BUSINESS TAXATION [G5] – GRADUATION LEVEL

Marks

Question No. 2

(a) (i) Finance Society: 02

Finance society includes a co-operative society which accepts money on deposit or otherwise for the purposes of advancing loans or making investments in the ordinary course of business.

(ii) Imputable Income: 02

Imputable income in relation to an amount subject to final tax means the income which would have result in the same tax, had this amount not been subject to final tax.

(b)

Name of Taxpayer	:	**Mr. Israr Raza**
National Tax Number	:	**XXX**
Tax Year Ended on	:	**June 30, 2017**
Tax Year	:	**2017**
Personal Status	:	**Individual – Salaried Person**
Residential Status	:	**Resident**

Salary Income:

	Note		Rupees	Marks
Basic salary (Rs. 300,000 x 9)		2,700,000		0.5
Utilities allowance (Rs. 30,000 x 9)		270,000		0.5
House rent allowance (Rs. 135,000 x 9)		1,215,000		0.5
Conveyance facility (Rs. 2,500,000 x 5% x 9/12)	N-1	93,750		0.5
Benefit on transfer of car	N-2	500,000		0.5
Fuel reimbursement	N-3	–		
Communication allowance (Rs. 5,000 x 9)	N-4	45,000		0.5
Medical reimbursement	N-5	–		
Interest free loan from employer	N-6	180,000		0.5
Waiver of loan on resignation	N-7	600,000	5,603,750	0.5
Gratuity	N-8		2,125,000	0.5
Taxable salary income			**7,728,750**	0.5

Tax Liability:

	Note		Rupees	Marks
Tax on Income under NTR:				
Tax on Rs. 7,000,000		1,422,000		0.5
Tax on balance of Rs.728,750 [Rs. (7,728,750 – 7,000,000) x 30%]		218,625	1,640,625	0.5
Tax on terminal benefits (Rs. 3,500,000 x 18%)	N-11		630,000	0.5
Tax on property income [Rs.20,000 + 10% of Rs.100,000 i.e. (700,000 – 600,000)]	N-9 & N-10		30,000	01
Total tax liability			2,300,625	
Less: Tax deducted at source				
By employer		1,197,000		0.5
By tenant		22,000	1,219,000	0.5
Net tax payable			**1,081,625**	0.5

Marks

Notes:

Mr. Israr Raza served with Softex Limited (SL) for nine months hence salary, allowances and other perquisites shall be computed on the basis of nine months.

N-1: Conveyance Facility:

When conveyance is used partly for business and partly for private purpose, 5% of the cost of vehicle is included in salary income. As the facility is availed for nine months, 9/12 of the amount shall be included in the salary. 0.5

N-2: Benefit on Transfer of Car:

Benefit on transfer of car is computed as below:

	Rupees	Marks
Fair market value of car	1,500,000	
Less: Price paid to employer	1,000,000	
Amount to be included in salary	500,000	01

N-3: Fuel Reimbursement:

As per the company policy, Mr. Israr was allowed to reimburse fuel up to 250 litres based on actual consumption in car used for business and private purpose hence, these type of reimbursement are exempt from tax and shall not be included in the income from salary. 0.5

N-4: Communication Allowance:

This allowance is taxable and shall be included in salary income. 0.5

N-5: Medical Reimbursement:

Reimbursement of medical expenses as per terms of employment is exempt from tax. 0.5

N-6: Interest Free Loan:

The loan of Rs. 2,400,000 is kept for 9 months so the interest shall be computed for the same period. The amount to be included in salary income shall be as below:

(Rs. 2,400,000 x 10%) x 9/12 = Rs. 180,000 01

N-7: Waiver of Part of Loan:

Waiver of part of loan is treated as a benefit to employee from employer and is included in the salary income. Amount of loan waived is as follows:

(Rs. 2,400,000 x 25%) = Rs. 600,000 01

N-8: Gratuity:

	Rupees	Marks
Gratuity	2,200,000	
Less: Exempt		
(Lessor of Rs. 75,000 or 50% of amount received)	75,000	0.5
	2,125,000	0.5

N-9: Income from Property:

	Rupees	Marks
Rent for 12 months [(Rs. 80,000 – Rs. 10,000) x 12]	840,000	01
Less: Rent not received during the year	(140,000)	01
Income from property rent chargeable to tax – On actual receipt basis	700,000	0.5

		Marks
N-10:	Income from property is treated as a separate block of income.	0.5
	It is presumed that amount of Rs.10,000 per month recovered from Digital Ltd. was actually incurred by Mr. Israr on providing the services of a servant, hence, nothing is taxable as income from other sources.	0.5
	Profit paid to a bank on a loan for reconstruction of a portion of the house shall have no tax treatment. Whereas, the amount spent on construction of a new house or acquisition of a house shall be treated as 'deductible allowance' under section 64A of the Income Tax Ordinance, 2001.	0.5
N-11:	**Compensation under the Redundancy Scheme:**	
	Compensation under the redundancy scheme shall be taxable as a separate block of income at the average rate of tax (ART) for the last three years, which under this case is **18%**.	01

Question No. 3

(a) (i) Entertainment Expenditure: 02

Entertainment' means the provision of meals, refreshments and reasonable leisure facilities in accordance with the tradition of business and subject to over all norms and customs of business in Pakistan.

