APPELLATE TRIBUNAL INLAND REVENUE, LAHORE BENCH, LAHORE.

ITA NO.703/LB/2014
(Tax Year 2006)

M/s. Zarco Exchange Company (Private) Limited., Lahore. .....Appellant

Vs

The CIR, RTO-II, Lahore. .....Respondent

Appellant by:- Sheikh Zulfiqar Ali, ITP

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

Date of hearing:-11-06-2014 Date of Order:-11-06-2014

ORDER

Titled appeal has been filed at the instance of the taxpayer calling in question the impugned order dated 30-11-2013 passed by the learned CIR(Appeals-II), Lahore.

2. Brief facts of the case are that the appellant, a private limited company, is principally engaged in the business of money exchange activities to deal in foreign currency notes, coins, postal notes, money orders, bank drafts, traveller cheques and transfers. The appellant is, licensed from State Bank of Pakistan under the Foreign Exchange Regulation Act, 1947. Return for tax year 2006, in the case of the appellant, was submitted on the due date and was deemed to be an assessment order issued under section 120 of the Income Tax Ordinance, 2001 ('Ordinance').The matter giving rise to the present appeal emanated from the earlier amendment order dated 30-03-2009 through which taxable income and the resultant tax liability was enhanced on various issues. Feeling aggrieved, the appellant filed appeal before the learned Commissioner Inland Revenue (Appeal-II), Lahore who vide order No. 38 dated 26-12-2011 remanded the case back to the concerned Additional

Commissioner Inland Revenue for de-novo consideration with the direction to provide proper opportunity of being heard.

In the context of the above, notice dated 25-02-2012 was issued by the Additional Commissioner Inland Revenue, Audit, Zone – VII, Regional Tax Office-II, Lahore ('ACIR') under section 122(9) read with section 122(5A) of the Ordinance, whereby intentions were shown to amend the assessment, earlier deemed to have been made under section 120 of the Ordinance, on the basis of various grounds stated therein. After availing adjournments and explaining the practical limitations faced by the appellant that the relevant documents/records were in the custody of the Federal Investigation Authority ('FIA'), the aforesaid show cause notice was responded to by the appellant through its Authorized Representative's letter TZE-2012/216 dated 6-12-2012, whereby appellant's position regarding the issues framed in the show cause notice was argued and explained in detail. The learned Taxation Officer/ACIR, however, feeling unconvinced by the arguments put forth by the appellant, in respect of various issues, proceeded on to amend the original assessment in terms of the provisions of section 122(5A) read with section 124 of the Ordinance through amendment order dated 01-01-2013 raising tax demand of Rs 30.192 million against the appellant.

The amendment order dated 1-1-2013 is presently impugned before this Tribunal through the following grounds of appeal:-

Ground of Appeal No. 3

The learned CIR (Appeals) was also not justified to confirm the addition made under the following heads:-

	Particulars	***Addition made (Rs)***
a.	*Initial depreciation*	*2,038,709*
b.	*Normal depreciation*	*533,791*
c.	*Addition u/s 21(n)on account of guest house expenses*	*4,537,804*

d.	*Addition u/s 21(n) pertaining to branch development expenses*	*5,178,274*
e.	*Provision for doubtful advances u/s 34*	*2,137,318*
f.	*Addition on account of business promotion expenses after amortization*	*6,149,535*
g.	*Commission income PTR @ 10 %*	*16,655,965*

3. At the outset the learned AR of the appellant has drawn our attention to the fact that the Additional Commissioner Inland Revenue, by simply ignoring that the relevant documents were in the custody of FIA, had concluded the impugned proceedings by merely considering the basis that *'no underlying details/documents to support the appellant's contentions were submitted'*. The appellant's position regarding availability of record etc has been explained both verbally to the concerned Additional Commissioner and also through various letters submitted on behalf of the appellant which are available on departmental record. Accordingly, proper opportunity of hearing was not given to the appellant. Notwithstanding this factual position, further submissions on behalf of the appellant are stated in the paragraphs to follow, with respect to each of the grounds of appeal:

4. a. **Admissibility of initial allowance – Rs.2,038,709**

The appellants' claim of initial allowance on building (Rs 389,104), Computers & Accessories (Rs 1,649,605) aggregating to Rs 2,038,709 has been rejected on the basis that the appellant is not eligible to claim initial allowance under section 23(1) of the Ordinance, since the status of the appellant was not that of a manufacturer and initial allowance is extended to

any taxpayer for the first time or the tax year in which commercial production is commenced.

