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Judgment Sheet

IN THE LAHORE HIGH COURT LAHORE
JUDICIAL DEPARTMENT

Case No: W.P. 17893/2013

Pakistan Fruit Juices Co. (Pvt.) Ltd., etc. **Versus** Federation of Pakistan, etc.

JUDGMENT

Date of hearing	19.05.2014
Petitioners by	M/s. Salman Akram Raja, Sameer Khosa, Munawar-us-Salam, Rana Muhammad Afzal, Waseem Ahmad Malik, Majid Ali Wajid, Advocates
Respondents by:	M/s. Naseer Ahmad Bhutta, Additional Attorney General for Pakistan alongwith Muhammad Mahmood Khan and Mian Irfan Akram, Deputy Attorney Generals for Pakistan. Mr. Nadeem Mahmood Mian, Standing Counsel. M/s. Muhammad Ilyas Khan, Abdul Hafeez Pirzada, Jawad Hassan, Mian Gul Hassan Aurangzeb, Hamid Ahmad, Shahid Pervaiz Jami, Tariq Saleem Sheikh, Muhammad Asif Hashmi, and Ch. Muhammad Anwar Bhor Advocates. Dr. Hamid Ateeq, Commissioner Inland Revenue, LTU, Lahore.

Syed Mansoor Ali Shah, J:- This consolidated judgment shall decide the instant petition, as well as, writ petitions mentioned in Schedule A, as common questions of law and facts arise in these cases.

2. Petitioners, who are manufacturers and suppliers of aerated waters / beverages have challenged the constitutionality and legality of The Federal Excise Duty and Sales Tax on Production Capacity (Aerated Waters) Rules, 2013 ("**Rules**") introduced through Notification dated 09.07.2013 (SRO.No.649(I)/2013) and

subsequently amended through Notification dated 28.02.2014 (SRO No. 140(I)/2014).

3. Salman Akram Raja, Advocate, leading the argument on behalf of the petitioners submitted that the impugned Rules allegedly impose *Capacity Tax* under section 3 (1A), (1B), (6) and section 50 of Sales Tax Act, 1990 ("STA") and sections 3(3)(a) and 40 of Federal Excise Act, 2005 ("FEA") *in lieu* of the sales tax and excise duty being charged under sections 3(2) of STA and 3(1) of FEA. He argued that section 3(1B) of STA permits a restrictive substitution of *Capacity Tax* limited to sales tax charged under section 3(1) only. While the impugned Rules impose *Capacity Tax in lieu* of sales tax being charged under section 3(2)(a) making these *ultra vires* Section 3 (1B) of STA. It is submitted that substituting sales tax charged under section 3(1) of STA with *Capacity Tax* does not mean that sales tax charged under section 3(2)(a) also stands substituted as both the charging sections are distinct and separate. Taxable supplies of the petitioners fall under the Third Schedule to the STA and are charged to sales tax on the basis of *retail price* [under section 3(2)(a)], instead of, *value of taxable supplies* [under section 3(1)]. Charge of sales tax on the basis of Retail Price is a distinct taxing regime under STA and has to be specifically substituted through clear and unambiguous legislation.

4. Learned counsel drawing a parallel with earlier cases decided on a similar legal issue, referred to *"Northern Bottling Co. (Pvt.) Ltd. v. Government of Pakistan, Ministry of Finance, Pakistan Secretariat, Islamabad through the Secretary Finance and 2 others"* **(2000 PTD 870)** and *"Tandlianwala Sugar Mills Ltd. and others v. Federation of Pakistan through Secretary, Ministry of Finance, Revenue and Economic Affairs, Islamabad and others"* **(2001 PTD 2094)**. In these cases, the matter that came up before the Court was in the context of

Section 3 (1A) of the STA whereby *further tax* was imposed *in addition to* the rates specified in specific sub-sections. It was held that *further tax* was not applicable to cases which did not find specifically mentioned in Section 3 (1A) reinforcing the independent and distinct character of different charging sections under section 3 of STA.

5. Mr. Abdul Hafeez Pirzada, Advocate, representing some of the private beverage companies supporting the Rules, referred to entries No.49 and 52 of the Federal Legislative List of the Constitution to submit that the tax on production capacity of plants or *Capacity Tax* enjoys constitutional support and section 3 (1B) of STA carries the constitutional sanction to automatically replace all the different charging sections under section 3 of the STA, hence the impugned Rules, being all embracing, even replace the distinct taxing regime based on retail price under section 3(2)(a) of the STA.

