

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 APPEALS NO.1590 TO 1598 OF 2006

(Against the judgment dated 1.9.2005/22.3.2006/16.2.2006/29.3.2006/8.3.2006/14.4.2006/2.5.2006/5.4.2006/26.4.2006 of the High Court of Sindh, Karachi passed in ITR No.13/1999, 133/1997, 38/1998, 173/1997, 949/1999, 22/1993, 459/1990, 56/1995 & ITC No.410/1997)

Commissioner of Income Tax Karachi

...Appellant(s)
(In all cases)

VERSUS

M/s Khalid Textile Mills	In C.A.1590/2006
M/s Karachi Electric Supply Corporation	In C.A.1591/2006
M/s Gulistan Textile Mills Ltd.	In C.A.1592/2006
M/s Gul Ahmed Textile Mills Ltd.	In C.A.1593/2006
M/s Faran Sugar Mills Ltd.	In C.A.1594/2006
M/s Mehran International Ltd.	In C.A.1595/2006
M/s National Printing & Packing Ltd.	In C.A.1596/2006
M/s Pfizer Laboratories Ltd.	In C.A.1597/2006
M/s Dewan Textile Mills Ltd.	In C.A.1598/2006

...Respondent(s)

For the appellant(s): Dr. Farhat Zafar, ASC
(In CA No.1590/2006)

Mr. Muhammad Habib Qureshi, ASC
Raja Abdul Ghafoor, AOR
(In CAs No.1591 to 1594/2006)

Mr. Muhammad Siddique Mirza, ASC
(In CA No.1595/2006)

For the respondent(s): Mr. Iqbal Salman Pasha, ASC
(In CAs No.1590, 1591, 1593 to 1595, 1597 & 1598/2006AH32)

Ex-parte
(In CAs No.1592 & 1596/2006)

Dates of hearing: 7.2.2017 & 8.2.2017

...
ORDER

MIAN SAQIB NISAR, CJ.- The question before this Court is whether tax credit(s) available under Section 107 of the erstwhile Income Tax Ordinance, 1979 (*the Ordinance*) were to be excluded while

computing the actual cost of an asset in order to determine its written down value for the purposes of calculating depreciation allowance in terms of Rule 8(8)(b) of the Third Schedule to the Ordinance. .

2. The brief facts (*in Civil Appeals No.1590 to 1592 and 1595 to 1597/2006*) are that the respondents (*assesseees*) are companies (*both public and private limited*) deriving income from various industrial activities. In their returns pertaining to various assessment years, they claimed tax credit(s) and depreciation allowance under the Ordinance on their plants and machinery. The assessment orders calculated the depreciation allowance **after** subtracting tax credit(s) from the written down value of the assets, thereby curtailing the respondent's claim of depreciation allowance (*note:- in Civil Appeal No.1597/2006, in the original assessment order, depreciation allowance was calculated without subtracting tax credit. However when the original assessment was re-opened under Section 66-A of the Ordinance, Inspecting Assistant Commissioner of Income Tax ordered that depreciation allowance be calculated after subtracting tax credit from the written down value of the assets, thereby curtailing the respondent's claim of depreciation allowance*). The learned High Court passed the impugned judgments in Income Tax references (*references*) in favour of the respondents by relying upon **Gulshan Spinning Mills Ltd. and others Vs. Government of Pakistan and others (2005 PTD 259)** (*note:- in Civil Appeal No.1595/2006, the learned High Court relied upon the impugned judgment rendered in Civil Appeal No.1590/2006, i.e. ITR No.13/1999*). This Court granted leave *vide* order dated 5.10.2006 to consider the following:-

“(i) Whether on the facts and circumstances of this case Hon’ble High Court and Income Tax Appellate Tribunal was justified in holding that assessee in (*sic*) entitled to depreciation calculated on the W.D.V. of assets without reducing there from (*sic*) the amount of tax credit u/s 107 of the Income Tax Ordinance, 1979, despite of

specific provision as laid down under rule 8(8)(b) of 3rd Schedule of the Income Tax Ordinance, 1979.

(ii) Whether on the facts and circumstances of this case Hon'ble High Court after holding that tax credit u/s 107 not being in the nature of exemption, allowance and deduction, has rightly allowed to exclude tax credit from depreciation calculated on the W.D.V. of assets under rule 8(8)(b) of 3rd Schedule of the Income Tax Ordinance, 1979."

