IN THE SUPREME COURT OF PAKISTAN
(Appellate Jurisdiction)

PRESENT:
MR. JUSTICE MUNIB AKHTAR
MR. JUSTICE MUHAMMAD SHAFI SIDDIQUI
MR. JUSTICE MIANGUL HASSAN AURANGZEB

C.P.L.A. 3169 of 2022
(Against judgment dated 16.06.2022 passed by the Lahore High Court, Lahore in P.T.R. No.349/2010.)

Coca Cola Pakistan Ltd. (The Coca-Cola Export Corporation, PB), Lahore **... Petitioner**

vs

Commissioner Inland Revenue, Large Taxpayers Officer, Lahore **... Respondent**

For the Petitioner : Mr. Adnan Haider, ASC

For the Respondent : Mr. Ahmed Pervaiz, ASC (via video-link, Lahore)

Date of Hearing : 03.10.2025

JUDGMENT

Munib Akhtar, J.: This matter is being disposed of as an appeal; see below. It arises out of the Income Tax Ordinance, 2001 ("2001 Ordinance") for the tax year 2003. A tax reference filed by the Commissioner (herein after referred to as the "Department") inter alia presented the following question of law for the consideration of the High Court in the facts and circumstances of the case:

> Whether the learned Appellate Tribunal was justified to hold that Rule 13 of the Income Tax Rules, 2002 ("2002 Rules") is not mandatory for purpose of apportionment of expenses under s. 67 of the 2001 Ordinance?

The question was answered in favor of the Department by means of the impugned judgment and the taxpayer now petitions this Court for leave to appeal against the same.

2. It will be convenient to first set out the relevant statutory provisions. Section 67 provided at the relevant time as follows:

> "**67. Apportionment of deductions**.— (1) Subject to this Ordinance, where an expenditure relates to –
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> (a) the derivation of more than one head of income; or
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> (ab) derivation of income comprising of taxable income and any class of income to which sub-sections (4) and (5) of section 4 apply, or;
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> (b) the derivation of income chargeable to tax under a head of income and to some other purpose,
>
> the expenditure shall be apportioned on any reasonable basis taking account of the relative nature and size of the activities to which the amount relates.
>
> (2) The Central Board of Revenue may make rules under section 237 for the purposes of apportioning deductions."

In Rule 13 of the 2002 Rules it is necessary only to consider the following provisions, as they stood at the relevant time:

> "(2) Any expenditure that is incurred for a particular class or classes of income shall be allocated to that class or classes, as the case may be."
>
> "(3) (a) Any common expenditure including financial expenses, excluding relatable or attributable to the non-business advances or loans and amount at (2); relatable to business including presumptive and exempt income, shall be allocated to each class of income according to the following formula [which provides for apportionment with reference to gross receipts and "net gains for the tax year of all classes of income"] ..."
>
> "(4) Where expenditures are to be allocated among different classes of income under sub-rule (3), consideration shall be given to the nature and source of each class of income, on reasonable basis to earn each class of income (particularly, in allocating selling expenses)."
>
> "(8) In this rule. -
>
> "class of income" means – ...
>
> (e) Pakistan-source income chargeable under the head "Income from Business" (other than income subject to section 19); ...
>
> (n) chargeable to tax under section 5, 6 or 7; ...

> "common expenditure" means expenditure that is not clearly allocable to any particular class or classes of income, such as general administrative and other such allocable expenditures."

(We may note in passing that the numbering of sub-rule (8) was an obvious typographical error inasmuch as the sub-rule prior thereto was numbered as (5). This and other such errors were cleaned up in 2009. This has no material bearing on the outcome of this case and we mention it only to avoid any possible confusion and to note that we will refer to the sub-rule here as numbered above.)

