Examiner's report
F6 Taxation (PKN)
December 2009

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. While there were some very good scripts with candidates achieving high marks, the performance of candidates overall was disappointing which seemingly could be attributed to:

- inadequate preparation for the exam
- selective study and not covering the entire syllabus
- failure to study and learn from the past exam papers
- failure to carefully read the content and requirement of questions.

Questions 1 and 5, the computational questions on corporate taxation and sales tax respectively were frequently the best answered questions, while question 4, a wholly narrative question was generally not well answered.

The standard of writing legibility was fair. However, there is need for improvement in the language in the narrative parts of the questions. In many cases the language was not clear to convey to the markers the candidates' point of view. Too many candidates do not follow the ACCA instruction of ticking the appropriate box for each question answered on the cover sheet of the answer paper and starting each question at the top of a new page with clear labelling to identify which question or part of a question is being answered.

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 and included two brief narrative questions on the residence of a company and the concept of a public company for tax purposes. In the narrative questions, many candidates failed to pick up from the scenario that since the Federal Government held 50% of the shares in XYZ Ltd, XYZ Ltd is a public company for tax purposes and is a resident company since the company was incorporated under the Companies Ordinance, 1984.

The computation part of the question was frequently the best answered question on the paper with many candidates gaining high marks. Poor presentation in the layout of the computation was a problem with some candidates. More marks could have been earned had the candidates given clear explanations for the inclusion or exclusion in the computation of income of each of the items given in the scenario.

Many candidates were not aware of:

- the provisions of group relief which allow a subsidiary company to surrender its assessed loss, other than brought forward losses and capital losses, in favour of the holding company

- the treatment in respect of share of profits received from an association of persons.

Other errors included:

- the gain in exchange on payment of an instalment of a foreign currency loan utilised for the import of an item of plant, not deducted from the written down value of plant and machinery

- no depreciation calculated on low value items of furniture charged off in the accounts

- profit on debt on government securities treated as the final tax

- payment to the Workers' Participation Fund not shown as a deduction from the total income to arrive at the taxable income

- loss of cash due to embezzlement by the cashier treated as a non-deductible charge.

Question Two

This 25-marks question was on the taxation of an individual having income from diverse sources. Besides testing the tax implication of some elements of salary income, the question also focused on:

- share of profits received from a partnership firm
- foreign source income
- final tax regime
- tax credit on investment in shares
- recoupment of tax credit allowed in the previous tax year.

As in question one, clear explanations were not given by the majority of candidates for the inclusion or exclusion in the computation of income of each of the items given in the scenario of the question.

Many candidates did not pick up from the scenario that:

- the basic salary of the employees of Atlas Pakistan Limited (Atlas) were deposited into each employee's bank account on the first working day of the following month as a result of which the basic salary of Mr Nadershah from Atlas was erroneously calculated for 11 months instead of 10 months

- since Nadershah was entitled to the benefit of free medical treatment or hospitalisation under his terms of employment with Atlas, the medical allowance paid in cash was chargeable to tax

- the foreign income from interest on US treasury bonds was chargeable to tax since Nadershah was a resident individual in the tax year 2008.

Other common error included:

- no explanation given for not including in the taxable income the annual payment of Rs. 100,000 made by the employer to an approved superannuation fund to provide for Nadershah's retirement

- treating the special allowance paid to Nadershah as his taxable income

- the tax collected by the Collector of Customs on the imported steel bars not treated as the final tax in respect of the transaction relating to the import

- erroneous treatment of the share of profit received from an association of persons

- treating Rs. 500,000 received from Mr. X as a windfall receipt instead of as taxable income

- the tax payable not increased by Rs. 50,000 for the recoupment of the tax credit allowed in the tax year 2008 on the purchase of shares from the Privatisation Commission of Pakistan

- the different sources of income not shown under the appropriate heads of income.

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 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. It was also not obvious that many candidates had read the examiner's article on capital gains in the Student Accountant.

Too many candidates did not pick up the point that the transfer of 1,000 shares in Fashions Inc by Mrs Dee to her brother Azhar was a non-arms length transaction and therefore Mrs Dee is treated as having received consideration equal to the fair market value of the shares at the time of the transfer. Again most candidates were unaware that Azhar acquiring the 1,000 shares in a non-arms length transaction is treated as having a cost equal to the amount which was treated as the consideration received by Mrs Dee. The issue of disposal of an asset in a non-arms length transaction has been examined in the past exams.

Other common errors included:

- failing to recognise that no gain or loss is taken to have arisen on the transfer by Mrs Dee of 25,000 shares in Dee's Boutique Pakistan Ltd to the Sorab Education Trust under the non-recognition rules

- treating the loss on the sale of jewellery as a capital loss

- the loan Rs 100,000 received in cash not shown as taxable income

Question Four
This wholly narrative question worth 15-marks was the least well-answered question on the paper. The scenario related to the accounting year ended 30 June 2009 (tax year 2009) of Agrochemicals

Pakistan Ltd (ACL) engaged in the manufacture of pesticides. The question, relating to the income tax return of ACL for the tax year 2009, focused on testing candidates' knowledge of the tax treatment relating to the following four issues:

- subsidy of Rs. 30,000,000 received by ACL from the Federal Government towards the cost of a new item of plant installed by ACL

- Rs. 1,500,000 paid to settle a forward contract entered into by ACL for the purchase of raw materials used for the manufacture of pesticides, to guard against loss through future price fluctuations

- US$ 40,000 remitted to HeartCare Hospital in Sydney, Australia for the medical treatment of the Chief Financial Officer of ACL. No tax was deducted from the amount remitted

- cash received from a dealer as an advance payment for sale of pesticides for delivery in the first week of July 2009.

Relatively few candidates were aware that the subsidy received by ACL was a capital receipt and not chargeable to tax and that in determining the cost of the plant for tax purposes, the actual amount spent by ACL in acquiring the plant was to be reduced by the amount of the subsidy received from the Federal Government.

In respect of the payment of Rs. 1,500,000 for the settlement of the forward contract, candidates did not pick up from the scenario that the forward contract matured on 1 July 2009 and under the accrual basis accounting, which is mandatory for companies, the amount of the liability under the forward contract crystallised on 1 July, 2009 i.e. in the tax year 2010. Therefore, the Rs. 1,500,000 was not a deductible charge in the tax year 2009.

Many candidates failed to recognise that HeartCare Hospital (HH) being a non-resident company for Pakistan tax purposes, the US$ 40,000 remitted to HH is not a Pakistan-source income of HH and is not chargeable to tax in Pakistan. Therefore ACL was not required to deduct tax from the payment.

In respect of the advance amount received in cash by ACL, most candidates were not aware that unlike other cash advances, cash received as an advance for the sale of goods is not to be treated as income chargeable to tax.

Question Five
This question worth 10-marks on the subject of sales tax required candidates to calculate the sales tax payable by or refundable to a registered person. Besides the normal items of sales and expenses for output tax and input tax respectively, the question also tested the treatment to be accorded for the claim of the input tax paid on the import of plant and machinery.

The question was generally well answered with some candidates scoring very high marks.