SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest rupee.
2. All apportionments should be made to the nearest month.
3. All workings should be shown.

TAX RATES AND ALLOWANCES

The following tax rates and information are to be used in answering the questions.

A. **Tax rates for individuals**
where salary income exceeds 50% of taxable income for the tax year 2009

Taxable income	Rate of tax
Up to Rs. 180,000*	0%
Rs. 180,001 – Rs. 250,000	0·50%
Rs. 250,001 – Rs. 350,000	0·75%
Rs. 350,001 – Rs. 400,000	1·50%
Rs. 400,001 – Rs. 450,000	2·50%
Rs. 450,001 – Rs. 550,000	3·50%
Rs. 550,001 – Rs. 650,000	4·50%
Rs. 650,001 – Rs. 750,000	6·00%
Rs. 750,001 – Rs. 900,000	7·50%
Rs. 900,001 – Rs. 1,050,000	9·00%
Rs. 1,050,001 – Rs. 1,200,000	10·00%
Rs. 1,200,001 – Rs. 1,450,000	11·00%
Rs. 1,450,001 – Rs. 1,700,000	12·50%
Rs. 1,700,001 – Rs. 1,950,000	14·00%
Rs. 1,950,001 – Rs. 2,250,000	15·00%
Rs. 2,250,001 – Rs. 2,850,000	16·00%
Rs. 2,850,001 – Rs. 3,550,000	17·50%
Rs. 3,550,001 – Rs. 4,550,000	18·50%
Rs. 4,550,001 – Rs. 8,650,000	19·00%
Rs. 8,650,001 and over	20·00%

* For a woman taxpayer, no tax is chargeable if taxable income does not exceed Rs. 240,000

B. **Tax rates for individuals**
to whom the rates given in A are not applicable for the tax year 2009

Taxable income	Rate of tax
Up to Rs. 100,000*	0%
Rs. 100,001 – Rs. 110,000	0·50%
Rs. 110,001 – Rs. 125,000	1·00%
Rs. 125,001 – Rs. 150,000	2·00%
Rs. 150,001 – Rs. 175,000	3·00%
Rs. 175,001 – Rs. 200,000	4·00%
Rs. 200,001 – Rs. 300,000	5·00%
Rs. 300,001 – Rs. 400,000	7·50%
Rs. 400,001 – Rs. 500,000	10·00%
Rs. 500,001 – Rs. 600,000	12·50%
Rs. 600,001 – Rs. 800,000	15·00%
Rs. 800,001 – Rs. 1,000,000	17·50%
Rs. 1,000,001 – Rs. 1,300,000	21·00%
Rs. 1,300,001 and over	25·00%

* For a woman taxpayer, no tax is chargeable if taxable income does not exceed Rs. 125,000.

C. **Tax rates for companies**

Tax year	Public company	Private company
2009	35%	35%

D. **Rates of deduction of tax at source**

Sale of goods	3·5% of gross payment
Commission or brokerage	10% of gross payment
Profit on debt	10% of profit paid
Prize on prize bonds	10% of gross payment

E. **Other tax rates**

On dividends received from a company	10%

F. **Capital allowances**

Depreciation		
Buildings (all types)	10%	of the tax written down value
Furniture and fittings	15%	
Plant and machinery (not otherwise specified)	15%	
Motor vehicles (all types)	15%	
Computer hardware	30%	
Initial allowance	50% of cost	

G. **Benchmark rate**

For determining the value of the perquisite on loans given to employees, the benchmark rate for the tax year 2009 is 11% per annum of the loan amount.

1 **(a)** XYZ Ltd (XYZ) is a public company incorporated under the Companies Ordinance, 1984, whose shares were traded on the Karachi Stock Exchange from 1 January 2008 until 29 June 2009, on which date the company was delisted. XYZ closes its accounts on 30 June each year. 49% of the shares in XYZ are held by the Government of the Kingdom of Saudi Arabia and 51% by the Federal Government of Pakistan. The control and management of the affairs of XYZ was situated partly in Saudi Arabia during the year ended 30 June 2009.

Required:

State, giving reasons, whether for Pakistan tax purposes for the tax year 2009 XYZ Ltd:

(i) is or is not a public company; and
(ii) is a resident or a non-resident company. (3 marks)

(b) Agrofert Limited (AL) is a public company listed on the Karachi Stock Exchange, which is engaged in the manufacture of fertiliser. The following information is provided for AL's year ended 30 June 2009.

(1) AL's accounting net profit for the year ended 30 June 2009 is Rs. 35,970,000

(2) Sales of fertiliser include Rs. 200,000,000 being sales of AL's own manufactured fertiliser. Tax at the applicable rate was deducted from the Rs. 200,000,000 and has been included as advance tax in the balance sheet as on 30 June 2009. The finance director of AL is of the view that the tax deducted is the final tax on these sales of Rs. 200,000,000.

(3) Deductions charged in the accounts include:

		Rupees
(i)	Accounting depreciation	2,780,000
(ii)	Tax collected by the Collector of Customs on the import of fertiliser for sale, in finished form	867,000
(iii)	Payment to the Collector of Customs for an erroneous declaration in a bill of entry for import	435,000
(iv)	Freight charges paid to a local contractor, in cash	385,000
(v)	Purchase of low value items of furniture charged off in the accounts in accordance with AL's consistent accounting policy	760,000
(vi)	Payment to the Workers' Participation Fund under the Companies Profit (Workers' Participation) Act, 1968	795,000
(vii)	Loss of cash embezzled by AL's cashier	125,000

(4) Income shown in the accounts includes:

		Rupees
(i)	Share of profit received from an association of persons (AOP) in which AL is a member. No tax was deducted from the payments received by the AOP for the sale of goods as the payers were not prescribed persons who were required to deduct tax. The taxable income of the AOP was Rs. 1,200,000 and the tax assessed on the AOP was Rs. 300,000	500,000
(ii)	Net income (adjusted for tax purposes) on the sale of the imported fertiliser (as in 3(ii)) No tax was deducted from the payments received for the sale of the imported fertiliser as the fertiliser was sold by AL in the same condition it was in when imported and tax was collected by the Collector of Customs at the time of the import of the fertiliser	4,300,000
(iii)	Gain on exchange on the payment of an instalment of a foreign currency loan, which had been utilised for the import of a unit of plant	73,000
(iv)	Commission received (net of tax) from the Federal Government for arranging the import of fertiliser on account of the Ministry of Agriculture	1,800,000
(v)	Profit on debt received (net of tax) on a fixed deposit account with Zee Bank (Pakistan) Ltd	270,000
(vi)	Accounting profit on the disposal of a building	7,000,000

(5) Fixed assets

(i) The tax written down values of AL's fixed assets on 1 July 2008 were:

	Rupees
Plant and machinery	10,073,000
Buildings	8,195,000
Motor cars	5,200,000
Furniture	3,450,000
Computer hardware	6,600,000

(ii) During the year ended 30 June 2009:

– a second-hand mixing plant, which had not previously been used in Pakistan, was purchased for Rs. 3,000,000; and

– a new motor car was purchased for Rs. 2,500,000

(iii) On 1 December 2008, one of the buildings was sold for Rs. 15,000,000. The cost of this building had been Rs. 9,800,000 and its tax written down value was Rs. 2,600,000.

