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Tax Bulletin

March 2025

Tax

Foreword

This publication contains brief commentary on Circulars, SROs and decisions of the adjudicating authorities issued during February 2025.

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Income Tax Ordinance, 2001

A. Reported Decisions:

1. VALIDITY OF AUDIT NOTICES ISSUED WITH REFERENCE TO SECTION 214D OF THE INCOME TAX ORDINANCE, 2001

2025 PTD 267
SINDH HIGH COURT
M/S UNITED CARPETS LTD. THROUGH DIRECTOR

VS

PAKISTAN THROUGH SECRETARY (REVENUE DIVISION) EX-OFFICIO CHAIRMAN, FEDERAL BOARD OF REVENUE, ISLAMABAD AND 2 OTHERS

APPLICABLE SECTIONS: SECTIONS 118, 119, 122, 137, 177, 214A AND 214D OF THE INCOME TAX ORDINANCE, 2001 (THE ORDINANCE)

Brief Facts:

Taxpayer in the instant case received notices under sections 177 and 122 of the Ordinance read with section 214D of the Ordinance i.e. Automatic selection for audit, in respect of Tax Years 2015, 2016 and 2017. The taxpayer challenged the legality of the notices on the basis that section 214D was inserted through Finance Act 2015 and was subsequently omitted through Finance Act, 2018 and after its omission no further audit proceedings can continue. It was further contended that a vested right has accrued to the Petitioners after omission of the said section and, therefore, the impugned notices are without lawful authority. It was further contended that introduction of section 214-E of the Ordinance through Finance Supplementary Act, 2018 and omission of Section 214D, supports the case of the taxpayer and therefore, all these Petitions are to be allowed.

On the contrary, the Respondent argued that the taxpayer had neither submitted the returns timely nor deposited tax in the Government Treasury, hence, was liable for the selection of audit.

Decision:

The petition was dismissed by the Sindh High Court. It was held that the taxpayer was in default due to late filing of return and not paying taxes on time. Also, the defaults were made in the tax years when section 214D of the Ordinance was not omitted. Moreover, the notices were issued under section 177 and 122 of the Ordinance which were also valid at the time of issuance. The Court stated that referencing Section 214D in the notices did not imply jurisdiction under a repealed law. The Court concluded that there were no grounds to challenge the legality of the notices, resulting in the dismissal of all petitions and allowing the Respondents to continue with the audit process.

2. SOFTWARE LEASE PAYMENTS DEEMED AS BUSINESS PROFIT, NOT A ROYALTY
(2025) 131 TAX 135 (S.C. Pak)

REVIEW OF SUPREME COURT JUDGEMENT (2023 SCMR 1803) DATED SEPTEMBER 8, 2023
INTER QUEST INFORMATION SERVICES

VS

THE COMMISISONER OF INCOME TAX

APPLICABLE SECTIONS: SECTION 44 OF THE INCOME TAX ORDINANCE, 2001.

Brief Facts:

The Petitioner is a company incorporated in Netherlands and a non-resident for income tax purpose in Pakistan, entered into two agreements with Schlumberger Seaco, Inc., a company operated in Pakistan.

The Petitioner, in its return of income, declared receipts under the agreements as business profit and sought exemption from income tax in Pakistan. However, the department treated these receipts as a royalty under the Article 12 of the DTT

between Pakistan and Netherlands. The CIRA and ATIR concluded that the payments received by the petitioner fell within the definition of royalty and therefore liable to income tax in Pakistan.

The HC ruled in favour of the petitioner. The respondent appealed to SC where the judgement by majority allowed the appeal, setting aside the HC's judgement However, two judges dissented with the majority decision and dismissed the respondent's appeals and upheld the High Court's judgement.

The decision under review was previously made against the petitioner on following grounds:

- It would not really matter to the petitioner if, under Article 12 of the Convention, it had to pay income tax in Pakistan, because the petitioner could offset any income tax paid in Pakistan by claiming a tax adjustment in the Netherlands.
- The HC did not note that the petitioner had an alternative remedy under Article 24 of the Convention to present its case to the competent authority of its own country, the Netherlands, which, if agreed with the respondent's stance, could take up the matter with the competent authority of Pakistan.
- The petitioner did not explain and prove the nature of the receipts for which it claims tax exemption before the Officer, CIRA and ATIR. It was unwarranted for the HC to have delved into the nature of the receipts.
- The HC incorrectly assumed the applicability of the OECD Model Convention, as Article 12 of the Convention adheres to Article 12 of the UN Model Convention and not to Article 12 of the OECD Model Convention; and
- The full definition of "royalties" in paragraph 3(a) of Article 12 of the Convention included payments for "information concerning industrial, commercial, or scientific experience".

