Daily Tax News (DTN)

Huzaima & Ikram
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This issue contains:

Kind regards

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Unearthing and retrieving hidden assets

by
Huzaima Bukhari & Dr. Ikramul Haq

Rich individuals and their families have as much as $32 trillion of hidden financial assets in offshore tax havens, representing up to $280 billion in lost income tax revenues, according to a research released on 22 July 2012[1]. Estimating the extent of global private financial wealth held in offshore accounts—excluding non-financial assets such as real estate, gold, yachts and racehorses—the study puts the sum somewhere between $21 and $32 trillion. The research was carried out by James Henry, former chief economist at consultants McKinsey & Co for Tax Justice Network, which campaigns against tax havens. He used data from the World Bank, International Monetary Fund, United Nations and central banks[2].

The report also highlights the impact on the balance sheets of 139 developing countries of money held in tax havens by private elites, putting wealth beyond the reach of local tax authorities. The research estimates that since the 1970s, the richest citizens of these 139 countries had amassed $7.3 to $9.3 trillion of "unrecorded offshore wealth" by 2010. Private wealth held offshore represents "a huge black hole in the world economy", Mr. Henry concludes in his study[3].

The report is published amid growing public and political concern about tax avoidance and evasion. Many authorities, including in Germany, have even paid for information on alleged tax evaders stolen from banks. Mr. Henry has revealed that the super-rich move money around the globe through an "industrious bevy of professional enablers in private banking, legal, accounting and investment industries.

The lost tax revenues, implied in this report, are huge—large enough to make a significant difference to the finances of many countries. This study is good news from the perspective that the world has located a huge pile of financial wealth that might be repatriated to contribute to the solution of most pressing global economic problems. Many countries have already taken concrete steps to retrieve lost taxes by signing agreements with countries where hidden wealth is lying.

Pakistan can also take legal measures to bring back looted and untaxed money from abroad as has been done by many countries of the world. India has recently renegotiated existing tax treaty with the Swiss government, as has been done by other countries, to retrieve billions in taxes if not the entire funds. It has also signed agreements for exchange

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1 http://www.taxjustice.net/cms/upload/pdf/Private%20Banking%202012.pdf

2 http://www.taxjustice.net/cms/upload/pdf/Appendix_1_-_The_Pre_History_of_estimates.pdf

3 http://www.taxjustice.net/cms/upload/pdf/APPENDIX_II_--_Price_of_Offshore_Revisited.pdf

of information with many tax havens. Officially in Pakistan, the Zardari regime will never take any such step as his own looted wealth is lying abroad. The same is true for many other politicians, businessmen and high-ranking officials.

Unfortunately, private efforts to invoke extraordinary jurisdiction of Supreme Court to bring looted wealth and untaxed money have also failed. The Supreme Court declared the petitions filed by a few private parties as "non-maintainable". On this vital issue no suo muto action has been taken by Supreme Court, which has raised many eyebrows. Many allege that near and dear ones of some of the judges have also kept undeclared assets abroad and therefore there is complete silence on this issue from the Chief Justice of Pakistan. On the contrary, the Indian Supreme Court, in its historic decision of 4 July 2011 in the case of *Ram Jethmalani and Other v Union of India* reported as 2011 PTR 1933 (S.C. Ind), set up a 'Special Investigation Team' to *supervise the Government-led investigations* into black money of Indians lying abroad.

The decision, given by Indian Supreme Court in pursuance of a Writ Petition filed by Indian veteran leader Ram Jethmalani alleging *inaction by the Government on unearthing of unaccounted money,* has special significance for Pakistan. The apathy of rulers in Pakistan in probing looted money lying abroad is a great cause for concern. Unfortunately, the government has successfully flouted the Supreme Court of Pakistan's judgement in the famous NRO case. The Supreme Court has also not made it an issue of public importance and its sole stress on Swiss Case related to Asif Ali Zardari has made the entire process person-specific.

The directions given by the apex Court in *Dr. Mobashir Hasan and others v Federation of Pakistan* (2010 PLD Supreme Court 265) have yet not been complied with—President and his son, Prime Minister, both present and former, in fact, entire People's Party including its veteran leader, Aitzaz Ahsan (once in the forefront of movement for independent judiciary) are in open defiance. This is sheer mockery of the rule of law. Common people, being highly disillusioned now, are candidly saying that even Supreme Court of Pakistan is proving to be yet another ineffective institution as far as matter of bringing back looted money is concerned. The Supreme Court of Pakistan in 2010 PLD Supreme Court 265 held:

> **"Since the NRO, 2007 stands declared void ab initio, therefore, any actions taken or suffered under the said law are also non est in law and since the communications addressed by Malik Muhammad Qayyum to various foreign fora/authorities/courts withdrawing the requests, earlier made by the Government of Pakistan for mutual legal assistance; surrendering the status of civil party; abandoning the claims to the allegedly laundered moneys lying in foreign countries including Switzerland, have also been declared by us to be unauthorized and illegal communications and consequently of no legal**

> **effect, therefore, it is declared that the initial requests for mutual legal assistance; securing the status of civil party and the claims lodged to the allegedly laundered moneys lying in foreign countries including Switzerland are declared never to have been withdrawn. Therefore the Federal Government and other concerned authorities are ordered to take immediate steps to seek revival of the said requests, claims and status".**

The apex Court also observed in this judgement:

> **"A Monitoring Cell shall be established in the Supreme Court of Pakistan comprising of the Chief Justice of Pakistan or a Judge of the Supreme Court to be nominated by him to monitor the progress and the proceedings in respect of Court cases (explanation added in detailed reasons) in the above notices and other cases under the NAO, 1999. Likewise similar Monitoring Cells shall be set up in the High Courts of all the Provinces comprising the Chief Justice of the respective Province or Judges of the concerned High Courts to be nominated by them to monitor the progress and the proceedings in respect of Court cases (explanation added in detailed reasons) in which the accused persons had been acquitted or discharged under Section 2 of the NRO, 2007".**

By summer of 2012, the people of Pakistan have lost all hope. Beneficiaries of NRO whom Supreme Court ordered to be tried under the law are holding key positions and have made Pakistan a State captive in the hands of criminals. The above referred directions of the Supreme Court have lost their meanings as government of PPP and its allies are not inclined at all to act upon them. The partners in PPP government, claiming to be champions of democracy (sic), should be ashamed of their stance and must leave the government at once if they want to survive politically. The Opposition should forge alliance on this issue and render resignation en bloc if verdict of Supreme Court is not implemented. The Opposition of Pakistan must learn from German and Indian Opposition parties how they forced their governments to be tougher while dealing with tax cheats.