(6) Other information

(i) During the year Rs. 500,000 was received from debtors and credited to the provision for bad debts. The Rs. 500,000 had been written off in previous years and allowed as a tax deduction.

(ii) AL directly holds 100% of the share capital of Tractors Private Ltd (TPL). TPL is an industrial undertaking and is not engaged in the business of trading. TPL furnished its complete return of income for tax year 2009, on 15 September 2009 to the Commissioner under the self-assessment scheme, declaring a tax loss of Rs. 313,220 which is made up as follows:

	Rupees
Business income for the year	76,480
Brought forward loss from the previous year	(389,700)
Assessed loss for the year	(313,220)

The loss of Rs. 313,220 is sought to be surrendered by TPL in favour of its holding company AL.

(iii) The advance tax paid by AL for the tax year 2009 is Rs. 2,700,000.

Required:

(i) Compute the total income and the taxable income of Agrofert Limited for the tax year 2009 under the appropriate heads of income, giving clear reasons/explanations for the inclusion or exclusion in the computation of taxable income of each of the items listed.

Note: the reasons/explanations for the items not listed in the computation of taxable income should be shown separately from the other reasons/explanations. (22 marks)

(ii) Calculate the tax payable by or refundable to Agrofert Limited for the tax year 2009. (5 marks)

(30 marks)

2 Mr Nadershah Bunvala (N), a citizen of Pakistan, is a reputed architect and the following information is provided by him.

(1) On 1 July 2008, N returned to Karachi from Dubai, where he had been in employment with Builders Associates Inc (BA Dubai) since 1 July 2004. N was present in Pakistan for not more than 30 days in each of the tax years 2005, 2006 and 2007. In the tax year 2008, N availed of his unutilised leave to tour the northern areas of Pakistan. His stay in Pakistan in the tax year 2008 was 183 days.

(2) On 1 July 2008, N commenced employment with Suleman Associates Lahore. N's terms of employment provided for the following:

(i) A basic salary of Rs. 400,000 per month.
(ii) A one time relocation allowance of Rs. 100,000.
(iii) A medical allowance of 10% of basic salary. N is not entitled to free medical treatment or hospitalisation or the reimbursement of such charges.
(iv) One month's notice in writing to be given on either side in case of cessation of employment or the payment of one month's basic salary in lieu of the notice period.

(3) On 15 July 2008, N was approached by BA Dubai to take up employment from 1 August 2008, as the technical director of Atlas Pakistan Limited (Atlas), a 100% subsidiary of BA Dubai, on the following terms:

(i) A basic salary of Rs. 700,000 per month.
(ii) A monthly medical allowance, paid in cash, of 10% of basic salary.
(iii) Two company maintained cars – one car for his business and private use and the other car solely for his private use.
(iv) Atlas to make an annual payment of Rs. 100,000 to an approved superannuation fund to provide for his retirement.
(v) Free medical treatment or hospitalisation or the reimbursement of such charges for himself and his wife.

(4) On 16 July 2008, N conveyed his acceptance of the offer of employment to Atlas and agreed to commence his employment with Atlas on 1 August 2008.

(5) On 31 July 2008, N resigned from Suleman Associates. N did not give the one month's notice in writing prior to his resignation as required under his terms of employment and Suleman Associates, with N's consent, did not pay N his basic salary of Rs. 400,000 for July 2008.

(6) The salary of Rs. 400,000 appropriated by Suleman Associates in lieu of the one months notice period not given by N, is sought to be claimed by N as a deduction.

(7) On 29 August 2008, BA Dubai transferred the equivalent of Rs. 400,000 in US dollars to N's foreign currency bank account in Dubai. BA Dubai informed N in writing that the Rs. 400,000 was a voluntary payment to reimburse N for the salary he had not received from Suleman Associates. BA Dubai further confirmed that the Rs. 400,000 was not a payment on behalf of Atlas nor would the amount be borne by Atlas or claimed by Atlas as a deductible charge. N is of the view that the Rs. 400,000 being a reimbursement of the loss suffered by him is not his income chargeable to tax.

(8) The basic salary of all employees of Atlas is deposited into each employee's bank account on the first working day of the following month. Any monthly allowances are paid to the employees on the last working day of each month.

(9) In addition to his other entitlements (as in (3) above) N also received a special monthly allowance of Rs. 20,000 from Atlas. The allowance which is not an entertainment or a conveyance allowance was specifically granted to meet expenses wholly and necessarily to be incurred in the performance of his duties as technical director.

(10) In order to provide the benefit of the two company maintained cars to N:

– a Toyota Saloon was taken on lease by Atlas on 1 August 2008 from an approved leasing company on a annual lease rental of Rs. 400,000 payable for five years. The cash price of the car, if purchased outright, would have been Rs. 1,680,000; and
– a Honda Accord was purchased by Atlas on 1 September 2008, for Rs. 2,400,000.

The Honda Accord is for the private use of N and the Toyota Saloon is for his business and private use.

(11) On 1 October 2008, N was granted a loan of Rs. 1,000,000 by Atlas, repayable in 10 equal monthly instalments. Profit on the loan is payable at the rate of 11% per annum.

(12) Other information furnished by N.

(i) On 21 March 2009, N received Rs. 1,000,000 as his share as a partner in the firm of NB Associates. The taxable income of the firm for the year ended 31 December 2008 (tax year 2009) was Rs. 2,000,000 and the tax paid by the firm on the Rs. 2,000,000 was Rs. 500,000.

(ii) On 30 June 2008, N had acquired 5,000 shares in LMN Ltd from the Privatisation Commission of Pakistan for Rs. 500,000 and had been allowed a tax credit thereon of Rs. 50,000 against the tax payable for the tax year 2008. LMN Ltd is a company listed on the Karachi Stock Exchange.

On 26 June 2009, N sold the 5,000 shares in LMN Ltd for Rs. 600,000 and from the proceeds invested Rs. 400,000 on 29 June 2009 in the purchase of 4,000 new shares in OPQ Ltd, a public company listed on the Lahore Stock Exchange. OPQ Ltd had offered these new shares to the public and N was an original allottee of the shares.

(iii) N has foreign interest income for the tax year 2009 of US$ 10,000 (Rs. 800,000) from US Treasury bonds. This foreign income is sought to be claimed as exempt from tax, on the contention that N was in employment outside Pakistan during the last four tax years (2005, 2006, 2007 and 2008) preceding the tax year 2009.

(iv) N received Rs. 500,000 from Mr X, a client of Atlas, in appreciation of his extraordinary efforts in meeting the due date of completion of a building project of X. As there was no agreement between N and X for the payment of the Rs. 500,000 and the payment made by X was voluntary, N contends that the Rs. 500,000 received is in the nature of a windfall and is therefore not taxable.

(v) During the year, N imported two consignments of steel bars for sale. The goods imported were declared for customs purposes as raw materials used in the construction of buildings. Due to a slump in the building trade, N incurred a loss of Rs. 1,893,000 on the sale of the steel bars, which is made up as follows:

	Rupees	Rupees
Sales		8,957,000
Cost		
Import value	10,000,000	
Advance tax collected by the Collector Customs	200,000	
Profit on a debt	650,000	(10,850,000)
Net loss		1,893,000

(vi) Rs. 360,000 (net of tax deducted) was received by N in the tax year 2009 as a prize on a prize bond.

