Certified Finance and Accounting Professional Stage Examination

The Institute of
Chartered Accountants
of Pakistan

9 December 2023
3 hours and 30 minutes – 100 marks

Tax Planning and Practices

CRN:						

Name: ______________________________

INSTRUCTIONS

Please carefully read the following instructions:

1. You are required to access your answer working area by using your Student ID and Password as mentioned on your Admit Card.
2. The overall duration of the exam is 3 hours and 30 minutes, which includes the 15-minute reading time and an extra 15 minutes of time that has been allocated due to the introduction of computer-based examinations, for the Winter 2023 examinations only.
3. All questions are compulsory.
4. Questions can be attempted in any sequence.
5. There is no specific time allocated for individual questions.
6. An auto-save function runs every minute. Further, your answers are saved automatically when you navigate between questions or click on the > **(NEXT)** or < **(BACK)** symbols.
7. Each question provides an answer area with a Rich Text Format (RTF) editor for writing your answers. Additionally, below the RTF editor, a spreadsheet is provided to facilitate examinees in doing rough calculations or other workings. **However, please note that any work performed in the spreadsheet will not be considered for marking. To ensure your work is considered, you must copy and paste it from the spreadsheet to the RTF editor.**
8. Work done in the spreadsheet of one question can also be copied into the RTF editor of the same or another question.
9. You may use Microsoft Office applications such as MS Word or MS Excel for rough working. However, please remember that any work performed in these applications cannot be copied into the examination software, and vice versa. Furthermore, any such work will not be uploaded with your exam for marking.
10. You may use pen and paper for rough work, but please note that pen and paper work should only be done on the last two pages of the question paper that are specifically allocated for this purpose. Remember that any rough work done on these pages will not be uploaded with your exam for marking.
11. In accordance with the open book policy of this paper, you are allowed to use only digital copies of the permissible books. Keeping a hard copy of any book or notes is not permissible and will be considered a violation of the use of unfair means policy, leading to disciplinary action.
12. An external calculator can be used, provided it is included in the list of permissible calculators issued by ICAP.
13. During the exam, access to any website other than Assessment Master and the digital copies of permissible books is strictly prohibited. Engaging in such activities will be considered a violation of the use of unfair means policy, leading to disciplinary action.

Q.1 Haq Halal Limited (HHL), an unlisted public company, is engaged in the manufacturing of various information technology (IT) products and provision of IT services. It is registered with and duly certified by the Pakistan Software Export Board.

The following information has been extracted from HHL's records for the year ended 30 September 2023:

	Rs. in million
Sales (net of sales tax)	260.0
Cost of sales	(182.0)
Gross profit	**78.0**
Administrative and selling expenses	(44.6)
Financial charges	(10.0)
Other income	5.0
Profit before taxation	**28.4**

Additional information:

(i) Sales are comprised of:

- a sum of Rs. 12.6 million (net of discount) received for the supply of IT products to charitable schools, run by an approved non-profit organization in the province of Balochistan. A special discount of 30% was granted to the schools on their purchases.
- an amount equivalent to Rs. 15 million invoiced for the provision of IT-enabled services to Kemal Associates located in Turkey. The entire amount was realized during the year after the deduction of applicable withholding tax.
- domestic sales of various IT products amounting to Rs. 232.4 million.

(ii) Cost of sales include depreciation of Rs. 11 million.

(iii) Other income is comprised of:

- a prize worth Rs. 1.2 million (net of withholding tax of Rs. 0.3 million) provided by one of HHL's suppliers as part of a sales promotion campaign.
- gain of Rs. 1.0 million from the sale of shares in Micro Limited (ML) and Chip Limited (CL).

  HHL had 150,000 shares in a listed company, Micro Limited. These shares were acquired on 30 April 2021 for Rs. 52 per share. On 1 June 2023, consequent to SECP's order, Micro Limited de-merged and split into two listed companies i.e. Micro Limited (ML) and Chip Limited (CL). Consequently, HHL's holding in ML was reduced to 90,000 shares in its CDC account and 110,000 new shares in CL were recognized in its account. On the date of the de-merger, the market values of each share of ML and CL were Rs. 25 and Rs. 55 respectively.

  On 30 September 2023, HHL sold 30,000 shares in ML for Rs. 35 each and 70,000 shares in CL for Rs. 65 each.

- the sale proceeds of Rs. 2.8 million generated from the sale of 85,000 shares in a listed company, Karobari Limited at a negotiated price. HHL had purchased these shares in June 2020 for Rs. 25 per share. On 15 August 2023, HHL sold these shares to an institutional investor through the over-the-counter (OTC) market. The market value of these shares at the time of sale was Rs. 35 each.

