JUDGMENT SHEET

ISLAMABAD HIGH COURT
ISLAMABAD

W.P. No. 3108/2011

SHABNAM ASHRAF.

Versus

DEPUTY COMMISSIONER & OTHERS.

Petitioner by:	Mr. Abdul Raheem Bhatti, Advocate.
Respondents by:	Mr. Saeed Ahmad Zaidi, Advocate.
Date of Hearing:	02.06.2020.

LUBNA SALEEM PERVEZ: Through this writ petition, the petitioner has challenged the show cause notice dated 13.09.2011, issued u/s 122(9) read with section 122(5) of the Income Tax Ordinance 2001, by Deputy Commissioner Inland Revenue *(the Respondent No. 1)*, notice dated 18.10.2011 issued by Commissioner Inland Revenue *(the Respondent No. 2)* intimating selection for audit and another notice dated 18.10.2011 issued by the Deputy Commissioner Inland Revenue *(the Respondent No. 1)* u/s 177 of the Income Tax Ordinance 2001, for the tax year 2010.

2. Facts of the case are that the Petitioner who runs a school under the name and style of Preparatory School Islamabad, declared Rs. 463,739/- as net business income from school and salary income as Rs. 600,000/- for the tax year, 2010. Respondent No. 1, after scrutiny of return and wealth statement confronted discrepancies through show cause notice dated 13.09.2011 u/s 122(9) read with section 122(5) of the Income Tax Ordinance 2001. The said notice when not responded to by the Petitioner, the Respondent No. 2 selected the case for total audit u/s 177 by intimating the discrepancies in the income tax return for the tax year 2010 through notice dated 18.10.2011 and on the same date Respondent No. 1 also issued notice for audit proceedings u/s 177 of the Income Tax Ordinance 2001. The petitioner, in response to notice dated 13.09.2011, through her tax

adviser, revised her return by incorporating income from Behbood Savings Certificate. Record revealed that the return for the tax year 2010 has been revised twice by the Petitioner on account of confronted discrepancies. The Petitioner, instead of joining the audit proceedings and filing reply to the notice u/s 177 of the Income Tax Ordinance 2001, challenged the jurisdiction and powers of Respondent No.2, for selection of return for audit u/s 177 of the Income Tax Ordinance, 2001 and subsequent proceedings vide notices dated 18.10.2011 by filing instant petition.

3. Learned Counsel for the Petitioner argued that the show cause notice dated 13.09.2011 u/s 122(9) read with Section 122(5) and the notices dated 18.10.2011 for selection and for proceedings u/s 177 of the Income Tax Ordinance, 2001 are illegal and have been issued with malafide intentions; that by operation of law, the income tax return for the tax year 2010 attained finality; that notice u/s 122(5) can only be issued on the basis of definite information acquired by the Commissioner from audit or otherwise; that the Respondent had no such definite information to commence proceedings for amendment of assessment u/s 122(5) through show cause notice dated 13.09.2011; that the Respondents acted illegally and malafidely by issuing notices dated 18.10.2011 u/s 177 of the Ordinance 2001 as through these notices the Respondent wanted to fish out material to equip her with definite information; that simultaneous issuance of notices dated 18.10.2011 for selection of case for audit by Respondent No. 2 and production of documents by Respondent No. 1 is a malafide and illegal act in league with Respondent No. 3. Learned counsel, in this regard, placed reliance on the case law reported as *Rana Muhamad Sarwar vs. Government of Punjab (1990 SCMR 999) & M/s. Pakistan Synthetics Limited vs. Waqar Ahmed & Others (2011 SCMR 11).* For initiating proceedings under section 122(5) of the Income Tax Ordinance, 2001, learned Counsel submitted that Respondent No. 1 is not in possession of definite information and in this regard placed reliance on the judgment titled *Commissioner Inland Revenue Versus Khan CNG and Filling Station* reported as *(2013 PTD 884).* Learned Counsel regarding initiation of proceedings for audit u/s 177 submitted that selection of petitioner's case for the tax year 2010 for audit is based on malafide intent and illegal as both proceedings cannot be conducted simultaneously; that no show cause notice has been served before selection of case

