value of the assets, not including taxes on immovable property.
(vii) Taxes on mineral oil, natural gas and minerals for use in generation of nuclear energy.
(viii) Taxes and duties on the production capacity of any plant, machinery, undertaking, establishment or installation in lieu of any one or more of them.
(ix) Terminal taxes on goods or passengers carried by railway, sea or air; taxes on their fares and freights.

Ans.8

Mehreen
Computation of taxable income and income tax liability
For the tax year 2016

	---------------- Rupees ----------------		
	Pakistan source	**Foreign source**	**Total**
Income from salary:			
Salary[300,000 × 10], [1,200,000 × 2] **(a)**	3,000,000	2,400,000	5,400,000
Income from business:			
Speculation business	-	600,000	600,000
Less: brought forward speculation loss	-	(380,000)	(380,000)
Net income from speculation business	-	220,000	220,000
Non-speculation business	-	1,480,000	1,480,000
Net business income **(b)**		1,700,000	1,700,000
(Loss) from other source **(Carried forward)**	-	(1,500,000)	(1,500,000)
Capital gain	-	950,000	950,000
Less: brought forward loss	-	(1,800,000)	(1,800,000)
Net capital loss **(Carried forward)**		(850,000)	(850,000)
Total income **(a+ b)**	3,000,000	4,100,000	7,100,000
Less: exempt income			
salary received from AM	-	(2,400,000)	(2,400,000)
Taxable income	**3,000,000**	**1,700,000**	**4,700,000**

Since salary income is more than 50% of the taxable income, therefore, the slab applicable to salaried individuals shall be applied.

Computation of net-tax liability:

Tax on Rs. 4,000,000			597,000
Tax @ 27.5% on the amount exceeding Rs. 4,000,000 (i.e. on 700,000)			192,500
Tax payable			789,500
Less: Tax credit			
Which is lesser of (A) or (B):	**Business**		
	Speculation	**Non-Speculation**	
Foreign taxes paid **(A)**	110,000	187,600	
Proportionate Pakistan tax [(789,500÷4,700,000) × 220,000] **(B)**	36,955	-	(36,955)
Proportionate Pakistan tax [(789,500÷4,700,000) × 1,480,000] **(B)**	-	248,609	(187,600)
			(224,555)
Total tax liability for the year			564,945
Less: Tax withheld at source (40,000 × 10)			(400,000)
Net tax payable for tax year 2016			**164,945**

Un-adjusted foreign tax credit shall not be refunded, carried back to preceding year or carried to the following year.

(THE END)

The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examinations

7 March 2016
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Wajahat, aged 48 years, is a marketing manager in Nayaab (Pvt.) Limited (NPL), a company engaged in the manufacture and supply of tissue papers. The details of his monthly emoluments during the year ended 30 June 20X6 are as under:

	Rupees
Basic salary	70,000
Dearness allowance	10,000
Conveyance allowance	8,000

In addition to the above, Wajahat was also provided the following:

(i) Provident fund (PF) contribution of Rs. 8,400 per month. An equal amount per month was contributed by Wajahat to the fund. Interest income of Rs. 391,000 at the rate of 20% of accumulated balance of PF was credited to his PF account.

(ii) Reimbursement of electricity bills during the year amounting to Rs. 60,000.

Following further information is also available:

(i) Wajahat received net dividend of Rs. 78,200 from BEE Limited, a company listed on Pakistan Stock Exchange Limited. Withholding tax and zakat deducted from dividend amounted to Rs. 9,200 and Rs. 4,600 respectively. He also received dividend of Rs. 65,000 from a company in U.A.E through normal banking channels. However, no tax was withheld either in Pakistan or U.A.E.

(ii) Wajahat contributed Rs. 890,000 in an approved pension fund under the Voluntary Pension System Rules, 2005.

(iii) On 1 September 20X5, Wajahat started a tuition centre for the students of finance in a posh locality. He received tuition fees of Rs. 2,198,000 and incurred following expenses:
- Monthly salary of Rs. 50,000 paid to himself and Rs. 35,000 to his friend Yousuf who taught financial accounting at the centre.
- Travelling, boarding and lodging expenses of Rs. 300,000. These expenses were incurred by Wajahat in Sri Lanka for attending teachers training workshop.
- Rs. 250,000 against purchase of used computers for the centre.
- Other miscellaneous expenses amounting to Rs. 195,000.

(iv) Wajahat's total taxable income during the previous tax year was Rs. 1,850,000.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the total income, taxable income and net tax payable by/refundable to Wajahat during the tax year 20X6. **(16)**

Note: Show all relevant exemptions, exclusions and disallowances. Tax rates are given on the last page.

Q.2 Akram has recently established an advertising agency in the name and style of Azad Advertising. For introducing his business to both international and local clients, he has allocated considerable chunk of his marketing budget to entertainment expenditures. Under the Income Tax Ordinance, 2001 and Rules made thereunder, advise Akram about the prescribed limits/conditions for the deduction of entertainment expenditure. **(07)**

Q.3 Under the provisions of the Income Tax Ordinance, 2001 explain the following:

(a) Special tax year **(03)**
(b) Transitional tax year **(03)**
(c) Order of application of various tax credits while computing the tax liability of the taxpayer **(03)**
(d) General provisions/rules which may apply to income subject to final tax. **(06)**

Q.4 Lone Traders (LT), a sole proprietorship, is engaged in the business of buying and selling of Maize and Wheat in bulk quantities. Following information has been extracted from LT's records for the year ended 31 December 2015:

(i) Wheat sold to food companies in Punjab amounted to Rs. 13,000,000. The sale was made after allowing discount of Rs. 680,000 to some of the new customers. The gross profit margin was 25% on gross sales.
(ii) LT paid Rs. 600,000 to a research institute for the development of a formula which is likely to improve the quality of wheat it purchases from the growers.
(iii) In August 2015, LT signed a future contract with Mubarak Enterprises (ME) for the purchase of 500 metric tons of maize at Rs. 15,800 per metric ton. The delivery was expected to be made in October 2015. ME also agreed to repurchase the entire lot at the price prevailing on the date of sale.
(iv) In October 2015 price of maize increased to Rs. 18,240 per metric ton and LT sold the entire lot to ME without taking delivery.
(v) LT incurred expenditure of Rs. 25,000 in respect of above future contract.
(vi) Administrative, selling and distribution expenses amounted to Rs. 2,500,000. These included a penalty of Rs. 45,000 which was imposed due to late payment of sales tax on wheat.
(vii) Assessed losses brought forward from previous year were as follows:

	Rupees
Trading business loss	550,000
Speculation business loss	300,000
Capital loss	250,000

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute LT's taxable income/(loss) and the amount of loss to be carried forward, if any, for tax year 2016. **(10)**

Q.5 Mulaqat Associates (MA), an association of persons, is registered under the Sales Tax Act, 1990 and is engaged in the business of manufacture and distribution of various products. Following information has been extracted from MA's records for February 2016:

	Rupees
Supplies:	
Jet fuel to Pak Airways proceeding to Oslo	800,000
Taxable goods to registered customers	500,000
Taxable goods to un-registered customers	375,000
Purchases:	
Taxable goods from registered suppliers	650,000
Taxable goods from un-registered suppliers	150,000
Exempt goods from registered suppliers	100,000
Imports – raw material	280,000

