

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN	
EXAMINERS' COMMENTS	
SUBJECT Advanced Taxation	SESSION Certified Finance & Accounting Professional (CFAP) Examination Winter 2016

General:

The examination consisted of seven questions. Approximately, 58 percent of the marks were allocated for computational skills and remaining 42 percent for essay based questions.

Although the result was better than the last attempt, however, the overall performance remained unsatisfactory. Except for question numbers 2 and 4 the performance in every question remained below average. Particularly question numbers 5(a) and 7(c) were extremely disappointing.

Inadequate knowledge mainly of those areas which are tested less frequently, use of inappropriate terms or vague language and failure to apply the legislation to the facts of the questions were some of the reasons for the low score. Candidates are advised to pay particular attention to the requirement as well as marks allocated to each question, as the marks have a strong bearing on the time which should be allocated to answer each question.

Question-wise comments are as under:

Question 1

This question required candidates to compute, under the correct head of income, the total income, taxable income and net tax payable by or refundable to a listed company (MTL) engaged in the business of manufacturing, export and supply of various products and services. It was a straight forward question; however, astonishingly candidates' performance remained below average. Most of the candidates committed following errors in the answer scripts:

- (i) Some of the information had no impact on the answer/computation but according to the requirement of the question candidates were required to show all relevant exemptions and exclusions in their working. Many candidates failed to show such exemptions/exclusions.
- (ii) A number of candidates failed to consider that on account of 'interior decoration services', tax on the basis of net profit was more than the tax withheld, therefore, the minimum tax regime was not applicable and the difference in tax was required to be paid by MTL along with the return of income.
- (iii) Many candidates considered 20% of the entire purchase of imported beverages of Rs. 6,900,000 as inadmissible because of failure of MTL to deduct withholding tax from the payment. Only few candidates appreciated that 60% of the total purchases which were sold in the same condition as they were imported, were admissible. Further, many candidates treated all the remaining 40% as inadmissible whereas only 20% of the remaining 40% should have been added back.

- (iv) A number of candidates incorrectly computed tax depreciation on fixed assets in proportion to the number of days in use. Some of the candidates also computed initial allowance of depreciation on furniture and fixtures.
- (v) Rent of machinery was incorrectly classified as “Income from Other Sources” instead of income under FTR.
- (vi) Many candidates failed to appreciate that income arising from ‘Web hosting services’ were exempt from tax.
- (vii) Many candidates failed to comprehend that, under the provisions of section 161 of the Ordinance; uncollected withholding tax of Rs. 9,000 on sale of beverages to distributors was to be paid by MTL along with the return.
- (viii) Majority of the candidates ignoring the requirement of the question did not compute total income.
- (ix) Some candidates, ignoring the requirement of the question, also computed ‘Minimum Tax’, ‘Alternative Corporate Tax’ and default surcharge.

Question 2

This question required candidates to briefly describe **five** fundamental principles of ethics for tax practitioners. Majority of the candidates performed well in this question.

Question 3

This question was divided into three parts (a), (b) and (c). Part (a) asked candidates to list the circumstances in which every person who has been issued a National Tax Number (NTN) is required to quote their NTN. Part (b) required candidates to describe the circumstances in which a Commissioner may recharacterise or disregard a transaction. Part (c) consisted of four independent situations and candidates were asked to discuss the tax treatment in each situation.

Question 3(a)

The performance in this part remained very poor. Majority of the answers were incomplete and were only confined to the statement that NTN should be quoted on all invoices and cash memos issued or returns filed by the taxpayer. The candidates may refer to Rule 83(2) of the Income Tax Rules, 2002 for a complete answer.

Question 3(b)

The performance in this part remained satisfactory. However, some candidates did not seem to distinguish between fraudulent evasion of tax and tax avoidance scheme. It must be appreciated that evasion of tax is a criminal offence under the Income Tax Ordinance, 2001 whereas ‘tax avoidance scheme’ refers to those transactions which are legitimately entered into for the purpose of avoiding or reducing the tax liability of any person under the Ordinance.