(vii) The tax deducted at source from N's salary by Suleman Associates and Atlas for the tax year 2009 aggregated to Rs. 1,500,000.

Required:

(a) Compute the taxable income of Mr Nadershah Bunvala for the tax year 2009 under the appropriate heads of income, giving clear reasons/explanations for the inclusion or exclusion in the computation of taxable income and tax payable of each of the items listed.

Note: the reasons/explanations for the items not listed in the computation of taxable income should be shown separately from the other reasons/explanations. (20 marks)

(b) Calculate the tax payable by or refundable to Mr Nadershah Bunvala for the tax year 2009. (5 marks)

(25 marks)

3 Mrs Alia Dee (Dee) and her brother Azhar are preparing their separate returns of income for the year ended 30 June 2009 and furnish you with the following details:

(1) Prior to her retirement, Dee was employed with Fashions Private Limited, a subsidiary company of Fashions Inc San Francisco (FIS), she had opted to participate in the FIS Employee Share Scheme (Scheme). The terms of the Scheme allowed a participant the free right to transfer the shares issued under the Scheme, only after a minimum holding period of nine months.

(2) On 1 July 2008, Dee was granted the right to acquire 4,000 shares in FIS at the exercise price of US$ 10 for one share. The US$ 10 was inclusive of a consideration of US$ 1 for the grant of the right to acquire the shares. Based on the then quoted price of one share in FIS on the New York Stock Exchange (NY stock exchange), the value of the right to acquire one share in FIS on 1 July 2008 was estimated by the custodian of the Scheme to be US$ 1·25. On 1 July 2008, Dee accepted the rights offered to her and made payment of US$ 4,000 to the custodian.

(3) On 7 July 2008, Dee disposed of the rights relating to 3,000 shares in FIS for Rs. 375,000

(4) On 1 August 2008, Dee exercised her right to acquire the remaining 1,000 shares in FIS and made the balancing payment of US$ 9,000 (US$ 9 per share), having paid US$ 1,000 at the time of acceptance of the rights. The price quoted for one share in FIS on the NY stock exchange on 1 August 2008 was US$ 18.

(5) A dividend of US$ 3 per share was declared by FIS for its year ended 31 December 2008. US$ 3,000 (US$ 3 x 1,000) was transferred through regular banking channels to Dee's current account with the Gogo Bank Karachi. The Gogo Bank, after deducting Rs. 5,000 as their bank charges, credited Dee's account with Rs. 235,000 [Rs. 240,000 (US$ 3,000) less Rs. 5,000].

(6) Dee was required to pay Rs. 1,000,000 against her overdrawn current account with the Gogo Bank by 19 March 2009. As Dee did not have the funds to discharge this liability, Dee's brother Azhar paid the Gogo Bank the Rs. 1,000,000 on 19 March 2009.

(7) On 1 May 2009, when Dee had the free right to transfer the 1,000 shares in FIS, the price quoted for one share in FIS on the NY stock exchange was US$ 20.

(8) On 29 May 2009, Dee transferred the 1,000 shares in FIS to her brother Azhar as repayment of the Rs. 1,000,000 which had been paid by Azhar to the Gogo Bank on her behalf. The price quoted for one share in FIS on the NY stock exchange on 29 May 2009 was US$ 22.

(9) Azhar sold the 1,000 shares in FIS to an employee of Fashions Private Limited for Rs. 1,960,000 on 30 June 2009 on which date the price of one share in FIS quoted on the NY stock exchange was US$ 24. Azhar is a retired person and had no other taxable income in the tax year 2009.

(10) On 1 December 2008, Azhar had given a temporary loan of Rs. 100,000 in cash to Dee, which was repaid by Dee on 1 January 2009

(11) Dee, as one of the founder members of Dee's Boutique Pakistan Ltd (DBL), had in the tax year 2005, purchased 30,000 shares in DBL at Rs. 100 per share. In the year ended 30 June 2007, Dee received 20,000 bonus shares in DBL. On 1 July 2008, the 50,000 shares in DBL were held by Dee in her personal name.

The 50,000 shares in DBL were disposed of by Dee on 1 December 2008, on which date the break-up value of one share in DBL was Rs. 100. The details of the disposal are as under:

(i) 10,000 shares were gifted to her son Behram. Behram is an employee of the Government of Pakistan and was posted in London during the tax year 2009. In the tax year 2009, Behram was present in Pakistan for 120 days.

(ii) 25,000 shares were given to the Sorab Education Trust (Trust) to provide for the education expenses of Sorab, who is Dee's grandson. The control and management of the trust was situated wholly in Pakistan at all times in the tax year 2009.

(iii) 15,000 shares were transferred to her husband Gustard under an arrangement to live apart. Gustard left for the Maldives on 15 December 2008 and returned to Pakistan on 4 July 2009.

(12) Other information:

(i) On 1 December 2008, Dee transferred her residential house to her son Behram. Dee had purchased the house for Rs. 2,000,000 in April 2007 and the market value of the house on the date of its transfer was Rs. 5,000,000.

(ii) On 1 December 2008, Dee sold her personal jewellery, making a gain of Rs. 750,000. The jewellery had been purchased by Dee on 21 March 2008. In the year ended 30 June 2008, a loss of Rs. 1,000,000 on the sale by her of personal jewellery had not been allowed as a deductible charge by the commissioner. The gain of Rs. 750,000 is sought to be claimed by Dee as not chargeable to tax on the contention that the loss on the sale of jewellery was not allowed as a deductible charge in the tax year 2008.

Required:

(a) Compute the taxable income of Mrs Alia Dee for the tax year 2009 under the appropriate heads of income, giving clear reasons/explanations for the inclusion or exclusion in the computation of taxable income of each of the items listed.

Notes:

1. **The reasons/explanations for the items not listed in the computation of taxable income should be shown separately from the other reasons/explanations.**
2. **The rate of exchange is to be taken at US$ 1 = Rs. 80 at all relevant dates.** (18 marks)

(b) Compute the taxable income of Mr Azhar under the appropriate heads of income for the tax year 2009, giving clear explanations of the treatment accorded to the items in the computation of taxable income. (2 marks)

(20 marks)

5 Sunglow Pakistan Limited, a registered person under the Sales Tax Act, 1990 is engaged in the manufacture of multimedia projectors. The business transactions of Sunglow Pakistan Limited for the month of October 2009 included the following:

	Rupees
Receipts from sale of multimedia projectors to registered persons	7,375,950
Receipts from sale of multimedia projectors to unregistered persons	8,040,150
Sale of accessories and lenses for the multimedia projectors.	1,615,785
Purchases of electronic components and lenses	6,987,354
Purchase of stores, supplies and raw material used in the manufacturing of multimedia projectors (Out of the total payment of Rs. 2,125,215 an amount of Rs. 225,215 was paid in cash)	2,125,215
Payment to a media company for placing advertisements on the electronic media	1,693,257
Import of plant and machinery	2,350,000
Payments to customs agents	580,900
Supplies purchased in September 2009 returned to the vendors for not meeting the specifications and required standard	1,050,650
Multimedia projectors sold in September 2009 returned by the customers for defective workmanship in October 2009.	980,500

Additional information:

(1) All figures relating to sales of taxable goods are stated exclusive of sales tax.
(2) All payments are stated inclusive of sales tax.
(3) All payments for the purchase of goods and materials have been made by crossed cheque or crossed pay order or credit card except when otherwise indicated.
(4) In the case of the purchase returns and sales returns, the debit/credit notes have been issued in conformity with the provisions of Sales Tax Act, 1990.