Following information is also available:

(i) Taxable goods purchased from registered suppliers include furniture of Rs. 45,000 which was acquired for use in the office of marketing manager.
(ii) Imports include raw materials worth Rs. 125,000 for the manufacture of shaving cream, covered under Third Schedule. However, en route from port to MA's warehouse in Uthal a serious damage was caused to the consignment. MA received insurance claim of Rs. 90,000 after surrendering the right of disposal of consignment in favour of the insurance company.
(iii) MA purchased 150 bags of cement, covered under Third Schedule, for the construction of a bungalow for managing partner. Cement was purchased at the wholesale price of Rs. 400 per bag. However, the retail price was Rs. 500 per bag.
(iv) Advance of Rs. 268,000 was made to Nomi Corporation for the purchase of packing materials.
(v) Taxable goods to un-registered customers include goods worth Rs. 200,000 sold to cottage industry in Bela. The rest of the goods were sold to educational institutions in Zhob.
(vi) On 15 February 2016 MA signed an agreement with Bali Traders (BT), a registered customer, for the sale of goods worth Rs. 290,000. On 20 February 2016 the goods were made available to BT. However, BT took the delivery of goods on 5 March 2016.
(vii) MA sold goods worth Rs. 52,000 to one of its customers on two months credit. The amount was inclusive of 4% mark-up.
(viii) MA distributed free samples of one of its new detergents Zeta among corporate clients. The value of these samples amounted to Rs. 65,000.
(ix) MA issued a debit note of Rs. 35,000 to Hali Brothers to rectify a mistake in MA's sales invoice. The invoice was originally raised in November 2015.
(x) On 1 February 2016 MA sold 4,000 packs of a new caramel ice cream, covered under Third Schedule, at a discounted price of Rs. 100 per litre pack. The retail price of the ice cream was Rs. 160 per litre pack.
(xi) Sales tax credit brought forward from January 2016 amounted to Rs. 245,000. This amount was inclusive of input tax of Rs. 120,000 paid on a chemical which could not be used before the expiry date and was consequently destroyed in February 2016.

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of **17%**.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by/refundable to MA and the amount of sales tax to be carried forward, if any, for the tax period February 2016. **(18)**
Note: show all relevant exemptions, exclusions and disallowances.

Q.6 Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, briefly describe the following:

(a) How and under what circumstances the Inland Revenue Department may recover the amount of sales tax from a person without issuing him a show cause notice. **(04)**
(b) Rule relating to change in the particulars of registration other than the change of business category. **(05)**
(c) What evidence(s) a person may be required to submit if he is applying for registration as a manufacturer on shared premises. **(02)**

Q.7 (a) Under the provisions of Article 160 of the Constitution of Pakistan, briefly describe the formation of National Finance Commission. Who may be the member(s) of such Commission? **(03)**

(b) 'Besides financing government operational expenditures, taxation is also utilized as a tool to carry out the national objective of social and economic development.' List any **five** non-revenue objectives of taxation. **(05)**

(c) List any **six** ethical issues which may be faced by tax administration authorities while discharging their duties under the four pillars of tax administration. **(03)**

Q.8 Baqir, Asad and Rahi are members of an association of persons (BAR) and share profits and losses in the ratio of 5:3:2 respectively. BAR is engaged in the business of trading consumer electronics and has two independent branches one each in Tehran and Dubai. Following information has been extracted from BAR's profit and loss account for the year ended 31 December 2015:

	Rupees
Sales	30,000,000
Cost of sales	(20,500,000)
Gross profit	9,500,000
Administrative and selling expenses	(4,732,000)
Financial charges	(980,000)
Other income	1,700,000
Profit before taxation	5,488,000

Additional information:

Cost of sales includes:

(i) Closing stock which has been valued at net realizable value of Rs. 1,820,000. The cost of closing stock under absorption costing was Rs. 1,950,000.

(ii) Provision of Rs. 75,000 against slow moving stores and spares.

(iii) Freight charges of Rs. 160,000. These were paid in cash to Momin Goods Transport for transporting goods to customers in Multan.

Administrative and selling expenses include:

(i) Commission of Rs. 290,000 paid to Baqir, annual performance award of Rs. 310,000 paid to Rahi and Rs. 455,000 paid to AB Bank Limited in final settlement of a loan obtained by Asad for the construction of his house in Muree.

(ii) Provision for bad debts of Rs. 735,000. The opening and closing balances of provision for bad debts amounted to Rs. 1,100,000 and Rs. 1,435,000 respectively. Bad debts written off include a loan of Rs. 280,000 provided to a supplier.

(iii) Sales promotion expenses of Rs. 275,000. These expenses were paid by Rahi through his personal credit card.

(iv) Rs. 86,000 paid to an institution operated by Federal Government for the training of industrial workers in Punjab.

Further information:

For the year ended 31 December 2015 Dubai branch made a profit of Rs. 1,500,000 and Tehran branch made a loss of Rs. 1,800,000. These figures are not included in the above profit and loss account.

Required:

Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the taxable income, net tax payable by BAR and the amount to be carried forward, if any, for tax year 2016. Assume tax and accounting depreciation is same. **(12)**

Note:
- ***Your computation should commence with the profit before tax figure of Rs. 5,488,000.***
- ***Show all relevant exemptions, exclusions and disallowances.***
- ***Tax rates are given on the last page.***

(THE END)

EXTRACTS FROM THE INCOME TAX ORDINANCE, 2001
THE FIRST SCHEDULE
Tax Rates for Every Individual and Association of Person Except for Salaried Taxpayer

S. No.	Taxable income	Rate of tax
1.	Upto Rs. 400,000	0%
2.	Exceeds Rs. 400,000 but does not exceed Rs. 500,000	7% of the amount exceeding Rs. 400,000
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 7,000 + 10% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,500,000	Rs. 32,000 + 15% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,500,000 but does not exceed Rs. 2,500,000	Rs. 144,500 + 20% of the amount exceeding Rs. 1,500,000
6.	Exceeds Rs. 2,500,000 but does not exceed Rs. 4,000,000	Rs. 344,500 + 25% of the amount exceeding Rs. 2,500,000
7.	Exceeds Rs. 4,000,000 but does not exceed Rs. 6,000,000	Rs. 719,500 + 30% of the amount exceeding Rs. 4,000,000
8.	Above Rs. 6,000,000	Rs. 1,319,500 + 35% of the amount exceeding Rs. 6,000,000

