
Answers

Notes:

- The suggested answers provide detailed guidance on the subject for use as a study aid to the question paper. Candidates were not expected to produce answers with this extensive detail, which would not be possible in a three hour exam.
- All references to legislation shown in square brackets are for information only and do not form part of the answer expected from candidates.

1 Anwar Chemicals Ltd ('ACL') Marks

(a) Computation of taxable income for the tax year 2014 (accounting year ended 30 June 2014)

| | Note | Rs. | Rs. | |
|---|------|-----------|--------------------|-----|
| Income from business | | | | |
| Net profit as per income statement | | | 19,000,000 | 0·5 |
| <i>Less:</i> | | | | |
| Income not accrued during the year | (1) | 500,000 | | 1·0 |
| Profit on fixed deposit with bank ('Income from other sources') | (2) | 1,000,000 | | 0·5 |
| | | | <u>(1,500,000)</u> | |
| | | | 17,500,000 | |
| <i>Add backs:</i> | | | | |
| Purchase of trademark | (3) | 3,285,000 | | 0·5 |
| Purchase of new laptop | (4) | 200,000 | | 0·5 |
| Penalty for late payment of sales tax | (5) | 100,000 | | 1·0 |
| Donation to a mosque | (6) | 50,000 | | 1·0 |
| Accounting depreciation on fixed assets | (7) | 4,500,000 | | 0·5 |
| Provision for gratuity | (8) | 1,400,000 | | 1·0 |
| Performance reward paid in cash | (9) | 400,000 | | 0·5 |
| Trade fair expenses | (10) | 20,000 | | 1·0 |
| Provision for bad debts | (11) | 300,000 | | 0·5 |
| Loan to an ex-employee – written off | (12) | 119,000 | | 1·0 |
| Fair value adjustment in stocks and shares | (13) | 800,000 | | 0·5 |
| Charges for installation of laboratory equipment | (14) | 26,000 | | 1·0 |
| Profit on funds obtained for non-business use | (15) | 900,000 | | 1·0 |
| Tax gain on disposal of machine | (16) | 100,000 | | 1·0 |
| | | | <u>12,200,000</u> | |
| <i>Less admissible deductions:</i> | | | | |
| Amortisation of intangible | (3) | 162,000 | | 1·5 |
| Initial allowance | (16) | 1,606,500 | | 1·5 |
| Tax depreciation | (16) | 4,197,925 | | 4·5 |
| | | | <u>(5,966,425)</u> | |
| Income from business | | | 23,733,575 | |
| Income from other sources | (2) | | 1,000,000 | 0·5 |
| | | | <u>24,733,575</u> | |

Items not included in the computation of taxable income.

- Software – Rs. 200,000
Software is an intangible. Since the useful life of the software acquired during the year was estimated to be one year only, it is admissible as revenue expenditure. [s.20(1) and (2)] 1·0
- Expenditure incurred on entertainment for shareholders of the company – Rs. 500,000
Entertainment expenditure incurred during the annual general meeting of shareholders is admissible expenditure and not prohibited under the law. [s.21(d) read with rule 10(1)(d) of the IT Rules, 2002] 1·0
- Car given to a dealer under a sales promotion scheme – Rs. 1,500,000
ACL was required to collect tax on the fair market value of the car [s.156(2)]. Non-withholding of tax on this account will attract certain adverse consequences under the law. However, the expenditure incurred on a prize for sales promotion does not become inadmissible for default of non-deduction of tax. [s.21(c)] 1·0

| | |
|---|-----------|
| (iv) Irrecoverable trade debts written off – Rs. 700,000 | |
| Since the trade debts were written off after taking all recovery measures, there are reasonable grounds to believe that the amount has become irrecoverable. The deduction being in accordance with law is admissible. [s.29] | 1-0 |
| (v) Lease rentals – Rs. 280,000 | |
| A lease rental comprises the principal amount and finance charges. Since the plant and machinery were taken on a finance lease from an approved leasing company, the lease rentals paid are fully admissible. [s.28(1)(b)] | 1-0 |
| (vi) Profit paid for funds taken to advance loans – Rs. 820,000 | |
| Profit paid to a bank on a loan taken for advancing concessional loans to staff as per the terms of their contracts of employment is an admissible expenditure being for the purposes of business. [s.20(1)] | 1-0 |
| | <u>27</u> |

Notes

Note 1

A company is required to account for income chargeable to tax under the head 'Income from business' on an accruals basis [s.32(2)] according to which revenue is to be recognised when a taxpayer is entitled to receive it. Since the amount was in the nature of an advance, it cannot be recognised as income. [s.34(1) and (2)]