In other countries, including India, corruption is an issue but at least there exists a strong will to fight it. Recently in India, two drafts of Lokpal Bill were discussed—one prepared by the government and the other, by activists led by Gandhian Anna Hazare. In Pakistan, on the contrary, political stalwarts (sic) are united to defeat the verdict of Supreme Court in NRO case and have passed obnoxious law such as Contempt Act, 2012. It is time that people like Dr. Mubashir Hassan should come forward and start a nationwide campaign by establishing protest camps outside all Press Clubs of the country. The resistance of

the government to write a letter to the Swiss government as per Supreme Court's NRO verdict should be countered politically by all concerned. It can pave the way for mass movement in Pakistan overthrowing corrupt and inefficient rulers who do not care a damn about welfare of the people.

All responsible governments in the world have in recent years shown commitment to retrieve untaxed money but in Pakistan, the government is acting as the main stumbling block to any such move even when binding judgement of the apex Court so requires and is enforceable under Article 189 of the Constitution. Pakistani tax authorities—knowing that there exists a treaty of avoidance of double taxation and exchange of tax information with all the governments where Pakistanis have parked untaxed money—have not yet taken any step to probe into hidden foreign accounts of Pakistanis or sign fresh treaties with them for this purpose as done by India and others. It is no secret that Pakistani tax evaders have been transferring huge amounts of money to many offshore havens. In Pakistan, we have no leaders like Ram Jethmalani and Anna Hazare having the will and courage to launch nation-wide campaigns against corruption. Ram Jethmalani and Anna Hazare have done so because their own hands are clean whereas in Pakistan, majority of the leaders cannot justify their tax declaration vis-à-vis standard of living and assets amassed during their public life. One hopes that people like Dr. Mubashar Hasan would come forward and start a nation-wide campaign for this cause.

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Sales tax collection: Sindh, Punjab swoop on lucrative telecom business

The newly enforced provincial sales tax laws have given a new dimension to the levy and collect sales tax on telecommunication services on the basis of "termination of a call" rather than "origination of call". A senior tax expert told here on Wednesday that as per section 3 of the Punjab Sales Tax on Service Act, 2012 and Section 3 of the Sindh Sales Tax on Services Act 2011 the services originating from a province and terminating into a certain province are both taxable.

This is a new concept to charge sales tax taking into account "termination of a call" and not the "origination of call". Under section 3 of the Sindh Sales Tax on Services Act 2011, the taxable service is a service listed in the Second Schedule of this Act provided: (a) by a registered person from his registered office or place of business in Sindh; (b) in the course of an economic activity, including in the commencement or termination of the activity. These sub-section deals with services provided by registered persons, regardless of whether those services are provided to resident persons or non-resident persons, it added.

Under Section 3 of the Punjab Sales Tax on Service Act, 2012, a taxable service is a service listed in Second Schedule, which is provided by a person from his office or place of business in Punjab in the course of an economic activity, including the commencement or termination of the activity. If a service listed in Second Schedule is provided to a resident person by a non-resident person in the course of an economic activity, including the commencement or termination of the activity, it shall be treated as a taxable service.

The concept of taxation of service at the point of origination seems logical; however, the concept of taxation of service at the place of termination seems a bit too extended that may fall into double taxation of a service especially when the concept of "multiple taxation" is in vogue by way of taxation through provincial legislation. It is clear that a telecommunication service may originate from Sindh and end up in Punjab. This was the call that will be taxed at origination by SRB and by PRA in Punjab at the point of termination. Same call shall be levied 19.5 percent sales tax twice ending up with a total taxation of about 40 percent.

It is clear that the generation of revenue should not be made in an ambitious manner but with a concept of progressiveness. The taxation authorities are of a clear mind to collect taxation from a

source which is doing well; no one is embarking on the project of finding new ways or base for taxation. Recently, Large Taxpayers Unit (LTU) Karachi also initiated the same trend by collecting FED from banks in the province of Sindh when the FED/ST was paid to the SRB.

Now, the LTU is maintaining the stance that FED is independent of the local/provincial taxation and till the time it is not withdrawn the same shall and can be recovered from banks even if it creates hardship, tax experts explained. The revenue authorities are clearly on the spree of having the industry come down to a halt by taxing them twice or thrice on the same point. Taxation should be done in a manner which should not create problems for the registered units, tax experts added. – *Courtesy Business Recorder*

Telecom companies" issue may cause reshuffle in FBR

The cases of telecom companies on interconnection charges are likely to become a highly controversial basis for a high-level reshuffle in the Federal Board of Revenue (FBR) and field formations. Sources told here on Wednesday that the transfers and postings are expected in the field formations of the FBR following the beginning of new fiscal, based on the performance of the Chief Commissioners of Large Taxpayer Units (LTUs) and Regional Tax Offices (RTOs) during 2011-2012.

According to sources, the FBR Chairman believe in autonomy of the FBR Members for transfers and postings in the field formations. The performance of the field formations in achieving the revenue collection targets for 2011-12 would be the main criterion for transfers and postings in the FBR. If the Chief Commissioners and Commissions have failed to achieve the target, it would be analysed whether this has happened due to inefficiency or another economic factor. "If the senior tax officials have not performed well and failed to deliver the desired results, there is no justification to allow them to stay on the key positions in the field formations", sources said.

Responding to a query, sources said that the LTUs have performed well and shown good performance during 2011-12. This is a remarkable performance of the LTUs to generate revenue in prevailing economic circumstances. The achievement of the assigned targets would be one of the key factors behind transfers and postings. These transfers and postings in the field formations is a regular feature and every year such reshuffle takes place.

When asked about any possible change in the position of the post of the Member Inland Revenue, sources said that the government can appoint any senior tax official as FBR Member. The seniority list and experience of the tax officials in the field formations and the Board is known to all concerned circles. The reputation of the tax official is known to everyone due to his repeated transfers and postings in the field formations. The official with honest and good reputation has been respected by all functionaries in the government departments. However, the decision of the transfers and postings of FBR"s Members was taken at the highest level.

