

JUDGMENT SHEET
IN THE LAHORE HIGH COURT LAHORE
JUDICIAL DEPARTMENT

W.P No.11253 of 2017

Treet Corporation Limited

Versus

Federation of Pakistan and others

J U D G M E N T

Date of Hearing.	06-03-2018
PETITIONERS BY:	M/s Shahzad Ata Elahi and Salman Zaheer Khan, Advocates.
RESPONDENTS BY:	M/s Shahid Usman and Shahid Sarwar Chahil, Advocates. Dr. Ishtiaq Ahmad Khan, Director Law, FBR.

Shahid Karim, J:- This petition under Article 199 of the Constitution of Islamic Republic of Pakistan, 1973 challenges the Tax Payers Audit Policy, 2016 (**Audit Policy, 2016**) which as a preamble has the following statement:-

"Since 2001 voluntarily compliance has been the primary focus of Federal Board of Revenue (FBR). FBR has always trusted tax payers for their declaration. In order to promote tax culture and compliance many audit policies were launched in the past. This Audit policy has been carefully drafted keeping in mind the wisdom and experience behind the past policies.

For the audit purposes, the selection of cases in the past was mostly through random ballot. The 'Audit Policy' 2016, has proposed a paradigm shift from the past. Its focus has been realigned from random to parametric selection and from general to risk based approach. This approach will minimize chances of selection of compliant tax payers resulting in increased confidence in the system. This new trend in taxpayers' audit will not only promote compliance with the existing tax laws but will also generate increased revenue through better declarations for better public spending by the Government. The right audit approach will help FBR in broadening the tax base and in focusing on high risk areas. This can be assured through equitable tax policies where a taxpayer knows that good citizens are appreciated."

2. The petitioner is a registered taxpayer under the Income Tax Ordinance, 2001 as well as the Sales Tax Act, 1990. Vide letter dated 01.01.2017 the respondent No.4, Deputy Commissioner (IR) Audit,03 Zone-I, LTU, Lahore, the petitioner was informed that it had been selected for audit for tax year 2015 under Section 72B of the Sales Tax Act, 1990. The result of the parametric computer balloting held on 05.01.2017 was also published on the website of the respondent No.2, FBR. The petitioner wrote a letter on 06.04.2017 to the Member (Audit) FBR, requesting to make available the parameters adopted by the FBR and the laid down criteria under which the petitioner had been selected for audit. A reply was received to the said letter in which the respondent No.3 informed the petitioner of the following parameters:

"where more than 30% sales are to unregistered persons".

3. Hence, the above was the basis on which the petitioner's case had been selected for sales tax audit. It is common ground between the parties that the petitioner's case for audit had been selected on the basis of Audit Policy, 2016.

4. On previous occasions too, audit policies have been challenged before this Court and as a consequence of a cluster of judgments, rules have been evolved by the superior courts which require the FBR to follow a certain mechanism in relation to selection of audit of the registered persons. The entire case of the petitioner

hinges on the precedents of the superior courts which lay down the guiding principles to be followed by FBR in the selection of cases for audit and the entire basis for such selection.

5. The first case to which a reference may be made is reported as Messrs Ittefaq Rice Mills v. Federation of Pakistan and others (2013 PTD 1274). In that case, the registered person had challenged a letter issue by the Commissioner Inland Revenue whereby the appellant had been selected for audit for the tax year 2011. The premise of challenge was that the risk parameters settled by the FBR for selection of cases for audit offended the understanding arrived at between the taxpayers and FBR in a judgment reported as Premier Industrial Chemical Manufacturing Co. v. Commissioner Inland Revenue and others (2013 PTD 398). The conclusion drawn by the Division Bench of this Court was as follows:-

"13. The real issue before us in this case is the scope and mechanism of the process of segregation of the taxpayers for developing a parametric group before it is funneled through the process of balloting. The nature and character of the 'parametric group' will depend on the mode and manner of application of the risk parameters to the taxpayers. This architecture and design of risk analysis forming part of the audit strategy/policy, for a particular tax year, is the sole prerogative of the FBR. The weightage of risk attached to a parameter falls within the technical and expert domain of the FBR. The courts may judicially review the audit policy announced by the FBR in order to satisfy itself regarding its fairness, openness and transparency besides ensuring that the audit policy has been fairly applied to the taxpayers across the board. Needless to say that FBR has to show that the risk parameters have been duly framed by FBR and have been publically advertised for the sake of

taxpayers convenience along with the risk strategy adopted by the FBR (reference - commitment made by FBR in Premier Industrial Chemical Manufacturing Co. case).

