

TAXATION

Overall Feedback

Overall performance of the candidates was satisfactory. However, it has been observed that quite often the candidates fail to comprehend the exact requirements of the question and try to write as much as they know. The candidates are advised that they will only get marks for the portion of the answer which is relevant. They will not get any credit whatsoever for displaying the knowledge of any areas which is irrelevant. Hence, they should refrain from giving irrelevant details.

Question-wise Comments

Q.1 Part wise comments on this question are as follows:

- (a) Response to this short objective type question was average. The students were required to explain whether certain benefits/perquisites were taxable or not under the ITO-2001. Comments on the responses received are as under:
- Situation (i) was correctly answered by majority of the examinees. However, many of them were of the view that this exemption is available because the transporter bears only minor costs. In actual, this exemption is given under Clause 61 of the Second Schedule to the ITO-2001.
 - In situation (ii), examinees were not clear about the rule that 10% of lease value of car is added to taxable income irrespective of the repairs and maintenance cost or any other cost incurred by the employer. Further, in the case of leased vehicles, fair market value at the inception of lease is relevant for working out the amount that is to be added to income taxable. This amount remains the same, for the first as well as all subsequent years.
 - In situation (iii), most of the candidates were unable to explain that medical allowance upto 10% is exempt only if free medical treatment or reimbursement of medical expenditure is not given.
- (b) The performance of the examinees was good in this question. However, following common mistakes were observed in this part:
- Few examinees mixed up the principles relating to professional firms and other than professional firms.
 - The rules that loss incurred by the professional firm is apportioned among the members, if it cannot be set off against any other income of the association, was mentioned by a few students only.
 - Some students who did mention the above rule, could not clarify that if the member is also unable to set off such loss against his other sources of income, he can carry it forward for a maximum of six years.
 - Many examinees were not aware of the fact that professional firms are only exempt from payment of tax. They are still required to file the return of total income annually.

- Q.2 (a) It consisted of five sub-parts. In each part a situation was given and the students were required to explain the tax treatment. Each part is discussed hereunder:
- i. Few students incorrectly assumed capital gain on disposal as exempt, on the assumption that since loss on disposal of “sculpture/antique” is not recognized, therefore, “gain” on the disposal of capital assets should also be excluded from the taxable income. Many students failed to mention the fact that 75% of the gain will be taxable, as the asset was held for more than 12 months.
 - ii. The candidates were not updated on the recent changes brought through Finance Act 2006 according to which the rental income became chargeable to tax under FTR at the rate of 5 percent. However, most of them did know that forfeited deposit is included in the definition of rent.
 - iii. Most students failed to specify that assets held for personal use are excluded from the definition of capital assets and therefore, proceeds from sale of car held for personal use are not chargeable to tax.
 - iv. Very few examinees knew that if any Pakistani citizen leaves Pakistan during the year and remains abroad during that tax year, his foreign source income is exempt from tax even if the tax payer remains a ‘resident’ according to the provisions of ITO 2001. Further, the ITO-2001 does not determine the incidence of tax on the basis of receipt of income, rather the thrust is on the place from where the income has been derived.
 - v. Most examinees were able to state correctly that tax deducted from payments for services shall be treated as final tax.
- (b) It was a straightforward question of four marks but surprisingly very few seemed to have read Sections 35(2) & 35(4). Most of the examinees got confused and explained the valuation of stock as mentioned in Sections 35(5) & 35(6) of the ITO 2001.
- Q.3 (a) A very poor response was observed in this part of the question. Majority of the examinees tried to explain the dictionary meaning of the terms and that too in a very casual manner. It is important to note that law conceives the definition of a term in a very specific manner and it should be explained accordingly.

- (b) It was an easy computational question on advance tax liability. Unfortunately, a large number of students did not manage to secure good marks. Common errors were as follows:
- There was a general lack of understanding about the method of calculating advance tax liability.
 - Quarterly liability (Gross) is determined simply by dividing the assessed tax of the latest tax year by four. The net amount payable for the quarter is determined by deducting the payments/deductions at source from the gross liability for the quarter. Instead, many students deducted the payments/deductions at source from the tax assessed for the latest year and then divided the net figure by four to arrive at the liability for the quarter.
 - Most of the examinees went on to calculate the income other than capital gain and dividend which was not required.
- Q.4 (a) The performance of examinees was average. Following common mistakes were observed:
- Many examinees mixed up the answers and failed to point out the real difference between straight deduction allowable in the case of donations mentioned in the Second Schedule and tax credit allowed in respect of other approved donations.
 - A large number of examinees failed to mention that donations under section 61 of the ITO-2001 should be made through banking channel.
 - The examinees were expected to mention the limit of donation i.e. 30% of taxable income, which was ignored by many students.
- (b) Most of the candidates were able to answer the question correctly, in accordance with Sections 19 and 58 of ITO 2001.
- Q.5 (a) The performance of many students was satisfactory and they managed to gain good marks by explaining the relevant provisions as given in Sections 81, 82 and 83 of the ITO 2001. However, there were few who did not know what was actually required from them and ended up discussing the taxability of resident and non resident persons. Few candidates gave incomplete answers i.e they explained the residential status of an individual only whereas the question required the residential status of all tax payers i.e Individual, Company and AOP.
- (b) This part relating to modes of recovery available in case of non-payment of tax was correctly answered by most of the examinees in accordance with Section 138 of the ITO 2001.
- Q.6 (a) This was a well attempted question and majority of the candidates were able to identify the types of capital assets on which capital loss cannot be claimed as narrated in section 38 of the ITO-2001.
- (b) This was also a very simple question from section 116 of the ITO-2001 and most of the candidates attempted it well and secured full marks.

- Q.7 (a) Very poor response was seen in defining the terms ‘taxable supply’ and ‘taxable activity’ in the context of law phrased in the question. Most of the explanations were given in a very ordinary manner without depicting the real intent of law involved in such terms.
- (b) This was a simple and straightforward question from Rule 4 of the Sales Tax Rules 2006. A mixed response was generally witnessed. The most common mistake was that instead of mentioning that registration becomes compulsory for manufacturers and retailers when their turnover in the ‘last twelve months’ exceed specified limit, many students incorrectly mentioned the term ‘last tax year’.
- Q.8 This was also a straightforward question and an average attempt enabled many examinees to get considerable marks. The common mistakes were as follows:
- Few candidates incorrectly charged sales tax at the rate of 15% on exempt as well as zero rated supplies.
 - Majority of the examinees did not explain that Rs. 3 million which was payable since December 20, 2006, will have no impact on the sales tax liability because the amount was due for less than 180 days.
 - Instead of deducting the amounts of penalty, arrears and surcharge, some candidates added these to sales tax refund amount.
 - Few examinees ignored the effect of credit note of Rs.500,000.
 - Majority of the students didn’t apportion the input tax between taxable supplies and exempt supplies.

(THE END)