



**Pakistan Institute
of Public Finance Accountants**

Model Solutions

Income Tax
(Application)

AGP

Summer Exam-2025

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Q.1.

Description	Monthly Pay	Yearly
Basic Salary	69,010	828,120
Conveyance allowance	5,000	60,000
Special allowance	3,200	38,400
SAS allowance	1,200	14,400
Medical allowance	1,847	22,164
Disparity Allowance	18,013	216,156
Total Yearly Salary	-	1,179,240
Accommodation	-	430,776
Total	-	1,610,016
Tax 30,000 + 15% amount exceeding 1,200,000	-	91,502
<u>Deductions by the employer</u>	-	-
Ad hoc Relief	6,971	-
Contribution to GP Fund	4,270	-
Group Insurance	1,090	-
Benevolent Fund	960	-

Q.2. Sections 9 and 10 of Income Tax Ordinance, 2001

Taxable Income.—The taxable income of a person for a tax year shall be the total income 1[under clause (a) of section 10] of the person for the year reduced (but not below zero) by the total of any deductible allowances under Part IX of this Chapter of the person for the year.

Total Income.— The total income of a person for a tax year shall be the sum of the 2[—] 3[(a) person's income under all heads of income for the year; and] 4[(b) person's income exempt from tax under any of the provisions of this Ordinance.]

Q.3. Explanation of section 22 of Income Tax Ordinance, 2001

a

For the removal of doubt, it is clarified that where any building, furniture, plant or machinery is used for the purposes of business during any tax year for which the income from such business is exempt, depreciation admissible under sub-section (1) shall be treated to have been allowed in respect of the said tax year and after expiration of the exemption period, written down value of such assets shall be determined after reducing total depreciation deductions (including any initial allowance under section 23) in accordance with clauses (a) and (b) of this sub-section.

Q.3. Pre-commencement Expenditure.

b

(1) A person shall be allowed a deduction for any pre-commencement expenditure in accordance with this section.

(2) Pre-commencement expenditure shall be amortized on a straight-line basis at the rate specified in Part III of the Third Schedule.

(3) The total deductions allowed under this section in the current tax year and all previous tax years in respect of an amount of pre-commencement expenditure shall not exceed the amount of the expenditure.

(4) No deduction shall be allowed under this section where a deduction has been allowed under another section of this Ordinance for the entire amount of the pre-commencement expenditure in the tax year in which it is incurred.

(5) In this section, “pre-commencement expenditure” means any expenditure incurred before the commencement of a business wholly and exclusively to derive income chargeable to tax, including the cost of feasibility studies, construction of prototypes, and trial production activities, but shall not include any expenditure which is incurred in acquiring land, or which is depreciated or amortised under section 22 or 24.

Q.3. Agricultural income.

c

(1) Agricultural income derived by a person shall be exempt from tax under this Ordinance.

(2) In this section, “agricultural income” means,

(a) Any rent or revenue derived by a person from land which is situated in Pakistan and is used for agricultural purposes;

(b) Any income derived by a person from land situated in Pakistan from

- (i) agriculture;
- (ii) the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by such person to render the produce raised or received by the person fit to be taken to market; or
- (iii) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by such person, in respect of which no process has been performed other than a process of the nature described in sub-clause (ii); or

(c) Any income derived by a person from

- (i) any building owned and occupied by the receiver of the rent or revenue of any land described in clause (a) or (b);
- (ii) any building occupied by the cultivator, or the receiver of rent-in-kind, of any land in respect of which, or the produce of which, any operation specified in sub-clauses (ii) or (iii) of clause (b) is carried on,

but only where the building is on, or in the immediate vicinity of the land and is a building which the receiver of the rent or revenue, or the cultivator, or the receiver of the rent-in-kind by reason of the person’s connection with the land, requires as a dwelling-house, a store-house, or other out-building.

Q.4. 59AA. Group taxation.

a

(1) Holding companies and subsidiary companies of 100% owned group may opt to be taxed as one fiscal unit. In such cases, besides consolidated group accounts as required under the 2 [Companies Act, 2017 (XIX of 2017)], computation of income and tax payable shall be made for tax purposes.

(2) The companies in the group shall give irrevocable option for taxation under this section as one fiscal unit.

(3) The group taxation shall be restricted to companies locally incorporated under the 3 [Companies Act, 2017 (XIX of 2017)].

(4) The relief under group taxation would not be available to losses prior to the formation of the group.

(5) The option of group taxation shall be available to those group companies which comply with such corporate governance requirements 4 [and group designation rules or regulations] as may be specified by the Securities and Exchange Commission of Pakistan from time to time and are designated as companies entitled to avail group taxation.

(6) Group taxation may be regulated through rules as may be made by the¹ [Board].