6. A reading of the paragraph above would show that this Court conceded that the weightage of risk attached to a parameter falls within the technical and expert domain of the FBR. However, the courts could review the audit policy in order to satisfy itself as regards its fairness and conformity with the structure of the law so as to satisfy itself that the audit policy had been fairly applied to the taxpayers across the board. The crucial finding of the Division Bench was that FBR had to show that risk parameters had been duly framed by FBR and publicly advertised for the sake of taxpayers convenience along with the risk strategy adopted by FBR. These were important factors which hedged in the powers of FBR to frame an audit policy.

7. The above case was followed by another judgment of this Court in Defence Housing Authority v. Commissioner Inland Revenue and others (2015 PTD 2538) in which again the audit for the tax year 2011 was called in question as the petitioner had been selected for audit by FBR on parametric basis. It was held in the DHA judgment that the power to select for audit was not unstructured and was to be based on reasonable criteria of selection to be laid down by FBR clearly and transparently.

8. Be that as it may, it seems that FBR has not, while selecting the case of the petitioner for audit, heeded to the concerns expressed by the superior courts in the judgments referred to above and a number of other precedents over time. The focus and emphasis of the superior courts has been on lending transparency and fairness to the entire process and in case the selection is parametric in nature, to lay down a clear audit policy by which it can be gleaned that FBR has duly framed the risk parameters and has publicized them openly. In the instant case, although an audit policy has duly been framed and from the preamble of the policy, reproduced above, it seems that much emphasis has been laid on a paradigm shift in the mindset of FBR which focuses on realignment from random to parametric selection and from general to risk based approach, FBR has woefully been lacking in laying down a clear policy which would show the risk parameters on the basis of which selection for audit is being conducted. It was only upon the prompting of the petitioner that the petitioner was informed of the reasons for selection of the petitioner's case for audit and which too has been reproduced above. However, this is not a proper compliance of the judgments of the superior courts brought forth above. The requirement of those judgments will not be satisfied if a person was informed at a later stage of the reasons which weighed with FBR in selecting a particular person for audit. The essential requirement is for the risk parameters to be laid down and clearly defined along

with the audit policy by FBR and those risk parameters should form the basis for parametric selection and none else. Since admittedly no risk parameters have been provided by FBR, this would give unbridled and unstructured powers in the hands of the officers of FBR to select any registered person for audit. This seems to have been the case in the instant matter as well. The *raison d'etre* of parametric selection has been brought forth in the preamble of the Audit Policy, 2016 itself and the underlying purpose seems to be to minimize chances of selection of compliant taxpayers resulting in increased confidence for the system. The purpose in the estimation of FBR is to assist FBR in broadening the tax base and to focus on high risk areas. In the column relating to percentage of selection, the following is also pertinent:-

"FBR shall conduct computer ballot on parametric basis for selection of 7.5% cases for audit out of the total Income Tax, Sales Tax and FED returns filed for Tax Year 2015 and Tax Period i.e. 1st July 2014 to June 2015 as determined by the Board-in-Council."

9. Thus, FBR has obligated itself to conduct computer ballot on parametric basis. To what avail, is the conducting of computer ballot if the parametric basis has not been framed and brought forth by FBR. Thus, the very basis of the computer ballot is knocked out and in fact there is nothing before FBR on which the computer ballot is being held. The mere framing of the Audit Policy, 2016 is insufficient until it is supported by clearly defined risk parameters on the basis of which the computer ballot ought to be held for selecting cases for

audit. Be that as it may, the Audit Policy, 2016 is utterly lacking in this regard and not only that it contradicts its mandate as expressed in its preamble adumbrated but it also runs counter to the judgments of this Court which compel FBR to formulate risk parameters so as to form an essential part of any audit policy. Thus the selection of the petitioner for audit does not comport with the judgments handed down by this Court. Plainly, FBR cannot proceed for the selection of audit and for taking a computer ballot until risk parameters have been laid down and adopted so as to form an integral part of the Audit Policy, 2016.

10. In view of the above, this petition is allowed. The notices issued to the petitioner with regard to the selection of audit for the period from 01.07.2014 to 30.06.2015 are hereby set aside. As a consequence thereof the case of the petitioner for selection of audit is also set aside. Although the challenge was also made to the Audit Policy, 2016 as a whole, I am not inclined to declare that Policy as unconstitutional. The Policy cannot be put into effect until FBR frames risk parameters on the basis of which the selection for audit is to be made.


(SHAHID KARIM)
JUDGE


JUDGE

Announced in open Court on 21.03.2018

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Rafaqat Ali