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JUDGMENT SHEET
IN THE LAHORE HIGH COURT, LAHORE
JUDICIAL DEPARTMENT

STR No.28 of 2012

Commissioner Inland Revenue

Versus

M/s Descon Engineering Limited

J U D G M E N T

Date of hearing: 08.06.2021.
Applicant by: Mr. Sarfraz Ahmad Cheema, Advocate.
Barrister Ameer Abbas Ali Khan, A.A.G. on Court's call.
Respondent by: M/s Mian Ashiq Hussain and Muhammad Arshad, Advocates.

MUHAMMAD SAJID MEHMOOD SETHI, J.- Through instant Reference Application under Section 47 of the Sales Tax Act, 1990 (**"the Act of 1990"**), following questions of law, urged to have arisen out of impugned order dated 08.10.2011, passed by learned Appellate Tribunal Inland Revenue, Lahore Bench, Lahore **("Appellate Tribunal")**, have been proposed for our opinion**:-**

a. Whether M/s Descon Engineering Limited violated provision of Section 3(1) of the Sales Tax Act, 1990 by not paying sales tax on acquisition of taxable goods regardless of their further disposal?

b. Whether on the facts and circumstances of the case, the ATIR was justified to hold that the goods consumed in the course of execution of construction were neither taxable nor constituted taxable supplies whereas the goods were fully taxable as they comprised of cement, welding electrodes, Bajri, sand, pipes etc.?

c. Whether with reference to the facts and circumstances of the instant case, the definition of taxable activity and taxable supply as provided under Section 2(35) and 2(41) of the Sales Tax Act, 1990 respectively, have been misinterpreted by the Appellate Tribunal Inland Revenue?

2. Brief facts of the case are that a show cause notice was issued to respondent-taxpayer alleging therein certain discrepancies found during audit for the period i.e. July, 2005 to June, 2006, which culminated in passing of order-in-original dated 25.11.2008. Feeling aggrieved, respondent-taxpayer filed appeal before Collector (Appeals), which was disposed of vide order dated 23.01.2009, whereby imposition of tax was upheld, however, matter was remanded for re-calculation of exact tax by giving effect to exempt goods by devising a formula and component of penalty was foregone but default surcharge was held applicable as per law. Respondent-taxpayer filed second appeal before learned Appellate Tribunal, which was partly allowed vide order dated 08.10.2011. Hence, this Reference Application.

3. Learned Legal Advisor for applicant-department contends that respondent-taxpayer violated the provisions of Section 3(1) of the Act of 1990 by not paying sales tax on acquisition of taxable goods regardless of their further disposal. He adds that goods consumed in the course of execution of construction were taxable, constituting taxable supplies as they comprised of cement, welding electrodes, *bajri*, sand, pipes etc. He further submits that learned Appellate Tribunal, while passing impugned order, has misinterpreted the definitions of "taxable activity" and "taxable supply" as provided in Sections 2(35) and 2(41) of the Act of 1990, respectively. In the end, he submits that impugned order is unsustainable in the eye of law. In support of his contentions, he relied upon *Commissioner of Sales Tax and others v. Hunza Central Asian Textile and Woolen Mills Ltd. and others* **(1999 SCMR 526)**, *Sheikhoo Sugar Mills Ltd. and others v. Government of Pakistan and others* **(2001 PTD 2097)**, *Collector of Customs, Central Excise and Sales Tax and others v. Mahboob Industries (Pvt.) Ltd. and others* **(2006 PTD 730)** and *Collector of Sales Tax and Central Excise, Lahore v. Water and Power Development Authority and others* **(2007 SCMR 1736)**.

4. On the contrary, learned counsel for respondent-taxpayer defends the impugned order. He contends that no supply of goods is involved in building the immovable property, which clearly falls outside the scope of "goods" provided in Section 2(12) of the Act of 1990. He has referred to the clarification of FBR dated 02.04.2002 according to which *there is no sales tax on immovable property such as building roads etc. since these are excluded from the definition of goods under the sales tax act.* In the end, he submits that construction of an immovable property is not covered by the provisions of Section 2(35) and 2(41) of the Act *ibid*.

