Tax Review/Taxation

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This special email service from Monday to Friday, part of subscription package, is aimed at keeping you informed about tax and fiscal matters. It contains news, legislative changes, case-law, in-depth articles and analyses covering all areas of taxes at domestic and international level. On every Saturday evening, we email weekly compilation of the entire material. Every month, ***Taxation*** in printed form, is sent through post and digital version of ***Tax Review International*** is made available for download at www.huzaimaikram.com.

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United States

Amazon collects sales tax in four more US states

With Amazon agreeing to begin the collection of sales taxes on January 1 in four more US states – Iowa, Louisiana, Nebraska, and Utah – the online retailer is informing its customers that taxes are now charged on items shipped to 32 states.

Amazon has been increasing the number of states in which it agrees to collect sales tax, particularly where it is building new warehouses. However, it has also been fighting the imposition of the tax on its online sales in many states, particularly those where it does not have a "physical presence."

Amazon's preferred solution would be for the US Congress to resolve the uncertainties still being caused by the 1992 "Quill" ruling of the US Supreme Court (SCOTUS) that established the physical presence test, where retailers are only required to collect sales tax in states where they also have bricks-and-mortar stores. It was also then decided that only Congress has the authority to regulate interstate commerce under the Commerce Clause of the US Constitution.

However, as Congress continues to be inactive in this respect and SCOTUS has refused, so far, to take up a reconsideration of Quill, states have been making a concerted push to collect taxes on internet purchases.

Amazon has now agreed to collect Iowa's six percent sales tax on online purchases by Iowan residents from January 1, 2017. In addition, from the same date, Amazon started to charge the five percent, 5.5 percent, and 4.7 percent state sales tax on purchases sent to Louisiana, Nebraska, and Utah, respectively. Arrangements may also be made with regard to local sales taxes.

Amazon now informs its customers on its website that items shipped to 32 states are subject to the collection of sales taxes. These include Alabama, Arizona, California, Connecticut, District of Colombia, Florida, Georgia, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Nebraska, Nevada, New Jersey, New York, North Carolina, North Dakota, Ohio, Pennsylvania, Tennessee, Texas, Utah, Virginia, Washington, West Virginia, and Wisconsin. – *Courtesy tax-news.com*

US chamber urges health insurance tax repeal

With talk beginning in the new Congress of a repeal of President Barack Obama's Affordable Care Act (ACA), the US Chamber of Commerce (USCC) has urged the immediate elimination of the health insurance tax (HIT) as an immediate necessity.

Beginning in 2014, the ACA provided for the HIT to be assessed on all health insurance providers (referred to as covered entities). The Internal Revenue Service calculates the tax amount for each covered entity based on its portion of market premiums for the data year, which is the year immediately preceding the year in which the tax is payable.

Although the Protecting Americans from Tax Hikes (PATH) Act, approved at the end of 2015, suspended the tax for 2017, the USCC pointed out that, without its immediate repeal, the HIT "will start hitting premiums again as early as February. As small businesses and consumers begin enrolling in health insurance coverage for 2018, they will begin paying premiums which include this tax. Insurance policies that provide coverage into calendar year 2018 will factor this tax into premiums."

The Chamber also noted that, according to previous analysis, "the HIT is a middle class tax. … The average family will pay an additional USD5,000 over 10 years in extra premiums because of the HIT."

Further, it added that "84 percent of the tax burden for the four-year period from 2014-2018 would be borne by those earning less than USD100,000 per year and more than 50 percent of the tax burden would be borne by those earning less than USD50,000 per year."

"The HIT is a tax on health plans sold in the fully-insured market, 86 percent of these plans are purchased by small businesses," the USCC continued. "Since they bear much of the brunt of the tax, many small business owners feel they're being punishing for offering health insurance to their employees." – *Courtesy tax-news.com*

Ireland

2016 'A good year for Irish public finances'

Irish Finance Minister Michael Noonan has said that "the amount of tax collected in 2016 is at an historic high."

Noonan welcomed the publication of the year-end Exchequer Returns for 2016. At the end of December, EUR47.86bn (USD50.29bn) had been collected in tax revenue, up 1.4 percent (EUR639m) on target and five percent (EUR2.26bn) on the previous year.

At EUR1.01bn, the budgetary deficit was up on the EUR64m recorded at the end of 2015, with the Finance Department attributing this to an expected decline in banking-related receipts. It said that when the one-off capital receipts from banking-related transactions from 2015 and 2016 are excluded, the Exchequer deficit shows an underlying year-on-year improvement of EUR864m.

Commenting on the improvement in the tax take, Noonan said: "It has provided not only for the extra expenditure incurred in 2016 but for the substantial tax reductions announced in the Budget in October 2015 and delivered during the course of 2016."

In cumulative terms, income tax revenues for 2016 were 0.9 percent (EUR174m) ahead of target and up 4.4 percent (EUR810m) year-on-year. Value-added tax receipts were up four percent on 2015, but down 3.4 percent on profile. The Department said that December was a non-VAT due month, and receipts for the month were EUR26m below target, due to higher than expected VAT repayments.

Corporation tax continued to perform strongly. On an annual basis, corporation tax receipts were 11 percent (EUR737m) higher than expected, and were up seven percent (EUR480m) year-on-year. – *Courtesy tax-news.com*

United Kingdom – Switzerland

UK-Swiss terminate savings tax deal for automatic info exchange

The UK and Switzerland have terminated tax arrangements under the Savings Tax Directive and will instead share information in tax matters automatically under the Common Reporting Standard.

The UK Government said, under the switch to the OECD's Common Reporting Standard, UK taxpayers will no longer be able to pay a withholding tax to stop their information being shared with HM Revenue and Customs.

Under the UK-Swiss Confederation Taxation Co-operation Agreement, agreed in 2011 and implemented from 2013, UK residents with Swiss bank accounts were required to either permit the disclosure of bank details to HMRC or pay a substantial withholding tax to maintain their anonymity. This arrangement was negotiated on the basis of the EU Savings Tax Directive.