(ii) Condition for Admissibility of Entertainment Expenditure: 02

In order to allow as entertainment expenditure as deduction against "Income from Business", it should satisfy the following conditions:

- The expenditure is incurred wholly and exclusively for the purpose of business.
- It satisfies the conditions laid down in Rule-10 of the Income Tax Rules, 2002.

(iii) Limitations on Deduction of Entertainment Expenditure: 05

Rule 10 of the Income Tax Rules, 2002 imposes certain limitations to claim a deduction on account of entertainment expenditure incurred by a person. These expenditure in excess of the prescribed limit is not allowable for deduction. According to aforesaid rule, a deduction shall be allowed if entertainment expenditure is incurred:

- Abroad in connection with the business;
- In Pakistan on entertainment of foreign or local customers and suppliers;
- At the meetings of members, agents, directors and employees;
- At the opening of branches; and
- On entertainment of persons related directly to business.

Marks

(b) Non-Recognition of Gain or Loss on Disposal of An Asset: 09

Normally, the gain or loss on disposal of an asset is taken into account. However, under the following cases no gain or loss shall be taken to arise, if the person acquiring the asset is a resident person:

- Where disposal is between spouses under an agreement to live apart;
- Where disposal is by reason of the transmission of the asset to an executer or beneficiary on the death of a person;
- Where disposal is by reason of a gift of the asset;
- Where disposal is by a company to its shareholders on its liquidation;
- Where disposal is by an association of persons to its members on its dissolution. However, under this case the asset should be distributed in accordance with the interest of members in the capital of AOP;
- Where disposal is by reason of the compulsory acquisition of the asset under any law. In order to avail this benefit the consideration received or disposal shall be reinvested (within one year of the disposal) in an asset of similar kind.
- If the person acquiring the asset is a non-resident person, the gain or loss on disposal of assets shall be computed as per normal procedure.

Cost and Disposal Value in Non-Arms Length Transactions:

The fair market value of the asset at the time of the transaction shall be taken respectively as cost and disposal consideration to the buyer and the seller, if the asset is purchased or sold in non-arm’s length transaction.

(c) Depreciation: 02

Where, in any tax year, a person disposes of a depreciable asset, no depreciation deduction shall be allowed under section 22 of the Income Tax Ordinance, 2001 for that year and-

- If the consideration receieved exceeds the written the written down value of the asset at the time of disposal, the excess shall be chargeable to tax in that year under the head “Income from Business’; or
- If the consideration received is less than the written down value of the asset at the time of disposal, the difference shall be allowed as a deduction in computing the person’s income chargeable under the head ‘Income from Business” for that year.

Question No. 4

(a) Rules for Carry Forward of Losses:

(i) Non-Speculation Losses: 03

Any unadjusted loss from business can be carried forward for setting it off against the profits and gains under the head “Income from Business”. This loss can be carried forward up to six (6) years immediately succeeding the tax year for which the loss was first assessed.

Where more than one tax year’s losses are being carried forward, loss of the earliest tax year shall be set-off first.

Any amount of unabsorbed depreciation shall be allowed as deduction against the incomes of following tax years. And while setting-off the previous years’ losses and unabsorbed depreciation, the losses shall be adjusted first and depreciation shall be taken into account last.

Marks

(ii) Speculation Losses: 04

A taxpayer may set-off any loss arising out of a speculation business against income from his any other speculation business carried on during the same tax year. This loss cannot be set-off against any other income.

The unadjusted speculation loss for a tax year shall be carried forward for adjustment against speculation gains/ incomes of the succeeding tax years.

The unadjusted speculation loss may be carried forward for a maximum period of six (6) tax years succeeding immediately after the tax year in which loss was incurred.

The carried forward losses are adjusted in such a way so that the loss pertaining to the earliest tax year shall be set off first.

(iii) Capital Losses: 02

Where a person sustains a loss for a tax year under the head 'capital gain' (hereinafter referred to as a 'capital loss') the loss shall not be set off against the person's income, if any, chargeable under any other head of income for the year, but shall be carried forward to the next tax year and set off against the capital gain, if any, chargeable under the head 'capital gains' for that year.

If a capital loss sustained by a person for a tax year under the head 'capital gains' is not wholly set off, then the amount of the loss not set off shall be carried forward to the following tax year, and so on, but no loss shall be carried forward to more than six tax years immediately succeeding the tax year for which the loss was first computed.

Where a person has a loss carried forward under section 59 of the Income Tax Ordinance, 2001 for more than one tax year, the loss of the earliest tax year shall be set off first.