Note 2

Since ACL is not a financial institution, its profit received from a fixed deposit maintained with a bank is taxable under the head 'Income from other sources' and not under the head 'Income from business'. Further, in the case of a company, profit on debt is taxed at the normal rate of tax and the tax deducted at source on the profit is adjustable against the tax liability worked out on total taxable income. [s.39 read with s.151(3)]

Note 3

A trade mark is included in the definition of an intangible asset in the Income Tax Ordinance, 2001 (the 'Ordinance'). [s.24(11)] The full cost of an intangible is not allowed as a deduction in any single tax year. It is to be amortised over the useful life of the intangible. An intangible asset whose useful life cannot be ascertained is treated as if it had a normal useful life of ten years. [s.24(4)(b)] Further, since the trade mark was used for 180 days during the tax year 2014, amortisation should be worked out as below:

| | |
|---|--|
| Cost of the intangible | Rs. 3,285,000 |
| Deemed useful life in years | 10 years |
| Amortised cost chargeable for the tax year 2014 | $\frac{3,285,000 \times 180}{10 \times 365} = \text{Rs. } 162,000$ |

[s.24(3) and (6)]

Note 4

The expenditure incurred on the purchase of a new laptop is of capital nature and not allowable as a deduction [s.21(n)]. However, it is eligible for initial allowance and depreciation as computed in note 16.

Note 5

Since the penalty of Rs. 100,000 was paid for violation of the provisions of the Sales Tax Act, 1990, it is not admissible. [s.21(g)]

Note 6

A donation paid to a mosque is not an admissible expenditure as it was not wholly and exclusively for the purposes of business. [s.20(1)] Further, it is not eligible for tax credit as it is not an approved institution. [s.61]

Note 7

Accounting depreciation is not a deductible charge. Tax depreciation and initial allowance are deductible at the rates prescribed in the Third Schedule and subject to the conditions mentioned in the relevant provisions [ss.22 and 23] of the Ordinance.

Note 8

Since ACL does not have an approved gratuity fund, any amount accrued on the basis of a provision for gratuity is not admissible due to the specific disqualification clause under the Ordinance to this effect. [s.21(e)]

Note 9

A performance reward given to an employee is included in the definition of salary and any salary paid exceeding Rs.15,000 per month other than by a crossed cheque or direct transfer of funds to the employee's bank account becomes an inadmissible expense. [s.12 and s.21(m)]

Note 10

Any expenditure which is undocumented or unverifiable is not allowable to that extent under the Ordinance. Hence, 5% of total trade fair expenses of Rs. 400,000 are to be added back at Rs. 20,000. [s.174(2)]

Note 11

Provision for bad debts at Rs. 300,000 has been made on a general basis which does not satisfy the essential conditions of:

- written off in the accounts; and
- existence of reasonable grounds for believing that the debt is irrecoverable.

The provision is, therefore, added back to the total income of the taxpayer being inadmissible. [s.29(1)(b) and (c)]

Note 12

Since the amount of the loan was not included earlier in the income from business of ACL chargeable to tax, it is not allowable as a deduction under the law. [s.29(1)(a)(i)]

Note 13

A fair value adjustment in stocks and shares is a notional loss and not actual. A notional loss is not allowable under the law. Also, an actual loss resulting from the disposal of stocks and shares is a capital loss which can neither be claimed as a deduction while computing 'Income from business' nor can it be set off against 'Income from business'. [s.56]

Note 14

Charges incurred for the installation of the laboratory equipment are capital in nature and are to be treated as part of the cost of the assets and not allowable as revenue expenditure. However, they will be eligible for tax depreciation and initial allowance. [s.76 read with s.22 and 23]

Note 15

ACL obtained funds borrowed from the bank which were not utilised for the purpose of deriving 'Income from business' by the company, hence the profit paid on them was not admissible under the law. [s.20]

