RESEARCH CENTRE

HIGH COURT OF BALOCHISTAN

# RESEARCH CENTER, HIGH COURT OF BALOCHISTAN

**COURT:** **Hon'ble C.J (A) Mr. Justice Ejaz Ahmed Sawathi BHC**

**SUBJECT:** **Tax Law**

**DATE:** **March 22, 2025**

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## *Queries*

*Does failure to deduct and deposit tax on salaries, bonuses, and other payments by a QESCO, **withholding agent,** trigger liability under **Income Tax Ordinance 2001**?*

*What are the essential **requirements for a valid show-cause notice** for reassessment or additional tax under **Income Tax Ordinance, 2001**?*

*Does Tariff Differential Subsidy (TDS) received by electric power companies constitute gross revenue and become subject to minimum tax under Section 113 of the Income Tax Ordinance, 2001?*

*Can penalty and default surcharge under Sections 33 & 34 of the Sales Tax Act, 1990, be imposed independently under Section 11(1), or must they be tied to an assessment order?*

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In response to the quires, it is submitted as follows: -

In 2023 SCMR 1516**,** the Supreme Court addressed the liability of Islamabad Electric Supply Company (IESCO) **for** failure to deduct withholding tax**, holding that** electric supply companies are withholding agents **under** Section 161 of the Income Tax Ordinance, 2001**, and are** personally liable if they fail to deduct and deposit tax**. On the** same analogy**,** Quetta Electric Supply Company (QESCO), being a similar entity, is equally obligated to deduct withholding tax on salaries, bonuses, and other taxable benefits of its employees**.** Failure to comply would make QESCO liable under Section 161, along with default surcharge under Section 205**.**

**Judicial rulings on the duty of withholding agents to deduct taxes and their liability for non-compliance.**

In **M/s Chawala Footwear v. Commissioner Inland Revenue --------------------------------------** the Supreme Court held that **a taxpayer qualifying as a withholding agent under Section 153(7) of the Income Tax Ordinance, 2001, is legally obligated to deduct tax at source**. **Failure to deduct tax constitutes a default under Section 161**, making the taxpayer liable for recovery proceedings. In paragraph 8, the Court observed as under:-

> *"**Consequently, if a taxpayer fails to collect or deduct tax from payments made during the tax year, such inaction is deemed as a default under section 161. Therefore, the point that sets the machinery of section 161 going to determine the tax liability is the failure to either collect tax or deduct it**. Before going further, we take a little pause to say that even the power to put that point on is not unfettered."*

In ________________________________________**2023 PTD 1046 (Lahore High Court)**, the Court reaffirmed that ***a withholding agent is legally bound to deduct tax at source under Section 153(1)(a) of the Income Tax Ordinance, 2001***, and failure to do so ***triggers liability under Section 161***. In paragraph 5, the Court held that:

> "5. ***It has been noted that the respondent is a prescribed person, obligated to deduct tax while making payments against purchases in terms of section 153(1)(a) of the Ordinance***……………………………………………………….."

In Commissioner Inland Revenue, LTU, Lahore v. Messrs Adamjee Insurance Company Ltd **(2023 PTD 1628)** [Inland Revenue Appellate Tribunal, Lahore Bench] the Tribunal held that:

*"13. **Under the existing provisions of the Income Tax Ordinance at the relevant time (tax year 2013), a company, being an employer, is required to deduct tax at the time of payment of salary to its employees.** However, there is no specific provision for deduction of tax on the remuneration paid to a director which is not in the nature of salary. The director has not provided any technical or professional services to the assessee and therefore payment of sitting fees does not constitute payment for rendering services under section 153(1)(b). Had it been included in section 153(1)(b), there was no need of insertion of subsection (3) in section 149 specifically providing the deduction of tax at the time of payment made for directorship fee. The amendment brought in tax year 2014 relating to deduction of tax on director's fee in section 149 is prospective and does not apply in the instant case. Hence, the CIR(A) rightly deleted the tax under this head. The appeal of the department on this issue fails.*

In Commissioner Inland Revenue v. MCB Bank Limited **(2021 SCMR 1325)**, the Supreme Court of Pakistan clarified the ***liability of withholding agents under Section 161 of the Income Tax Ordinance, 2001***; ***requirement for issuing specific and objective show-cause notices*** rather than vague or general inquiries and that ***the initial burden is on the tax authorities*** *to establish a prima facie failure to deduct tax* before shifting the burden to the taxpayer.