Although the UK Government at the time had been optimistic that the deal would bring in substantial revenues, the deal resulted in just a quarter of the anticipated revenue in its first fiscal year in operation. The Agreement has now been terminated. – *Courtesy tax-news.com*

Oman

Oman hikes airport tax, announces tax reforms

Oman increased its airport tax by OMR1 (USD2.6) to OMR11 per head on January 1, 2017.

The tax is added to international fares, including transfers. Domestic flights will not be affected by the increase.

Meanwhile, in its new Budget, Oman has announced plans to reform the country's income tax laws and introduce new taxes on tobacco and alcohol. It will also rein in tax breaks for certain businesses and make tax administration more efficient. – *Courtesy tax-news.com*

Mass transit projects:: ECC likely to grant exemption from taxes, duties

The Economic Co-ordination Committee (ECC) of the Cabinet is likely to grant exemption from taxes and duties on import of equipment for rail-based mass transit projects in provinces under China-Pakistan Economic Corridor (CPEC) today (Friday). Sources told that the ECC will also consider a request for reduction in the price of imported urea available with National Fertilizer Marketing Limited (NFML).

The proposal of Ministry of Planning Development and Reforms is on the agenda of the ECC meeting. The ministry has requested for exemption in duties and taxes, including withholding tax, on the import of equipment for Lahore Orange Line mass transit project as well as for Quetta and Karachi projects.

The governments of Pakistan and China entered into a Framework Agreement on 22nd May, 2014 for construction, equipment, procurement and financing of Lahore Orange Line Metro Train Project. As per framework agreement, the Orange Line will be designed, constructed and supervised by Chinese enterprises. Identification of Chinese companies for execution of the project from amongst the recommended companies through a competitive bidding procedure was also agreed upon.

The project to be executed on EPC (Engineering Procurement and Construction) mode envisages construction of a 27.1 kilometres-long dedicated signal-free corridor for rail-based mass transit system in Lahore along with 26 stations, one depot and procurement of rolling stock with allied facilities. The project was approved by the ECNEC on 13th May, 2015 at the cost of Rs 165.226 billion including a Foreign Exchange Component (FEC) of Rs 103.0986 billion without involvement of funding from the federal PSDP. The loan amount would be repaid by the government of Punjab.

Punjab transport department is getting the project implemented through the Punjab Mass Transit Authority and Lahore Development Authority respectively. Bids from two Chinese companies, namely CR-NORINCO JV and SINORAIL - JV, were received on 18th July, 2014.

The government of Punjab signed the commercial contract agreement on 20th April, 2015 with the lowest evaluated bidder ie CR-NORINCO-JV for implementation of the project. 'The commercial contract includes provision and installation of electrical and mechanical (E&M) equipment with testing and commissioning, besides civil work being sublet to the Pakistani side.

The contract included withholding income tax at the rate of 6% applicable at the time of bidding in the bid price. As per commercial contract, the income withholding tax for E&M works, 6% of contract price for E&M works, was considered. The employer will be responsible for the payment of balance due to increase in income tax withholding rate in accordance with the regulations of Pakistan. Unless otherwise stated, the contractor would be exempted from all obligations or responsibilities for the payment of all the other Pakistani taxes arising of the contract such as sales tax and contract tax.

Furthermore, the Chinese contractor, under the commercial contract, will be importing all E&M equipment under its own name for subsequent ownership of the Pakistani side. The commercial contract further reads that unless otherwise stated in this contract, the employer would pay all customs, import duties and taxes in consequences of the importation of equipment to be furnished in the Orange Line Project. If the contractor is required to pay such customs, import duties and taxes, the employer would reimburse the amount, thereof, within 30 days upon submission of proper documentation, invoice and proof of payment.

The total incidence of tax on CR-NORINCO JV increases beyond 6%, the additional tax liability, if any, will have to be paid for by the Pakistani side in accordance with the provisions of contract agreement. As a result, the government of Punjab has estimated that roughly Rs 20 billion are to be paid in the form of taxes and duties on import of equipment for Lahore Orange Line Metro Train Project which will have to be borne by the provincial government as charge on Provincial Consolidated Fund, if exemptions are not granted.

The government of Punjab, therefore, requested for a grant of exemption from the ECC in respect of Lahore Orange Line Metro Train Project on the lines allowed to NHA for CPEC infrastructure projects on grounds that this project is acknowledged within CPEC framework by the Chinese side as ongoing building of CPEC in the framework agreement that CR-NORINCO JV may be exempted from withholding income tax beyond 6% of E&M contract price and CR-NORINCO JV may be exempted from all tax amounts including but not limited to income taxes, withholding taxes, sales taxes, custom duties and taxes on import of equipment to be furnished in Orange Line Project.

The Quetta Mass Transit Project sponsored by Balochistan has been agreed upon with the Chinese side for implementation through CPEC under Chinese financing. Furthermore, Karachi Circular Railway (KCR) project sponsored by the government of Sindh has also been approved. Modalities of both projects were discussed with the Chinese side in the Joint Co-operation Committee (JCC) meeting. The cost of these projects including the loan repayment will be borne by the respective provincial governments.

The ministry forwarded a proposal to the ECC requesting the grant of exemptions from income tax withholding beyond 6% of E&M contract price and taxes and duties on import of equipment to be furnished / installed for Quetta Mass Transit Project and Karachi Circular Railway (KCR) may also be considered, in principle. – *Courtesy Business Recorder*

There's 'way out' for those who want to come into tax net: Dar

Following selection of 93,277 cases for audit through computerised balloting, Finance Minister Ishaq Dar said Thursday that some 'way out' could be provided to those who wanted to come into tax net after witnessing developments on OECD's anti-tax evasion agreement at international level and making global asset registry mandatory through fresh companies ordinance in Pakistan.

He was addressing a function arranged by the Federal Board of Revenue (FBR) to select parameter and risk-based audit through computerised balloting at the FBR House here on Thursday. Parametric computer ballot was carried out as per Audit Policy 2016 for selection of cases for audit for Tax Year 2015 and Tax period July 1, 2014 to June 30, 2015, in respect of Income Tax, Sales Tax & FED. Ishaq Dar pushed the button to select the cases for corporate sector of income tax.