In this respect, it is submitted that under the scheme of law providing for the admissibility of initial tax depreciation/deduction on account of 'assets' whose enduring benefit exceed one year ,entire amount expanded by a taxpayer is allowable against the income. For the purpose, under the provisions of section 22 & 23 of the Ordinance respectively deduction on the account of depreciation and initial allowance has been provided, rates whereof have been prescribed in third schedule of the Ordinance .The initial allowance/ depreciation are deducted from the cost to compute the 'written down value' for working out depreciation for subsequent tax year. Accordingly, the claim of initial allowance as deduction against income for the year did not affect the revenue on an overall basis as the aggregate quantum of the 'cost' admissible to the appellant was duly reduced by such initial allowance.

Notwithstanding the above submissions, it is contended that the Additional Commissioner contentions of 'claim of initial allowance only for a manufacturer' were never confronted earlier and the Revenue department had always accepted the claim of initial depreciation allowance on eligible depreciable assets for non-manufacturing companies as well. Strength in this regard could be further drawn from the relevant provisions of section 23(4) of the Ordinance, through which initial tax depreciation allowance in respect of owned eligible depreciable assets has been allowed by the legislature itself to a leasing company or an investment bank or a modaraba or a scheduled bank or a development finance institution (non-manufacturing companies).

In view of foregoing, the treatment adopted by the ACIR in the impugned order for disallowing the claim of initial allowance is unjustified which has been upheld by the learned CIR(A) without any basis, hence deleted being not tenable in the eyes of law.

5. **b. <u>Admissibility of normal depreciation – Rs.533,791</u>**

In the impugned order, while disallowing the initial depreciation allowance at page 2 of the impugned order, the ACIR has allowed the normal depreciation on the enhanced written down value of the assets (building, computers and accessories). However, while computing the taxable income, the effect of normal depreciation aggregating to Rs.533,791/- has not been considered vis-à-vis adjusted/reduced by the aforesaid amount while computing the amended taxable income.

This treatment, which is not tenable under the law and also against own treatment of the Additional Commissioner in the impugned order has also been upheld by the learned CIR(A) which is ordered to be deleted and the claim of normal tax deprecation along with the initial allowance is allowed.

6. c. **Admissibility of guest house expenses – Rs 4,537,804**

d. Admissibility of branch development expenses – Rs.5,178,274

Through the impugned order, the guest house expenses and branch development expenses aggregating to Rs 9,716,078 were disallowed, being devoid of documentary evidence and therefore not proved of being in the nature of revenue expenses, accordingly addition is made under section 21(n) of the Ordinance.

During the year under consideration, the appellant incurred expenses aggregating to Rs 4,537,804 under the head '**guest house expenses**' used to provide accommodation facility for its business visitors and claimed the same as deduction against income of the year. The nature of such expenses included 'usual upkeep' of the rent house, 'house-keeping' and 'maintenance' expenses necessary for preservation of the guest house in a liveable condition.

In respect of the '**branch development expenses**' amounting to Rs. 5,178,274 it is submitted that the appellant is undertaking its business through its branches; the nature of such expenses comprised the cost incurred

on interior decorations and domestication of the atmosphere for the clientele. Therefore, the expense is classifiable as incurred for the preservation/maintenance of the existing premises.

The learned A.R. averred at the bar that in view of the above explained position, it is very much clear that the useful life of such expenses did not exceed one year as the fashion and tastes change frequently in view of the specific requirements of the business, therefore, the above expenses incurred are revenue in nature and rightly claimed as period cost against income for the year. However, the concerned Additional Commissioner on the mere basis that no documentary evidence was provided to further support the claim of the appellant that the subject expenses were revenue in nature proceeded to disallow the said expenses under section 21(n) without giving any evidence contrary to the appellant's submissions. This practice has always been deprecated by the higher appellate authorities. The learned CIR(A) has failed o appreciate these facts and the legal position therefore the impugned order of the learned CIR(A) in this regard is vacated and for the foregoing reasons, the ACIR's order, is annulled to this extent and the expenses claimed by the appellant on account of 'guest house expenses' and 'branch development expenses' aggregating to Rs. 9,716,078 are allowed in full.

7. Regarding the admissibility of provisions for doubtful advances-Rs.2,137,318/- we have found the Taxation Officer has disallowed the clam for the reason that the advances which are claimed as doubtful recoveries amounting had never been offered for tax therefore the same cannot be deducted against the revenue of the business. Further, no documentary evidence has been provided to support the claim of the appellant, therefore the claimed amount is disallowed in preview of section 34(3) of the Ordinance.