3. The petitioner-taxpayer is a well known company involved inter alia in the manufacture and sale of beverages. As presently relevant, over the period in question its income was sourced in two ways. Firstly, it came from the sale of soft drinks manufactured in Pakistan. This was a class of income under clause (e) of sub-rule (8) of Rule 13. The other was imported soft drinks, which were sourced in final form and were sold as such (i.e., without any manufacturing or other such operation at all) in the country. Income tax was paid on such imports under s. 148 at import stage and as therein (then) provided constituted "final" tax thereon. This was a class of income within the meaning of clause (b) of subsection (4) of s. 4 read with s. 5 and hence a class within the meaning of clause (n) of sub-rule (8) of Rule 13. Such income is commonly known as "presumptive tax regime" or "final tax regime" income, abbreviated as PTR or FTR income; income that would fall within the scope of taxable income, generally defined, is referred to as non-PTR (or –FTR) income. (Non-PTR income is also commonly referred to as "normal tax regime" (or NTR) income.) The income under clause (e) of sub-rule (8) of Rule 13 was non-PTR income.

4. The taxpayer filed its return under s. 120 which became a deemed assessment order in terms thereof. This was sought to be amended by the Department as regards proration of expenditures for the PTR and non-PTR income, i.e., a matter which related to clause (ab) of subsection (1) of s. 67. The taxpayer had divided the relevant expenditures on the basis of gross profit ratio. The taxpayer's position was that in the facts and circumstances of the

case this was a reasonable basis for purposes of the subsection. The Department however contended that Rule 13 had to be applied and as required by clause (a) of sub-rule (3) the proration had to be done on the basis of sales (i.e., gross receipts) in terms of the formula as therein stated. The deemed assessment order was amended accordingly. A departmental appeal against this decision failed but the taxpayer succeeded on further appeal to the Appellate Tribunal. The Department approached the learned High Court in tax reference and, as noted, by means of the impugned judgment the decision of the learned Tribunal was reversed.

5. Learned counsel for the taxpayer contended that in applying Rule 13 the Department had taken into account all expenditures including those for the manufacture of the locally sourced beverages. It was submitted that such expenditures related solely to the non-PTR income and had nothing to do with the PTR income where no manufacturing expenditures were at all incurred, the goods being sold in exactly the form as imported. On such basis it was contended that the basis for proration in terms of Rule 13 was incorrect and that adopted by the taxpayer, i.e., on gross profit basis, was reasonable within the meaning of that expression as used in s. 67(1) and that the learned High Court had erred in coming to the contrary conclusion. Learned counsel for the Department on the other hand contended that the learned High Court had reached the correct conclusion. It was prayed that the leave petition be dismissed.

6. We have heard learned counsel as above and considered the record and the relevant provisions. Rule 13 has clearly been framed with reference to subsection (2) of s. 67. The principal question is how the said rule interacts with the requirements of subsection (1), which lays down the principle to be adopted for purposes of proration. Now, subsection (1) provides that expenditures “shall” be apportioned “on *any* reasonable basis”. The factors that have to be taken into account when so apportioning are set out in the concluding part of the subsection: “the relative nature and size of the activities to which the amount relates”. The question is whether whatever is set down by the