Explaining the legal issue involved in interconnection charges, tax experts explained that telecommunication companies are paying FED (in sales tax mode) on telecommunication services at the rate of 19.5 % of the call charges. Telecom companies provide interconnect services to each other but do not pay FED on the interconnect service charges paid by them on the grounds that FED is paid on the total amount billed to the customer for the taxable service including "Interconnect Charges" and no separate FED for "Interconnect Charges" is required to be paid by the telecommunication companies. Moreover, even if a telecommunication company is forced to pay FED separately on the transfer of money to the other company on account of "Interconnect Charges", the FED paid on such amount by the company becomes its adjustable input tax, thus reducing its payable amount of FED by exactly the same amount. The Government is, therefore, not going to benefit by a single rupee in this case.

The cases initiated on the basis of non-payment of FED on interconnect charges are, however, decided against the telecommunication companies by the Adjudicating Authority as well as the Appellate Tribunal. The telecommunication companies have filed reference applications before the High Court against an order of the tribunal. The telecommunication companies approached Large Taxpayers Unit, Islamabad through their representatives for consideration of their case under section 65 of the Sales Tax Act, 1990, for a waiver of their past liabilities on account of "Interconnect Charges".

The concerned officers forwarded the case to FBR for its consideration. The FBR, examined the case and ascertained that no loss of revenue was involved, as FED on interconnect service charges even if recovered, would have to be allowed as input tax to

the provider of interconnect service and having already discharged their liability they would be obliged to revise their returns and claim refunds. It is a fact that had this amount being recovered from the telecom companies the same would have been claimed as refund by the telecom companies by revising their tax returns. On this basis there was no loss of revenue and the provisions of section 65 of the Sales Tax Act could have been used.

Sources confirmed that the FBR has exercised its powers under section 65 for granting exemption of sales tax under Sales Tax Act, 1990. The following exemptions were granted under Section 65 of the Sales Tax Act: SRO805(I)/93 has granted exemption on Woolen Fabrics to M/S. Lawrancepur Woollen and Textile Mills Ltd; SRO554(I)/2000, Loose or unbranded butter to M/S. Nestle Milk Pak Ltd Lahore; SRO824(I)/2000, Formaldehyde resin, urea formaldehyde moulding compound, melamine formaldehyde moulding compound and polystyrene resin to M/S. Dyno Pakistan Ltd, M/s. Rapid Ltd & M/s. Pakistan Styrene (Pvt) Ltd; SRO837(I)/2000, Hand-knotted carpets to M/s. Afghan Carpet, Karachi; SRO239(I)/2001, Bus and truck chasis to M/S. Hinopak Motors Ltd, M/s. National Motors Ltd, M/S. Sindh Engineering Ltd & M/s. Ghandara Nishan Diesel Ltd; SRO215(I)/2002, Loose or unbranded butter to M/S. Noon Pakistan Ltd; SRO605(I)/2002, Speedometers for vans and pick-ups to M/s.Automotive Components Limited; SRO454(I)/2003, Foryl CP to M/S Ameeje Valleegee and Sons (Private) Limited Karachi; SRO784(I)/2003, Activated Bleaching Earth to M/S. Phoenix Chemicals, Sheikhupra; SRO913(I)/2003, Activated Bleaching Earth to M/S. Pakistan National Chemical Industries (Pvt) Limited, Karachi to M/S. Ittehad Chemicals Limited, Lahore and M/s. Neelum Chemicals (Pvt) Limited, Lahore; SRO74(I)/2004, Motor cycle ignition switch sets to M/S. General Locks (Pvt) Limited; SRO345(I)/2004, Sliver Cans to M/s. Polycon Pakistan (Pvt) Limited, Lahore; SRO104(I)/2005, Acrylic sheets to M/S. Lucky Plastic Industries (Pvt) Ltd, Lahore; SRO105(I)/2005, Acrylic sheets to M/S. Wazirabad Poly Industries (Pvt), Ltd, Lahore; SRO217(I)/2005, Everyday UHT Tea Whitener to M/s. Nestle Milkpak Ltd, Lahore; SRO434(I)/2005, Desk machine to M/s. New Chaudhary Agricultural Mechanical Engineers, Multan; SRO598(I)/2005, Bellapas Plaster to M/S. Dr Sethi (Pharma) Industries, Chichawatni; SRO.868(I)/2005, Liquor to M/S. Avari Hotels ltd, Lahore; SRO.869(I)/2005, Liquor to M/S. Pearl Continental Hotel, Lahore; SRO.870(I)/2005, Liquor to M/S. Pearl

Continental Hotel, Peshawar; SRO.131(I)/2007, Liquor to M/S. Flashman"s Hotel, Rawalpindi; SRO.409(I)/2008 to Liquor, M/s. Best Western Hotel, Islamabad; SRO.816(I)/2008 to Liquor, M/S. Serena Hotel, Faisalabad; SRO.249(I)/2010, Liquor to M/s. Islamabad Marriot Hotel, Islamabad and SRO.287(I)/2010 has granted exemption on Liquor to M/s. Pearl continental, Rawalpindi under section 65 of the Sales Tax Act. – *Courtesy Business Recorder*

Experiment to re-designate posts of FBR Member flops

The Federal Board of Revenue's experiment to re-designate posts of FBR Member Enforcement and Accounting as FBR Member Enforcement and Withholding Taxes and FBR Member Administration as FBR Member Admin and Sales Tax Input Adjustments failed to recover withholding taxes or plug illegal input tax adjustments of Rs 100-150 billion till June 30, 2012.

Sources told here on Wednesday that the posts were re-designated as FBR Member Enforcement and Withholding Taxes and FBR Member Admin and Sales Tax Input Adjustments with the objective to generate additional revenue by the end of June 2012. The policy decision was taken by former FBR Chairman Mumtaz Haider Rizvi which failed to achieve the desired results.

The additional charge of Withholding Taxes and Sales Tax Input Adjustments to the FBR Members stand abolished as on June 30, 2012. This wrong policy measure was taken to achieve the assigned revenue collection target of Rs 1952 billion by June 30, 2012. The measure created serious problems in the reporting functions of the line members like FBR Member Inland Revenue.