On the other hand learned AR of the appellant argued that in order to meet the business requirements of the customers, your appellant acquired certain services of other exchange companies. In this connection, the appellant made advance payments to such exchange companies on behalf of

the customers which were duly settled within the prescribed period of time. However, during the year under consideration, an amount of Rs 2,137,316 (inadvertently written as Rs 6,149,535 in ground of appeal), earlier advanced to local exchange company could not be settled despite rigorous recovery/settlement efforts undertaken by the appellant's management. Consequently, such amount was charged to profit and loss account as 'provisions for doubtful advances' on the management's decision and adequately disclosed at notes 7.3 and 12 to the audited financial statements and rightly claimed by the appellant under section 20(1) of the Ordinance.

The claim of 'provision for doubtful advances/receivables' is also accepted by the honourable higher appellate authorities of Pakistan. Strength in this respect could be drawn from the Tribunal decision in **ITA Nos.1003/LB/08 and 1142/LB/08** dated 19-05-2009 where in following findings were recorded by the Tribunal:-

> *"...*
> *30. On the matter of **doubtful advances**, the learned AR relied upon 2009 PTD 121 which holds, in unequivocal that claim for doubtful advances is admissible deduction in computing taxable income and as such this claim should not be correlated with provisions of section 29 of the Ordinance. We fully agree that **such claim needs all the attributes of section 20 of the Ordinance** and is fully allowable under the provisions of law...." (emphasis is added)*

The above referred judgment of the Tribunal for allowing 'doubtful advances', has been reaffirmed through a latest consolidated order in **ITA Nos. 1567 and 1568/LB/2010** dated 01-03-2012 for tax years 2007 and 2009 in the case of another taxpayer. The relevant extracts of the judgment is reproduced below:

> *".....*
>
> *19. Coming to the claim regarding **provision for doubtful receivables**, we agree with the AR that the writing off a 'doubtful receivable' does not come within the domain of section 29 as this section deals with only those amounts of bad debts that have previously been offered to tax as income. This is not the case with doubtful receivables representing advances given to vendors. Since this **Tribunal has already dilated upon this issue in a number of judgments, including MA (AG) Nos.***

75 & 76 /LB/2009, ITA Nos. 495 & 496/LB/2009 and 2009 PTD (Trib.) 121 and decided the matter in favour of the taxpayer, *we following the earlier precedents allow the claim of the taxpayer company." (emphasis is added)*

In view of above reproduced clear findings of the Tribunal on the issue, disallowance of the appellant's claim on mere non production of documentary evidence is not justified. In view of the above, it is observed that the addition made by the Additional Commissioner on account of 'provision for doubtful advances' amounting to Rs.2,137,318 is deleted, being against the position settled by the appellate authorities as discussed above.

8. Regarding the admissibility on account of business promotion expenses – Rs. 6,149,535 and admissibility on account of advertisement expenses – Rs 14,486,495 which has been agitated through the additional ground we have found that through the impugned order, the Additional Commissioner disallowed the 'business promotion expenses' amounting to Rs 6,832,817 and 'advertisement expenses' amounting to Rs 16,096,105 on the basis that the appellant did not object the amortization of expenses carrying benefit for period extending beyond the tax year under consideration. Therefore the same are being amortized, allowing 10% expenses, adding back the balance expenses under section 24 of the Ordinance.

In this respect, it is submitted by the representation of the appellant / taxpayer that the appellant is engaged in a business of foreign exchange activities where severe competition exists, substantial business promotion, marketing /advertisement expenditure is a regular feature. These expenses are continuously and regularly incurred in order to increase its business and the resultant profits. In the context of the matter, we reiterate that it is essential to incur such expenses on a regularly basis and with short intervals and this is the only way to remain in and survive in the market. The effect of such advertisements, in terms of their impact on customers/consumers, can in no way be considered to last over a longer period, as the effect of new advertisements by competitors has to be mitigated

/ countered by way of new and continuous business promotion/marketing campaigns and advertisements. It, therefore, needs to be appreciated that the subject expenses could not be regarded as of enduring nature and the benefit thereof or useful life lasts for a very small span of time and does not, in any case, go beyond a period of year.

Needless to say that a conclusion as to 'enduring benefit' could only, and rightly so, be drawn in a case where expenditure is incurred only once for all times to come meaning thereby that the taxpayer need not to incur the same expenditure again and again as the expenditure so incurred would lend its benefit over future/coming periods as well.