Out of total 93,277 cases, the FBR has selected 2,173 cases for audit from corporate sector income tax, 82,090 cases from non-corporate sector of income tax, 987 cases from Sales Tax (corporate), 7,976 from Sales Tax (non-corporate), 30 cases from Federal Excise Duty (corporate) and 21 cases from FED (non-corporate). National Tax Numbers (NTNs) of cases selected for audit have been displayed on the official website of FBR.

Dar dispelled the impression that the revenue has been increased through imposition of new taxes, saying, “No new taxes have been imposed but tax net has been widened.” He said in 2018, the energy crisis will not only come to an end but the electricity will be available in surplus.

While addressing the ceremony for selection of audit, Ishaq Dar said that the FBR has selected 7.5 per cent cases for holding audit out of total received returns under Universal Self Assessment Scheme (USAS). Dar said that all those who are honest should not worry about it if their names were included into the list of selected audit cases. He said that he had faced such things in life but came out with clean hands.

Without mentioning anyone’s name, the minister said that the jet plane was declared on company’s name but it was being used for political purposes. The minister said that he was the one who dared present summaries before the cabinet for signing Organisation for Economic Co-operation and Development (OECD) agreement on anti-tax evasion for exchange of information and for initiating agreement with Swiss authorities on bilateral level. “We have refused to grant extraordinary concessions to Swiss authorities and now they have invited us to initiate talks on exchange of information,” he maintained.

He cited examples of the US and UK and said that one rich woman was selected for audit and put behind the bar for three years because she had declared one painting on her company’s name but had hung it at her own house. He said that Swiss authorities had demanded reduction in taxes and MFN status in their favour but they did not succumb to the pressure. He said that the SECP issued notices to 42,000 companies related to global asset registry after promulgation of fresh companies’ ordinance that was replaced after 34 years. He said that one should pay his due taxes as the FBR achieved 60 per cent revenue in last three years as it was used to achieve growth of just 3.3 per cent before 2013.

Special Assistant to PM on Revenues Haroon Akhtar Khan said that it was lifeline for USAS to hold audit in effective manner as it could jeopardise the whole system if the audit remained ineffective. He said that unfortunately the audit was challenged into courts so now they decided to hold parameters and risk-based audit after getting guidelines from the judiciary. “We have excluded 65 per cent returns from the audit as only those sectors were included which possessed high risks," he added.

In UK, the IR authorities could check restaurants so deterrence is needed to be put in place to make USAS successful in Pakistan, he said. Haroon Akhtar emphasised the importance of audit in a country like Pakistan where universal self assessment scheme is prevalent. He ensured that the tax audit shall be conducted in a professional and transparent manner.

FBR Chairman Nisar Muhammad Khan apprised of the paradigm shift in selection of cases for audit. Earlier, it was random ballot but for the Tax Year 2015, the selection is based on risk parameters. Resultantly compliant taxpayers will not be selected. Later on, computer ballot was conducted in respect of SIX categories ie corporate cases of Income Tax, Sales Tax & FED & Non-corporate case of Income Tax, Sales Tax and FED. The ceremony was attended by representatives of Federation of Pakistan Chamber of Commerce and Industry (FPCCI), Institute of Chartered Accountant of Pakistan (ICAP), Pakistan Tax Bars Association (PTBA), Pakistan Tax Advisors Association (PTAA), Islamabad Women Chamber of Commerce and Industry, and FBR officers.

Ishaq Dar initiated the ballot process by pressing computer button for Income Tax (Corporate), Haroon Akhtar Khan pressed button for Income Tax (Non-Corporate), Vice President of FPCCI Mian Shaukat Masood pressed the button for Sales Tax (Corporate) and Mian Abdul Ghaffar, Advocate President of Pakistan Tax Advisors Association, pressed the button for Sales Tax (Non-Corporate). Further Selection of cases for Federal Excise (Corporate) was made by Mohsin Nadeem, President Pakistan Tax Bar Associations, and Samina Fazal, representative of Islamabad Women Chamber of Commerce & Industry, completed the process by pressing the button for Federal Excise (Non-Corporate). – *Courtesy Business Recorder*

SBP proposes issuance of ISBs, tax exemption on NSS

The State Bank of Pakistan (SBP) has proposed introduction of Islamic Saving Bonds and tax exemption on National Savings Scheme's return on small investment aimed at attracting more investment. The downward revision in NSS rates continued to dampen the net investment in NSS instruments, which recorded an increase of only Rs 26.8 billion during Q1-FY17, the SBP revealed in its recent report.

According to a report, the composition of NSS indicates that all major schemes, except for Defense Saving Certificate (DSC), witnessed decline in inflows during the quarter. The major contribution came from Behbood Saving Certificate (BSC) that is being exempted from withholding tax and Zakat.

Special Saving Scheme (SSS) and Regular Income Certificate (RIC) witnessed net retirements during the period. It is worth noting that the share of NSS in domestic debt stock has been falling persistently. This trend needs to be reversed in order to reduce the government's reliance on borrowing from banks and external sources. Therefore, the SBP, in its first quarterly report on economy, has suggested the following recommendations to increase NSS inflows through introduction of new retail instruments as well as changes in the existing ones.

Expanding distribution network: Distribution is an important factor in mobilising funds through retail debt issuing activity. In areas without national saving centers and/or banks, the NSS instruments could be offered to general public through retail shops offering some money transfer facility or through better marketing and optimally utilising the existing set-up of Pakistan Post Offices.

Allowing flexibility on premature withdrawal: Anecdotal evidence suggests that some retail savers do not want to lock in their savings for a longer period, and hold cash to meet expenses related to children's education or marriage, etc. Therefore, offering an option to withdraw investment without much cost in terms of forgone interest - that is, offering return on pro-rata basis - could encourage that segment to invest in NSS instruments and withdraw when the need arises.

Islamic bonds (floating rate/asset based): A large segment of the population in Pakistan does not like to keep their savings in bank accounts or invest in NSS instruments to avoid interest. Introduction of retail products on the lines of Ijara Sukuk might attract such small savers who prefer to invest in instruments based on the principles of Islamic finance.

Electronic retail system: The objective to design electronic retail debt instruments is to reach the investors who consider it cumbersome to go to a bank or national saving centre. Although the individuals in Pakistan have direct access to primary market of government securities through Investor Portfolio Services

Account, no such facility is available for non-tradable retail debt instruments. The introduction of electronic retail system to subscribe retail debt instruments or withdraw their investment would not only attract more retail investors but also could make it a relatively cost-efficient option.