Note 16

Initial allowance and tax depreciation:

| Asset | TWDV on 1 July 2013 | Addition/ (deletion) during the year | Initial allowance at 25% | TWDV for depreciation | Rate of depreciation | Depreciation |
|--|------------------------|--|--------------------------------|-----------------------------|-------------------------|----------------------|
| (1) | (2) | (3) | (4) | 5 = (2 + 3) – (4) | (6) | (7) |
| | Rs. | Rs. | Rs. | Rs. | | Rs. |
| Freehold land | 9,000,000 | – | – | – | – | – |
| Building on freehold land | 7,000,000 | 5,000,000 | 1,250,000 (see (a)) | 10,750,000 | 10% | 1,075,000 |
| Plant, machinery and equipment | 10,000,000 | (900,000) (see (b)) 1,226,000 (see (c)) | – 306,500 | 9,100,000 919,500 | 15% 15% | 1,365,000 137,925 |
| Computers and other IT related equipment | 2,000,000 | 200,000 (see (d)) | 50,000 | 2,150,000 | 30% | 645,000 |
| Furniture and fittings | 3,000,000 | – | – | 3,000,000 | 15% | 450,000 |
| Motor vehicles | 3,500,000 | (see (e)) | – | 3,500,000 | 15% | 525,000 |
| Total | | | <u>1,606,500</u> | | | <u>4,197,925</u> |

[ss.22 and 23 read with 3rd Sch.]

Sub-notes to note 16

- (a) The rate of initial allowance on new buildings of all types (including quarters for workers) used for business during the tax year is 25%.
- (b) Any gain or loss on the sale of assets eligible for depreciation is assessable under the head 'Income from business', therefore, any gain or loss is to be recognised in the year in which it is accrued and not in the year of receipt of sale proceeds. Hence, Rs. 100,000 being the excess of sale proceeds of Rs. 1,000,000 over the tax written down value of Rs. 900,000 will be treated as income from business. [s.22(8)(a)] Further, no depreciation is allowable for the tax year in which an asset is disposed of.
- (c) The cost of the laboratory equipment includes the purchase price of the equipment and the expenditure incurred on the installation (as referred to in note 14). The asset is eligible both for initial allowance and depreciation. Payment of installation charges in cash does not disentitle them from initial allowance or depreciation.
- (d) New laptop as per note 4.
- (e) The car taken on a finance lease is not owned by ACL, hence no initial allowance or tax depreciation is allowable. Lease rentals have already been claimed and allowed as per s.28(1)(b).

(b) Tax liability for the tax year 2014

| | Rs. | Rs. | |
|---|----------------|--------------------|------------------|
| Taxable income for the tax year 2014 (from (a)) | | 24,733,575 | |
| Brought forward from the tax year 2010 | | (1,500,000) | 1-0 |
| Taxable income | | <u>23,233,575</u> | |
| Tax at 34% | | 7,899,416 | |
| Less: Tax already paid | | | |
| Advance tax paid in cash [s.147] | 3,000,000 | | 0-5 |
| Tax collected by bank on cash withdrawals [s.231A] | 100,000 | | 0-5 |
| Tax deducted on payments received for the supply of goods [Proviso to s.153(3)] | 5,000,000 | | 0-5 |
| Tax deducted by bank from profit [ss.168 and 151] | <u>100,000</u> | | 0-5 |
| | | <u>(8,200,000)</u> | |
| Tax refundable [s.170] | | <u>(300,584)</u> | |
| | | | <u>3-0</u> |
| | | | <u>30</u> |

2 Ms Xiang

(a) Computation of taxable income for the tax year 2014 (accounting year ended 30 June 2014)

| | Rs. | |
|---|-------------------------|-----|
| Income from salary | | |
| Basic salary (200,000 x 12) [s.12(2)(a)] | 2,400,000 | 0·5 |
| Fixed medical cost (400,000 – (2,400,000 x 10%)) [Cl. (139) of Pt. I of 2nd Sch.] | 160,000 | 1·5 |
| Perquisite representing car (working 1) | 90,000 | 1·5 |
| Fuel allowance (25,000 x 12) x 50% [s.12(2)(c) and (d)] | 150,000 | 1·5 |
| Perquisite representing accommodation (working 2) | 1,080,000 | 1·5 |
| Services of a security guard (working 3) | 96,000 | 1·5 |
| Employee share scheme – amount to be treated as salary (working 4) | 1,000,000 | 1·5 |
| Reimbursement of child's school fee (25,000 x 9) [s.12(2)(d)] | 225,000 | 1·0 |
| Perquisite representing concessional loan (working 5) | 18,301 | 1·5 |
| Perquisite representing return air ticket to Beijing [s.12(2)(d)] | 150,000 | 0·5 |
| Income under the head 'salary' | <u>5,369,301</u> | |
| Income from other sources | | |
| Income from delivering lectures [working 6] | 300,000 | 1·5 |
| Total/Taxable income under the normal tax regime | <u><u>5,669,301</u></u> | |
| Tax on taxable income | | |
| (600,000 + (5,669,301 – 4,000,000) x 27·5%) [Para (1A) of Div. I of Pt. I of 1st Sch.] | 1,059,058 | 1·0 |
| Tax on income assessable under the final tax regime (FTR) | | |
| 1. Tax on commercial imports of Chinese food supplements [working 7] | 22,000 | 1·5 |
| 2. Tax on commercial import of toys from China [working 8] | 27,500 | 1·5 |
| Total tax payable | <u>1,108,558</u> | |
| Tax already paid | | |
| | Rs. | |
| Tax paid with school fee of her child [ss.168 and 236] | 15,000 | 0·5 |
| Tax deducted at source by her employer [ss.149 and 168] | 940,000 | 0·5 |
| Tax collected on imports (22,000 + 27,500) [ss.148(7) and 169] | 49,500 | 0·5 |
| Tax collected at the time of purchase of pre-paid cards for mobile phone [ss.168 and 236] | <u>15,000</u> | 0·5 |
| Total tax paid | <u>(1,019,500)</u> | |
| Tax payable with return/statement of FTR | <u>89,058</u> | |