Decision:

SC, while reviewing its earlier decision, responded to the above grounds and upheld the judgement of HC as follows:

- The availability of a tax adjustment or an alternative remedy in the Netherlands did not justify the HC refusing to address the legal questions raised in the reference application.
- Under Article 199, the High Court may decline to exercise its jurisdiction if it finds that the petitioner has an alternate adequate remedy. However, it escaped notice of SC that a reference application is akin to an appeal and the reference jurisdiction is similar to appellate jurisdiction, as held by SC in M/s Squibb Pakistan v. CIT (2017 SCMR 1006).Therefore, neither a reference application can be dismissed, nor can the exercise of reference jurisdiction be declined, on the ground of availability of some alternate remedy.
- The ATIR, in its well-reasoned and considered orders, referred the following questions of law to the High Court:
    - Whether the ATIR was right in holding that receipts of the applicant [petitioner] from the leasing FLIC Tapes were not "business profits".
    - Whether the learned Appellate ATIR was right in holding that receipts of the Applicant [petitioner] from leasing FLIC Tapes were income from "Royalty" and were not business profits.

  It is self-evident from reading the above questions referred to the HC by the ATIR that the nature of the receipts was an admitted fact, and the questions referred were questions of law. Therefore, the observations made by SC in earlier decision, that it was unwarranted for the HC to have delved into the nature of the receipts, appear to have overlooked the said orders of the ATIR.

- The only material difference between the definitions of "royalties" in the UN MC and the OECD MC is that the former includes payments received as consideration "for the use of, or the right to use, industrial, commercial or scientific equipment" in its definition.

  However, since neither the Officer, the CIRA, the ATIR, nor the respondent before SC relied upon this clause of the definition of "royalties" as FLIC tapes containing computer software programs are admittedly not "equipment", this difference was immaterial to the decision of the case.

It was concluded that the receipts received by the petitioner for the lease of FLIC tapes containing computer software programs fall neither within the clause "information concerning industrial, commercial or scientific experience" nor within any other clause of the definition of "royalties". If a payment is in respect of the rights to use the copyrights in a program, (e.g. by reproducing it and distributing it) then such a payment would be considered as a royalty. Other payments, however, only give a user the right to operate the program, where a consumer pays for a copy of computer program to use, this is not royalty payment.

We hold that the ATIR was not correct, and the HC was correct, in determining that the receipts received by the petitioner for the lease of FLIC tapes containing computer software programs were not income from "royalties" but were "business profits", as claimed by the petitioner in its tax returns.

Sales Tax Act, 1990

A. Notifications:

1. S.R.O. 164(1)/2025 dated February 17, 2025

Through this notification, FBR has made amendments in the Sales Tax Rules, 2002 by introducing new measures to tackle violations in the issuance of unverified invoices by retailers, empowering authorities to seal business premises or retail stores of Tier-I retailers found in breach of the rules.

Key changes brought through amendments include:

Rule 150ZEO- Retailers may face penalties, including the sealing of their premises, if they issue unverified invoices (earlier the requirement was in case of issuance of 3 unverified invoices in a day and 5 unverified invoices in a week), do not enter offline invoices into the system within 24 hours, or disconnect from the FBR database for 48 hours, the business premises of the registered person may be sealed. Additionally, if the retailer's invoicing device fails to record sales during offline periods, the premises could also face closure.

Rule 150ZEQ - Procedure for de-sealing of business premises of integrated tier-1 retailers

A revised procedure for de-sealing business premises sealed under rule 150ZEO is established. This includes:

- the Commissioner Inland Revenue may Impose a penalty under section 33 of the Act;
- de-sealing order shall be issued within 24 hours post-penalty payment, provided outstanding audit demands are resolved and issues like software bugs are fixed and comply with all requirements set forth under Chapter XIV-AA of the Sales Tax Rules;
- the registered person may file appeal against the de-sealing order;
- The Commissioner IR must perform a software audit on all POS machines in the retailer's branches within three working days after de-sealing.
- The Commissioner will determine the exact amount of under-declared sales identified in the software audit and create a tax demand for the evaded amount.
- If the retailer does not make the required payment, de-sealing will occur after one month, with re-sealing of the business premises fifteen days later if default continues.