Required:

Calculate the sales tax payable by or refundable to SunGlow Pakistan Limited for the month of October 2009, giving a clear explanation for the treatment accorded to the claim of input tax on the import of the plant and machinery.

(10 marks)

Answers

Marks

1 (a) (i) XYZ Ltd is a public company for Pakistan tax purposes since the Federal Government holds at least 50% of the shares in XYZ Ltd. [s.2(47)(a)]. The condition of being listed on a stock exchange in Pakistan at the end of the tax year is not relevant since XYZ Ltd meets the test of being a public company under s.2(47)(a). 1·5

(ii) A company is a resident company for a tax year if, *inter alia*, it is incorporated or formed by or under any law in force in Pakistan [s.83(a)]. As XYZ Ltd is incorporated under the Companies Ordinance, 1984, XYZ Ltd is a resident company for the tax year 2009. The test of control and management of the affairs of the company whether or not situated wholly in Pakistan is not relevant, since XYZ Ltd meets the test of being incorporated under the Companies Ordinance, 1984. 1·5

3

(b) (i)

Agrofert Limited
Accounting year ended 30 June 2009
Tax year 2009

Computation of taxable income	Rupees	Rupees	Marks
Income from business			
Accounting profit		35,970,000	
Add: Accounting depreciation (Note 1)	2,780,000		0·5
Tax collected by the Collector of Customs (Note 2)	867,000		1
Payment for erroneous declaration in bill of entry (Note 3)	435,000		1
Cost of furniture written off (Note 4)	760,000		1
Payment to Workers Participation Fund (Note 5)	795,000		0·5
Recovery against bad debts (Note 6)	500,000		1
Tax profit on sale of building (Note 7)	7,200,000		1·5
		13,337,000	
		49,307,000	
Less: Accounting profit on the disposal of building (Note 8)	7,000,000		0·5
Gain on exchange (Note 9)	73,000		1
Commission received (net of tax) (Note 10)	1,800,000		1
Profit on debt (net of tax) (Note 11)	270,000		0·5
Initial allowance (Note 12)	1,500,000		2
Depreciation (Note 13)	6,051,000		3·5
		(16,694,000)	
		32,613,000	
Income from other sources			
Profit on debt on government securities (refer Note 11)		300,000	0·5
Total income		32,913,000	
Allowance for Workers' Participation Fund (refer Note 5)		(795,000)	0·5
Taxable income		32,118,000	

The relevant notes for the explanations of the treatment of items included in the computation of taxable income and tax payable will be considered in allocating marks against each item.

In addition to the above, specific marks will be awarded for the explanations of the treatment of items not included in the computation of taxable income (1 mark for each item) as follows: 6

22

Items not included in the computation of taxable income.

(1) The tax of Rs. 7,000,000 (3·5% of Rs. 200,000,000) deducted on the gross sales of own manufactured fertilisers is not the final tax since Agrofert Limited (AL) is a public company listed on a registered stock exchange in Pakistan [second *proviso* to s.153(6)]. As the gross amount of Rs. 200,000,000 is included in the profits of the company, no adjustment is required to be made in the computation of income.

Marks

(2) Any expenditure, in aggregate, under a single head of account in excess of Rs. 50,000 other than by crossed bank cheque or cross bank draft or any other banking instrument is not deductible with certain exceptions. One of the exceptions is any expenditure on account of freight charges. The Rs. 385,000 paid to a local contractor for freight charges in cash is deductible and therefore no adjustment is required.

(3) The loss of cash of Rs. 125,000 due to embezzlement by the cashier is a loss in the course of business and is therefore deductible. No adjustment is required.

(4) The share of profit of Rs. 500,000 received from the association of persons (AOP) has correctly been included as the income of AL [s.88A(1)]. As the AOP has paid tax on its income, AL is allowed a tax credit against its tax payable [s.88A(2)].

(5) The net income of Rs. 4,300,000 on the sale of the imported fertiliser is income chargeable to tax since, AL being a manufacturer of fertiliser, the tax collected by the Collector of Customs on the imported fertiliser is not the final tax on the income arising from the import [s.148(7)(b)]. No adjustment is required, since the Rs. 4,300,000 is included in the profits of the company.

(6) The provisions of group relief (s.59B), subject to certain conditions, allow a subsidiary company to surrender its assessed loss, other than brought forward losses and capital losses, in favour of its holding company. As the assessed loss of Rs. 313,220 of Tractors Pakistan Limited (TPL) is a brought forward loss from the previous year, the Rs. 313,220 cannot be surrendered by TPL in favour of AL and consequently the Rs. 313,220 cannot be set off by AL against its taxable income for the tax year 2009.

(ii) Computation of tax payable

	Rupees	Rupees	Marks
Tax on taxable income of Rs. 32,118,000 at 35%		11,241,300	0·5
Tax credit for the tax paid by the AOP (Note A)		(125,000)	1·5
		11,116,300	
Tax collected by the Collector of Customs	867,000		0·5
Tax deducted on profit on debt	30,000		1
Tax deducted on sales of own manufactured fertiliser	7,000,000		1
Advance tax paid	2,700,000		0·5
		(10,597,000)	
Tax payable		519,300	
			5
			30

Note (A) Tax credit on the tax paid by the AOP

		Rupees
Share of profit received from the AOP	(A)	500,000
Taxable income of the AOP	(B)	1,200,000
Tax assessed on the AOP	(C)	300,000
A/B x C		
500,000/1,200,000 x 300,000		125,000

Notes referred to in the computation of taxable income.

Note (1) Accounting depreciation is not deductible. Tax depreciation and initial allowance is deductible at the rates prescribed in the Third Schedule.

Note (2) The tax of Rs. 867,000 collected by the Collector of Customs is not deductible. It is also not the final tax on the income derived from the sale of the imported fertilisers since Agrofert Limited (AL) is a manufacturer of fertiliser [s.148(7)(b)]. The Rs. 867,000 is available to AL as a tax credit.

Note (3) Rs. 435,000 paid to the Collector of Customs for the erroneous declaration in the bill of entry is a penalty for the violation of the customs law and is not deductible [s.21(g)].

Note (4) The cost of furniture purchased is capital expenditure and is not deductible. For tax purposes the Rs. 760,000 is treated as a depreciable asset (Note 13).

Note (5) Rs. 795,000 paid to the Workers' Participation Fund is not deductible in computing the total income. The Rs. 795,000 is an allowable deduction from the total income to arrive at the taxable income [s.9 read with s. 60B)].

Note (6) Rs. 500,000, received from debtors and credited to the provision for bad debts, are receipts against debts, which were written off as bad and allowed as deductions in the previous years. The Rs. 500,000 is now chargeable to tax since it represents recoupment of losses previously allowed as a deduction (s.70).