The posts of FBR Member Enforcement and Withholding Taxes and FBR Member Admin and Sales Tax Input Adjustments remained operative till June 30, 2012 with the sole objective of immediate generation of revenue in the form of recovery of withholding taxes as well as illegal input tax adjustments. However, the FBR's data revealed that the recovery of the illegal adjustments and withholding taxes during 2011-2012 was only due to the enforcement actions of the Directorate General of Intelligence Inland Revenue, Directorate General of Withholding Taxes and field formations. However, no new kind of methodology has been applied by the said re-designated positions as the powers of the line members were indirectly curtailed by giving specific powers of the tax laws to other members of the Board.

Sources said that the experiment was not successful and such kind of restructuring has affected the regular work of the line members. Former Chairman had re-designated these two top posts for the recovery of over Rs 150 billion arrears of wrongfully claimed input tax adjustment on sales tax side and recovery of withholding tax withheld by the banks but failed to deposit in the national kitty. However, there has been no major recovery from withholding side as well as wrongly claimed in put tax adjustment.

The tax collection that was reported to Ministry of Finance on July 25, 2012 stands at Rs 1915 billion including Rs 25 billion of Sindh Revenue Board. According to the estimates submitted to ECC meeting on July 24, 2012, the total net tax collection have been recorded at Rs 1.881 trillion (excluding SRB collection) against the actual budgetary target of Rs 1.952 trillion fixed for the last fiscal year. However, the federal tax collection has shown a 20.8% growth in 2011-12 with a total collection of Rs 1.881 trillion against the collection of Rs 1.558 trillion during the last fiscal year 2010-11.

As per latest chart of the economic indicators including revenue collection chart presented before the Economic Co-ordination Committee (ECC) of the Cabinet on Tuesday, no details of the payment of refunds and rebates has been given to the ECC. The direct taxes collection amounted to Rs 731.9 billion during 2011-12 as compared with direct taxes collection of Rs 602.5 billion in the last fiscal year 2010-11, showing an increase of 21.5%.

The indirect taxes collection during the last fiscal year 2011-12 amounted to Rs 1.149 trillion against the net indirect taxes collection of Rs 955.7 billion during the last fiscal year 2011-12, projecting an increase of 20%. The general sales tax collection has been recorded at Rs 809.3 billion in the last fiscal year 2011-12 against the collection of Rs 633.4 billion of the previous fiscal year 2010-11, showing an increase of 27.8%.

The federal excise duty collection amounted to Rs 122 billion in 2011-12 as compared with the collection of Rs 137.4 billion in the last fiscal year 2010-11, showing a decrease of 11.2%. The Customs duty collection has been recorded at Rs 218.2 billion in last fiscal year 2011-12 against the collection of Rs 184.9 billion in the previous fiscal year 2010-11, reflecting an increase of Rs 18%. – *Courtesy Business Recorder*

Taxpayers experiencing problems in filing electronic tax returns

The business community is experiencing a number of problems in filing electronic sales tax returns due for the tax period June 2012 because of system limitations. Experts pointed out the need for necessary modifications and amendments in the sales tax returns, urging the authorities to make them easier for the business class, saying that it would help generate more revenue.

A renowned Karachi-based sales tax expert, Arshad Shehzad told here on Wednesday that serious limitations were causing practical problem in filing electronic sales tax returns, which was reported while filing sales tax return for the tax period of June 2012. Among the limitations are: There is no provision/column available for reporting of sales tax paid at import stage by importers on bill of additional duties and challans.

In cases of any valuation dispute the Customs authorities usually cleared consignment on submission of post dated cheque/sureties by importers and marked the case to valuation collectorate to ascertain the correct value. Later on, if the value determined by the valuation department is more than declared value, customs charges differential amount of duties and taxes from the importer by generating manual bill of miscellaneous and additional duties.

However, since the bill is issued manually there is no provision for its reporting in electronic sales tax filing system. Therefore, component of sales tax paid on such bills cannot be claimed in sales tax return as input tax, in spite of legal backing provided under Section 7 of the Sales Tax Act, providing entitlement of input tax adjustment on sales tax paid at customs stage.

Shehzad further said that this year in June the number of such cases were settled being last month of the fiscal, therefore large number of taxpayers are facing problem in reporting such input tax in their sales tax return. He said that system also put limitation on reporting sales during last couple of months. Now, he said, a taxpayer could only report sales pertaining to current tax period ie filing month of sales tax return, the question raises, if the taxpayer fails to report sales of previous months and now intend to report the same in next month though legally he can report by paying default surcharge and penalty u/s 33 and 34, how can system limits or restrain them reporting such sales? The system is simply now allowing such sales the taxpayer can only report

through filing of revision of return, which causes undue hassle to the registered persons.

He also pointed out that all such amendments and limitation, prior to introduction of electronic form were publicised through notifications and clarifications, but nothing was observed in update system, which increases confusions. Therefore, there was a dire need for all minor practical modifications and amendments to be publicised properly to timely educate taxpayers and to avoid confusion, he said. – *Courtesy Business Recorder*

Assurance to IT, computer industry: government to revisit matter regarding GST exemption

Abbas Khan Afridi, Minister of State for Commerce has assured the computer industry that the government would revisit the matter regarding general sales tax (GST) exemption for IT and computer industry of the country.

While talking to a delegation of Pakistan Computer Association (PCA), led by Munawar Iqbal, the President PCA Central, Abbas Khan Afridi said on Wednesday that IT sector is vital for the growth of overall economic development of the country and hence every possible measure would be taken to boost this vital sector of the economy.

This requires amendment in the Sixth Schedule of the Sales Tax Act 1990 to restore sales tax exemption for IT industry of Pakistan. Besides others, Abdullah Malik, President PCA Islamabad, Rashid Ali, Zafar Shahzad and Atta Ur Rehman Tahir were also present on the occasion. Munawar Iqbal on the occasion briefed the minister about the state of the affairs pertain to IT and computer industry in Pakistan. He said that due to ill conceived policies of last dictatorial regime, the IT has lagged behind in this region and in order to fill this gap and for a rapid growth the nascent industry needs a tax exemption at least for next few years.

The president of PCA Central highlighted the issue of registration of PCA as trade body with concerned department of the ministry and said that the association is representative body of the vendors in the industry and hence it couldn't be forced to link with any software developers' body. He also apprised the minister that the PCA has made stern efforts to promote free software in Pakistan to save precious national exchequer on the purchase of software.