It bears mention that leave in these cases was granted on the basis of the leave granting order dated 14.6.2005 passed in Civil Appeal Nos.612 to 636/2005 and although the noted cases were disposed of *vide* order dated 3.4.2008 that was done on the basis of the parties' consent. Therefore, the aforementioned question of law remains to be determined by this Court.

3. Learned counsel for the appellant department (*in Civil Appeal Nos.1591 to 1594/2006*) argued that tax credit applicable on plant and machinery under Section 107 of the Ordinance fell within the expression "value of assistance" received by an assessee from Government or any other authority or person appearing in Rule 8(8)(b) which (*expression*) had a wide connotation and the only type of assistance it specifically excluded was that of any loan repayable with or without interest. He submitted that Rule 8(8)(b) applied to tax credits under Section 107 and therefore the impugned judgments were liable to be set aside. According to him, when an assessee claimed tax credit at the rate of 15% of the assets, the actual cost of the asset to the assessee was accordingly reduced, as in terms of Rule 8(7)(b) the written down value was to be calculated on the basis of the actual cost to the assessee and not the total cost of the asset. His arguments were adopted by the

learned counsel for the appellant in Civil Appeal Nos.1590/2006 and 1595/2006.

4. Learned counsel for the respondents (*in Civil Appeal Nos.1590, 1591, 1593 to 1595, 1597 and 1598/2006*) argued that tax credit under Section 107 was claimed on the actual cost of plant and machinery which was to be deducted from the tax payable for the year and not from the taxpayer's income, therefore, tax credit was not a grant, subsidy, rebate, commission, deduction or allowance under the Ordinance. According to him, the learned High Court rightly held that Rule 8(8)(b) was not applicable to tax credits under Section 107. He relied on the case of **Gulshan Spinning Mills** (*supra*).

5. Heard. The relevant portions of Section 107 and Rule 8 (*of the Third Schedule*) of the Ordinance are reproduced as under:-

***“107. Tax credit for replacement, balancing and modernisation of machinery or plant.- (1) Where an assessee being a Pakistani company invests any amount in the purchase of plant and machinery for installation at any time between the first day of July, 1976 and the thirtieth day of June, 1988 or between the first day of July, 1990 and the thirtieth day of June, 1991, in an industrial undertaking set up in Pakistan and owned by it, for the purposes of replacement, balancing or modernisation of the machinery and plant already installed therein, credit at the rate of fifteen per cent of the amount so invested shall be allowed against the tax payable by it in the manner hereinafter provided.*”**

Explanation.- As used in this sub-section,-

(a) "amount", in case of plant and machinery acquired on lease, means the amount expended by the lessor in the purchase of the said plant and machinery; and

(b) "purchase of plant and machinery" includes acquisition of plant and machinery on lease from a scheduled bank, a financial institution or a leasing

company on such terms and conditions as may be approved by the Central Board of Revenue.

(2) The amount of credit admissible under this section shall be deducted from the tax payable by the assessee in respect of the income year in which the machinery or plant in the purchase of which the amount referred to in sub-section (1) is invested is installed.

(3)

(4) The provisions of sub-section (1) and (2) shall also apply in the like manner to any plant and machinery installed, for the purposes of extension of the industrial undertaking:-

- (i) on or after the first day of July, 1978, and before the thirtieth day of June, 1983 in the territories of Pakistan; or*
 - (ii) on or after the first day of July, 1983, in the territories of Pakistan (excluding Talukas of Karachi and Hyderabad, and Tehsils of Faisalabad and Lahore, and such adjoining areas of Lahore Tehsil as may be notified in this behalf by the Federal Government).*
- ⋮*
- (8)*

THE THIRD SCHEDULE
(See Section 23)

RULES FOR THE COMPUTATION OF DEPRECIATION ALLOWANCE

- 1. Allowances for depreciation.** *(1) Where, in any income year, any building, machinery, plant or furniture owned by an assessee is used for purposes of any business or profession carried on by him...an allowance for depreciation shall be made in computing the profits and gains of the business or profession of the assessee in the manner hereinafter provided.*
- 8. Definitions.-** *For the purpose of this Schedule,-*
- (7) "written down value" means-*

- (a) in the case of a ship or any asset to which sub-rule (3) of rule 2 applies,-
 - (i) for purpose of rule 7, as in sub-clause (b), and
 - (ii) for any other purpose, the actual cost thereof to the assessee; and
- (b) in the case of other assets,-
 - (i) where the asset, was acquired in the income year, the actual cost thereof to the assessee; and
 - (ii) where the asset, was acquired before the income year, the actual cost thereof to the assessee as reduced by the aggregate of the allowance for depreciation allowed to him under this Ordinance or the repealed Act in respect of the assessments for earlier years.

