102 TAT 5/14 recalled and reversed 1025

22(K) ie Rs 50000 expenditure on applicable to P&L A/c

APPELLATE TRIBUNAL INLAND REVENUE (PAKISTAN) KARACHI

ITA No.468/KB/2010
(Tax Year 2007)

M/s. Farhan Food Industries. Appellant.

Versus.

The CIT, Audit Division-II, RTO, Karachi. Respondent.

Appellant by	:	Mr. Abdul Khaliq, Advocate.
Respondent by	:	Mr. Sajidullah Siddiqui, DR.
Date of hearing	:	20.10.2010
Date of order	:	25.10.2010.

ORDER

This appeal has been filed by the taxpayer/appellant against the order of the learned CIR(A) which was decided on 09.08.2010 vide ITA No.468/KB 2010. However M.A was filed by the appellant wherein it was contended that power of attorney in favour of Mr. Muhammad Fareed, Advocate was cancelled on 28.06.2010. Hence his representation was unauthorized. The M.A was decided by this Tribunal and main appeal was recalled vide ITA NO.311/KB/2010 dated 30.09.2010 to give proper opportunity of hearing to the appellant.

2. The appeal has been filed on the following grounds.

"1. *That the Order passed by the CIT Appeal Zone-II Karachi is bad in law and on facts.*

2. *That the learned CIT Appeal has erred in confirming the order passed u/s.122(1)(5) of the Income Tax Ordinance 2001 by the taxation officer/inland revenue officer audit-20 audit division II R.T.O Karachi, wherein he has added purchases made by the assessee of wheat in cash from the farmers to the tune of Rs.60,864,447/- on the plea that since these are made in cash so these are disallowed being more than Rs.50,000/- u/s.21(1)(L) of the income tax ordinance 2001 read with para-6 of CBR Circular No.2006 date 01.07.2006 hence these are not allowed.*

3. *That section 21(l) reads as under:-*

> *"(l) any expenditure for a transaction, paid or payable under a single account head which, in aggregate, exceeds fifty thousand rupees, made other than by a crossed cheque drawn on a bank or by crossed bank draft or crossed pay order or any other crossed banking instrument showing transfer of amount from the business ban k account of the taxpayer:*

4. *This sub section (l) talks any expenditure not of purchases so the learned taxation officer and the learned commissioner of income tax (Appeal) are wrong in ready purchases in the words any expenditure which does not includes purchases.*

5. *That the Taxation Officer and the appellate Commissioner could not under stand section 20 & 21 of the Income Tax Ordinance, 2001.*

6. *That section 20 of the Income Tax Ordinance 2001 shows as to how first the gross profit of income from business is to be worked out by deducting purchases*

from the sales where as section 21 talks of expenses to be not allowed from the gross profit as worked out u/s.20. It enumerates such expenses which are not allowed as deduction from gross profit. Section 20 Sub section (l) talks of such expenditure for transaction paid or payable under a single account head which in aggregate exceeds fifty thousand rupees, made other than by a crossed cheque drawn on a bank or by Cross bank draft or crossed pay order or any other crossed pay order or any other crossed banking instrument showing transfer of amount.

7. *That sub section (l) does nowhere talks of purchases. It speaks of only expenditure not of purchases which are considered under section 20 in working out gross profit which is worked out by deducting the purchased from sales.*

8. *Thus both taxation officer and learned commissioner of income tax Appeal Zone II were wrong in reading purchases in any expenditure mentioned in sub section (L) which talks of any expenditure for a transaction (which does not include purchases)."*

3. Gist of the case is to determine whether purchases can be added to the income of the assessee for non-compliance of provision of section 21(1)?

4. Mr. Abdul Khaliq, learned AR of the appellant arguing the case has contended that method of computing the taxable income of a person has been enshrined in Section 20 of the Income Tax Ordinance, 2001 where it has been provided that a deduction shall be allowed for any expenditure incurred by a person and "an override" has been given in section 21 which speaks of deductions only. The word DEDUCTION has not been defined in the Income Tax Ordinance, 2001. However, same is defined in Black's Law Dictionary as under:-

> *"a. Deduction. 1. The act or process of subtracting or taking away. 2. Tax. An Amount subtraced from gross income when calculating adjusted gross income when calculating taxable income."*

5. The word deduction has been interpreted by in Principles of Income Tax Law with International Tax Glossary (Third Revised Addition 2003) as under:-