Tax exemption on return for a minimum investment: The return/profit on most NSS instruments are subject to withholding taxes, except for BSC and PBA. To attract more investment from small savers, return on some minimum level of investment can be exempted from the withholding tax.

Inflation-indexed bonds: In countries where inflation is relatively high and volatile, people would want to protect the purchasing power of their assets. In inflation-indexed bonds, both the capital and coupon are linked to the consumer price inflation. Many countries, such as US, UK, Japan and South Africa, offer inflation indexed retail bonds to the savers. However, the disadvantage to government for issuing such bonds is the increase in cost with the increase in inflation.

Exchange rate indexed bonds: Some investors are more concerned about the value of their assets in terms of foreign currency. To make debt instruments attractive to such investors, creating a linkage to an international currency might be an alternate option. Such bonds are generally denominated in domestic currency but the coupon and capital amount are linked to an international currency. Thus, the government does not need to have foreign exchange to serve this type of debt. – *Courtesy Business Recorder*

GST collection: FBR implementing new system for cellular companies

The Federal Board of Revenue (FBR) is implementing a new system for cellular companies for accurate collection/deposit of withholding tax from its subscribers through online withholding data integration with all mobile operators. Senior FBR officials informed that the tax authorities have decided to commence the process for establishing online withholding data integration with all cellular companies simultaneously to ensure precision in the count of taxes collected from phone users.

“The FBR has decided to launch a pilot project for real time connectivity from January 17 to ensure precision in the count of taxes collected from phone users,” said FBR officials while briefing the Senate Standing Committee on Information Technology and Telecom. The committee met with Shahi Syed in the chair here on Thursday.

The committee was briefed on the mechanism adopted by FBR and Pakistan Telecommunication Authority (PTA) regarding collection of taxes ie GST and WHT from cellular operators. The committee raised question on the mechanism of tax collection from mobile users and its deposit in the national exchequer.

The chairman of the committee observed that it is a serious issue whereby billions of rupees are being collected on account of GST, WHT and Service charges from cellular subscribers, even from poor people of Pakistan who do not fall under the tax network, and unfortunately the FBR has still no mechanism to analyse the data of taxes collected by Telcos; resultantly, the FBR has failed to provide relief to the common man. Members of the committee suggested that legislation may be brought in the Parliament in this regard.

The FBR officials admitted that it is a policy issue and endorsed the idea making legislation in this regard. The FBR officials informed that Rs 47 billion were collected as WHT from consumers, where Rs 14 billion were adjusted. However, the chairman said that the amount is estimated to be huge. He further said telecom companies are collecting an estimated amount of Rs 81 billion per annum from consumers in the name of maintenance and services.

Regarding the mechanism adopted by FBR for collection of taxes from cellular operators, the FBR representative briefed the committee that they have established a new Intelligent Tax System with the help of PRAL (Pakistan Revenue Automation Pvt Ltd), which will help out analyse the exact data of taxes collected by the mobile phone operators. Through this system the exact usage and taxes collection process will be properly monitored by the FBR. For this purpose a pilot project for real-time connectivity is being launched which might start working by January 17, 2017.

Senator Rehman Malik asked about the details and figures collected on account of withholding tax from cellular phone subscribers and the mechanism adopted for returning the same to them. The FBR replied that a mechanism is being worked out and in three to four months they would submit a detailed report in this regard with the committee.

The chairman committee also directed to provide comprehensive details of Sales Tax/FED deposited by the Telcos into the government treasury of the Federation as well as all provinces, during the last three years.

The committee also asked about the action taken by the ministry on the recommendations of committee given in its last meeting regarding payment of pension to the pensioners of PTCL at the rate announced by the government from time to time. The committee was briefed by the ministry that the matter is still sub judice in the apex court. On a query raised by the chairman committee regarding next date of hearing of the case, it was apprised that the same has not been fixed yet. – *Courtesy Business Recorder*

Tax evasion in various sectors needs to be checked, taxmen told

Directorate General of Intelligence and Investigation Inland Revenue (IR), Federal Board of Revenue (FBR), will implement a national enforcement strategy to control the illicit trade of non-duty paid cigarettes and take measures to control tax evasion in cement sector, sugar mills, services sector/professionals, paper/paper board industry and cosmetic sector.

Sources told here on Thursday that the daylong Directors' Conference of the Intelligence and Investigation IR was held at the FBR House. Beside all intelligence directors of I&I IR, the morning session was attended by FBR Chairman Nisar Muhammad Khan. Evening session was attended and addressed by Special Assistant to PM on Revenues Haroon Akhtar Khan. FBR Members and senior intelligence officials from the field formations attended the conference.

It was a first of its kind of conference which focused whole day on different strategies and measures to control evasion in potential sectors. The conference discussed novel ideas/proposals to check tax evasion, revenue leakages, frauds and money laundering under the mandate of the agency and took important decisions. Khawaja Tanveer Ahmad, Director General Intelligence & Investigation (IR) approved a strategy paper to check tax evasion and fiscal frauds. The conference reviewed the overall performance of each Directorate of I&I IR and assigned new targets to the field formations to assist the FBR in achievement of assigned revenue collection target for 2016-17.

Directorate General of Intelligence and Investigation Inland Revenue (IR), Federal Board of Revenue (FBR), will take new measures to control the illicit trade of non-duty paid cigarettes by strengthening the agency's workforce and joint actions by DG I&I IR and customs intelligence.

Sources said that the issue of illicit trade in tobacco sector was discussed during the Directors' Conference of the Intelligence and Investigation IR held at the FBR House. It was noted with concern that the tax evasion in tobacco industry has increased which requires immediate enforcement measures to check movement of non-duty paid/smuggled cigarettes. It has been proposed to establish check posts of the Intelligence and Investigation IR to control movement of non-duty paid cigarettes. This would be instrumental in seizure of non-duty paid items on the spot.

Another proposal is to conduct joint enforcement actions by the DG I&I IR and customs intelligence.