He said that PCA seeks the support of the ministry in this regard. Abbas Khan Afridi assured delegation of the full support of his ministry and said that the issue raised by PCA would be resolved as soon as possible. He said that the government wants to promote this sector and would make all-out efforts to facilitate the industry. – *Courtesy Business Recorder*

2012 PTR 1280 (Trib. Ind.)

INCOME TAX APPELLATE TRIBUNAL
MUMBAI "E" BENCH, MUMBAI

G.E. Veerabhadrappa, President and Vijay Pal Rao, Judicial Member

FACTS/HELD

1. **S. 147: Non-supply of recorded reasons before passing reassessment order renders the reopening void. Subsequent supply does not validate reassessment order**

2. After completing the s. 143(3) assessment, the AO received information from the Volcker Committee report that the assessee had paid "*illegal*" commission for supply of goods to Iraq under the "Oil for Food Programme" of the UN. The AO issued a s. 148 notice to disallow the commission and *supplied the assessee with only the "gist" of the recorded reasons*. The *complete recorded reasons were furnished only after the passing of the reassessment order*. In the reassessment order, the AO disallowed the commission. The CIT (A) upheld the reassessment. On appeal by the assessee to the Tribunal, HELD allowing the appeal:

> As per GKN Driveshafts 259 ITR 19 (SC) and the rules of natural justice, the AO was bound to furnish reasons within a reasonable time so that the assessee could file objections against the same. The **adherence to this procedure is a necessity** because at the preliminary stage itself, the AO may be satisfied with the explanation of the assessee. A reassessment completed without furnishing the reasons actually recorded by the AO for reopening of assessment is not sustainable in law. **The *subsequent supply* of the reasons would not make good of the illegality suffered at the stage of reopening of the assessment**. On facts, though the assessee asked for the recorded reasons, the same was supplied to him **only after** the passing of the reassessment order. This failure on the part of the AO renders the reassessment order invalid (Fomento Resorts

& Videsh Sanchar Nigam 340 ITR 66 (Bom) (SLP dismissed) followed (*included in file*)).

Appeals allowed.

I.T.A. Nos. 3359 to 3361/Mum/2009 (Assessment Years : 2001-01, 01-02 and 2002-03).

Heard on: 14th June, 2012.

Decided on: 29th June, 2012.

Present at hearing: Dinesh Vyas, for Appellant. Jay Kumar, for Respondent.

JUDGMENT

Per Vijay Pal Rao:– (Judicial Member)

These 3 appeals by the assessee are directed against 3 separate orders of Commissioner of Income Tax (Appeals) all dated 27.2.2009 for the assessment years 2000-01, 2001– 02 and 2002 – 03 respectively.

2 The assessee has raised common grounds in these appeals; therefore, the concise grounds raised for the assessment year 2000-01 are reproduced as under:

1. *The ld Commissioner of Income Tax(Appeals)) erred in upholding the validity of –*
   - (i) *the reopening, purportedly under Section 147,, the appellant's assessment u/s 1543(3) dated 27th March 2003 an d*
   - (ii) *the making of the Reassessment Order,*

   and in not accepting the several challenges to the reassessment proceedings raised before him (and more specifically referred to in the original grounds of appeal urged before this Hon'ble Tribunal.

2.1. *Without prejudice to the above, the [earned Commissioner(Appea(s) erred in upholding the Assessing Officer's disallowance of the aggregate commission of Rs 11,98,505.*

2.2. *Without prejudice to the above, the learned Commissioner(Appeal(s) erred in upholding the Assessing Officer's invocation of, and reliance upon, the Explanation to Section 37(1) (in disallowing the aggregate commission of Rs 11,98,505).*

2.3. *Without prejudice to the above, the (earned Commissioner(Appeals) erred in rejecting the Appellant's Ground 2.3 urged before him to the effect that, assuming whilst denying that the Assessing Officer's inference to the effect that the said aggregate commission represented ITF and ASSF was*

correct in Law, no part of such commission was disallowable for the reason also that all the commission payments having been made exactly in terms of the Appellant's Agency Agreements, such commission was allowable in full, and, therefore, ought to have been so allowed.

3. *Without prejudice to the Appellant's submission that the Reassessment is bad in law and illegal and hence liable to be annulled, the learned Commissioner(Appeals) erred in having "partly allowed" the Appellant's Ground 3 urged before him to the effect that the Assessing Officer erred (while recomputing the Total Income) in omitting to give effect to the Appellate Order under Section 250 of the (earned Commissioner(Appeals) dated 2nd January, 2006, made in the Appellant's appeal against the Original Assessment. The Appellant submits that the (earned Commissioner(Appeals) ought to have allowed the said Ground 3 by directing the Assessing Officer to give effect to the said Appellate Order.*

4.1. *The learned Commissioner (Appeals) erred in upholding the Assessing Officer's charging of interest under Section 234-D amounting to Rs 55,78,316.*

4.2. *Without prejudice to the generality of Ground 4.1, the (earned Commissioner(Appeals) erred in not following the binding order of the Special Bench of this Hon'ble Tribunal in ITO v Ekta Promoters (P) Ltd 12008] 113 lTD 719 (Del)(SB), which order was not merely cited before the learned Commissioner(Appeals) by the Appellant, but which order the learned Commissioner(Appeals) was aware of, as would be evident from his reference to the Appellant having "relied on some judgments" (in paragraph 4.2 of his Appellate Order)."*

3 Ground number 1 regarding validity of reopening assessment:

3.1 The original assessment for all 3 years was completed under section 143 (3). Subsequently, as per the CBDT information, the Assessing Officer noted that during the year under consideration the assessee supplied goods to Iraq under the Scheme called 'Oil for Food Programme of the UNO'. The name of the assessee had appeared at Sl. No. 113 of the Volcker Committee report submitted on 27.10. 2005 wherein it was mentioned that the commission paid was illegal. The Assessing Officer issued a notice under section 148 of the I T Act dated 31.01.2007. In response to the notice, the assessee submitted a letter dated 8.3.2007 and requested to furnish the reasons for issuing the said notice in view of the decision of Hon'ble Supreme Court in case of *GKN Drivershafts (India) Ltd vs. ITO* reported in 259 ITR 19. Thereafter, the Assessing Officer issued a fresh notice under section 148 dated 28.03.

2007 along with a covering letter dated 28.3.2007 stating that the earlier notice dated 31.1.2007 may be treated as cancelled for technical.