Other information: (not included above)

(i) On 30 September 2023, HHL received a share of Rs. 6.0 million in income from the AOP. The AOP's total gross turnover amounted to Rs. 125 million, and HHL holds a 32% interest in the AOP.

(ii) Tax depreciation amounts to Rs. 30.4 million.

(iii) HHL has not submitted the withholding tax statement for the tax year 2024 with the FBR.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, compute under the correct head of income, the total income, taxable income and tax liability of HHL for the tax year 2024. **(22)**

Notes:
- ***Ignore WWF, WPPF and default surcharge, if any.***
- ***Show all relevant exemptions, exclusions and disallowances.***

Q.2 Augment (Private) Limited (APL), a manufacturing company, has investments in the following companies:

Name of investee	Investee's business	% of shareholdings	Date of acquisition
Boundary (Private) Limited (BPL)	Manufacturing company	90%	1 October 2021
Compound (Private) Limited (CPL)	Trading company	80%	1 October 2022

The following information has been extracted from the tax records of APL and its investee companies for the year ended 30 September 2023:

	APL	BPL	CPL
Income from business	-------- **Rs. in million** --------		
Taxable business income	240	(150)	50
Less: Brought forward losses related to tax year 2022	-	(280)	-
	240	**(430)**	**50**
Capital gains			
Gain/(loss) on sale of shares of a listed company	120	(200)	-
Income from other sources			
Profit on debt	60	80	-

Required:
In accordance with the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, explain the amount of abovementioned losses of BPL that can be claimed by any of the group companies in the tax year 2024. **(06)**

Notes:
- ***Show all necessary computations.***
- ***Discussion on associated conditions to be met in future is not required.***

Q.3 Consider each of the following independent situations in the light of Income Tax Ordinance, 2001 and Rules made thereunder.

(a) Apna Ghar Limited (AGL), a non-banking finance company, is engaged in the housing finance. AGL has been operating in major cities across Pakistan since 1 July 2020. Below are the details of consumer loans and related income since its incorporation, extracted from its financial statements:

	Tax year		
	2021	**2022**	**2023**
	------- **Rs. in million** ------		
Interest income from consumer loans	42.00	144.00	220.00
Receivables - consumer loans	280.00	540.00	680.00
Bad debts expense in respect of doubtful receivables - consumer loans	1.05	4.70	6.10

Required:
Calculate the allowable bad debt expense for the tax years 2021, 2022, and 2023, along with the carried forward amounts, if any, in these tax years. **(04)**

(b) Murad has been a shareholder in Joyland (Pvt) Limited (JPL) since its incorporation. JPL specializes in producing plastic toys. On 1 November 2023, due to severe financial distress, JPL was forced into liquidation, with an unpaid tax liability of Rs. 15 million for the tax year 2023. Subsequently, the Commissioner of Income Tax issued a notice to Murad, requiring him to settle JPL's outstanding tax dues for the tax year 2023.

Required:
Evaluate the validity of the Income Tax Commissioner's notice to Murad and examine Murad's position in this scenario. **(04)**

Q.4 Glow Cosmetic (Pakistan) Limited (GCPL), a listed company, is engaged in the manufacturing and sale of cosmetic products. It operates as a subsidiary of a UK based company.

GCPL's tax manager is in the process of finalizing the tax return for the tax year 2024 and has presented the following information along with supporting notes for the year ended 30 September 2023 for management's approval:

Income from business:	**Note**	**Rs. in million**
Profit before taxation	(i)	59.00
Add/(Less): Inadmissible expenses/(income)		
Dividend income (being FTR income)	(ii)	(10.00)
Lease rental income of new unit	(iii)	(18.00)
Brokerage fees	(iii)	0.82
Loss on discontinuance of business segment	(iv)	15.00
Accounting depreciation	(v)	34.90
Tax depreciation	(v)	(40.76)
		40.96
Income from property:		
Gross lease rentals	(iii)	18.00
Less: 1/5th for repair		(3.60)
Brokerage fees (restricted to 4% of the gross rent)		(0.72)
		13.68
Income from other sources:		
Expenses reimbursed by the parent company	(vi)	3.00
Taxable income for the year		**57.64**

Notes to the computation:

(i) Profit before taxation includes insurance compensation of Rs. 8.4 million received from Loyal Insurance Limited. The compensation was received against the loss of one of GCPL's warehouses in Sukkur. The warehouse was completely gutted down due to a fire ignited by a short circuit. This warehouse was constructed in July 2021 at a cost of Rs. 12 million. At the time of the fire, the warehouse had fair market value of Rs. 11.5 million whereas its accounting and tax written down values were Rs. 9.6 million and Rs. 8.1 million, respectively.