**Withholding Agents' Under Section 161 Liability on failing to deduct tax**

*"12. At the time of the issuance of the show cause notices section 161 provided in material part as follows (emphasis supplied):*

> *"161. Failure to pay tax collected or deducted.- (1) Where a person -*
>
> *(a) fails to collect tax as required under Division II of this Part or Chapter XII or deduct tax from a payment as required under Division III of this Part or Chapter XII or as required under section 50 of the repealed Ordinance;*
>
> *the person shall be personally liable to pay the amount of tax to the Commissioner who may pass an order to that effect and proceed to recover the same."*

*It will be seen that the section becomes applicable not simply because a payment is made (or a transaction or event happens) but rather on a failure to either collect tax or deduct it. It is the failure that is the triggering event. In each case, the consequence is the same: the person becomes personally liable to pay the amount of the tax………………………………………………………………………………"*

**Requirement for a Valid Show-Cause Notice and shifting of burden on the taxpayer.**

*"It is in our view a gross misreading of it to conclude that for the section to apply all that the Commissioner has to do is point to a payment, and that is sufficient to cast the burden wholly and solely on the taxpayer to show that there was no failure. There must, at least initially, be some reason or information available with the Commissioner for him to conclude that there was, or could have been, a failure to deduct. That reason or information must satisfy the test of objectiveness, i.e., must be such as would satisfy a reasonable person looking at the relevant facts and information in an objective manner. The threshold is not so stringent as to require "definite information" (using this term in the sense well known to income tax law) but it is also not so low as to be bound merely to the subjective satisfaction of the Commissioner. And it is certainly not what the tax authorities currently take it to be, based on an incorrect understanding of Bilz.* ***It is only if this threshold is successfully***

***<u>crossed that the notice can be issued,</u> and it is only then that the burden may shift on the person allegedly in default to show that section 161 does not, or ought not to, apply***."

In **PLD 2002 SC 353 (Bilz Case)**, the Supreme Court held that a ***show-cause notice is valid without naming recipients***, as ***the taxpayer bears the burden of maintaining records and justifying non-deduction***. Failure to deduct tax triggers ***default and liability,*** and procedural objections do not invalidate the notice. It was observed in the paragraph

"7. In our opinion, there was no necessity for the Assessing Officer to identify the names of the parties to whom the supplies were made because the record is maintained by the supplier i.e. petitioner and it is the duty of~ the petitioner to maintain the record and show that as to why deductions were not made - from different parties at the time of making supplies to them."

In **2021 PTD (Trib.) 47**, the Tribunal held that **prior issuance of a proper show-cause notice and an opportunity of hearing are fundamental rights of a taxpayer**. It ruled that **any adverse action taken without issuing a notice violates the principle of natural justice (audi alteram partem)** and is liable to be set aside. The relevant portion is reproduced below:

"4………………………………………………………………………………………………………………………………….. ***<u>We hold that even issuance of a proper show-cause notice to a person is an essential ingredient of the legal maxim "audi alterm partem". The right of being issued with a show cause notice and the right of being personally heard are inseparable and inalienable rights of the taxpayer and cannot be denied under any circumstances.</u>*** Resultantly, the impugned orders are vacated and the case is remanded back to the Assessing Officer for providing proper opportunity of hearing to the taxpayer and then pass afresh order in accordance with law. The taxpayer is also directed to present his case along with documentary evidence before the Assessing Officer and avoid from unnecessary adjournments."



In *2016 PTD 596*, the Islamabad High Court held that **Section 122(5A) powers** can only be exercised if the assessment is **erroneous and prejudicial to revenue**, with a **mandatory show cause notice** ensuring due process.

> *"11. <u>Section 122 of the Ordinance empowers the Commissioner to amend an assessment made under section 120 or 121 of the Ordinance.</u> Subsection (1) of section 122 vests in the Commissioner the power to amend an assessment order treated to have been issued under sections 120, 121 or 122C by making such alteration or additions as he or she may consider necessary. The limitation prescribed for exercising the said power has been prescribed i.e. a period of five years from the end of the financial year in which the Commissioner has issued the assessment order to the tax payer.* ***<u>Subsection (5A) of section 122 vests power in the Commissioner to amend or further amend an assessment order after making or causing to be made such inquiries as he deems necessary, and if in his or her opinion the assessment order is erroneous in as much as it is prejudicial to the interest of revenue. Subsection (5A) has expressly been made subject to subsection (9) which provides that no assessment shall be amended or further amended unless the tax payer has been provided with an opportunity of being heard.</u>*** *Subsection (6) of section 122 imposes a duty on the Commissioner to issue an amended assessment order to the tax payer after making an amended assessment under subsection (1), subsection (4) or <u>subsection (5A) and such amended assessment order is declared to be treated in all respects as an assessment order for the purposes of the Ordinance</u>."*

In *2024 PTD 619*, the Islamabad High Court held that **Section 122(5A) powers** require a **proper show cause notice** and can only be exercised if the assessment is **erroneous and prejudicial to revenue**, ensuring due process.