> *"In its most common usage "deduction" denotes, in an income tax contest, an item which is subtracted (deducted) in arriving at, and which therefore reduces, taxable income, Usually deductions are granted in recognition of some expenditure or loss incurred or to be incurred by the Taxpayer, and perform the function, very broadly speaking, of reducing gross income to net income or profit.*
>
> *Tax legislation normally provides that certain expenditures are to be allowed as deductions while other are not. This may be by way of a general provision which, for example, allows deductions only for expenditure incurred for certain purposes (typically business purposes) or by way of specific provisions disallowing or allowing particular kinds of expenditure. For example, entertainment expenditure or bad debts not actually written off may be specifically disallowed as deductions (See: Bad debt). Deduction are also sometimes granted in fixed amounts, for example, a wear and tear allowance in respect of rented property, where the deduction given is a fixed percentage of rental income received.*
>
> *"Deduction" is also used to describe an amount which is to be subtracted from the tax otherwise payable – alternatively referred to as a credit or rebate (See: Credit, tax). A deduction in this sense, of course, provides the taxpayer with a reduction in tax payable*

equal to the amount of the deduction. whereas a deduction in the first sense will only reduce tax payable to the extent of the deduction multiplied by the tax rate."

6. From the above meanings of the word deduction it is crystal clear that Section 21(l) can only deal with the expenses debatable to P&L account. A careful reading of all the provisions of Section 21 shows that the entire section deals with expenses debitable to profit and loss account and even if it is to cover trading account, it will touch only deductions like rent, wages, fuel, commission, interest, Salary (relating to manufacturing cum trading account). And purchases cannot be termed as deductions, by any stretch of imagination, within the meaning of Section 21.

7. The learned AR contended that in such like situations doctrine of EJUSDEM GENERIS is squarely attracted and courts have happily acknowledged and approved the same in a large number of cases. Reliance is placed on the judgments of Honorable Supreme Court of Pakistan reported as PLD 2000 S.C 111 and High Court in the case of Prime Commercial Bank and other vs. ACIT reported as (1997) 75 Tax 1 (H.C.Lah.).

8. The Hon'ble Apex Court observed in judgment reported as PLD 2000 S.C 111 as under:-

> *"The doctrine of ejusdem generic is well-settled. It means that where general words follow an enumeration of persons or thing, by words of a particular and specific meaning such general words are not to be construed in their widest extent, but are to be held as applying only to persons or things of the same general kind or class as those specifically mentioned."*

9. In another case reported as 75 Tax 1, the Hon'ble High Court held as under:-

> *"..... the provision itself which is read as a whole leaoves no room to hold that the words (special deposit receipt) must be interpreted ejusdem generis and must take colour from the preceding and subsequent words."*

10. Learned AR of the appellant contended that purchase cannot be treated as deductible expenses within the meaning & scope of Section 21. He further argued that the revenue has accepted the entire Sales of the appellant, therefore, entire action of the Taxation Officer in contradictory as he has accepted the sales which fact itself testifies that there were purchases which turned into sales. If there were no purchases, wherefrom sales came? Further if trading account is re-casted after rejecting purchases, the G.P rate will go as high as 50% which in this line of business is just impossible.

11. The learned AR of the appellant further argued that even otherwise all the purchases of wheat were made from different areas of the country. He produced

copies of truck builties showing movement of the goods. According to learned AR the purchases are made directly from growers and they (grower) do not accept cheques. The taxpayer is left with no alternate but to make cash payments. In such a situation there are two options for the taxpayer i.e. either to close his business or make cash payment to sellers (growers) to run the flour mills. The taxpayer has no control over the situation. In such a situation the taxpayer cannot be termed as defaulter (non-complier of law). He contended that courts cannot ignore the ground realities while deciding an issue involving unavoidable circumstances. The AR in support of his argument placed reliance on a judgment of learned ATIR reported as 1999 PTD 1302. The learned ATIR while deciding the appeal observed as under:-

"Expression default connotes an element of will ful and deliberate failure to fulfill an obligation and negligence in the performance of the duty. Every failure on the part of a person without any ulterior design and mala fide intention would not equate with the expression default as used in its strict legal sense. Before a person is declared to be in default, it is absolutely necessary that there should have been a demand to make payment of a determined sum which should have remained un-responded and unattended for a period beyond the period prescribed by law. Issue of default in the context of Rent Laws was set at rest in the famous case reported as Ghulam Muhammad Lundkhor vs. Safder Ali (PLD 1967 SC 530). In the words of the apex Court the word default in legal terminology necessarily imports an element of negligence or fault and means something more than mere non-compliance. To establish default one must show that the non-compliance has been due to some culpable cause for a person who ought not to be

