QUESTION NO. 1

(a) ACCUMULATED PROFITS [SEC. 2(1)]

(i) Any reserve maintained by an organization out of its profits.

(ii) All the profits of the company kept in whatever shape, whether capitalized or not upto the date these are distributed.

(iii) In case of liquidation of company or trust, its all profits upto the date of liquidation.

Explanation:

Many business organizations do not distribute their all profits among the shareholders. They keep a part of profits as reserve to meet the unseen or unexpected expenditures of the future. It must be noted that the amount of reserve may ultimately be distributed among the shareholders or owners.

(b) PAKISTAN SOURCE INCOME [SEC. 2(40)]

Pakistan-source income includes the income which a person earns in Pakistan, irrespective of the fact that where it is actually received. Some examples of this income are as follows:

Salary Income:

(1) Salary received by virtue of employment in Pakistan, wherever paid.

(2) Salary paid anywhere in the world by or on behalf of the federal government or provincial government or local authority in Pakistan.

Business Income:

(1) Income derived from any business carried on in Pakistan.

(2) Business income of a non-resident person from a permanent establishment in Pakistan.

Dividend Income:

Any dividend paid by a resident company.

Profit on Debt:

Profit on debt paid by a resident person, if the profit is from a business carried on in Pakistan.

Royalty Income:

(1) Rental income derived from the lease of immovable property in Pakistan.

(2) Rental income from the lease of a right to explore natural resources in Pakistan.

Pension or Annuity:

Any pension or annuity paid by a resident.

Technical Fee:

Any technical fee paid by a resident person from the business carried on in Pakistan.

Capital Gain:

Any gain from on the disposal of shares of resident company.

(c) DIVIDEND [SEC. 2(19)]

According to income tax ordinance 2001, the following distributions made by the company are considered as dividend:

(i) Distribution to shareholders out of current years profit.

(ii) Distribution to the shareholders out of accumulated profit.

(iii) Distribution to the shareholders out of share premium received by a company.

(iv) Distribution to the shareholders in form of debentures or debenture stock out of accumulated profit.

(v) Distribution to the shareholders at the time of liquidation to the extent accumulated profit.

(vi) Distribution to the shareholders at the time of reduction of capital to the extent of accumulated profit.

(vii) Distribution to the shareholders by a private company or trust in form of loan and advance out of accumulated profit.

Note: *It is not necessary that dividend must be paid in cash, it can be paid in money's worth.*

(d) PRINCIPAL OFFICER

See Paper 2014 Question No. 1(c)

QUESTION NO. 2

(i) AGRICULTURAL INCOME

Tax Treatment = Totally Exempt

(i) Upto assessment years 1987–88, the agricultural income was not included in the total income of a taxpayer.

(ii) Through Finance Ordinance 1988, it was decided that the agricultural income shall be included in total income but only for rate purpose by a person who has business income or he is a director of company and receiving salary.

(iii) According to assessment year 2002–03, if a person has agricultural income upto Rs. 80,000 alongwith other incomes then same tax rates or procedure shall be applied or used as applied on other incomes and if the agricultural income is above Rs. 80,000 in total income then different tax rates or procedure shall be applied.

(iv) From tax year 2007, there is no difference in applying tax rates or procedure of calculating tax on taxable income irrespective of the amount of agricultural income. It means same tax rates or procedure shall be used to calculate the amount of tax whether the agricultural income is upto Rs. 80,000 or more than Rs. 80,000.

Note: *It is also notable that in all above cases, the agricultural income remained totally exempt.*

(ii) PENSION

Tax Treatment = Totally Exempt

Legal Provisions:

- Received from United Nations or its specialized agencies.
- Received by an employee of Pakistan Armed Forces.
- Received by an employee of Federal Govt.
- Received by an employee of Provincial Govt.
- Received by Public Servant or personal of Armed Forces due to injuries or bodily disabled.
- Received by dependents of SHAHEEDS.
- Received by any citizen of Pakistan from his former employer.

