



**THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF
PAKISTAN (ICPAP)**

Stage	Professional (Old)	Course Code	XII
Examination	Winter-2011	Course Name	Advanced Taxation
Time Allowed	03 Hours	Maximum Marks	100

NOTES:

1. All questions are to be attempted.
2. Answers are expected to be precise, to the point and well written.
3. Neatness and style will be taken into account in marking the papers.
4. Income Tax Rates sheet is provided.

Question No 1: Mr. Saleem is a telecommunication engineer working with Mobilink as their chief technical officer for the last many years. He has provided you with the following information relating to his assessment for the year ended June 30, 2011.

- i. Monthly salary of Rs. 600,000 was paid to him by the company consisting of the following:

	Rupees
Basic Salary	500,000
Medical allowance	40,000
Conveyance allowance	60,000

- The salary was credited to his bank account on the 28th of every month. He incurred actual medical expenses of Rs. 150,000 during the year. These expenses were reimbursed to him by the company in accordance with the terms of his employment.
- ii. He received a bonus of Rs. 1.0 million. Employer also agreed to pay tax on such bonus to the extent of Rs. 100,000.
 - iii. Apart from his employment with a Mobilink, he also served as a visiting faculty member at a local engineering university and received a total of Rs. 470,000. Mr. Saleem incurred an expenditure of Rs. 70,000 towards this service. Withholding tax was deducted from the payments made by the university.
 - iv. In August 2010, he participated and won a quiz competition arranged by Pakistan Urdu Academy. The prize money of Rs. 200,000 was paid to him after deduction of a tax of Rs. 40,000.
 - v. He inherited a plot of land from his father on his death in July 2000. On October 1, 2010 he entered into a contract of sale with Mr. Mohsin for a consideration of Rs. 50.0 million. Mr. Mohsin paid a deposit of Rs. 1.0 million and agreed to pay the balance within one month of the date of contract. On due date, Mr. Mohsin defaulted in making the payment upon which Mr. Saleem forfeited the deposit in accordance with the terms of the contract. Later on, the plot was sold to Mr. Pervaiz at a price of Rs. 50.0 million.

- vi. Mr. Saleem purchased another plot of land for a consideration of Rs. 56 million. He borrowed Rs. 5.0 million from his sister for the purchase of this plot. The amount was received in cash.
- vii. Mr. Saleem also inherited a painting from his father. The painting was valued at Rs. 500,000. On April 1, 2011 he gifted the painting to his brother who came from Canada after five years. He went back to Canada after staying in Pakistan for a period of two months. The value of the painting was Rs. 1.0 million when it was gifted.

Required:

Compute the taxable income of Mr. Saleem for the tax year 2011. Give brief reasons under the Income Tax Ordinance, 2001 in support of your treatment of each of the above items.

(20 marks)

Question No 2: Javed Pharmaceuticals Co (JPC), a partnership firm, registered under the Partnership Act 1932, is in the business of manufacturing pharmaceuticals. The assessment of JPC for the tax year 2011 (accounting year ended 30 June 2011) was selected for audit under s.177 of the Income Tax Ordinance, 2001.

- 1) On completion of the audit, the Commissioner informs JPC that he intends to amend the assessment for the tax year 2011 to:
 - i. Levy minimum tax of 0.5% on the firm's turnover of Rs. 18,000,000.
 - ii. Disallow Rs. 1,830,000 out of travelling expenses, being the travel and hotel expenses for JPC's technical manager's visit to Japan.
 - iii. Disallow Rs. 500,000 being the contribution paid by JPC to the unrecognized Javed Employees Provident Fund.
 - iv. Disallow Rs. 175,600 expended on the annual Eid-Milan party for JPC's employees and their families.
 - v. Disallow Rs. 1500,000 being damages paid to JPC's sole distributor.
 - vi. Disallow the donation of Rs. 1,000,000 paid to a hospital.
 - vii. Disallow the Rs. 1,200,000 salary paid to Mr Akram.

The Commissioner has required JPC to furnish explanations/reasons as to why he should not amend the assessment on the lines indicated.

- 2) The following information on the issues raised by the Commissioner is provided to you:

- i. Minimum tax
JPC was not aware of the concept of minimum tax payable.

- ii. Travelling expenses

The travel to Japan was entirely for business purposes. It was necessary for the firm's technical manager to travel to Japan for the purpose of selecting a second-hand mixing machine, so as to ensure that the machine was compatible with the company's existing plant.

- iii. Contribution to the unrecognized provident fund.

JPC, in its accounting system, has ensured that when any payment is made from the fund to an employee, tax would be deducted at source from the amount of the payment, if the amount is chargeable to tax as the salary income of the employee.

iv. Eid-Milan party

The expenditure on the party was motivated by the purpose of maintaining cordial relations between the employees and the management.

v. Damages paid to the sole distributor

Due to the failure to deliver supplies within the time stipulated in the contract, JPC had to pay damages to their sole distributor. The failure to deliver the supplies in time was due to the negligence of the dispatch department of the firm and not due to the violation of any law.

vi. Donation

The donation was not paid to any private hospital but to a hospital which was established in Pakistan by the Federal Government.

vii. Salary paid to Mr. Akarm

Mr. Akarm is a partner in the firm of JPC. He is also the Chief Executive Officer (CEO) of the firm devoting his fulltime to managing the affairs of the firm. His salary was approved by the partners.