made liable for a failure due to some cause for which he is, in no way, responsible or which was beyond his control. It is not lightly to be presumed that the law intends to cause injustice or hardship, thus, unless the Legislature has made its intention clear that construction must be preferred which will prevent manifest injustice and obviate hardship. On this principle also the expression default should mean an act done in breach expression default should mean an act done in breach of a duty or in disregard of an order or direction. This view was followed in the subsequent cases reported as Muhammad Hassan Khan vs. Mirza Abdul Hamid (1981 SCMR 799), Irshad Hussain vs. Abdul Rehman Kazi (1983 SCMR 471), M. Imamuddin vs. Surriya Khanum (PLD 1991 SC 317) and NDFC vs. Naseemuddin (PLD 1997 SC 564)."

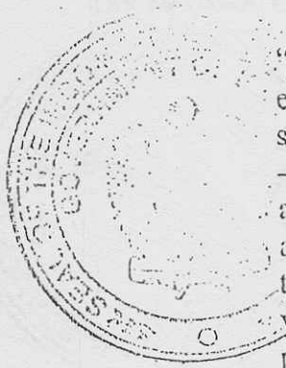
12. In another case reported as 28 Tax 181 (H.C Lah.), the Hon'ble High Court held as under:-

"If a person is required by law to do something which becomes impossible for him to do, not on account of his own negligence or fault, but on account of something which was unavoidable and in any case not subject to his control, he cannot be said to have failed to perform that which the law or and order passed under the law required him to do."

13. It was argued by the learned AR of the appellant that the Taxation Officer has failed to point out even a signal defect in the books of accounts produced at the time of hearing except the alleged cash purchases of wheat to the tune of Rs.60,864,447/- out of total purchases of Rs.135,358,068/-. Suffice to say that the appellant is a law compliant person and has made purchases on cash

payment from growerers on the situation which was beyond his control and therefore he cannot be penalized for an act which was not under his control.

14. The learned AR of the appellant further contended that taxation should be in accordance with law, fair and justifiable, the taxpayer should not be destroyed by using taxing powers to get more and more tax from the businessmen. Reliance in this regard has been placed on the famous case of Ellahi Cotton Mills Ltd. Vs. Federation of Pakistan reported as 76 Tax 5 (S.C). The Hon'ble Apex Court held that (head note):-

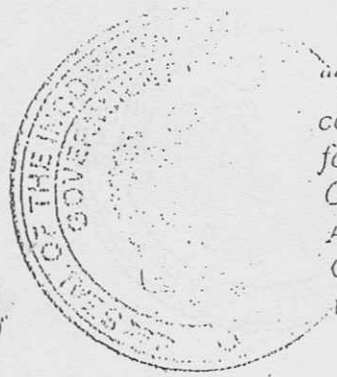


> "Taxation - Validity - Power t tax cannot be used to embarrass and destroy the business/occupation *which* are since qua non for the prosperity of the people and the country – Taxes should not be expropriator and confiscatory in nature and should not be imposed in such a way so as to result in acquiring properties of those to whom the incidence of taxation fell and if that is so, then such legislation would be violative of fundamental rights to carry on business or to hold properties as guaranteed by the Constitution."

15. It was further contended by the learned AR of the appellant that facts and circumstances were beyond the control of the appellant as such the taxpayer cannot be taxed merely on the ground that he did not make the payments of wheat purchased through banking channel.

16. The learned DR on the other hand supported the impugned order of the ACIR & CIR(A). He argued that the Taxation Officer had rightly disallowed the purchases as the payment were made in cash and as per Circular No.1 of 2006 dated 01.07.2006 issued by CBR and incorporated in the body of order, the CBR has clarified that the purchases are also covered u/s.21(L) of the Income Tax Ordinance 2001.

17. The learned AR of the appellant vehemently argued that Interpretation of law is not the domain of CBR Reliance has been placed on a case reported as 68 Tax 86 (SC). Their lordships in the above referred case have held as under:-



"The interpretation of any provision of the Ordinance can be rendered judicially by the hierarchy of the forums provided for under various sections of the Ordinance, namely, the Income Tax Officer, Appellate Assistant Commissioner, Appellate Tribunal, High Court and this Court and not by the CBR. Therefore, interpretation of statute is not CBR's domain."

18. The learned AR further added that as per Plain and simple reading of the provisions of section 21 one can safely say that it deals only with deductions only.