Q.4. 108. Transactions between associates.

b

(1) The Commissioner may, in respect of any transaction between persons who are associates, distribute, apportion or allocate income, deductions or tax credits between the persons as is necessary to reflect the income that the persons would have realised in an arm's length transaction.

(2) In making any adjustment under sub-section (1), the Commissioner may determine the source of income and the nature of any payment or loss as revenue, capital or otherwise.

(3) Every taxpayer who has entered into a transaction with its associate shall:

(a) maintain a master file and a local file containing documents and information as may be prescribed;

(b) keep 2[, maintain and furnish to the Board] prescribed country-by-country report, where applicable;

(c) keep and maintain any other information and document in respect of transaction with its associate as may be prescribed; and

(d) keep the files, documents, information and reports specified in clauses (a) to (c) for the period as may be prescribed.

(4) A taxpayer who has entered into a transaction with its associate shall furnish, within thirty days the documents and information to be kept and maintained under 3[clause (a), (c) or (d) of] sub-section (3) if required by the Commissioner in the course of any proceedings under this Ordinance.;

(5) The Commissioner may, by an order in writing, grant the taxpayer an extension of time for furnishing the documents and information under sub-section (4), if the taxpayer applies in writing to the Commissioner for an extension of time to furnish the said documents or information:

Provided that the Commissioner shall not grant an extension of more than forty-five days, when such information or documents were required to be furnished under sub-section (4), unless there are exceptional circumstances justifying a longer extension of time.

Q.4. 21. Interpretation

c

(a) "**comparable uncontrolled transaction**", in relation to a controlled transaction, means an uncontrolled transaction that satisfies one of the following conditions, namely:-

(i) The differences (if any) between the two transactions or between persons undertaking the transactions do not materially affect the price in the open market, the resale price margin or the cost plus mark up, as the case may be; or

(ii) if the differences referred to in sub-clause

(iv) do materially affect the price in the open market, the resale price margin or the cost plus mark up, as the case may be, then reasonably accurate adjustments can be made to eliminate the material effects of such differences;

- (b) "**controlled transaction**" means a transaction between associates;
- (c) "**Transaction**" means any sale, assignment, lease, license, loan, contribution, right to use property or performance of services;
- (d) "**Uncontrolled persons**" means persons who are not associates; and
- (e) "**Uncontrolled transaction**" means a transaction between uncontrolled persons.

22. Subject to the other rules, the Commissioner, in applying this Chapter shall also be guided by international standards, case law and guidelines issued by the various tax-related internationally recognized organizations.

23. Arm's length standard.

- (1) In determining the income of a person from a transaction with an associate, the standard to be applied by the Commissioner shall be that of a person dealing at arm's length with a person who is not an associate (referred to as the "arm's length standard").
- (2) A controlled transaction shall meet the arm's length standard if the result of the transaction is consistent with the result (referred to as the "arm's length result") that would have been realized if uncontrolled persons had engaged in the same transaction under the same conditions.
- (3) Subject to sub-rule (6), the following methods shall apply for the purposes of determining an arm's length result, namely: -
 - (a) the comparable uncontrolled-price method;
 - (b) the resale price method;
 - (c) the cost plus method; or
 - (d) the profit split method.
- (4) The method in clause (d) shall apply only where the methods in clauses (a), (b) and (c) cannot be reliably applied.
- (5) As between clauses (a), (b) and (c), the method that, having regard to all the facts and circumstances, provides the most reliable measure of the arm's length result as in the opinion of Commissioner shall be applied.
- (6) Where the arm's length result cannot be reliably determined under one of the methods in sub-rule (3) the Commissioner may use any method provided it is consistent with the arm's length standard.

24. Comparable uncontrolled price method:- The comparable uncontrolled price method determines whether the amount charged in a controlled transaction gives rise to an arm's length result by reference to the amount charged in a comparable uncontrolled transaction.

25. Resale price method:-

(1) The resale price method determines whether the amount charged in a controlled transaction gives rise to an arm's length result by reference to the resale gross margin realized in a comparable uncontrolled transaction.

(2) The following steps shall apply in determining the arm's length result under the resale price method, namely:-

(a) determine the price that a product purchased from an associate has been sold to a person who is not an associate (referred to as the "resale price"); and

(b) from the resale price is subtracted a gross margin (referred to as the "resale gross margin") representing the amount that covers the person's selling and other operating expenses and, in light of the functions performed (taking into account assets used and risks assumed), make an appropriate profit;

(c) from that amount is subtracted any other costs associated with the purchase of the product, such as customs duty; and

(d) the amount remaining is the arm's length result.

(3) The resale price margin of a person in a controlled transaction may be determined by reference to:

(a) the resale price margin that the person earns on products purchased and sold in a comparable uncontrolled transaction; or

(b) the resale price margin that an independent person earns in comparable uncontrolled transaction.