The treatment of claiming promotion/ advertisement/ marketing activities, being revenue in nature, in the same tax year has also been accepted by the Tribunal in many other cases. Reliance in this regard could be placed on a reported judgement in **2009 PTD (Trib.) 1559**, where advertisement/marketing expenses were amortized over two years by the taxation officer on similar grounds. The matter, when taken up in appeals, was decided by both the Commissioner Inland Revenue (Appeals) and the Tribunal in favour of the taxpayer by holding that the subject expenses were permissible being revenue in nature. This position has again been reaffirmed by the Tribunal in another case **ITA No. 999/LB/2010** order dated 3-3-2012. Further reliance could also be placed on similar issue on a latest judgment of the Tribunal reported as **(2013) 107 Tax 389 (Trib.)**.

In view of the above findings of the Tribunal which are squarely applicable on the issue in hand, the contentions of the Additional Commissioner are not correct and contrary to the facts of the matter. The expenditure, being of revenue nature, is allowable as for-the-year deduction under section 20 of the Ordinance. Also, the appellant's treatment is in line with the practice followed in the preceding years, which has never been disputed by the tax authorities.

In view of the above submissions, it is observed that the treatment adopted by the officers below of amortizing the 'business promotion' and 'advertisement expenses ' at the rate of 10% under section 24 of the Ordinance merits deletion and the claim of such expenses is ordered to be allowed in full.

9. Regarding the Commission Income -Tax under PTR @ 10% - Rs 16,655,965/- it was argued by the learned DR that since the appellant has failed to substantiate its submissions through documentary evidence, therefore, the company's commission income amounting to Rs.166,559,657 was rightly required to be treated under the Final Tax Regime with the levy of tax @ 10%.

On the other hand learned AR of the appellant submitted that the action adopted by the Additional Commissioner involves core issue that requires deliberation whether appellant's commission income is subject to tax under section 233 of the Ordinance as income under Final Tax Regime ('FTR'). In case, the answer to such proposition is in affirmative, the amendment made in the impugned order shall be legally justified and otherwise the treatment adopted in return would not call for any interference.

Under the provisions of section 233(1) of the Ordinance, where a commission income is paid by government (i.e. federal, provisional or local), company or association of persons, such amount of income attracts the withholding of tax and the amount of tax deducted/collected is treated as final discharge of tax liability of the recipient in terms of sections 233(3)/169 of the Ordinance. There is no other view to above explained interpretation of section 233.

In the above explained provisions of law, since appellant earned commission income from persons (individuals) which have not been mandated / prescribed as withholding agents in section 233 of the Ordinance, thus, no amount of tax was collected against appellant's commission income. This

aspect is readily verifiable from appellant's return of total income for the year under consideration. Consequently, the appellant's commission income falls outside the scope of final tax regime provided for in the provisions of the section 233(3) of the Ordinance. In support of appellant's stance that its receipts of commission income have not been subjected to tax withholding under section 233 of the Ordinance and hence cannot be considered as income subject to tax under FTR in terms of section 233 read-with 169 of the Ordinance, reliance is placed on Tribunal's judgment reported as **2012 PTD (Trib.) 1478**. Relevant portion is reproduced below:

> *"We are further of the view that no deduction of income tax is involved in this case, rather the appellate has paid the advance tax under section 147 of the income tax ordinance, 2001 against the further income of the respective tax year and since no deduction of the income tax has been effected by the payer in this case, therefore, the provisions contained in section 169 of the income tax ordinance, 2001 are not attracted in this case."*

In view of clear and unambiguous findings of the Tribunal, the action of the Additional Commissioner of treating the commission income subject to Final Tax Regime ('FTR') is not justified as this income was neither subject to tax withholding under section 233 of the Ordinance nor did it undergo tax deduction/collection. For the foregoing reasons and case, we are of the view that the action of the officer below in the impugned order being not tenable under the law, hence the addition made is hereby deleted.

10. The appellant has also framed an additional ground that

"Without prejudice to ground No. 2 & 3 above, the learned Additional Commissioner Inland Revenue has erred in not allowing the credit of taxes paid for the year under consideration."

In this respect we are of the opinion keeping in view the above discussed facts that the Additional Commissioner Inland Revenue was not justified to disallow the credit of taxes paid merely due to non-submission of documentary evidence due to the practical limitation being faced by the

appellant and already explained that the record/underlying documents were impounded by the FIA authority/State Bank of Pakistan. The treatment of the Additional Commissioner of not allowing the law full right of the appellant is not tenable under the law and therefore merits deletion.

16. Under the circumstances, the impugned order is vacated and the declared version of the appellant is ordered to be accepted.

Sd/-
(JAWAID MASOOD TAHIR BHATTI)
CHAIRPERSON

Sd/-
(FIZA MUZAFFAR)
ACCOUNTANT MEMBER