Explanation of items not included in the computation of taxable income

- (i) Amount paid to Institute of Engineers in China
No deduction on account of any expenditure incurred by an employee to derive the amount chargeable to tax under the head 'Salary' is allowed in computing taxable income. [s.12(4)] 1·0
- (ii) Rent from apartment in Zhangshen, China
Xiang is a resident of Pakistan by virtue of her employment here and her stay in Pakistan does not exceed three years. Further, the amount of rent has not been received in Pakistan. Therefore, her income from the rent of the apartment in China is exempt from tax in Pakistan. [s.50] 1·0
- (iii) Donation paid to the Beijing University, China
The donation paid to the Beijing University, China is not an admissible deduction. Further, the amount does not qualify for tax credit as the university is situated outside Pakistan. [ss.12(4) and 60] 1·0

23

Workings:

Working 1

Where a car is provided for personal as well as business use, 5% of the fair market value of the car is treated as salary income on account of this perquisite. Total lease rentals to be paid over the lease term or the lease rentals paid during the year are not relevant for the computation of the value of perquisite.

| | |
|---|------------|
| | Rs. |
| Fair market value (FMV) of the car at the time of obtaining lease | 1,800,000 |
| 5% of FMV to be treated as value of the perquisite (1,800,000 x 5%) [s.13(3) read with rule 5 of the Income Tax Rules, 2002] | 90,000 |

Working 2

Accommodation provided by her employer is a perquisite and is taxable. The valuation of this perquisite is equal to the amount which would have been paid by the employer if such accommodation was not provided, subject to a minimum valuation equal to 45% of basic salary. Since Xiang was entitled to a house rent allowance of 40% of her basic salary, had she not been provided with the accommodation, the minimum amount to be taken as the value of the perquisite is:

| | |
|--|------------|
| | Rs. |
| Basic salary | 2,400,000 |
| Value of the perquisite (2,400,000 x 45%) [s.13(12) read with rule 4 of the Income Tax Rules, 2002] | 1,080,000 |

Working 3

Since the services of the security guard were provided by the employer, the amount chargeable to tax to Xiang will include the total amount paid to the security guard as computed below:

| | |
|---|------------------|
| | Rs. |
| Annual salary paid to the security guard (18,000 x 12) | 216,000 |
| Less amount paid by Xiang to the employer on this account (10,000 x 12) | <u>(120,000)</u> |
| Value of the perquisite taxable as salary [s.13(5)] | <u>96,000</u> |

Working 4

The fair market value of the shares, received by Xiang under the employees' share scheme, on the date on which the restriction to transfer the shares was removed is treated as consideration received by the employee. The value to be treated as salary is:

| | |
|---|------------------|
| | Rs. |
| Deemed consideration on 1 June 2014 when restriction to sell the shares was removed (50,000 x 30) [s.14(3)(a)(i)] | 1,500,000 |
| Less cost of acquisition of shares (50,000 x 10) | <u>(500,000)</u> |
| Amount to be treated as salary [s.14(3)(b)] | <u>1,000,000</u> |

Working 5

Xiang was given a loan at a markup of 6% per annum on 1 August 2013 whereas the benchmark rate for the tax year 2014 is 10% [s.14(a)(ii)]. The concession in the markup is treated as perquisite as computed below:

| | |
|--|-----------------|
| | Rs. |
| Loan given to Xiang on 1 August 2013 | 500,000 |
| Benchmark rate of markup per annum for the tax year 2014 [s.14(a)(ii)] | 10% |
| Markup on the basis of benchmark rate (500,000 x 10%) x 334/365 | 45,753 |
| Markup actually charged at 6% per annum (500,000 x 6%) x 334/365 | <u>(27,452)</u> |
| Concession to be treated as salary | <u>18,301</u> |

