

Form HCJD/C-121  
**ORDER SHEET**  
**IN THE LAHORE HIGH COURT, MULTAN BENCH, MULTAN**  
**(JUDICIAL DEPARTMENT)**  
**ITR No.53 of 2022**  
**Commissioner Inland Revenue, Legal Zone, LTO., Multan**  
**Versus**  
**M/s Al-Hilal Industries (Pvt.) Ltd.**

S.No.of order/ Proceeding	Date of order/ Proceeding	Order with signature of Judge, and that of parties or counsel, where necessary
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18.11.2025 Mr. Muhammad Shaukat Qamar, Advocate for applicant.  
M/s Muhammad Usman Hadi and Jamil Ahmad Shaikh,  
Advocates for the respondent.

Following questions, statedly arising out of order  
of 20.04.2022 by the Appellate Tribunal Inland Revenue,  
Multan Bench, Multan (the “Tribunal”), are proposed for  
determination.

1. *Whether on the facts and circumstances of the case the learned ATIR has failed to appreciate that the profit on redeemable capital on the basis of profit/loss sharing basis is not an admissible expense under any provision of Income Tax Ordinance, 2001?*
  2. *Whether on the facts and circumstances of the case the learned ATIR has failed to appreciate that the profit on redeemable capital is not in the nature of interest on borrowed money therefore, no deductible u/s 21 of the Income Tax Ordinance, 2001?*
  3. *Whether on the facts and circumstances of the case the learned ATIR has failed to appreciate that Participation Term Finance Certificates were issued for redeemable capital u/s 120 of the Companies Ordinance, 1984 which are not interest based.*
2. Tax Year was 2010. Record depicts that the Tribunal had dismissed the appeal of the department on the ground that no recharacterization of the transaction, presented by the taxpayer while furnishing return or through lateral explanation, could be directed in

absence of any notice or prior intimation, indicating an intent to recharacterize the transaction in question – presently, respondent taxpayer had sought allowable deduction on the premise of payment of profits, subject to tax deductions under section 151 of the Income Tax Ordinance 2001 ('Ordinance'), to the holders of Participatory Term Finance Certificates (PTFCs), happened to be the shareholders / directors of respondent company ('certificate holders'). In this case notice under section 122(5A) / (9) of the Ordinance, intending an amendment of assessment for relevant tax year, was conveyed. Tribunal had not determined the admissibility or otherwise of the deduction claimed but dismissed department's appeal in wake of absence of due process requirement. It is pertinent to identify that certificate holders had extended redeemable capital to the company – distinguishable from transaction of equity injection against acquisition of shares.

3. In the context of operative and material observations recorded by the Tribunal, actual controversy hinges on the interpretation of scope and effect of section 109 of the Ordinance. And incidentally, questions proposed do not reflect the actual controversy, we, therefore, recast the question of law:

***Whether section 109 of the Ordinance could be given effect while undertaking an exercise of amendment of assessment proceedings?***

4. Learned counsel for the respondent submits that recharacterization of transaction was not a legally permissible course, while amending the assessment; adds that if at all such recharacterization was warranted, such course could be adopted by issuance of fresh and separate notice, accordingly. Submits that precise allegation in show cause notice was that profits paid to certificate holders were not subjected to payment of tax under section 151 of the Ordinance, which query was addressed, whereafter, there was no basis for recharacterization.

5. Conversely, learned counsel for the applicant department submits that declaration of recharacterization does not require issuance of separate notice but such course was the consequence of analysis undertaken pursuant to notice under section 122(5A) of the Ordinance.

6. Heard.

7. Evidently, respondent claimed deduction of the sums paid as profits to certificate holders, as an allowable expense incurred and accordingly deductible. Transaction came under scrutiny and analysis thereof convinced the Assessing officer that substance of the

transaction was not aligned with the form thereof – the way it was presented by the taxpayer. Undisputedly, when asked about the nature of the transaction, substance and economic rational thereof, [taxpayer] was obligated to justify, explain and substantiate that deduction claimed was in accordance with the law and otherwise not intended as a tool to avoid tax – otherwise bordering tax evasion. And if taxpayer fails, the Assessing officer is within the scope of jurisdictional mandate to unshackle the transaction and identify its true character – Assessing officer is not bound to accept the transaction as devised by the taxpayer but entitled to unfold the layering and understand substance thereof. This course is permissible and is, legally, classified as, recharacterization of the transaction – envisaged in terms of section 109 of the Ordinance. Section 109 of the Ordinance starts with the *caveat* “..... *for the purposes of determining liability of tax under the ordinance....*”, which indicates that resort to recharacterization mechanism could be made in the circumstances and such pathway is a permissible mode for determining the tax liability. It is fallacious to believe that recharacterization process is independent of scrutiny undertaken in terms of section 122 of the Ordinance – no similarity could be claimed qua

recharacterization mechanism and an instance where explanation was sought in the context of section 111 of the Ordinance, when in later case taxpayer is confronted with the identity / acquisition of a tangible asset or possession of money, and asked to provide source thereof and in former case transaction was transacted and claimed as valid one. And what was required to be determined is true character or substance thereof. Piercing of transaction to unfold its true character is in essence recharacterization thereof – which is elaboration of concept of "look at versus look through".

Recharacterization is the consequence of exercise of jurisdiction under section 122 of the Ordinance and objective thereof is to reverse an unintended tax advantage, not otherwise available. Tribunal non-suited the department and annulled determinations on the ground that no prior notice was issued before embarking upon an exercise of recharacterization of transaction. This understanding of concept of recharacterization under section 109 of the Ordinance is grossly flawed. Power / authority to recharacterize transaction is part and parcel of the jurisdiction exercisable while undertaking re-assessment of deemed assessment order - it is evident from the contents of show-cause notice that explanation was sought qua

legality of an expense / deduction claimed with respect to the profits paid to the certificate holders and explanation provided was found inadequate and commercially deviant, whereupon the Assessing officer denied claim of an allowable expense after unearthing the true character / substance of the transaction – in brief, recharacterization is an incidence / process of evaluating and defining the real nature of the transaction. Therefore, power to ascertain substance of the transaction, contrary to its form, while undertaking re-assessment of assessment order, is not a mutually exclusive exercise but mutually inclusive process. And is part and parcel of jurisdiction to amend the assessment.

No violation of due process principle was apparent when respondent taxpayer was put to notice with respect to the transaction claimed as allowable deduction, and same would always be entitled to explain the transaction and establish objectivity thereof, to dislodge impression of avoidance of tax. We refrain from commenting on the merits of the transaction and admissibility thereof in the context of deduction claimed.

8. In view of the above, we hold that process of recharacterization of transaction is part of the jurisdiction exercised under section 122 of the

Ordinance and no fresh notice was required before uncovering the substance of the transaction. Since Tribunal had dismissed the appeal on the ground of absence of due process requirement – absence of notice before carrying out recharacterization of transaction - therefore, we are inclined to remand the matter to the Tribunal for deciding the appeal of the department on merits, afresh.

9. Reframed question of law is answered in affirmative and decided in favour of the applicant department and reference application is allowed accordingly. Questions originally framed need not to be discussed.

10. Office shall send copy of this order under the seal of the Court to the learned Appellate Tribunal as per the requirements of Section 133(8) of the Income Tax Ordinance, 2001.

**(Abid Hussain Chattha)**  
Judge.

**(Asim Hafeez)**  
Judge.

Approved for reporting.

**(Abid Hussain Chattha)**  
Judge.

**(Asim Hafeez)**  
Judge.