6. Dr. Hamid Ateeq, Commissioner Inland Revenue, LTU, Lahore submitted that there are four separate charging sections under Sales Tax Act namely; sections 3 (1), 3(1A), 3 (2) (a) and 3 (6). He submits that, inspite of the same, the principal charging section is section 3 (1) while the remaining charging sections are mere sub-sets of the main charging section. Hence, section 3(1B) replaces all the charging sections under STA. Without prejudice to the above he further submits that the impugned Rules have been jointly promulgated *in lieu* of sales tax and federal excise duty and there being no parallel provisions to section 3(2) (a) under the FEA, the impugned Rules to the extent of Federal Excise Duty are valid and should be allowed to continue. Learned counsel for the FBR, the Federation and the Attorney General[1] adopted the arguments of the learned counsel for the private respondents.

[1] put on notice under Order 27-A CPC vide order dated 17.09.2013

7. Learned counsel for the petitioner in rebuttal submitted that the impugned Rules jointly replace sales tax and federal excise duty with a composite amount of *Capacity Tax*, hence they are not severable or operable independently. He referred to Rule 4 of the Rules to submit that there is a consolidated *Capacity Tax* on the rate per filling value or spout and the Rules do not provide for any mechanism to separate the two taxes. He further referred to Rule 6 to submit that the adjustment of input tax is available against the consolidated amount mentioned under Rule 4, but the Rules cannot be severed on this ground, therefore, if the impugned Rules are declared *ultra vires* the STA, the Rules as a whole stand declared *ultra vires*.

8. Opposing contentions of the parties have been heard and deliberated upon. Before examining the vires and legality of the impugned Rules, it is important to visit and understand the constitutional and legislative construct of *Capacity Tax* under the law. The constitutive genesis of *Capacity Tax* is found in *entry 52* of the Federal Legislative List (4th Schedule) to the Constitution, which states:

> "52. Taxes and duties on the production capacity of any plant, machinery, undertaking, establishment or installation **in lieu of the taxes and duties** specified in entries 44, 47, 48 and 49 or **in lieu of any one or more of them**." *(emphasis supplied)*

The above enables the Federal Legislature to impose *Capacity Tax* on the *production capacity* of a plant, machinery, undertaking, establishment or installation *in lieu* of the taxes and duties provided under all or anyone of the following entries: 44 (Excise Duty), 47 (Income Tax), 48 (Taxes on Corporations) and 49 (Sales Tax). In other words Federal Legislature enjoys the legislative competence to replace the existing sales tax, federal excise duty or any other tax mentioned above, with a new singular tax known as the *Capacity Tax.*

9. Incidence of *Capacity Tax* is on the *production capacity* of a plant, machinery, establishment, etc, hence characteristically and constitutionally, *Capacity Tax* is a new specie of tax, different from the taxes and duties mentioned above. Unlike other taxes, *Capacity Tax* pre-supposes the existence of levy of the abovementioned taxes and duties. The phrase "in lieu of" means "instead of", "in place of", "in substitution for."[2] "In lieu of" implies existence of something for which a substitution is being made.[3] In *Elahi Cotton case,* the apex court has explained the term *in lieu of* in the following manner:

"34… However, we may point out that in Entry 52, the key words used are "in lieu of taxes and duties specified in entries 44, 47, 48 and 49 or in lieu of any one or more of them". In order to understand the real import of the above portion of Entry 52, we will have to refer to the meaning of the words "in lieu of". In this regard, reference may be made to Black"s Law Dictionary, Sixth Edition, Ballentine"s Law Dictionary, Third Edition; and the Legal Thesaurus by Steven C. De Costa, which read as follows:---

Black"s Law Dictionary, page 787:

"In lieu of": Instead of; in place of; in substitution of. It does not mean "in addition to".

Ballentine"s Law Dictionary, page 628:

"In lieu of"; Proposition as a substitute for, as an alternative, by proxy or, in place of, instead of, on behalf of, rather than, representing.

35. A perusal of the above-quoted meanings of the above expression "in lieu of" indicates that the same connote, instead of, in place of, in substitution of, but it does not mean, in addition to. *(emphasis supplied)*

If we were to construe Entry 52 of the Legislative List keeping in view the above meanings of the expression "in lieu of", it becomes evident that the Legislature has the option instead of invoking Entry 47 for imposing taxes on income, it can impose the same under Entry 52 on the basis of capacity to earn in lieu of Entry 47, but it cannot adopt both the methods in respect of one particular tax. Since under section 80-C and 80-CC the imposition of presumptive tax is in substitution of the normal method of levy and recovery of the income tax, the same is in consonance with Entry 52.[4]"