The amount of the loan obtained was not used for the acquisition or construction of a house, therefore, it is not eligible for any tax credit. [s.64]

Working 6

Gross receipts of Rs. 300,000 are on account of services rendered for delivering lectures at a Chinese language coaching centre. The payer was not a withholding agent. Therefore, the receipts were chargeable to tax under the normal law and not under the final tax regime. Since the expenditure of Rs. 50,000 was not documented, this cannot be claimed as an admissible deduction. Since delivering the lectures was not the business of the taxpayer, the amount of Rs. 300,000 is assessable under the head 'Income from other sources'. [s.39 and 174]

Working 7

| | | |
|---|---------------|----------------|
| | Rs. | Rs. |
| Total sale proceeds from the sale of Chinese food supplements | | 550,000 |
| Less: | | |
| Cost of imports | 400,000 | |
| Payment to salesman | <u>20,000</u> | |
| | | (420,000) |
| Income | | <u>130,000</u> |

Tax deducted at the import stage at 5.5% of the import value of Rs. 400,000 at Rs. 22,000 shall be treated as the final tax on the income of the importer arising from such imports. [s.148 read with s.169] The net income from this business is not relevant for the computation of tax liability on the imports business.

Working 8

| | |
|---------------------------------------|------------------|
| | Rs. |
| Total sale proceeds from sale of toys | 350,000 |
| Less cost of import of toys | <u>(500,000)</u> |
| Loss from the transaction | <u>(150,000)</u> |

Tax deducted at the import stage at 5.5% of the import value of Rs. 500,000 at Rs. 27,500 is treated as the final tax. [s.148 read with s.169] The loss resulting from the transaction is to be ignored and cannot be set off against other income, including income from the other imports referred to in working 7 above.

(b) Ms Xiang is required to file her return of income for the tax year 2014 by 31 August 2014. [s.118(3)(a)] 1.0

(c) Every resident individual taxpayer who is required to file a return of income or a statement of final tax regime [FTR] is also required to file a wealth statement in the prescribed manner along with his or her return of income/statement of FTR irrespective of their nationality. [ss.116(2) and 116(4)] Therefore, Ms Xiang will be required to file her wealth statement in the prescribed manner. 1.0

25

3 (a) (i) Two persons can generally be treated as associates if the relationship between them is such that:

- one person may reasonably be expected to act in accordance with the intentions of the other person; or
- both persons may reasonably be expected to act in accordance with the intentions of a third person. [s.85(1)] 2.0

(ii) Where the Commissioner is of the view that any transaction between persons who are treated as associates for tax purposes is not on an arm's length basis, he has the powers to distribute, apportion or allocate income, deductions or tax credits between the persons, so as to arrive at the income of each person which would have been earned by each of the persons in an arm's length transaction. [s.108(1)] 2.0

(b) Mr Shehzad

Tax payable for the tax year 2014 (accounting year ended 30 June 2014)

| | Note | Capital gain/(loss) Rs. | Tax Rs. | |
|--|--------|----------------------------|----------------------|-----|
| Capital gains and tax on the disposal of immovable properties taxable as a separate block | | | | |
| On the sale of the house in Islamabad | (1) | 3,100,000 | 155,000 | 2·0 |
| On the sale of agricultural land | (2) | 100,000 | 10,000 | 2·0 |
| | | | <u>165,000</u> | |
| Capital gains on securities taxable as a separate block | | | | |
| On the disposal of shares in Balochistan Minerals (Pvt) Ltd (BMPL) | (3) | 310,000 | 24,800 | 1·5 |
| Income under the head 'Capital gains' assessable to tax along with other heads of income | | | | |
| On the sale shares in Mushtaq (Pvt) Ltd | (4) | 168,750 | | 1·0 |
| On the sale of shares in Sindh Fisheries Ltd | (5(a)) | (50,000) | | 1·5 |
| On the sale of shares in Computer Technologies (Pvt) Ltd | (6) | 315,000 | | 1·5 |
| On sale of antique coins | (7) | 250,000 | | 1·0 |
| Total taxable capital gains | | <u>683,750</u> | | |
| <i>Less:</i> | | | | |
| Capital loss brought forward from the tax year 2008 | | <u>(150,000)</u> | | 0·5 |
| Taxable income | | <u><u>533,750</u></u> | | |
| Tax at 10% of the gain exceeding Rs. 400,000 (533,750 – 400,000) [Para (1) of Div. I, Pt. I of the 1st Sch.] | | | | |
| | | | 13,375 | 0·5 |
| Tax on income assessable under the final tax regime (FTR) | | | | |
| Total dividend | (5(b)) | <u>90,000</u> | | |
| Tax at 10% (90,000 x 10%) [s.5] | | | <u>9,000</u> | 0·5 |
| Total tax | | | 212,175 | |
| <i>Less: Tax already paid</i> | | | | |
| – on the sale proceeds of agricultural land [s.236C] | | 45,000 | | 0·5 |
| – on dividend [ss.5 and 150] | | 9,000 | | 0·5 |
| – with motor vehicle tax [ss.168 and 234] | | 2,000 | | 0·5 |
| – advance tax paid [ss.147 and 168] | | <u>140,000</u> | | 0·5 |
| | | | <u>(196,000)</u> | |
| Tax payable with return | | | <u><u>16,175</u></u> | |