Notes:

(1) If a person receives more than one pensions, only the amount of higher pension will be exempt.

(2) Exemption will not be available if a retired person works for the same employer in any capacity.

(iii) PROFIT ON DEBT

Any amount received, as profit on debt shall be:

Tax Treatment = Totally Exempt

Legal Provisions:

(i) Profit on debt to any non-resident person against loan approved by Federal Government.

(ii) Profit on loan in foreign exchange against export letter of credit which is used exclusively for export of goods manufactured or processed for exports in Pakistan.

(iii) Profit on debt to a foreign individual, company, firm or association of persons in respect of a foreign loan for industrial sector in Pakistan on or after the first day of February, 1991 under the agreement registered with the State Bank of Pakistan. (This exemption shall not be applicable to new contacts after 30.06-2010).

(iv) Profit on debt to Hub Power Company Limited on its bank deposits or accounts with financial institutions.

(v) Profit on debt under an approved loan agreement or in respect of foreign currency instrument of an agency of foreign government, foreign national or other non-residents.

(vi) Profit on debt from foreign currency accounts held with the authorized banks in Pakistan or certificate of investment issued by investment banks.

(vii) Profit on Rupee account held with a scheduled bank in Pakistan by a Pakistani residing abroad and the deposits are created from his remittances.

(viii) Profit from private foreign currency accounts held with the authorized banks in Pakistan or certificate of investment issued by investment banks only on such deposits as were on 16-12-1999.

QUESTION NO. 3

PROVIDENT FUND

For income tax purposes provident funds can be classified into the following three categories:

(1) Government provident fund

(2) Recognized provident fund

(3) Un-recognized provident fund

(1) GOVERNMENT PROVIDENT FUND:

A provident fund maintained by government, or semi government organizations like railways, universities, local authorities etc. is known as Government provident fund or statutory provident fund.

Tax Treatment

The tax treatment of contribution of the fund and payment therefrom are as under:

Employee's Contribution:

Employee's own contributions to the fund are already included in his annual salary and chargeable to tax in the hands of employee.

Employer's Contribution:

Employer's contributions are neither to be included in the annual salary of the employee nor are taxable in the hands of employee.

Interest on Accumulated Balance:

Interests on Accumulated Balance both on employee's own contribution and employer's contributions are not included in total income.

Payment of Accumulated Balance:

Accumulated Balance at the credit of an employee received on retirement or death is not included in total income of the employee in the year of receipt and is totally exempt.

(2) RECOGNIZED PROVIDENT FUND:

A recognized provident fund is one, which is maintained by a private organization and fulfills the prescribed conditions and on an application made, the Commissioner Inland Revenue grants recognition to such funds.

Tax Treatment

The tax treatment of contribution of the fund and payment there from to the employee is as under:

Employee's Contribution:

Employee's own contributions to the fund are already included in his annual salary and chargeable to tax in the hands of employee.

Employer's Contribution:

Employer's contribution upto 10% of salary of employee is not included in total income of employee. If the employer's contribution exceeds 10% of the salary then the excess amount is to be included in the salary income of the employee.

Interest on Accumulated Balance:

Interest on Accumulated Balance both on employee's contribution and employer's contribution is not included if the rate of interest is up to 16% and the amount of interest is less than 1/3rd of salary. Otherwise the excess amount will be included in total income.

Payment of Accumulated Balance:

The accumulated balance due and becoming payable to an employee participating in a recognized provident fund shall not be included in the computation of total income.

(3) UNRECOGNIZED PROVIDENT FUND:

An unrecognized provident fund is one which is maintained by the private organizations which has not been granted recognition by the income tax authorities because;

(a) The conditions prescribed in the law regarding the provident fund are not fulfilled.

(b) No application for recognition has been made by the organization

(c) The application is turned down on some technical grounds by the income tax authorities.

Tax Treatment

The tax treatment of contribution of the fund and payment therefrom are as under:

Employee's Contribution:

Employee's own contributions to the fund are already included in his annual salary and chargeable in the hands of employee.