3.2 In response to the notice under section 148 dated 28.03.2007, the assessee again demanded the reasons for issuing the said notice vide letter dated 25.04.2007. The Assessing Officer, vide its letter dated 28.6.2007 supplied the reasons (gist of the reasons) for reopening of assessment.

3.3 The assessee was not satisfied with the reasons supplied by the Assessing Officer being the gist of reasons and therefore again requested vide letter dated 25.07.2007 for the supply of the true copy of the reasons actually recorded by the Assessing Officer in terms of section 148 (2).

3.4 The Assessing Officer, vide his letter dated 27.07.2007 reiterated that the reasons for reopening has been supplied vide letter dated 28.06.2007. The assessee, still not satisfied with the response of the Assessing Officer again requested vide its letter dated 13.8.2007 for the supply of the reasons actually recorded. The Assessing Officer proceed with the re-assessment proceedings and passed the assessment order under section 143 (3) read with section 147 of IT Act on 31.12. 2007 whereby disallowed the commission paid by the assessee for the supply of goods to the Iraq under the scheme 'Oil for Food Programme of the UNO'.

4 The assessee challenged the action of the Assessing Officer before the Commissioner of Income Tax (Appeals) and raised the issue of validity of reopened assessment. The main objection of the assessee against the reopening of assessment is on the ground that it was neither provided with the recorded in its entirety nor was given the copies of certain letters relied upon by the Assessing Officer.

4.1 The Commissioner of Income Tax(Appeals) was not impressed with the contentions and the objections raised by the assessee and accordingly, rejected the objections raised against the validity of reopening of assessment.

5 Before us Mr Dinesh Vyas, the ld Sr. Counsel of the assessee has submitted that the entire procedure mandated by law has been violated while reopening of assessment. He has referred the notice under section 148 of the I T Act dated 31.1.2007 and submitted that the said notice was issued after the expiry of 4 years from the end of the relevant assessment year. He has further submitted that the said notice was withdrawn by the Assessing Officer and a fresh notice under section 148 dated 28.3.2007 was issued. The ld Sr counsel has submitted that the Assessing Officer has not mentioned as to why the earlier notice under section 148 was withdrawn and cancelled. He has pointed out that once the notice dated 31.1.2007 was withdrawn, the second notice dated 28.3.2007 is not sustainable in the absence of the reasons recorded by the Assessing Officer.

5.1 He has further contended that even otherwise the case falls under the proviso to section 147 of the I T Act and it is mandatory condition for reopening of assessment that assessee has failed to disclose fully and truly all material facts necessary for assessment. He has referred the reply of the assessee dated 8.3.2007 to the notice under section 148 dated 31.1.2007 and submitted that the assessee had specifically demanded and requested to furnish the reasons for reopening. The ld Sr counsel referred the entire correspondence between the assessee and the Assessing Officer and submitted that the assessee has repeatedly requested the Assessing Officer to supply the reasons actually recorded by the Assessing Officer in terms of section 148 (2) of the I T Act. The Sr counsel then referred the letter dated 28.6.2007 of the Assessing Officer whereby the gist of the reasons were supplied to the assessee and submitted that the assessee was not supplied full reasons of reopening of the assessment and therefore, despite the repeated requests, the Assessing Officer failed to supply the reasons till the completion of assessment and even till date.

5.2 The ld Sr counsel has referred and relied upon the decision of Hon'ble jurisdictional High Court in case of *Commissioner of Income-tax vs. Videsh Sanchar Nigam Ltd.* reported in 340 ITR 66 and submitted that supply of reasons after the completion of assessment has no effect and the exercise is futility. Since the reasons are not furnished, the reassessment order is bad in law. Thus the ld Sr counsel has submitted that gist of reasons is no substitute of reasons recorded by the Assessing Officer and therefore, in the absence of supply of reasons recorded by the Assessing Officer to the assessee, the reassessment is bad in law. In support of his contention, the ld Sr counsel has relied upon the decision of Hyderabad Bench of the Tribunal in case of *Jasti Rama Rao vs. ITO* reported in130 TTJ 66 (unreported).

5.3 Apart from this, the ld Sr counsel has also contended that despite the request of the assessee, the sanction of the Commissioner was not supplied and the sanction of the Commissioner should not be mechanical; but a due application of mind should reflect from the same. The ld Sr. counsel has also cited a series of decisions of Hon'ble High Courts as well as this Tribunal on the point that the reasons have to be recorded before issue of notice under section 148 and if the are not supplied, it can be presumed that reasons were not recorded prior to issue of notice under section 148.

5.4 Alternatively, the ld Sr counsel has submitted that even in the reasons recorded, there is no allegation that the income has escaped assessment due to assessee's failure to make full and true disclosure of all material facts necessary for the assessment and as such, the absence such allegations renders the reassessment proceedings invalid. He has reiterated that reasons recorded cannot be improved upon subsequently.

5.5 The ld Sr counsel for the assessee has also raised an objection against recording of reasons by one officer and issuing notice under section 148 by other. In support of his contention, he has relied upon the decision of Hon'ble Gujarat High Court in case of *Hynoup Food and Oil Industries Ltd. vs. Assistant Commissioner of Income-tax* reported in 307 ITR 115.

5.6 On the other hand the ld DR has submitted that the Assessing Officer has duly recorded the reasons prior to issue of notice under section 148. He has filed a copy of reasons recorded on 31.01.2007 for reopening of the assessment and submitted that in the gist of reasons supplied to the assessee, nothing material has been left. He has further submitted that it is to be seen that what material part of regions was left or any deviation from the reasons original recorded and those supplied to the assessee. The ld DR has further submitted that the assessments have been reopened on the basis of information received from the CBDT.

5.7 The ld DR has referred the decision of Hon'ble Supreme Court in case of *GKN Driveshaft (India) Ltd vs. ITO* (supra) wherein the Hon'ble Apex Court has held that the Assessing Officer is bound to furnish reasons within a reasonable time and after receipt of the reasons, the assessee is entitled to file objection of issuance of notice and the Assessing Officer is bound to dispose of the same by passing a speaking order. Thus the ld DR has submitted that when the substantial reasons were furnished by the Assessing Officer, than the assessee cannot challenge the reopening of assessment on the ground of non-furnishing of reasons. He has further submitted that if prima facie some material is there on the basis of which the Assessing Officer could form an opinion that the income assessable to tax has escaped assessment, than the reopening is justified. In the case in hand, the Assessing Officer received the information through CBDT about the Volcker Committees report and came to know that the commission was illegally paid by the assessee, than the income assessable to tax has escaped assessment to the extent the deduction allowed in the original assessment on account of commission paid by the assessee. In support of his contention, he has relied upon the decision of Hon'ble Supreme Court in the case of *Raymond Woollen Mills Ltd. vs. Income-tax Officer*, reported in 236 ITR 34. He has further contended that the reopening is valid, even based on internal audit and therefore, the reopening on the basis of information received from CBDT is valid. He has relied upon the decision of the Hon'ble Supreme Court in the case of *CIT vs. P V S Beedies P Ltd* reported in reported in 103 Taxmann 294. He has also relied upon the orders of the authorities below.

