

IN THE SUPREME COURT OF PAKISTAN
(APPELLATE JURISDICTION)

PRESENT:

MR. JUSTICE MIAN SAQIB NISAR, HCJ
MR. JUSTICE UMAR ATA BANDIAL
MR. JUSTICE FAISAL ARAB

CIVIL APPEAL NO. 1338 OF 2007

(On appeal against the judgment dated
14.03.2006 passed by the High Court of Sindh,
Karachi in ITR No. 03/1994)

Commissioner of Income Tax, Companies Zone, Islamabad
... Appellant

VERSUS

M/s Pak Saudi Fertilizer Ltd
...Respondent

For the Appellant: Dr. Farhat Zafar, ASC
Raja Abdul Ghafoor, AOR

For the Respondent: Mr. Iqbal Salman Pasha, ASC

Date of Hearing: 20.02.2017

JUDGMENT

FAISAL ARAB, J.- In the assessment years 1987-88, 1988-89 and 1989-90, the respondent invested a sum of Rs.14,99,99,762/- in the purchase of National Funds Bonds. The interest income on such Bonds was exempt from tax under the provisions of Clause 170 to the Second Schedule to Part I of the erstwhile Income Tax Ordinance, 1979. In these assessment years, the respondent on such investment derived interest income to the tune of rupees 19.6 million. Considering the fact that the respondent on the one hand was claiming exemption on interest income and on the other hand interest expense was being incurred on loans borrowed from Asian Development Bank and Government of Saudi Arabia, the Income Tax Officer drew an inference that borrowed monies were diverted to purchase the National Funds Bonds to derive tax free income. The Income Tax Officer thus disallowed the interest accrued on the loans in proportion to the interest income derived from the Bonds to the extent of rupees 12.13 million.

2. The decision of the Income Tax Officer was challenged by the respondent upto the stage of Income Tax Tribunal but without success. The respondent then filed Reference in the High Court of Sindh, which framed the question "*whether on the facts and in the circumstances of the case the learned Income Tax Appellate Tribunal was justified in confirming the disallowance of proportionate interest*". This question was answered in the negative against the department and in favour of the respondent. After taking into consideration the plea of the respondent that the loans that were obtained by the respondent from Saudi Arabian Government as well as from the Asian Development Bank were utilized in the purchase of fixed assets and the investment in the National Funds Bonds was made from the capital and unappropriated profits available with the respondent, the learned High Court held that the Tribunal's findings were based merely on assumptions and conjectures as it failed to examine whether the Bonds were in-fact purchased from the borrowed monies or not. Aggrieved by such decision, the appellant filed the present appeal with the leave of this Court.

3. Learned counsel for the appellant argued that as a huge loan amount was outstanding against the respondent, the investment made in the National Funds Bonds for deriving tax free income was not justified for the reason that on the one hand the interest expense was being claimed on the borrowed monies and on the other hand tax free income was being derived by investing the very same amount in the Bonds, thereby taking undue advantage.

4. In rebuttal, learned counsel for the respondent submitted that from the statement of accounts of the respondent relating to the tax years in question it was evident that long term loans were obtained, which were utilized in the purchase of capital assets for setting up fertilizer plant and the investment that was made in National Funds Bonds was out of respondents' own capital and unappropriated profits, which had no nexus with the loan amount and this aspect was not considered at any stage upto

the Income Tax Tribunal and was only taken into account by the High Court.

5. It is an admitted position that the interest income on the investment made in the National Funds Bonds was exempt from tax under Clause 170 to the Second Schedule to the Part I of the Income Tax Ordinance. The appellant's counsel failed to point out that there was any restriction under the law that would have disentitled the respondent from claiming exemption on the interest income in case there were loans standing against it. A perusal of the copies of the statement of accounts filed by the respondent, it is quite evident that long term loans were obtained by the respondent prior to the purchase of the Bonds which were to be discharged with interest over a long period of time. Hence, independent of the financial obligation against the long term loans, the respondent made investment in the National Funds Bonds with its own funds generated from its business. The interest income derived thereon was admittedly exempt under the law and had no co-relation whatsoever with the loans. Irrespective of any co-relation between the two, no provision of law was shown to us to establish that mere existence of financial obligation in the form of loans would have disentitled the respondent from claiming exemption granted under Clause 170 to Second Schedule to Part I of the defunct Income Tax Ordinance, 1979.

6. We, therefore, find no justification to reverse the findings arrived at by learned High Court of Sindh. This appeal is, therefore, dismissed.

CHIEF JUSTICE

JUDGE

JUDGE

Islamabad, the
20th of February, 2017
Approved For Reporting
Khurram