Employer's Contribution:

Employer's contributions are neither to be included in the annual salary of the employee nor are taxable in the hands of employee.

Interest on Accumulated Balance:

Interests on Accumulated Balance both on employee's own contribution and employer's contributions are not included in total income of the employee.

Payment of Accumulated Balance:

Accumulated balance representing employee's contribution and interest thereon is not included in the total income in the year of receipt.

Accumulated balance of employer's contribution and interest thereon are treated as profit in lieu of salary in the year of receipt and included in total income.

Items	Government Provident Fund	Recognized Provident Fund	Unrecognized Provident Fund
Employee's contribution	Included in total Income	Included in total Income	Included in total Income
Employer's contribution	Not included in total income	Not included if the amount is upto 10% of salary, excess amount shall be included	Not included

Interest credited	Not included	Not included if the rate of interest is upto 16% & amount is less than 1/3rd of salary excess amount will be included	Not included
Receipt of accumulated balance	Not included	Not included	Included to the extent of employer's contribution & interest thereon

Note: *Here salary means basic salary + dearness allowance.*

QUESTION NO. 4

SET OFF THE LOSSES

If a taxpayer has more than one sources of income, it is not necessary that all the sources or heads of income should provide him gain or benefit during the tax year. So, the income tax law allows the taxpayer to adjust the loss of one head of income against the income of same head or other head in the same year. The adjustment of loss of one head against the income of same head or other head is known as "Set off the Losses".

EXCEPTIONS:

To the general principle of "Set of the Losses" there are few exceptions which are as under:

(1) Set Off the Losses of Companies Operating Hotels:

A company registered in Pakistan or Azad Jammu & Kashmir and is operating hotels at both the places, if it sustains a loss from business at one place, the loss can be adjusted against company's income at the other place.

(2) Set Off the Speculation Loss:

Where a person sustains a loss in any tax year in respect of any speculation business, he can set off such loss only against profits of another speculation business carried on by him. It means that loss from speculation business cannot be adjusted against another head.

(3) Set Off the Capital Loss:

The treatment of capital loss is exactly in the same manner in which we treat the loss from speculation business. Where a taxpayer sustains a capital loss, it can only be set off against the capital gains received by him in the same year.

(4) Loss Sustained by an AOP:

If an association of persons sustains a loss during a tax year, it will be set off against any other income of the AOP according to the general principle mentioned in Section 56.

(5) Set Off the Loss of Certain Companies:

If loss is sustained by a company and the company subsequently is merged with another company, the loss of the company being merged can be set off against the profits of amalgamated company. Moreover, if the amalgamated company has any accumulated loss it can set off such a loss with the amalgamating company. This is not in accordance with the general principle that the person who sustains a loss, only he himself can set off the loss.

(6) Group Taxation:

If two or more companies are allowed group taxation, the loss sustained by any one company will be set off automatically against the profits and gains of other company or companies. Any loss sustained by a company prior to the formation of the group will not be available to be set off in the subsequent years.

CARRY FORWARD OF LOSSES

It is quite possible that a taxpayer sustains a loss during the tax year and he does not have any other income or loss is so heavy that it cannot be adjusted fully during that year. In such cases, the loss not adjusted in the same year is to be adjusted against the income of future years. This procedure is known as 'carry forward of losses'.

FEATURES:

The main features of the carry forward of losses are as under:

(1) Loss which cannot be Carried Forward:

If a taxpayer sustains a loss under the head income from other sources and such a loss cannot be set off against any other had in the same tax year due to absence or inadequacy of other income then such loss cannot be carried forward to the next year.

(2) Carry Forward of Loss from Business:

If a business loss cannot be fully set off in the same year, it can be carried forward to the next year and adjusted only against the person's income chargeable under the head 'income from business' and not against any other head of income. But no loss can be carried forward to more than six tax years.