Rule 150ZER - The Commissioner IR shall impose a penalty by passing an order prescribed under serial No. 25A of section 33 of the Act.

B. Reported Decisions

1. DUE PROCESS MUST BE FOLLOWED BY THE DEPARTMENT BEFORE ISSUING BLACKLISTING ORDER AND INITIATING RECOVERY PROCEDINGS.

2025 PTD 292
APPELLATE TRIBUNAL INLAND REVENUE

MURTAZA A HASSAN

VS

THE COMMISSIONER INLAND REVENUE
Applicable provisions: 11 and 25 to the Sales Tax Act, 1990 (the Act)

Brief facts:

The appellant is a textile mill which faced suspension and subsequent blacklisting of its sales tax registration through the assessment order claiming the appellant was non-existent at the registered address and that the declared closing stock was missing. The Department issued order for blacklisting and after the black-listing the department initiated the recovery proceedings and passed an order under section 11(2) of the Sales Tax Act, 1990.

Being aggrieved, the appellant filed appeal before the Commissioner (Appeals) and contested these claims by providing evidence from two previous physical verifications that confirmed their existence at the registered address. The learned Commissioner (Appeal) annulled the order of the assessing officer confirming no sales tax demand is outstanding against the appellant for the period under question. However, with respect to the blacklisting order, the appellant challenged the same before the Appellate Tribunal with the argument that it lacked due process, jurisdiction, and was fundamentally flawed. The appellant further argued that the tax authorities failed to follow proper procedures under Sections 11(2) and 25 of the ST Act, before blacklisting the appellant and initiating recovery proceedings.

Decision:

The Appellate Tribunal decided the case in favour of the appellant and annulled the blacklisting order determining it was unjustified and affirming that due process was not observed.

The Tribunal determined that the tax authorities had acted prematurely by blacklisting without completing necessary adjudication or proving tax liability. The appeal was allowed, and the Tribunal ordered the reinstatement of the appellant's sales tax registration status, emphasizing the need to follow legal procedures in such cases to protect the rights of taxpayers.

2. JURISDICTION TO BE EXCERCISED BY KEEPING IN VIEW WHETHER EQUALLY EFFICACIOUS REMEDY IS AVAILABLE.

2025 TAX 191
LAHORE HIGH COURT

M/S. RELIANCE WEAVING MILLS LIMITED

VS

FEDERAL BOARD OF REVEUE

Applicable provisions: Section 47 and 48 of the ST Act.

Brief facts:

In the instant case, Reliance Weaving Mills Limited filed a constitutional petition against the Federal Board of Revenue (FBR) seeking the suspension of recovery notices issued by the tax department. These notices were related to a demand for sales tax raised through an Order in Original. The petitioner argued that recovery actions were initiated while a Sales Tax Reference challenging the legality of the tax assessment was still pending before the High Court. The petitioner contended that the issuance of the recovery notices was motivated by a grudge against the filing of the Sales Tax Reference. The notices mandated that the bank accounts of the petitioner be attached to facilitate the recovery of the sales tax dues.

Decision:

The Court concluded that the petition was not maintainable due to the availability of an alternate remedy, as the petitioner had already filed a reference application that was pending a hearing.

The Court emphasized that it is well-established principle that statutory provisions provide a hierarchy of appeals and remedies; therefore, relief under the constitutional jurisdiction was not appropriate if there was an equally effective legal avenue accessible to the petitioner. The Court discussed principles of fairness and the right to a fair trial, concluding that the correct procedural recourse for the petitioner was to expedite the hearing of their pending Sales Tax Reference rather than seek immediate relief via a constitutional petition.

Ultimately, the petitioner’s counsel indicated a desire to withdraw the petition to pursue the available legal remedies under the law, leading the Court to dispose of the case.

3. PENALTY COULD BE WAIVED IF THE RETAILER INTEGRATE WITH THE FBR SYSTEM BEFORE A FURTHER PENALTY APPLIED.

2025 TAX 215
ISLAMABAD HIGH COURT

THE COMMISSIONER INLAND REVENUE

VS

PRESIDENT'S SECRETARIATE (PUBLIC) AND OTHERS

Applicable provisions: Section 2(43A), 3, 33 and 150ZER of the Sales Tax Rules, 2006

Brief facts:

In the instant case, a notice was issued to a retailer classified as a Tier-1 entity under Section 2(43A) of the ST Rules, requiring him to install Point of Sales (POS) Software integrated with the Federal Board of Revenue's (FBR) computerized system as mandated by Section 3(9A) of the ST Rules. The retailer failed to comply with the requirement of the notice which led to a sealing order by the Chief Commissioner of Inland Revenue. Subsequently, the retailer requested de-sealing of his premises and paid the penalty amount under Section 33(24) of the ST Act.

