THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN CERTIFICATE IN ACCOUNTING AND FINANCE (CAF) EXAMINATIONS EXAMINERS' COMMENTS	
SUBJECT Principles of Taxation	**SESSION** Spring 2020

Passing %

Question-wise								Overall
1	2	3	4	5	6	7	8	
29%	50%	32%	18%	44%	66%	26%	45%	39%

General comments

The overall performance improved significantly from Autumn 2019 as the pass percentage increased from 31% to 39% in Spring 2020. Question numbers 2 and 6 were attempted well by majority of the examinees whereas question numbers 1, 3, 4 and 7 proved to be more challenging to the examinees. The underperformance in these questions may be attributed to selective studies and paying little attention towards theoretical questions. With particular reference to question number 4, poor presentation and failure to apply theoretical knowledge to practical situations seemed to be the main reasons for low marks.

Question-wise common mistakes observed

Question 1

- Sources of income were not classified under appropriate heads.
- Examinees failed to comprehend that only the difference between the values of closing stock under absorption cost and prime cost were to be added to the accounting profit. Whereas, difference between the opening balances of the stock-in-trade under the two methods required no adjustment.
- The whole amount of packing material was considered as inadmissible deduction whereas only 20% of the amount was inadmissible.
- Freight charges and salary paid to brother were considered as inadmissible whereas penalty of Rs. 15,000 was treated as admissible deduction.
- Examinees considered Rs. 950,000 incurred on the development of a product as admissible deduction in the same period whereas it was to be amortized over the period of five years.
- Unabsorbed tax depreciation was adjusted against 'Total income' instead of 'Income from business'.
- Examinees failed to appreciate that the value of profit on debt was gross of withholding income tax and zakat. Moreover, in some of the cases, profit on debt was not reclassified as "Income from other sources" being FTR income.

- Examinees failed to gross up the amount of capital gain at Rs. 51,750.
- Examinees did not reclassify agriculture income as 'exempt income'.
- Examinees failed to appreciate that the tax credit of Rs. 15,000 earlier claimed on purchase of shares in Metal Limited was to be reversed as these shares were disposed of within 24 months of purchase.
- Tax deducted at source by customers of Rs. 875,000 was treated as admissible deduction whereas no tax credit was claimed against the taxes deducted at source by customers on capital gain and fixed deposit account while computing the final tax liability..

Question 2

- In case of AOP, salaries and interest paid on capital to partners were not considered as inadmissible deductions. Similarly, in the hands of individual members of an AOP, these amounts were not considered as part of their taxable income for rate purposes.
- Kamran's share of loss from second AOP was adjusted against his share of profit from first AOP for computing taxable income for rate purposes. On the other hand, many examinees did not add his income from sole proprietorship business for calculating his total taxable income.
- Tax liability of Kamran on income from other sources was ignored.
- The amount of dividend received by Rehan was not considered as FTR income and the net amount of dividend instead of the gross amount was added to his taxable income.
- Examinees failed to appreciate that members of AOP who did not have any other source of income, were not liable to pay any tax on their income from AOP.
- Examinees were of the opinion that Farhan and Rehan were also liable to pay tax on their income.

Question 3(a)

Most of the examinees failed to appreciate that entertainment expenditure is allowed as admissible deduction only when incurred on:

- deriving business income chargeable to tax
- entertainment of persons directly related to the business
- entertainment of foreign customers and suppliers in Pakistan

Question 3(b)

- Examinees failed to comprehend that filing of foreign income and asset statement applies only to 'individuals who are resident tax payers.'.
- Examinees ignored the fact that the Commissioner may, by a notice in writing, require any individual to furnish the foreign income and asset statement.
- Examinees thought that following are the particulars which should be included in foreign income and asset statement:
  - wealth reconciliation statement
  - list of assets and liabilities
  - comparison of average rate of Pakistani tax in respect of foreign tax withheld by foreign Government

Question 3(c)

- Examinees did not know the meaning of concealed assets and resorted to guess work.
- Examinees were of the opinion that the Commissioner-IR is empowered to sell the concealed assets in the auction and transfer the amount received to Government treasury.
- Examinees failed to acknowledge that while issuing the assessment order the Commissioner, shall take into account the computation of taxable income and tax payable for the last completed tax year of the person during which the concealed asset was accounted for.

Question 4(a)

- Examinees failed to comprehend that flat received by Sadiq as a gift from his uncle was to be added to capital gain at the fair market value of Rs. 4,500,000.
- Examinees also failed to appreciate that non-recognition rule applies only when a gift is received from grandparents, parents, spouse, brother, sister, son or a daughter.

Question 4(b)

- Examinees failed to comprehend that the insurance claim received was to be apportioned between the two sculptures in the ratio of their respective fair market values at the time of loss and then the respective cost was to be reduced therefrom to determine the gain or loss.
- Examinees instead of determining gain / loss separately for each sculpture, performed calculation on aggregate basis by deducting cost of sculpture of Rs. 885,000 from consideration received of Rs. 940,000.
- Examinees also failed to restrict the amount of capital gain to 75% of the total gain in view of the holding period which was more than one year.

Question 5(a)

Many examinees failed to appreciate that since A's total income was less than Rs. 200,000, his income was not chargeable to tax. Whereas in case of B, the income was chargeable to tax due to his other source income.

Question 5(b)

- Examinees failed to appreciate that leave encashment was chargeable to tax under the head 'Salary'.
- The exemption limit of unapproved gratuity was wrongly considered to be Rs 150,000 .
- Examinees considered fair market value of the vehicle as fully taxable.

Question 6

In case of Taha

- Input tax on machinery was apportioned on taxable supplies, exempted supplies and zero rated supplies despite the fact that it was specifically mentioned in the question that machinery was used for exempt and zero rated supplies.
- Examinees failed to adjust inadmissible input tax relating to exempt supplies from total input tax. Similarly, input tax on zero rated supplies was not shown as refundable.

In case of Shan

- Input tax on machinery was wrongly apportioned between taxable and exempt supplies.
- Excess of input tax over output tax was erroneously considered as refundable where in fact it was to be carried forward.

Question 7(a)i

Examinees were of the opinion that since Raheel was operating as a retailer and would have been paying sales tax through electricity bill, he was not required to be registered.

Question 7(a)ii

Many answers were limited to the statement that Raheel should respond to the notice within the specified time otherwise Commissioner would compulsorily cause to register him through computer system.

Question 7(b)i

Good performance was observed in this part of the question.

Question 7(b)ii

- Few examinees were of the view that immovable property or personal assets of the taxpayer may also be attached for the recovery of tax liability.
- In view of some of the examinees, following were the circumstances in which the Inland Revenue Department may recover the amount of sales tax without issuing a show cause notice:
  - Person is about to leave Pakistan permanently.
  - Person transferring his assets to another person.
  - Issuance of fake invoices.

Question 7(b)iii

Examinees mixed-up the concept of 'residual input tax' with provisional and final adjustment in relation to apportionment of input tax.

Question 8(a)

Examinees performed well in this part of the question. However, some of the examinees discussed cannons of taxation which was totally irrelevant.

Question 8(b)

Good performance was observed in this part of the question.

The End