Note (7) Any accounting profit or loss on the disposal of a depreciable asset is ignored for tax purposes. The tax profit or loss on the disposal of the asset is the difference between the consideration received and the tax written down value of the asset [s.22(8)]. In the case of immovable property (other than land) where the consideration received on the disposal exceeds the cost of the property, the consideration received is treated as the cost of the property [s.22(13)(d)].

As the consideration received (Rs. 15,000,000) for the building sold is more than the cost of the building (Rs. 9,800,000), Rs. 15,000,000 is treated as the cost of the building (deemed cost) for working out the tax profit/loss on the sale of the building.

The tax profit of Rs. 7,200,000 on the disposal of the building is computed out as under:

	Rupees	Rupees
Sale consideration		15,000,000
Less: Tax written down value		
Deemed cost	15,000,000	
Depreciation allowed (actual cost Rs. 9,800,000 less tax written down value Rs. 2,600,000)	(7,200,000)	
		(7,800,000)
Tax profit		7,200,000

Note (8) The accounting profit of Rs.7,000,000 on the disposal of the building is not to be considered in the determination of taxable income as explained in Note (7).

Note (9) Where an asset has been acquired with a loan denominated in foreign currency (repayable in foreign currency) and before the loan is fully repaid, any difference in exchange arising on the repayment of the loan as expressed in rupees, is to be adjusted against the cost of the asset [s.76(5)]. The gain in exchange amounting to Rs. 73,000 is therefore not chargeable to tax. The tax written down value of plant and machinery has been reduced by Rs. 73,000 (Note 13).

Note (10) Commission received, *inter alia*, from the Federal Government, is subject to a 10% withholding tax which is the final tax on such income. Rs. 200,000 being the tax deducted at source (10% of the gross amount of Rs. 2,000,000) is the final tax and therefore the net commission amount of Rs. 1,800,000 is not chargeable to tax under any head of income (s.233 read with s.169).

Note (11) Profit on debt received on government securities is subject to a 10% withholding tax on the gross amount of the yield. The tax withheld is not the final tax on the profit on debt accruing to a company [s.151(1)(c) and (3)]. Rs. 30,000 being the tax deducted at source (10% of the gross yield of Rs. 300,000) is allowed as a tax credit and the gross yield of Rs. 300,000 is taxable under the head 'Income from other sources' [s.39(1)(c)].

Note (12) Initial allowance

	Rupees
Cost of mixing plant	3,000,000
Initial allowance at 50%	1,500,000

A second-hand plant which has not previously been used in Pakistan is entitled to a deduction for initial allowance.

Any road transport vehicle not plying for hire or furniture is not entitled to a deduction for initial allowance [s.23(1) and (5)].

Marks

Note (13) Depreciation

	Plant and machinery	Buildings	Computer hardware	Motor cars	Furniture	Total depreciation
Rate of depreciation	15%	10%	30%	15%	15%	
	Rs.	Rs.	Rs.	Rs.	Rs.	Rs.
Written down value	10,073,000	8,195,000	6,600,000	5,200,000	3,450,000	
Gain on exchange (Note 9)	(73,000)					
Disposal (Note 7)		(2,600,000)				
	10,000,000	5,595,000	6,600,000	5,200,000	3,450,000	
Depreciation	1,500,000	559,500	1,980,000	780,000	517,500	5,337,000
Additions	3,000,000			2,500,000	760,000	
Initial allowance (Note 12)	(1,500,000)			–	–	
	1,500,000			2,500,000	760,000	
Depreciation	225,000			375,000	114,000	714,000
						6,051,000

2 Mr Nadershah Bunvala

Accounting year ended 30 June 2009

Tax year 2009

(a) Computation of taxable income	Rupees	Rupees	Marks
Salary			
From Suleman Associates			
Basic salary for one month (Note 1)	400,000		1·5
Relocation allowance (Note 2)	100,000		1
Medical allowance – exempt (Note 3)	–		1
From Atlas Pakistan Limited			
Receipt from Builders Associates Inc Dubai (Note 4)	400,000		2
Basic salary for 10 months (Note 5)	7,000,000		1
Medical allowance for 11 months (Note 6)	770,000		1
Special allowance – exempt (Note 6A)	–		1
Benefit of company maintained cars (Note 7)	277,000		2
		8,947,000	
Income from business			
Share of profit from NB Associates – exempt (Note 8)		–	1
Capital gains – exempt (Note 9)		–	1
Income from other sources			
Foreign income – interest on US Treasury bonds (Note 10)	800,000		1·5
Receipt from Mr X (Note 11)	500,000		1
		1,300,000	
Taxable income		10,247,000	

The relevant notes for the explanations of the treatment of items included in the computation of taxable income and tax payable will be considered in allocating marks against each item.

In addition to the above, specific marks will be awarded for the explanations of the treatment of items not included in the computation of taxable income (1 mark for each item) as follows: 5

20

Marks

Items not included in the computation of taxable income.

(1) The annual payment of Rs. 100,000 made by Atlas Pakistan Limited (Atlas) to an approved superannuation fund is not Nadershah's (N) income chargeable to tax since the Rs. 100,000 had not been received by N in the tax year 2009. Furthermore, until such time as N retires, he has no right to any part of the pension contribution made by Atlas to the approved superannuation fund.

(2) No deduction is allowable for any expenditure incurred by an employee in deriving income chargeable under the head 'salary' [s.12(4)]. The payment of one month's salary to Suleman Associates in lieu of the notice period is therefore not deductible.

(3) A taxable benefit on a loan given by an employer would arise only if no profit is payable on the loan or the rate of profit payable is less than the benchmark rate for the relevant tax year [s.13(7)]. As the profit payable by N on the loan is at the rate of 11% per annum, which is equal to the benchmark rate for the tax year 2009, there is no impact on the computation of taxable income.

(4) The net loss Rs. 1,893,000 on the sale of the imported steel bars is not deductible under any head of income since the advance tax of Rs. 200,000 collected by the Collector of Customs on the imported steel bars is the final tax in respect of the transaction relating to the import [s.148(7) read with s.169(1)(a)].

(5) The Rs. 360,000 received by N as a prize on a prize bond is after deduction of tax at 10% of the gross amount of Rs. 400,000. The tax of Rs. 40,000 is the final tax on the income from the prize. The Rs. 400,000 is not chargeable to tax under any head of income and is therefore not included in the computation of income [s.156(3) read with s.169(1)(b)].

(b) Computation of tax payable

Rs. 1,000,000 being the share of profit received by Nadershah (N) from the association of persons (AOP) is exempt from tax [Note (8) of the notes referred to in the computation of taxable income]. However, for the purpose for determining the rate of tax applicable to the taxable income (i.e. income other than the share of income from the AOP), the Rs. 1,000,000 is included in N's taxable income as if the Rs. 1,000,000 was chargeable to tax.