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[2] Words and Phrases, Permanent Edition, Volume 21A p.187
[3] Ibid p.188
[4] *"Elahi Cotton Mills Ltd. v. Federation of Pakistan* **(PLD 1997 Supreme Court 582)** Pp.682-683

10. Explaining the scope of *Capacity Tax*, august Supreme Court of Pakistan in *Seven Up Bottling* case held as under:[5]

> "The authority to levy excise duty by the Federal Government (hereinafter to be called as the Government") on goods is derived under Entry No.44 of the Federal Legislative List of the Fourth Schedule (hereinafter to be called as „the List") to the Constitution of Islamic Republic of Pakistan (hereinafter to be referred as „the Constitution" only). The Government is further authorized to levy taxes and duties under Entry No.52 of the list on the basis of production capacity of any plant, machinery, undertaking establishment or installation, in lieu of taxes and duties leviable under Entries Nos.44, 47, 48 and 49 of the List. The two different modes of levy of excise duty by the Government under the Constitution are, therefore, mutually exclusive. The Government, may, accordingly, elect to impose excise duty on any one of the two modes mentioned above. As a necessary corollary, therefore, it follows that where the Government decided to recover excise duty on the basis of production capacity of plant, machinery etc. it could not demand the excise duty on the basis of actual production of goods. Sections 3 (1) and 3(4) of the Act enact these two alternative principles for levy of excise duty on goods envisaged by Entries Nos. 44 and 52 of the List of the Constitution. The rational behind these two mutually exclusive modes of levy of excise duty on goods is quite obvious; when the excise duty is recovered on the basis of actual production of goods under section 3 (1) of the Act, the production capacity of the plant, machinery etc. has no relevancy at all. Similarly, when excise duty is sought to be imposed on the basis of production capacity of plant, machinery etc. the actual production of goods becomes irrelevant.

Capacity Tax, therefore, replaces or substitutes, the earlier levy in force, under the aforementioned laws. *Capacity Tax* is not to co-exist with the existing tax but infact supplants and replaces the existing taxing regime and its philosophy with the new taxation theme of production capacity. In other words the existing tax is rendered dysfunctional and ineffective alongwith its supporting legal framework comprising the statute, rules, notifications, etc and the new tax regime of *Capacity Tax* takes over, as if repealing the existing tax regime.

11. While Entry 52 of the Federal Legislative List provides legislative space to the Federal Legislature to impose *Capacity Tax*,

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[5] *"Central Board of Revenue and 3 others v. SEVEN-UP Bottling Company (Pvt.) Ltd."* **(1996 SCMR 700)** p.705

the finer design, structure and extent of its applicability remains solely within the prerogative of the Federal Legislature. Therefore, the shape of the new *Capacity Tax* may substitute the entire existing tax(es) or restrict the substitution to a particular specie of tax within the existing taxes.

12. It is axiomatic that *Capacity Tax* like any other tax would require an independent and comprehensive legislative framework which embodies its essential components like: *levy, assessment and collection*, *etc.* In the present case, *Capacity Tax* has been imposed through singular provisions i.e., section 3(1B) under the STA and section 3(3)(a) of the FEA, reproduced hereunder for reference:

Section 3 (1B) of the Sales Tax Act, 1990: Scope of tax:

(1B) The Board may, by notification in the official Gazette, *in lieu* of levying and collecting tax under sub-section (1) on taxable supplies, levy and collect tax –

(a) on the production capacity of plants, machinery, undertaking, establishments or installations producing or manufacturing such goods; or

(b) on fixed basis, as it may deem fit, from any person who is in a position to collect such tax due to the nature of the business.

Section 3 (3) (a) of the Federal Excise Act, 2005: Duties specified in the First schedule to be levied.

(3) The Board may, by notification in the official Gazette, in lieu of levying and collecting under sub-section (1) duties of excise on goods and services, as the case may be, levy and collect duties, --

(a) on the production capacity of plants, machinery, undertakings, establishments or installations producing or manufacturing such goods; or