(ii) During the year, GCPL received dividend income equivalent to Rs. 8.5 million from a UAE based entity, after the deduction of tax at source @ 15% in the UAE.

On 1 October 2022, GCPL made an investment of Rs. 63 million by acquiring a 42% shareholding in recently incorporated unlisted trading company, Shine LLC (SL), based in UAE.

During the year ended 30 September 2023, SL earned solely income from property in the UAE, amounting to AED 500,000, on which SL is not liable to pay income tax in UAE.

GCPL carries this investment in SL at cost in its books of accounts.

Rate of PKR / AED on 30 September 2023 was Rs. 80.

(iii) In November 2022, GCPL completed the construction of a factory building, at a cost of Rs. 98 million to enhance the manufacturing of skin care products. Further, GCPL purchased and installed used plant and machinery within the new facility, for Rs. 38 million. The machinery was in the same condition as when it was originally imported from Germany by a commercial importer. No withholding tax was deducted by GCPL when making payment to the importer.

Due to some unavoidable reasons, the new factory did not commence manufacturing as planned. On 1 January 2023, GCPL leased the factory to Jalal Associates at a monthly rent of Rs. 2 million and paid brokerage fees of Rs. 0.820 million to a real estate broker for letting out the new unit on rent.

(iv) During the year, GCPL sustained a loss of Rs. 15 million on its business segment relating to anti-aging products, which was discontinued in July 2022.

(v) Both accounting and tax depreciation are inclusive of depreciation charged on the newly constructed factory building and used plant and machinery installed therein.

(vi) It represents 70% of the total expenditure incurred by GCPL in the tax year 2023 in relation to the export of skin care products to its parent company.

Required:
Under the provisions of the Income Tax Ordinance, 2001 and Rules made thereunder, comment on each element of the above computation of the taxable income, including adjustments, along with the accompanying notes prepared by the tax manager for the tax year 2024. Give suggestion(s), wherever necessary. **(24)**

Notes:
- ***Revised computation of taxable income is not required.***
- ***Ignore the discussion on tax liability.***
- ***Ignore WWF, WPPF, Minimum tax u/s 113 and Alternative Corporate Tax, if any.***
- ***Ignore tax treaty.***

Q.5 (a) On 1 January 2023, Ahmed issued purchase order to Care Enterprises (CE), a registered person, for purchase of CCTV cameras worth Rs. 300,000 (exclusive of sales tax) for his shop. He made an advance payment of 20% against an advance payment receipt on the same date. The remaining 80% was paid on 25 February 2023, when the cameras were delivered to Ahmed. On 5 March 2023, CE's staff installed the cameras in Ahmed's shop.

On 14 February 2023, the government announced an increase in the rate of sales tax from 17% to 18%.

Required:
Explain the amount of sales tax charged by CE to Ahmed. ***(Show all necessary computations)*** **(04)**

(b) Bari (Pvt) Limited (BPL) is a registered business involved in the import, export and supply of garments. On 1 July 2021, BPL imported 1,000 pieces of ready-made garments from Taiwan for equivalent to Rs. 2 million and paid applicable sales tax thereon. Originally intended for sale in Punjab, these garments remained unsold due to unforeseen circumstances that led to a business shutdown.

In August 2023, BPL resumed its operations. On 20 November 2023, BPL exported these garments to a customer in Morocco for equivalent to Rs. 3 million.

Required:
Under the provisions of the Sales Tax Act, 1990, discuss the sales tax implications in the above scenario. ***(Show all necessary computations)*** **(05)**

Q.6 Zang Electronics (ZE), a subsidiary of a Chinese company Ming Electronics (ME), is engaged in the business of manufacturing and supply of household electronic appliances with its principal place of business in Lahore. It is registered as an importer, manufacturer, and distributor with the Sales Tax Authorities. The following information has been extracted from ZE's records for the month of November 2023:

	Rs. in million
Purchases	
From registered suppliers	42.0
From unregistered suppliers	1.2
Imports	185.0
Supplies	
To registered suppliers	104.5
To unregistered suppliers	64.0

Additional information:

(i) Purchases from registered suppliers comprised of the following:

- Tempered glass worth Rs. 15 million from a local manufacturer, Shining Glass (SG). On 2 December 2023, SG was blacklisted by the sales tax authorities due to the issuance of fake invoices.
- Packaging material worth Rs. 24 million from a local manufacturer.
- Furniture worth Rs. 3 million for use in ZE's head office.

