IN THE SUPREME COURT OF PAKISTAN
(Appellate Jurisdiction)

Present
Mr. Justice Umer Ata Bandial
Mr. Justice Munib Akhtar
Mr. Justice Sayyed Mazahar Ali Akhtar Naqvi

Civil Appeal No.647 of 2018
(On appeal from the judgment dated 16.6.2011 passed by the Peshawar High Court, Peshawar in WP No.602 of 2011)

The Commissioner Inland Revenue

...Appellant(s)

vs

The Secretary Revenue Division and others

...Respondent(s)

For the Appellant(s) (in both cases).	:	Mr. Ghulam Shoaib Jally, ASC Mr. Masud Akhtar, Chief Legal, FBR
Respondent No.3	:	Ex-Parte
For respondent No.4	:	Qazi Ghulam Dastegir, ASC
Date of hearing:		28.9.2020

JUDGMENT

Munib Akhtar, J.: This appeal arises out of the Income Tax Ordinance, 2001 ("2001 Ordinance"). The question in issue is whether, in the facts and circumstances of the case, the respondent taxpayer was entitled, for the relevant tax years, to the benefit of clause (126F) (since omitted) of Part I of the Second Schedule to the said Ordinance (herein after referred to as the "exemption clause"). The exemption clause had provided in material part as follows:

> "**(126F)** Profits and gains derived by a taxpayer located in the most affected and moderately affected areas of Khyber Pakhtunkhwa, FATA and PATA for a period of three years starting from the tax year 2010...."

2. The respondent-taxpayer is a franchisee of a mobile company, Mobilink, and has its business/outlet in District Nowshera. It is not disputed that District Nowshera was declared

to be a "moderately affected area" for purposes of the exemption clause during the relevant period. In respect of the business activities carried out by the taxpayer as franchisee (sales/services provided to customers), which were all at its business outlet, it was entitled to payment of commission by Mobilink. Ordinarily, in terms of s. 233 of the 2001 Ordinance, advance tax would be deducted by Mobilink (i.e., the franchisor) on the commission payments being made to the taxpayer (i.e. the franchisee). However, on account of the exemption clause the respondent contended that no such deduction ought to be made. It applied to the concerned Commissioner under s. 159 for a certificate of exemption in this regard. That was refused, which led to the respondent filing a writ petition in the High Court. By means of the impugned judgment the learned High Court concluded that the respondent was entitled to the benefit of the exemption clause and, allowing the petition, directed the concerned Commissioner to issue the exemption certificate. Against this decision, the department sought leave to appeal in this Court, which was granted vide order dated 18.5.2018 to consider whether, in the facts and circumstances of the case, the respondent was entitled in terms as held by the learned High Court keeping in mind, in particular, the judgment of the Court reported as *Husnain Cotex Limited v. Commissioner Inland Revenue* 2017 SCMR 822, 2017 PTD 1561 ("*Husnain Cotex*").

3. Learned counsel for the appellant-department submitted that the learned High Court had failed to properly appreciate the relevant provisions of the 2001 Ordinance. Referring to s. 233, learned counsel submitted that as provided in subsection (3) thereof, at the relevant time (i.e. for the tax years in question) the tax to be deducted in advance was treated as a final tax. Learned counsel then drew attention to, and relied on, s. 169, which sets out the effects and consequences of tax being collected or deducted as final tax. Referring to the various clauses of subsection (2) learned counsel relied, in particular, on clause (e) to submit that the result and effect of the impugned judgment would be that the respondent taxpayer would become entitled to a refund of the tax deducted by the franchisor. It was submitted that this would be contrary to law. Relying on *Husnain Cotex* learned counsel further

submitted that the impugned judgment (though of course delivered many years before the former) was inconsistent with the law as laid down by this Court and hence was liable to be set aside. Learned counsel for the respondent-taxpayer on the other hand fully supported the impugned judgment and submitted that the respondent came within the scope of the exemption clause and that this entitlement could not be denied by reference to s. 169. Learned counsel submitted that the exemption certificate had been wrongly refused, which error had been corrected by the learned High Court. It was prayed that the appeal be dismissed.

4. After hearing learned counsel for the parties, and considering the relevant provisions and in particular the judgment in *Husnain Cotex*, we concluded that the appeal could not succeed. As noted, there is no dispute that the place of business of the respondent was located in a "moderately affected area" within the meaning of the exemption clause. No doubt the commission paid by the franchisor was from, and in, an area outside the areas identified in the exemption clause, but equally there can be no doubt that the business activities were carried out within such an area. It seemed to us that the profits and gains made by the respondent therefore arose therein. Accordingly (and putting to one side for the moment the effect, if any, of s. 169), it would appear to be the case that the respondent was entitled to the benefit of the exemption clause. However, we now need to consider whether there is anything in *Husnain Cotex* that would lead to a different conclusion.

