



Examiners' report

F6 Taxation (IRL)
December 2007

General

This is the first occasion the examination is conducted under the new syllabus and regulations. The paper now comprises five questions, all of which have to be attempted by the candidate. The marks pattern, remains as before with the first two questions carrying 55 marks and the other three 15 marks each. It appears that some candidates used the technique of picking certain topics to revise, omitting others. This can work where there is choice on the paper, but not on a compulsory paper.

Students have shown a very disappointing trend of not reading the question paper properly and not realising what is expected of them in an answer. In some cases, as pointed out earlier, the format of the adjustments, etc., to be made has not also been properly realised by the students. Thus students did not perform as well as could be expected.

Question Paper

The question paper follows the pattern laid down in the guide-notes and strictly adheres to the syllabus. The two compulsory questions deal with the computation of income and ascertainment of income tax payable by a non-corporate and a corporate person. The third question is on capital gains. Questions 4 and 5 deal with certain issues relating to assessment procedure, basic structure of the law and incidental problems. Questions set are direct and should in normal circumstances not present any great problems to the students.

Given below is an analysis of the question paper – question by question, the answer expected from the students and the actual performance.

Question 1

This question relates to the taxation of an individual, a lady, covering the computation of her income and also the tax payable by her for the assessment year 2007-08. The heads of income covered in this question concern property, profession and other sources. The performance of the candidates in regard to the computation of an income under the head "property", is found to be good. As regards the profession, many candidates overlooked the fact that a businessman can, under law, keep her accounts either under the cash system or mercantile system of accounting provided that the system is consistently adopted over a period of time. In the present case, the question clearly indicated that the lady was keeping her accounts on a cash basis. Hence, there was no necessity to adjust the receipts of the year by items outstanding at the beginning and the close of the year. This was a major area where the candidates did not fare well.

Within this question, there was also a capital gains computation to be carried out. The only issue to be decided in this case was the adoption of the cost of the property to the original owner as the cost to the lady and allowing her the benefit of indexation. Though many students could refer to this and solve the problem correctly, a handful did not do so and therefore lost valuable marks.

Overall, the performance of the candidates in answering this question was found to be satisfactory.

Question 2

This dealt with the computation of the income and tax of a corporate body. Various claims, receipts, etc., were highlighted as relating to the company's accounts for the years ended 31st March, 2007 and students were expected to ascertain the taxable income dealing with each of those issues to indicate whether they had any role to play in the determination of income. Most of the students showed a familiarity with the approach to be adopted by taking the profits of the business for the year ended 31st March, 2007 as the starting point and making adjustments. However in some cases, it was very disappointing to note that the students did not

understand the basics of the computation. They had proceeded on the basis of these items on a stand-alone basis which was totally wrong.

Behind each of the claims/receipts the issue of application of a particular section of the Incometax Act or the application of a recent decision of a Supreme Court was involved. Students were expected to be familiar with these issues and though a majority of them could appreciate the nuances behind each of the claims, some of them appeared to lack the knowledge completely. For example, in the first adjustment regarding the raising of a construction on leasehold land, there are two views possible; namely, that because of the amendment to section 32 of the Incometax, the cost of property raised on leased land cannot be allowed as a deduction and a contrary decision of the Supreme Court stating that since the property is raised on a leased land of which the lessee is not the owner, it could be written off as revenue. Both the answers were to be taken as right depending on the arguments given by the student.

The requirement clearly asked students to give their reasons for the treatments. Full marks cannot be awarded if no explanation is given. It was noted that generally, none of the students cared to indicate the reasons behind the treatment of a particular item as an allowable deduction in the computation of income or to be added to the income already disclosed.

In some cases, expenditure like family planning and scientific research which is to be distributed over a period of time did not receive proper treatment. The candidates were tested also on priority of adjustments of carried forward business losses, capital losses and unabsorbed depreciation. The provision of non-carry forward of business losses beyond 8 years was also tested.

In general, answers from most of the students were found to be satisfactory.

Question 3

This is a question on capital gains in the case of a lump sale. There was a difficulty on the part of the students to arrive at the value of assets sold. None of them was in a position to indicate the right figure. The second difficulty was in regard to the treatment of the capital gains either as being long term or short term.

The second sub-division asking for the plan to reduce the capital gains liability on the facts of the case had not been properly answered by any of the candidates who sat for the examination. The paper tested the students' awareness of the provisions of law which indicate that a transfer of an asset between a holding company and a subsidiary company or a subsidiary company and the holding company, subject to the condition of retention of the asset by the transferee for the period of 3 years, would be exempt from being treated as a transfer for purposes of determination of capital gains. This was an issue which was required to be brought out by the student in the answer.

This question was not well answered by students and a number chose not to attempt it at all. However, question 3 will always cover capital gains tax so it is an area that students must practise.

Question 4

This question consisted of 3 sub-divisions. None of which was answered by the candidates to the fullest satisfaction of the examiner.

The first part dealt with the allowance of a claim of loss of assets due to seizure effected by the police. Some of the students were able to indicate in the answer that business profits either of a legal business or illegal business are subjected to tax, if they were disclosed by the taxpayer. Though a claim raised on illegality of purpose would not be allowed as a proper business deduction, the Supreme Court in a case had indicated clearly that the claim could not be considered under section 37, namely, allowance of expenditure against business, but one under the

basic section 28 ie., computation of business income. The Court held that in a situation like that, the claim which is indicated in the problem could be allowed.

The second part dealt with the compulsory audit in respect of an assessee. The question was asked only having in view a specific provision of Finance Act, 2007 incorporated in sec. 44 AB that before a special audit is ordered by the Incometax Department, the taxpayer must be given a reasonable opportunity to represent against such a move. None of the students could give this answer.

The third part of the question dealt with the concept of substituted service. None of the students could appreciate the purport of this problem even though section 282 of the Act, was specifically mentioned in the problem. The question of substituted service stands apart from the normal service of notices either under sec. 142 (1) or 143 (2). Rigorous procedure has been indicated in sec. 282 where the Tax Department has to satisfy the Court that proper reasons have been recorded by the Assessing Officer for resorting to substituted service and only after that the procedure laid down under sec. 282 to be followed.

Students did better in this question than question 3, but it still was not answered satisfactorily by most students.

Question 5

This again had three parts. Many of the answers regarding part (a) were found to be very good. The answers clearly analysed the provisions of the law regarding residence, resident, but not ordinarily resident etc.

The second part dealt with the application of section 64 of the Incometax Act on the clubbing of income. Many of the answers failed to reach the pass mark. They did not even reflect an understanding of sec. 64.

The third part regarding signing of the return of income had been done fairly well by most of the students and the overall mark for most students was satisfactory.