Ref : KTBA/04.2022/030
Date : April 25, 2022

Mr. Qaiser Iqbal,
Member-IR (Operations),
Federal Board of Revenue,
Islamabad.

ADJUSTMENT OF TAX REFUNDS WITH TAX LIABILITY
NOTICES UNDER SECTION 221 OF THE INCOME TAX ORDINANCE, 2001

Dear Mr. Qaiser Iqbal

As you may be aware that show cause notices on the captioned subject have been issued en-masse by certain Departmental Officers, Inland Revenue, whereby the cause has been asked to be shown as to why the Tax Returns filed for TY 2021, which are taken as deemed assessments under the Ordinance, proposed to be rectified under Section 221 of the Income Tax Ordinance, 2001 on the premise that refunds have, presumably been found, to be adjusted against the tax liability without being determined under Section 170(4) of the Ordinance.

2- We at Karachi Tax Bar Association (KTBA) would like to highlight an important issue in this context that needs your urgent attention for its prompt resolution and for the sake of avoidance of any unwarranted potential litigation. This is in the wake of number of complaints from our members that notices issued from the field offices are without lawful jurisdiction.

No Rectification against Deemed Assessment

3- You must be aware of the legal position that provisions of Section 221 of the Ordinance empower a Commissioner to amend any order passed by him. The issue of adjustment of previous years refund, however, does not come within the ambit or scope of rectification of mistake as provided for under Section 221 of the Ordinance. Section 221 of the Ordinance, states that a Commissioner may rectify "ANY ORDER PASSED BY HIM", while in the instant case, no formal order, using application of mind, has been passed by the learned Commissioner Inland Revenue ("CIR") himself or by any of his learned predecessor. It would not be out of context to elaborate here that clause (b) of sub-section (1) of section 120 of the Ordinance provides that a return filed to be taken as an assessment order passed by the CIR.

4- The purpose of this letter is to apprise your office, of the illegality, which has been allowed to permeate through the whole process. It is by virtue of this deeming provision and the fiction of law, the return filed is treated as an assessment order, which however, by any stretch of imagination, cannot be treated as formal assessment order, which would have factually been passed by a CIR.

Bar Chamber, Ground Floor, Regional Tax Office Building, Shahrah-e-Kamal Attaturk, Karachi – 74200
Ph: 021-99211792, Cell: 0335-3070590 Website: www.karachitaxbar.com
Email Address: info@karachitaxbar.com ktba01@gmail.com

This dictum is validated by the superior courts in number of cases. A very relevant judgement in this regard would be that given by LHC wherein the ratio has been settled. The Hon'ble Lahore High Court in W.P No. 13284 of 2012 in the case of M/s Ibrahim Fibers Limited Versus Federation of Pakistan & Others observed as follows:

> *5. ……..Therefore, if an order is not passed by the Commissioner, no question of rectification of mistake committed by the Commissioner arises which can only be the case if there is an order passed by the officer and in which a mistake has crept which is sought to be rectified at a later stage. The mistake if at all in the assessment order is that of the taxpayer and not that of the Commissioner and thus, the power under Section 221 cannot be exercised in respect of an assessment order issued under section 120 of the Ordinance....*

You would agree that if the illegality is not arrested in the beginning of the process, it would render the whole exercise to end in the inevitable litigation between the taxpayer and the department, which can well be avoided today.

Adjustment of Tax Refunds has been allowed to be made

5- It would equally be critical to highlight here that refund becomes due when the assessment order under Section 120 of the Ordinance come into existence and thereafter the refunds of previous years can very much be adjusted against the liability of current year. This legal notion has been endorsed by the judgements of the superior courts as well. Hon'ble Lahore High Court has held in a case reported as 2021 SLD 48 LHC as under.

> *"Examination of provisions, contained in Section 170, has itself answered the confusions noted supra. The proviso to subsection (1) of Section 171 is required to be read with Section 170. After collective reading of these provisions, we are not convinced by the arguments of learned counsel for the respondents that word "may" used in subsection (1) of Section 171 makes filing of application for refund as optional. The word "may" is used for applying to the Commissioner for refund within two years. It appears that option to apply for refund in two years is given for the reason that taxpayer can also opt for adjustment of refund against his future tax liability or for adjustment against demand under other taxing statutes."*

In another decision the hon'ble Appellate Tribunal in a case reported as 2010 PTD 519 (Trib.) has held as under.

> *....we are constrained to observe that section 171 is to be read in the light of section 120 as refund becomes due the moment an assessment order creating the said refund comes into*

Bar Chamber, Ground Floor, Regional Tax Office Building, Shahrah-e-Kamal Attaturk, Karachi – 74200
Ph: 021-99211792, Cell: 0335-3070590 Website: www.karachitaxbar.com
Email Address: info@karachitaxbar.com ktba01@gmail.com