Items not included in the computation of capital gain

1. Loss on theft of jewellery

Shehzad received Rs. 350,000 from the insurance company whereas his cost incurred on the purchase of jewellery was Rs. 400,000. Though he has incurred a loss of Rs. 50,000, it is not recognised for the purposes of computing his taxable gains/losses. [s.38(5)(b)]

1·0

2. Loss in US dollar transactions – Rs. 50,000

The loss suffered by Shehzad was from his dealings in forward contracts for the purchase and sale of US dollars. Since the contracts were settled without actual delivery or transfer of the US dollars, it falls under the definition of 'speculation business'. [s.19(2)] Any loss from speculation business incurred during a year can only be set off against income from any other speculation business of the person during the year. A speculation loss cannot be set off against capital gains.

1·0

16**20**

Notes:

Note 1

Sale of the house in Islamabad

The capital gain on the disposal of the house in Islamabad is computed as:

| | Rs. | Rs. |
|---|------------------|---------------------|
| Consideration received on 15 July 2013 | | 20,000,000 |
| <i>Less:</i> | | |
| Purchase price of the house on 1 January 2012 [s.37(2)] | 15,000,000 | |
| Commission paid to the broker [s.76(2)(b)] | 100,000 | |
| Registration charges for acquisition of the house [s.76(2)(b)] | 800,000 | |
| Structural improvements in the house [s.76(2)(c)] | <u>1,000,000</u> | |
| | | <u>(16,900,000)</u> |
| Capital gain | | <u>3,100,000</u> |
| Tax at 5% as the holding period of the house was more than one year but less than two years (3,100,000 x 5%) [Div. VIII of Pt. I of 1st sch.] | | <u>155,000</u> |

Note 2

Sale of agricultural land

| | Rs. | Rs. |
|--|-----------|--------------------|
| Consideration received on 30 August 2013 | | 9,000,000 |
| <i>Less:</i> | | |
| Price paid for the purchase of land on 1 February 2013 | 8,000,000 | |
| Levelling of land and installation of tube well [s.76(2)(c)] | 900,000 | |
| Valuation fee paid in cash inadmissible [s.37(4)(b)] | <u>0</u> | |
| | | <u>(8,900,000)</u> |
| Capital gain | | <u>100,000</u> |
| Tax at 10% as the holding period of the immovable property was less than one year (100,000 x 10%) [Div. VIII of Pt. I of 1st Sch.] | | <u>10,000</u> |

Note 3

Since 50% of the shares in Balochistan Minerals (Pvt) Ltd (BMPL) are held by the provincial government of Balochistan, it is treated as a public company. [s.2(47)(a)] A share of a public company is included in the definition of a 'security'. [s.37A(3)]. Accordingly, the gain on the disposal of shares of BMPL shall be computed and taxed as a separate block as below:

| | Rs. |
|--|------------------|
| Fair market value of plot received in exchange for shares on 20 November 2013 [s.77(1)] | 850,000 |
| Cost of acquisition of 6,000 shares of BMPL on 20 December 2012 | <u>(540,000)</u> |
| | <u>310,000</u> |
| Tax at 8% of the capital gain as the holding period is more than six months but less than 12 months (310,000 x 8%) [Div. VII of Pt. I of 1st Sch.] | <u>24,800</u> |