19. We have heard the rival parties, perused the case law cited on bar and the case record available in this Court. Before parting with the issue involved, it would be more appropriate if the provision of section 20 & 21 are reproduced here to arrive at some fair conclusion and know the exact intention of the legislature:-

"20. **Deductions in computing income chargeable under the head "Income from Business".**— (1) Subject to this Ordinance, in computing the income of a person chargeable to tax under the head "Income from Business" for a tax year, a deduction shall be allowed for any expenditure incurred by the person in the year 2[wholly and exclusively for the purposes of business].

[(1A) Subject to this Ordinance, where animals which have been used for the purposes of the business or profession otherwise than as stock-in-trade and have died or become permanently useless for such purposes, the difference between the actual cost to the taxpayer of the animals and the amount, if any, realized in respect of the carcasses or animals.]

(2) Subject to this Ordinance, where the expenditure referred to in subsection (1) is incurred in acquiring a depreciable asset or an intangible with a useful life of more than one year or is pre-commencement expenditure, the person must depreciable or amortise the expenditure in accordance with sections - 22, 23, 24 and 25."

4[(3) Subject to this Ordinance, where any expenditure is incurred by an amalgamated company on legal and financial advisory services and other administrative cost relating to planning and implementation of amalgamation, a deduction shall be allowed for such expenditure.]"

"21. **Deductions not allowed.** – Except as otherwise provided in this Ordinance, no deduction shall be allowed in computing the income of a person under the head "Income from Business" for – (a) any cess, rate or tax paid or payable by the person in Pakistan or a foreign country that is levied on the profits or gains of the business or assessed as a percentage or otherwise on the basis of such profits or gains;

(b) any amount of tax deducted under Division III of Part V of Chapter X from an amount derived by the person;

(c) *any salary, rent, brokerage or commission, profit on debt, payment to non-resident, payment for services or fee paid by the person from which the person is required to deduct tax under Division III of Part V of Chapter X or section 233 of chapter XII, 1[unless] the person has 2[paid or] deducted and paid the tax as required by Division IV of Part V of Chapter X;*

(d) *any entertainment expenditure in excess of such limits 3[or in violation of such conditions] as may be prescribed;*

(e) *any contribution made by the person to a fund that is not a recognized provident fund 4[approved pension fund], approved superannuation fund, or approved gratuity fund;*

(f) *any contribution made by the person to any provident or other fund established for the benefit of employees of the person, unless the person has made effective arrangements to secure that tax is deducted under section 149 from any payments made by the fund in respect of which the recipient is chargeable to tax under the head "Salary";*

(g) *any fine or penalty paid or payable by the person for the violation of any law, rule or regulation;*

(h) *any personal expenditures incurred by the person;*

(i) *any amount carried to a reserve fund or capitalized in any way;*

(j) *any profit on debt, brokerage, commission, salary or other remuneration paid by an*

association of persons to a member of the association;

(k) any expenditure for a transaction, paid or payable under a single account head which, in aggregate, exceeds fifty thousand rupees, made other than by a crossed cheque drawn on a bank or by crossed bank draft or crossed pay order or any other crossed banking instrument showing transfer of amount from the business bank account of the taxpayer:

Provident that online transfer of payment from the business account of the payer to the business account of payee as well as payments through credit card shall be treated as transactions through the banking channel, subject to the condition that such transactions are verifiable from the bank statements of the respective payer and the payee:

Provided further that this clause shall not apply in the case of -

(a) expenditures not exceeding ten thousand rupees;

(b) expenditures on account of –

(i) utility bills;
(ii) freight charges;
(iii) travel fare;
(iv) postage; and
(v) payment of taxes, duties, fee, fines or any other statutory obligation;]

(l) any salary paid or payable exceeding][fifteen] thousand rupees per month other than by a crossed cheque or direct transfer

of funds to be employees [illegible] account; and

(m) except as provided in Division [illegible] of this Part, any expenditure paid or pay[illegible] of a capital nature."

20. A plain reading of the titles of the section 20 & 21 and word u[illegible]ein i.e. DEDUCTION as well as considering the doctrine of ejusdem generis, not inclined to find ourselves in agreement with the learned ACIT or CIR (A hence orders of both the authorities below are hereby vacated with the direction delete impinged additions of Rs.60,864,447/- made u/s.21(l).

21. Up shot of the all above discussion is that the addition made on account of purchases U/s.21(l) is not maintainable in the eye of law and on facts, therefore, the same is directed to be deleted.

Appeal succeeds as indicated above.

(ZARINA N. ZAIDI)
ACCOUNTANT MEMBER

(SYED MUHAMMAD JAMIL RAZA ZAIDI)
JUDICIAL MEMBER

*IRSHAD/**