5. Arguments heard. Available record perused.

6. Perusal of record shows that respondent-taxpayer has two segments of business i.e. Descon Engineering Works and Descon Engineering Limited. The former is engaged in the manufacturing of huge industrial items like Mobile Towers, Industrial Boilers etc., whereas the latter is engaged in the construction of roads, dams and other engineering services which filed sales tax returns for the period i.e. July, 2005 to June, 2006. During the course of audit, LTU, Lahore pointed out discrepancies involving non-payment or short-payment of sales tax i.e. *sales tax not charged on sale of scrap; sales tax not charged on transportation / delivery charges; inadmissible input tax claimed on supplies made to training school; sales tax not charged on sale of fixed assets; and taxable materials used in the projects undertaken by the Descon Engineering Limited*. The Additional Collector (Adjudication) concluded that supply / consumption of the goods in question was liable to tax, therefore, respondent-taxpayer was directed to deposit sales tax amounting to Rs.421,025,158/- for violating the provisions of Sections 3, 6, 11, 22, 23 & 26 of the Act of 1990 recoverable under Section 36(1) of the Act and default surcharge along with 5% penalty of sales tax amount.

7. The issue involved in question 'a' has already been dealt with by the Hon'ble Supreme Court in *Messrs Noon Sugar Mills Limited*

v. The Commissioner of Income-Tax, Rawalpindi **(PLD 1990 Supreme Court 1156)** wherein it has been observed that the liability to pay the tax arises by virtue of the charging sections alone, though quantification of the amount payable may be postponed. Likewise, the Apex Court in *B.P. Biscuit Factory Ltd., Karachi v. Wealth Tax Officer and another* **(1996 SCMR 1470)**, while defining "assets" with regard to immovable properties, has quoted Maxwell as under:-

> "It is well-settled rule of law that all charges upon the subject must be imposed by clear and unambiguous language, because in some degree they operate as penalties: the subject is not to be taxed unless the language of the statute clearly imposes the obligation and language must not be strained in order to tax a transaction which, had the legislature thought of it, would have been covered by appropriate words."

8. Section 3 of the Act charges tax on the supplier of goods and not on the purchaser, hence, the allegation raised in the first question that the respondent violated provision of Section 3(1) of the Act on the acquisition (purchase) of taxable goods is contrary to the language of the provision. The question is, therefore, beyond the scope of the charging section. For ready reference, the relevant extracts of Section 3 *ibid* are reproduced hereunder:-

> "**3. Scope of tax.– (1)** Subject to the provisions of this Act, there shall be charged, levied and paid a tax known as sales tax at the rate of seventeen per cent of the value of–
>
> **(a)** taxable supplies made by a registered person in the course or furtherance of any taxable activity carried on by him; and
>
> **…..**
>
> **(3)** The liability to pay the tax shall be,-
>
> **(a)** in the case of supply of goods, of the person making the supply, and
>
> **…..**"

9. The above statutory provision leaves no doubt that taxing the respondent-taxpayer as the purchaser of the goods was flagrant violation of the charging provisions of the Act and the decision of the learned Tribunal is in accordance with law. The question of

taxing the respondent-taxpayer as purchaser / consumer of goods is misconceived.

10. Likewise, the issue involved in question 'b' has also been decided by this Court in *Messrs Sarwar & Co. (Pvt.) Ltd. v. Customs, Central Excise and Sales Tax, Appellate Tribunal, Lahore and another* **(2006 PTD 162)**, wherein it has been observed that the building material consumed in the construction of immovable property is neither taxable supply nor in furtherance of taxable activity, hence, beyond the scope of sales tax under the Act. The construction of immoveable property is not taxable activity, which is essential ingredient to charge tax. The consumption of material in an activity, which is not taxable under the Act, therefore, is not chargeable to sales tax under the Act. No construction of immovable property is possible without building material. Consumption of building material by a person, being non-taxable activity, falls out of the supply chain under Section 3 of the Act. Learned Appellate Tribunal followed the above-referred judgment of this Court, which is not open to any exception.

Thus, to the extent of issues already decided by this Court are not repetitively maintainable in instant Reference Application.