Question 3(c)

The performance in each of the sub-parts is discussed below:

- (i) The performance in this part remained average. Majority of the candidates stated correctly that the cash loan shall be treated as income of the borrower but did not specify the relevant head of income i.e. Income from other sources. Moreover, a sizeable number of candidates were of the view that since the loan has been received from the brother it is personal in nature and as such has no tax implication.
- (ii) The performance in this part remained below average. Many candidates stated that sale of securities with the condition to acquire them back tantamount to Wash Sale which was incorrect as well as irrelevant. Majority of the candidates failed to appreciate that Rs. 52,500 shall be taxable in the hands of Wahab under the head *income from other sources* because the transfer was made with an understanding that Naeem would buy back the shares.
- (iii) The performance in this part remained satisfactory as almost all students performed well.
- (iv) The performance in this part remained average. Some of the candidates thought it to be the case of Group Relief as discussed under section 59B of the Income Tax Ordinance, 2001. They were of the opinion that losses can only be claimed if Gama Limited continues to carry on its business for the next five years whereas the actual rule is different and can be seen in section 98 of the Income Tax Ordinance, 2001.

Question 4

This question was related to the Sales Tax Act, 1990, Federal Excise Act, 2005 and Rules made thereunder. It required candidates to compute sales tax payable by or refundable to a registered person [Arzu Limited (AL)] in a given tax period. The overall performance in this question remained average. Following common errors were found in the answer scripts:

- (i) Many candidates ignored the fact that under the given circumstances, taxable value of imported finished goods should be restricted to 60% of the import value as AL cannot claim input tax on such portion of import on which duty/sales tax has not been paid. A number of candidates also failed to compute the 'value addition tax' on commercial imports.
- (ii) Input tax paid on agricultural equipment, governed under the Eight Schedule, was considered to be admissible.
- (iii) Many candidates failed to realize that debit note received from the supplier cannot be claimed unless a corresponding credit note has been issued.
- (iv) A number of candidates failed to appreciate that if a person is blacklisted, the refund or input tax credit claimed against the invoices issued by such person, whether prior or after such blacklisting, shall be rejected. Therefore AL was required to reverse the input tax of Rs. 85,000 claimed in October 2016 on purchase of taxable goods from ME.

- (v) Supply of chemical to registered manufacturers belonging to five major export sectors was considered taxable instead of zero rated.
- (vi) Many candidates did not realize that sales tax withholding on supplies to un-registered person was to be made on grossed up basis.
- (vii) A number of candidates failed to appreciate that sales tax was required to be withheld on purchase of agricultural equipment.
- (viii) Majority of the candidates failed to appreciate that sales tax under the Sales Tax Act, 1990 is not required to be withheld from the payment made against courier and shipping charges.
- (ix) Further tax charged on supplies to un-registered customers and extra tax on biscuits [covered under Chapter XIII of Sales Tax Special Procedure Rules, 2007] was wrongly considered as part of output tax.
- (x) Many candidates failed to elucidate that supply of biscuits was exempt from the levy of further tax, being made to an end consumer.
- (xi) Some candidates did not compute the amount of residual input tax and adjusted the entire amount of input tax against output tax liability.

Question 5

This question was divided into two parts (a) and (b) and was related to the provisions of Federal Excise Act, 2005 and Rules made thereunder. Part (a) was further divided into two sub-parts (i) and (ii). Part (a)(i) and (ii) required candidates to briefly describe the provisions relating to 'Filing of revised return' and 'Filing of special return in respect of goods and services' respectively. Part (b) was scenario based and required candidates to compute the amount of duty payable by a firm in a situation where the firm had failed to file its excise duty return and pay the amount of duty on due date.