Rates of Tax for Salaried Individuals

S. No.	Taxable income	Rate of tax
1.	Upto Rs. 400,000	0%
2.	Exceeds Rs. 400,000 but does not exceed Rs. 500,000	2% of the amount exceeding Rs. 400,000
3.	Exceeds Rs. 500,000 but does not exceed Rs. 750,000	Rs. 2,000 + 5% of the amount exceeding Rs. 500,000
4.	Exceeds Rs. 750,000 but does not exceed Rs. 1,400,000	Rs. 14,500 + 10% of the amount exceeding Rs. 750,000
5.	Exceeds Rs. 1,400,000 but does not exceed Rs. 1,500,000	Rs. 79,500 + 12.5% of the amount exceeding Rs. 1,400,000
6.	Exceeds Rs. 1,500,000 but does not exceed Rs. 1,800,000	Rs. 92,000 + 15% of the amount exceeding Rs. 1,500,000
7.	Exceeds Rs. 1,800,000 but does not exceed Rs. 2,500,000	Rs. 137,000 + 17.5% of the amount exceeding Rs. 1,800,000
8.	Exceeds Rs. 2,500,000 but does not exceed Rs. 3,000,000	Rs. 259,500 + 20% of the amount exceeding Rs. 2,500,000
9.	Exceeds Rs. 3,000,000 but does not exceed Rs. 3,500,000	Rs. 359,500 + 22.5% of the amount exceeding Rs. 3,000,000
10.	Exceeds Rs. 3,500,000 but does not exceed Rs. 4,000,000	Rs. 472,000 + 25% of the amount exceeding Rs. 3,500,000
11.	Exceeds Rs. 4,000,000 but does not exceed Rs. 7,000,000	Rs. 597,000 + 27.5% of the amount exceeding Rs. 4,000,000
12.	Exceeds Rs. 7,000,000	Rs. 1,422,000 + 30% of the amount exceeding Rs. 7,000,000

Rate of Dividend Tax

10% in case of dividend received by a person from a mutual fund.
12.5% in all other cases.

THE THIRD SCHEDULE
Part I
Depreciation Rates

1.	Building (all types)	10%
2.	Furniture and fittings	15%
3.	Plant and machinery	15%
4.	Motor vehicles (all types)	15%
5.	Computer hardware	30%

Part II
Initial Allowance and First Year Allowance

The rate of initial allowance for eligible depreciable assets shall be 25%.

Ans.1

Wajahat
Computation of income tax liability
For the tax year 20X6

		Rupees
Income from Salary:		
Basic salary (70,000×12)		840,000
Dearness allowance (10,000 × 12)		120,000
Conveyance allowance (8,000 × 12)		96,000
PF contrib. [(8,400 × 12) – (lower of Rs. 100,000 or 1/10th of basic + DA)]		4,800
Working: (100,800) or (lower of Rs.100,000 or (840,000+120,000)/10= 96,000		
Interest on PF [391,000 – (higher of: interest @16% or 1/3rd of basic + DA)]		71,000
Working: (391,000/20% × 16% = 312,800 or ((840,000+120,000)/3= 320,000)		
Reimbursement of electricity bill		60,000
Total income under the head salary		1,191,800
Income from business:		
Tuition fees (for ten months ended 30 June 20X6)		2,198,000
Less: Admissible expenses:		
Salaries paid: Wajahat (inadmissible being the owner of the centre)		-
Friend (35,000 × 10)		(350,000)
Training expenses		(300,000)
Dep.: Computers (250,000 × 30%) [no initial allowance is admissible]		(75,000)
Other misc. expenses		(195,000)
		1,278,000
Income (Separate block):		
Dividend received from BEE Limited (78,200 + 9,200 + 4,600)		92,000
Dividend received from a company in U.A.E		65,000
		157,000
Total income		**2,626,800**
Less: Separate block income -		(157,000)
Less: Zakat		(4,600)
Taxable income		**2,465,200**
Since salary income is less than 50% of the taxable income, therefore, the slab applicable to non-salaried individuals shall be applied:		
Computation of net tax liability:		
Tax on Rs. 1,500,000		144,500
Tax @ 20% on the amount exceeding Rs. 1,500,000 (i.e. on 965,200)		193,040
Tax payable under NTR		337,540
Less: Tax credit on investment in pension: (887,472 × 337,540/2,465,200)		(121,514)
Which is lesser of (A), (B) or (C):		
▪ Total contribution paid by Wajahat **(A)**	890,000	
▪ 20% of taxable income (2,465,200 × 20%)	493,040	
Add: 2% add. for each year of age above 40 years (2%×8×2,465,200)	394,432	
(B)	887,472	
▪ 50% of last assessed taxable income (1,850,000 × 50%) **(C)**	925,000	
		216,026
Add: Tax payable on dividend income (157,000 × 12.5%) (FTR)		19,625
Total tax liability for the year		235,651
Less: Tax withheld at source (Dividend)		(9,200)
Net tax payable for tax year 2016		**226,451**

Ans.2 Entertainment expenditure:

Akram would be allowed a deduction for entertainment expenditure if the following conditions are satisfied:

The expenditure should be incurred in deriving income from business chargeable to tax and should be limited to expenditure incurred which satisfies the following conditions:

- expenditure incurred outside Pakistan on entertainment in connection with business transactions or is allocated as head office expenditure;
- expenditure incurred in Pakistan on entertainment of foreign customers and suppliers;
- expenditure incurred on entertainment of customers and clients at the person's business premises;
- expenditure incurred on entertainment at a meeting of shareholders, agents, directors or employees; or
- expenditure incurred on entertainment at the opening of branches.

A deduction shall only be allowed for expenditure incurred on the entertainment of persons related directly to Akram's business.

Ans.3 (a) **Special tax year:**

Where a person's income year is different from the normal tax year, or where, by an order, a person has been allowed by the Commissioner Inland Revenue to use a twelve months' period different from normal tax year, such income year or such period shall be that person's special tax year and shall be denoted by the calendar year relevant to normal tax year in which the closing date of the special tax year falls.

The Board has authority to prescribe any special tax year in respect of any particular class of taxpayers.

(b) **Transitional tax year:**

Where the tax year of a person changes as a result of an order by the Commissioner of inland revenue either from the normal tax year to special tax year or vice versa, the period between the end of the last tax year prior to change and the date on which the changed tax year commences shall be treated as a 'transitional tax year'.

(c) **Application of tax credits while computing the tax liability of the taxpayer:**

If a taxpayer is allowed more than one tax credit for a year, the credits shall be applied in the following order:

(i) Any foreign tax credit; then
(ii) Any tax credit allowed under Part X of Chapter III; such as
- Charitable donations
- Investment in shares and insurance
- Contribution to an approved pension fund
- Tax credit for employment generation by manufacturer u/s 64B

(iii) Second schedule credits e.g. reduction in tax liability due to full time teacher allowance etc.
(iv) Any tax credit allowed for quarterly advance tax paid u/s 147 and for tax collected / deducted at source u/s 168

(d) **General provisions/ rules apply to income subject to final tax:**

Following rules apply to income subject to final tax:

(i) Tax imposed is a final tax
(ii) Such income is not chargeable to tax under any head of income in computing the taxable income of the person
(iii) No deduction is allowed for any expenditure incurred in deriving such income
(iv) The amount of such income is not reduced by:
- Any deductible allowance
- The set off of any loss

(v) The final tax payable is not reduced by any tax credit allowed (foreign tax credit or tax credits on donations, investments etc.)