Central (now Federal) Board of Revenue (herein after the “Board”) in exercise of the statutory power conferred by subsection (2) is to have an exclusive or overriding effect over the principle set out in subsection (1)? The answer has to be in the negative. A rule making power (being subordinate legislation) has to be exercised consistently with the requirements of the principal enactment, being primary legislation, and not in derogation from or negation of or inconsistently therewith. This is a well settled principle requiring no elaboration. It is pertinent to note that the rule making power conferred by subsection (2) is discretionary and not mandatory; the Board “may” make rules for purposes of apportionment. The parent provision, i.e., subsection (1), on the other hand uses the mandatory “shall”. The approach taken by the Department (and accepted by the learned High Court) would in effect mean that as long as the rule making power under subsection (2) is not exercised then it is open for any reasonable basis to be adopted in the facts and circumstances of a case (in conformity with the factors set out at the tail end of subsection (1)). However, as soon as the statutory power is exercised that becomes the only basis for proration in the facts and circumstances of all cases within its scope. With respect, such an approach is impermissible. The result would in effect be that “any” would mean precisely that as long as the rule making power is not exercised but immediately and automatically collapse into “only” when it is. There is no warrant in either s. 67 or the well known principles applicable to the interpretation of statutes (with particular reference to subordinate legislation) that could lead to such a conclusion or warrant such a result. “Any” means precisely that, both before and after the exercise of rule making power by the Board. Furthermore, this has to be read keeping in mind the mandatory “shall” preceding it. In other words, it remains mandatory at all times to use “any” reasonable basis while apportioning expenditures. At the same time, it must be remembered that a statutory power is specifically conferred on the Board by subsection (2) for purposes of s. 67. Rule 13 has not been framed solely in exercise of the general rule making power conferred by s. 237. It is a specific grant. The reference to s. 237 in subsection (2) must be understood as meaning that the

procedural requirements of that provision have to be met when framing the appropriate rules. Thus, for example, the requirement of prior publication laid down in subsection (3) of s. 237 must be adhered to (subject to the exception of first publication) and the principle of prospectivity articulated in subsection (4) must also be taken into account.

7. The question raised, i.e., how is Rule 13 to interact with subsection (1), is to be answered in the foregoing framework. In our view the correct approach is as follows. In the first instance, it must be carefully considered whether Rule 13 at all applies, on its own terms, to the facts and circumstances of the case. If so, then it is to be regarded as a reasonable basis for apportionment of expenditures. If not then it cannot, *ipso facto*, be regarded as a reasonable basis within the meaning of subsection (1). However, even if it is found to apply it cannot be regarded as "the" reasonable basis, i.e., to the exclusion of all others. "Any" cannot transmute into "only". It would be open to the taxpayer to show that the basis of apportionment actually applied by it was also reasonable in the facts and circumstances of the case. If so, then that basis is to apply in terms, and for the purposes, of s. 67. It is in this way that the rule making power under subsection (2) that "may" be exercised is reconciled with the mandatory requirement of subsection (1) that "any" reasonable basis be used. It is important to keep in mind that it is not necessary for the taxpayer to show that the basis laid down in Rule 13 would be unreasonable in the facts and circumstances of the case (when it would in any case not apply), or that the basis actually applied by it is more reasonable. It may be that each is a reasonable basis for apportionment, i.e., both may be regarded as "evenly" placed. As long as that is so, that suffices for the application of the basis actually adopted by the taxpayer. In other words, the basis laid down in a rule framed by the Board under subsection (2) cannot be given primacy over the basis adopted by the taxpayer as long as both are, each in its own terms, a reasonable basis for apportionment. Obviously, if one or the other is not a reasonable basis within the meaning of subsection (1) that is enough to displace it in favor of the other. However, the use of the mandatory

"shall" means that simply because the Board has exercised its rule making power that cannot, in and of itself and for that reason alone, override or displace the basis actually adopted by the taxpayer.

8. It is also important to keep in mind that the question now before the Court arose in the context of the Department seeking to amend the deemed assessment order. This can be done, as presently relevant, in terms of s. 122, subsection (5) of which lays down the grounds for amendment. These are as follows (and so stood for tax year 2003):

> "(i) any income chargeable to tax has escaped assessment; or
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> (ii) total income has been under-assessed, or assessed at too low a rate, or has been the subject of excessive relief or refund; or
>
> (iii) any amount under a head of income has been mis-classified."

