

2013 P T D 682**[Sindh High Court]****Before Aqeel Ahmed Abbasi and Sadiq Hussain Bhatti, JJ****Messrs SARAH CONSTRUCTION CO. through Partner, Karachi****Versus****TAXATION OFFICER-5, AUDIT-2, KARACHI and 2 others**

Income Tax Reference Application No.421 of 2010 out of I.T.A. No.363/KB of 2008 decided on 20th December, 2012.

(a) Income Tax Ordinance (XLIX of 2001)---

---Ss.121 & 174---Best judgment assessment without issuing notice under S.121 of Income Tax Ordinance, 2001---Powers of Taxation Officer---Scope---Taxation Officer, in case of failure of taxpayer to provide required information or evidence, could pass such judgment on basis of available information or material, but could not make arbitrary and fanciful estimate of his income---Principles.

There seems to be no embargo upon a Taxation Officer to make best judgment assessment under S.121 in case of a person who fails to comply with the notice issued under section 177 by the Taxation Officer.

While passing best judgment assessment in the case of a taxpayer, who fails to comply with the legal requirements or the notices issued by the Taxation Officer seeking certain explanation or calling for the documents/evidence in support of the return of income filed by the taxpayer, a Taxation Officer is required to pass best judgment assessment on the basis of available information or material, whereas he is not permitted under law to make arbitrary and fanciful estimate of the income of a taxpayer.

(b) Income Tax Ordinance (XLIX of 2001)---

---S.133---Reference application---Jurisdiction of High Court---Scope---High Court could examine only question of law arising from order passed by Appellate Tribunal---Principles.

Emad-ul-Hasan for Applicant.

Amjad Javaid Hashmi for Respondents.

Date of hearing: 11th December, 2012.

ORDER

AQEEL AHMED ABBASI, J.---Through instant reference application, following questions were formulated by the applicant, which were said to have arisen from the impugned order passed by the Appellate Tribunal Inland Revenue (Pakistan) Karachi, in I.T.A. No.363/KB of 2008 (Tax Year 2005):-

- (1) Whether the Income Tax Appellate Tribunal was justified holding actions of the learned Commissioner of Income Tax (Appeals-I) Taxation Officer-5, Audit-2 of various additions without any basis?
- (2) Whether the assessment may be finalized without any decision by ITAT as well as CIT (Appeals) on the alleged assessed income?
- (3) Whether in the absence of alleged 'certain information' the Taxation Officer is authorized to add any amount arbitrarily and without any basis?

2. On 2-2-2011, when the matter was taken-up for hearing before another Division Bench of this Court, it was observed that the above questions do not arise out of the order of the Tribunal. However, keeping in view the controversy involved in the instant matter, following three questions were formulated and notice was issued to the respondent: --

- (i) Whether the order under section 121 can be passed for the assessment year 2004-2005?
- (ii) Whether the Tribunal was justified in upholding the best judgment of assessment claimed by the Assessing Officer to be a judicious best judgment assessment?

3. On 14-11-2012, when this matter came-up for hearing before this bench, learned counsel for the applicant referred to the questions formulated by another bench of this Court vide order dated 2-2-2011, as referred to hereinabove, and submitted that the above questions arise from the impugned order passed by the Tribunal, which may be considered and opinion may be given thereon. Learned counsel for the respondent extended his no objection. However, from perusal of the re-framed question No.1, it was noted that instead of mentioning tax year 2004, it was inadvertently mentioned as assessment year 2004-2005. The concept of income year and assessment year was available in the Repealed Income Tax Ordinance, 1979, whereas, in the Income Tax Ordinance, 2001, only Tax Year has been defined. Accordingly, by consent of both the learned counsel, question No. 1 was re-formulated, hence the questions, which require our opinion now, read as follows:-

- (1) Whether the order under section 121 can be passed for the tax year 2005?
- (2) Whether the Tribunal was justified in upholding the best judgment of assessment claimed by the Assessing Officer to be a judicious best judgment assessment?

4. The brief facts as stated by the learned counsel for the applicant are that the applicant is an Association of Persons engaged in the construction business, who filed Return of Income for tax year 2005 declaring a net business loss of Rs.837,452 under the Self-Assessment. The case of the applicant was selected for audit by the Commissioner vide letter No.4209 of 2006 dated 3-4-2006 on account of following reasons:-

- (1) Declared loss for assessment year 2001-2002 has been adjusted instead of assessed loss for tax year 2005.
- (2) The profit & loss expenses for tax year 2005 at a rate of 93% of GP are very high, and need to be verified.
- (3) Except for tax year 2005, losses have been declared.