(vi) The liability of the recipient of such income is discharged to the extent that:
- In the case of shipping and air transport income, the tax is paid in accordance with relevant sections of the Ordinance; or
- In any other case, the final tax payable has been deducted at source

Ans.4

Lone Traders (LT)
Computation of Taxable income / (loss)
For the tax year 2016

Rupees

Particulars		Speculation Business	Trading Business	Total
Gross sales [18,240 × 500] & [13,000,000 + 680,000]		9,120,000	13,680,000	22,800,000
Less: Discount		-	(680,000)	(680,000)
Net sales		9,120,000	13,000,000	22,120,000
Gross profit [9,120,000 – 7,900,000] & [13,680,000 × 25%]		1,220,000	3,420,000	4,640,000
Less: Exp. - Direct				
▪ Scientific research		-	(600,000)	(600,000)
▪ Expenditure in respect of future contract		(25,000)	-	(25,000)
Less: Exp.- Common [gross sales basis i.e. 40:60]				
Admin., selling and distrib.	2,500,000			
Less: inadmissible - penalty	(45,000)			
Allowable common expenses	2,455,000			
Admin., selling and distrib. [2,455,000 × 40% & 60%]		(982,000)	(1,473,000)	(2,455,000)
Net business income		213,000	1,347,000	1,560,000
Brought forward losses		(300,000)	(550,000)	
Taxable income/(loss) for the year		(87,000)	797,000	

- Speculation loss of Rs. 87,000 would be carried forward to the next year.
- Speculation loss cannot be set off against trading business income of Rs. 797,000.
- Similarly capital loss of Rs. 250,000 would be carried forward to next year as it cannot be set off against any other head of income.

PRINCIPLES OF TAXATION
Suggested Answers
Certificate in Accounting and Finance – Spring 2016

Ans.5

Mulaqat Associates (MA)
Computation of Net Sales Tax Liability
For the tax period February 2016

SALES TAX CREDIT (INPUT TAX)	**Taxable Value**	**Sales Tax Rate**	**Amount of Sales Tax**
Taxable goods from registered suppliers [650,000 – 45,000]	605,000	17%	102,850
Furniture for use in marketing manager's office	45,000	inadmissible	-
Taxable goods from un-registered suppliers	150,000	inadmissible	-
Exempt goods from registered suppliers	100,000	-	-
Import of raw material	280,000	17%	47,600
Purchase of cement [being personal in nature] [150x500]	75,000	inadmissible	-
Advance against purchase of packing material	268,000	17%	45,560
			196,010
Add: Credit brought forward from previous month			245,000
Less: input tax on chemicals destroyed			(120,000)
			125,000
Input Tax for the month (Accumulated credit)			**321,010**
SALES TAX DEBIT (OUTPUT TAX)			
Jet fuel to Pak Airways	800,000	0%	0
Taxable goods to registered customers	500,000	17%	85,000
Taxable goods to Cottage Ind. In Bela	200,000	17%	34,000
Taxable goods to un-registered -end consumers	175,000	17%	29,750
Raw material to insurance company [treated as supply]	90,000	17%	15,300
Taxable goods to Bali Traders	290,000	17%	49,300
Taxable goods on two months credit	52,000	17%	8,840
Free samples of detergent Zeta	65,000	17%	11,050
Debit note issued to Hali Brothers	35,000	17%	5,950
Caramel ice cream [4,000 x 160]	640,000	17%	108,800
Output tax for the month			**347,990**
Further tax on supplies to cottage Ind. [200,000 × 2%]			4,000
Further tax on supplies to un-registered end consumers-Exempt [175,000 × 0%]			0
Admissible credit (lower of 321,010 or 90% of 347,990 = 313,191			(313,191)
Sales tax payable (347,990 – 313,191 = 34,799) + (4000)			**38,799**
Input tax to be carried forward [321,010 – 313,191]			**7,819**

Ans.6 (a) **Short paid amounts recoverable without notice:**

Where a registered person pays the amount of tax less than the tax due as indicated in his return, the short paid amount of tax along with default surcharge shall be recovered from such person by stopping removal of any goods from his business premises and through attachment of his business bank accounts, without giving him a show cause notice and without prejudice to any other action prescribed under section 48 of this Sales Tax Act or the rules made thereunder:

(b) **Change in the particulars of registration (other than change of business category):**

(i) In case there is a change in the name, address or other particulars as stated in the registration certificate, the registered person shall notify the change in the Form STR-1 to the computerized system, within fourteen days of such change.
(ii) In case of approval of the change applied for, a revised registration certificate shall be issued through computerized system, which shall be effective from the date the person applied for the change.
(iii) Where a person is unable to file application for change in particulars of registration directly in computerized system, he may submit the prescribed application and required documents to the concerned Commissioner Inland Revenue at RTO, who shall ensure entry of the application and documents in computerized system within three days.
(iv) The commissioner may, based on available information or particulars and after making such inquiry as he may deem necessary and after providing reasonable opportunity of being heard to a person, by an order in writing, make modifications in registration of the person.

(c) In case the person applying for registration as manufacturer is sharing the premises, he shall provide evidence of:

(i) demarcation of manufacturing premises for registration, and
(ii) installation of sub-meter by the relevant utility company, in case he does not have independent industrial utility connection but is using electricity or gas through sub-meter.

Ans.7 (a) **National Finance Commission:**

Within six months of the commencing day and thereafter at intervals not exceeding five years, the President shall constitute a National Finance Commission consisting of the Minister of Finance of the Federal Government, the Ministers of Finance of the Provincial Governments, and such other persons as may be appointed by the President after consultation with the Governors of the Provinces.

(b) **Non-revenue objectives:**

Following are the five non-revenue objectives of taxation:

(i) To strengthen anaemic enterprises by granting them tax exemptions or other conditions or incentives for growth;
(ii) To protect local industries against foreign competition by increasing local import taxes;
(iii) As a bargaining tool in trade negotiations with other countries;
(iv) To counter the effects of inflation or depression;
(v) To reduce inequalities in the distribution of wealth;
(vi) To promote science and invention, finance educational activities or maintain and improve the efficiency of local forces;
(vii) To implement laws which eliminate discrimination among various elements in the markets/businesses.
(viii) To discourage certain undesirable sectors and activities.

(c) Following are the six ethical issues faced by tax administration authorities under the four pillars of tax administration:
- (i) Acceptance of gifts
- (ii) Conflict of Interest
- (iii) Selective application of the law/ or inconsistency in applying the law
- (iv) Political influence
- (v) Confidentiality/secrecy
- (vi) Discretion
- (vii) Corruption
- (viii) Lack of Autonomy

Ans.8

BAR (AOP)
Computation of income tax liability
For the tax year 2016

		Rupees
Accounting profit before taxation		5,488,000
Add: Inadmissible expenses:		
Closing stock-in-trade adj. [1,950,000 – 1,820,000]		130,000
Provision for slow moving stock		75,000
Freight charges paid in cash		-
Commission paid to Baqir		290,000
Annual performance award – Rahi		310,000
Bank loan of Asad paid by BAR		455,000
Provision for bad debts		735,000
Sales promotion expenses		275,000
Employee training and facilities (FG run institution)		-
Loss from Tehran branch	1,800,000	
Profit from Dubai branch	(1,500,000)	
Net loss from foreign source (to be carried forward for adjustment against foreign source income of the following tax year, if any.)	300,000	
		2,270,000
		7,758,000
Less: Admissible expenses:		
Bad debts written off	**(W-1)**	(120,000)
Net taxable income		7,638,000
Tax on Rs. 6,000,000		1,319,500
On balance Rs. 1,638,000 tax @ 35%		573,300
Net Liability		1,892,800