11. As regards question 'c', firstly the definitions referred to in the said question are reproduced hereunder:-

> "**2. Definitions.—** In this Act, unless there is anything repugnant in the subject or context,--
>
> **.....**
>
> **(35) "taxable activity"**, means any economic activity carried on by a person whether or not for profit, and includes –
>
> **(a)** an activity carried on in the form of a business, trade or manufacture;
>
> **(b)** an activity that involves the supply of goods, the rendering or providing of services, or both to another person;
>
> **(c)** a one-off adventure or concern in the nature of a trade; and

> **(d)** anything done or undertaken during the commencement or termination of the economic activity,
>
> but does not include –
>
> **(a)** the activities of an employee providing services in that capacity to an employer;
>
> **(b)** an activity carried on by an individual as a private recreational pursuit or hobby; and
>
> **(c)** an activity carried on by a person other than an individual which, if carried on by an individual, would fall within sub-clause (b).]
>
> **.....**
>
> **(41) "taxable supply"** means a supply of taxable goods made by an importer, manufacturer, wholesaler (including dealer), distributor or retailer] other than a supply of goods which is exempt under section 13 and includes a supply of goods chargeable to tax at the rate of zero per cent under section 4;."

12. Due to unique distribution of taxing powers between the Federation and the Provinces under the Constitution of the Islamic Republic of Pakistan, 1973 (**"the Constitution"**), the above definitions have to be interpreted harmoniously and consistently with constitutional provisions. Article 142 (c) of the Constitution (before and after Eighteenth amendment) read with entry 49 of the Federal Legislative List reads as under:-

> ***BEFORE AMENDMENT***
>
> "**142. Subject-matter of Federal and Provincial laws**
> Subject to the Constitution—
> (c) A Provincial Assembly shall, and Majlis-e-Shoora (Parliament) shall not, have power to make laws with respect to any matter not enumerated in either the Federal Legislative List or the Concurrent Legislative List;
>
> ***AFTER AMENDMENT***
>
> **142. Subject-matter of Federal and Provincial laws**
> Subject to the Constitution—
> (c) Subject to paragraph (b), a Provincial Assembly shall, and Majlis-e-Shoora (Parliament) shall not, have power to make laws with respect to any matter not enumerated in the Federal Legislative List.

Federal Legislative List
PART I

> **49.** Taxes on the sales and purchases of goods imported, exported, produced, manufactured or consumed.

13. Under the above distribution of taxing powers, taxable activity for the purpose of the Federation is confined to activity in respect of goods and cannot spill over to supply of services or immovable property because taxable supply and taxable activity in respect of both subjects of services and immovable property fall within the exclusive jurisdiction of the provinces. Since both the subjects are not included in the taxing power of the Federation, they cannot be indirectly taxed by means of interpretation. Reliance is placed upon *State and another v. Sajjad Hussain and others* **(1993 SCMR 1523)**.

14. In the context of Section 3(1)(a), the taxable supply and taxable activity must co-exist to attract the charge of sales tax under the Act. Absence of either of the ingredients excludes the other from purview of aforesaid charging provision. In the light of the above referred constitutional provisions, building of immoveable property is not taxable activity for Federation. In the absence of any taxable activity within the taxing power of the Federation, no charge of sales tax arises. In the instant case, however, even no taxable supply was involved. Section 2(41) of the Act specifies the persons of which supply of taxable goods is to be considered as taxable supply. They are importers, manufacturers, wholesalers (including dealers), distributors or retailers. In this regard, learned Appellate Tribunal has recorded findings of facts that taxpayer's case falls outside the definition of "taxable supply". The relevant observations of learned Appellate Tribunal are reproduced below:-

> "Even otherwise, the registered person is not the producer or manufacturer of the goods consumed for construction of the immovable properties, hence it falls outside the definition of taxable supplies nor it falls in the definition of an importer, manufacturer, supplier, wholesaler (including dealer), distributor or retailer. Hence it was not making any taxable supplies to itself.

> From the factual as well as legal position discussed above and the ratio settled through judgments of superior fora relied upon by the AR of the registered person we are of the firm and considered view that the goods consumed in the course of execution of a construction are neither taxable goods nor can be termed as taxable supplies, hence, fall outside the scope of section 3 of the Sales Tax Act. Accordingly the charge of sales tax on goods consumed in connection with execution of construction contract in this case is ordered for its deletion."