5. The applicant initially responded to the query vide letter dated 29-4-2006, whereafter another letter dated 21-9-2006 was issued by the Taxation Officer requiring the applicant to furnish wealth statements of partners and books of accounts required to be maintained under section 174 of the Income Tax Ordinance, 2001. The said letter was not responded. Whereafter Taxation Officer, passed an order under section 121 of the Income Tax Ordinance, 2001.

6. Being aggrieved by such order, the applicant filed an appeal before the Commissioner of Income Tax (Appeals-I), Karachi, under section 129 of the Income Tax Ordinance, 2001, who vide order dated 7-2-2008 dismissed the appeal and upheld the order passed by the Taxation Officer under section 121 of the Income Tax Ordinance, 2001. The applicant assailed the order of the Commissioner (Appeals) by filing an appeal before the Appellate Tribunal Inland Revenue (Pakistan), Karachi, who vide impugned order dated 19-11-2009 concurred with the finding of the CIT (Appeals) and dismissed the appeal of the applicant, who has impugned the same by filing instant reference application.

7. Learned counsel for the applicant has argued that the best judgment assessment under section 121 in the instant case could not be passed as the said authority was not vested with the Taxation Officer prior to amendment made by Finance Act, 2010, whereby subsection (10) was added in section 177, which

authorized the Commissioner to proceed to make the best judgment assessment under section 121 of the Income Tax Ordinance, 2001, where a person fails to produce any accounts, documents and records required to be maintained under section 174 of the Income Tax Ordinance, 2001. Per learned counsel, since in the instant case return was filed, assessment was made under section 122(3), whereafter the case was selected for audit and the applicant had complied with the notice issued by the respondent, therefore, provisions of section 177(6) could be invoked by the Taxation Officer, which provide that after completion of the audit and after obtaining explanation of the taxpayer on all the issues raised in the audit, the Commissioner could amend the assessment under subsection (1) or subsection (4) of section 121, as the case may be and could not pass an order under section 122. Learned counsel for the applicant has further argued that even otherwise the best judgment assessment made by the respondent in the instant case is without any basis, whereas the Taxation Officer has arbitrarily disallowed 50% of trading expenses as well as 50% of profit and loss account expenses without any reasonable justification. It has been submitted that the Taxation Officer could have disallowed such expenses keeping in view the nature of the business of the applicant or the history of the case, whereas, the 50% disallowance under the circumstances was not justified.

8. Conversely, learned counsel for the respondent has submitted that no question of law arises from the order passed by the Appellate Tribunal Inland Revenue (Pakistan), Karachi, in the instant case, whereas there is concurrent finding of fact recorded by both the appellate forums below. It has been contended that after selection of the case for audit the Taxation Officer issued notices to the applicant requiring certain documents to be produced while conducting the audit. However, the applicant, in spite of opportunity having been provided by the Taxation Officer, did not furnish the required documents nor could explain or respond to the queries as raised by the Taxation Officer in the notices served upon the applicant. Under the circumstances, per learned counsel for the respondent, the Taxation Officer was left with no other alternate to finalize the assessment of the applicant under section 121(1)(d) on the basis of available record. It is further contended by the learned counsel that nothing has been added by the Taxation Officer except the information available on record and in the accounts of the applicant, whereas merely disallowance of expenses in trading account and profit and loss account to the extent of 50% has been made for want of supporting documents and evidence in this regard. Per learned counsel, in terms of section 174(2) of the Income Tax Ordinance, 2001, the Commissioner has authority to disallow or reduce any claim of taxpayer if the taxpayer is unable to provide the evidence in support of such claim. It has been further contended that reference to section 177 subsection (10) is not relevant in the instant case as the provisions of section 121(1)(d) were always available in the Statute book which have been rightly invoked by the Taxation Officer in the instant case. Per learned counsel, instant reference has no merits and the same is liable to be dismissed.

9. We have heard both the learned counsel, perused the record as well as the impugned order passed by the Appellate Tribunal Inland Revenue (Pakistan), Karachi and the orders of taxation authorities in the instant case.

10. In response to question No.1 as reframed hereinabove, the contention of the learned counsel for the applicant that the Taxation Officer could not pass an order under section 121 of the Income Tax Ordinance, 2001 as such authority was not vested in him prior to amendment by Finance Act, 2010, whereby subsection (10) was inserted in section 177 of the Ordinance, 2001, which authorized a Taxation Officer to pass an order under section 121, in case where a taxpayer fails to produce the accounts and the details, appears to be misconceived in law.