		Rupees
W-1:	Computation of bad debts written off:	
	Opening balance of provision for bad debt account	1,100,000
	Add: provision during the year	735,000
		1,835,000
	Less: Closing balance of provision for bad debt A/c	(1,435,000)
	Debts written off during the year	400,000
	Less: loan to supplier written off **[W-1(a)]**	(280,000)
	Bad debt written off allowed for tax purpose	120,000

(THE END)

The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examinations

7 September 2015
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Mukarram is working as a Commercial Manager in Airmen Engineering Limited (AEL), an unlisted public company, for the past many years. He derived following emoluments during the tax year ended 30 June 20X5:

	Rupees
Basic salary (per month)	250,000
Medical allowance (per month)	37,500
Housing allowance (per month)	25,000
Travel allowance (per month)	11,500

In addition to above, Mukarram was also provided the following:

(i) A used company maintained car for both business and personal use. This car was provided to him on 1 July 20X4 in replacement of his previous car. This car was purchased three years ago at a price of Rs. 1,000,000. However, the fair market value of the car on 1 July 20X4 was Rs. 800,000. On 1 September 20X4, in accordance with the terms of his employment, AEL transferred the previous car to Mukarram free of cost. The market value of the car at the time of transfer was Rs. 400,000 whereas its book value was Rs. 200,000. On 1 June 20X5, Mukarram sold this car to his neighbour at a price of Rs. 350,000.

(ii) Performance related bonus of Rs. 500,000. The bonus was however, paid to him on 5 July 20X5.

(iii) Two free buffet dinner coupons per month, one each for Mukarram and his wife in a five star hotel. The coupons were provided in line with AEL's policy for its management employees. The dinner costs AEL Rs. 2,000 per person.

(iv) Reimbursement of Rs. 20,000 in respect of telephone and internet charges. 20% of this amount was spent by Mukarram in performance of his official duties.

(v) Two air-conditioners and a washing machine for use at home. The combined book value of these appliances was Rs. 300,000. The appliances are returnable to AEL after three years' time. AEL charged 10% depreciation on these appliances.

(vi) An option to purchase 20,000 shares in AEL on 1 May 20X5 at Rs. 25 per share. The break-up value of AEL on that date was Rs. 85 per share.

Other information relevant to tax year 20X5 is as under:

(i) On 1 April 20X5, Mukarram sold a diamond ring to his brother Zohaib for Rs. 250,000. The ring was purchased on 1 January 20X3 at a price of Rs. 280,000.

(ii) Mukarram has 65 acres of agricultural land in Badin and a building in immediate vicinity of the land. Mukarram rented out 30 acres of his land along with the building to Dino who is a cultivator. Dino uses the building as a store house. Mukarram received annual rents of Rs. 750,000 and Rs. 325,000 in respect of the land and building respectively.

Mukarram is also running a small rice husking unit in Badin. He uses entire agricultural produce in the husking unit which is grown on the remaining portion of his land. During the year he brought 5,000 kilograms of raw rice from his land to the unit for husking. He would have earned Rs. 2,500 per 40 kilogram of raw rice had he sold it directly to the market. His sales from rice husking unit stood at Rs. 850,000 whereas other operating expenses were of Rs. 400,000.

(iii) On 31 May 20X5 a painting was destroyed by heavy rains. Mukarram had purchased the painting on 30 June 20X2 for Rs. 100,000. However, due to constant increase in the value of the painting, he had insured it at a premium of Rs. 15,000. He received insurance claim of Rs. 275,000 on 15 June 20X5.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute the taxable income of Mukarram for tax year 20X5. **(20)**
Note: show all relevant exemptions, exclusions and disallowances.

Q.2 Under the provisions of the Income Tax Ordinance, 2001 what would be the cost of an asset for the purpose of depreciation deduction in each of the following circumstances?

(a) Mr. Aamir acquired a new machine partly in exchange for an old machine. He paid freight to bring the old machine to the seller's location and also purchased cooling equipment which was attached to the new machine for its smooth functioning. **(04)**

(b) Mr. Saulat acquired production machinery by utilizing a loan repayable in euro. The loan is expressed in rupees and is repayable in two years' time. Mr. Saulat also received 20% subsidy on such machinery from the Provincial Government. **(04)**

(c) On 1 July 2015 Mr. Talha started using his personal computer for business purposes. He also had to upgrade the operating system to comply with his business needs. **(02)**

(d) Mr. Rahi constructed a furnace for his factory in Korangi Industrial Area. **(02)**

Q.3 (a) Mr. Baqir was working in Pakistan Embassy in United Kingdom for the past ten years. He returned back to Pakistan five months back and is now working with a British conglomerate in Islamabad. He is in the process of filing his return of income for tax year 20X5 and has sought your advice on the following matters:

(i) Whether I would be a non-resident for tax year 2015 as my period of stay in Pakistan is less than 183 days under the Income tax Ordinance, 2001? **(02)**

(ii) Whether I can claim a foreign levy paid on my foreign income, equivalent to PKR 150,000, as foreign income tax in my return of income to avoid double taxation under the Income Tax Rules, 2002? **(03)**

(iii) Whether I would be required to file a wealth statement and what particulars should I disclose in the statement under the provisions of the Income Tax Ordinance, 2001? **(05)**

(iv) For the purpose of disclosure of securities in wealth statement, what would be regarded as supportive evidence in respect of securities I acquired after my return to Pakistan under the Income Tax Rules, 2002? **(03)**

(v) I jointly with my brother Owais own a two story house in Lahore. Each story of the house has been rented out to two separate families. What would be the tax treatment of income from such property under the Income Tax Ordinance, 2001? **(02)**

(b) Under the provisions of the Income Tax Ordinance, 2001 determine the date by which appeal can be filed with the Commissioner (Appeals) in the following cases:

(i) Assessment order for tax year 2014 was made on 31 December 2014. Demand notice was served on 1 January 2015. **(02)**

(ii) Refund application was filed on 18 April 2015 but no refund order was passed within 60 days. **(02)**

Q.4 (a) What do you understand by the terms 'Security' and 'Derivative products' as provided in the Income Tax Ordinance, 2001 and Rules made thereunder? **(03)**

(b) Under the provisions of the Income Tax Ordinance, 2001 compute taxable gain or loss, under the correct head of income, in each of the following cases. Also identify, giving reasons, whether the company is a public or private company for tax purposes:

(i) Ashiq has 5,000 shares in Rumi (Pvt.) Limited (RPL). 52% of the shares of RPL are held by Delta Plc. which is owned by the British Government. Ashiq inherited these shares from his father on 1 January 2014. His father had purchased these shares on 31 May 2012 at a price of Rs. 250 per share. The market value of these shares at the time of inheritance was Rs. 300 per share.

On 30 June 2015 Ashiq sold 2,500 shares in RPL at a price of Rs. 325 per share when the break-up value of RPL was Rs. 350 per share. **(04)**

(ii) What would be your answer in (i) above, if 40% of the shares of RPL were held by the Provincial Government, 48% by the British Government and 12% by individual investors. **(03)**

Q.5 Rahbar is registered under the Sales Tax Act, 1990 and is engaged in the business of manufacture and supply of specialized equipment. Following information has been extracted from his records for the month of August 2015.