		Rupees	
Tax at 20% on taxable income if the share of profit from the AOP were chargeable to tax [20% of Rs. 11,247,000 (Rs. 10,247,000 + Rs. 1,000,000)	(A)	2,249,400	
Taxable income if the share of profits from the AOP were chargeable to tax	(B)	11,247,000	
Actual taxable income	(C)	10,247,000	
Tax on taxable income			
A/B x C			
(2,249,400/11,247,000 x 10,247,000)		2,049,400	1·5
Less: Tax credit on purchase of shares (Note 12)		(60,000)	2
		1,989,400	
Add: Tax credit of tax year 2008 recouped (Note 13)		50,000	1
		2,039,400	
Less: Tax deducted at source by Suleman Associates and Atlas Pakistan Limited from salary income		(1,500,000)	0·5
Tax payable		539,400	5
			25

Notes referred to in the computation of taxable income and tax payable.

Note (1) All income included under the head 'salary' is chargeable to tax when the income is received by an employee [s.12(1)]. A person is treated as having received an amount, *inter alia*, when the amount is applied on behalf of the person, at the instructions of the person [s.69(b)]. The salary of Rs. 400,000 earned by Nadershah (N), though not paid to N, is treated as his salary income since, with the consent of N, the Rs. 400,000 was applied by Suleman Associates (SA) towards the one month's salary payable by N to SA, in lieu of the written notice of cessation of employment not given by N to SA.

Note (2) All allowances received by employees are chargeable to tax with certain exceptions. A relocation allowance is not one of the exceptions and therefore the Rs. 100,000 is chargeable to tax.

Note (3) Any medical allowance received by an employee not exceeding 10% of the basic salary of the employee is exempt from tax provided, under the terms of employment, the employee is not entitled to free medical treatment or hospitalisation or reimbursement of such expenses [clause (139)(b) of Part I of the Second Schedule]. The Rs. 40,000 medical allowance received from SA is exempt from tax as N is not entitled to free medical treatment or hospitalisation or reimbursement of such charges under the terms of employment.

Note (4) An amount is treated as received by an employee from any employment regardless of whether the amount is paid *inter alia* by the employer or an associate of the employer [s.12(5)(a)]. Since Builders Associates Inc (BA Dubai) holds 100% of the shares in Atlas Pakistan Ltd (Atlas), BA Dubai is an associate of Atlas [s.85]. The Rs. 400,000 received by N is therefore treated as received from an employment and is chargeable to tax under the head 'salary'.

Note (5) As the basic salary of each month is deposited by Atlas into the employees bank account on the first working day of the following month, the salary for June 2009 was only received by N in July 2009 and is therefore chargeable to tax in the tax year 2010. The basic salary chargeable to tax in the tax year 2009 is for 10 months (August 2008 to May 2009).

Note (6) As all allowances are payable by Atlas to their employees on the last working day of each month, the allowances received in the tax year 2009 are for 11 months (August 2008 to June 2009). The medical allowance of Rs. 770,000, though not in excess of 10% of N's basic salary, is not exempt from tax as N is entitled to the benefit of free medical treatment or hospitalisation or reimbursement of such charges under the terms of employment.

Note (6A) The special allowance of Rs. 20,000 per month granted to N to meet expenses wholly and necessarily incurred in the performance of the duties of an office is exempt from tax [clause (39) of Part I of the Second schedule].

Note (7) The Toyota Saloon taken on lease on 1 August 2008 was for N's business and private use. The taxable benefit of the perquisite is 5% of the fair market value (FMV) of the car on 1 August 2008 proportionate to the number of months the car was in the use of N. Rs. 1,680,000 the cash price of the car on 1 August 2008 is considered to be the FMV of the car on that date.

	Rupees
Annual benefit – 5% of Rs. 1,680,000	84,000
Car in use for 11 months (August 2008 to June 2009)	77,000

The Honda Accord purchased on 1 September 2008 for Rs. 2,400,000 was for the private use of N. The taxable benefit is 10% of Rs. 2,400,000 proportionate to the number of months the car was in the use of N.

	Rupees
Annual benefit – 10% of Rs. 2,400,000	240,000
Car in use for 10 months (September 2008 to June 2009)	200,000

The taxable amount for the use of the two cars is Rs. 277,000 (77,000, + 200,000).

Note (8) The partnership firm of NB Associates is assessed to tax as an association of persons (AOP) [s.80(2)(a)]. An AOP is liable to tax separately from the members of the AOP and if the AOP has paid tax on its taxable income, the share of profits received by a member out of the taxable income of the AOP is exempt from tax [s.92(1)]. As NB Associates has paid tax on its income, the Rs. 1,000,000 received by N from the firm in his capacity as a member of the AOP is exempt from tax.

Note (9) The gain of Rs. 100,000 on the sale of the 5,000 shares in LMN Ltd is exempt from tax as LMN Ltd is a listed company on the Karachi Stock Exchange [clause (110) of Part I of the Second Schedule].

Note (10) N's contention for claiming the interest of US$ 10,000 (Rs. 800,000) on US treasury bonds as exempt from tax is erroneous. The exemption would have been available if N had not been a resident in any of the four tax years (2005, 2006, 2007 and 2008) preceding the tax year 2009 when he became a resident [s.51(1)]. N became a resident in the tax year 2008 as his stay in Pakistan in that year was 183 days. The interest income of Rs. 800,000 is therefore chargeable to tax under the head 'Income from other sources' [s.39(1)(c)].

Note (11) The Rs. 500,000 received by N from Mr X is not a windfall. It is also not income from his employment with Atlas but the Rs. 500,000 is a taxable receipt by reason of his employment with Atlas. The Rs. 500,000 is taxable under the head 'Income from other sources' since the income is not included in any other head of income [s.39(1)].

Note (12) A person (other than a company) is entitled to a tax credit for a tax year on the cost of acquiring in the year, new shares offered to the public by a public company listed on a stock exchange in Pakistan, provided the person is the original allottee of the shares [s.62(1)]. N is eligible for a tax credit on Rs. 400,000 being the cost of acquiring new shares in OPQ Ltd on 29 June 2009, since he is the original allottee of new shares offered to the public by OPQ Ltd, a public company listed on the Lahore Stock Exchange.

			Marks

The amount on which the tax credit is to be calculated is the lowest of (a) the cost of acquiring the shares, (b) 10% of the person's taxable income or (c) Rs. 300,000. Since both the cost of acquiring the shares (Rs. 400,000) and 10% of N's taxable income (Rs. 1,024,700) are more than Rs. 300,000, the tax credit is calculated on Rs. 300,000 [s.62(2)].

		Rupees
The tax credit allowable is calculated as under:		
Tax assessed before allowance of tax credit	(A)	2,049,400
Taxable income for the year	(B)	10,247,000
Amount of investment on which tax credit is to be calculated	(C)	300,000
A/B x C		
2,049,400/10,247,000 x 300,000		60,000

Note (13) On 30 June 2008 (tax year 2008) N had purchased 5,000 shares in LMN Ltd from the Privatisation Commission of Pakistan and was allowed a tax credit of Rs. 50,000 against the tax payable for the tax year 2008. The 5,000 shares were sold on 26 June 2009 (tax year 2009). As the shares were disposed of within 12 months of the date of its acquisition, the tax credit allowed in the tax year 2008 is recouped and the amount of tax payable for the tax year 2009 is increased by Rs. 50,000 being the amount of tax credit allowed in the tax year 2008 [s.62(3)].