11. As per facts of this case the taxpayer filed return under self-assessment, which stood assessed under section 122(3) of the Ordinance, 2001, thereafter the case of the taxpayer was selected for audit under section 177. Notices were issued for production of certain documents and the accounts as required to be maintained in terms of section 174 of the Ordinance, 2001, however, the applicant did not respond to such notices nor produced any documents or the accounts in support of his return of income. It will be advantageous to reproduce the relevant provisions of section 121(1)(d) and section 174(2) of the Income Tax Ordinance, 2001 invoked in the instant matter, which read as follows:-

"121. Best judgment assessment.---(1) Where a person fails to

(d) produce before the Commissioner;-or any person employed by a firm of chartered accountants or a firm of cost and management accountants under section 177, accounts, documents and records required to be maintained under section 174, or any other relevant document or evidence that may be required by him for the purpose of making assessment of income and determination of tax due thereon.

the Commissioner may, based on any available information or material and to the best of his judgment, make an assessment of the taxable income [or. income] of the person and the tax due thereon [and the assessment, if any, treated to have been made on the basis of return or revised return filed by the taxpayer shall be of no legal effect]."

"174(2) The Commissioner may disallow [or reduce] a taxpayer's claim for a deduction if the taxpayer is unable, without reasonable [cause], to provide a receipt, or other record or evidence of the transaction or circumstances giving rise to the claim for the deduction.

12. From the perusal of hereinabove provisions, it emerges that if any person fails to produce the accounts, documents and records required to be maintained under section 174 before the Commissioner/ Taxation Officer, then the Commissioner/Taxation Officer is authorized to make an assessment of the taxable income of the person and the tax due thereon. There seems no embargo upon a Taxation Officer to make best judgment assessment under section 121 in case of a person, who fails to comply with the notice issued under section 177 by the Taxation Officer. It is clear that prior to amendment made by Finance Act, 2010 in section 177 by adding subsection (10), the best judgment assessment in terms of section 121(1)(d) of the Income Tax Ordinance, 2001 could be made by the Taxation Officer, hence objection in this regard as raised by the applicant is misconceived.

13. In response to the re-framed question No.2, as referred to hereinabove, we have noted that Return of Income for the tax year 2005 was filed by the applicant under self-assessment, whereafter the case of the applicant was selected for audit by the Commissioner of Income Tax, Medium Taxpayers Unit Karachi, vide Letter No.4209 of 2006 dated 3-4-2006 on account of following reasons:--

(1) Declared loss for assessment year 2001-2002 has been adjusted instead of assessed loss for tax year 2005.

(2) The profit and loss expenses for tax year 2005 at a rate of 93% of GP are very high, and need to be verified.

3.???????? Except for tax year 2005, losses have been declared.

Information Document Request was issued, which was initially complied by providing some details, thereafter another notice dated 21-9-2006 was issued to the taxpayer requesting him to furnish wealth statements of partners and books of accounts required to be maintained under section 174 of the Income Tax Ordinance, 2001. However, admittedly, the taxpayer did not comply with such notice and in view of non-compliance by the taxpayer, the Taxation Officer issued a notice dated 18-6-2007 under 121(1) of the Income Tax Ordinance, 2001, whereby the taxpayer was confronted with the following terms:

You were, vide information document request under reference, requested to furnish books of accounts prescribed under Rule 30 of Income Tax Rules, 2002. However, it is regrettable to note that response from your side is not received on the due date.

As such, the assessment finalized under section 120 of the Income Tax Ordinance, 2001 for tax year 2004 in your case becomes invalid under the provisions of clause (d) of subsection (I) of section 121 of the Income Tax Ordinance, 2001.

Resultantly, this office intends to make assessment in your case based on available information or material and to the best of judgment, under section 121 of the Income Tax Ordinance, 2001 in the following manner:

- (1) You have not provided evidence regarding refund of Rs.30,000 as mentioned in Annexure IIA to the return of income. Therefore, the same is disallowed for the want of proof.
- (2) You have declared trading expenses to the tune of Rs.3,625,248 without providing their bifurcation. In the absence of books of accounts, this office intends to disallow 50% of these expenses under subsection (2) of section 174 of the Income Tax Ordinance, 2001.
- (3) You have declared profit & loss expenses to the tune of Rs.336,704 without providing their bifurcation. In the absence of books of accounts, this office intends to disallow 50% of these expenses under subsection (2) of section 174 of the Income Tax Ordinance, 2001.