Question 5(a)

Candidates performance in part (a)(i) remained average as about half the candidates gave the correct answer. However, two incorrect views were generally expressed by the candidates i.e. that a return could be revised within 90 days of the filing of the first return or within one year; as against the correct limit of 120 days.

The performance in part (a)(ii) was very poor. Majority of the candidates had little understanding about filing of special return. They thought that a special return is filed either in case of closure of business or disposal or sale of a business. Some candidates stated that the Commissioner may require a person to file the special return. The candidates are advised to refer to Section 4(5) of the Federal Excise Act, 2005.

Question 5(b)

The performance in this part remained satisfactory. However, some candidates failed to appreciate that default surcharge was only to be calculated on the amount of duty due and not the amount of penalty of Rs. 50,000 which was payable to the Sindh Revenue Board.

Question 6

This question required candidates to compute the taxable income and tax payable by or refundable to an individual taxpayer. The question also asked candidates to give reasons for their treatment of item numbers (ii), (iii) and (v) in the question.

The overall performance was below average. A number of mistakes were observed. Some of the commonly observed mistakes were as follows:

- (i) Only handful of candidates were able to comprehend that gross receipts on sale from embroidery business, classified under the head “Income from Business”, were taxable under FTR. Many candidates wrongly considered that in respect of embroidery business, tax is payable on ‘net income basis’, thus profit before tax figure given in the question was taken as “Income from Business”.
- (ii) Many candidates failed to appreciate that according to Rule 13P(r) of the Income Tax Rules, 2002, the sales proceed on disposal of letter of rights is treated as capital gains. Many candidates did not understand that the letter of rights have been sold and were of the view that these have been utilized i.e. the shares had been subscribed. Various other basic errors were also witnessed in the computation of capital gains on the sale of shares; which are not expected at this stage.
- (iii) Gain on disposal of cow held for personal use was wrongly treated as taxable. Among those who correctly considered it as exempt, many could not give the proper reason i.e. because the cow was not a business asset. They thought that it was exempt because of being agricultural income.
- (iv) Many candidates considered gain on disposal of shares by way of gift to be exempt from tax on the presumption of non-recognition rule. They failed to appreciate that the non-recognition rule does not apply where the person receiving the gift is a non-resident.
- (v) In order to determine the gain or loss on settlement of claim of paintings, many candidates wrongly apportioned the insurance claim received in proportion to the cost of the paintings instead of their fair market values. Moreover, loss arising on ‘Painting I’ was incorrectly considered to be adjustable against other capital gains.
- (vi) The amount of total income was not computed.

Question 7

This question was divided into three parts (a), (b) and (c). Part (a) was further sub-divided into two parts (i) and (ii). It was based on Sales Tax Act, 1990 and required the candidates to explain when an order is treated to be properly served on a resident individual other than in a representative capacity and also on association of persons when the association has already been dissolved. Part (b) pertained to the provisions of Sales Tax Special Procedures Rules, 2007 and asked candidates to state the circumstances in which the value addition tax is not charged on import of taxable goods. Part (c) pertained to Provincial Sales Tax on Services Acts and required candidates to describe the terms ‘Provision of service or providing of service’ and ‘Public relations services’.

Question 7(a)

The overall performance in part (a) was satisfactory. However, in sub-part (a)(i) very few candidates acknowledged that the notice served on a representative of an individual is only considered properly served if the individual suffers any legal disability. Similarly, only few candidates were aware that a notice served on the person in a manner prescribed for service of summon under the Code of Civil Procedure, 1908 is also treated as a notice properly served on a resident individual.

In response to (a)(ii), majority of the candidates did not mention that service of notice on any person who was the principal officer of an association of persons immediately before its dissolution is also treated to be properly served.

Question 7(b)

The performance in this part remained satisfactory as most of the candidates gave the correct answer.

Question 7(c)

The performance in this part of the question was very disappointing and majority of the candidates did not attempt it altogether. Most of those who attempted the question produced variety of answers based on absolute guess work. The performance was clearly indicative of selective studies.

(THE END)