5.9 In rebuttal, the ld Sr counsel for the assessee has submitted that there is no failure on the part of the assessee to furnish the true and correct facts necessary for assessment. The Assessing Officer is bound to furnish the reasons actually recorded and not the gist of the reasons.

Therefore, in the absence of furnishing the reasons recorded by the Assessing Officer, the reassessment is illegal and not sustainable. The ld Sr counsel has also advanced the argument on the merits of the case and on the point that the Volcker Committees report is only an investigation and not a judicial finding. It cannot be said that the assessee has committed any illegality on the basis of the committee report until and unless it is established that the act of the assessee is against some statute. He has further submitted that nothing has been brought on record to show that the payment of commission is against any existing low in force. Both the ld Sr counsel as well as the ld DR have referred certain decisions of this Tribunal on the merits of the issue of addition on the basis of Volcker Committee report.

6 We have considered the rival contentions as well as relevant material on record. We have also carefully perused the various decisions relied upon by the parties. Though the arguments from both sides were also addressed on the merits of the issue; however, at this stage, we confined ourselves to the issue of validity of reopened assessment.

6.1 As we have noted above that initially the Assessing Officer issued a notice under section 148 dated 31.1.2007. The said notice was cancelled/withdrawn and a fresh notice under section 148 was issued on 28/03/2007. The assessing officer has given the reasons of treating the said notice dated 31/01/2007 as cancelled for technical reasons and fresh notice was issued to rectify the procedural lacuna in the earlier notice dated 31/01/2007. Though nothing has been elaborated either in the communication dated 28/03/2007 or in the reassessment order as what was the technical reason and a procedural lacuna in the earlier notice however, it appears from the record that the earlier notice dated 31/01/2007 was issued prior to the approval of the Commissioner of income tax dated 26/03/2007 and therefore, the earlier notice was cancelled and treated as withdrawn. The Assessing Officer, than obtained the approval of the Commissioner of Income Tax on 26/03/2007 and thereafter issued the fresh notice dated 28/03 2007 on the basis of which the Assessing Officer, proceeded with the reassessment proceedings. Thus, after the fresh notice 28/03/2007, the notice dated 31/01/2007 becomes non-est, immaterial and irrelevant for reassessment proceedings and therefore, has no consequence whatsoever with regard to the validity of reassessment.

6.2 The main objection of the assessee against the reassessment is non-supply of the reasons recorded by the Assessing Officer for reopening of assessment. There is no doubt that the Assessing Officer recorded the reasons on 31/01/2007 for reopening of the assessment and accordingly issued a notice under section 148. The regions as recorded by the Assessing Officer are as under:

> *"This case appears in the list of companies who had supplied goods to Ira under the scheme of "Oil for Food Programme of the*

UNO". The name of the assessee company appears at Sr. No. 113 of the Voicker Committee Report submitted on 27/10/2005 wherein the mention of illegal commission under the heads of AASF & Inland Transportation fees amounting to US 370780 & 399361 respectively had been paid.

Details were called from M/s. Tata International Ltd and from the details submitted it is seen that these payments have been made during the period relevant to A.Y. 2000-01 to 2002-03. Hence, it is clear that based on the additional information of the Voicker Committee, the commission payment has been made by the assessee.

As per the information gathered, it can be seen that commission o Rs.9,82,542/-,, Rs.1.27,42,120/- and Rs.t,06,09,979/- for A.Y. 2000-01. 2001-02 and 2002-03 respectively has been paid. The payment of kicks backs/bribe is prohibited by law and therefore, squarely thus within the ambit explanation to section 37(1) of the I.T. Act, 1961 and requires to be disallowed. Therefore, I have reasons to believe that income to that extent has escaped assessment. As such the assessment needs to be reopened u/s 147 of the 1.T. Act, 1961 to tax the escaped income. The case is fit for issue oft notice uis.148 of the 1.T. Act, 1961.

Notice u/s.J48 of the 1.T. Act is issued to the assessee for A.Y. 2C00 01, 2001-02 & 2002-03."

6.3 In response to the fresh notice under section 148 dated 28/03/2007 the assessee vide its letter dated 25/04/2007 specifically requested the Assessing Officer to furnish the reasons for issuing the notice under section 148. The averments made in paragraph 3 of the said letter are as under:

"We also take this opportunity to renew our request to you to furnish to us the reason(s) for issue by you of your said notice under section 148 dated 31st Jan 2007 and of the fresh notice, in accordance with the procedure laid down by the Supreme Court in GKN Driveshafts (India) Ltd v ITO (2003)259 ITR 19(SC)."

6.4 In pursuant to the said request of the assessee the Assessing Officer has supplied the gist of the reasons of reopening vide letter dated 28/06/2007 as under:

"Vide the above referred letter wherein we have requested that the reasons for Issue of the said notice dated 28.03.2007 be furnished in accordance with the procedure laid down in the case of GKN Driveshafts (I) Ltd. vs. ITO [2003] 259 ITR 19 (SC). The gist of the reason for reopening is as under

"During the year under consideration, the assessee company has supplied/goods to Iraq under the scheme 'Oil for Food

Programme of the UNO'. The name of the assessee company appears at Sr.No. 113 of the Voicker Committee Report submitted on 27.10.2005 wherein mention of the illegal commission under the head 'AASF' and 'Inland Transportation Fees' had been paid. Therefore, I have reasons to believe that income to that extent has escaped assessment,"

6.5 Since only the gist of the reasons were supplied, the assessee was not satisfied with the reasons as supplied by the Assessing Officer and requested vide its letter dated 25/07/2007 and demanded the true copy of reasons actually recorded by the Assessing Officer in terms of section 148 (2) of the Income Tax Act instead of the gist of reasons for reopening reproduced in the letter dated 28/0 6/2007.