	Rupees
Supplies:	
to corporate customers – registered	20,000,000
to Government hospitals – un-registered	3,780,000
Purchases - Raw material:	
from cottage industry	550,000
from local registered persons	25,800,000

Following information is also available:

(i) Purchases from local registered persons include the following:
- Material worth Rs. 1,600,000 against which a discrepancy has been indicated by the CREST.
- Raw-material of Rs. 2,000,000 purchased from AB Enterprises on 2 August 2015.The payment was made on the same day by pay order. On 15 August 2015, AB Enterprises informed Rahbar that with effect from 1 August 2015 their registration has been suspended by the Commissioner Inland Revenue.
- Wires and cables of Rs. 500,000 and electrical and sanitary fittings of Rs. 900,000. These items were used in the renovation of a factory building.

(ii) An electronic cash register was purchased from High Tech Limited at Rs. 250,000.

(iii) On 18 August 2015 Rahbar acquired a machine on operating lease from Aroma Limited. The total lease rentals payable over the lease term of two years are Rs. 3,500,000. The fair value at the inception of the lease amounted to Rs. 3,100,000.

(iv) On 28 August 2015, Rahbar paid sales tax of Rs. 170,000 on electricity bill.

(v) Own manufactured equipment worth Rs. 375,000 was used for internal testing purposes in R&D department.

(vi) Rahbar made free replacement of faulty parts on request from three of his customers. These parts were covered under warranty and had a market value of Rs. 175,000.

All the above figures are **exclusive of sales tax**, wherever applicable. Sales tax is payable at the rate of **17%**.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute the amount of sales tax payable by or refundable to Rahbar and the amount of sales tax to be carried forward, if any, for the tax period August 2015. **(18)**
Note: show all relevant exemptions, exclusions and disallowances.

Q.6 (a) Under the provisions of the Sales Tax Act, 1990 explain the following:

(i) Input tax in relation to a registered person **(03)**

(ii) Supply **(04)**

(b) Baber Associates, who is registered with the Inland Revenue Department for sales tax purposes, has supplied a heavy duty motor to Mubarak Enterprises on one month's credit. However, due to sharp decline in petroleum prices, the price of the motor has reduced by 10% in the local market. Upon request from Mubarak Enterprises, Baber Associates has finally agreed to reduce the price of motor by 8%.

In view of the Sales Tax Rules, 2006 describe the procedure which may be followed by both the parties to give effect to the above price change. **(03)**

Q.7 Briefly describe any three main canons of taxation which can be helpful in formulating a good tax system. **(03)**

Q.8 What do you understand by 'Federal consolidated fund'? Enumerate the expenditures which are charged upon the Federal consolidated fund. **(08)**

(THE END)

The Institute of Chartered Accountants of Pakistan

Certificate in Accounting and Finance Stage Examinations

7 March 2015
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 On 1 July 20X4, Tahir commenced business of manufacturing garments. Income statement of the business for the year ended 30 June 20X5 is as follows:

	Notes	Rs. in 000
Sales		49,330
Less: Cost of sales	(i)	(39,150)
Gross profit		10,180
Less: Administrative and selling expenses	(ii)	(9,140)
Financial charges	(iii)	(2,500)
Other charges	(iv)	(1,358)
		(2,818)
Add: Other income		3,875
Profit before taxation		1,057

Notes to the income statement:

(i) On 15 July 20X4, used machinery was imported from China valuing Rs. 1,500,000. Depreciation @ 15% was charged on machinery for the whole year and is included in cost of sales.

(ii) Administrative and selling expenses include:
- Rs. 975,000 paid for the purchase of computer software. The software is likely to be used for twelve years.
- Cost of preparation of a feasibility study amounting to Rs. 250,000 which was issued prior to the commencement of business.
- Salary of Rs. 50,000 per month was paid to Tahir's brother who handles the financial matters of the business.

(iii) Financial charges include Rs. 80,000 pertaining to a vehicle obtained on lease from a leasing company. The cost of vehicle was Rs. 1,300,000. Depreciation of Rs. 260,000 has been included in administrative and selling expenses. Lease rentals paid during the year amounted to Rs. 300,000.

(iv) Other charges include:
- running and maintenance expenses of vehicle amounting to Rs. 295,450. Use of vehicle for personal purposes was approximately 20%.
- provision for bad debts amounting to Rs. 25,000.

Other information:

(i) Tahir was working in UAE for the past five years and had come back to Pakistan in April 20X4. He received an amount equivalent to Rs. 150,000 from his ex-employer as differential amount on his final settlement in August 20X4.

(ii) He sold a plot for Rs. 3,500,000 which was inherited from his father in 20X1. Fair market value of the plot at the time of inheritance was Rs. 1,500,000.

(iii) 5,000 shares were purchased for Rs. 600,000 from initial public offering of a new listed company.

(iv) Premium of Rs. 300,000 was paid on Tahir's life insurance policy.

Required:

Under the provisions of the Income Tax Ordinance, 2001 compute the taxable income and tax liability of Tahir for the tax year 20X5. Provide comments in respect of items which do not appear in your computation. ***(Tax rates are given on the last page)*** **(18)**

Q.2 (a) List the persons who are required to furnish a return of income for a tax year under the Income Tax Ordinance, 2001. **(06)**

(b) Specify the circumstances under which the Commissioner has powers to issue notice demanding a return of income from certain person(s) for less than one year. **(03)**

(c) State the powers of the Commissioner if a taxpayer fails to furnish return as required under part (b) above, within the specified time. **(04)**

Q.3 Munir resigned from his employment with Ali Industries Limited (AIL) with effect from 31 December 2014. He received following amounts in final settlement:

- Rs. 150,000 as Leave Encashment.
- Rs. 4,000,000 under a Golden Handshake Scheme.

Munir had received a salary of Rs. 350,000 per month for a period of six months upto December 2014. His taxable income and tax liability during the preceding five tax years were as under:

Tax year	**2010**	**2011**	**2012**	**2013**	**2014**
Total taxable income (Rs)	2,000,000	2,450,000	2,700,000	3,100,000	3,650,000
Total tax paid (Rs)	300,000	392,000	472,500	542,500	650,000

Required:
As a tax consultant, advise Munir about the amount of income tax payable by him for the tax year 2015, under the Income Tax Ordinance, 2001. ***(Tax rates are given on the last page)*** **(06)**

Q.4 (a) (i) Explain the term 'Rent' in context of 'Income from property'. **(02)**

(ii) Specify the head of income under which the following amounts would be chargeable to tax:
- rent from sub lease of a building.
- amount included in rent for the provision of amenities, utilities and any other service connected with renting of the building. **(02)**

(b) On 1 July 2014, Fahim agreed to rent out a house to Mirza at a monthly rent of Rs. 180,000 with effect from 1 August 2014 and received one year's rent in advance. He also received Rs. 800,000 as a security deposit which was partly used to repay the security deposit amounting to Rs. 400,000 received from the previous tenant in July 2010 and partly used for renovation of the house.

Fahim also incurred the following expenses in respect of the above house:
(i) property tax of Rs. 15,000.
(ii) payment of interest amounting to Rs. 200,000 to his friend against amount borrowed for renovation of the house.
(iii) insurance premium of Rs. 110,000.
(iv) Rs. 5,000 per month to Wasif for collection of rent.