Sources said that joint operations by the DG I&I IR and customs intelligence could also play an important role in checking tax evasion in the tobacco industry. The conference noted with concern that there are reports of tax evasion in sugar sector, cement manufactures, cosmetic industry, services providers including doctors and medical practitioners and high net individuals operating out of the tax net.

The conference also discussed the issue of stay orders granted by the courts, which are hindering actions in big cases of tax frauds and tax evasion. Only in Karachi 58 stay orders have been issued against the agency's enforcement actions of tax evasion and concealments. The agency's high-ups also informed the conference about huge revenue implications involved in major cases where stay orders were issued without hearing directorate general I&I IR side.

The FBR's intelligence arm is confident to complete action against the tax evaders and those committing tax frauds to ensure recovery of the evaded amount to the tune of billions of rupees, they said. The Directorate General of I&I-IR was established under section 230 of the Income Tax Ordinance 2001 and has been conferred upon with powers through respective FBR's SROs vide Nos. 115(1)/201 5, 116(1)/2015 and 117(1)/2015 dated 09.02.2015. Directorate General of I&I-IR is mandated with enforcement of Income Tax Ordinance, 2001, Sales Tax Act, 1990 and FED Act, 2005. The key function of the Directorate General is to act against tax frauds/evasion and create deterrence against such fiscal crimes.

The conference was informed that since inception, the Directorate General I&I-IR has been highly successful in its core functions of enforcement, deterrence and revenue realisation in short span of time. Having faced deterring actions by I&I-IR, the tax evading community has developed a reactive trend of incessant litigation against the department. Success rate of department's actions under respective sections of fiscal statutes and prosecution proceedings has been very encouraging. Consequentially the taxpayers are in a rush to file suits and writ petitions in the courts. The courts have granted stay/restraining orders against the departmental proceedings consequent to legal actions taken under sections 175, 176 and 177 of Income Tax Ordinance, 2001 and section 37B, 38 and 40 of the Sales Tax Act, 1990 and section 23 of FED Act, 2005 in particular.

The agency also decided to intensify efforts to complete investigations of anti-money laundering cases. New cases of money laundering cases are being detected based on suspicious transactions reports received by the agency.

The conference reviewed in detail progress on strategy paper for 2016-2017, performance in High Networth Individual (HNI) cases, progress in finalisation of cases by the field formations, progress regarding litigation cases, progress on STRs-anti money laundering activities, enforcement activities such as raids, FIRs, arrests, etc, and sharing of out of box investigation carried out by each directorate. – *Courtesy Business Recorder*

FBR sends list of over 100 taxpayers to field formation

The Federal Board of Revenue (FBR) has reportedly communicated a list of over 100 taxpayers to its field formation for aggressive tax recovery exercise in order to overcome a whopping revenue shortfall of over Rs 127 billion reported in the first half of current fiscal year; it is learnt here Thursday.

According to sources, the FBR has appeared panicky especially after witnessing a revenue shortfall of over Rs 127 billion in the first half of current fiscal year hence the list of over 100 taxpayers has been established to commence aggressive tax recovery exercise. In first six months of current fiscal year, the revenue collection of Rs 1466 billion was made as against the target of Rs

1593 billion, depicting a whopping revenue shortfall of over Rs 127 billion.

Keeping the said in view, the list of over 100 taxpayers has been made in haphazard manner because the board has also included non-resident companies in it, which the sources termed as sheer negligence of law. They said that the board had communicated the said list to its field formation and directed them to ensure tax recoveries at any cost. Therefore, the field officers despite realizing that it was against the law have no option but to start attaching the bank accounts for tax recoveries, dragging the taxpayers in a state of hysteria.

Meanwhile, Adnan Mufti confirmed that the FBR has initiated tax recovery exercise against non-resident companies, saying that board without fulfilling due procedure has also attached the bank accounts of non-resident companies. He further said that the issue came on surface when the withholding zone of regional tax office had issued tax recovery notice of Rs 1.5 million to the non-resident company and its bank accounts have later been attached without issuing recovery order or giving hearing opportunity.

When contacted, top tax official denied to have established the list of over 100 taxpayers for tax recoveries, saying that FBR did not communicate any list to its field formation. He also assured to inquire the matter and resolve the issue if any such practice being continued at tax departments across the country. – *Courtesy Business Recorder*

Firpo asks Nawaz to withdraw FBR's discretionary powers

President of Karachi Chamber of Commerce and Industry (KCCI), Shamim Ahmed Firpo has urged the Prime Minister Mian Muhammad Nawaz Sharif to withdraw all discretionary powers given to the Federal Board of Review (FBR) which have proven to be counterproductive.

In a letter to the Prime Minister, on behalf of the KCCI, Firpo urged him to withdraw all the discretionary powers given to the FBR in the last four budgets which, the letter said, proved to be counterproductive and a tool to harass the business and industrialist community alongside increasing corruption manifolds. The letter further said that Karachi Chamber being the largest chamber of the country and representing the business and industrialist community of Karachi whose participation in the economy/revenue of Pakistan is exceptional and undeniable, had been submitting budget proposals in the past.

"However, this was not the case anymore as our Budget Proposals submitted during the last four budgets have been totally ignored and we were never taken on board prior to finalising these budget documents. On the contrary, massive discretionary powers were entrusted to corrupt FBR officials who used these powers to further twist arms and squeeze the existing registered taxpayers and that is the basic reason why the overall tax-base remains limited between 800,000 to 900,000 income taxpayers, and also the number of registered Sales Tax payers remains similar," complained the letter.

For that reason KCCI, under protest, decided not to submit budget proposals now.

The KCCI letter praised finance minister Ishaq Dar saying he is doing a great job but somehow FBR Officials have been successful in acquiring these discretionary powers through the Finance Bill and even blocking the recommendations of Tariff Reform Commission (TRC) on the subject matter.

The KCCI letter requested the Prime Minister to consider the hardships being faced by the business and industrialist community due to widespread corruption and arm-twisting tactics by the FBR which has to be tackled. Shamim Firpo proposed that the problem could be sorted out by completely withdrawing the discretionary powers and that would strengthen business and industrialist environment for the progress and prosperity of Pakistan. He said that the KCCI's proposal the only way forward to enhance the revenue collection by attracting new taxpayers into the net. KCCI president pointed out following discretionary powers of the FBR: SALES TAX ACT 1990: (1) Section 37, Sub Section (3); (2) Section 37A; (3) Section 37B; (4) Section 51; (5) Section3 (Sub Section-7); & (6) Section-3 (Sales Tax Scheme Chapter-II of Sales Tax Special procedure 2007).