> *12. As per law,* ***the Additional Commissioner was duty bound to amend the assessment order so as to bring the deemed order in harmony with law and as such, the only requirement to provide an opportunity of being heard has been extended before amending the order.*** *<u>The record reveals that the relevant information and data provided by the applicant taxpayer in the return has been scanned for correct arithmetical working of the tax demand, per se, this aspect does</u>*

> *not put any clog upon the tax authorities to call for information as to whether the deemed order is within four corners of law or not. It has been observed by the forums below that the tax liability has not been assessed and calculated by the applicant company in accordance with provisions of law. In such eventuality, it is legal duty and obligation of the Additional Commissioner Audit to give effect to the provisions of law ill a strict manner and when he observed that the tax has not been calculated in a proper manner, he considered it to be erroneous on the part of applicant company, who is, avoiding the tax liability, resultantly the assessment order is considered to be prejudicial to the interest of revenue, where the jurisdiction in terms of section 122(5A) of the Ordinance has rightly been exercised even with the only condition of limitation to provide an opportunity to the applicant company of being heard in terms of Section 122(9) of the Ordinance as held in 2016 PTD 596 Islamabad (Pakistan Tobacco Company Ltd. v. Federation of Pakistan). Hence, no illegality has been observed in this regard, therefore, respondent No. 3 Additional Commissioner Audit-II has rightly invoked the provision of Section 122(5A) of the Ordinance.*

In *Deputy Collector, Central Excise & Sales Tax v. ICI Pakistan Ltd.* (2006 SCMR 626), the Supreme Court of Pakistan held that the imposition of additional sales tax and penalty under Sections 33 and 34 of the Sales Tax Act, 1990, is not automatic and requires a determination of whether the short payment was wilful or mala fide. The Court upheld the Lahore High Court’s decision, which set aside the additional tax and surcharge, emphasizing that liability must be assessed on a case-by-case basis, considering the taxpayer’s intent and circumstances. In paragraph 7, it was held as under:-

“The above provisions would clearly indicate that in case of failure of a registered person to pay the sales tax within time, he shall also be liable to pay additional tax and surcharge. The liability being not automatic B would be determined by the appropriate authority as to whether or not there was any reasonable ground for default in payment of sales tax which could be considered to be wilful and deliberate……………………………………..”

In *2016 PTD 1393*, the Supreme Court **explained** and defined that **turnover under Section 113(3)** includes **gross receipts from sales, services, commissions, and contracts**, and must be **interpreted strictly**, excluding any additional sources: the most relevant portion is copied as follows:

> *“Where the legislature defines, in the same statute, the meaning of a word used therein, such definition most authoritatively expresses its intent which definition and construction is binding on the courts. When a word has been defined to mean such and such, the definition is prima facie restrictive and exhaustive.* ***Upon a plain reading of the definition of 'turnover' provided in Section 113(3) of the Ordinance of 2001 it is manifest that it (turnover) means: (i) gross receipts derived from the sale of goods; (ii) gross fees for the rendering of services or giving benefits, including commissions; (iii) gross receipts from the execution of contracts; and (iv) the company's share of the amounts stated above of any association of persons of which the company is a member. The meaning in the said subsection has been assigned to the word 'turnover' used in Section 113 and therefore the phrase 'turnover from all sources' in subsection (1) is to be read in conjunction with such definition which is exhaustive in nature and nothing further can be added thereto, thus the argument of the appellants/petitioners' that 'turnover' covers all sources under various heads of income is not tenable in law.”***

In *2022 PTD 1844*, the Balochistan High Court held that **turnover under Section 113** includes all **gross receipts from sales**, including **Tariff Differential Subsidy (TDS)**, making it subject to **minimum tax**.