for audit. Learned counsel in support of his contention placed reliance on case law reported as *Roots Montessori and High School, Rawalpindi Versus Commissioner of Income Tax (Audit), Rawalpindi (2010 PTD 395) & Pakistan Telecommunication Company Ltd. Versus Federation of Pakistan (2016 PTD 1484)* and submitted that the judgments cited above are binding on this court**.** Learned counsel also relied on the observations recorded by the Hon'ble Supreme Court vide its judgment re: *Commissioner Inland Revenue vs. M/s. Allah Din Steel and Rollong Mills (2018 SCMR 1328)* whereby time frame for completion of audit in the policy guidelines have been discussed. Learned counsel contended that after Finance Act, 2010, power of selection of cases for audit is no more available with the Commissioner and transferred to the Federal Board of Revenue under newly incorporated section 214-C of Finance Act, 2010 and that sub-section (4) & (5) of Section 177 were no more on statute book when the impugned notices dated 18.10.2011 were issued and further that selection of case for audit is time barred u/s 120 of the Ordinance 2001. Reliance in this regard was placed on Northern Bottling Company (Pvt.) Ltd. Industrial Estate, Peshawar versus Federation of Pakistan *(2013 PTD 1552*). Learned counsel lastly submitted that the selection of petitioner's case for audit is violative of article 2A, 4, 18, 23 & 25 of the Constitution and in support referred case law reported as *Chenone Stores Ltd. through Executive Director (Finance Accounts) versus Federal Board of Revenue through Chairman (2012 PTD 1815) and* Lala Musa Flour and General Mills, Gujrat Versus Chairman, Federal Board of Revenue, Islamabad *(2013 PTD 391).*

4. Conversely, learned Counsel for the Respondents contended that in case re: Nestle Pakistan Ltd. vs Federal Board of Revenue [2017 PTD 686 (Lahore)] decided on 9-1-2017, the Hon'ble Lahore High Court has examined in detail the extent of Tax Department's powers to carry out audit and has held that audit was a fundamental and necessary approach to address non-compliance issues and that scope of audit was beyond mere verification of correct reporting by the taxpayers. Learned counsel further submitted that another objective was to create a deterrence against tax evasion; that judgment was challenged before a Division Bench of the said Court through ICA No. 338 of 2017 in the same case, which was decided in favor of Revenue vide judgment dated 8-7-2017; subsequently, the Hon'ble Supreme Court also maintained the judgment of Single Bench of the Lahore High Court with certain observations regarding time for completion of audit proceedings

etc. and dismissed the CPLAs filed by taxpayers as well as the Tax Department vide its judgment in C.P. No. 2370-L etc. of 2018. Learned counsel further contended that a writ petition is not maintainable against a show cause notice and relied on Nestle's case supra wherein it has been held, inter alia, *that a remedy by way of representation under section 7 of the FBR Act, 2007 was available to the taxpayer aggrieved of selection of his case for audit*. Learned counsel argued that in view of availability of alternate remedy, instant petition is not maintainable. Learned counsel while referring the above said judgment of the Hon'ble Lahore High Court, Lahore further submitted that as held therein, State has a right to audit and correspondingly it is the duty of the taxpayer to make correct declarations and comply with the statutory commands under three Federal Taxing/Revenue Statutes; that selection of case for and conduct of audit is not ex facie detrimental to the interest of taxpayer; that the petition is not maintainable as no legal right or entitlement has been infringed. Arguing on the facts and merits of the case he submitted that show cause notice dated 13.09.2011 was issued as there was glaring discrepancies of concealing interest income from Behbood Savings Certificates and other un-reconciled amounts declared in the income tax return and wealth statement for the tax year 2010, as such, proceedings of section 122(5) read with section 122(9) were initiated to tax the concealed income of the Petitioner; that the show cause notice dated 13.09.2011 has been issued for valid reasons as in response to this show cause notice, the Petitioner also revised her return twice to incorporate undeclared income; that revision of return is an admission of concealment; that facts and circumstances necessitated total audit of the petitioner's return thus her case was selected by the Commissioner exercising powers u/s 177 of the Income Tax Ordinance 2001 and consequent upon the selection, Respondent No. 1 proceeded to conduct audit in accordance with law by requisitioning the documents and record, therefore, no miscarriage of justice is caused so as to invoke the writ jurisdiction; that section 120(1A) empowers the Commissioner to select a person for audit of income tax affairs; that the petitioner has been intimated for audit of income tax affairs for the tax year 2010 vide notice dated 18.10.2011 for the reasons contained therein; that the petitioner has neither been discriminated nor there is any illegality or malafide involved while proceeding against her and adequate opportunity was provided to authenticate her claim in the income tax return. Learned counsel lastly contended that the petition is

liable to be dismissed as petitioner approached the court with unclean hands and reliance was placed on the case law reported as *Justice Khurshid Anwar Bhinder Versus Federation of Pakistan (2010 PLD 483 SC) & Tasnim Jalal versus Deputy Director, A.N.F. (2010 SCMR 72)*