(8) For the purposes of clause (7),-

- (a)
- (b) in computing the actual cost of an asset, the amount of any grant, subsidy, rebate or commission and the value of any assistance (not being in the nature of any loan repayable with or without interest) received by an assessee from Government or any other authority or person and any deduction or allowance admissible under this Ordinance or the repealed Act shall be excluded;
⋮
- (h)

Explanation..... ”

6. Chapter X of the Ordinance, particularly Sections 105 to 107AA, which pertained to tax credits for various types of investments, is instructive in this regard. A tax credit is an incentive or relief given to the taxpayer, usually for the purposes of promoting certain industries or activities. Section 107 of the Ordinance allowed for tax credit at the rate of 15% of the amount invested for the replacement, balancing and modernization of machinery or a plant against the tax payable.

According to Section 107(2) the amount of credit was to be deducted from the tax payable by the assessee in respect of the income year in which the said machinery or plant was installed. Tax credit was not defined in the Ordinance. Black's Law Dictionary (9th Ed.) defines it as *"an amount subtracted directly from one's total tax liability, dollar for dollar, as opposed to a deduction from gross income"*. P. Ramanatha Aiyar's Concise Law Dictionary (4th Ed.) states, *"Tax credit is a legal provision permitting taxpayers to deduct specified sums from their tax liability"*. The Oxford Advanced Learner's Dictionary of Current English (8th Ed.) provides that tax credit is *"money that is taken off your total tax bill"*. Thus tax credit is an amount which is directly offset against or adjusted/deducted from the tax liability and not the gross income.

7. The relevant provision with regard to depreciation allowance was Section 23(1)(v) of the Ordinance according to which for the purposes of computing income under the head "income from business or profession", certain allowances and deductions were admissible in terms of the Third Schedule in respect of depreciation; including First Year Allowance or Reinvestment Allowance or Industrial Building Allowance, of any building, machinery, plant, furniture or fittings, being the property of the assessee, except depreciation or First Year Allowance on assets given on lease which was to be allowed against income from lease rentals only, and such depreciation allowance was to be computed in terms of the rules in the Third Schedule. In similar terms, Rule 1 of the Third Schedule provided that where, in any income year, any building, machinery, plant or furniture owned by an assessee was used for purposes of any business or profession carried on by him, or in any income year commencing on or after the first day of July, 1982, any machinery or plant was given on lease by the assessee, being

a scheduled bank, a financial institution (*or such modaraba or leasing company as is*) approved by the Central Board of Revenue for purposes of the Third Schedule, an allowance for depreciation would be made in computing the profits and gains of the business or profession of the assessee. Rule 2 of the Third Schedule stipulated the various rates at which depreciation allowance was admissible, which was a certain percentage of the written down value of the asset. Rule 8 of the Third Schedule contained the definitions of various words which were “*For the purpose of this [Third] Schedule*” and Clause (7) thereof defined “written down value” as reproduced above which was either the actual cost thereof to the assessee or the actual cost thereof to the assessee reduced by the depreciation allowance for assets acquired before the income year in question. The actual cost of the asset to the assessee was elucidated and clarified in Clause (8) which began with the phrase “*For the purposes of clause (7)*”. Part (b) thereof stipulated that in computing the actual cost of an asset, the following were to be excluded:-

- i. the amount of any grant, subsidy, rebate or commission and the value of any assistance (*not being in the nature of any loan repayable with or without interest*) received by an assessee from the Government or any other authority or person; and
- ii. any deduction or allowance admissible under this Ordinance or the repealed Act.

The word “excluded” needs to be elucidated. According to Chambers 21st Century Dictionary (2007), “exclude” means “*to omit someone or something or leave them out of consideration*” while “excluding” means “*not counting; without including*”. The Oxford Advanced Learner’s Dictionary of Current English (8th Ed.) defines “exclude” as “*to deliberately not include*

[something] in what you are doing or considering". In the light of the aforementioned definitions, exclude essentially means to remove from consideration. The implication of this is significant. It means that the amount of any grant, subsidy, rebate, or commission, and the value of any assistance (*not in the nature of any loan repayable with or without interest*) received by an assessee from the Government or any other authority or person, and any deduction or allowance admissible under this Ordinance (*or the repealed Act*) were not to be considered while computing the actual cost of an asset. Therefore the interpretation adopted by the learned counsel of both the parties to the effect that excluded meant deducted or subtracted is absolutely incorrect and misconceived.

