

APPELLATE TRIBUNAL INLAND REVENUE LAHORE BENCH LAHORE

ITA No.776/LB/14
(Tax year 2011)

ITA No.777/LB/14
(Tax year 2012)

M/s. Q. Mart Corporation (Pvt)., Ltd., Lahore. ... Appellant

Versus

The CIR. RTO., Lahore. ... Respondent

Appellant by:- Mr.Muhammad Irshad ITP

Respondent:- Mr. Sajjad Tasleem, D.R.

Date of hearing:-09-06-2014 Date of Order:-09-06-2014

ORDER

Through titled appeals pertaining to Tax Years 2011 and 2012, the taxpayer assailed the consolidated order dated 12-09-2012, passed by the learned CIR (A), Lahore. The appellant / taxpayer assailed the order of the learned CIR (A) on the following common grounds of appeal: -

1. That the order of the learned Commissioner Inland Revenue (Appeals) is bad in law and against the facts of the case.
2. That the learned Commissioner Inland Revenue (Appeals) was not justified in confirming the tax demand of Rupees 1,906,794/- for tax year 2011 and Rs.1,926,150/- for tax year 2012 u/s 113 of the Income Tax Ordinance, 2001 by the learned ACIR, when no accounting pattern was changed by the appellant. His action by ignoring the written submissions and by misunderstanding the provisions of law and facts of the case, is illegal and unsustainable.

3. That the learned Commissioner Inland Revenue (Appeals) was not justified in confirming the illegal and wrong charge of default charge amounting to Rupees 665,659/- for tax year 2011 and Rs.346,707/- for tax year 2012.
4. The learned Commissioner Inland Revenue (Appeals) has failed to instruct the learned ACIR to allow credit of tax deducted at source of the appellant amounting to Rupees 768,430/- for tax year 2011 and Rs.218,533/- for tax year 2012.

2. The relevant common facts in brief are that the taxpayer in this case is a private limited company derives income as a retailer in all types of general merchandise. Returns for the tax years 2011 and 2012 were filed declaring loss of Rs.16,091,263/- and Rs.15,621,588/- respectively. Returns filed were deemed to be treatment as assessment in terms of section 120 (1) of the Income Tax Ordinance, 2001. Subsequently, during the course of scrutiny of these deemed assessments / returns of income, it was found by the concerned Additional Commissioner that the deemed assessments completed are erroneous insofar as prejudicial to the interest of revenue in as much as the taxpayer /company had claimed profit and loss expenses under the manufacturing /trading account (cost of sales) and due to this claim the trading account gross loss has been arrived during both the years under appeal. On the basis of this discrepancy, the Additional Commissioner, issued show cause notice u/s 122 (5A) to amended the deemed assessment for tax years 2011 and 2012. In response, the taxpayer / company submitted that they had rightly claimed the expenses in the trading account as these are directly attributable to the main business activity and ultimately become the part of cost of material sold. However, the assessing authority being not convinced with the submissions made by the taxpayer, has amended the

assessments u/s 122 (5A) for tax years 2011 and 2012, by rejecting the selling / P & L expenses and charged minimum tax u/s 113 as the gross loss was converted into gross profit in both the years under appeal. The assessing authority also charged default surcharge in both the years as the taxpayer has not paid the minimum tax alongwith the returns of income. Similarly, the claim of tax credit for tax year 2011 and 2012 has also been rejected on the ground that the required documents were not submitted by the taxpayer.

3. Being aggrieved, the taxpayer went in appeal before the learned CIR (A) and assailed the treatment meted out by the assessing authority on a number of legal and factual grounds. However, the learned CIR (A) being not satisfied with the submissions made by the learned AR, has rejected both the appeals by observing as under: -

"I have given due consideration to the rival arguments in consultation with the record and I am of the view that the submissions made at the bar carry no weight. Perusal of impugned order indicates that prior to tax year 2011, the appellant was claiming the cost of sales in the trading account whereas afterwards it prepared their account whereby the selling administrative expenses are also included in the cost of sales. It may be correct as per accounting standard but under the Income Tax Law it is not legally correct. I am of the view that the appellant has changed its accounting system just to avoid the proper incidence of taxation. I agree with the treatment accorded by the Officer of Inland Revenue which is supported by parallel cases duly mentioned in the body of the impugned order."