5. The facts of the petitioner-taxpayers (more than one case being decided by a common decision) are set out in para 2 (pg. 825):

> "[The petitioner-taxpayers]… have their business establishments either in Lahore or Multan. As they derive income from executing construction contracts, their business activity, by virtue of sections 153(1)(c) and 153(3) read with section 169(b) of the Ordinance falls within the domain of 'final tax regime'. Hence the amount deducted at the rate specified in the First Schedule of the Ordinance from the payments made to them towards fulfillment of their contractual obligations are to be treated as their final tax liability. Accordingly, the petitioners submitted their income tax statements… disclosing the deductions made from the payments received against their respective

> contracts performed in the affected areas. Later it occurred to the petitioners that they were entitled to claim exemption on such payments in terms of Clause 126F, so they applied to the Commissioner for refund of the amount deducted towards their income tax liability. They initially succeeded in obtaining refund, however, the Additional Commissioner, Inland Revenue issued show cause notices to the petitioners under section 122(5A) of the Ordinance, proposing to disallow the exemption that was allowed earlier.... After hearing the matter, the Additional Commissioner held that as the petitioners fall within the domain of 'final tax regime' and not under 'normal tax regime', the exemption granted under Clause 126F was not intended for them. This decision was challenged in appeal.... After his decision in appeal, the aggrieved party assailed the appellate order before the Appellate Tribunal, Inland Revenue, which held that the petitioners were entitled for exemption. The tax department then filed References before the Lahore High Court which vide impugned judgments reversed the findings of the Tribunal after holding that the petitioners fall within the domain of 'final tax regime' whereas the term 'profits and gains' occurring in Clause 126F was relatable to such taxpayers only who fall within the domain of 'normal tax regime', hence not entitled to claim exemption. Feeling aggrieved by such decision the petitioners have preferred these petitions for leave to appeal."

After referring to the relevant statutory provisions, as well as Circular No.14 of 2011 dated 6.10.2011 ("Circular 14") that had been issued by the department to provide clarification with regard to the exemption clause, it was held as follows (pg. 828; emphasis supplied):

> "7. A person who was carrying on business in the affected areas but was unable to sell his goods or services to the extent he used to in normal business environment is the person who can only be described as an affectee of the adverse business environment. It was thus the adverse business environment which directly impacted his business with the result that his profits and gains diminished. The whole stimulus behind the tax exemption granted in 2010 under Clause 126F on the face of it was that sometime in the past the businesses located in the affected areas could not make profits on account of adverse business environment that was being experienced there. So it was purely an external factor that diminished the capacity of the businesses to make profits and gains that was germane in granting tax exemption under Clause 126F. Hence exemption in question was intended for such taxpayers only. These taxpayers could only be the ones who fall under the 'normal tax regime'. As to the taxpayers who fall under the 'final tax regime', they face no such situation. Firstly, they are not located in the affected areas. They only went to the affected areas when they succeeded in securing contracts, which in itself created business opportunity for them, adverse business environment notwithstanding their business activity starts only when they secure contracts. It can very well be imagined that before he submits his bid, he

> estimates the component of all costs that he is to incur towards the fulfillment of his contractual obligation. To cost he adds his margin of profit. He then adds the income tax liability at the rate specified in the First Schedule to the Ordinance. Where the contract is awarded to be performed in the areas affected by adverse business environment, the same has no impact on contractor's margin of profit which he has already incorporated in the contract price. The contractor is thus not affected by any external factor that is not conducive for doing good business. So the business environment of the area where contract is to be performed doesn't have any correlation with contractor's profit and gains. They therefore, cannot equate themselves with those taxpayers falling under the domain of 'normal tax regime', whose businesses being located in affected areas suffered financially on account of adverse business environment. *While determining the scope of exemption granted under Clause 126F, one should not lose sight of the fact that the precise reason for granting tax relief under Clause 126F was to ameliorate the financial conditions of certain taxpayers who were real affectees of business environment that had affected their capacity to make profits and gains from their businesses*. To extend the benefit of this exemption to the other category of taxpayers who did not even exist in the affected areas before succeeding in obtaining contracts to be performed there could never have been envisioned by the Legislature while incorporating Clause 126F in the Ordinance. We are, therefore, of the considered opinion that in view of the distinction between the two categories of taxpayers discussed above, the taxpayers such as petitioners who fall under the domain of 'final tax regime' cannot claim exemption under Clause 126F. The case law relied upon by petitioners' counsel, therefore, has no application to the case in hand."