(3) Carry Forward of Loss of Speculation Business:

The loss from a speculation business can be set off in the same year only against the speculative gains. If such a loss cannot be fully set off due to inadequacy or absence of speculation gain, it can be carried forward to the next tax year to be adjusted only against speculative gains of next tax year. If the whole or part of loss still remains unadjusted, it can be carried forward to the following six tax years.

(4) Carry Forward of Capital Loss:

Where a taxpayer sustains a capital loss and it cannot be set off against the capital gains of the same year, the portion not so set off shall be carried forward to the following tax year to be adjusted only against capital gains of that year. It should be noted that no capital loss can be carried forward for more than six years.

(5) Carry Forward of Losses of Association of Persons:

If an association of persons sustains loss during a tax year, it can be set off against any other income of the AOP in the same tax year and the unadjusted loss, if any, can be carried forward by the AOP for six years.

(6) Carry Forward of Losses of Certain Companies:

Any loss of the amalgamating company or companies (other than loss brought forward and capital loss) shall be set off against profits and gains of other amalgamating company or companies in the year of amalgamation. If such a loss cannot be adjusted against the profits and gains of the same tax year then unadjusted loss can be carried forward to set off upto the next six tax years by amalgamated company.

QUESTION NO. 5

Up till 30th June 2007, "Board" considered as Central Board of Revenue, established under CBR Act 1924. On the commencement of FBR Act 2007, "Board" means Federal Board of Revenue. The working of FBR is regulated according to CBR Act 1924 and all other powers vested under Federal Board of Revenue Act, 2007.

Appointment:

It is a statutory body, appointed by the Federal Government. It is attached to Ministry of Finance, Government of Pakistan. The main purpose of its appointment is collection of tax in the country.

Organization:

The Federal Government appoints a full time chairman of the Federal Board of Revenue and not less than seven members (presently twelve) to perform its functions.

POWERS AND FUNCTIONS OF BOARD

(1) Appointment of Inland Revenue Authorities:

The FBR may appoint as many Inland Revenue Authorities as are necessary.

(2) Appointment of the Auditor:

The Board is empowered to appoint a firm of Chartered Accountant or Cost and Management Accountants to conduct the audit of any person.

(3) Determination of Jurisdiction:

The Board by an order may assign the functions and areas to CCIR, the CIR and the CIR (appeals) and to officers of Inland Revenue.

(4) Formulation and Implementation of Fiscal Laws:

The Board has the powers to formulate and implement the provisions of all the fiscal laws for the time being in force and to exercise all powers provided under the provision of the fiscal laws and to take any action.

(5) Approval of Leasing Companies and Modaraba:

The FBR may approve any leasing company or Modaraba, where lease rental payment made to such company is allowed as deduction against income from business to that person who makes such payment.

(6) Method of Accounting:

The Board may specify the method of accounting for certain business or any other source of income or any class of persons.

(7) Power to Make Rules:

The FBR makes the rules for carrying out efficient administration of the Ordinance by notification in the Official Gazette.

(8) Approval of Charitable Institution:

The FBR approves the charitable institutions for the purposes of Income Tax Ordinance, specially, for donation purpose.

(9) Apportionment of Deductions:

The FBR may make the rules for apportionment of any deduction (expenditure) where it relates to the derivation of incomes of more than one head.

(10) Unexplained Income or Assets:

The FBR may make rules for the valuation and taxation of unexplained income or assets discovered by any Inland Revenue Authority.

(11) Power to Demand Particular Data:

The FBR authorizes any department or agency of the Government to collect and compile any data in respect of income from industrial and commercial undertakings exempt from tax.

(12) Authority of Circulars:

The Board may issue circulars for the guidance of taxpayers and officers of the Board to achieve consistency in the administration of the Ordinance.

(13) Maintenance of Documents:

The Board may order any person for maintaining the prescribed documents, books and records etc., for the purposes of the Income Tax Ordinance, 2001.

(14) Approval of Employee Training Scheme:

The FBR may approve a Pakistani employee training scheme against which deduction is allowed to business.