(b) Computation of Taxable Income and Tax Liability:

Taxable Income:

		Rupees	
Pakistan source income		2,800,000	0.5
Foreign source income:			
Speculation	600,000		0.5
Less: B/f speculation loss	250,000	350,000	0.5
Non-speculation business loss c/f	(1,100,000)	–	01
Capital gain	750,000		
Less: B/f capital loss	1,400,000		
Capital loss c/f	650,000	–	01
Other source		1,350,000	0.5
Taxable income		4,500,000	01

Tax Liability:		Rupees	Marks
Income tax on Rs. 4,500,000 [Rs. 719,500 + 30% of Rs. 500,000]		869,500	01
Foreign tax credit on speculation business			
(a) Tax paid in foreign country	150,000		0.5
(b) 869,500 / 4,500,000 x 250,000	48,306		0.5
Whichever is lower		(48,306)	0.5
Foreign tax credit on other sources			
(a) Tax paid in foreign country	187,500		0.5
(b) 869,500 / 4,500,000 x 1,350,000	260,850		0.5
Whichever is lower		(187,500)	0.5
Total tax liability		633,694	01

(c) Wealth Statement: 05

The Comissioner is empowered to require any taxpayer (being an individual) to finish a wealth statement within a time period specified in the notice. The statement should contain the following information:

- Total asset and liabilities of the taxpayer as on the date specified in the notice;
- Total assets and liabilities of his spouse, minor children and dependents as on the date specified in the notice;
- Any assets transferred by him to any person during the specified period;
- Detail of the total expenses incurred by the taxpayer, his spouse, minor children and dependents during the specified period; and
- The reconciliation statement of wealth.

Question No. 5

(a) Manufacture: 03

Manufacture or produce includes:

- Any process in which an article singly or in combination with other articles, materials, components, is either converted into another distinct article or product or is so changed, transformed or reshaped that it becomes capable of being put to use differently or distinctly and includes any process incidental or ancillary to the completion of manufactured product.
- Processof printing, publishing, lithography and engraving and
- Process and operations of assembling, mixing, cutting, diluting, bottling, packaging, repacking or preparation of goods in any other manner.

Marks

(b) • **Separate Registration For Each Outlet:** 04

Under the Sales Tax Act, 1990 a person can have only one registration, thus there is no possibility of obtaining separate registration for each general store.

• **Classification Of The Person:**

The Sales Tax Act, 1990 specifies that 'Retailer' means a person supplying goods to general public for the purpose of consumption.

Any person who combines the business of import, manufacturing or production with retail shall have to observe the following conditions:

- He shall notify and advertise wholesale prices and retail prices separately; and
- He shall declare the addresses of his retail out lets.

In the light of above provision Mr. Amir will be classified as retailer if he fulfils the above conditions.

(c) Return of Goods by Shaheen Limited (SL):

(i) The following procedure shall be adopted by SL if it decides to return the part of supply due to inferior quality: 03

- The buyer may return the taxable goods within one hundred and eighty (180) days of the supply. The Commissioner, at the request of the supplier, may extend this period up to further one hundred and eighty (180) days.
- The buyer shall return the goods along with a debit note.
- The supplier, on receipt of the goods supplied by him shall issue a credit note.

(ii) The debit and credit notes shall be issued in duplicate and shall contain the following information: 02

- The description of the goods;
- The quantity of the goods;
- The value of the goods, based on the invoice issued at the time of supply;
- The amount of sales tax paid; and
- The number and date of the original tax invoice.

Marks

Question No. 6

Talha Furnitures Ltd.
Sales Tax Liability
For the month of December 2016

		Rupees	Marks
Output Tax:			
On taxable supplies			
Sale made to registered person (Rs. 9,000,000 x 17%)		1,530,000	01
Sale made to unregistered person			
Sales tax (Rs. 1,500,000 x 17%)	255,000		01
Further tax (Rs. 1,500,000 x 2%)	30,000	285,000	01
Scrap sales (Rs. 300,000 x 17%)		51,000	01
Advance payment received for goods to be supplied (Rs.700,000 x 17%)		119,000	01
		1,985,000	
Less: Credit note issued for return for goods (Rs. 900,000 x 17%)		(153,000)	01
Total output tax		**1,832,000**	
Input Tax:			
On the purchase of raw materials for which payments were made:			
In cash into the business bank account of the suppliers		–	0.5
Through crossed cheque into a personal bank account of the suppliers		–	0.5
Online transfer to the business bank account of the suppliers (Rs.5,510,000 x 17/117)		800,598	01
Sales tax credit brought forward from November 2016		300,000	01
Total input tax		**1,100,598**	
Total Tax Payable with Return:			
Total Output Tax		1,832,000	
Total Input Tax		(1,100,598)	
Total sales tax payable for the month of December 2016		**731,402**	01

THE END