5. Arguments heard, record perused with the able assistance of learned counsel for the parties.

6. The Petitioner through this petition has challenged the notices issued by the income tax authorities for initiating proceedings against her. First notice was issued by Respondent No. 1 for proceedings under section 122(5) of the Income Tax Ordinance 2001 on 13.09.2011, on the grounds that the petitioner while declaring the business income has shown business expenses which constitute 99% of the gross income from school and that the petitioner had declared investment in Behbood Savings Certificates but has not declared income therefrom, further huge amounts of loan were reflecting in the wealth statement for the tax year 2010 which required explanation. Record revealed that no compliance was made by the Petitioner on the given date but subsequently she revised income tax return twice by declaring the interest from investment in Behbood Savings Certificates. Record further revealed that instead of continuing proceedings u/s 122(5), Respondent No.2 initiated audit proceedings on the basis of same discrepancies to check and eliminate possible risk to the revenue and, therefore, exercising powers under section 177, notice dated 18.10.2011 was issued to the Petitioner whereby reasons for selecting the case for audit for the tax year 2010 were communicated and audit proceedings were also started vide a separate notice of the same date by Respondent No. 1. The Petitioner, instead of joining the audit proceedings preferred to file the present writ petition and challenged above said notices alleging illegality and malafide on the part of the respondents. Careful examination of the record revealed that after initiation of audit proceedings u/s 177 on 18.10.2011 no further notice u/s 122(5) was served on the Petitioner, thus the allegation of conducting simultaneous proceedings u/s 122(5) and 177 against the petitioner has no force, hence, rejected. It has been observed that the Petitioner, has alleged malafide against the Respondents perhaps on the view that the proceedings against her is the outcome of personal vendetta, grudge or vindictiveness, however, neither the record appended with the petition nor any document or convincing material has

been put forth during the hearing of the case. The income tax authorities, being the collectors of tax/revenue, have a responsibility to check the possible revenue leakages and safeguard the interest of the exchequer in accordance with law and for that purpose the prescribed mode of communication is through notices for various reasons and under various Sections, which may upset the taxpayers though and create disturbance, but it is not proper to level allegation of malafide, personal bias and vengeance of the authority for issuing show cause notice in every case and file petition before the High Court on such unsupported assertions. In the present case, it is apparent from the record that proceedings u/s 122(5) have been initiated on the basis of non-declaration of interest income by the petitioner and the revision of return is the admission of filing incorrect return by the Petitioner. This incorrect return, in view of the Respondents, required further verification, hence, action as prescribed u/s 177 was commenced, as such, the actions of the Respondents do not contain element of malafide, personal grudge or vendetta.

7. The petitioner has also challenged the jurisdiction of Respondent No. 2 for exercising powers to select its case for audit u/s 177 and has relied on various judgments and case laws in this regard. Learned Counsel has referred the amendment made, vide Finance Act, 2010, in section 177 and insertion of section 214C in the Income Tax Ordinance, 2001 and submitted that after these amendments, the Commissioner has no powers to select case for audit as the return for audit can only be selected through random or parametric ballot only. Points agitated by the learned counsel have been answered by the Hon'ble Lahore High Court in its judgment re: ***Federal Board of Revenue vs. M/S. Chenone Stores Ltd (2018 PTD 208).*** It is pertinent to mention that M/s Chenone Stores Ltd filed a Writ Petition No. 393 of 2012 before the Hon'ble High Court to challenge notices for audit issued by the Commissioner u/s 177 of the Income Tax Ordinance, 2001; Section 25 of the Sales Tax Act, 1990 and Section 46 of the Federal Excise Act, 2005, and the Hon'ble Court, vide judgment in the case titled ***M/S. Chenone Stores Ltd vs. Federal Board of Revenue*** reported as ***(2012 PTD 1815)*** was pleased to declare the impugned notices as illegal and without lawful authority, by striking down first proviso to the section 177 (1). This decision which decision was challenged by the FBR through intra court appeals (ICAs), whereby, the Learned Division Bench, vide judgment reported as ***(2018 PTD 208)*** referred above, was pleased to hold that *the Explanations inserted, in the Federal Taxing Statutes, through Finance*