8. The question is whether tax credit fell within the ambit of Rule 8(8)(b) in the Third Schedule of the Ordinance in that it was not to be considered while computing the actual cost of an asset. Rule 8(8)(b) of the Third Schedule can be bifurcated into two parts as highlighted in the preceding paragraph. The first part pertains to the amount of any grant, subsidy, rebate or commission and the value of any assistance (*not being in the nature of any loan repayable with or without interest*) received by an assessee from Government or any other authority or person. In our view tax credit does not fall within the domain of any of these terms, i.e. grant, subsidy, rebate, commission or the value of any assistance by dint of the fact that they are not benefits received by an assessee under the Ordinance but received otherwise from the Government or any other authority or person. It is the second part of Rule 8(8)(b) which related to **any deduction** or allowance **admissible under the Ordinance** (*or the repealed Act*). We now need to determine whether tax credit fell within the second part of Rule 8(8)(b), i.e. was it a deduction or allowance admissible under the Ordinance?

9. Section 24 of the Ordinance categorically set out those deductions which were not admissible under the Ordinance and therefore did not fall within the ambit of Rule 8(8)(b). However various types of deductions **were** allowed under the Ordinance. By way of illustration, Sections 18, 20, 23 and 31 pertained to deductions to be made whilst computing income under the heads interest on securities, income from house property, income from business or profession and income from other sources respectively. These were deductions made to the total taxable income. According to Section 107(2) of the Ordinance, the amount of credit admissible under Section 107 “*shall be **deducted** from the tax payable by the assessee...*” [Emphasis supplied]. Therefore whilst tax credit is undoubtedly a deduction, it is made against the tax payable as mentioned in paragraph 6 of this opinion. It is pertinent to note that Rule 8(8)(b) did not make any distinction between deductions from the taxable income and deductions from the tax payable. The test was only that of “*any deduction...admissible under the Ordinance*” (or the repealed Act) and we are of the view that tax credit is a deduction albeit from the tax payable [Section 107(2)] and being admissible under the Ordinance (Section 107) it clearly fell within the ambit of Rule 8(8)(b) of the Third Schedule. Therefore, the key question identified in the opening paragraph of this opinion is answered in the affirmative, in that, tax credit available under Section 107 of the Ordinance did fall within the purview of Rule 8(8)(b) of the Third Schedule to the Ordinance and thus was to be excluded or rather not to be considered while computing the actual cost of an asset when determining the written down value thereof for the purposes of calculating depreciation allowance.

10. In the case of **Gulshan Spinning Mills** (*supra*) relied upon by the learned counsel for the respondents and the learned High Court in the impugned judgments it was held that:-

“...tax credit is neither an allowance nor deduction permissible under the Income Tax Ordinance, 1979, for the purpose of determining the total income (assessed income). It is not in the nature of exemption as well. Anything in the nature of exemption, allowance or deduction shall form part of the assessment order and this, shall be integral part of the assessment process and therefore, shall be allowed in accordance with law prevailing in the assessment year. As held above, the tax credit under section 107 of the Income Tax Ordinance, is not in the nature of exemption, allowance or deduction for the purpose of computing the income under the head business or profession, therefore, it shall not be a part of assessment process/assessment order.”

A perusal of the aforesaid extract makes it clear that the reference to tax credit under Section 107 of the Ordinance in the said case was with respect to the determination of total taxable income and not the written down value of an asset for the purposes of depreciation allowance. The issue at hand and the interpretation of Rule 8(8)(b) of the Third Schedule was not under consideration in the case of **Gulshan Spinning Mills** (*supra*).

11. In the light of the above, Civil Appeals No.1590 to 1592 and 1595 to 1597/2006 are dismissed.

As regards Civil Appeals No.1593, 1594 and 1598/2006, the issue involved (*particularly before the learned High Court in the tax references*) was not whether tax credit should be considered while calculating the written down value for the purposes of determining depreciation allowance. Rather, the moot point was whether the dates of installation of the plant and machinery were relevant for the purposes of claiming tax credit

under Section 107 of the Ordinance, and not the date of purchase thereof. This was the precise issue decided by the learned High Court in **Gulshan Spinning Mills** (*supra*), however this was neither brought to the attention of this Court during the leave granting stage and nor have we received any assistance on this point, therefore the leave granting order(s) in the noted cases are withdrawn and the petitions are accordingly dismissed as no point requiring the grant of leave has been made therein.

CHIEF JUSTICE

JUDGE

JUDGE

Announced in open Court
on **29.3.2017** at **Islamabad**
Approved For Reporting
Waqas Naseer/*