INCOME TAX: (1) Powers to Enter and Search U/S 175(1) & (2); & (2) Powers to Obtain Information under Section 176 of the Income Tax Ordinance 2001 The letter said that federal excise duty (FED) under Federal Excise Act 2005, causes dual and exorbitant taxations and also proved to be very detrimental for numerous businesses so such FED should be immediately phased out or drastically reduced after consultation with concerned stakeholders. *– Courtesy Business Recorder*

2017 TRI 22 (S.C. Ind.)

SUPREME COURT OF INDIA

A.K. Sikri and Abhay Manohar Sapre, JJ.

Gopal and Sons (HUF)
v.
CIT Kolkata-XI

FACTS/HELD

S. 2(22)(2) Deemed Dividend: The argument that as the shares are issued in the name of the Karta, the HUF is not the "registered shareholder" and so s. 2(22)(e) will not apply to loans paid to the HUF is not correct because in the annual returns filed with the ROC, the HUF is shown as the registered and beneficial shareholder. In any case, the HUF is the beneficial shareholder. Even if it is assumed that the Karta is the registered shareholder and not the HUF, as per Explanation 3 to s. 2(22), any payment to a concern (i.e. the HUF) in which the shareholder (i.e. the Karta) has a substantial interest is also covered

1. The assessee is a Hindu Undivided Family (HUF). During the previous year to the Assessment Year, the assessee had received certain advances from one M/s. G.S. Fertilizers (P) Ltd. (hereinafter referred to as the 'Company'). The Company is the manufacturer and distributor of various grades of NPK Fertilizers and other agricultural inputs. In the audit report and annual return for the relevant period, which was filed by it before the Registrar of Companies (ROC), it was found that the subscribed share capital of the said Company was Rs. 1,05,75,000/- (i.e., 10,57,500 shares of Rs. 10/- each). Out of this, 3,92,500 number of shares were subscribed by the assessee which represented 37.12% of the total shareholding of the Company. From this fact, the AO concluded that the assessee was both the registered shareholder of the Company and also the beneficial owner of shares, as it was holding more than 10% of voting power. On this basis, after noticing that the audited accounts of the Company was showing a balance of Rs. 1,20,10,988/- as "Reserve & Surplus" as on 31st March, 2006, this amount was included in the income of the assessee as deemed dividend. In the appeal filed by the assessee, the

aforesaid addition was affirmed by the CIT(A). The Tribunal reversed the CIT(A). The High Court reversed the Tribunal. Before the Supreme Court, the assessee argued that being a HUF, it was neither the beneficial shareholder nor the registered shareholder. It was further argued that the Company had issued shares in the name of Shri Gopal Kumar Sanei, Karta of the HUF, and not in the name of the assessee/HUF as shares could not be directly allotted to a HUF. On that basis, it was submitted that provisions of Section 2(22)(e) of the Act cannot be attracted. The Supreme Court had to consider the following question of law:

> "Whether in view of the settled principle that HUF cannot be a registered shareholder in a company and hence could not have been both registered and beneficial shareholder, loan/advances received by HUF could be deemed as dividend within the meaning of Section 2(22)(e) of the Income Tax Act, 1961 especially in view of the term "concern" as defined in the Section itself?"

2. HELD by the Supreme Court dismissing the appeal:

(i) Section 2(22)(e) of the Act creates a fiction, thereby bringing any amount paid otherwise than as a dividend into the net of dividend under certain circumstances. It gives an artificial definition of 'dividend'. It does not take into account that dividend which is actually declared or received. The dividend taken note of by this provision is a deemed dividend and not a real dividend. Loan or payment made by the company to its shareholder is actually not a dividend. In fact, such a loan to a shareholder has to be returned by the shareholder to the company. It does not become income of the shareholder. Notwithstanding the same, for certain purposes, the Legislature has deemed such a loan or payment as 'dividend' and made it taxable at the hands of the said shareholder. It is, therefore, not in dispute that such a provision which is a deemed provision and fictionally creates certain kinds of receipts as dividends, is to be given strict interpretation. It follows that unless all the conditions contained in the said provision are fulfilled, the receipt cannot be deemed as dividends. Further, in case of doubt or where two views are possible, benefit shall accrue in favour of the assessee.

(ii) A reading of clause (e) of Section 2(22) of the Act makes it clear that three types of payments can be brought to tax as dividends in the hands of the share holders. These are as follows:

(a) any payment of any sum (whether as representing a part of the assets of the company or otherwise) by way of advance or loan to a shareholder.

(b) any payment on behalf of a shareholder, and

(c) any payment for the individual benefit of a shareholder. [See: Alagusundaran Vs. CIT; 252 ITR 893 (SC)]

(iii Certain conditions need to be fulfilled in order to attract tax under this clause. It is not necessary to stipulate other conditions. For our purposes, following conditions need to be fulfilled:

(a) Payment is to be made by way of advance or loan to any concern in which such shareholder is a member or a partner.

(b) In the said concern, such shareholder has a substantial interest.

(c) Such advance or loan should have been made after the 31st day of May, 1987.

(iv) Explanation 3(a) defines "concern" to mean HUF or a firm or an association of persons or a body of individuals or a company. As per Explanation 3(b), a person shall be deemed to have a substantial interest in a HUF if he is, at any time during the previous year, beneficially entitled to not less than 20% of the income of such HUF.

(v) In the instant case, the payment in question is made to the assessee which is a HUF. Shares are held by Shri. Gopal Kumar Sanei, who is Karta of this HUF. The said Karta is, undoubtedly, the member of HUF. He also has substantial interest in the assessee/HUF, being its Karta. It was not disputed that he was entitled to not less than 20% of the income of HUF. In view of the aforesaid position, provisions of Section 2(22)(e) of the Act get attracted and it is not even necessary to determine as to whether HUF can, in law, be beneficial shareholder or registered shareholder in a Company.