Required:
Under the provisions of the Income Tax Ordinance, 2001 compute the taxable income of Fahim for tax year 2015 assuming he has no other income. **(07)**

Q.5 (a) Under the provisions of the Income Tax Ordinance, 2001 state the rules relating to residential status of an Association of Person (AOP). Also explain the taxability of income of AOP, in the hands of the firm and its members. **(05)**

(b) State the rules relating to set-off and carry-forward of losses of AOP and its members. **(02)**

Q.6 Aslam is a resident taxpayer who operates his business from Lahore (LHR) and Paris (PAR). In August 2014, he established a new branch in Berlin (BER).

Following information is available in respect of his business operations for tax year 2015:

	LHR	PAR	BER
	----- Rs. in million -----		
Income / (loss) from business	29	40	(15)
Advance taxes paid in respective countries during the year	10	5	3
Income from capital gain (net of income tax of Rs. 3 million)	-	27	-
Carried forward losses:			
Loss from business	-	55	-
Capital loss	-	6	-

The following amounts paid by Aslam in respect of BER have been charged to LHR:
(i) salaries for the first three months amounting to Rs. 5 million.
(ii) rent expense for the year amounting to Rs. 7 million.

Required:
Under the provisions of the Income Tax Ordinance, 2001 calculate the tax payable by Aslam in the tax year 2015 and foreign tax losses to be carried forward to next year, if any. **(09)**

Q.7 Bashir is registered under the Sales Tax Act, 1990 and is engaged in the business of export and supply of consumer goods. Following information has been extracted from his records for the month of February 2015.

	Rupees
Supplies	
To registered persons	25,980,000
To unregistered persons	2,500,000
Exempt supplies	1,874,000
Export to USA	2,000,000
Purchases	
Purchases from registered person	21,710,000
Import of a machine	2,500,000

Following additional information is also available:

(i) supplies to registered persons include goods amounting to Rs. 300,000 which were supplied to an associated company at a special discount of 25%.
(ii) input tax amounting to Rs. 55,900 was paid in January, 2015 but inadvertently it could not be claimed in the return for January 2015.
(iii) a registered supplier had supplied goods worth Rs. 500,000 to Bashir in February 2015. However, Bashir did not receive the sales tax invoice from the supplier.
(iv) the imported machine was put into operation during February, 2015.
(v) sales tax credit of Rs. 410,000 is to be brought forward from January 2015.

Sales tax is payable at the rate of 17%. All the above amounts are exclusive of sales tax, wherever applicable.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, compute sales tax payable/refundable and input tax credit to be carried forward, if any, for tax period February 2015. **(13)**

Q.8 Saleem is registered under the Sales Tax Act, 1990 and is engaged in the business of export and distribution of electronic appliances.

Required:
Under the provisions of the Sales Tax Act, 1990 and Rules made thereunder, advise Saleem on the following matters:

(a) any **six** situations in which input tax is not allowed to be adjusted against the output tax liability. **(06)**

(b) exports which are outside the purview of zero rating. **(03)**

(c) eligibility for a refund if input tax is paid in excess of the output tax payable for the month. **(02)**

(d) concept of provisional and final adjustment in relation to 'Apportionment of input tax'. **(02)**

Q.9 State any **five** ways through which taxes can be used for development of the country. **(05)**

Q.10 Briefly explain any three indirect taxes applicable in Pakistan. **(05)**

(THE END)

EXTRACTS DROM THE FIRST SCHDULE OF THE INCOME TAX ORDINANCE, 2001

Rates of Tax for Non-salaried Individuals

S. No.	Taxable income	Rate of tax
3.	Where the taxable income exceeds Rs.750,000 but does not exceed Rs.1,500,000	Rs. 35,000 + 15% of the amount exceeding Rs. 750,000
4.	Where the taxable income exceeds Rs. 1,500,000 but does not exceed Rs.2,500,000	Rs. 147,500 + 20% of the amount exceeding Rs. 1,500,000
5.	Where the taxable income exceeds Rs. 2,500,000 but does not exceed Rs.4,000,000	Rs. 347,500 + 25% of the amount exceeding Rs. 2,500,000
6.	Where the taxable income exceeds Rs. 4,000,000 but does not exceed Rs.6,000,000	Rs. 722,500 + 30% of the amount exceeding Rs. 4,000,000
7.	Where the taxable income exceeds Rs.6,000,000	Rs. 1,322,500 + 35% of the amount exceeding Rs. 6,000,000

Rates of Tax for Salaried Individuals

S. No.	Taxable income	Rate of tax
4.	Where the taxable income exceeds Rs.1,800,000 but does not exceed Rs.2,500,000	Rs. 140,000 + 17.5% of the amount exceeding Rs. 1,800,000
5.	Where the taxable income exceeds Rs.2,500,000 but does not exceed Rs.3,000,000	Rs. 262,500 + 20% of the amount exceeding Rs. 2,500,000
6.	Where the taxable income exceeds Rs.3,000,000 but does not exceed Rs.3,500,000	Rs. 362,500 + 22.5% of the amount exceeding Rs. 3,000,000
7.	Where the taxable income exceeds Rs.3,500,000 but does not exceed Rs.4,000,000	Rs. 475,000 + 25% of the amount exceeding Rs. 3,500,000
8.	Where the taxable income exceeds Rs.4,000,000 but does not exceed Rs.7,000,000	Rs. 600,000 + 27.5% of the amount exceeding Rs. 4,000,000
9.	Where the taxable income exceeds Rs.7,000,000	Rs. 1,425,000 + 30% of the amount exceeding Rs. 7,000,000

Capital Gains on disposal of Immovable Property

S. No.	Period	Rate of tax
1.	Where holding period of immovable property is up to one year.	10%
2.	Where holding period of immovable property is more than one year but not more than two years.	5%
3.	Where holding period of immovable property is more than two year.	0%

The Institute of
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of Pakistan

Certificate in Accounting and Finance Stage Examinations

9 September 2014
3 hours – 100 marks
Additional reading time – 15 minutes

Principles of Taxation

Q.1 Sultan is working as electronic engineer with Ansari Electrical Company Limited (AECL). He has provided you with the following information for the tax year ended 30 June 2014:

(a) His monthly cash remuneration in AECL is as follows:

	Rupees
Basic salary	480,000
Medical allowance	48,000
Utilities allowance	55,000
Market value of rent free accommodation	75,000

(b) He was also provided the following benefits in accordance with the terms of his employment:

(i) Leave encashment amounting to Rs. 300,000.
(ii) Hospitalization cost is covered by an insurance policy upto the amount of Rs. 1.5 million. The insurance premium relating to this benefit amounted to Rs. 55,000.
(iii) He is allowed to use his personal car for office use. Reimbursement of car running and maintenance expenses amounted to Rs. 550,000. 15% of these expenses pertain to personal use.