13. With this constitutional and legislative architecture of *Capacity Tax* , I examine the arguments of the learned counsel for the parties. Section 3(1B) provides for substitution of capacity tax *in lieu* of tax provided under section 3(1) of STA. Section 3, otherwise, encapsulates a basket of charging sections, imposing distinct variants

of sales tax along with their peculiar procedure and mechanism. Section 3(1) provides for charge of Sales Tax on the VALUE of taxable supplies, while section 3(2)(a) provides for charge of sales tax on the RETAIL PRICE of the taxable supplies. Section 3(5) imposes EXTRA RATE OF TAX in addition to section 3(1) while Section 3(6) empowers the Federal Government and the Board to impose SUCH AMOUNT OF TAX AS IT MAY DEEM FIT in lieu of sales tax under Section 3(1), section 3(8) imposes special tax on CNG stations. Legislature in its wisdom under Section 3(1B) has substituted just one set of the charging sections i.e., Section 3 (1) from amongst the above-mentioned basket of charging sections provided under the STA. Every charging section maintains an insular independent status. Reference is also made to sub-sections 3(1A), 3(5) and 3(6) of STA, which clearly mark with precision the sub-sections they replace or substitute. Hence legislation must specifically provide for substitution. Legislature could have replaced section 3(2)(a) under Section 3(1B) but it has not. Even otherwise, any such intention could have been easily actualized by the Federal Government by invoking the *Proviso*[6] to section 3(2)(a) and taking out aerated waters from the Third Schedule, but this was not done. Hence, section 3(1B) only replaces sales tax imposed on the basis of VALUE of taxable supplies and does not extend or replace the other charging sections including section 3(2)(a), where taxable supplies are taxed on RETAIL PRICE. The impugned Rules state that *Capacity Tax* is *in lieu of* tax imposed under section 3(2) of STA when section 3(1B) unambiguously limits the substitution to section 3(1) of STA only. Therefore, it is clear that the *Capacity Tax* under the impugned Rules does not extend to sales tax being charged under section 3(2)(a) of STA as a consequence the

[6] "Provided that the Federal Government, may, by notification in the official Gazette, exclude any taxable supply from the said Schedule or include any taxable supply therein; and"

impugned Rules, therefore, transgress the limits provided under section 3(1B) of STA.

14. While Section 3(1B) limits the scope of *Capacity Tax* to section 3(1) of STA, no such parallel provision exits under FEA. The Commissioner Inland Revenue argued that the impugned Rules are, therefore, valid and functional to the extent of Federal Excise Duty. There is no doubt that *Capacity Tax* can be imposed separately for all or any of the taxes and duties mentioned in Entry 52 of the Federal Legislative List. However, in this peculiar case, the construct of *Capacity Tax* substitutes and replaces sales tax and federal excise duty jointly. The amount of *Capacity Tax* under Rule 4 of the impugned Rules is in substitution for both sales tax and excise duty, hence severance of the Rules is not possible without rendering the Rules inoperable. Rules 6 and 8 do not improve the position in any manner. The impugned Rules will have to be reconfigured, with *Capacity Tax* replacing Federal Excise Duty only, if they need to survive under FEA.

15. In view of the above discussion, I hold that the impugned Rules (SRO No. 649(I)/2013 and SRO No. 140 (I)/2013) are *ultra vires* section 3(1B) of the Sales Tax Act, 1990 and cannot be extended to the taxing regime based on RETAIL PRICE provided under section 3(2)(a) of STA and are, therefore, illegal and without lawful authority. The impugned Rules impose *Capacity Tax* *in lieu* of sales tax and federal excise duty jointly in a consolidated manner, therefore, the Rules are not severable and hence are equally ineffective and invalid under the FEA.

16. There are other worrying questions which have surfaced while examining the constitutionality and legality of the impugned Rules. I place them for further deliberation of the FBR

A). Whether imposition of *Capacity Tax* under section 3(1B) of STA or 3(3)(a) FEA replaces sales tax or federal excise duty alongwith its supporting statutory legal framework ?

B). Whether section 3 (1B) of STA or Section 3 (3) (a) of EFA carry sufficient guidelines for the selection of plant of aerated waters or other plants?

C). Whether section 3(6) of STA is available to the new *Capacity Tax* or is it a separate charging section under STA authorizing Federal Government or the Board to levy a new specie of tax *in lieu* of section 3(1) of STA

17. For the above reasons, the instant petition, as well as, the connected petitions are allowed in the above terms with no order as to costs. Petitioners shall, however, continue paying Sales Tax and Excise Duty under the provisions of STA and FEA in accordance with law.

(Syed Mansoor Ali Shah)
Judge

Iqbal

APPROVED FOR REPORTING

SCHEDULE A

Sr. No.	Case Number
1.	W.P. No.9195/2014
2.	W.P. No.20804/2013
3.	W.P. No.19274/2013
4.	W.P. No.18834/2013
5.	W.P. No.19270/2013
6.	W.P. No.20461/2013
7.	W.P. No.22080/2013
8.	W.P. No.8437/2014
9.	W.P. No.10774/2014
10.	W.P. No.18101/2013

(Syed Mansoor Ali Shah)
Judge

Iqbal