Examiner's report

F6 Taxation (PKN)
June 2010

General Comments

The examination consisted of five compulsory questions with an approximate 85:15 split requirement for computation and narrative respectively.

Most candidates attempted all five questions. Whilst there were some very good scripts with candidates achieving high marks, the performance of candidates overall was disappointing which could be attributed to:

- Failure to cover the entire syllabus and study guide
- Failure to take guidance from the past exam papers
- Superficial knowledge of certain basic concepts

Questions 2 and 5, the computational questions on Individual's taxation and sales tax respectively were frequently the best answered questions, while question 4, a narrative question aimed to check certain concepts of final tax regime was generally not well answered.

To obtain marks for narrative questions or even where the computational questions required notes / reasoning for a particular treatment, it becomes important for the candidate to convey his point of view in a clear language.

Specific Comments

Question One

This 30-marks question on corporate taxation, tested candidates' ability to deal with various aspects of the computation of taxable income.

The computational question has always remained the best attempted question in the past and most of the candidates were able to secure high marks. This time, however, the overall performance with regard to the computational question on corporate taxation remains comparatively bad.

Common mistakes committed by the candidates were:

- the amount spent on the replacement of old worn-out parts of an item of plant was wrongly capitalised whereas the same was an expenditure incurred wholly and exclusively for the purposes of business. No adjustment was, therefore, required in this regard.
- the treatment in respect of income from property derived from persons, who were not prescribed persons for the purposes of section 155. The said rent was required to be included in the computation of taxable income, however, excluded for the purposes of computing tax liability.
- Out of the total expenditure incurred for repairs and maintenance of the building, only 20% was deductible that was attributable to the space in building occupied by the Chief executive officer of the company.
- in computing the tax loss of a destroyed intangible, amortisation for the year of disposal was also calculated on a monthly basis whereas the same was not admissible.
- Tax credit on the purchase of shares was also calculated, which is not admissible to companies.

- Depreciation on workers' residential quarters was claimed wrongly as the same were not occupied by the workers before the year-end.

Question Two
This 25-marks question was on the taxation of an individual having income from different sources. Whilst the main focus of this question was on the taxation of items taxed under the head salary, following concepts were also tested.

- Final tax regime on income from sale of locally purchased goods
- Tax credit on purchase of shares
- Treatment of certain withholding taxes

Generally, this question was well attempted and many candidates were able to secure high marks, however, there were instances where the candidates failed to give clear and concise reasons for inclusion or exclusion of certain items from the computation of taxable income.

The most common mistakes committed by many candidates were related to the following items:

- the salary and allowances of each month are transferred to employees' bank accounts on the first working day of the following month and, therefore, the monthly remuneration for the month of June (received in July) was chargeable to tax in the tax year 2010.

- since Zaki was not entitled to the benefit of free medical treatment or hospitalisation under his terms of employment with Aromatic Oils, the medical allowance paid in cash was exempt upto 10% of his basic salary

- the benefit of company maintained car was to be apportioned for the period of four months and also the amount of Rs 10,000 paid by Zaki was to be deducted from the value of such benefit

Other common error included:

- pension received by Zaki from an associate of his past employer was wrongly claimed as exempt

- gratuity received outside Pakistan was not eligible for the exemption of 50% or Rs 75,000

- the tax collected against the monthly electricity bills was not allowable as a tax credit as the same did not exceed Rs 30,000

- not treating the bonus as separate block of income, chargeable to tax at the rate of 30%

- not subjecting the golden handshake payment to average rate of tax

Question Three
This question on the subject of capital gains was generally not well answered. The result could have been better considering that the subject of capital gains is not complicated since the law is common for corporate and unincorporated taxpayers. Candidates who were unable to secure pass marks demonstrated a lack of understanding of the principles involved. As similar topics have been examined in the past exams, it was apparent that candidates continue not to use the past papers in their preparation for the exams.

Most of the candidates were not aware of the provisions of section 101(10) whereby any gain from the alienation of any share in a company, the assets of which consist wholly or principally, directly or indirectly, of immovable property in Pakistan, is considered to be Pakistan-source. Accordingly, they failed to give a correct answer with regard to the treatment of gain derived by Mr. Property on the disposal of his shares in Building Rental Inc.

Other common errors included:

- not understanding that the status of XYZ Limited is that of a public company by virtue of its 50% shares held by the Austrian Government and, therefore, no loss is deductible on sale of its shares, which are exempt from tax.

- Inability to identify that no gain or loss could arise on transfer of cash, even when the same constitutes disposal

- No loss was to be recognised on the disposal of jewellery

Question Four
This question worth 15-marks was the least well-answered question on the paper.

Very few candidates were aware that under the provisions of section 153(6), if the tax payable by a resident Association of Persons is less than the tax deducted from the payments received by the AOP for rendering of or providing of services, the tax deducted is treated as minimum tax. Accordingly, they failed to identify that the view of Aabee's Chief Financial Officer with regard to claiming refund of Rs 225,000 was incorrect, as the same was in excess of its tax liability.

Also, most of the candidates failed to mention that for the tax deducted from a non-resident (Prime Builders Corporation) under section 152(1A) to be treated as the final tax, non-resident is required to specifically opt for the assessment under the final tax regime and such option must be furnished in writing to the Commissioner within three months of the commencement of the tax year.

Many candidates failed to recognise that the remittance of after tax profits of an Exploration and Petroleum Company's branch is excluded from the definition of "dividend" and, therefore, not attracted by 10% tax.

Question Five
This question worth 10-marks on the subject of sales tax tested the candidates' knowledge with regard to registration requirements and filing of returns where there has been a change in the rate of tax during the tax period. Besides that, the question also required the candidates to compute the sales tax payable for a tax period.

The question was generally well answered with some candidates scoring very high marks, however, many candidates failed to restrict the input tax at 90% of the output tax for a month, as required by section 8B of the Sales Tax Act.