(15) Supervision of Subordinate Authorities:

The FBR may supervises the functions, duties and jurisdiction of its subordinate authorities.

(16) Procedures for Furnishing Documents:

The Board determines the procedure of furnishing returns and other documents including on electronic medium i.e., e-filing, e-payment and e-notice etc.

(17) Permission for Tax Year:

The FBR may permit a person or class of persons to use special tax year instead of normal tax year and vice versa.

(18) Delegation of Powers:

The FBR may delegate all or any of its powers and functions to any Inland Revenue Authority.

(19) Registration of ITPs:

The FBR may make rules for the registration of income tax practitioners.

(20) Preparation of Forms and Notices:

The FBR prepares prescribed forms, notices, returns, statements, tables and other documents required for the purposes of Income Tax Ordinance 2001.

QUESTION NO. 6

(a) TAX INVOICE [SEC. 2(14)]

It means a document required to be used under section 23 of the Sales Tax Act.

Explanation:

Section 23 requires that every registered person while making a taxable supply is required to issue a serially numbered tax invoice containing:

(1) Name, address and registration number of the supplier.

(2) Name address and registration number of the recipient.

(3) Date of issue of invoice.

(4) Description and quality of the goods

(5) Value exclusive of tax

(6) Amount of sales tax

(7) Value inclusive of tax

Note: *No person, other than registered person, or a person paying turnover tax or a person paying retail tax, shall issue a sales tax invoice.*

(b) INPUT TAX [SEC. 2(40)]

In relation to a registered person, means:

(1) The tax levied under this act on the supply of goods received by that person;

(2) The tax levied under this act on imported goods entered and cleared under the Customs Act, by that person;

(3) The tax levied under the Sales Tax Act 1990 of the Pakistan as adopted in the state of Azad Jammu and Kashmir, the supply of goods received by that person and shall include duties of excise chargeable under the Central Excise Act, 1944 on such excisable services as are notified by the Federal Government.

Explanation:

Purchases made by the registered person for business purposes are known as inputs and tax on such purchases is called input tax. Input tax is worked out by multiplying rate of tax with the value of the purchases.

(c) SUPPLY [SEC. 2(33)]

It includes sale, lease or other disposition of goods carried out for consideration and also includes:

(a) putting to private, business or non-business use of goods acquired, produced or manufactured in the course of business;

(b) auction or disposal of goods to satisfy a debt owed by a person; and

(c) possession of taxable goods held immediately before a person ceases to be a registered person.

(d) TAX FRACTION [SEC. 2(36)]

"Tax fraction" means the amount worked out in accordance with the following formula:

$$\frac{a}{100 + a}$$

('a' is the rate of tax specified in section 3).

QUESTION NO. 7

	Rs.	Rs.
Local Taxable Supplies:	25,00,000	
Sales to registered persons	230,000	
Taxable supplies to consumers on instalment basis	120,000	
Taxable supplies to associated persons	150,000	
Taxable supplies @ 20% discount in a normal business practice	250,000	32,50,000
Sales to retailers		200,000
Sales to non-registered person		34,50,000

Zero Rated Supplies:

Supplies to DTRE registered person	300,000
Zero-rated supply	180,000
	480,000
Exempted sales	340,000

Computation of Input Tax:

		Rs.
GST paid on electricity bill		70,000
GST paid on sui gas bill		50,000
Purchases from registered person (Rs. 500,000 @ 17%)		85,000
Purchases from non-registered person	Rs. 280,000	-
Purchases from wholesaler (Rs. 175,000 @ 17%)		29,750
		234,750
Purchased raw material (used in exempt and taxable supplies) (Rs. 400,000 @ 17%)		68,000

Apportionment of Input Tax:

	Turnover	Input Tax		Input Tax (Exempted + Taxable supplies)
Local taxable	34,50,000	206,078	(N–1)	54,941 (N–3)
Exempt sales	340,000	-		5,415 (N–4)
Zero rated	480,000	28,672	(N–2)	7,644 (N–5)
	42,70,000	234,750		68,000