Note 4

Disposal of shares in Mushtaq (Pvt) Ltd

| | Rs. |
|--|------------------|
| Consideration received on 15 December 2013 [s.77(1)] | 425,000 |
| Cost of acquisition being fair market of the shares on 1 July 2008 [s.37(4A)(d)] | <u>(200,000)</u> |
| Capital gain | <u>225,000</u> |

Since the disposal was made after more than one year of holding the asset, 75% of the capital gain is taxable, i.e. Rs.168,750. [s.37(3)]

Note 5

(a) Disposal of shares in Sindh Fisheries Ltd ('SFL')

Sindh Fisheries Ltd is a non-listed company and the shareholding of the provincial government of Sindh is less than 50%, therefore it is to be treated as a private limited company. The capital gain is computed as:

| | |
|---|------------------|
| | Rs. |
| Sale proceeds of 6,000 preference shares in SFL on 26 December 2013 | 650,000 |
| Cost of 6,000 shares in SFL acquired on 1 January 2010 | <u>(700,000)</u> |
| Capital loss | (50,000) |
| | |
| (b) Net dividend income received on shares in SFL | 81,000 |
| Tax deducted on dividend income at 10% (81,000 x 100/90) = 90,000 x 10% [s.150] | <u>9,000</u> |
| Gross amount of dividend | <u>90,000</u> |

Note 6

Disposal of shares in Computer Technologies (Pvt) Ltd ('CTPL')

Although the transaction was carried out in US dollars, the capital gain or loss shall be computed in Pakistan rupees on the basis of the exchange rate prevailing on the date of the transaction [s.71] as:

| | |
|--|--------------------|
| | Rs. |
| Sale proceeds of 9,000 shares in CTPL sold on 31 December 2013 (US\$ 36,000 x 100) | 3,600,000 |
| Cost of 9,000 shares in CTPL purchased on 15 January 2013 (US\$ 36,500 x 90) | <u>(3,285,000)</u> |
| Capital gain | <u>315,000</u> |

Note: Had the capital gain or loss been admissible on the basis of US\$, there would have been a loss of US\$ 500.

Note 7

Antique coins fall in the definition of capital assets. [s.37(5) read with s.38(5)(e)] Since the antique coins were sold to his brother, an associate, at a price less than their fair market value, the sale proceeds shall be taken as their fair market value on the date of disposal and a capital gain calculated accordingly as below:

| | | |
|---|---------------|------------------|
| | Rs. | Rs. |
| Deemed sale proceeds of antique coins being fair market value [s.77(1)] | | 550,000 |
| Less: | | |
| Purchase price of the coins | 270,000 | |
| Custom duties and other indirect taxes | <u>30,000</u> | |
| | | <u>(300,000)</u> |
| Capital gain | | <u>250,000</u> |

4 (a) Mr Fahim

Default surcharge payable

Instalment

| | Default surcharge Rs. | |
|--|-----------------------------|------------|
| 1st instalment due on 15 September 2013 not paid so surcharge is due to 30 September 2014 (50,000 x 18% x 380/365) | 9,370 | 1-0 |
| 2nd instalment due on 15 December 2013 but paid on 26 December 2013 (50,000 x 18% x 11/365) | 271 | 1-0 |
| 3rd instalment due on 15 March 2014 but paid on 31 March 2014 (50,000 x 18% x 16/365) | 395 | 1-0 |
| 4th instalment due on 15 June 2014 | | |
| – Rs. 40,000 paid on 30 June 2014 (40,000 x 18% x 15/365) | 296 | 1-0 |
| – Rs. 10,000 not paid so surcharge is due to 30 September 2014 (10,000 x 18%)107/365) | <u>528</u> | <u>1-0</u> |
| Total | <u>10,860</u> | <u>5-0</u> |

Tutorial note: Default surcharge is payable at 18% per annum on the amount of tax not paid or short paid for the period starting on the date on which it was due and ending on the date on which it was paid or 30 September 2014 when his return of income was due, whichever is earlier. [s.147(5) read with s.205(1A)]

(b) Mr Zulquarnian**(i) Penalty for late filing**

| Taxable income Rs. | Tax payable Rs. | Penalty at 0.1% of tax payable for each day of default Rs. | 50% of tax payable Rs. | Minimum penalty Rs. | Penalty payable Rs. | |
|-----------------------|--------------------|--|---------------------------|------------------------|------------------------|-----|
| 6,000,000 | 1,322,500 | $[1,322,500 \times 0.1\% \times 30] = 39,675$ | 661,250 | 25,000 | 39,675 | 4.0 |
| | 0.5 | 1.0 | 1.0 | 1.0 | 0.5 | |