3 (a)

Mrs Alia Dee
Accounting year ended 30 June 2009
Tax year 2009

Computation of taxable income	Rupees	Rupees	Marks
Salary			
Employee share scheme			
Gain on the disposal of the rights to acquire 3,000 shares (Note 1)	135,000		1·5
Benefit on the acquisition of 1,000 shares (Note 2)	800,000		2·5
		935,000	
Capital gains			
Gain on the disposal of 1,000 shares (employee share scheme shares) (Note 3)	160,000		3
Gain on the disposal of 15,000 shares in Dee's Boutique Private Ltd (Note 4)	450,000		2·5
Gain on sale of jewellery (Note 5)	750,000		1·5
Income from other sources		1,360,000	
Loan received in cash (Note 6)		100,000	1
Taxable income		2,395,000	

The relevant notes for the explanations of the treatment of items included in the computation of taxable income will be considered in allocating marks against each item.

In addition to the above, specific marks will be awarded for the explanations of the treatment of items not included in the computation of taxable income (1 mark for each item) as follows: 6

18

Items not included in the computation of taxable income.

(1) The value of a right or option to acquire shares in an employee share scheme granted to an employee is not chargeable to tax [s.14(1)]. Therefore the value of US$ 1·25 assigned to the right to acquire one share in Fashions Inc San Francisco (FIS) by the custodian of the FIS Employee Share Scheme (Scheme) is not treated as the income of Mrs Alia Dee (Dee) in the computation of income.

(2) In an employee share scheme (ESS), where there is any restriction on the transfer of the shares acquired under the ESS, the benefit accruing to the employee on the purchase of such shares is chargeable to tax at the time the employee has the free right to transfer the shares or when the employee disposes of the shares (if so allowed by the custodian of the ESS), whichever is the earlier [s.14(3)(a)].

Dee acquired 1,000 shares in FIS under the Scheme at the exercise price of US$ 10 per share when the market value of one share was US$ 18. As Dee will have the free right to transfer the 1,000 shares in FIS only after a holding period of nine months, the difference of US$ 8 per share equivalent to Rs. 640,000 [US$ 8 x 1,000 = US$ 8,000 (Rs. 640,000)], though a benefit of employment, is not included in the computation of taxable income.

(3) A tax of 10% is imposed on every person who receives a dividend from a company irrespective of the tax status of the company. The tax of 10%, which is imposed on the gross amount of the dividend is the final tax, *inter alia*, of an individual and the gross amount of the dividend is not chargeable to tax under any head of income. Furthermore, no deduction is allowable for any expenditure incurred in earning such income (s.5 read with s.8).

As no tax was deducted from the payment of the dividend, Dee is required to pay tax of Rs. 24,000 [10% of Rs. 240,000 (US$ 3,000)]. The Rs. 24,000 is the final tax on the dividend income of Rs. 240,000. The Rs. 240,000 is not chargeable to tax under any head of income and is therefore not included in the computation of taxable income. Furthermore the Rs. 5,000 charged by the Gogo Bank as their charges is not allowable as a deduction.

(4) Under the non-recognition rules, no gain or loss is taken to have arisen on the disposal of an asset, *inter alia*, by reason of a gift of the asset provided the person acquiring the asset is not a non-resident person at the time of the acquisition [s.79(1)(c) and (2)].

As Behram is an employee of the Federal Government posted abroad in the tax year 2009, he was a resident person [s.82(c)] when the 10,000 shares in Dee's Boutique Pakistan Limited (DBL) were transferred to him. Since the 10,000 shares in DBL were gifted to Behram by Dee and Behram was not a non-resident individual when he acquired the shares, no gain or loss is taken to have arisen on the disposal of the 10,000 shares. Therefore, this transaction is not included in the computation of income.

(5) The Sorab Education Trust (Trust) is treated as a company for tax purposes [s.80(2)(b)(v)] and is a resident person in the tax year 2009 since the control and management of the Trust was situated wholly in Pakistan in the tax year 2009 [s.83(b)]. No gain or loss is taken to have arisen on the transfer of the 25,000 shares in DBL to the Trust, since the Trust was not a non-resident Trust when it acquired the shares. Therefore this transaction is not included in the computation of income.

(6) A capital gain can only arise on the sale of a capital asset. Any immoveable property is excluded from the definition of a capital asset [s.37(5)(c)]. Therefore the gain of Rs. 3,000,000 (FMV Rs. 5,000,000 less cost Rs. 2,000,000) on the transfer of the residential house is not chargeable to tax.

Notes referred to in the computation of taxable income.

Note (1) Any gain on the disposal of a right to acquire shares under an employee share scheme is chargeable to tax on the employee under the head 'salary' [s.14(5)]. The gain of Rs. 135,000 on the disposal of the right to acquire 3,000 shares in Fashions Inc San Francisco (FIS) is therefore chargeable to tax as the salary income of Alia Dee (Dee). The Rs. 135,000 is made up as under:

	Rupees
Consideration received on the disposal of the rights	375,000
Cost of the rights – US$ 1 x 3,000 = US$ 3,000 (US$ 1 = Rs. 80)	(240,000)
	135,000

Note (2) Where shares issued under an employee share scheme are subject to a restriction on the transfer of the shares, the amount chargeable to tax to the employee under the head 'salary' is the fair market value (FMV) of the shares at the earlier of the time the employee has the free right to transfer the shares or disposes of the shares, as reduced by the amount paid to acquire the shares including any amount paid for the grant of a right to acquire the shares [s.14(3)(a) and (b)].

On 1 August 2008, Dee had exercised the right to purchase 1,000 shares in FIS under the Scheme for US$ 10 per share. The 1,000 shares issued to Dee were subject to a restriction on their transfer as the shares could only be transferred after a minimum holding period of nine months. On 1 May 2009 (i.e. nine months after 1 August 2008) Dee had the free right to transfer the shares. The FMV of one share in FIS on 1 May 2009 was US$ 20 being the price quoted on the New York Stock Exchange (NY stock exchange) on that date. The benefit of Rs. 800,000 on the acquisition of the 1,000 shares in FIS under the Scheme is made up as under:

Marks

	Rupees	Rupees
FMV of 1,000 shares in FIS (US$ 20 x 1,000 = US$ 20,000)		1,600,000
Consideration paid at the time of:		
– accepting the right to acquire the 1,000 shares (US$ 1 x 1000 = US$ 1,000)	80,000	
– exercising the right to acquire 1,000 shares (US$ 9 x 1000 = US$ 9,000)	720,000	
		800,000
Benefit on the acquisition of the 1,000 shares		800,000

Note (3) Gain on the disposal of 1,000 shares in FIS acquired under the Scheme.

	Rupees
Consideration on the disposal of 1,000 shares (Note 3A)	1,760,000
Cost of 1,000 shares to Dee (Note 3B)	1,600,000
Gain on disposal	160,000

As the shares were held by Dee for not more than one year, the entire gain of Rs. 160,000 is chargeable to tax under the head 'Capital gains'.