Mr. Abdul Jabbar (Registered Manufacturer)
CNIC No. --
NTN --
For the month of August ------------------------
Computation of Sales Tax Payable

		Rs.	Rs.
Output	**Tax:**		
	Taxable supplies (Rs. 34,50,000 @ 17%)		586,500
Less:	**Input Tax:**		
	Paid against such supplies		
	(Rs. 206,078 + 54,941)	261,019	
		(OR)	
	90% of output tax (Rs. 586,500 @ 90%) – W.E.L.	527,850	
		261,019	
	Previous month input tax c/f	30,000	291,019
			295,481
Add:	Further tax @ 3% of Rs. 200,000		6,000
			301,481
Add:	WHT from unregistered person		
	1% of (280,000 × 100/117)		2,393
	Sales tax payable with return		303,874

Refund of input tax against DTRE and zero-rated supplies:

= Rs. 28,672 + 7,644 = Rs. <u>36,316</u>

<u>WORKING:</u>

N-1 $= \dfrac{234{,}750}{39{,}30{,}000} \times 34{,}50{,}000 = \text{Rs. } 206{,}078$

N-2 $= \dfrac{234{,}750}{39{,}30{,}000} \times 480{,}000 = \text{Rs. } 28{,}672$

N-3 $= \dfrac{68{,}000}{42{,}70{,}000} \times 34{,}50{,}000 = \text{Rs. } 54{,}941$

N-4 $= \dfrac{68{,}000}{42{,}70{,}000} \times 340{,}000 = \text{Rs. } 5{,}415$

N-5 $= \dfrac{68{,}000}{42{,}70{,}000} \times 480{,}000 = \text{Rs. } 7{,}644$

Note: (i) *No input tax is allowed on lunch provided to the staff.*

(ii) *An unregistered person cannot issue tax invoice under the law, so no input tax adjustment is possible. However, withholding tax (WHT) @ 1% in case of purchases from the un-registered person shall be with held and added in tax liability.*

QUESTION NO. 8

Mr. Asif Habib
Tax Year: xxxxx
Tax Year Ended: xxxxx
Residential Status: Resident
Computation of Tax Payable

	Rs.	Rs.
Income from Salary U/S 12:		
Basic salary		300,000
Cost of living allowance		100,000
Senior post allowance		30,000
House rent allowance		150,000
Leave fare assistance		10,000
Conveyance allowance		40,000
		630,000
Income from Property U/S 15:		
Property income (Net) – Not taxable upto Rs. 200,000	120,000	-
Income from Business U/S 18:		
Business income (UK)		20,000
Capital Gain U/S 37:		
Gain on disposal of shares		50,000
Profit on sale of house	150,000	-
Total income		700,000
Less: Worker welfare fund		30,000
Taxable income		670,000

Computation of Tax

	Rs.	Rs.
Tax on Rs. 500,000		2,000
Tax on Rs. 170,000 @ 5%		8,500
		10,500
Less: Concession @ 50% of tax as senior citizen: = (21,500 × 50/100)		5,250
		5,250
Less: Concession @ 40% of tax on salary income as a teacher:		
Salary income	630,000	

Tax on salary income:		
= 2,000 + (130,000 × 5/100)	8,500	
Less: Concession @ 50% of tax as senior citizen	4,250	
	4,250	
= 4,250 × 40/100		1,700
		3,550
Less: Tax credit on foreign income:		
(i) Foreign tax paid	500	
(ii) = 3,550/670,000 × 20,000	106	
(W.E.L. between i and ii)		106
Less: <u>Average Relief:</u>		3,444
= 3,444 / 670,000 × 80,000		411
Tax payable with return		3,033

Note: ***Amount Allowed for Relief:*** *Donation to educational institution Rs. 80,000 (OR) 30% of Rs. 670,000 = Rs. 201,000 (W.E.L.), so Rs. 80,000.*