4. The learned AR on behalf of Taxpayer / Company assailed the above observation of the learned CIR (A) as contrary to law and facts of the case. It is contended by the learned AR that the deemed assessment completed for both the years were neither erroneous nor prejudicial to the interest

of revenue which were unjustifiably and illegally amended by the assessing authority by resorting to the provisions of section 122 (5A) of the Income Tax Ordinance, 2001. It is submitted by the learned AR that the taxpayer is maintaining proper books of accounts and supporting documentation in accordance with the international accounting standards and in accordance with the provisions of section 32 (2) of the Companies Ordinance, 1984. It is contended by the learned AR that the assessing authority has misunderstood the business activity of the taxpayer/company and disallowed the expenses which were rightly attributed to the trading expenses. It is explained by the learned AR that operating expenses includes salary of cashier on cash counter, floor helpers, store manager, electricity charges of store, generators running cost, freight charges, repair and maintenance of store, rent of store building etc. It is asserted by the learned AR that these expenses were rightly claimed by following "accrual basis" of accounting principle as required under sub-section (2) of section 32 of the Companies Ordinance, 1984. On the contrary, the learned DR supported the order passed by the authorities below and contended that the assessing officer has rightly invoked the provisions of section 122 (5A) while making the amendment of assessment for both the years.

5. We have heard the arguments *put-forth* by the learned representatives of both the sides and have carefully gone through the available record. After due consideration, we find that the Additional Commissioner Inland Revenue has amended the both orders for the tax years 2011 and 2012 u/s 122(5A) of the Income Tax Ordinance, 2001, for the common reason that the taxpayer has changed its accounting pattern and erroneously charged administrative and selling expenses in the trading account resulting into gross loss rather than the

gross profit. Accordingly, he has charged the said expenses to profit and loss account and thereby levied minimum tax u/s 113 of the Ordinance, on gross turnover for the said both tax years. However, the authorities below have failed to discard the books of accounts and accounting principle as adopted by the taxpayer as no plausible explanation / justification was given while discarding the accounting methodology adopted by the taxpayer/company. Admittedly, the taxpayer company incorporated under the Companies Ordinance 1984, follows "accrual basis" of accounting as required under sub-section (2) of section 32 of the Ordinance. Rule, 32(2) of Part-III, Chapter – VII, 'General form of books of accounts, documents and records, of Income Tax Rules, 2002 requires as under:

"(2) The books of accounts, documents and records required to be maintained by a company in accordance with this Chapter shall be maintained in accordance with international accounting standards and as required under the Companies Ordinance, 1984."

Similarly, paragraph 38 of International Accounting Standard (IAS) 2 'Inventories' (purchases), defines 'cost of sales' as under:-

"38 The amount of inventories recognised as an expense during the period, which is often referred to as cost of sales, consists of those costs previously included in the measurement of inventory that has now been sold and unallocated production overheads and abnormal amounts of production costs of inventories. The circumstances of the entity may also warrant the inclusion of other amounts, such as distribution costs."

In the returns of income filed for tax years 2011 and 2012, the taxpayer has classified following significant costs as 'cost of sales' in its financial statements.

- Salaries of cashiers on cash counters, floor helpers, store managers, sweepers
- Electricity charges of retail stores
- Generator running costs at retail stores
- Freight charges incurred on purchase of goods
- Repair and maintenance of retail stores
- Rent of retail stores buildings
- Cost of bar code stickers affixed on goods, etc.

6. From the perusal of above, it is crystal clear that the taxpayer has rightly claimed the expenses under the head trading account in terms of sub-section (2) of Section 32 of the Companies Ordinance, 1984 and Rule 32 (2) of Part-III, Chapter VII, of the Income Tax Rules, 2002. The learned CIR (A) duly admitted in the body of his impugned order that the accounting methodology adopted by the taxpayer is correct as per accounting standards. It seems that the authorities below has misunderstood the nature of business of the taxpayer and has failed to discard the accounting methodology adopted by the taxpayer / company by giving any plausible reasoning. Therefore, we are of the firm opinion that the amendment of assessment as made by the assessing officer by resorting to the provisions of section 122 (5A) is not maintainable in the eye of law which is hereby cancelled for both the years under appeal. Order of the learned CIR (A) is accordingly vacated.

7. Appeals of the taxpayer succeed in the above manner.

SdL
(FIZA MUZAFFAR)
ACCOUNTANT MEMBER

SdL
(JAWAID MASOOD TAHIR BHATTI)
CHAIRMAN

Aftab