Act, 2013, have effectively obliterated binding force of the judgment in Chenone Stores' Case. The relevant paras are also reproduced below, for ready reference:-

> *"Learned counsel for the taxpayers argued that scheme of law has been changed after amendments through Finance Act, 2010, therefore, only Federal Board of Revenue ("FBR") can and Commissioner cannot select for audit. On insertion of Explanations; it is argued first; that these shall not have retrospective effect and secondly that the Explanations have not removed the defects pointed out in Chenone Stores' judgment, therefore, are ineffective.*
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> *9. …… Learned Single Bench of this Court through judgment in Messrs Syed Bhais (Pvt.) Ltd. through Director v. Central Board of Revenue, Islamabad through Chairman and another (2007 PTD 239) dismissed the petitions, relying upon the judgment in Media Network's Case, supra, besides referring to the section 177(3), ibid, to hold that publication of criteria before filing of returns was not mandatory; The amended provisions of section 177 were declared to have two parts; first, related to selection on the criteria to be laid down by the Board and the second was dealing with selection by Commissioner directly under subsection (4) of section 177; The words "in addition to" and "may also", used in this subsection, were emphasized. It was held that criteria before selection was relevant only if so provided by CBR. It was clarified that in Fatima Sharif's Case direction was for Commissioner to disclose reasons in the notices for selection and not before filing of returns.*
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> *10. Subsequent notices of selection for audit, by Commissioner, under the amended section 177, ibid, were again challenged before this Court and the petitions were decided by two learned Single Benches through judgments at variance. First judgment was delivered in MohsinRaza v. Chairman, Federal Board of Revenue and others (2009 PTD 1507), accepting the petitions, mainly, for the reason that Commissioner could not invoke the provisions of section 177(4) in absence of criteria to be laid down by CBR under section 177(1), besides holding that Commissioner had to form an opinion that income declared under section 120 was incorrect. The other judgment was delivered subsequently in MessrsSadarAnjuman-e-Ahmedia through General Attorney v. Commissioner of Income Tax (Audit Division), Faisalabad and 3 others (2010 PTD 571), wherein it was held that powers of Commissioner under section 177(4) were independent of section 177(1) & (2); Fatima Sharif's Case was relied upon, besides putting emphasis on the words "in addition to" and "also", used in the section 177(4).*
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> *11. It is important to note that the judgment in Syed Bhais' Case, supra, was not set aside, therefore, holds the field, in light of law laid down by Apex Court in Fatima Sharif and Media Network's Cases.*
> *……The law holding field, till this stage i.e. before amendments through Finance Act, 2010, can conclusively be summarised as under:*
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> *i) Guidelines (Selection criteria) are not required to be disclosed before filing of returns under Self-assessment; (Media Network's Case)*
> *ii) Commissioner is bound to disclose the reasons/criteria in the notice if selecting the cases for audit independently; (Fatima Sharif's Case)*
> *iii) Commissioner is bound to follow the criteria of selection, if laid down by the FBR; (Syed Bhai's Case) and*
> *iv) Commissioner has independent power to select for audit under section 177(4) and his power to select on the criteria given by FBR is different. (Syed Bhai's Case)*
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> *12. Through Finance Act, 2010; FBR has been given powers, for the*

first time under the Ordinance of 2001, to select for audit by inserting section 214C in it. Commissioner is entrusted with power to call for record and conduct audit, by substituting subsection (1) and omitting subsection (4) from section 177. This power is qualified through first proviso by stipulating that the record shall be called after recording reasons and the reasons shall be communicated to the taxpayer. The first proviso is not applicable, under subsection (2) of section 214C, if the selection is made by FBR.

14. Learned Single Bench examined various provisions of the Ordinance of 2001 to hold that selection for audit is a neutral, impartial and equitable function, therefore, use of audit provision for investigation, would give the department a license to carry out a roving inquiry into the affairs of any taxpayer and to fish for defaults. It was held that 'Legislative policy of the Ordinance cannot equip the Commissioner with naked power to pick and choose according to his whims and wishes.