15. So far as reliance placed by learned counsel for applicant-department on the cases of *Hunza Central Asian Textile and Woolen Mills Ltd.*, *Sheikhoo Sugar Mills Ltd.*, *Mahboob Industries (Pvt.) Ltd.* and *Water and Power Development Authority* supra, is concerned, said case law is distinguishable from the instant case on the ground that respondent-taxpayer is not a manufacturer of any intermediary good or any final good liable to sales tax. No intermediary good has been identified to have been manufactured by the respondent-taxpayer, which could have been sold in market as separately identifiable goods. What was handed over to the principal was an immovable property which was not chargeable to sales tax.

16. It is also pertinent to mention here that the contract of construction of immovable property is indivisible. The issue of indivisibility of contract of construction of immovable property was also considered by this Court in *International Body Builders v. Sales Tax Officer, Lahore and 2 others* **[(1980) 41 TAX 60 (H.C. Kar.)]**, wherein it was approved that a building contract is one and indivisible and involves no sale of goods. It was further observed that in such a contract, goods pass on as accession to immoveable property and no supply of goods is involved.

17. The expression "taxable supply" and "taxable activity" both operate in their own respective fields. The quantum of tax liability is determined on the basis of the value of taxable supply, but the liability to pay tax under the charging section would arise only when such supply is made in furtherance of taxable activity. The

taxable activity defined in the Act meant any activity involving in whole or in part, the supply of goods to any other person. Keeping in view the definition of "goods" in sub-section (12) of Section 2, construction of immovable property cannot be treated as "goods" by any stretch of imagination. Therefore, it is held that supply of material consumed in the course of execution of construction was not made in furtherance of a taxable activity, therefore, taxpayer cannot be held liable to pay sales tax. The Courts while construing the provisions of statutes should made efforts that the interpretation of the relevant provisions of statute should be in consonance with the provisions of the Constitution and the grund norms of human rights. All the statutory provisions have to be interpreted harmoniously and consistently with the constitutional provisions, the paramount law, already occupying the field. Reference can be made to *Messrs Noon Sugar Mills Limited v. The Commissioner of Income-Tax, Rawalpindi* **(PLD 1990 Supreme Court 1156)**, *The State v. Syed Qaim Ali Shah* **(1992 SCMR 2192)**, *State and another v. Sajjad Hussain and others* **(1993 SCMR 1523)**, *B.P. Biscuit Factory Ltd., Karachi v. Wealth Tax Officer and another* **(1996 SCMR 1470)**, *Messrs Sarwar & Co. (Pvt.) Ltd. v. Customs, Central Excise and Sales Tax, Appellate Tribunal, Lahore and another* **(PTCL 2006 CL. 1 = 2006 PTD 162)**, *Ghulam Mustafa Jatoi, Karachi v. Commissioner of Income Tax, Central Zone-B, Karachi* **(2006 PTD 1647)** and *Caretex v. Collector Sales Tax and Federal Excise and others* **(2013 PTD 1536)**.

18. Undoubtedly, the building material i.e. cement, crush, iron etc., being constituent parts of immovable property, are integral part of such property. Thus, the entire proceedings of assessment were based on misapplication of law, and have been rightly annulled by learned Appellate Tribunal. Learned Legal Advisor for applicant-department failed to pinpoint any illegality or legal infirmity in the impugned order.

19. In view of the above, our answer to the proposed question 'c' is in ***negative*** i.e. in favour of respondent-taxpayer and against the applicant-department, whereas since questions 'a' & 'b' have already been decided in the cases of *Messrs Noon Sugar Mills Limited* and *Messrs Sarwar & Co. (Pvt.) Ltd.* supra, same are ***answered accordingly***.

20. This Reference Application, being without any merits, is ***decided*** against the applicant-department.

21. Office shall send a copy of this judgment under seal of the Court to learned Appellate Tribunal as per Section 47 (5) of the Act of 1990.

(Abid Hussain Chattha)
Judge

(Muhammad Sajid Mehmood Sethi)
Judge

A.H.S.