(vii) It is also found as a fact, from the audited annual return of the Company filed with ROC that the money towards share holding in the Company was given by the assessee/HUF. Though, the share certificates were issued in the name of the Karta, Shri Gopal Kumar Sanei, but in the annual returns, it is the HUF which was shown as registered and beneficial shareholder. In any case, it cannot be doubted that it is the beneficial shareholder. Even if we presume that it is not a registered shareholder, as per the provisions of Section 2(22)(e) of the Act, once the payment is received by the HUF and shareholder (Mr. Sanei, karta, in this case) is a member of the said HUF and he has substantial interest in the HUF, the payment made to the HUF shall constitute deemed dividend within the meaning of clause (e) of Section 2(22) of the Act. This is the effect of Explanation 3 to the said Section, as noticed above. Therefore, it is no gainsaying that since HUF itself is not the registered shareholder, the provisions of deemed dividend are not attracted. For this reason, judgment in C.P. Sarathy Mudaliar 1972 SCR 1076, relied upon by the learned counsel for the appellant, will have no application. That was a judgment rendered in the context of Section 2(6-A)(e) of the Income Tax Act, 1922 wherein there was no provision like Explanation 3.

Appeal accordingly dismissed.

Civil Appeal No. 12274 of 2016.

Decided on: 4th January, 2017.

Present at hearing: S.B. Upadhyay, for Assessee.

JUDGMENT

A.K. Sikri, J.–

The appellant/assessee, in the instant appeal, has raised following question of law for determination:

> "Whether in view of the settled principle that HUF cannot be a registered shareholder in a company and hence could not have been both registered and beneficial shareholder, loan/advances

received by HUF could be deemed as dividend within the meaning of Section 2(22)(e) of the Income Tax Act, 1961 especially in view of the term "concern" as defined in the Section itself?"

2) The aforesaid question has arisen, which pertains to Assessment Year 2006-07, under the following circumstances:

3) The assessee herein had filed the return in respect of the said Assessment Year declaring his total income at Rs. 1,62,745/-. The Assessing Officer (for short, 'AO') carried out the assessment resulting into passing of assessment orders dated 31st December, 2008 whereby the net income of the assessee was calculated at Rs. 1,30,31,280/-. Obviously, number of additions were made which contributed to the enhancement of income to the aforesaid figure, in contrast with the paltry income declared by the assessee. Here, we are concerned only with one addition which was made on account of deemed dividend within the meaning of Section 2(22)(e) of the Income Tax Act, 1961 (hereinafter referred to as the 'Act'). Suffice it to state that other additions were deleted by the Income Tax Appellate Tribunal (ITAT) and the position affirmed by the High Court, but the Revenue has not challenged those deletions.

4) Insofar as addition under Section 2(22)(e) of the Act is concerned, a sum of Rs. 1,20,10,988/- was added on this account. The assessee is a Hindu Undivided Family (HUF). During the previous year to the Assessment Year, the assessee had received certain advances from one M/s. G.S. Fertilizers (P) Ltd. (hereinafter referred to as the 'Company'). The Company is the manufacturer and distributor of various grades of NPK Fertilizers and other agricultural inputs. In the audit report and annual return for the relevant period, which was filed by it before the Registrar of Companies (ROC), it was found that the subscribed share capital of the said Company was Rs. 1,05,75,000/- (i.e., 10,57,500 shares of Rs. 10/- each). Out of this, 3,92,500 number of shares were subscribed by the assessee which represented 37.12% of the total shareholding of the Company. From this fact, the AO concluded that the assessee was both the registered shareholder of the Company and also the beneficial owner of shares, as it was holding more than 10% of voting power. On this basis, after noticing that the audited accounts of the Company was showing a balance of Rs. 1,20,10,988/- as "Reserve & Surplus" as on 31st March, 2006, this amount was included in the income of the assessee as deemed dividend.

5) In the appeal filed by the assessee, the aforesaid addition was affirmed by the Commissioner of Income Tax (Appeals) (for short 'CIT(A)'). Though, this addition was questioned by the assessee on various grounds, we would take note of the submission which is advanced before us as the challenge is confined only on the basis of said submission. The assessee had argued that being a HUF, it was neither

the beneficial shareholder nor the registered shareholder. It was further argued that the Company had issued shares in the name of Shri Gopal Kumar Sanei, Karta of the HUF, and not in the name of the assessee/HUF as shares could not be directly allotted to a HUF. On that basis, it was submitted that provisions of Section 2(22)(e) of the Act cannot be attracted.

6) We would like to reproduce that portion of Section 2(22)(e) of the Act at this stage, which is relevant for the instant appeal:

> "S.2(22) of the Income Tax:- Dividend includes:
>
> xxx xxx xxx
>
> (e) any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) [made after the 31st day of May, 1987, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern)] or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits;
>
> but "dividend" does not include—
>
> xxx xxx xxx
>
> Explanation 3.— For the purposes of this clause,
>
> (a) "concern" means a Hindu undivided family, or a firm or an association of persons or a body of individuals or a company;
>
> (b) a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous year, beneficially entitled to not less than twenty per cent of the income of such concern."

7) Taking note of the aforesaid provision, the CIT(A) rejected the aforesaid contention of the assessee. The CIT(A) found that examination of annual returns of the Company with Registrar of Company (ROC) for the relevant year showed that even if shares were issued by the Company in the name of Shri. Gopal Kumar Sanei, Karta of HUF, but the Company had recorded the name of the assessee/HUF as shareholders of the Company. It was also recorded that the assessee as shareholder was having 37.12% share holding. That was on the basis of shareholder register maintained by the Company. Taking aid of the provisions of the Companies Act, the CIT(A) observed that a shareholder is a person whose

name is recorded in the register of the shareholders maintained by the Company and, therefore, it is the assessee which was registered shareholder. The CIT(A) also opined that the only requirement to attract the provisions of Section 2(22)(e) of the Act is that the shareholder should be beneficial shareholder. On this basis, the addition made by the AO was upheld.

8) Undeterred, the assessee approached the next higher forum, i.e., ITAT in the form of appeal under Section 253 of the Act. In this endeavour, the assessee succeeded as appeal of the assessee was allowed holding that the ingredients of Section 2(22)(e) of the Act were not satisfied and, therefore, addition of the aforesaid nature could not be made.