On the basis of these observations, this office intends to finalize your assessment under subsection (1) of section 121 of the Income Tax Ordinance, 2001 in the following manner:--

This may be treated as opportunity of being heard under subsection (1) of section 121 of the Income Tax Ordinance, 2001. You are requested to furnish your reply regarding 'the above-mentioned discrepancies on or before 25-6-2007.

Please note that in case of non-compliance or inappropriate compliance, it will be presumed that the above mentioned working is correct and your income will be assessed accordingly.

14. Since the taxpayer did not respond to such notice, the Taxation Officer finalized the assessment under section 121 of the Income Tax Ordinance, 2001, in which 50% of the trading expenses as well as profit and loss expenses were disallowed for want of evidence. The applicant felt aggrieved by such disallowances, preferred appeal under section 129 of the Income Tax Ordinance, 2001, before the Commissioner (Appeals), however, neither any documents or evidence were produced before the Commissioner (Appeals) in support of the claim of expenditure nor the applicant could point out any error in the order passed by the Taxation Officer. Accordingly, the order of the Taxation Officer was upheld by the Commissioner of Income Tax (Appeals) in the following terms:

"Certain details were due from the appellant. as per above mentioned notice, but such date of hearing also went by default. Obviously the opportunity offered was not availed, and hence the onus lay squarely on the shoulders of the appellant. In consequence the action of the Taxation

Officer-5, Audit Division-II, MTU, Karachi, in framing the assessment under section 121 of the Income Tax Ordinance, 2001 is upheld. The total assessed income amounting to Rs.2,62,322 is also found to be reasonable under the circumstances and hence upheld."

15. The applicant still feeling aggrieved by the order passed by the Commissioner (Appeals) filed an appeal before the Appellate Tribunal Inland Revenue, who vide impugned order dated 19-11-2009 has upheld the orders passed by two forums below and dismissed the appeal of the applicant.

16. From perusal of the impugned order and the grounds of appeal raised by the applicant before the Appellate Tribunal, it appears that the applicant did not produce any document before the Tribunal nor could refer to any such document or evidence either before Taxation Officer or the Commissioner (Appeals), which could possibly support the claim of the applicant towards expenses claimed in trading account and profit and loss account. Before us also it is not the case of the applicant that the notice issued by the Taxation Officer, calling for the books of accounts and the evidence in support of the expenses claimed by the applicant, was duly complied with by the applicant, on the contrary, disallowance of expenses to the extent of 50% out of trading account and profit and loss account, by the Taxation Officer has been disputed. There is no cavil to the proposition that while passing best judgment assessment in the case of a taxpayer, who fails to comply with the legal requirements or the notices issued by the Taxation Officer, seeking certain explanation or calling for the documents/evidence in support of the return of income filed by the taxpayer, a Taxation Officer is required to pass best judgment assessment on the basis of available information or material, whereas he is not permitted under law to make arbitrary and fanciful estimate of the income of a taxpayer.

17. In the instant case, we have noted that nothing extraneous from the available information or material has been taken into consideration nor any addition in this regard has been made in the income of the applicant. Under the provisions of section 121(1)(d) read with section 174(2) of the Income Tax Ordinance, 2001, the Commissioner of Income Tax/Taxation Officer is empowered to disallow or reduce a taxpayer's claim for deduction, if the taxpayer is unable without reasonable cause, to provide a receipt or other record or evidence in support of his claim. The applicant did not produce any material or evidence either before Taxation Officer, Commissioner of Income Tax (Appeals), Appellate Tribunal Inland Revenue (Pakistan) Karachi or even before us to dislodge the treatment meted out by the Taxation Officer in respect of the claim of the applicant towards trading expenses and profit & loss expenses, nor could refer to any past history or parallel cases in this regard. We are not inclined to undertake a subjective appraisal of the accounts to determine the extent of actual disallowance of trading account expenses or the profit and loss account expenses, particularly in the absence of any material, history or parallel case. Moreover, such exercise cannot be undertaken by this Court in its reference jurisdiction which is limited to the extent of examining the questions of law which may arise from the orders passed by the appellate tribunal.

18. Under the circumstances, we are not inclined to interfere with the concurrent finding of the two forums below, recorded under the peculiar facts and circumstances of this case, which otherwise, does not give rise to any substantial question of law. Accordingly, question No.1 is answered in affirmative, and question No.2 as referred to hereinabove is answered in negative, both against the applicant.

Reference Application stands disposed off in the above terms.

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Order accordingly.

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