Mr. Akarm, as CEO of JPC, wants you to explain the relevant statutory tax provisions on the issues raised by the Commissioner.

Required:

State giving reasons whether or not in each case, the amendment proposed by the Commissioner is or is not in accordance with the provisions of the Income Tax Ordinance 2001.

Note: the allocation of marks is as follows:

(20 marks)

Question No 3: Mr. Raheel is evaluating the possibility of starting a large scale import and retail business of consumer goods through a chain of stores supplying to wholesale as well as general body of consumers.

Required:

- a) Advise him about the payment of advance tax at the import stage and the treatment thereof, under the Income Tax Ordinance, 2001.
- b) With reference to Sales Tax Act 1990, advise him on the following:
 - i. Whether he will be required to obtain separate registration for each outlet?
 - ii. Will he be classified as a retailer specially with reference to the supplies made other than to the general body of consumers?
 - iii. Can he claim input tax on his purchases? Assume that 30% of all sales will be collected in cash.

(10 marks)

Question No 4: Ufone Limited, a listed company, has made the following payments without deduction of withholding tax:

- a) Reimbursement of boarding, lodging and incidental expenses incurred by nonexecutive directors of the Company for attending the Board's quarterly meeting held in Dubai.
- b) Payment to a non-resident debtor on account of out of court settlement of a dispute and payment of fee to the lawyer for handling such settlement. The lawyer was also a non-resident.
- c) Payment to a resident company as consideration for obtaining a right to manufacture certain goods.
- d) Reimbursement made to a foreign associate in respect of salary of the Director Finance of Ufone Limited. The Director Finance is a foreign national and receives part payment of his salary in his home country. The foreign associate had not deducted any tax from the payment made by it to the Director Finance.

Required:

Comment on the above transactions in the light of Income Tax Ordinance, 2001.

(10 marks)

Question No 5:

- i. Brown Chemical Limited (BCL) is engaged in the manufacturing of chemical products. The Company has three branches in Pakistan and one branch each in Qatar and Oman. BCL sells its products through various distributors. Assume that the company's profit and loss account and the related details for the period ending June 30, 2011 are as under:

	Rs. in '000
Sales	96,000
Cost of sales	<u>(66,850)</u>
Gross profit	29,150
Administrative and selling expenses	(10,600)
Finance cost	(3,100)
Other charges (including WWF of Rs. 0.50 million)	(2,400)
Other income	4,100
Profit before taxation	<u>17,150</u>

Cost of sales includes:	Rs. in '000
Accounting depreciation	3,200
Provision for slow moving stock	1,300
Demurrage paid to custom authorities	100
Royalty paid against manufacturing rights to a non-resident	1,200

Administrative and selling expenses include:	Rs. in '000
Accounting depreciation	8,00
Damages paid to distributors on breach of contract	300
Provision for bad debts	1,100
Small items of office equipment charged off (useful life more than 1 year)	1,400

Opening and closing balance of provision for bad debt account was Rs. 2.50 million and 3.10 million respectively. Bad debts written off during the year include an interest free loan of Rs. 0.20 million provided to Oman branch.

Finance cost includes unrealized exchange loss of Rs. 1.35 million and interest of Rs. 1.30 million paid on a working capital loan acquired from a non-resident foreign bank. No tax was deducted by the company on payment of interest considering the bank did not have any permanent establishment in Pakistan.

Other income includes:	Rs. in '000
Profit from Qatar branch	2,700
Loss from Oman branch	(3,400)

Tax depreciation for the year was Rs. 6.00 million. There was also a carried forward tax loss of Rs. 6.10 million and an unadjusted foreign tax credit of Rs. 0.12 million from tax year 2009. Following taxes were paid by the company during the year:

	Rs. in '000
Deducted and paid by distribution	2,450
Paid on import of raw material	(3,400)
Taxes paid in Qatar	225
Unadjusted minimum tax for prior years	450

Required:

Compute the income tax liability of the company for the tax year 2010. Tax rate applicable to the company is 35%.

(15 marks)

ii. Please reply:

a) If the assessee is not satisfied with the decision of commissioner of Income Tax (appeals) he can file second appeal to _____

(1½ marks)

b) The assessee is required to file wealth statement along with Return of Total Income whose declared income exceeds is Rs. _____

(1½ marks)

c) Whether an assessee whose income from property exceeds Rs. 1000,000 can claim repair & maintenance allowance?

(2 marks)

(5 marks)

Question No 6:

i. Explain

- a) Zero rated supply
- b) Input Tax
- c) Output Tax
- d) Tax period
- e) Taxable goods

(5 marks)

ii. Pakistan Dairy Form (Pvt.) Limited is a registered manufacturer of ice cream. Data regarding his business for the month of June 2011 is given below:

1. Sales of ice cream to registered persons	Rs. 3,00,000
2. Sales of ice cream to consumers (inclusive of sales tax)	1,50,000
3. Supplies of ice cream to school children (during factory visits)	20,000
4. Sales of ice cream to non-registered persons	1,00,000
5. Sales of dairy products to retailer	2,00,000
6. Purchases of milk and vegetables without brand names	70,000
7. Purchases of milk and vegetables from registered persons under brand names	50,000
8. Purchase of cream from non-registered person	80,000
9. Ice cream flavor imported	30,000
10. Purchases of syrup from wholesaler (used in ice cream)	18,000

Required:

Calculate his sales tax payable.

(15 marks)

(THE END)