Of these grounds it would seem that in the facts and circumstances of the present case only ground (i) or the first part of ground (ii) could be applicable, i.e., that a failure to apply Rule 13 led to income chargeable to tax escaping assessment or for the total income to be under-assessed. In our view, as long as "any" reasonable basis is adopted for purposes of proration of expenditures as mandatorily required by s. 67(1), even if it is not the one laid down in Rule 13, it cannot be said either that income has escaped assessment or total income has been under-assessed within the meaning of the grounds set out in s. 122(5). It must be remembered that it is a well established principle of income tax law that a taxpayer is entitled to so arrange his affairs as minimizes his tax liability, subject to any applicable exceptions or impermissibilities. In the present context the correct appreciation of the mandatory nature of s. 67(1) can be regarded as a statutory expression of this principle. As long as "any" reasonable basis is used for the proration of expenditures the basis applied by the taxpayer cannot be defeated or denied simply for the reason that applying Rule 13 would result in a larger or enhanced tax liability. Or, to invert what has just been said, it is impermissible to conclude that since the non-application of Rule 13 (and the

reasonable basis actually adopted by the taxpayer in its stead) results in a smaller tax burden that, in terms of s. 122(5), amounts to income chargeable to tax escaping assessment or leads to the total income being under-assessed. That would be to completely misconstrue and misapply both that provision and s. 67(1).

9. Turning now to consider the facts and circumstances of the case in the light of the foregoing analysis, it will be seen that clause (a) of sub-rule (3) of Rule 13 applies in the case of “common expenditures”. This is a defined term, and inter alia means such expenditure as is not “clearly” allocable to any particular class or classes of income. Obviously, any expenditure clearly so allocable falls outside the scope of the definition. The point, for present purposes, is reinforced by sub-rule (2) which provides that any expenditure incurred for a particular class or classes of income is to be regarded as so allocated. From this, it is clear that learned counsel for the petitioner was correct in submitting that the manufacturing and other such expenses incurred for the local production of beverages had to be allocated solely to the non-PTR income and had nothing to do with the PTR income. For such expenditure the question of proration did not arise. The order amending the deemed assessment shows that the Department, while applying the formula laid down in sub-rule (3), has taken “total admissible expenses” into account, which is incorrect in the facts and circumstances of the case. However, even if this were not so, and the Department had sought to apply the formula set out in sub-rule (3), i.e., allocated common expenditures on the basis of “gross receipts” or sales that would not, in our view, have altered the position. The reason is that even if such application of the sub-rule could be regarded as a reasonable basis for apportioning the relevant (common) expenditure that would not mean that the basis actually adopted by the taxpayer stood excluded, for the reasons set out above. In our view, given the nature of the exercise required (i.e., allocation between PTR and non-PTR income) and keeping in mind the relevant factors as applicable (i.e., the relative size and nature of the activities (local manufacture versus import) to which the expenditure related) the

basis actually adopted was a reasonable one. That sufficed for purposes of subsection (1) of s. 67. It follows that the approach taken by the Department and upheld by the learned High Court is, with respect, not sustainable.

10. We may note that in coming to the conclusion that it did the learned High Court relied on an earlier decision of that Court reported as *Commissioner Inland Revenue v Monnoowal Textile Mills Ltd.* 2022 PTD 305. That decision had followed and applied a judgment of the Sindh High Court reported as *Commissioner Inland Revenue v Quality Textile Mills Ltd.* 2013 PTD 2095. Both decisions were concerned with the interplay and the applicability (or otherwise) of Rules 13 and 231 of the 2002 Rules. The latter rule related, as its marginal note attested, to the "[c]omputation of export profits and tax attributable to export sales". The present case is concerned with PTR income on the importation of goods. The cited case law does not therefore, with respect, have any bearing on the facts and circumstances of the case at hand.

11. Accordingly, this leave petition is converted into an appeal and the question posed in the beginning of the judgment is answered in the affirmative in the facts and circumstances of the case. Since that answer is in favor of the taxpayer and against the Department it follows that the appeal succeeds and is hereby allowed.

Judge

Judge

Judge

Announced in the Court on 12/11/2025 at Islamabad

Sd/-
Judge

Approved for reporting