Being aggrieved, the retailer filed a complaint with the Federal Tax Ombudsman (FTO) seeking a refund of the penalty amount, which was granted. The FTO directed the Commissioner of Inland Revenue (CIR) to refund the penalty within 30 days. The FBR's subsequent representation against this decision was denied by the President of Pakistan, which led the CIR to file a constitutional petition contesting the decisions of the FTO and the President.

Decision:

The Court upheld the orders issued by the FTO and the President of Pakistan, finding no jurisdictional error in their decisions.

The Court highlighted that, according to Section 33(25A) of the ST Act, if the retailer as a Tier-1 retailer, integrated his operations with the FBR's system before a penalty for a second default was imposed, then the penalty for the first default shall be waived. Since there was no evidence indicating that the retailer had not integrated his business after the initial penalty that could lead to the ground for imposing a second penalty.

As such, the Court dismissed the petition *in limine*, affirming the validity of the refund order against the CIR.

Sindh Sales Tax on Services Act, 2011

A. Notifications

1. No. SRB/3-4/06/2025 dated February 3, 2025

SRB has made further amendments to the previous notification No. SRB/3-4/43/2023 dated August 15, 2023 whereby exemption was granted from Sindh sales tax on certain taxable services provided or rendered to WAPDA for use in the construction and completion of Greater Bulk Water Supply Scheme of the K-IV Project (Phase-I) which was valid only till construction and completion phase of the aforesaid project.

Through this amending notification, the exemption provided through notification dated August 15, 2023 has been made effective retrospectively from July 15, 2021 subject to the condition that no refunds of any Sindh sales tax already paid by service providers or recipients, shall be allowed.

Punjab Sales Tax on Services Act, 2012

B. Reported Decision

1. THE COURT REFRAINED FROM MAKING A CONCLUSIVE RULING ON THE MERITS OF THE CASE BUT DIRECTED THE COMMISSIONER OF PRA TO TREAT THE WRIT PETITION AS A REPRESENTATION.

2025 PTD 255
LAHORE HIGH COURT

GULF CONSTRUCTION (PVT.) LIMITED
VS
GOVERNMENT OF PUNJAB

Applicable provisions: Section 25, 25(1)(a), 27 and 29(2) of the Punjab Sales Tax on Services Act, 2012

Brief facts:

The petition was filed under Article 199 of the Constitution of Islamic Republic of Pakistan, 1973, by Pak Gulf Construction (Private) Limited challenging the vires of order of the Commissioner PRA to compulsory register it in terms of Section 27 of the Punjab Sales Tax on Services Act, 2012 (the "Act").

Pak Gulf Construction (Pvt.) Limited is a company which operates a development project known as "Centaurus," located in Islamabad and includes a shopping mall, residential apartments, and a hotel. The company is registered for sales tax with the Federal Board of Revenue (FBR) due to its physical location in Islamabad and complies with the Islamabad Capital Territory (Tax on Services) Ordinance.

The petitioner contends that it is not required to register with the Punjab Revenue Authority (PRA) under Section 25 of the Punjab Sales Tax on Services Act, 2012. This section mandates registration for those providing taxable services from a place of business located in Punjab. The petitioner asserted that since all services are rendered in Islamabad, the PRA has no jurisdiction over the petitioner and therefore lacks the authority to enforce compulsory registration. The PRA, responding to the petitioner's claims, referenced Section 29(1) of the Act, which allows for the deregistration of persons who do not meet the registration requirements, suggesting that where the petitioner is not required to register, it could seek deregistration through the proper channels.

Decision:

The Court refrained from making a conclusive ruling on the merits of the case but directed the Commissioner of PRA to treat the writ petition as a representation.

The Court ordered that the Commissioner must decide the matter within four weeks, ensuring that all relevant parties, including the petitioner, are heard and that a reasoned decision is issued in accordance with Section 29(2) (i.e. De-Registration) of the Punjab Sales Tax on Services Act, 2012.

The Court also advised a stopgap arrangement, protecting the petitioner by restraining the PRA from taking any coercive actions against the petitioner until the representation is resolved.

The Court emphasized the importance of the statutory remedy under Section 29(2) of the Punjab Sales Tax on Services Act, 2012 for addressing disputes regarding registration.

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