> *“22. For what has been discussed above we are of the considered opinion that the amount received / receivable by electric power supply companies from the Government of Pakistan on account of difference between lower than the NEPRA Tariff rate charged to consumers and the rate notified by NEPRA is not subsidy. It is the balance price of electricity which is paid by the Government on behalf of electricity consumers to provide relief to such consumers.* ***The electric power supply***

> ***companies receive their full price of electricity sold to consumers partly from consumers and partly from the Government. Hence such total amount constitute gross revenue on account of sale of electricity and such revenue is liable to minimum tax under section 113 of the Ordinance unless a specific exemption is brought into Part IV of the Second Schedule to the Ordinance.*** *The learned Tribunal has erred in holding TDS as subsidy and exempt from minimum tax under section 113 of the Ordinance. The learned Tribunal has also erred in treating TDS as trade discount because trade discount although mentioned on sale invoices is not charged from the buyers. In case of electricity bill no such trade discount is mentioned which is not received from the consumers. Further the learned Tribunal has erroneously referred to Clause (102A) Part I of the Second Schedule to the Ordinance while discussing exemption from minimum tax under section 113 of the Ordinance because Part I of the Second Schedule to the Ordinance provides exemption from total income only and it has no concern with exemption from specific provision which is covered in Part IV of the Second Schedule to the Ordinance. Therefore our answers to the proposed questions are in affirmative i.e. against the Respondent/ Taxpayer and in favour of the Applicant/Department."*

In *2014 PTD 1256*, the Sindh High Court held that a **Collector cannot reopen an adjudicated matter and remand it to a subordinate officer** without first recording **illegality or impropriety**. The Court ruled that under **Section 195 of the Customs Act, 1969**, the **Collector must decide the case personally** and cannot delegate this power. Any remand without justification is **void and without jurisdiction**. It was held that:

> *"The order which is being re-opened should be such, in which there is any* ***illegality or impropriety****, for which the order is required to be re-opened by the Collector. This is the* ***first pre-condition****, which must be present and fulfilled. However, in the instant matter, while passing the order for reopening,* ***nothing has been recorded or shown*** *as to what circumstances prevailed upon the Collector to exercise this power under Section 195 of the Customs Act, 1969. The Collector* ***cannot reopen the matter and delegate it to some other officer****; if an order is reopened,* ***it is the Collector who must decide it personally****. Any delegation of this function renders the proceedings* ***without lawful authority and void ab initio****."*

In *2015 PTD 1330*, the Lahore High Court held that the **Appellate Tribunal cannot remand a case without proper justification**, emphasizing that as the **final fact-finding authority**, it must **thoroughly examine the record before ordering remand**

> *The Appellate Tribunal, as the final fact-finding authority, must exercise its jurisdiction diligently and cannot remand a case without recording proper reasons. A remand should only be made where factual findings are unclear or further inquiry is necessary. Failure to properly exercise jurisdiction is a question of law, as held by the Supreme Court in 2002 SCMR 527, and unjustified remand orders are liable to be set aside."*

In **2025 P T D 121**, the Lahore High Court held that under **Sections 33 & 34** of the **Sales Tax Act, 1990**, penalty and default surcharge remain applicable even if the principal tax is paid voluntarily before proceedings under **Section 11(1)**. The court rejected a restrictive interpretation that would nullify compliance enforcement. The matter was **remanded** for fresh adjudication due to legal defects in the Appellate Tribunal's decision.

> "Even if upon filing of return after due date no tax—defined in terms of Section 2(34) of the Sales Tax Act, 1990 and subject to the context—is payable, still penalty and default surcharge could be ordered and claimed. Restrictive interpretation of the scope of 'order of assessment of tax' would nullify the disciplined compliance envisaged in law and otherwise render Sections 33 and 34 of the Sales Tax Act, 1990, redundant. This redundancy needs to be avoided upon a harmonized reading of applicable provisions."

In **2022 P T D 1265**, the Balochistan High Court held that **penalty and default surcharge under Sections 33 & 34** of the **Sales Tax Act, 1990** cannot be imposed independently under **Section 11(1)** without an assessment order. It ruled that if a taxpayer **files a return late but pays tax voluntarily before a show-cause notice**, proceedings abate. The court upheld the **Appellate Tribunal's decision**, dismissing the department's reference.

"Proviso to subsection (1) of section 11 of the Sales Tax Act, 1990 provides that where a person required to file a tax return files the return after the due date and pays the amount of tax payable in accordance with the tax return along with default surcharge and penalty, the notice to show-cause and the order of assessment shall abate. It means that even if a registered person falls in any of the aforesaid two eventualities and the Officer issues a show-cause notice or passes an assessment order under subsection (1) of section 11, but thereafter the registered person files a return after the due date and also pays tax along with default surcharge and penalty, then the show-cause notice as well as the assessment order under subsection (1) of section 11 shall abate.

**The End**