26. Cost plus method:-

(1) The cost plus method determines whether the amount charged in a controlled transaction gives rise to an arm's length result by reference to the cost plus markup realised in a comparable uncontrolled transaction.

(2) The following steps shall apply in determining the arm's length result under the cost plus method, namely:-

(a) determine the costs incurred by the person in a controlled transaction;

(b) to this amount is added a mark up (referred to as the "cost plus mark up" to make an appropriate profit in light of the functions performed and market conditions; and

(c) the sum of the amounts referred to in clauses (a) and (b) is the arm's length result.

(3) The cost plus mark up of a person in a controlled transaction may be determined by reference to:-

(a) the cost plus mark up that the person earns in a comparable uncontrolled transaction; or

(b) the cost plus mark up that an independent person earns In comparable uncontrolled transaction.

27. Profit split method.

(1) The profit split method may be applied where transactions are so interrelated that the arm's length result cannot be determined on a separate basis.

(2) The profit split method determines the arm's length result on the basis that the associates form a firm and agree to divide profits in the manner that independent persons would have agreed on the basis that they are dealing with each other at arm's length.

(3) The Commissioner may determine the division of profits on the basis of a contribution analysis, a residual analysis or on any other basis as appropriate having regard to the facts and circumstances.

(4) Under contribution analysis, the total profits from controlled transactions shall be divided on the basis of the relative value of the functions performed by each person participating in the controlled transactions.

(5) Under residual analysis, the total profits from controlled transactions shall be divided as follows:

(a) each person shall be allocated sufficient profit to provide the person with a basic return appropriate for the type of transactions in which the person is engaged; and

(b) any residual profit remaining after the allocation in clause (a) shall be allocated on the basis of division between independent persons determined having regard to all the facts and circumstances.

(6) For the purposes of clause (a) of sub-rule (5), the basic return shall be determined by reference to market returns achieved for similar types of transactions by independent persons.

Q.5. 13A. Acquisition of securities.-

a

(1) A security may be acquired through purchase, exchange, bonus issue, right issue, gift, bequest, inheritance, leverage schemes and derivative contracts.

(2) A security may be acquired in the electronic book entry form or in the form of physical certificate.

(3) A security may be acquired through the trading platform provided by a stock exchange or through off market transactions.

(4) In case of securities other than units of an open mutual fund, broker's bill for the purchase, broker generated computerized ledger statement of the investor's brokerage account, CDC statement of the investor's CDC sub account and payment of cost of acquisition through cheques shall be supportive evidence of acquisition of securities.

(5) In case of units of an open end mutual fund, certified statement of investor's account provided by the asset management company shall be supportive evidence of acquisition of securities.

13B. Disposal of securities.

(1) A security may be disposed of through sale, gift, exchange or transfer by the security holder in any other way.

(2) A security may be disposed of in the electronic book entry form or in the form of physical certificate.

(3) A security may be disposed of through the trading platform provided by a stock exchange or through off market transactions.

(4) In case of securities other than units of an open mutual fund, broker's sale proceeds or difference bill, broker generated computerized ledger statement of the investor's brokerage account, CDC statement of the investor's CDC sub-account and proof of payment through cheques

shall be supportive evidence of disposal of securities.

(5) In case of units of an open end mutual fund, certified statement of investor's account provided by the asset management company shall be supportive evidence of disposal of securities.

13C. Holding period.

(1) Securities held for a period upto a maximum of one eighty-two days and for a period upto maximum of three sixty-five days shall be taken as held for six months and one year respectively.

(2) In case of short positions, holding period shall be the period intervening between the date when a security is sold short and the date when the security is purchased to cover the short position.

(3) In case of futures contracts, holding period shall be the period intervening between the date of entry into a futures contract and the date of exit from such contract.

13D. Computation of capital gain or loss.

(1) Capital gain or loss arising on the disposal of any security shall be computed on the basis of First In First Out (FIFO) inventory accounting method.

(2) Capital loss arising on disposal of securities in any tax year shall be set off against capital gain arising from the disposal of securities during that tax year to determine the taxable capital gain arising from the disposal of securities.

(3) Capital loss arising on disposal of listed securities in tax year 2019 and onwards that has not been set off against the gain of the person from disposal of listed securities chargeable to tax during the tax year shall be carried forward to the following tax year and set off only against the gain of the person from disposal of listed securities chargeable to tax but no such loss shall be carried forward to more than three tax years immediately succeeding the tax year for which the loss was first determined;]

Q.5.
b

Rent received during the year	1,500,000
Less: Property Tax paid	30,000
Less: Insurance premium paid to insure the rented building	100,000
Less: 1/5 th of Rent	300,000
Taxable rent	1,070,000
Tax 5% of the amount exceeding PKR 600,000	23,500