Tutorial note: The penalty for late filing is 0.1% of the tax payable on the declared income in the income tax return, for each day of default, subject to a maximum penalty of 50% of the tax payable and a minimum penalty of Rs. 25,000. [sr. 1 of table to s.182(1)]

(ii) Imposition of penalty where no tax is payable with the return of income

The expression 'tax payable' used in the Ordinance for the purpose of charging a penalty for the late filing of a return means tax chargeable on the taxable income on the basis of assessment treated to have been made upon filing of the return [s.120] or an amended order or a provisional assessment or the best judgement order, as the case may be. This means that even in cases where all of the tax liability on the basis of the declared income stands discharged before or with the filing of the return, the penalty will still be payable on the basis of tax chargeable on the declared income. [Explanation to sr. no. 1 of the table to s.182(1)]

2.0

(c) Mr Basharat**(i) Income from unexplained sources****(1) Foreign remittance – Rs. 1,000,000**

The amount credited in the books of account of a person to the extent it originates from foreign exchange remitted from outside Pakistan through normal banking channels which is cashed into Pakistan rupees by a scheduled bank is not taxable under s.111. Hence the amount of Rs. 1,000,000 is not taxable. [s.111(4)(a)]

1.0

(2) Cash received from uncle – Rs. 2,000,000

Since Mr Basharat has received the amount from his uncle and all the documentary evidence to this extent is available, it is explainable in his hands and cannot be treated as income under s.111 of the Ordinance. [s.111(1)]

1.0

(3) Agricultural income – Rs.2,000,000

Where a taxpayer explains the nature and source of any amount credited in his books of account by way of agricultural income, such explanation is acceptable only to the extent of the agricultural income worked back on the basis of agricultural income tax paid under the relevant provincial law of agricultural income tax. Consequently, only Rs. 300,000 will be treated as explainable and Rs. 1,700,000 will be treated as income under s.111 of the Ordinance. [second proviso to s.111(1)]

1.0

3.0

(ii) Mr Basharat has obtained a loan from his uncle of Rs. 2,000,000 in cash which is fully documented and explainable for the purposes of s.111. However, since the amount has been received from his uncle otherwise than by a crossed cheque drawn on a bank or through a banking channel, it will be treated as income chargeable to tax under the head 'Income from other sources'. [s.39(3)]

1.0

15

5 Rameez Enterprises Ltd ['REL']

(a) Sales tax payable for January 2014

| | Rs. | |
|--|-------------|-----------|
| Output tax | | |
| On taxable supplies | | |
| – in local market to registered persons (Rs.4, 000,000 x 17%) [s.3(1)] | 680,000 | 0·5 |
| – in local market to unregistered persons (Rs.6,000,000 x (17 + 1%)) [s.3(1A)] | 1,080,000 | 1·0 |
| – exported to Hong Kong (Rs. 2,000,000 x 0%) | 0 | 0·5 |
| – given to an executive director (Rs. 600,000 x (17 + 1%)) | 108,000 | 0·5 |
| | 1,868,000 | |
| Less sales tax on sales return from registered person (500,000 x 17%) | (85,000) | 1·0 |
| Output tax | 1,783,000 | |
| Input tax | | |
| | Rs. | |
| On purchases of Rs. 2,000,000 from unregistered persons | 0 | 0·5 |
| On purchases of raw materials from registered persons: | | |
| Purchases inclusive of sales tax Rs. 8,190,000 | | |
| Input tax (Rs. 8,190,000 x 100/117 = 7,000,000 x 17%) | 1,190,000 | 1·0 |
| Sales tax credit brought forward from December 2013 | 300,000 | 1·0 |
| | 1,490,000 | |
| Admissible input tax credit 90% of output tax [Rs. 1,783,000 x 90% = 1,604,700] or input tax [Rs. 1,490,000] whichever lower [s.8B(1)] | (1,490,000) | 1·0 |
| Sales tax payable for the month | 293,000 | 7·0 |
| (b) The sales tax return for the month of January 2014 would be due to be filed on 15 February 2014. [s.2(9)] | | 1·0 |
| However, where the return is filed electronically, it need not be filed until 18 February 2014 provided that the tax due was paid by 15 February 2014. [Rule 18(3) of the Sales Tax Rules, 2006] | | 1·0 |
| | | 2·0 |
| (c) A registered person may file a revised return, with the approval of the Commissioner, within 120 days of the filing of the return to correct any omission or wrong statement made therein. [s.26(3)] | | 1·0 |
| | | 10 |