(ii) Purchases from unregistered persons comprised of utility and food items purchased for ZE's head office.

(iii) Imports comprised of the following:

- Imports of deep freezers, touch screens to be installed in smart fridges and ovens, and solar panels. The details are as follows:

	Deep freezers	Touch screens	Solar panels	Total
	-------- Rs. in million			--------
Costs	50.5	26.0	20.5	97.0
Value assessed by the custom authorities	51.0	25.0	21.0	97.0
Retail price	62.0	30.0	25.0	117.0

- Plastic at a cost of Rs. 88 million from Ming Trading (MT), another Chinese subsidiary of ME. MT operates as the central purchasing unit for ME and all its subsidiaries, enabling it to secure 12% discount on market value due to its large purchasing volume. MT supplies these plastic to ME's subsidiaries without adding any extra charges. Surplus plastic that exceeds the requirement of these subsidiaries is then sold at market value.

The value of imports is inclusive of custom and federal excise duties but exclusive of sales tax.

(iv) Supplies to registered persons comprised of the following:

- Microwave ovens of Rs. 90 million. The retail price of these ovens was Rs. 100 million. During the month, 5% of these ovens were returned by the customers due to mechanical faults. ZE replaced these faulty units with new ones at no additional charge, honouring their one-year warranty.
- Commercial ovens of Rs. 14.5 million, specifically purchased to fulfill an order from a restaurant owner. The retail price of these ovens was Rs. 16 million.

(v) Supplies to unregistered persons consisted of the following:

- Sales of solar panels amounting to Rs. 22.5 million (net of discount) made through an online marketplace. In celebration of 10-year anniversary, these items were offered at a discount of 10%.

- Microwave ovens returned from customers were sold to a scrap dealer for Rs. 1.5 million.
- Sales of deep freezers of Rs. 40 million to a retailer, PQR Electronics (PQRE). Retail price of these deep freezers was Rs. 45 million. PQRE used to pay its sales tax through its electricity bill till September 2023. In October 2023, PQRE relocated its outlet from DHA, Lahore to an air-conditioned mall in Gulberg, Lahore.

(vi) ZE donated smart refrigerators costing Rs. 18 million to a hospital run by a non-profit organization. The retail price of these refrigerators was Rs. 20 million.

(vii) During the month, ZE paid a royalty of Rs. 15 million to ME.

(viii) During the month, ZE purchased 20 economy plus air tickets to Saudi Arabia costing Rs. 5 million from a travel agent, registered in Lahore. These tickets were for employees eligible to perform Umrah, as per the company's policy, with the expenses borne by ZE. The travel agent charged a fee of Rs. 0.2 million for his services.

All the payments were made through cross cheque / pay order. All the above figures are **exclusive of federal excise duty (FED) and sales tax**, unless specified otherwise.

Required:

(a) In the light of the provisions of the Sales Tax Act, 1990, Federal Excise Act, 2005 and Rules made thereunder, compute the amount of sales tax payable by or refundable to ZE and the amount of input tax to be carried forward, if any, for the tax period November 2023. Also compute withholding tax, wherever applicable. ***(Show all relevant exemptions, exclusions and disallowances)*** **(22)**

(b) State the reason(s) for your treatment in part (a) above in respect of replacement of faulty microwave units, royalty payment, purchase of air tickets and travel agent fee as discussed in point nos. (iv), (vii) and (viii). **(03)**

Q.7 Razia Sultana, ACA, is a senior financial analyst in a firm of Chartered Accountants. She reports to Dawood Khan, FCA, a senior partner in the firm.

Currently, Razia Sultana is conducting a comprehensive financial analysis for Mubarak Limited (ML), a listed company. During her analysis, she uncovers evidence of potential financial and tax misconduct within ML. These irregularities could significantly impact ML's financial statements and tax filings. She decides to bring this issue to the attention of Dawood Khan. In response, Dawood Khan states that their firm's responsibility is limited to financial analysis, not investigating potential financial or tax issues. Therefore, he believes they should not concern themselves with these irregularities.

Required:

Briefly discuss how Dawood Khan may be in breach of the fundamental principles of the ICAP's Code of Ethics. Also, identify the potential threats that Razia Sultana may face in the above circumstances and how she should respond. **(06)**

(THE END)