Note (3A) The transfer of 1,000 shares in FIS by Dee to her brother Azhar on 29 May 2009 as a repayment of the Rs. 1,000,000 paid by Azhar on her behalf to the Gogo Bank, is treated as a disposal of the 1,000 shares for a consideration of Rs. 1,000,000. On 29 May 2009, the price of one share in FIS quoted on the NY stock exchange was US$ 22. The fair market value (FMV) of the 1,000 shares on the date of its transfer to Azhar is therefore Rs. 1,760,000 [US$ 22 x 1,000 = US$ 22,000 (Rs. 1,760,000)].

Due to the close relationship of Dee and Azhar coupled with the fact that the 1,000 shares in FIS having a FMV of Rs. 1,760,000 were transferred to Azhar for Rs. 1,000,000, the transaction for the transfer of the 1,000 shares is a non-arm's length transaction. When an asset is disposed of in a non-arm's length transaction, the person disposing of the asset shall be treated as having received consideration equal to the FMV of the asset at the time of its disposal [s.78(a)]. Therefore, Dee is treated as having received a consideration of Rs. 1,760,000 on the disposal of the 1,000 shares.

Note (3B) The cost of the shares acquired under an employee share scheme is the sum of (i) the consideration, if any, paid by the employee for the right or option to acquire the shares, (ii) the consideration, if any, paid by the employee for the shares, and (iii) the amount chargeable to tax as the salary income of the employee on the acquisition of the shares [s.14(4)].

		Rupees
(i)	US$ 1 paid on accepting the right to acquire 1,000 shares US$ 1 x 1,000 = US$ 1,000	80,000
(ii)	US$ 9 paid on the acquisition of 1,000 shares US$ 9 x 1,000 = US$ 9,000	720,000
(iii)	Amount charged to tax as salary income on the acquisition of the shares (Note 2)	800,000
	Cost of 1,000 shares	1,600,000

Note (4) The non-recognition rules [s.79] referred to in items (4) and (5) of the 'Items not included in the computation of taxable income' is not applicable to the transfer of 15,000 shares in Dee's Boutique Pakistan Ltd (DBL) to her husband Gustard under an arrangement to live apart, since Gustard was a non-resident person at the time of the acquisition of the 15,000 shares. Gustard was a non-resident person since he was neither present in Pakistan for a period of 183 days or more nor was he an employee of the Federal or Provincial Government posted abroad in the tax year 2009 [s.82].

The transfer of the 15,000 shares in DBL is a disposal of the shares and has resulted in a gain of Rs. 450,000 which is made up as under:

Marks

	Rupees
Consideration received	
Rs. 100 being the break-up value of one share in DBL is taken as the FMV of one share in DBL (15,000 x Rs. 100)	1,500,000
Cost (Note 4A)	(900,000)
Gain on disposal	600,000
As the 15,000 shares were held by Dee for more than one year, 75% of the gain is chargeable to tax (75% of Rs. 600,000)	450,000

		Rupees
Note (4A)	Cost of 15,000 shares in DBL	
	– 30,000 shares purchased for Rs. 100 per share (30,000 x 100)	3,000,000
	– 20,000 bonus shares received	–
	– Cost of 50,000 shares	3,000,000
	– Cost of per share	60
	Cost of 15,000 shares	900,000

Note (5) Moveable assets (with certain exceptions) held for personal use are excluded from the definition of a capital asset. The exceptions include jewellery. Any jewellery even if held for personal use is a capital asset and any gain on its disposal is chargeable to tax as capital gains [s.37(5)(d)]. However, a loss on the disposal of jewellery is not deductible [s.38(5)(b)] and therefore the loss of Rs. 1,000,000 on the sale of the jewellery in the tax year 2008 was not allowed as a deductible charge. The entire gain of Rs. 750,000 on the disposal of the jewellery in the tax year 2009 is chargeable to tax since the jewellery had not been held by Dee for more than one year.

Note (6) Any loan received in cash from a person other than a banking company or a financial institution, is treated as the income of the recipient chargeable to tax as 'Income from other sources' [s.39(3)]. The Rs. 100,000 received in cash by Dee is therefore Dee's income chargeable to tax under the head 'Income from other sources'.

(b)

Mr Azhar
Accounting year ended 30 June 2009
Tax year 2009

Computation of taxable income	**Rupees**
Capital gains	
Gain on the disposal of 1,000 shares in Fashions Inc San Francisco (Note 1)	200,000
Taxable income	200,000

Note (1) The gain of Rs. 200,000 on the sale of the 1,000 shares in FIS is made up as under:

	Rupees
Consideration received for the 1,000 shares in FIS	1,960,000
Cost (Note 1A)	1,760,000
	200,000

As the shares had not been held for more than a year the entire gain of Rs. 200,000 is chargeable to tax. 2

Note (1A) As explained in note (3A) of the 'Notes referred to in the computation of taxable income' of Alia Dee (Dee), the transaction of the transfer of 1,000 shares in Fashions Inc San Francisco (FIS) by Dee to her brother Azhar is a non-arm's length transaction for the reason that Dee and Azhar are closely related and the 1,000 shares having a fair market value (FMV) of Rs. 1,760,000 were transferred to Azhar for a consideration of Rs. 1,000,000. Dee, as the person disposing of the 1,000 shares in FIS, was treated as having received a consideration of Rs. 1,760,000 being the FMV of the 1,000 shares in FIM at the time of the disposal [s.78(a)].

Azhar, the person acquiring the 1,000 shares in the non-arm's length transaction, is treated as having a cost equal to the amount which has been treated as the consideration received by Dee, the person disposing of the 1,000 shares in FIS [s.78(b)]. Therefore the cost of the 1,000 shares in FIS, to Azhar, is Rs. 1,760,000.

20

Marks

5 SunGlow Pakistan Limited

Output tax		**Rupees**	
On sale of multimedia projectors to registered persons at 16%		1,180,152	0·5
On sale of multimedia projectors to unregistered persons at 16%		1,286,424	0·5
On sale of accessories and lenses for the multimedia projectors at 16%		258,526	0·5
		2,725,102	
Less: Credit note issued and debit note received for the return of multimedia projectors at 16%		(156,880)	1
	A	2,568,222	

Input tax	**Rupees**	**Rupees**	
On purchase of electronic components and lenses (Rs. 6,987,354 x 16/116)		963,773	1
On purchase of stores, supplies and raw material for use in the manufacture of multimedia projectors	2,125,215		
Less: Amount paid in cash	225,215		
	1,900,000		
(Rs. 1,900,000 x 16/116)		262,069	2
On payment to media company for placing advertisements on the electronic media (Rs. 1,693,257 x 16/116)		233,553	0·5
On payments to customs agents (Rs. 580,900 x 16/116)		80,124	0·5
		1,539,519	
On import of plant and machinery (Note 1)		27,011	2
		1,566,530	
Debit note issued and credit note received for purchases returned (Rs. 1,050,650 x 16/116)		(144,917)	1
	B	1,421,613	
Sales tax payable for the month of October 2009 (A – B) = (2,568,222 – 1,421,613)		1,146,609	0.5
			10

Note:

1. The input tax adjusted is Rs. 27,011 which is made up as under:

	Rupees
Input tax on the import of plant and machinery (Rs. 2,350,000 x 16/116)	324,138
Adjustable against the output tax in 12 equal monthly instalments (s.8b) (324,138/12)	27,011