16. Through judgment in Kohinoor Sugar Mills, the Explanations were held to be declaratory; having clarified that Commissioner has independent power to select for audit, under section 177, in presence of FBR's power under section 214C. It was held that legislature was competent to clarify its intent by inserting the Explanations. As the notices issued after 01.07.2010 were carrying reasons for calling record to conduct audit, therefore, were declared to have validly issued by the Commissioner. Reliance was placed upon the judgments in Syed Bhais' and Fatima Sharif's Cases, supra. It was observed that provisions of section 177 are machinery in nature, therefore, are effective retrospectively. It was opined that language of section 177 clearly confers a power on Commissioner to call for any record or documents including books of accounts, maintained under the Ordinance, for conducting audit of income tax affairs.

22. In light of the law discussed above; now we revert to examine the effect of the Explanations, inserted in the Federal Taxing Statues through Finance Act, 2013, in consequence of the Chenone Stores' judgment:
…… After the clarification and declaration of Legislative Policy that Commissioner's power to select and conduct audit are independent of FBR's power to select for audit, the binding force of the judgment in Chenone Stores' Case has effectively been obliterated.

23. Purpose of audit has been discussed in number of cases by the Superior Courts and is held that after extending the facility of self-assessment, to audit a taxpayer's declaration in the return filed under it, is the right of Tax Administrator. It is discernable from the law laid down by August Supreme Court in Media Network and Faitma Sharif Cases that selection and conduct of audit, being administrative in nature, is not detrimental to the interest of a taxpayer. State, through FBR, has a right to audit, against taxpayer's corresponding duty to make correct declarations and comply with the statutory commands under three Federal Taxing Statutes. Findings in Chenone Stores' judgment that 'use of audit provisions for investigation, would give the department a license to carry out a roving inquiry into the affairs of any taxpayer and to fish for defaults' is against the basic concept of audit. The concept of audit, as being internationally accepted, has traveled beyond mere verification of correct reporting by taxpayer and raising revenue. Besides creating deterrence by punishing the defaulting taxpayer, an effective audit program pinpoints non-compliant trends; defects in system, ambiguities in practice and the law. On the basis of gathered information and intelligence from an effective audit, and its publication, future Tax Administration can be reshaped; necessary steps can be taken to suggest

> *curative legislation and clarifications of ambiguous practices. The results achieved from effective audit program may help to improve risk management techniques and determine 'Parameters' for future selection of high risk cases for audit.*
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> *The argument by Mr. MansoorUsmanAwan Advocate, that the Explanations shall have retrospective effect till 01.07.2010, is found correct on the face of it because the provisions of law being interpreted, clarified and so declared through the Explanations have attained current shape after amendment through Finance Act, 2010 having effect from the date ibid. Yet it does not mean that Commissioner did not have such power before these amendments. The law, as discussed above, had been settled till 30.06.2010 i.e., Commissioner's power to select for audit as per the criteria given, under the then section 177(1), by FBR was different from his power to select independently and conduct audit under the section 177(4) as these subsections were existing before amendments through Finance Act, 2010.*
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> *25. Appeals filed by department (listed in Annex-A) are allowed to the extent and in the manner as discussed above, by declaring that the Explanations inserted, in the Federal Taxing Statutes, through Finance Act, 2013, have effectively obliterated binding force of the judgment in Chenone Stores' Case.".*

8. The above judgment has resolved all the issues and controversies regarding powers of the Commissioners to select cases for audit and it has been settled that the Commissioner has always possessed these powers independently even prior to the amendment made vide Finance Act, 2010.

9. Learned Counsel for the Petitioner has also relied on the judgment of Hon'ble Supreme Court in Allah Din's case (2018 SCMR 1328), however, this judgment is not applicable to the facts involved in the present petition as through the above judgment, the Apex Court has decided the issues regarding Audit Policy 2015/policy guidelines and time frame of completion of audit conducted by tax authorities, whereas, the present petition pertains to jurisdiction & power of Commissioner to select a case for audit, pertaining to tax year, 2010.

10. For the above said discussion, instant petition, being devoid of any merit, is accordingly **dismissed**.

(LUBNA SALEEM PERVEZ)
JUDGE

Announced in the Open Court on _____**.**

JUDGE

Approved for Reporting.