(c) Rs. 200,000 were received from a private limited company for attending board meetings.
(d) A lump sum amount of Rs. 1.2 million was received as the author of a literary work. Sultan took three years to complete this literary work.
(e) Sultan is also a part time singer and owns a studio. He sold the premises in which the studio was situated for Rs. 10 million and shifted his musical instruments to new premises which he purchased for Rs. 15 million. He received Rs. 2.5 million from his father in cash as loan to pay for his new studio. The previous premises was purchased several years ago for Rs. 1.4 million and had a tax written down value of Rs. 600,000 at the time of disposal.
(f) The net income from the studio for tax year 2014 was Rs. 990,000. The expenses include salaries of two workers at Rs. 15,000 and Rs. 18,000 per month and utility bills amounting to Rs. 110,000. All expenses were paid in cash.
(g) He won a car, in a competition held by Star Motor Limited for promotion of its sales. The fair market value of the car was Rs. 850,000.
(h) He gifted 40 fans having a fair market value of Rs. 100,000 to an approved charitable organisation.
(i) An amount of Rs. 500,000 was paid by him as contribution to an approved pension fund.

Required:
Under the provisions of the Income Tax Ordinance, 2001 compute the taxable income and tax thereon for the tax year 2014. ***Tax rates are given on the last page.*** **(20)**

Q.2 Briefly discuss the provisions of Income Tax Ordinance, 2001 in respect of the following situations:

(a) Farhan received Rs. 960,000 as his share of profit from AOP, during the tax year 2014. He also earns income from other sources. **(05)**

(b) ABC (Private) Limited has decided to provide a loan of Rs. 5 million to one of its shareholders, for the purchase of a house. **(04)**

Q.3 Zaman is working as the Chief Executive Officer in Yasir Limited (YL). Following are the details of sale and purchase relating to his capital assets during the tax year 2014.

(a) Under an employee share scheme, 25,000 shares of YL were allotted to Zaman, on 1 December 2011 for Rs. 25 each. According to the scheme, he was not allowed to sell/transfer the shares before completion of two years from the date of transfer. The face value of each share is Rs. 10 per share. Fair market value of the shares was as follows:
- Rs. 40 per share on 1 December 2011
- Rs. 48 per share on 30 June 2012
- Rs. 55 per share on 30 November 2013
- Rs. 61 per share on 30 June 2014

(b) He sold 24,000 shares of HQ (Pvt.) Limited on 30 June 2014 for Rs. 200 per share. He had acquired these shares as follows:
- 18,000 shares were purchased at Rs. 55 per share on 25 June 2013.
- 6,000 shares were allotted as bonus shares on 28 February 2014.

(c) A gain of Rs. 300,000 was realized on the sale of shares of Zeeshan Industries Limited (ZIL), a public listed company, in June 2014. The shares were acquired on 31 May 2013.

(d) Zaman sold a painting to his brother on 23 March 2014 for Rs. 1,800,000. Zaman had purchased this painting for his residence, in an auction for Rs. 2,000,000 on 10 July 2011.

(e) He sold his old furniture to Furqan for Rs. 285,000 on 25 June 2014. The furniture was purchased in 2012 for Rs. 250,000.

Required:
Compute the amount to be included in the taxable income of Zaman for the tax year 2014 and specify the head of income under which the income would be classified. **(10)**

Q.4 In Income Tax Ordinance, 2001 the term "disposal" has a wider connotation than sale because it includes exchange, relinquishment, and extinguishment.

List the situations under which an asset owned by a person shall be treated to have been disposed of. **(05)**

Q.5 (a) Under the Sales Tax Act, 1990 and Rules made thereunder:

(i) List the persons who are required to be registered. **(05)**
(ii) Change in rate of tax during a tax period **(04)**

(b) There are certain food items in the inventory of XY Limited (XYL) which were returned by the customers after the expiry date. Specify the procedure which must be followed under the Sales Tax Rules, 2006 if XYL wishes to destroy these items. **(03)**

Q.6 Ali Trading Company (ATC) is registered under the Sales Tax Act, 1990 and is engaged in the business of manufacture and supply of consumer goods. Following information has been extracted from the records of ATC for the month of August 2014.

	Rupees
Supplies	
Local supplies to wholesalers	14,500,000
Local supplies to distributors	10,254,980
Exports	18,650,000
Local supplies to registered retailers	980,000
Supply of exempted goods	5,500,000
Purchases	
Local purchases from registered persons	50,982,000
Local purchases from un-registered persons	9,200,000

Following additional information is also available:

(i) Supplies amounting to Rs. 540,000 were returned by registered retailers.
(ii) An early settlement discount of Rs. 250,000 was given to local distributors.
(iii) An amount of Rs. 500,000 was received from Imran Associates, representing 25% advance payment in respect of supply of a special order. ATC will supply this order in November 2014.
(iv) Goods pledged with a bank, were disposed of by the bank for Rs. 4 million in satisfaction of debt owed by ATC.
(v) Sales tax credit brought forward from previous month amounted to Rs. 854,700.
(vi) Proper debit and credit notes have been issued wherever necessary.

Sales tax is payable at the rate of 17%. All the above figures are exclusive of sales tax.

Required:
Under the provisions of the Sales Tax Act, 1990 compute sales tax payable/refundable and input tax credit to be carried forward, if any, for August 2014. **(14)**

Q.7 The primary objective of a taxation system is to collect revenue. You are required to list the other objectives (non-revenue) which a taxation system can achieve. **(10)**

Q.8 Briefly explain the ethical responsibilities of the tax implementing authorities. **(10)**

Q.9 (a) List the taxes which can be imposed by the Federal Government. **(06)**

(b) Briefly describe the duties of National Finance Commission. **(04)**

(THE END)

EXTRACTS FROM THE FIRST SCHEDULE OF THE INCOME TAX ORDINANCE, 2001

RATES OF TAX
Division I
Rates of Tax for Individuals

S. No. (1)	Taxable income (2)	Rate of tax (3)
1.	Where taxable income does not exceed Rs. 400,000	0%
2.	Where the taxable income exceeds Rs.400,000 but does not exceed Rs.750,000	5% of the amount exceeding Rs. 400,000
3.	Where the taxable income exceeds Rs.750,000 but does not exceed Rs.1,400,000	Rs. 17,500 + 10% of the amount exceeding Rs. 750,000
4.	Where the taxable income exceeds Rs.1,400,000 but does not exceed Rs.1,500,000	Rs. 82,500 + 12.5% of the amount exceeding Rs. 1,400,000
5.	Where the taxable income exceeds Rs.1,500,000 but does not exceed Rs.1,800,000	Rs. 95,000 + 15% of the amount exceeding Rs. 1,500,000
6.	Where the taxable income exceeds Rs.1,800,000 but does not exceed Rs.2,500,000	Rs. 140,000 + 17.5% of the amount exceeding Rs. 1,800,000
7.	Where the taxable income exceeds Rs.2,500,000 but does not exceed Rs.3,000,000	Rs. 262,500 + 20% of the amount exceeding Rs. 2,500,000
8.	Where the taxable income exceeds Rs.3,000,000 but does not exceed Rs.3,500,000	Rs. 362,500 + 22.5% of the amount exceeding Rs. 3,000,000
9.	Where the taxable income exceeds Rs.3,500,000 but does not exceed Rs.4,000,000	Rs. 475,000 + 25% of the amount exceeding Rs. 3,500,000
10.	Where the taxable income exceeds Rs.4,000,000 but does not exceed Rs.7,000,000	Rs. 600,000 + 27.5% of the amount exceeding Rs. 4,000,000
11.	Where the taxable income exceeds Rs.7,000,000	Rs. 1,425,000 + 30% of the amount exceeding Rs. 7,000,000