For this purpose, the ITAT referred to the judgment rendered by its Mumbai Bench in the case of *Binal Sevantilal Koradia (HUF) Vs. Department of Income Tax*[1]. In fact, the only exercise done by the ITAT in the said order was to quote from the aforesaid judgment with the observations that the issue is squarely covered by the said decision. In Koradia (HUF), it was held by the Tribunal that HUF cannot be said to be shareholder or a beneficial shareholder. Since these are the twin conditions to attract the provisions of Section 2(22)(e) of the Act, both have to be satisfied. As per the ITAT, since HUF, in law, cannot be a registered shareholder or a beneficial shareholder, provisions of Section 2(22)(e) would not be attracted.

9) As noticed above, the High Court, in the impugned judgment rendered in the appeal preferred by the Revenue, has reversed the judgment of the ITAT, thereby restoring the addition which was made by the AO. The order of the High Court reveals that it has done nothing but to extract the language of Section 2(22)(e) of the Act and sustained the addition made by AO with one line observation, viz., 'the assessee did not dispute that the Karta is a member of HUF which has taken the loan from the Company and, therefore, the case is squarely within the provisions of Section 2(22)(e) of the Income Tax Act'.

10) The arguments before us remain the same. Mr. S.B. Upadhyay, learned senior counsel appearing for the assessee, argued that the ITAT had correctly explained the legal position that HUF cannot be either beneficial owner or registered owner of the shares and, therefore, no addition could be made under Section 2(22)(e) of the Act. For buttressing this submission, the learned counsel relied upon the following observations in judgment of this Court in *CIT, Andhra Pradesh Vs. C.P. Sarathy Mudaliar*[2]:

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[1] ITA No. 2900/Mum/2011, AY 2007-08 dated 10.10.2012.

[2] 1972 SCR 1076

> "....It is well settled that an HUF cannot be a shareholder of a company. The shareholder of a company is the individual who is registered as the shareholder ion the books of the company. The HUF, the assessee in this case, was not registered as a shareholder in books of the company nor could it have been so registered. Hence there is no gain-saying the fact that the HUF was not the shareholder of the company."

11) Learned Additional Solicitor General, on the other hand, after reading the relevant portions of the orders of AO and CIT(A), submitted that on the facts of this case, the Revenue was justified in making the addition.

12) Section 2(22)(e) of the Act creates a fiction, thereby bringing any amount paid otherwise than as a dividend into the net of dividend under certain circumstances. It gives an artificial definition of '*dividend*'. It does not take into account that dividend which is actually declared or received. The dividend taken note of by this provision is a deemed dividend and not a real dividend. Loan or payment made by the company to its shareholder is actually not a dividend. In fact, such a loan to a shareholder has to be returned by the shareholder to the company. It does not become income of the shareholder. Notwithstanding the same, for certain purposes, the Legislature has deemed such a loan or payment as '*dividend*' and made it taxable at the hands of the said shareholder. It is, therefore, not in dispute that such a provision which is a deemed provision and fictionally creates certain kinds of receipts as dividends, is to be given strict interpretation. It follows that unless all the conditions contained in the said provision are fulfilled, the receipt cannot be deemed as dividends. Further, in case of doubt or where two views are possible, benefit shall accrue in favour of the assessee.

13) A reading of clause (e) of Section 2(22) of the Act makes it clear that three types of payments can be brought to tax as dividends in the hands of the share holders. These are as follows:

> (a) any payment of any sum (whether as representing a part of the assets of the company or otherwise) by way of advance or loan to a shareholder.
>
> (b) any payment on behalf of a shareholder, and
>
> (c) any payment for the individual benefit of a shareholder.
>
> [See: *Alagusundaran vs. CIT*; 252 ITR 893 (SC)]

14) Certain conditions need to be fulfilled in order to attract tax under this clause. It is not necessary to stipulate other conditions. For our purposes, following conditions need to be fulfilled:

> (a) Payment is to be made by way of advance or loan to any concern in which such shareholder is a member or a partner.

(b) In the said concern, such shareholder has a substantial interest.

(c) Such advance or loan should have been made after the 31st day of May, 1987.

15) Explanation 3(a) defines "concern" to mean HUF or a firm or an association of persons or a body of individuals or a company. As per Explanation 3(b), a person shall be deemed to have a substantial interest in a HUF if he is, at any time during the previous year, beneficially entitled to not less than 20% of the income of such HUF.

16) In the instant case, the payment in question is made to the assessee which is a HUF. Shares are held by Shri. Gopal Kumar Sanei, who is Karta of this HUF. The said Karta is, undoubtedly, the member of HUF. He also has substantial interest in the assessee/HUF, being its Karta. It was not disputed that he was entitled to not less than 20% of the income of HUF. In view of the aforesaid position, provisions of Section 2(22)(e) of the Act get attracted and it is not even necessary to determine as to whether HUF can, in law, be beneficial shareholder or registered shareholder in a Company.

17) It is also found as a fact, from the audited annual return of the Company filed with ROC that the money towards share holding in the Company was given by the assessee/HUF. Though, the share certificates were issued in the name of the Karta, Shri Gopal Kumar Sanei, but in the annual returns, it is the HUF which was shown as registered and beneficial shareholder. In any case, it cannot be doubted that it is the beneficial shareholder. Even if we presume that it is not a registered shareholder, as per the provisions of Section 2(22)(e) of the Act, once the payment is received by the HUF and shareholder (Mr. Sanei, karta, in this case) is a member of the said HUF and he has substantial interest in the HUF, the payment made to the HUF shall constitute deemed dividend within the meaning of clause (e) of Section 2(22) of the Act. This is the effect of Explanation 3 to the said Section, as noticed above. Therefore, it is no gainsaying that since HUF itself is not the registered shareholder, the provisions of deemed dividend are not attracted. For this reason, judgment in C.P. Sarathy Mudaliar, relied upon by the learned counsel for the appellant, will have no application. That was a judgment rendered in the context of Section 2(6-A)(e) of the Income Tax Act, 1922 wherein there was no provision like Explanation 3.

18) We, thus, do not find any merit in this appeal, which is accordingly dismissed.