6.6 In response to the assessee's letter dated 25/07/2007, the Assessing Officer vide its letter dated 27/07/2007 reiterated that the reasons for reopening were supplied vide letter dated 28/06/2007. Since the request of the assessee for furnishing the reasons actually recorded by the Assessing Officer was not given heed; therefore, the assessee again demanded the reasons as recorded by the Assessing Officer for reopening of the assessment vide its letter dated 13/08 2007. Despite repeated requests and demand of the assessee the Assessing Officer was adamant on his stand for not supply of the reasons actually recorded for reopening of the assessment and insisted upon that the same have been supplied to the assessee vide letter dated 28/06/2007.

7 As held by the Hon'ble Supreme Court in case of GKN Driveshafts (India) Ltd (supra) that the Assessing Officer is bound to furnish reasons within a reasonable time so that the assessee could file objection to the issuance of the notice and the Assessing Officer, accordingly, bound to dispose of the same by passing a speaking order. Thus, the supply of reasons is to facilitate the assessee to present its defence and objection against the reopening of the assessment.

7.1 Even otherwise as per the rule of natural Justice, the assessee is entitled to know the reasons on the basis of which the Assessing Officer has believed and formed an opinion that the income assessable to tax has escaped assessment. It is not understandable as to why the Assessing Officer was so reluctant and hesitant to furnish the reasons actually recorded for reopening of assessment. We see no reason and rather justifiable reasons for depriving the assessee of the reasons actually recorded by the Assessing Officer for reopening of the assessment.

8 In the case of *CIT vss Videsh Sanchar Nigam Ltd*, the Hon'ble jurisdictional High Court has confirmed the order of this Tribunal whereby the reassessment was held as invalid because the reasons recorded for reopening of the assessment were not furnished despite repeated requests and furnished only after completion of assessment. The Hon'ble High Court has observed in para to as under:

> *"2 The fining of fact recorded by the Income Tax Appellate Tribunal is that in the present case the reasons recorded for reopening of the assessment through repeatedly asked by the assessee were furnished only after completion of the assessment. The Tribunal following the judgment of this Court in the case of CIT vs Fomento Resorts & Hotels Ltd, Income Tax Appeal no.71 of 2006 decided on 27th November 2006 has held that though the reopening of the assessment is within three years from the end of relevant assessment year, since the reasons recorded for reopening of the assessment were not furnished to the assessee till the completion of assessment, the reassessment order cannot be upheld. Moreover, Special leave Petition filed by the revenue against the decision of this Court in the case of Fomento Resorts & Hotels Ltd has been dismissed by the Apex Court vide order dated 16th July 2007."*

8.1 Thus the reasons are required to furnish within a reasonable period of time so that the assessee can raise the objections at the preliminary stage of proceedings. If the reasons are not supplied during the assessment proceedings, than furnishing the reasons subsequent to the assessment proceedings would achieve no purpose and tantamount to deprive and deny the assessee of its right to raise the objections against the validity of notice issued under section 148.

8.2 Thus reassessment completed without furnishing the reasons actually recorded by the A.O. for reopening of assessment is not sustainable in law because the A.O. is duty bound to supply the same within reasonable time as held by the Hon'ble Supreme Court in case of GKN Driveshafts (India) Ltd (supra). The subsequent supply of the reasons would not make good of the illegality suffered by the reopening of assessment. A similar view has been taken by this Tribunal in case of Fomento Resorts & Hotels Ltd vs JCIT and decided a similar issue in para 7 as under:

> *"7 We have considered the submissions made by both the sides, perused the orders of the authorities below and material on record. It is an admitted fact that the assessee has not filed return of expenditure tax in the normal course. The Assessing Officer issued notice purportedly u/s 11 but inadvertently on the notice, u/s 8 was mentioned in lieu of sec. 11. In this regard, we are in agreement with the findings of the ld Commissioner of Income Tax(Appeals) that this mistake was covered by the provisions of see. 292B of the Income Tax Act, therefore, we do not find any merit in the contentions of the assessee in this regard. As far as the issuance of notice u/s 11 is concerned, the preliminary condition of not filing of return is satisfied. Therefore, in such a situation, notice can be issued, provided the same is not barred by limitation. However, after issue of notice, if*

the assessee asks for furnishing of reasons for issuance of such notice, the Assessing Officer is bound to furnish such reasons. The adherence to this procedure is a necessity because at the preliminary stage itself, if the proceedings can be completed if the Assessing Officer gets satisfied with the explanations given by the assessee. it is an undisputed fact that the Assessing Officer, in the present case has not supplied reasons to the assessee, therefore, the notice issued by the Assessing Officer is bad in law and consequently the assessment made in pursuance of such notice is liable to be quashed. In this view of the matter, we cancel the impugned assessment. We order accordingly."

9 The order of this Tribunal was upheld by the Hon'ble jurisdictional High Court as mentioned in the decision in the case of *Videsh Sanchar Nigam Ltd* (Supra). Even the SLP filed by the revenue against the decision of Hon'ble jurisdictional High Court has also been dismissed by the Hon'ble Supreme Court vide order dated 16 July 2007. Thus, it is settled proposition as laid down by the Hon'ble Supreme Court as well as Hon'ble High Court that the reasons as recorded by the Assessing Officer are required to be furnished to the assessee and the reasons recorded cannot be improved upon or amended by any correspondence, letters etc. It is an undisputed fact that the reasons actually recorded by the Assessing Officer were not furnished to the assessee till 14.06.20012 despite repeated requests and demands and therefore, the gist of reasons as furnished vide letter dated 28th June 2007 cannot be treated as reasons actually recorded by the Assessing Officer as per section 148 (2) and as mandated by the Hon'ble Supreme Court in case of *GKN Driveshafts (India) Ltd* (supra). Thus, the Assessing Officer has failed to furnish the reasons recorded for reopening of the assessment within the reasonable time and rather prior to the completion of assessment, than the reassessment order passed without supply of reasons as recorded for reopening of the assessment, is invalid and cannot sustain. Accordingly, we set aside the reassessments for all 3 years under consideration being invalid.

10 Since we have quashed the reassessment being invalid; therefore, we do not propose to go into the merits of the issue raised in these appeals.

11 In the result the appeals filed by the assessee are allowed.

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