As regards the aforementioned Circular 14 (reproduced at pp. 826-7) it was held as follows (pg. 830):

> "8. As to the legal effect of the Circular No.14 of 2011, suffice is to state that it was issued with the intention to interpret Clause 126F in a manner so that the benefit of exemption is extended even to such taxpayers also who were located outside the affected areas but they partly did business in the affected areas. In our view this explanatory Circular does not depict the correct interpretation of the scope of Clause 126F as it traveled into altogether a different direction from what we have discussed hereinabove. It appears that ultimately better sense prevailed with the Federal Board of Revenue as we were informed by learned counsel for the department that Circular No.14 of 2011 was subsequently withdrawn vide letter dated 07.06.2013."

6. A perusal of *Husnain Cotex* shows, in our view, that rather than supporting the case of the department in the facts and circumstances of the present case, it is rather the case of the respondent-taxpayer that is made out. This position clearly emerges, in particular, from the portion that has been emphasized

in the extracts taken above. We may note that the term "located" as used in the exemption clause was considered in the context of various scenarios in para 3 of Circular 14, which was as follows:

> "3. The word "located" as used in Clause (126F) can possibly have more than one dimension. The relevant scenario[s] along with the corresponding exemption/taxable status are outlined below:-

Sr. No.	**Situation**	**Exemption/Taxability**
(i)	The taxpayer is located inside the affected and moderately affected areas (hereinafter 'the specified areas') and his business is also carried on inside the specified areas.	**Exempt**
(ii)	The taxpayer is located outside the specified areas but his business is carried on within the specified areas.	**Exempt**
(iii)	The taxpayer is located inside the specified areas, but his business is carried on outside the specified areas.	**Taxable**
(iv)	The taxpayer is located outside the specified areas, but his business is partly carried on inside the specified areas.	**Exempt** to the extent of the income attributable to the business operations carried on inside the specified areas.

It is clear that the facts and circumstances of the taxpayers in *Husnain Cotex* came within the scope of situations (ii) and/or (iv) and this was the basis on which they claimed exemption. However, this Court took a contrary view and held that the interpretation put by the department on the exemption clause was not correct. We fully agree. On the other hand, the case of the present respondent falls squarely within situation (i) of the aforementioned table. It is clear that the department itself regarded the income of such taxpayers as entitled to the benefit of the exemption clause. This scenario has been clearly confirmed in para 7 of the judgment in *Husnain Cotex*, where such persons have been described as the

"affectees" of the "adverse business environment" for whom the exemption clause was intended. In our view, the facts and circumstances of the respondent's case come within the scope of the exemption clause. We come to this view independently of what was said in Circular 14, and regardless of whether or not the department subsequently took a contrary view. We may also note that the sentence appearing in para 7, i.e., that "These taxpayers could only be the ones who fall under the 'normal tax regime'" was not, in our view, germane to the analysis and conclusions arrived at by the Court. In particular, it cannot be taken to mean that even those taxpayers who otherwise came squarely within the scope of situation (i) (i.e., the "affectees" of the "adverse business environment") had also (and only) to be those from whom tax was not being deducted as a final tax. That would create an anomalous situation by creating two classes both falling within the scope of the exemption clause in the facts and circumstances of their case, and yet the benefit thereof being extended only to the one and not the other. In our view, such a conclusion would not merely defeat the exemption clause but would also run against the tenor of *Husnain Cotex* when read as a whole. We may also note, with respect, that the decision in *Husnain Cotex* was a leave refusing order. It is now the jurisprudence of this Court that such orders do not constitute binding authority. Thus, on any view of the matter, the reliance placed by learned counsel for the department on certain portions of the judgment is, with respect, not correct.

7. Insofar as s. 169 is concerned, in our view, with respect, the reliance placed on the same by learned counsel for the appellant was also misconceived. In particular, clause (e) of subsection (2) thereof, which disallows the refund of any tax deducted unless it comes within the condition laid down therein, cannot obviously stand in the way of the respondent taxpayer in the facts and circumstances of the present case. This is so because the question of any "refund" payable to it arose entirely, and only, because of the failure and refusal of the Commissioner to grant the exemption certificate applied for and to which the respondent was entitled as a matter of law. Clearly, the department cannot take the benefit of its own failure to correctly apply and follow the law. It appears from the record that the respondent applied for the certificate in a

timely manner. The return of any money (incorrectly) deducted as advance tax would merely restore the position that, in law, existed all along. It would not be tantamount to a "refund" within the meaning of s. 169(2)(e). Furthermore, as already noted, to hold that the respondent was affected by s. 169 in the facts and circumstances of its case would be to entirely deny it the benefit of the exemption clause, which is clearly not warranted in law. Therefore, in our view s. 169 did not, and could not, stand in the way of the respondent enjoying the benefit of the exemption.

8. For all of the foregoing reasons, it was announced in Court at the conclusion of the hearing that the appeal stood dismissed.

Judge

Judge

Judge

Islamabad, the
28th September, 2020
*Nisar/**

Approved for reporting